"Rane Group -Q2 FY '19 Earnings Conference Call"

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the Rane Group Limited Q2 FY '19 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. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Diwakar Pingle from Christensen IR. Thank you and over to you, Mr. Pingle.

Diwakar Pingle: Thank you, Janice. Good Afternoon friends, Welcome to the Q2 and FY '19 earnings call of the Rane Group. To take you through the results and answer your questions today, we have the management team from Rane Group represented by Mr. L. Ganesh – Chairman and Managing Director of Rane Holdings Limited; Mr. Harish Lakshman – Vice Chairman, Rane Holdings Limited; Mr. Padmanabhan P. A. – President, Finance and Group CFO; Mr. Siva Chandrasekaran – Executive Vice President of Secretarial and Legal Services; and Mr. J. Ananth – CFO of Rane Holdings Limited.

Please note that we have sent you the press release and also a presentation link of the deck was sent out this morning. In case any of you have not received the presentation, you could look at it on our website or even the BSE site of Rane, or you could also write to us and we will be happy to send the detailed earnings presentation over to you.

Before we start, I would like to say that everything that is said on this call that reflects any outlook for the future or which can be construed as a forward-looking statement must be viewed in conjunctions with risk and uncertainties that we face. These uncertainties and risks are included, but not limited to what we have mentioned in prospectus and subsequently annual reports which you can find on our website. With that said, I now hand over the call to Mr. Ganesh. Over to you, Sir.

L. Ganesh: Thank you, Diwakar. Good Afternoon, Ladies and Gentlemen, thank you for dialing in. I Welcome you to this teleconference. You would have seen the Q2 FY '19 performance highlights of the group of all the companies posted on our website. I would like to provide certain additional remarks and then we will proceed. This quarter has been overall positive with strong demand from all the customers. We have experienced some headwinds in terms of increased raw material and employee cost and Forex. Of course, this we discussed even in Q1 and this has further enhanced during Q2.

Turning to the group performance, Rane Group sales registered a growth of 18% in Q2. The EBITDA margin at a group level declined from 12.7% to 10.7%. This was mainly due to the unfavorable Forex movement, the adverse material cost impact, and increased employee cost from minimum wages, increments, and also some long-term settlements. The aggregate PBT without exceptional items declined from 7.5% to 6.1% at the Group level. Rane Madras standalone experienced a 20% growth with strong off take for steering products from Indian OEM customers.

Despite the unfavorable mix, inflationary pressures on raw materials and employee cost, EBITDA margin improved by 43 basis points mainly due to the increased volume and operational performance was good at all the locations. Rane Precision Die Casting, we are seeing some improvement in operational performance although the business did experience some higher costs on utilities, repairs, and tooling maintenance. We continue to work on securing new orders for this business and have taken some steps to further improve operational performance.

As you are aware, the revival of the operational performance of REVL is underway. We experience good offtake from customers both international and domestic. The plants have all started improving both in terms of output and also quality performance, so the delivery issues have come down to minimum, and also premium freight. However, there were some adverse Forex movement, again little bit of an unfavorable product mix the aftermarket being lower and OEM being higher, and of course, steep increase in raw material prices and employee costs for the same reason as other group companies, so this contributed to a drop in EBITDA margin. Better operational performance did offset to some extent. We are working on passing some of these raw material price increases to customers. We have recovered from some customers, the paper work etc. is in progress, and we will hopefully during this quarter close and try to recover as much of the cost increase as possible from customers. We also expect some more efficiencies in terms of operations during this quarter.

In Rane Brake Linings, the total sales increased by 8% driven by a strong demand from Indian OE segment; however, there was a slight drop in the aftermarket sales. This is partly because of the high base effect if you recall Q2 of FY '18 was the post-GST quarter where we had exceptional sales, therefore, this quarter has been lower. We are focusing on aftermarket which as you all know is a very important segment for this company and in the future quarters, we have done some new product launches. We are expanding some of our distribution network and we are focusing a lot on increasing aftermarket and recovering some of this in second half. Unfavorable product mix and Forex again impacted this company, raw material and employee cost resulting in a drop in EBITDA margin. This was also accentuated because there was a one-time reversal in the previous quarter of some excise duty and provision for bad debts towards the Railways which we have made in this quarter, this we will discuss later if you have some questions.

In Rane TRW, the growth was strong in the steering business based on strong growth in the commercial vehicle industry. Of course, there were increases in raw material costs resulting in some impact on the margins, but we were able to recover most of the increases.

