“Rane Group of Companies Q2 and H1 FY ’21 Earnings Conference Call”

November 12, 2020

MANAGEMENT: MR. L. GANESH – CHAIRMAN AND MANAGING DIRECTOR, RANE HOLDINGS LIMITED
MR. HARISH LAKSHMAN – VICE CHAIRMAN, RANE HOLDINGS LIMITED
MR. P.A. PADMANABHAN – PRESIDENT, FINANCE & GROUP CFO, RANE GROUP
MR. SIVA CHANDRASEKARAN – EXECUTIVE VICE PRESIDENT OF SECRETARIAL AND LEGAL SERVICES, RANE HOLDINGS LIMITED
MR. J. ANANTH – CFO, RANE HOLDINGS LIMITED

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Rane Group of Companies Q2 and H1 FY '21 Earnings Conference Call. As a reminder, all participants' lines will be in listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note this conference is being recorded. I now hand the conference over to Mr. Diwakar Pingle from Christensen IR. Thank you and over to you, Sir.

Diwakar Pingle: Thank you, Vikram. Good Morning, Good Afternoon friends, Welcome to the Q2 FY '21 earnings call of Rane Group. To take you through the results and answer your questions today, we have the Management team from the Rane Group, Mr. L. Ganesh, Chairman and Managing Director, Rane Holdings Limited; Mr. Harish Lakshman, Vice Chairman, Rane Holdings Limited; Mr. P.A. Padmanabhan, President, Finance & 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 a press release and also the latest presentation link of the deck. In case any of you have not received the presentation, you can look at our website or even the BSE site of Rane or you could 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 anything 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 conjunction with uncertainties that we face. These uncertainties and risks are included but not limited to what we mention in the prospectus and subsequent annual reports which you can find on our website. With that said, I will now hand over the call to Mr. L. Ganesh. Over to you, Sir.

L. Ganesh: Thank you, Diwakar. Good Morning Ladies and Gentlemen, thank you for dialing in, I would like to Welcome you all for this teleconference. You would have seen the Q2 FY '21 performance highlights of the group companies posted on our website, just like to provide few additional comments. We saw gradual improvement in the demand environment with the opening of the economy. The plant's Management teams effectively rose to the occasion, handled the sudden ramp up of production from Q1 to Q2 despite continuing supply chain and some labor availability challenges. The group continues to prioritize on cost reduction measures, pursue to minimize the impact on account of the Quarter-1 lockdown which still hangs on our half yearly results. The group aggregate total revenue declined by about 1%, so effectively we are just about flat. Revenue from Indian OE customers grew just by 1% on a whole, however, the revenue from international customers declined by 9% and with cost control and lower employee cost, the EBITDA margin improved by about 166 basis points and the aggregate PBT for the group was about 14.8 crores compared to a loss of 34.8 crores in the previous Q2 of FY '20.

Turning to the brief comments on the companies, the Rane Madras (RML) standalone net sales increased by 8% led by growth in all the segments, sales to Indian OE customers by 5%, international customers by 6%, and a very robust growth in the aftermarket by nearly 29%. Fixed cost reduction resulted in 168 basis point increase in EBITDA margin, the strong growth in farm tractor volumes is helping this business significantly in Quarter-2. Turning to the light metal castings India business is seeing good traction with new orders, in fact I am happy to share that in Q2 we have won a new order of nearly about 36 crores per year from a leading European passenger vehicle customer. With the current order book position, LMCI business is likely to have a very decent performance in the year '21-22. US subsidiary (LMCA) however continues to face challenges based on lower volumes and the COVID impact in the US market is much more than what we see in India and other parts of the world. Significant drop in sales and under absorption of semi-variable manufacturing costs resulted in higher loss in the US subsidiary. We continue to see good progress in operational improvements, however, as mentioned earlier the RML Board is closely monitoring the performance, the order books, the new orders etc. to take a future call sometime by middle of next year on this business.

