"Mahindra CIE Automotive Limited Q4 CY '17 Earnings Conference"

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MANAGEMENT: **MR. HEMANT LUTHRA – CHAIRMAN, MAHINDRA CIE AUTOMOTIVE LIMITED**
MR. ANDER ARENAZA ÁLVAREZ – CEO, MAHINDRA CIE AUTOMOTIVE LIMITED
MR. K. JAYAPRAKASH – CFO, MAHINDRA CIE AUTOMOTIVE LIMITED
MR. VIKAS SINHA – SENIOR VICE PRESIDENT, STRATEGY, MAHINDRA CIE AUTOMOTIVE LIMITED

MODERATOR: **MR. VENIL SHAH – RESEARCH ANALYST, ICICI SECURITIES**

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Mahindra CIE Automotive Limited Q4 CY '17 Earnings Conference Call hosted by ICICI Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Venil Shah from ICICI Securities Limited. Thank you and over to you, Sir.

Venil Shah: Good Afternoon everyone. Thanks for joining us for the Mahindra CIE Automotive Q4 CY '17 Earnings call. From the management side, we are represented by Mr. Hemant Luthra, Chairman; Mr. Ander Arenaza Álvarez, CEO; Mr. K. Jayaprakash, CFO; and Mr. Vikas Sinha, Senior Vice President, Strategy. I would now like to hand the call over to the management for their initial remarks. Over to you, Sir.

Hemant Luthra: Welcome everybody, thank you for joining us. This is Hemant Luthra and I normally use this introductory time to say something, but I think given the results that we have got for the year and for the quarter, there is no point trying to gild the lily. The effort of the team and the results that they have produced speaks for itself, so rather than take up more air time, I am going to hand it over to Vikas who will analyze what we have already put on the website to you and then when we will get into question and answer mode, feel free to direct the questions if you have somebody specific in mind, whether you want to Ander to respond, please do so; if you want Vikas as the Head of the Strategy to respond, he is there or JP – our CFO, and they will take the tough questions, I will take the easy ones and we can get started.

Vikas Sinha: Thanks Hemant. Good Afternoon to all, I also welcome Mr. Ander Arenaza, our CEO, who is present on the call. I will make a few comments on the investor presentation about MCIE performance in the fourth quarter and full-year CY '17 before we open the call to questions. We start the presentation with Slide three, which presents the simplified legal structure of Mahindra CIE. This is one of the key highlights for this calendar year and these highlights are presented on Page 4. In this year, we have simplified the legal structure by merging Mahindra Gears into MCIE and eliminating all Mauritius subsidiaries. Our Mexican plant spearheaded by Bill Forge is now operational. Bill Forge India has also inaugurated, and automated machining plant meant for global supplies to Ford F150 trucks. On the customer front, we have acquired new customers in gears and stampings divisions in India. We have also started supplies in small numbers to electric vehicles from a stampings and composites division in India. It is to be noted that the results of Q4 C '17 is also the first full quarter of direct comparison of quarterly results, post the merger of Bill Forge. We will start with India results on Pages five and six.

MCIE India had an excellent performance in 4Q C '17 in both revenue and profitability. EBITDA increased by 25% when compared with the same period last year leading to a 0.6 increase in EBITDA margins. Year-on-year, quarterly growth was 18%. If we remove the positive impact of Bill Forge, the rest of the divisions in India grew 16% versus 4Q 2016. The sequential comparison of MCIE India versus the previous quarter Q3 C '17, shows a slight decline, but that is largely due to provision for VRS and forgings and other one-offs. Without these one-offs, the MCIE India EBITDA margin would have been 15% in Q4 C '17. The full-year C '17 result also tells a similar story of increase of growth and improvement in profitability. The full-year EBITDA margins have grown from 11.5% to 13.3%. The growth of MCIE India minus Bill Forge is a healthy 16% while the EBITDA margins have remained similar. The main driver of our growth in India has been the positive market evolution across segments as well as the growth of our key customers. It should be noted that MCIE India has grown higher than its key customers namely M&M, Maruti, and Tata Motors both in 4Q '17 and over the full-year C '17. A word about Bill Forge, while we do not show its results separately, its performance has been in line with expectations that had been set out at the time of acquisition. On a full-year basis, it has achieved an EBITDA margin of approximately 20% and revenues of close to Rs. 7000 million.

Our European results are shown in Pages seven and eight. On a quarterly basis, MCIE Europe has grown by 24% in 4Q where we have had a 5% positive exchange impact, but this includes the full-year impact of increase in prices as Germany to the tune of Rs. 68 million and this increase is not just for one quarter. The equivalent full-year growth figures are 11% and that too there is a negative exchange rate impact of 1% reducing it to 10. The growth is driven by growth at CIE Forgings and Metalcastello. Profitability has improved on a year-on-year basis both in 4Q and full-year results and the EBITDA margins for MCIE Europe in C '17 is 13.6%. Quality and delivery issues at our German operations have been resolved. Now, if we go to Slide nine and 10, we will see the consolidated results for Q4 C '17 and full year 2017, which are a combination of the positive evolution in both India and Europe. The consolidated sales are at Rs. 62,456 million at an EBITDA margin of 13.5%, which represents a growth of 22% in sales and an improvement in margins by 2.4%. In the Slide 11, you will see our balance sheet and working capital situation has improved in line with what we had mentioned on our previous calls. Our overall net debt situation is slightly better to what it was at the end of last year and now stands at Rs. 9029 million. Please note that we have on page 12 mentioned the CAPEX of Rs. 3054 million on a consolidated basis and a significant amount of this is growth for CAPEX whose breakup is given in the notes on Page #12.