Rane NSK continued to see good demand on the served models and we have started some new programs also. The adverse material cost and higher administrative costs partly because we have started operation or just about to start operation in Gujarat, so the setting up of this plant had some expenses in this quarter, there was some impact on the EBITDA margin. As we see forward as of now we see some uncertainty in the passenger car segment, but of course as you know the industry feels is only temporary, we will have to wait and watch, but other segments like commercial vehicles, farm tractors, and Two-wheelers continue to remain quite optimistic. With these opening remarks, I will hand you over to Harish for his comments after which we will take your questions. Thank you.

Harish Lakshman: Good Afternoon everyone, just a couple of more comments on the market and group performance of the last quarter. We continue to experience strong growth across all the domestic OE business. The revenue grew by 24% and this was supported by strong growth across all segments and we had superior growth in the passenger vehicle segment vis-a-vis the market because of the served models and the entry into some new models. We continue to have very strong growth in the commercial vehicle segment although revenue wise there has been a slower growth only in the small commercial vehicle, but despite that it is still a very strong numbers. In farm tractor segment, Rane Madras steering business continued to be strong. We gained market share from manual steering gear as well as we entered into new models with several of our hydraulic steering products. The performance in the Two-wheeler segment is supported by ramp up in supplies of valve train components which were mainly from REVL across all the key customers like HERO and TVS.

Our overall international business grew by about 6% including exports largely driven by the business in Rane Madras as well as in Rane TRW, the occupant safety business. The aftermarket continues to be overall okay. We grew about 5% over the previous year, so overall we expect the growth to continue at a similar rate. The capacity expansion what Mr. Ganesh mentioned about Rane NSK Gujarat, as well as our occupant safety that we had shared setting up a new plant in Trichy is also progressing as per plan in order to meet the enhanced demand in the coming years, so with these few words I would like to open the session for any questions.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. We will take the first question from the line of Viraj Kacharia from Securities Investment Management. Please go ahead.

Viraj Kacharia: First is if you look at the group key subsidiaries and JV our expectation back in Q1 even subsequently was that we will get price increase from OEs to offset the increase in raw material cost, so the margin impact that you have seen in Q2 is that even after us getting the price increase from OEs, that is one? Added to that is the bulk of the cost in terms of key raw material, FX reflected in Q2 or we expect more such pressures in coming quarters?

Harish Lakshman: To answer your first question, there is some lag effect on the commodity increases that we have got from customers. The amount varies from business to business, but however while there could be a lead lag effect, we are confident that we will retrieve everything so there could be a spillover to next quarter etc.

Viraj Kacharia: Second question was like the bulk of the increase in raw material prices or the FX impact, is that largely reflected in our Q2 numbers or we expect more such cost pressures in coming quarters?

Harish Lakshman: Whatever has been incurred is reflected in this quarter, however, we do not know what is going to happen to FX if there is a further deterioration obviously that will impact our numbers and also there is some talk of further tightening of certain types of commodities in the upcoming quarters especially some of the special alloy, steels etc., so if that happens then that will further impact the coming quarters.

Viraj Kacharia: If we look at a group level what will be the FX impact, we would have seen in Q2?

Harish Lakshman: About half a percent negative.

Viraj Kacharia: Going forward, do we expect margins across group to be at Q2 levels or do we expect margins to incrementally improve going forward?

Harish Lakshman: We generally do not give forward-looking statements, honestly it is very difficult to predict with all the uncertainties both on the demand side as well as some of these cost items.

Viraj Kacharia: Second question was on the demand side, are we seeing any communication with OEs in terms of any changes in production schedules, how are we seeing demand across key categories in Q3 and Q4?

Harish Lakshman: You are asking across all vehicle segments?

Viraj Kacharia: Yes.

Harish Lakshman: Again, we cannot give you any specific numbers, but all I can tell you is we have had some conversations with senior people across all our various customers and general high-level message that is coming through is commercial vehicle and farm tractors, the strong double digit growth will continue. We are not seeing any let up in the momentum is the feedback that we are getting. Of course, in passenger cars, clearly there has been some slowing down in the growth rate and we are not getting a clear signal as to how the second half will look except there is no panic or any such sort of a thing. In Two-wheeler also the growth will continue, whether the rate of growth will continue at 8% to 9% is to be seen.

Viraj Kacharia: Last question was on the NSK side, if you look at the key OEs whom we supply to say Maruti, Honda, and if we look at their production volume growth in Q2, they have been around 7% to 8% but for NSK our growth in Q2 has been around 20%, so what has driven this outperformance for us vis-a-vis the market?