REVL, the revenue decreased by about 12% driven by a drop in volumes in domestic and international customers, this was partly due to commercial vehicle volumes not picking up and also some diesel engine production coming down among most of our customers. Plants continue to improve operational performance, much better fixed cost control, and reduction in manufacturing costs due to improvement in operational performance like quality, productivity etc. helped to mitigate the adverse product mix and despite the volume drop, we managed the EBITDA margin at similar levels as last year. Rane Brake Linings experienced about a 4% decline in revenue, sales to OE dropped by 8% and the aftermarket segment posted a marginal 1% growth. However, favorable material price movement and product mix helped in margin improvement. There was also a one-off selling price correction, which we got from the customers for prior periods and there were some write back of provisions, so this also helped in this quarter. As you are aware, Rane Brake Linings announced a buyback. This decision was taken by the Board considering the cash reserves in the company and the fact that not much of CAPEX is required for the next couple of years given the capacity utilization currently, so to utilize the cash reserves at least part of that, a decision was taken to buy back shares, this buyback is now underway.

Turning to the joint venture, Rane TRW had a 3% decline in revenue, revenues from steering gear products declined due to some volume drop in the export business and also muted volumes in the commercial vehicle segment. Revenue from the occupant safety system increased on account of better schedules from international customers, under absorption of semi-variable manufacturing cost resulted in marginally lower EBITDA in this company. Rane NSK sales increased by nearly 8%, this was due to the better off take in served models and as you know, Maruti Suzuki, a major customer has done very well in Q2. Lower employee cost and reduction in other fixed cost helped in margin increase. There was an extraordinary expense of Rs. 20 crores, which is an incremental provision towards product warranty claim. We remain cautiously optimistic about the sustenance of demand post festive season, we will have to wait and see but as of now the indications are that Q3 schedules are quite good from customers. With these opening remarks, I take this opportunity to wish you all a very Happy Diwali and safe festival season and hand it over to Harish for his comments after which we will take your questions. Thank you.

Harish Lakshman: Thank you. Good Morning everybody, just a few more comments from my side relating to the market, the past quarter Q2 was an extremely challenging quarter and in many ways exact opposite of Q1 where we struggled to ramp up volumes and meet customer demand because of the strong recovery in the domestic market. To compare the group's performance vis-a-vis the market, let me share some details around the vehicle segment. Our performance is better than most of the major vehicle segments except the farm tractor and small commercial vehicles where our presence is less than 3%. In the farm tractor segment, although we had a positive growth rate, the growth is lower than industry rate due to the lower growth of manual steering in tractors compared to the power steering, while we are there in both segments, our market share in manual steering is much higher, so hence the growth is lower. In the passenger vehicle segment, the higher off take in the served model help us perform much better than the industry. In the LCV segment, the increase in penetration of power steering resulted in higher PACK value and higher growth from Rane TRW and in M&HCV segment, we also managed to increase our share of business which helped us achieve better performance in the industry. The growth in two-wheeler segment is driven by share gain with some of the key customers as well as better off take in some of our served models. At the market segment level, our sales to the Indian customers grew by 1% over last year. Revenue from Indian aftermarket grew by 9% whereas our sales to international customers declined by 9% specifically coming from engine valve train business that we supply from REVL and some of the hydraulic power steering from RTSSL. As per Q2 FY '21 sales, our international business is about 23% of the total group turnover, so with these few words, we will now open up for any questions that you may have. Thank you.

Moderator: Thank you very much, Sir. Ladies and Gentlemen, we will now begin the question and answer session. We have our first question from the line of Shyam Sundar Sriram from Sundaram Mutual Fund. Please go ahead.

Shyam Sundar Sriram: Sir, Good Morning, thanks for taking my question, Sir wonderful performance on TRW per se, you have highlighted in the presentation of increase in share of business in these commercial vehicle steering side, if you can comment on that, and secondly, how much was exports this quarter and how are we looking at exports, we have also commented on new export order to Russia, so if you can give some perspective on both of these points?