At this point, we would also like a minute to talk about the key financial parameters which we monitor and which I mentioned on page 13. We can see EBIT at 9%, which is close to the target of 10%. RONA is also better compared to last year at about 12%. All the other parameters are in line with our expectations. On Slide 14, we have charted the evolution of the revenue and EBITDA percentage since we switched to the sales without excise format of reporting. The sustained and continuous improvement is a reflection of the strategy adopted by Mahindra CIE. This strategy is explained in Slide 16. For the Europe, the focus will be on existing projects of the new crankshaft machining line at Lithuania and ramp up of the Caterpillar order at Metalcastello in Italy. In India, the integration with the parent CIE is getting tighter with Synergy projects being identified for process improvement and technology transfer, and some of these projects have been described in Slide 17, 18, and 19, which was something that you have asked for in the past. These elucidate the specific objectives, the CIE partnering, process and benefits envisaged and accrued so far. If anyone wants any details on these case studies, they are very welcome to circle back to us, and now with this I will hand over the call back to Hemant for his final comments before the Q&A.

Hemant Luthra: As I said on behalf of the team, we are very pleased with what has happened. It does not happen too often that we have a quarter on quarter increase of 22%, we have a quarter on quarter increase of 96% on EBITDA on a consolidated basis or year-on-year increase of 48% on a consolidated basis for Mahindra CIE, so Gentlemen it is all over to you. If you let us, let me handle it, I will direct the questions, otherwise, you are more than welcome to direct the questions directly to the CEO or to the CFO or to Vikas. Back to the moderator.

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 Ronak Sarda from Axis Capital. Please go ahead.

Ronak Sarda: Two questions, first on Bill Forge, if you can just highlight how the Mexico plant ramp up is going through and the new Ford F150 that would be exports from India, right?

Vikas Sinha: Yes, that is right.

Ronak Sarda: What is the revenue potential for this order?

Hemant Luthra: Ander, the question was how is Mexico doing and the F150 orders that are coming are they exported from here or where?

Ander Arenaza Álvarez: Yes, I was last week in Mexico, the company is now in the ramp up process of our customer product, the main product that we launched in Mexico. We have started the production I think in approximately March-April last year. Right now, we are at let us say 50% of the output more or less and we continue growing, so the company is performing better and better. We have this learning curve in that and we are supporting them also with the CIE team in Mexico, we expect that this company will be at full rate by the end of this year. Now, we are following our customer demand. On top of that, we got a new project for another customer and we decided, we have to let it build in addition onto create bigger building for this new project and we are new press that is now being ready and we will keep up during March the company, what we are now really happy with the performance of this plant and we will continue growing in the next year, so we expect to have in this moment the sales are very low as we are ramping up, but we will tackle the output in the next month and after the new project is starting, we will be growing even more, so we expect to have a very good let us say growth and very positive impact in the CIE, thanks to the Bill Forge Mexico plant.

Ronak Sarda: Just if you can quantify how large would be this F150 export order?

Hemant Luthra: I think this is competitive information, I think we would not have highlighted it if it was not substantial, but I am uncomfortable without getting the approval of specific customers whether we can speak about volume of export orders because that might then reflect on how many F150 they are selling and so on and so forgive me not.

Ronak Sarda: This is largely for the US market?

Hemant Luthra: I would imagine so.

Ander Arenaza Álvarez: It is for the US market, yes.

Ronak Sarda: Second question is on the Europe business, both MFE and the CIE Europe business, how do you look CY '18 in terms of revenue growth and we have kind of achieved the best margin for that business, so are we still looking to improve it or this would be the sustainable performance going ahead?

Hemant Luthra: It is always in the improvement mode, but since Ander has been responsible for supervising what has been happening in Europe, I am asking Ander to talk about what has been done at the plant and maybe Vikas can tell you about what is happening in the market, and therefore, you will get a more complete view?

Vikas Sinha: The market growth is whatever it is and you know we have presented all market growth data in one of our annexure, so that detail is there but the growth in Europe is essentially coming from these two projects that I have highlighted, the Caterpillar project at Metalcastello and the crankshaft project in CIE, Lithuania.

Ander Arenaza Álvarez: My answer regarding the MFE German business that as you know that was our main concern in 2016 where we had this not properly done closure of Jeco plant that created a lot of stress and difficulties also in the deliveries and quality with customers and let us say that decision was tough. During 2017, we have sold and we have consolidated all the management and we have started supplying with normality, even you saw that we had important growth more than 10% of growth in this business and we are finally also in positive EBT numbers, so it is true that we did a great job in 2017 and we expect to continue improving, of course, this is we are still below the CIE Standard in Germany and we need to continue working, yes. It is tough because it is not a easy environment, but the strategy is to continue improving the business and as Vikas explained, we have also growth strategy especially in Metalcastello with all this Caterpillar businesses that are now ramping up and also with new crankshaft line that we installed in Lithuania plant and this will give us additional growth to the businesses, so my view is that we will continue growing. In 2017 when the market grew something like 2%, our growth in Europe was more than 10%, about 8% to 10% that means that we were far above the market and in 2018, we expect to continue growing. The demand in the market in this last month continues let us say very, very high.

Ronak Sarda: What I wanted to understand was given these new orders assuming industry remains where it is, can we achieve this 10% growth again, how large are these orders if you can just highlight?

Hemant Luthra: Ronak, I do not know whether, we will maintain a momentum but do not ask me for a number for 10%, it could be more, it could be less, but do not ask me to forecast a number. The fact that

Europe has grown in triple digits in Q4 should give you some idea that we will do right going forward.

Moderator: Thank you. The next question is from the line of Jinesh Gandhi from Motilal Oswal Securities. Please go ahead.

Jinesh Gandhi: First of all I have couple of clarifications, one is would you be separately sharing the Annexure which you shared on excise, operating other income?