Harish Lakshman: The served models, the growth in the served models that is why we have been able to outgrow the passenger car segment.

Viraj Kacharia: So which key models if you can highlight us that has kind of given that extra Delta this quarter?

Harish Lakshman: All the Maruti new project like Swift, Baleno and Brezza.

Viraj Kacharia: Would we be there in any of the Maruti's or Honda's recent launches in terms of Ertiga, Amaze, and going forward how are we seeing in terms of our wallet share for these two OEs for the new programs?

Harish Lakshman: It will continue at this rate, now Maruti generally divides up the business between us and JTEKT, so we do not expect any major changes.

Viraj Kacharia: Any update on any new OE additions for NSK?

Harish Lakshman: Nothing to report right now.

Moderator: Thank you. We will take the next question from the line of Nikhil Upadhyay from Securities Investment Management. Please go ahead.

Nikhil Upadhyay: If we look at our group CAPEX guidance, we were looking at 200 to 250 crores of CAPEX now considering the demand environment has little bit slowed down or the feeling is not so exciting, would you sustain with this CAPEX or do you see that this CAPEX can be prolonged to next year considering our capacity utilizations?

L. Ganesh: I think the CAPEX will remain as per plan because most of them were for specific programs. One is all the other segments continue to grow as Harish was mentioning and even in pass car whatever we are investing is for programs where we are serving, so we do not see any slowing down in CAPEX, we are going to spend close to plan.

Nikhil Upadhyay: Secondly Sir, on PDC if I consider our sequential business performance even on our sales degrowth what we are seeing is that the EBITDA losses have reduced, so the benefits on the cost side which we have been able to bring in to the P&L, do you see that can sustain from here on and probably that is the cost structure with which we will be operating from now on or is it just some one-offs and probably there could be the losses that can be equivalent to what we have seen in the previous quarters, if you can just highlight to some extent on that?

Harish Lakshman: Honestly, it is very difficult to give a clear quarter wise estimate what will happen. As we have communicated in some of the previous calls, when we acquired the business in 2016, we were hoping for losses for three years and breakeven at the end of three years. Now, we are looking at four to five years, so while quarter to quarter there may be some movement because of some improved performance or market condition or even some accounting adjustments, I think the losses will continue for some more time, at least another 18 months is what we see.

Nikhil Upadhyay: I get that point Sir, the only point which I was looking at is like if we look at this quarter's performance it is on a lower sales and lower gross margin and still our EBITDA losses have reduced, so I was just trying to understand that if we remove the raw material cost and even on lower sales, is it the cost structure on which we have got a hold of and now probably it is more of a sales which we would be looking at in terms of improving the performance, that is what I was trying to understand?

Harish Lakshman: This improvement that you are seeing in the last quarter is because of some provisions that we had made on certain types of expenses that we did not incur during the first half of year, so it was reversed.

Nikhil Upadhyay: Lastly Sir, on TRW if you can give the breakup between occupant safety and steering, and have we seen some kind of a lower sales growth on the occupant safety side?

Harish Lakshman: Yes, we are seeing some lower sales on the occupant safety side. This is because of domestic market. While the export market continues to be strong, in the domestic market there is a high dependence on both Ford and Mahindra which vis-a-vis the market. these two OEMs their automotive business at least, Mahindra ignore the tractor side but on the automotive side of Mahindra and Ford, they are not doing as well as the market is so that is getting reflected in our numbers.

L. Ganesh: Seatbelt and Airbag split is 55% and 45%.

Moderator: Thank you. The next question is from the line of Shyamsundar Shriram from Sundaram Mutual Fund. Please go ahead.

Shyamsundar Shriram: Sir, broadly in your opening remarks you had mentioned about softening the passenger vehicle demand, so from NSK perspective are you seeing cuts through production schedules compared to what you have budgeted at the beginning of the year?

L. Ganesh: As far as Rane NSK is concerned, there is no significant drop in schedules because as we mentioned earlier, the served models where we are supplying, they are also producing in Suzuki in Gujarat, though the waiting period has come down, but in terms of numbers they are not coming down significantly. I think the drop has been little bit more in the A segment and some other models where we are not serving, so fortunately for us we have not seen the drop as of now.

Shyamsundar Shriram: Sir, in TRW how much was the exports in H1?

L. Ganesh: About Rs.170 crores in H1.

Shyamsundar Shriram: You mentioned broadly there is a slowdown in Ford and Mahindra, but Mahindra is also launching new models of Marazzo and another model is coming up, will we also be supplying occupant safety products for these models?