Harish Lakshman: The first one is because of good work done by the Management last year in terms of ensuring our power steering models are engineered on all the BS6 vehicles as you know from April 1st, the production has all moved to BS6, so, that helped us to achieve a significant increase in share of business. Of course, eventually competition will catch up and it will be difficult for us to sustain this kind of share, but of course we will continue to be the market leader, so I hope that answers your question. As far as exports I will ask Mr. Ananth to answer.

J. Ananth: The total export of RTSSL is close to 110 crores.

Shyam Sundar Sriram: Okay, and which means which is very close to what we were doing last year per se on a like-to like-basis, last year we did around 115 odd crores?

J. Ananth: Yeah, correct.

Shyam Sundar Sriram: You also commented very strong export momentum, so this revenue per quarter from an export will increase going forward into the future quarters, is that the fair understanding and the new export order win to Russia will also start by this fiscal year itself?

Harish Lakshman: The answer to your first question is yes, it will continue but not in this fiscal year, I think that export to Russia is 2023.

Shyam Sundar Sriram: Thanks for that Sir, and secondly, on the NSK side Sir, you spoke about our revenue momentum has been better than the underlying production, so one is on the served models for Maruti has done better for us, secondly LCV also is there any pickup from that side also for NSK?

L. Ganesh: Rane NSK, the manual column for commercial vehicle, we are extremely well positioned, so like Rane TRW what Harish mentioned, it so happened that we proactively worked on all the BS6 models, so we are extremely well positioned so as the commercial vehicle business picks up which is expected to happen in the second half, we will benefit from that and on the LCV with Ashok Leyland, Tata Motors, we are very well positioned and with M&HCV also gradually all the new generation vehicles will have our columns.

Shyam Sundar Sriram: Thanks for that Sir, and generally on the fixed cost initiatives in RBL also we saw very good fixed cost reduction similarly on the Rane Madras standalone, if you can comment on how much do we expect, will these costs normalize as the business momentum normalizes in the second half of this fiscal year and specifically on RBL, the gross margin we had very good improvement there, so you did comment on the lower commodity prices and price hikes. With this commodity benefit, we can assume to sustain there, is that a fair understanding on these two?

Harish Lakshman: As far as fixed cost is concerned, definitely this kind of savings is not sustainable. Many of us in the industry including Rane, all the management and in many plants even the unions took a salary cut which flowed into the Q2 and now we have started restoring compensations because the market is close to coming back to normal, so a large part of the fixed cost is also salaries of employees, so obviously that savings is not sustainable, but many additional cost-saving measures that the company undertook, we definitely see several of those initiatives continuing even into the coming quarters, so therefore while one significant portion will not continue, there are some certain other initiatives that will continue. As far as RBL is concerned, I think we had also mentioned after the quarterly results in the media that one of the main reason, of course in addition to the commodities, the main reason was there was a one-off price settlement with one of our customers that was recognized in that quarter, that is the main reason. Now, but to comment on commodities, we are definitely seeing pricing is hardening- steel, iron, scrap, everything is starting to go up, we are starting to get pressure from our suppliers for price increases and of course we have already started engaging in conversations with our vehicle manufacturers on the same, so I think commodities we will start seeing an increase in the coming quarters especially if the demand continues.

Shyam Sundar Sriram: Understood Sir, from NSK perspective on the warranty provisions, if you can give some comment we thought that probably the first quarter would have been the last quarter of provisions, so from that perspective how are we seeing things panning out for the remainder part of the year and what is the outlook there per se and any new order wins per se from NSK that you would like to highlight at this point?

L. Ganesh: As far as the warranty is concerned, some warranty returns still continue although we are able to identify most of them to the pre-countermeasure production, so some bunching up also perhaps happened during the lockdown, we were not getting anything. Now, after that the vehicle usage has started increasing, but we are not fully clear, but some pre-countermeasure claims continue to come. Hopefully, this should start coming down now. We are watching this very closely. We will get a better picture in the next two months, but as I mentioned in the last time also, the impact will be nowhere near 2019-20, it will be much less but it has not completely disappeared, claims still are coming, so as an abundant caution we have made a provision this quarter also. New orders continue, we bid for businesses, we get some, fortunately so far this has not affected any of our new orders although recently there have been no big order coming from any of our customers, but as a routine winning orders for new platforms.