K. Jayaprakash: On excise I think you will get all the details in the SEBI report, so you have both including Bill Forge in the consol, so that is what you will get and on operating income, you want to know the breakup is it?

Jinesh Gandhi: Yes, operating other income and other income for India and European business?

K. Jayaprakash: I will share with you a little later, right now I do not have it.

Jinesh Gandhi: Secondly, the standalone numbers which have reported, the fourth quarter includes six month performance of Mahindra Gears or?

K. Jayaprakash: Yes, six months of Mahindra Gears.

Jinesh Gandhi: Thirdly, with respect to this RM related price increase in Europe, that is for the full year accounted only in fourth quarter?

K. Jayaprakash: Yes.

Jinesh Gandhi: And accounting that comes in revenue line item?

K. Jayaprakash: Yes.

Jinesh Gandhi: Coming to other questions, so primarily in India business if I see there has been a sharp reduction in RM cost primarily standalone numbers sharp reduction in RM cost and sharp increase in other expenses, is there anything to do with mix of outsourcing as such or there is some other issues?

K. Jayaprakash: The other expenses like Vikas explained we have one-off expense, we are trying to sort of, there was a recent regulation and we are trying to use that to sort of get some permission for the old plant we have, so it is a one-off provision about Rs. 110 million.

Vikas Sinha: Other than the VRS?

K. Jayaprakash: VRS is anyway shown as an exceptional item separately.

Jinesh Gandhi: This 110 million pertains to provisioning for?

K. Jayaprakash: Some building approvals we wanted to take, we have had these plants in the Gram Panchayat and now we need to take an approval from the town planning.

Jinesh Gandhi: The RM cost reduction which we have seen as a percentage of sales on QOQ basis, is that to do with any mix change or how should we read that?

K. Jayaprakash: I would think it is mix largely.

Jinesh Gandhi: Largely mix, nothing to do with any efficiency-related savings?

K. Jayaprakash: Efficiency keeps going up every quarter, but otherwise it is the mix.

Jinesh Gandhi: Lastly, with respect to India business, how would the share of M&M and Tata Motors in India revenues now versus say CY '16?

Vikas Sinha: It is roughly the same that we were talking about, it is roughly in the range of between 35% to 40% combined M&M and Tata Motors of MCIE India revenues including Bill Forge.

Jinesh Gandhi: The stronger growth in India business vis-a-vis our key customers is led by what, I would have presumed that it is because of new customers, but if share is similar then is it increase in content with existing customers or what?

Vikas Sinha: It is basically the growth at our customers has happened plus we have talked in the past about some new customers that are coming in, JP in the previous call had mentioned about in our stampings business we were talking to Ashok Leyland, we are talking for some export business in Forgings so those businesses have also and Gears has also new business which we have anyway highlighted in our key highlight section, so there has been growth in our existing customers and also growth from other than that, the Gear was TBK India.

Jinesh Gandhi: Coming to MFE, how should we read MFE's growth in this quarter particularly because if we see on YOY basis, we have seen a significant outperformance to the industry, but on QOQ basis industry growth has been very strong, but MFE's growth has been relatively weaker?

Vikas Sinha: MFE or MCI Europe are you talking about?

Jinesh Gandhi: Sorry, MCIE Europe.

Vikas Sinha: MCIE Europe of course in Q4, we have that extra 68 million so not all of it is because of that quarter, only one-fourth of that 68 million is because of the Q4 price increase, so there is a little bit of bump up that is coming because of that. Other than that, it is because of not the market growth per se but it is because of this ramp up in Caterpillar business and the Lithuania crankshaft business.

Jinesh Gandhi: Because on QOQ basis then we have underperformed industry materially, so is there anything to read into that or it is more to do with the ramp up or any seasonality?

Hemant Luthra: I do not think we have underperformed, I think we are in the same range per se, few things here and there, when you say Q4 if you look at the Q4 commercial vehicles degrew by minus 5.4% if you look at page 33 of our presentation, so commercial vehicles degrew by minus 5.4% on a year-on-year basis and Q3 had degrown by minus 18.5, so to that extent you are seeing between Q3 and Q4 a better performance on the market side, but nevertheless both are negative numbers on commercial vehicles. On again the same story repeats on passenger vehicles, on Q3 numbers if you look at that, the Q3 results were pretty bad from a market point of view minus 0.4% market growth in Q3 which is now 6% in Q4, so there is some adjustment going on between the two quarters, inventory correction and so on, so I do not think we are very far off from the market figures in Q3.

Jinesh Gandhi: Sir, referring to page 7 and their numbers are slightly different, October and December '17 versus July-September, the passenger vehicle is 16.5% growth and commercial vehicle is 20% growth, so maybe you are referring to different numbers in that case?

Vikas Sinha: No, I am referring the same numbers, I have said very clearly that the Q4 on a year-on-year basis is 6% for passenger cars and it is minus 5.4% for commercial vehicles, so those numbers are the same. What you are showing as '16 and '19 is basically between Q3 and Q4 and the explanation that I am giving is that Q3 numbers were very low. The growth in Q3 was very low, it was negative in both the cases and it was very low negative, and therefore, you are seeing a lot of growth on a sequential basis, that is all I am saying so there are no discrepancies in the numbers.

Jinesh Gandhi: Lastly, in terms of the QOQ margin improvement in MCIE Europe, this is primarily driven by what?

Vikas Sinha: You are saying July to September was 12.3 and October to December was 15.5?

Jinesh Gandhi: Yes, the 320 basis point?

Vikas Sinha: Some part of it is because of the extra raw material increase that roughly Rs. 51 million is extra, that is straight away sitting there, so that you have to take into account.