Harish Lakshman: Not for the Marazzo, but for the future models, yes.

Shyamsundar Shriram: Sir, in Rane Brake Lining, aftermarket on a run rate basis seems to have come down on a quarter on quarter basis as well, what is happening in the aftermarket, being a very important piece of that business?

L. Ganesh: One is of course as I mentioned earlier it is the base effect. We have not lost any market share that is something which I can tell you, but the base effect is one thing and the second is the price increase is that we have done in the market, there is always some adjustment in the market as dealers pre-buy a little bit and those kind of things affect quarter to quarter, but there is no loss of market share, however, in certain products like asbestos free brake lining for commercial vehicle, we have now introduced a few new kind of products with high performance and we think that will pick up and that will kind of makeup. To some extent Kerala floods also affected us, we are very strong in South as you know and Kerala was almost shutdown for a couple of months, so to some extent that also affected us, but overall I think we should be able to make up that is not a matter of concern for us.

Shyamsundar Shriram: Sir, in Rane Brake Linings we have also continued to see RM cost pressures quarter after quarter, so what is the outlook here in terms of the cost pressures here?

L. Ganesh: This continues, most of Rane Brake Lining products or many of them are linked to petroleum product prices, so as petroleum goes up these commodities go up so it is a challenge and we see continuous increase as you said, so we are kind of trying to recover some of it, not all can be recovered in that product because it is very difficult to relate one-to-one being a formulation, so we are trying to recover as much as possible. We have done some price corrections already in the first half and we are working with customers to do so in the second half, so the idea will be to recover as much and of course to focus a lot more on localization as far as possible, some change in sources, some cost reduction projects, so we are trying to mitigate some through efficiency and recover part of it.

Shyamsundar Shriram: What is the outlook over the second half of the year in terms of the gross margins here, Sir?

L. Ganesh: As we said the mix etc. we are working on so I will not be able to give you exact number on that depending on the product mix, depending on how we catch up in the aftermarket, but as far as raw material is concerned we think the kind of same cost structure is our target to maintain by doing some of these initiatives.

Shyamsundar Shriram: Sir, in Rane Brake you had spoken about some provision of bad debt etc. if you can please elaborate on that?

L. Ganesh: The two effects in the Rane Brake Lining, the EBITDA has fallen significantly. Out of that, one is of course overall product mix, the other is Forex and raw material cost increase, but there are two elements there, one is provision which was reversed in the last quarter in the last year, so that is not there this year, that is one effect. The other is for some old railway debt as per our policy, we have made a provision of nearly about Rs.1 crore or so, but we are still working on collecting it, but we have a policy by which we make a provision, so that provision has also been made in this quarter.

Shyamsundar Shriram: Sir, in Rane Madras you had spoken in the presentation also you had spoken about some new products in the hydraulic steering segment, if you can talk about the new product?

L. Ganesh: In hydraulics, there are two things one is our range of cylinders is increasing, so we are adding more customers in commercial vehicle and farm tractors, so a range of cylinders that we make both for tractor and commercial vehicles steering is adding customers, and therefore new kind of products for those customers. The other is in hydraulic steering for tractors, we are adding customers also as we mentioned and discussed last time so that is taking off quite well with new customers and there are one or two new hydraulic products which we have made for some specific customers which go with the farm mechanization, with farm equipment, some import substitution products, very early to say how much that will generate, but overall all our hydraulic sales has almost doubled in this quarter compared to previous year's quarter, so it is going very well, it is almost grown by 90% plus.

Shyamsundar Shriram: Sir, you spoke about some new customers, which new customers have we added here?

L. Ganesh: I think one is Escorts and the other is Swaraj tractors, these are the two new customers we added and for cylinders may be a few commercial vehicles like Tata Motors we have added.

Shyamsundar Shriram: Sir, here in Rane Madras how much is the domestic die casting revenues in H1?

L. Ganesh: It is about Rs.21 crores of domestic sales.

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

Ronak Sarda: Firstly, in the various segments you have highlighted the Forex movement impacts the profitability, if you can just highlight on an overall basis, how much is the import content and given currency depreciation has been a constant factor for the country, are you looking to localize some of it or these imports are something which you think the capability is not there at present in the country?

L. Ganesh: We have addressed this in the past, except in airbags where there is a significant import which includes the inflator and some electronic components in the EPS, and some Rane Brake Lining raw materials which come for formulation, other than that, Rane Engine Valve and Rane Madras by and large we have tried to localize, even aluminum we have now shifted more towards local purchase for local die cast division, so it is only the electronics part, the inflator for the airbag and some materials for Rane Brake Lining and you know the answer, these are going to continue to be imported for a while but all other mechanical parts, we are clearly on the localization path and we are increasing it year by year.