Shyam Sundar Sriram: Thank you sir. I will call back in queue in case of any other questions.

Moderator: Thank you. The next question is from the line of Pratik Kothari from Unique Asset Management. Please go ahead.

Pratik Kothari: Good Morning Sir and thank you for the opportunity, my question is on the RPDC part where you mentioned that the Board will take a view somewhere in the middle of next calendar year, if you can just talk about internally what are the parameters that we are looking at which will decide as to either continue with this decision or to flip it, just quantitatively if you can, what are the things that we are looking at?

Harish Lakshman: It is a very difficult question to answer the specific parameters, it is a combination of so many things in terms of customer order booking, efficiency improvement in plant, interest rates etc., but ultimately the key metric will be sustainable profitability and ensuring that we can get a return on the capital that we are employing there, so that will be the ultimate metric, so we need to have the visibility for that, so that is what Mr. Ganesh said that we will take a view in the middle of next year whether that visibility is there or not.

Pratik Kothari: Like you said two or three points which you said you looked at a combination of everything in terms of visibility, so in terms of if you look at visibility today, what should change six months later that will help us change our way, because I believe currently we do not have enough visibility on that part at least, what should change in the six months at least in the terms of customer booking etc. that will help us make the decision?

Harish Lakshman: The key is customer booking whether some new contracts that we are winning, many are undergoing negotiations and also there are I think we have already announced there are two new businesses that we are launching in Q4 of this year that is January ’20-21, between Jan-Feb-March that quarter, we are launching some new customer programs, how they take off, it could do much better than market, so those are the things.

Pratik Kothari: This is on the non-auto part, right, the one you are launching in Q4?

Harish Lakshman: One is auto and other is non-auto.

Pratik Kothari: Fair enough, and just to reconfirm, in middle of next year is when the Board will decide, June-July next year?

Harish Lakshman: Yeah, we will take a view at that time on what the future is for that business.

Pratik Kothari: Fair enough Sir, season greeting to everyone and all the best.

Harish Lakshman: Thank you.

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

Naresh Ranka: Sir, a very Good Morning, and hearty congratulations on decent results and thank you for the opportunity, I would like to know currently what will be the capacity utilization of all the plants, basically Rane NSK and Rane TRW, currently what will be our capacity utilization levels?

Harish Lakshman: Again, it varies from plant to plant depending on the customer mix, but I would say for Rane NSK and Rane TRW at least on the steering side maybe in the range of about 70% to 80% would be the utilization levels, whereas on the occupant safety side it is probably closer to 90%.

Naresh Ranka: Sir, just one more question, generally we have seen that for auto ancillaries if they have more share of business in the aftermarket, it is more profitable, but I feel that our Rane Group share of business in the aftermarket is lesser than our competitors like when we see Talbros and all that, so are we doing anything to increase our presence both domestic and international aftermarket business?

Harish Lakshman: You are asking specifically on steering or general?

Naresh Ranka: Generally, Sir, because steering and suspension will be the major components?

Harish Lakshman: Generally, Rane has a reasonably solid presence in the aftermarket, in fact our number one product line is brakes, you know Rane Brake Lining, the products that we make in Rane Brake Lining, I think almost 45% to 50% of that company's revenue is aftermarket and Rane Madras also it is substantial, we definitely are a market leader in many of our product lines, I would think we are significantly larger than QH, as a percentage it may not be comparable because Rane Madras has a lot of steering products that we do, we do exports to multiple countries etc., so aftermarket as a percentage of RML maybe smaller because the OE thing is bigger because of exports etc., but I would think aftermarket to aftermarket comparison we should be even larger than QH.

Naresh Ranka: Okay, because what I can see from the stats available, I think maybe we are little lesser especially Rane Madras, I think we have 15% of the business is maybe aftermarket, is there any more potential to increase because Rane TRW and Rane NSK I think almost lower presence in the aftermarket?