Jinesh Gandhi: Yes, that is about 80 basis points.

Vikas Sinha: Other than that, it is all improvements.

Jinesh Gandhi: This is largely sustainable?

Vikas Sinha: Yes.

Moderator: Thank you. The next question is from the line of Chetan Vora from Value Quest. Please go ahead.

Chetan Vora: Vikas, you said that 5.1 crores is on account of this raw material thing, but wanted to understand the balance difference because that is quite large enough in the European operations, the margin has gone up from 12.3% to 15.5% this quarter, so would like to understand what were the verticals which has contributed to this margin improvement?

Vikas Sinha: That I will direct it to Ander, Ander basically the question is why has the margin jumped up in Europe from 12.3 to 15.5 even if we take away the raw material increase, that would still be an increase from 12.3% to roughly 14.5%, so what accounts for the 2% increase sequentially in margins in Europe?

Ander Arenaza Álvarez: Mainly the raw material impact is clearly explained, I mean we are sitting with customers during all the years and finally we got approximately in October we were paid in advance with let us say all the amounts over from 1st of January to end of October, so that is the amount of Rs. 68 million that was one of the impact. The other impact that we had that was one off was that during the year we were taking some provisions for stocks especially for the obsolete stocks that we had in the balance sheet, but finally all this stock we have in the balance sheetr when we make an inventory, let us say we had additional or provisions in excess, so we have to adjust this amount in the P&L, so that was specifically the impact of additional profit that we had in the first quarter in Germany. Right now, let us say all the business is performing well and we will continue in this trend that is our expectation and even we expect to continue improving, that is technical accountancy issues that we were working conservatively during the year and we finally did not have to make these perovisions.

Chetan Vora: You mean to say the provisions which you were taking earlier in the last three quarters or earlier there off also, and in this quarter there was a write back of those provisions, is it right?

Ander Arenaza Álvarez: That is right.

Vikas Sinha: Therefore, if you look at the full year results that will give you a better picture because the full year results there is no impact of either of these one-offs, so if you take the full year picture, so MCIE full-year result is 13.6%, so that is a very good representation of our performance.

Chetan Vora: On the European operation, the difference between EBITDA and the EBIT which is ideally a depreciation in other calls has increased from 36 crores to 47 crores on a QOQ level, why there would be a jump of 10 crores on a QOQ level?

K. Jayaprakash: You are looking at December '16 versus December '17, right?

Chetan Vora: No, I am looking at December '17 versus September '17, Sir.

K. Jayaprakash: Last time I explained September the depreciation would be low because of low number of working days, because of holidays, August closure, Europe. They provide it on the basis of number of working days.

Chetan Vora: But still in the June quarter also it was like 36 crores Sir, even if I exclude the September quarter, if I refer to June '17 quarter, it was 36 crores which has gone up to 47 crores, just wanted to understand the reason, because 47 crores is one of the highest number in as many as many quarters if I look at it, so just would like to understand even if the September is say lower because of the lower working days?

K. Jayaprakash: Let me come back to you, Chethan.

Chetan Vora: Sir, again on the standalone thing, the Indian operation I am asking not the standalone but the Indian operation, the difference between the EBIT and PBT, which ideally is our interest expenses that the EBIT was like 58.6 crores and PBT was 47 crores, so there is a dip of 11 crores, which is quite a high number, would like to understand the reason for that for this quarter?

K. Jayaprakash: You are referring to…

Chetan Vora: Indian operations, Sir, the numbers what you have reported the EBIT is 58.6 crores?

K. Jayaprakash: Yes.

Chetan Vora: The PBT is 47 crores, right?

K. Jayaprakash: You are looking at the quarter number or full year?

Chetan Vora: I am just looking at the December '17 number, Sir, not comparing vis-a-vis with any quarters, I am just asking for the December quarter?

K. Jayaprakash: We have 406 there.

Chetan Vora: For the December, the EBIT is 58.6 crores?

K. Jayaprakash: No, 406 million is what we are reporting here. You are looking at the SEBI results or?

Chetan Vora: No, Sir, I am looking at your presentation, which is on the Slide five, so if you see EBIT is 52.2 crores?

K. Jayaprakash: That is EBIT.

Chetan Vora: The EBT is 40.6 crores, so just wanted to understand why there would be dip of close to 12 crores?

K. Jayaprakash: You have Gears merged in this quarter and gears have significant debt of about 40 crores and you will have six months interest sitting at line.

Chetan Vora: For this quarter December, the gears number are like for 6 months, you are saying?

K. Jayaprakash: Yes.

Moderator: Thank you. The next question is from the line of Ujwal Shah from Quest Investment Advisors. Please go ahead.

Ujwal Shah: Sir, I was just looking through the presentation from that on the stamping side we now have Ashok Leyland as a customer as well and we also have started a fully automated press line, considering that we were previously catering mainly only to M&M, what kind of an opportunity does Ashok Leyland bring on table and the impact that could have on the margins?

Vikas Sinha: First, to clarify we were not only supplying to M&M, and as I said M&M today is roughly in the range of 35% to 40% of our India revenues and even earlier it was not as if it was 100%, at its max it was in the range of 50% to 55%.

Ujwal Shah: Even for stamping business?

Vikas Sinha: For stamping business, it is much higher, that is correct, so if your question is related to the stamping's business then it is correct observation that M&M is a very large participant in our stamping's business that is right and that is one of the reasons why we are looking at other customers.

Ujwal Shah: My question was how big can the Ashok Leyland in this regard?

Vikas Sinha: Do not ask me for a number please, but again as Hemant said we would not put it up if it was not substantial enough, only place where we are actually saying it is not substantial is EVs business, so we have said very clearly it is in very small numbers at the outset itself why I mentioned that the EVs business is a pretty small supplies, but for Ashok Leyland and TDK that we have mentioned and for Ford numbers F150, those are all substantial numbers.