Ronak Sarda: Is it true for Rane NSK and Rane TRW as well on the steering part, not on the airbags part but on the steering part have we achieved almost like 90% localization or?

L. Ganesh: Yes, in the hydraulic steering there is hardly, very insignificant imports I think some seals if I am not mistaken.

Ronak Sarda: The electronic steering part the passenger vehicle part?

L. Ganesh: In Passenger vehicle, some parts are still getting imported but even that now we are getting the motor from the company locally, so I do not know the components of that may be imported but as far as we are concerned, the motor is being now invoiced to us from India in Rupees, so perhaps some ECU etc., we are also working with the sources and with Maruti so that these also can be procured later in India, they are also trying to setup some facilities in India, so yes, the direction is towards more and more local content.

Ronak Sarda: The second question was if you can just highlight what is the gross and net debt on the group level and any specific company which has higher debt portion, maybe Rane Madras?

L. Ganesh: I will just give you the numbers, no company has had to borrow significantly in the first half, also because overall generation was good. REVL although generation was not good, we have not had any significant CAPEX, maybe a marginal increase. I will tell you the number. But Rane Madras is not significant at all because generation has been good. At the group level, our debt is about Rs.700 crores, actually there is not much change from June to September.

Ronak Sarda: This is net debt you are saying?

L. Ganesh: Gross debt.

Ronak Sarda: So net debt would be, the cash would not be a significant portion?

L. Ganesh: Not very significant, Rs.30-40 crores.

Moderator: Thank you. We will take the next question from the line of Ravi Purohit from Securities Investment Management. Please go ahead.

Ravi Purohit: Just one quick clarification, the last point on this gross debt this is basically our share of the debt or this is the group debt?

L. Ganesh: At the group level

Ravi Purohit: So our share will be much lower than this, we own 50% in TRW and 50% in NSK and if they have Rs.100 crores debt on their balance sheet, our share is Rs.50 crores, right?

L. Ganesh: Yes, this is total debt.

J. Ananth: We do not consolidate balance sheet now, as per Ind AS.

Ravi Purohit: From analyst point of view what we are looking for is our share of the debt in the balance sheet in the sense, so that should not be Rs.700 crores, right?

J. Ananth: That is not Rs.700, that will be around Rs.400 to Rs.450.

Ravi Purohit: Actually my question is a more broad strategic in nature in the sense, our capital allocation decisions in the last few years, we have made one acquisition in the US which I think when we had mentioned at the time of making the acquisition that we paid like $1 for that and it was supposed to be based on one of our clients to kind of acquire that and it has been kind of a struggle since then, the losses have only expanded and what was earlier a three-year breakeven has now become a five-year breakeven, when do you kind of decide that let us say it does not breakeven in five years also or four years also and the losses keep expanding, it is kind of draining your resources from India, you have to extend loans to that company or you have to raise resources for that company? Second question then we had also acquired a small company in the mobility space, which I think last year reported some Rs.4 crores loss and then recently we increased our stake in REVL, which has been a loss-making company for a fairly long period of time, so Rane Holding basically is kind of lot of money that is generated by good operating businesses like TRW, NSK, and Madras is being kind of diverted towards loss-making, sub par ROE businesses, so is there any, what should us as long-term investors kind of take home from that in the sense what really that companies overall thinking in terms of capital allocation, we have any IRR expectations from these investments that we have made?

Harish Lakshman: I will try and answer the question to the best extent possible and again this would be at a broad level. If we were having this call in 1999, you would be asking why is Rane TRW bleeding so much, if this call was in 2005 the same would have been asked about Rane NSK, some businesses start making money in seven to eight years, some has taken even 12 years in the group. Today, the fruits of what you are seeing in Rane NSK and Rane TRW, we have been through some very difficult times in the earlier part of 2000. So we take decisions based on what we think there is potential and like everything else in world nothing goes according to plan, there are some setbacks, there are some upsides also that we enjoy, but at the same time we take your point that ultimately all of us, our job is to ensure we deliver return on capital. I think I mentioned even in the earlier calls coming to the specific about the US investments, while clearly after the acquisition there are certain assumptions that we made in terms of new business did not come through, which is also impacting the business. In addition, we have had some unanticipated operational challenges and both are getting addressed.