Harish Lakshman: Rane TRW the steering side definitely there is some aftermarket potential, but it will not be as large as what we see in Rane Madras or Rane Brake Lining and of course on the occupant safety side, the aftermarket is almost non-existent because we make seatbelts and airbags and even for Rane NSK, there is not a significant opportunity.

Naresh Ranka: Okay, even the loose components do not have a potential, the loose components?

Harish Lakshman: Yeah, very little, I mean as I said in Rane TRW on the steering side, there is some, but it is not significant.

Moderator: Thank you, Sir. We have next question from the line of Ashwin Agarwal from Akash Ganga Investments. Please go ahead.

Ashwin Agarwal: Good Afternoon Sir, earlier, you had mentioned about 80 to 90 crore per annum order for General Motors through Nexteer for rack and pinion, so has this business commenced or when will it commence?

Harish Lakshman: It has commenced that is the good news Ashwin, it has commenced from last month.

Ashwin Agarwal: Okay, and the size remains the same, the size of 80 to 90 crore per annum remains the same?

Harish Lakshman: Yeah, as of now it is looking to be the same.

Ashwin Agarwal: You spoke that if this goes well, we can get additional orders of the same product, is there a possibility?

Harish Lakshman: I mean definitely there is a possibility, there is no firm order booking as yet because obviously they want to see our performance, but there is lot of discussions going on and the pipeline is looking healthy.

Ashwin Agarwal: Sir, you had also spoken about some ball joints order from Daimler and few other customers, so have those orders commenced and what is the status?

Harish Lakshman: I am not clear, which one directly to Daimler or?

Ashwin Agarwal: I do not know, Daimler. You said some ball joints orders have commenced or you have secured some orders?

L. Ganesh: Daimler we have not got any direct export orders, but other ball joint export orders we have been getting, but not in terms of value not so high as rack and pinion, but we are getting export orders in ball joints.

Ashwin Agarwal: So what can be the exports of Rane Madras in next two-three years because of the domestic COVID scenario and also our subsidiary which we already spoke about, how can we scale up our exports, what are the ideas or what are we planning to do so that we can make this big?

Harish Lakshman: Ashwin clearly exports is a major focus area of our Rane Madras and I can tell you that the way the current book of order, firm order that we have on hand and the pipeline that we have I think there is visibility that it will grow faster than the domestic market, of course, now if next year domestic market starts growing at 25% or something like that then it is a different matter, but let us assume the Indian car market is going to grow at 10% to 12% and commercial vehicle market is going to grow at 8%, if that happens, the export will be even higher than that.

Ashwin Agarwal: Okay, and this will continue for next two years?

Harish Lakshman: Including the casting business also, as Mr. Ganesh said, I think as far as the India Casting business, the worst is behind us and the order books are now good and production has started etc., so that is also part of Rane Madras.

Ashwin Agarwal: We had a capacity of around 170 crores of domestic die casting, so what can be the revenue next year from, this year I am not looking at, next year maybe?

Harish Lakshman: 170 crores is not domestic, total value capacity that has been there is about close to 170 crores, next year we should be very close to that number.

Ashwin Agarwal: Next year?

Harish Lakshman: Yeah, next financial year.

Ashwin Agarwal: Okay, and the cost-cutting also lot of measures we had taken on that front?

Harish Lakshman: Correct.

Ashwin Agarwal: Wish you all the very best and we hope we can take some decisions on our US subsidiary maybe next year?

Harish Lakshman: Absolutely.

Ashwin Agarwal: All the best sir, thank you.

Moderator: Thank you. We have next question from the line of Manish Goyal from Enam Holdings. Please go ahead.

Manish Goyal: Thank you very much and very Good Morning, Sir on the warranty claim provisions in Rane NSK, just want to know that has the problem been identified and has it been resolved so that going forward we do not have further claims?