Hemant Luthra: I think the positive way of looking at Ashok Leyland is that even though Mahindra is in the truck business, Tata is in the truck business, and the Maruti's and the other compete with Mahindra in the SUV business. All these companies have got enough confidence in the governance standards of Mahindra CIE to be able to say that never mind if you supply a competitor and never mind if the competitor owns 17% of the stock. We trust you to deliver on what we want. Their intellectual property remains confidential, their numbers remain confidential, I do not want to discuss their forecasts of Ashok Leyland because I do not think I should be sharing commercial sensitive information about M&M to Ashok Leyland or vice versa.

Vikas Sinha: Basically, lot of this movement has happened because of the new norms on the cabin that has come up, you k now earlier as you are aware a lot of the sheet metal part, commercial vehicles had very little sheet metal part of the business because most of the bodybuilding was done outside and was not done by the OEMs, but now as you are aware there are new safety norms around the driver cabin and so on, and therefore, there is a need on the part of OEMs to source some of these material and that is how we are benefiting out of Ashok Leyland.

Ujwal Shah: Secondly on the casting business, in the Q4 Slide five, we have mentioned that main profitability improvement has happened in castings, so what exactly has led to this?

Vikas Sinha: Ander, we have mentioned specifically on Slide Number five that our profitability in castings has improved, so the question is what are we doing in…

Hemant Luthra: We were discussing this yesterday with Manoj, so maybe you can talk about efficiency.

Ander Arenaza Álvarez: I am in fact now in the casting plant, so we are making the operational review with all the team here in Urse plant. It is clear that during the last, I would say the last month we have done a great job here in the casting plant. We have made some organizational changes, some positions and key positions we have changed, and we have been working to eliminate the bottleneck in the production. During all the I would say the last couple of years, we have been trying to fulfill with the delivery demand from our customers, we were short with deliveries especially because we have a couple of internal problems that we were not able to solve. During last two to three months, we have improved, we have solved these bottlenecks especially in the fledling area that we had a big problem. We changed some part, we made big project with the support from our Spanish engineer in central team so we will improve also our scrap rate reducing the problem in the most critical part, so just to give you an example, we were positioned 3500 tons per month in the month that was our average output on the plant. Right now, we are producing more than 4000 tons per month. Since October-November, we started producing more than 4000 tons per month, so with solved our delivery issues with the customers, we improved our internal efficiencies. Now, the plant is working really, really hot, so I would say that it has been a management issue that we have already sorted internally and the results are improving, so it is helping us a lot the growth even because we can now sell more than we sold before and of course with the profitability.

Hemant Luthra: Ujwal, on Slide 18 if you look at we have put one of the synergy case study is actually pertaining to the castings business to the Foundry plant, of course that is more on the quality and efficiency improvement plan. There you can see that we have talked about the savings of Rs. 1 million per month and how it has come about, there are some photographs also and how it has been enabled, how material saving has happened and so on and so forth, so you can have a look at that, so that is an illustration of what kind of work we are doing in the Foundry business.

Ander Arenaza Álvarez: This is an example of the technology transfer from CIE to Mahindra to India. We have had a team working one week per month here in India from Spain to support the local team to give the training, to prepare all the engineering tools to be used here in India and this job that was done in the last six to seven months, now is giving fruits and we can see now the improvements on the P&L and also on the customer satisfaction. Just for your information also this team is also here with us, I did not know that, but when I arrived here in the morning they are working this week also continue improving especially the yield, the rejection rates, where we are now focused on, so let us say that this is a good example of technology transfer and finally we are getting the expected results.

Ujwal Shah: The last question to Ander, in terms of the EU business what are our margin targets for CY '18 and where do you think margin expansion can come from especially for the MFE business, if not the numbers if you can tell me in terms of what are the areas which you are targeting to get the desired margin expansion specially for the MFE Germany business?

Ander Arenaza Álvarez: In the European business, we expect continue growing in terms of sales, internal should increase. In terms of margin, we see that the Italian Gears plant as we are now growing importantly, and we expect to have important growth, we will expect also to improve slightly the margins. Our forgings are doing perfectly, I think the Spanish forgings are doing properly and in Lithuanian plant, we will increase also the margin because we will continue growing and as the new crankshaft line is already working, so those improvements will be there especially because of the sales growth. This is the volume improvement due to this. Finally, regarding Germany, in Germany you know that we were struggling a couple of years ago and we during 2017, we stabilized the business and quarter by quarter, we have been showing better results. We, as you can see the overall EBITDA margin, you can see the Calendar Year '17 report, but it has not been flat during the same old year, so we started from lower figures and we are going up as in a ramp, so we expect to continue growing this margins, probably the growth will not be strong as it is because we started one from a very low margin, so that easier to continue growing, but we are still far from our standards, so let us say that we expect growth volumes Italy and Lithuania and we expect also improvement in Germany, I cannot give you the figures because I cannot disclose this information, but I can say to you that we are strongly committed to continue growing this margins and as I told you during 2017, quarter by quarter we were improving slightly and consolidating EBITDA margin.

Ujwal Shah: Just to probe a bit more, so in terms of Germany margins, do you think that now from here on it would be difficult to get margin expansion or which are the areas in particular that you are seeing there can be margin expansion for the German business?

Ander Arenaza Álvarez: I think that we have still some room for expansion. Once we have reached the level or the minimum level that we fixed, we still have some room for improvement and we expect to improve a little more, yes. It will not be huge improvement because the technology and the market prices are not allowing to have an excellent margins on those components, but at least I would say that we have still some percentage to be improved.