We are still hopeful at this point in time, in fact now we are in some advance stages of securing some new contracts for the US business and if that comes through, that can be the beginning of some turnaround that we have all been hoping for, so obviously if two years from now also we are still losing money and we do not see the light at the end of the tunnel, you can be rest assured that we are not going to completely be putting good money to bad money. So I think that definitely, as of now, the visibility is five years and we remain committed to our strategy of trying to grow and turnaround the US business. I think maybe in the next three quarters or four quarters, we will have more clarity on the future direction for that business in terms of what the potential is.

Again, the mobility business is a very new acquisition, this is an evolving space where there are lots of opportunities, there are also lots of players, but that business we have some good clientele. I think we have mentioned in some of the earlier announcements, we have customers like Ola, we have customers like Mahindra Logistics, and we believe this business has got lot of potential and of course this business' capital intensity is very low so to that extent, low risk involved in this business, this is not a business where we are to bring lot of assets and machines etc. Based on certain future projects, a lot of it is manpower related and engineering resources related, so for this business, again we need to take a longer view on all of this. I think minimum five to seven years view is what we would like to take and obviously we are using the money that we are generating from our current businesses, investing for the future because we believe there is a future in some of these businesses. I think as far as engine valve is concerned, we have mentioned again in the past, it has been very painful for us but this restructuring is an absolute necessity keeping in mind the future of the business. I think Mr. Ganesh had also indicated back in June or July, we are looking at 18 to 24 months' time to complete all our restructuring and that is still going according to plan.

Moderator: Thank you. We take the next question from the line of Sunil Kothari from Unique Investments. Please go ahead.

Sunil Kothari: Sir, my question is on die casting part of Indian business, I think we are also waiting for a good time. You are always very positive in currency we are crossing Rs.60 to Rs.65, now it is almost Rs.70 plus, so any thought process for a long-term to create a good export base from steering business, hydraulics parts, from ball joints, and next is this die casting?

Harish Lakshman: I will answer your question in two parts, as far as India die casting business is concerned, operationally a lot of improvements have been made. For us the only thing is, there is still a lot of capacity under utilization, so we need to fill up the order book. I think that is the main challenge in that business. A lot of work is going on and we are looking at strategy of both short-term and long-term, when I mean short-term there could be some small pieces of business we can go and get a one year contract from a customer etc. and there are some businesses which are more five years, six years like a new program. That typically has a 18 months' time process for decision-making, sample approval etc., so we are adopting both strategies and we are hopeful that even next year while you will see the die casting domestic business has been slightly negative, we had a small de-growth, so that business is -4% first half last year to this year, so unfortunately this year, we could not find any opportunities to improve the capacity utilization, but I can tell you we are definitely hopeful that next year the capacity utilization will be much better than this year, but it will still not be where it needs to be. I think that we are hoping the year after that we will see good capacity utilization and even the underlying EBITDA in this business continues to be quite decent, so we know that if the capacity utilization is there, this business will generate profits. The second part, yes, ball joints, hydraulic, everything we are aggressively working on exports and now as you have said with Rupee depreciating suddenly our competitiveness has increased further. There are some new RFQs also that are getting pursued, so we are hopeful that this will continue and you can see the steering side of Rane Madras exports has been very good in the first half.

Sunil Kothari: Sir, yesterday or two days back some notice regarding we are withdrawing from JMA marketing India operation, so is there any change in thought process from not pursuing aftermarket in a bigger way or what is this exactly?

L. Ganesh: Actually JMA Rane is a joint venture with one of our major distributors, which some years ago we started because at that time we felt as a group our Western region distribution was not strong enough and there were one very traditional distributor who was kind of having some financial problems, so we wanted to strengthen that area. Now, that has been achieved, JMA Rane has given us that growth. Today, JMA Rane is about maybe 45% to 50% of Rane products and the rest is non-Rane products, so what we thought over the last few years is that JMA has got many companies in this distribution, so we thought that this is not our core. We will continue our relationship with JMA Rane as a distributor, but we said that having the small investment we are not involved in the management and this is not our core area, so we thought it is better; however, the relationship will continue and it is a very small investment which we are selling to JMA so that they become 100% owners.

Sunil Kothari: Sir, the aftermarket focus and opportunity which we were anticipating that remains, right?

L. Ganesh: Absolutely, our own aftermarket branding that is growing very well, so aftermarket is very vital for us in terms of profitability.

Sunil Kothari: How that is growing Sir, aftermarket, general at large?