L. Ganesh: As I have been telling you, it is a very complex problem and actually NSK and ourselves we have been breaking our heads on this, so we believe we have identified all the issues, there were some product issues, some manufacturing issues also. We believe that we have identified and put countermeasures in place, so one positive sign is post countermeasure, the products that are coming back for warranty is very, very miniscule almost 0.006/0.0007 percentage. That is the trend we have seen, which makes us believe that the countermeasure has been effective, but whatever we are getting till now is the pre-countermeasure production,. As I explained last time, it depends on the mileage, so the usage and mileage we cannot predict how each person uses his vehicle and sometimes after two years, two-and-a-half years it comes so that is the reason why we have not been able to fully correctly predict, but as far as countermeasures are concerned, the indications are that post-countermeasure the warranty claims are very, very small percentage, so we think we are behind that as far as the problem is concerned.

Manish Goyal: Thank you so much, and on Rane TRW would it be possible to share the revenue breakup between the steering business and the occupant safety overall basis?

Harish Lakshman: For the quarter?

Manish Goyal: For the quarter and half yearly, Sir.

J. Ananth: For the quarter, the steering business is close to 100 crores and occupant safety is around 170 crores.

Manish Goyal: As compared to last year quarter?

J. Ananth: Last year quarter steering was 112 crores, occupant safety was 172 crores.

Manish Goyal: Okay, and can you please provide for half yearly as well?

J. Ananth: Half early the steering number is 123 crores for the current year first half and occupant safety is 240 crores.

Manish Goyal: Can you provide the comparative numbers as well?

J. Ananth: Comparative of previous year first half for steering is 286 crores and occupant safety is around 350 crores.

Manish Goyal: Sir, coming to Rane Madras die casting domestic business, like what we understand that earlier due to underutilization, we were incurring losses so on full utilization assuming next year we probably reach near to our full utilization, what kind of EBITDA and PBT margins we can see, just a ballpark number and how much of that would be exports of that total revenue which we book next year?

Harish Lakshman: As you are aware in the last two years, the investment we made in India for the casting business, we had problems because some of the export orders did not take of the way the volumes we were anticipating and then one order we had lost etc., so we desperately started looking for new orders and in the process we started getting more domestic business, that was in the last two years and now in the last six to eight months we have now started winning a lot of export orders as Mr. Ganesh also mentioned and they all kick in '22-23 etc. now, the profitability of export business is better than domestic business, so therefore while you will see a significant growth in the next 12 to 24 months that is coming from a mix of domestic and export with a higher proportion of domestic, so now to answer your question on EBITDA, we have said at one point in time, we were looking at about 14%-15% EBITDA, but the more domestic we do, obviously the margin is lower, so I do not know the exact numbers, but maybe in 11%-12% is the number that you will see.

Manish Goyal: 11%-12% at EBITDA level or PBT level?

Harish Lakshman: EBITDA, since your question was specific for next year I am answering. If you ask me what is the long-term sustainable EBITDA for this business, it is higher.

Manish Goyal: Ok sure. Thank you so much, I will get back to you in case of any queries.

Moderator: Thank you, Sir. We have next question from the line of Sreemant Dudhoria from Unifi Capital. Please go ahead.

Sreemant Dudhoria: Good Morning and thanks for the opportunity, I joined the call a bit late, so maybe I may be repeating this question, the question is specifically on Rane Brakes, last year we saw an increase in the gross block in the company and could you please comment what could be the additional CAPEX addition for the next two years in Rane Brakes and what is this related to, is it for domestic market or it is for the exports? That's the first question.

L. Ganesh: Well, in terms of CAPEX last year significant CAPEX was mainly on R&D, we have now fully kind of equipped ourselves for R&D so we do not expect significant investments in that R&D for the next two-three years. Capacity also we are currently at about 70% to 75% utilization, so again for the next couple of years, we do not expect any significant CAPEX in that business.

Sreemant Dudhoria: Okay, so out of the 40 crores of CAPEX that was done last year, how much was towards the R&D and what was this related to because there is a significant increase in the gross block?

L. Ganesh: I will just check and get back to you.

Sreemant Dudhoria: Sir, the second question is again on Rane Brakes, if you could help us provide a mix between the asbestos and the non-asbestos braking both in the OE business and in the aftermarket, what is the mix right now and what could be the transition in the next couple of years?