Hemant Luthra: One of the reasons why we try and encourage you to look at the company as a whole because Ander as a CEO is responsible for the global forging plus everything else, but I am just saying that when he is responsible for global forgings, he can take decisions and is evaluating them that if Bill Forge has got a shortage of capacity, can that be serviced by doing something in Chakan. If in India the volumes are growing, can that be serviced by moving physically a press which may be underutilized in Europe, so I cannot go through every little piece of what we are doing but the focus on improving margins does not necessarily only come from the obvious stuff of tweaking something here or there, something for those of you who understand Hindi, apologies for those of who do not, "*kabhi kabhi bolthena sou sonarki aur ek loharki*" and that translates that a Goldsmith uses hundred little taps of the hammer and the guy who works with iron and metal can do the same thing by using one big crack at the hammer, and therefore, being more effective, so there are small steps you can take also, big steps you can take, so keep watching this space because you all have I believe would have been pleasantly surprised with what has happened in Europe and I hope we will continue to surprise you not by only tinkering, but by taking some bold steps with respect to how the business has managed most optimally.

Moderator: Thank you. The next question is from the line of Venkat Subramaniam from Organic Capital. Please go ahead.

Venkat Subramaniam: The question is to Mr. Ander, MCIE actually has benefited enormously from the CIE Association, but I just wanted to understand your thoughts on our capital structure, given our capital structure, Mr. Ander, our Indian acquisitions are not going to be as accretive to shareholders as they can be let us say in the hands of other Indian companies, this is because you are foreign owned etc. and there are domestic restrictions with respect to borrowing, are you exploring non-equity options as and when an acquisition happens, Sir?

Ander Arenaza Álvarez: You know that we have this limitation to move to the let us say financial market to buy the company due to the Indian law, so we have to fund this through equity and our idea is still let us say that we unless the law is changed, and Hemant can make some comments on that. We have no chance to go into this capital increase whatever our funding through equity. However, what I would like to the say is that, we are always thinking on the shareholders when we do this and we want to create value, we will only do when the operations or capital increase if we are creating value to our shareholders, so this is very, very clear we do not want to and that is what we expect that they realize and with the growth that wheel of fortunes giving us and let us say the wider customer type that we have with Bill forge with Mexican business already starting to share and to open a new market for us, let us say that all of this is creating value, so we expect that any purchase that we do in the market in the next year or in the next quarter whatever will create value for all of us. The point and we as you know that we want and we have the clear idea to continue growing our business, we want to be one of the key players in the Indian market. We want to develop our business most organically and inorganically, so let us say that we will continue creating the value that we have I mean till now and of course we will show this, we will prepare and we are now also it is important that we are preparing our strategic plan for the next five to six years, so all of this will be considered in our strategic plan.

Venkat Subramaniam: Mr. Ander the limited point one was making, Sir…

Hemant Luthra: Let me jump in and supplement this before you ask a follow up question and see if this helps you. You referred to some regulation, which say that there are some restrictions on foreign owned companies. We would not have go to where we have got with CIE showing a 4.5X price increase in three or four years since we have had this joint venture and Mahindra CIE showing a three to four X price in increase since we have the joint venture if there had not been some out of the box thinking. My suspicion in my interaction with Government official at the senior most level has led me to believe that this regulation that came was during the time when India was concerned about foreign owned companies piling up debt and that debt affecting Indian track record if that debt was not paid, and therefore, they said that foreign owned Indian companies should have some restrictions borrowing, but that restriction on borrowing creates some absurd situation.

If we are looking at the company in India and if you look at an equivalent company in Asia, because our mandate is not just India but it is Asia and if both the companies are the same size and both the companies have got kind of a customer base that suits us, under present Indian law, you can buy the foreign company and get debt from India, and therefore, when I have made presentations to the Government of India, I have found a very sympathetic ear which says that by having this regulation, you are not serving the cause of Make in India because if it is easier for Mahindra CIE to buy a company abroad with identical numbers then I am not doing Make in India, but I might end up doing Make in Korea, Make in Vietnam, Make in Thailand all of where such opportunities are available. At the same time, the banks keep running to us and saying that company A, B, C, or D is under NCLT and under IBC processes, would you like to consider it, some of these companies could be of interest to us. Thirdly, the government's owned philosophy may have been determined at a time when the Rupee had slipped to 69 and they wanted to make sure that whenever companies were bought more foreign exchange were brought into the country, but at this time, you have the opposite situation where the Rupee has gone from 69 to 63 and there is a surfeit of dollars never mind the hiccups that have happened recently, so is it possible and I believe it is that the Government is so focused on creating jobs might have a sympathetic ear to tweaking the regulation, to serve the large cause of creating jobs in India and Make in India and I am reasonably optimistic that not only can the regulations be tweaked legitimately, I think they are sympathetic ears and also if you look at our track record where the net financial debt to EBITDA is may be 1, 1.1 the debt to equity is whatever, I think we are more conscious than anybody else that the return on equity must be protected so that you as shareholders feel comfortable. I cannot give you any specific dates about when I believe some of these things can happen, but trust Ander and trust us to make sure that the return on equity that you are looking for happens with some out of the box thinking.

Venkat Subramaniam: Mr. Luthra see the limited point here is that Government since it is actually running an agenda where there are as they are dealing more important issues this may take a while, so pending that I just wanted to find out whether Mr. Ander as CEO of MCIE would be open to supporting from CIE's balance sheet through a debt in case domestic opportunity presents itself, so that is really what I wanted to hear from Mr. Ander?

Ander Arenaza Álvarez: Principal, yes, I mean we can support anything that is good for the company, we are analyzing the situation in the opportunities that we have in each region and CIE of course is yet to support anything that is good for the company and is supporting the growth for the company, so I would say that we are not close to that, but we are now seeing all the opportunities and we will decide accordingly.