Harish Lakshman: Overall, it is good, this year I think over 6% is the overall growth in aftermarket across the group. It has been a mixed bag, the engine components growth has been much lower than both Rane Madras and Rane Brake Lining type of parts and this phenomenon is not only for Rane Engine Valves, but across the industry. Generally, engine-related components and aftermarket growth is coming down year-on-year, I think the engine quality improving, the kind of warranty customers are providing, etc. As far as Rane Madras and Rane Brake Lining is concerned we continue to be quite optimistic and also you have that other aftermarket division that we started within Rane Madras, the RAP, so all those three we are quite positive and we think that this business will continue to grow at about 10%. It is not a very high double digit, but a steady growth but profitability is good in this segment.

Sunil Kothari: Sir, last question is, RPDC, now I think question is of getting some major customer and major orders, but operationally are we overcome the problem whatever we were facing in die cast?

Harish Lakshman: I would say yes and no, if you see clearly there has been improvement from Q1 to Q2 there is improvement. Sunil, what I am not able to guarantee is that every quarter there will be quarter on quarter improvement, there could be some quarters due to some setback and some quarters will be better and we are also having some issues with certain customers there were some quality rejection and accounting thing is not as robust, they delayed by a quarter and then there is a debit charge etc., so some of those things also play a role in the this thing, but to tell you overall definitely there is improvement in the operations compared to where we were of Q3 of last year, the slide started in Q3 of last year, compared to that definitely we are much better, but we are still not where we need to be, so I think there is a lot of focus in trying to get that improvement. In fact, some more resources, when I say resources manpower resources have been sent from India to help improve the operations, so that is one part but I think clearly the more important part is getting new business and I can tell you from last call to this phone call we are far more optimistic because we clearly see some major contracts coming our way.

Moderator: Thank you. We will take the next question from the line of Manish Goel from Enam Holdings. Please go ahead.

Manish Goel: On Rane TRW, I just wanted to know why is the margins being impacted so much, number one, and number two, if you can please give us the breakup of steering business and the occupant safety for the Q2 and comparable number for Q2?

Harish Lakshman: If you see the main drop in margin is because of the safety business on the occupant safety side business and that is largely driven due to couple of things, one is of course the customs duty. As you know in March, the customs duty went up from 7.5% or 10% to 15% for the imports, so obviously that has impacted this business and second is Forex. Of course, we are working very hard to recover all of this from our customers and we are also 95% confident that we will recover the entire amount, but that impact you will hopefully see in the coming quarters, which is why the margin of overall RTSS has dropped.

Manish Goel: So it is just a lag effect which probably will catch up?

Harish Lakshman: Yes, as far as the customs duty and the Forex is concerned.

Manish Goel: I do have a follow up question, but if you can just provide the breakup between the actual numbers of the steering system and occupant safety for the Q2?

J. Ananth: Out of Rs.320 crores, occupant safety is close to Rs.130 crores, remaining is steering.

Manish Goel: Can you repeat, how much is occupant safety?

J. Ananth: For the Q2 FY '19, occupant safety is around Rs.130 crores.

Manish Goel: What was it in the previous Quarter-2, comparable number?

J. Ananth: Close to Rs.120.

Manish Goel: Can you give us a breakup of this Rs.130 crores between seatbelt and airbags for the current quarter?

J. Ananth: Seatbelt is around Rs.70 crores and airbags is around Rs.58 crores.

Manish Goel: For the first half, Sir?

J. Ananth: Seatbelt will be Rs.152 crores and airbags is Rs.110 crores.

Manish Goel: Harish, what we probably saw is couple of days back announcement from one of the competitors that they have retrenched large part of the employees and they did face a problem couple of quarters back and that is where we had gained market share, so you expect that Rane TRW with CV cycle doing well, the steering business will continue to do well?

Harish Lakshman: Correct, definitely we will continue to do well. Obviously, this announcement that has come up day before yesterday, my sense is, this was already a planned thing, this is not a sudden thing, this is the continuation of old problem, so while we strengthened our position in the last eight to nine months and that position will continue, I am guessing that their situation is not going to deteriorate further. I think they have taken this action after ensuring they can continue to have regular supplies.

Manish Goel: Coming to Rane Brake, if I probably see, you did mention that Q2 aftermarket sales were down, but if I just look at the first half numbers as for the aftermarket, because last year Q1 was bad, Q2 was good. This year again Q1 was good, Q2 looks bad, but what we see is that still the aftermarket business on half yearly basis, the number I calculated has seen a 18% growth so from Rs.71 crores to Rs.83 crores, so the sense I would like to get is that this growth number will continue and because now you have taken price hike also, so that should help in the margins going forward?