L. Ganesh: In terms of OE it is almost 100% non-asbestos, asbestos free so in terms of aftermarket, some of the commercial vehicle brake lining still is asbestos, but we are gradually introducing new asbestos-free products in the market which is gaining traction, so our idea is in the next two to three years, we go completely to asbestos-free including the aftermarket.

Sreemant Dudhoria: Sir, some of the leading regulators in the developed markets are transitioning towards lower copper content in the braking systems, is there any such regulation in Indian markets and should we expect anything of that to be coming and do we have the R&D to make that?

L. Ganesh: Well, to answer your question not yet in India market, but this trend in the global market what you say is right, so Nisshinbo, our partners have already developed the copper free formulation for their American customers, so whenever it is required, we will be able to introduce those combinations in India.

Sreemant Dudhoria: Sir, how does export look in the braking systems, should we see a strong growth in the braking systems export in the coming years, should the proportion in the overall mix increase?

L. Ganesh: So far the export focus has not been there in this business and we have been focusing more on the domestic market and whatever exports we are doing, it has been in the regional areas, neighboring countries etc. little bit to the Middle East, but now the company is focusing a lot on this, so from 3%-4% of sales, we would like to take it to about 10% in the next two to three years 10% of sales, so lot of focus now we are working seeing other markets, studying other markets, so certainly we would like to take it to about 10% of sales in the next couple of years.

Sreemant Dudhoria: Sir, is there an opportunity for us to export in the aftermarket business of Nisshinbo?

L. Ganesh: Nisshinbo does not do any aftermarket, so therefore we have the freedom to do it in any market that we want that is how we are now, our strategy is based on that, we are trying to understand and get approvals for aftermarket formulation in other markets, so Nisshinbo does only OEM.

Sreemant Dudhoria: To the OE developed markets when Nisshinbo supplies, is there opportunity for us?

L. Ganesh: OEM, it is very, very difficult, this is a safety critical product and most customers before buying, they are very, very cautious on this particular product, so while some niche areas are possible, bulk OE buying from outside so far we do not see that trend, but we see lot of aftermarket opportunities.

Sreemant Dudhoria: Fine Sir, lastly on our gross margin has expanded in the current quarter in the braking systems, how sustainable are these margins going forward?

L. Ganesh: As Harish explained earlier before you joined, partly it was because of an old price correction which we got for previous period, which was credited during this quarter and also there were some provisions we had made earlier for slow-moving materials etc. due to COVID, which has started moving and some write backs were there, so that is the reason why the profitability jumped up so much, that is not sustainable. Out of the 40 crores CAPEX that you asked, almost 25 crores were R&D.

Sreemant Dudhoria: Sir, this is a significant R&D expense, could you please elaborate what was this related to and how will this help us in the coming times?

L. Ganesh: We have equipped ourselves with various types of dynamometers, and these dynamometers help us in testing and validation, so we have probably got the most sophisticated for rail Metro braking blocks, we have got for passenger cars, now we have equipped ourselves for two wheelers, last year we equipped ourselves with the latest including noise and vibration and harshness, NVH capabilities, so we probably have the best facilities for R&D in India in this field of friction material and this will help us for many, many years to come.

Sreemant Dudhoria: 16 crores was towards the capacity building, so we see?

L. Ganesh: No, there was also a solar, we invested in a solar plant in one of our plants in Pondicherry, so I think it was a 3 Megawatt, so there was a solar investment also, so capacity was more balancing last year. There is no significant investment in capacity, some balancing equipment etc. was added here and there, but no big line was added.

Sreemant Dudhoria: We do not see any further significant increase in the capacity?

L. Ganesh: Not for the next couple of years.

Sreemant Dudhoria: Sir, on the operating margin front, so our sustainable margin should be in the 11% and 11.5% range, operating margins?

L. Ganesh: It always varies in this company based on two important things, one is the product mix, segment mix and aftermarket does well margins improve and commodity prices and Forex, so very difficult to predict because it is very heavily dependent on these three factors, but obviously our attempt will be to try to maintain as healthy a margin as possible.