Venkat Subramaniam: Sir, I just had a follow up question, as you would have noticed there are number of questions with respect to German operations, our German operations in terms of financial parameters have continuously lacked, the CIE parameters, margins are lower, etc. and they also have tended to actually the blended margins and the blended parameter has also taken effect because this is not a small, it is close to 200 million Euros, being a financially managed company and a very prudent company, would you hesitate to actually monetise these in case of higher growth opportunity persist, you do not have to commit, but I just wanted to understand what your thoughts are, is it a holy cow in the Indian context?

Ander Arenaza Álvarez: Let us see that our idea as we are it is my experience in the past and also my mindset is fully operational, my idea is to solve and to make these German operations profitable for the company and that is where we are now. You know that we like we want to continue growing and let us say that we are not considering any selling of these businesses in the short term. You need to also realize that some of the customers are the main customers in Germany are also global CIE customer like Daimler or Mann or Scania or Volvo and of course we need to protect these customers, so in principal I think that our main task now is to continue with turnaround of the business. Now, I think that 2017, we did tremendous step in the right direction, so our idea now is in 2018 we should improve a little more given our step up to be closer and closer to the CIE standard, so globally speaking I would say that our focus right now is not selling it, I mean that will be the way of making business. We want to continue there and we want to solve the companies.

Venkat Subramaniam: So aspirationally to get close to the CIE parameters, would you say two years, three years, Sir, how long do you think it can probably take?

Ander Arenaza Álvarez: I would say broadly the CIE parameters are really, really tough, the benchmark in our automotive market. We will probably not be that figures, but what we would like is to be little close perhaps 20% to 30% below CIE target that would be the target there.

Venkat Subramaniam: That may take about two years you would say, Mr. Ander?

Ander Arenaza Álvarez: In couple of years, yes.

Hemant Luthra: I just want to add to my response to Venkat, because Ander has addressed the issue of addressing the needs of the customer and putting the customer first, if there is a method by which we can do that, again some out of the box thinking. You have seen it being done in the case of Jeco where one plant was shut and it took some effort to fix it, but it has been fixed, and therefore, the overall numbers of Germany have gone up, but I do not think it will be fair to either the customer, the employees or anybody else to discuss on a public call what restructuring can be done other than to convey to you the confidence that whatever is done will be done in the interest of the customer and the shareholder and the employee. I do not want to get into a discussion as to what will be the restructuring, when will be restructuring, how the restructuring happens because this is a public forum and I do not want to jump any gun on that.

Moderator: Thank you. The next question is from the line of Mahesh Bendre from Karvy Stock Broking. Please go ahead.

Mahesh Bendre: Sir, what are the capital expenditure plan for next two years?

K. Jayaprakash: We have done about 300 crores this year and I think since we are really now operating in many of the plants at full capacity, I would expect it to be around these numbers.

Mahesh Bendre: For next two years?

K. Jayaprakash: Yes.

Moderator: Thank you. The next question is from the line of Bharat from Quest Investments. Please go ahead.

Bharat: We have this time outperformed Indian operations in terms of EBIT margin, EBIT margin is almost 50 basis points higher than the Indian operations and we wanted to reach I mean this CIE EBIT margin level by 2020, this whole journey where exactly we are at this stage?

K. Jayaprakash: Your question is…

Bharat: Indian EBIT margin around 8.7 and Europe margin is 9.2 resulting 9% for the whole company, so we have some kind of EBIT margin is by 2020 so in that tell me where we are and how do we see every year next couple of years?

K. Jayaprakash: We have said that our goal is to get to 10% on EBIT and you can see Europe is already pretty close and India also, if you were to remove that one-time impact that we have in this quarter, of course our annualized it will have little impact, we are in India also looking at reaching this 10% in the next couple of years, we are on that we have some capacity, we have some room to improve and we will get there.

Bharat: We have already reached 9% and next three years we are looking for 10%, but do you think that the kind of pace that we have taken I mean improvement and now further we are improving CAPEX on putting in Mexico in Bill Forge as well as in Lithuania which is a high margin business, so can we cross that 10% margin by this 2020 EBIT margin?

K. Jayaprakash: This is for Europe or your saying at consol level?

Bharat: Consol level.

K. Jayaprakash: I would think surely because if we are getting top line growth making some capital expenditure will definitely leverage our existing cost structure and we should be able to do better.

Moderator: Thank you. The next question is from the line of Priya Ranjan from Systematix Shares and Stocks. Please go ahead.

Priya Ranjan: My question is on the key financial metric, Sir, the key covonants what you said, so in terms of two to three parameters still we are way behind particularly the RONA and FCF to EBITDA which is I think the FCF to EBITDA target is somewhere around 50% and RONA is around

20%, so do you see that it is achievable in next two to three years or what is the mid-term target in that sense?

K. Jayaprakash: To answer your question, yes the RONA is at 12% and you would know that because of the only recent acquisition of Bill Forge, so we expect Bill Forge to do the growth that was envisaged and like you heard earlier they are very much on line, so as the growth kicks in from Bill Forge at that kind of high margins, the RONA should definitely improve. Having said that we will have to also improve in Europe and some of our business in India which is all on the radar and that is how we are going to get the RONA that we have sort of set out to achieve. FCF, I think it would be RONA, which we would really pursue and on FCF yes, if CAPEX is required, we will have to make them, right.

Priya Ranjan: But the CAPEX will come with the growth as well…

K. Jayaprakash: Yes, so I think we will go ahead with the CAPEX if growth is coming.

Priya Ranjan: What you are seeing is that we will prioritize RONA over EBITDA?