Harish Lakshman: Yes, this growth should continue.

Moderator: Thank you. We will take the next question next question from the line of Viraj Kacharia from Securities Investment Management. Please go ahead.

Viraj Kacharia: Just had some questions on Rane TRW, in the first half the occupant safety business that you grow like around 10% for the reasons you mentioned, now if we look at historically our own internal expectation on this business if we look at more medium-term, it has been growing at least 20% of our run rate, so do we expect diverse of that growth to continue, if you can elaborate a bit in terms of new OE additions or exports which we are expecting probably in H2 or FY '20 to materialize?

Harish Lakshman: Definitely, this growth will continue and you will actually see higher growth numbers than what you have seen, I mean that is our outlook that is largely driven by export. We are working on some major programs with our partner. As it is exports is growing well and there is some more new business that we are looking at and in domestic also there is some new orders that we are winning as we speak with various OEMs here, so customers like Mahindra, some with Ford etc., so all that will also be in the domestic growth, so the outlook remains positive for the business.

Viraj Kacharia: Just on a question to what the previous participant asked, now if we look at the key competitor for TRW in steering, they will be commissioning the need capacity somewhere in Q4 or Q1 next year, so is there any risk of price pressure in steering considering the kind of capacity expansion they are coming out with?

Harish Lakshman: You are talking of ZF putting up their second plant in Indore or you talking of WABCO?

Viraj Kacharia: ZF.

Harish Lakshman: Personally, we do not think there will be any major price pressure because commodities are continuing to go up and these people have also making an investment and they will have to recover the investment etc., both of us even WABCO are investing in capacities because we are seeing the continued market growth, so we are all investing for growth while we are doing it in our existing location, we have decided to go to a new location, so I do not expect pricing pressure to get impacted as a result of this.

Viraj Kacharia: For Rane Madras how should we look at overall debt levels, in the past we had done our preferential issue partly to repay some of the gross debt which we had which has not really materialized, so going forward considering even if we see on a standalone basis, we have been having a good amount of free cash generation, the investment on PDC incrementally are pretty much on course, so how should we look at overall debt position for Rane Madras?

L. Ganesh: Rane Madras will continue to be comfortable, steering division is generating enough internal accruals to fund its expansion and die cast India for the next couple of years we do not expect any CAPEX because capacity utilization as you know is only around 65% or so. So the only funding that we will require some support for probably RPDC in US which we will be able to do, so I do not expect any significant increase in debt to capital employed in Rane Madras for the next couple of years.

Viraj Kacharia: But in absolute terms should we see any further moderation in debt levels from here on, I mean how should one look at it?

L. Ganesh: I do not remember the numbers going forward how it will look, but our idea of bringing equity is to keep it at this kind of level of not more than 50% debt to capital employed, we think we will continue to operate at that level.

Viraj Kacharia: Last question was on RBL even if we adjust for the one-off in terms of excise duty and other provision, we have also still the jump in other expenses has been quite sharp and that has been going on for last two three quarters, so what cost factors are actually driving this increase?

L. Ganesh: Apart from the things which I mentioned Forex and material prices increase has been an impact. The product mix has an impact because the OE has grown and the aftermarket is negative, there is an impact, as you know the margins are different in these segments and marginal increase in packing and freight, but that is not very significant. We did have a one-time R&D maintenance expenditure in the sense that testing expenditure which we had to do for some new program which we are developing for one of the major customers, so the increase in the dyno we had to upgrade the dyno during this quarter, so it is kind of timing effect, that is about Rs.50 lakhs, so these were some of the one-offs during this quarter.

Viraj Kacharia: Do we book any impact of FX in other expenses? or that's?

L. Ganesh: FX normally goes into the purchase price and anything export goes into sale and any translation goes into the other expenses mark to market.

Moderator: Thank you very much. Ladies and Gentlemen, that seems to be the last question for today. I would now like to hand the conference over to the management for their closing comments.

L. Ganesh: Thank you very much and I know these are uncertain times, I will not say necessarily challenging but some uncertain times we hope that all the segments will continue to grow and we will be able to or see signs of turnaround from one or two of our businesses which need to be done, and hopefully, give you some more positive news in the next quarter. In the meanwhile, wish you all a very Happy Diwali and thank you for joining us.

Moderator: Thank you very much. Ladies and Gentlemen, on behalf of Rane Group, we conclude today's conference. Thank you all for joining us and you may disconnect your lines now.