Sreemant Dudhoria: Sure sir, Thank you so much.

Moderator: Thank you, Sir. We have next question from the line of Shyam Sundar Sriram from Sundaram Mutual Fund. Please go ahead.

Shyam Sundar Sriram: Sir, thanks for taking my question again, basis your interaction with various OEMs across vehicle segments over a period of say one-and-a-half years per se, I am just giving a slightly broader perspective, how are you seeing the production or outlook from the different segments, commercial vehicle, passenger vehicle, tractors, if you can give some perspective on basis your discussions with the industry participants?

Harish Lakshman: Definitely, the mood is very upbeat and I think as Q2 has shown, the recovery has been stronger than what most of us expected and most of the OEMs are of the view that this is going to sustain in the coming months while post festive season in December may be early part of January, there will be a slight dip, but they are of the view that this will sustain and going forward the next financial year should also be a much better year, so the general mood is very upbeat. In Rane, we are taking a very cautiously optimistic approach just because the economic impact of COVID on the GDP has been so high, it is not clear whether what we are seeing in Q2 and some in Q3 is a combination of pent-up demand and festive season because April, May, June, there were almost no sales, very little sales, so therefore if there is a pent-up demand that is catching up or whether it will sustain is still unclear, so we are taking a little bit more conservative approach about the immediate future.

Shyam Sundar Sriram: Understood Sir, on commercial vehicles on the heavy commercial side specifically, can we assume that the worst is in the past and then incrementally the volumes will get better from here from a production perspective?

Harish Lakshman: Definitely it is going to get better, but let us be clear, the volume we saw in 2018-19 sitting where we are today, I do not think we will see that till '23 where the industry was, M&HCV industry, so we have come down significantly, but I think clearly the bottom is behind us and month on month it is improving, so that is definitely an encouraging sign and I think even all the NBFCs are beginning to talk more positively about truck buying etc.

Shyam Sundar Sriram: Understood Sir, on TRW from a domestic occupant safety perspective we had highlighted the starting of seatbelt orders for Maruti and even new order from Hyundai and when we compare from last year levels, it does look like the domestic occupant safety has also started moving up well, so how much is the domestic occupant safety within the occupant safety itself for the first half, I understand the industry volumes would have been pretty low, but just to get some sense from a mix perspective, how has it moved from last year to now, Sir?

Harish Lakshman: It is about the same, it is 40:60 mix, 40% domestic and 60% export.

Shyam Sundar Sriram: Okay, understood, Sir one last question, if I may squeeze per se, the Government has announced a production linked incentive mechanism, according to you what are the top five aggregates that are more reliant on imports and where the Government may want to reduce the import content per se, I mean the finer details are not yet available, but from your perspective, from an industry perspective what could be the top five aggregates that could be focus area for the Government to act on it from this perspective?

Harish Lakshman: It is still too early because only yesterday the announcement was made and there are absolutely no details in it, I mean while clearly electronics is one general area where import dependence is high, so there will be more and more pressure on to bring localization of electronic items, but my understanding is this scheme is also focused on enhancing exports in a significant way, I think there are likely to be some incentives for exporting companies as well is my understanding especially because the auto industry has been hurt very badly with the withdrawal of the MEIS scheme, which is an important part, so my understanding is this scheme, this production linked incentive scheme will also try to solve the problem that was created by withdrawal of MEIS, of course these are all just what we read in media and what people like ACMA and all have been lobbying in the Government, we are waiting for the details.

Shyam Sundar Sriram: Understood sir, Thank you so much.

Moderator: Thank you, Sir. As there are no further questions from the participants, I would now like to hand the conference over to the Management for closing comments. Over to you, Sir.

L. Ganesh: Thank you very much, I wish you all a very happy and safe Diwali.

Harish Lakshman: Thank you all, Happy Diwali to each and every one.

Moderator: Thank you very much, Sir. Ladies and Gentlemen, on behalf of Rane Holdings Limited, that concludes this conference call. Thank you for joining with us and you may now disconnect your lines.