K. Jayaprakash: Yes.

Hemant Luthra: The other thing is that we move from 9% to 11.9, I am sorry we have not moved from 9 to 20 in one year but the heart is in the right place and the focus is in the right place, that is all that I can say, we hear you loud and clear.

Priya Ranjan: My worry is that in India the assets does not come at cheap like so even if we go ahead and do couple of more acquisitions, so RONA will be under pressure because it will come with a significant amount of goodwill?

Hemant Luthra: I hear you loud and clear, I think you heard Ander also saying that we are hearing this feedback from our shareholders, recording it, and absorbing it, it is not as if it is only external, it is internal because the benchmark against ourselves that we know that shareholders have a choice to go elsewhere wherever they get a better return, so you have heard Ander say that we are going to look at stuff whatever we do is going to be earnings accretive. You also heard him say that there people are spending a week, a month over here to make sure that the improvement that you see in Gears, in Stampings and others is and what you see in Foundry is accelerated, so you will have to trust us to not to ignore your feedback about RONA and ROE.

Priya Ranjan: Sir, on capacity utilization and what capacity utilization will be in Europe, each geography separately if you can say that?

Hemant Luthra: Ander, I do not know how you can define it because there may be some pieces of Europe that are running flat-out, some that are not, but for example in the case of Metalcastello, you know our conscious decision was taken that you would weed out the unprofitable product so that you would create headroom and get the EBITDA margins up which they have succeeded in doing quite brilliantly, so let me turn it back to Ander because there is forging, there is gears and everything cannot be.

Ander Arenaza Álvarez: I would say that the capacity utilization is of course is different in each of the units that we have, but speaking overall in let us say our capacity right now in Europe can be something like 90% that is the European capacity. In Germany, we have slightly less than that, I mean we can be at 70% of capacity, this is the average and in India, it is also depending on the business as we have some businesses where we are at full rate like full capacity for stamping in Bill Forge or we are at full capacity also in the gears business and in those businesses, we can have an 75% to 80% of utilization, so that is more or less our situation.

Priya Ranjan: In terms of the new orders, you have saved the orders which I think the execution has already happened, so can you say some the new orders or any which are yet to be executed maybe in next one year or two year you plan to execute?

Ander Arenaza Álvarez: Yes, one of the key commercial important fact or indicator that we follow our new order incoming, they say that in 2017 in India and in Europe we will fulfill our internal targets that means that we have been successful in the market. Right now, even in the beginning of 2018, we have had some important and we were making the follow up during the business, we have been successful to get new businesses with all the customers, some of them are for export, so let us say that for their book is really strong in the last month was important and we fulfill our internal targets and 2018 has started also with a very strong order book realization, so globally speaking I think that we are in good path, what we are perceived by the customer as reliable supplier and that is where we are working right now, so I cannot disclose the contract that we have been awarded, but the trend is positive and expectations are also very good.

Moderator: Thank you. The next question is from the line of Jinesh Gandhi from Motilal Oswal Securities. Please go ahead.

Jinesh Gandhi: You mention that in European business there is this write back of provisioning for stocks, what would be the quantum for that, for that write back?

Ander Arenaza Álvarez: What we did during the complete year, just in order to avoid any problem at the end of the year during the audit period, we provisioned some of the stocks as let us say that they control over the stocks in our German companies in the beginning of let us say after the crisis, it was not really reliable so we set up the internal SAP system properly, but just in case we created some provisions in order to protect ourselves by the end of the year because you know that our companies especially in Germany, we have more than 1000 live part numbers in each of the clients, that means that the control is quite complex. Right now everything is perfectly controlled in the system, the SAP system was set up and completely clean and let us say we corrected this provision that we made, let us say we made this provision on excess, so that was the reason of this correction in the stocks.

Jinesh Gandhi: My question was what would be the quantum for that write back?

Ander Arenaza Álvarez: Something less than €1 million.

Jinesh Gandhi: Secondly, you talked about Mexico plant, we have added one new customer and that would in turn require to add new capacity, so can you throw light on is this equally as big as a order as we have got for the original Mexico plant or this would be just a supplementary order and what would be the CAPEX which would have to do for Mexico plant?

Ander Arenaza Álvarez: The order is supplementary, the main order that we got from GKN was much bigger than this, but this is supplementary, but it is relevant. We are talking about more than €5 million, so this is important order and regarding the investment, we have already done during the 2017, but the investment was one press that we have already installed and okay we have now commissioned this press, so we are still have to fulfill complete investment line but the most important part of this investment is already done.

Jinesh Gandhi: €5 million is a cumulative order or annual size?

Ander Arenaza Álvarez: Annual size.

Jinesh Gandhi: Lastly, on Mexico plant, you indicated current output is 30% of utilization?

Ander Arenaza Álvarez: Yes.

Jinesh Gandhi: By year end, we should be close to about 50% to 60%?

Ander Arenaza Álvarez: We are in ramp up with the customer, right now we are already at I would say 40% more or less, we expect to be just 70% to 80% by the end of the year.

Moderator: Thank you. As there are no further questions, I now hand the conference over to the management for their closing comments.

Hemant Luthra: Gentlemen, thank you very much. We note that you have liked the results and we note your concerns about the future and how return on capital employed and return on equity needs to be protected to satisfy you and the management will continue to push for operating results and as team leaders, we will continue to push in the direction of the concerns that you have voiced on the call today. Should any of you have any follow-on questions, I think most of you know Vikas and if there are other questions I think Vikas can be used as a funnel to address any unanswered inputs. Thanks very much everybody and Good Day and Good Afternoon.

Moderator: Thank you. Ladies and Gentlemen, on behalf of ICICI Securities Limited that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.

Note: This statement has been edited to ensure quality