"Federal-Mogul Goetze India Limited's Q2 FY'22 Earnings Conference Call"

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MANAGEMENT: **MR. VINOD KUMAR HANS – MANAGING DIRECTOR, FEDERAL-MOGUL GOETZE (INDIA) LIMITED**
MR. MANISH CHADHA – CHIEF FINANCIAL OFFICER & DIRECTOR, FINANCE, FEDERAL-MOGUL GOETZE (INDIA) LIMITED
DR. KHALID IQBAL KHAN – DIRECTOR, LEGAL & COMPANY SECRETARY, FEDERAL-MOGUL GOETZE (INDIA) LIMITED

Moderator: Ladies and gentlemen, good day and welcome to the Q2 & H1 FY'22 Earnings Conference Call of Federal-Mogul Goetze India 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 '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ashish Samal from Perfect Relations. Thank you and over to you, sir.

Ashish Samal: Thank you, Margaret. Good evening, everyone and thank you for joining us on Federal-Mogul Goetze India Limited Q2 FY'22 Earnings Conference Call. Today, we have with us the senior management represented by Mr. Vinod Kumar Hans -- Managing Director, Mr. Manish Chadha -- CFO and Finance, Director; Dr. Khalid Khan, Director, Legal and Company Secretary.

Before we begin, I would like to add that some of the statements to be made in today's discussion may be forward-looking in nature.

We will begin the call with the opening remarks and followed by presentation from the management, after which we'll have the forum open for interactive Q&A Session.

I would now request Mr. Vinod Kumar Hans to make his opening remarks. Over to you, sir.

Vinod K Hans: Thank you, Ashish. Good morning, good afternoon and welcome to this meeting today. Just a quick note, overall on the market side, we saw a good recovery from first quarter perspective which is April to June in this quarter, but however, I would say that this quarter could have been much better as claimed by OEMs, but it was heavily impacted by the semiconductor shortages, particularly in fact in the passenger car and commercial vehicle in a major way. With that, there was a lot of uncertainty and volatility in the market because of this situation of semiconductor, so had also a lot of fluctuation in demand and also planning perspective.

Also, I would say another phenomenon for this quarter was record commodity prices which we saw in aluminum, copper, nickel, silicon, some of these commodities achieved highest ever level in the history of these commodities. Along with that was also the freight line, particularly, the shipping lines were increased not only by lead time, but also the rates. So, overall, I would say much recovered in the quarter, but could have been better. Also, when we compare to last year, the improvement is good, but last year also this quarter we were recovering from the COVID. So overall talking about COVID, COVID is also impacting some of the regions in a major way. You have seen in Europe, most of the western Europe is going through the highest level of COVID cases, Russia again, reporting some of the highest numbers. So impacted by COVID and also the impact of semiconductor was more pronounced, I would say, in the western world in Europe and US. Somehow the Japanese OEMs performed little better because they were closer to the semiconductor manufacturers.

Having said that, these numbers, which you've seen in some of the OEMs were the drop of about 20% however, as the company was nicely segmented into different segments, so fortunately we have the aftermarket, we have the EIT, what we call Energy, Industrial and Transport segment, where the reliance of semiconductor was not there, and so therefore I would tend to believe that the diversification in segment did help us and some of the impact which you see on the OEMs affected by the semiconductor did not cost us impacted us in a major way. But having said that, this quarter also recovered from the previous quarter for us, but still lower than the best quarter which we saw in January to March, not only from the OEM perspective from our perspective as well.

The situation is getting stabilized as we get this information from the market. So, at least, I would say we have clear view coming from customers and the situation should improve in next three to four weeks. But having said that, this impact of semiconductor would impact the passenger car and commercial vehicles till I would say next two quarters at least and then things would look better. That's the overall view.

With that, I would request Khalid to start the presentation.

Dr. Khalid I Khan: Thank you so much. Let's come to the company overview. As you all know, company's subsidiary company of Tenneco Inc. and it was established in the year 1954. And this company is based out of Gurugram, India and is engaged in the manufacture, supply and distribution of automotive components in India as well as internationally. The company mainly offers pistons, piston rings, piston pins, valve seat and valve guides. It caters to automotive, heavy duty, motorcycles, energy, industrial, power generation, railways and defense industries. It manufactures world-class products at its plants, which are located at Patiala, Punjab, Bangalore and Bhiwadi, Rajasthan.

Regarding the shareholding pattern as on 30th, September 2021, promoters are holding 74.98% and the balance 25.02% is held by the general public which includes 1.57%, which is held by mutual funds and 0.12% by FIIs and FPIs.

Coming to the board of directors, there is no change in the board of directors. We still have nine directors on the board and as per the requirements of SEBI, three directors are independent, one out of the independent directors is a woman director, and we have executive directors which comprises Mr. Vinod Hans who is the Managing Director, Mr. Rajesh Sinha, Manish Chadha and myself. And then we have other non-executive directors; Mr. Sunit Kapur, Stephen Shaun Merry.

I will request Mr. Vinod Hans to walk you through the next slide. Mr. Vinod Hans, over to you.

Vinod K Hans: Thank you, Dr. Khalid. So, next six seven slides are very similar to what we hinted in the previous investor meet. So, on the competitive strength, our credit rating is long term A+, Short term A1+. We continue to have you know good technical support coming from global for the technology transfer, some of this we will discuss during the Q&A session and our diversified segment percentage remains there, and in terms of liquidity, again, we had a strong I would say quarter from a cash perspective. And then our experienced team retention is pretty good at a senior level.

On the manufacturing side on slide #7, we have these major ones which Dr. Khalid mentioned in Patiala, Punjab or Bangalore, Karnataka, both making Piston, Piston Rings and then we have a plant in Bhiwadi in Rajasthan.

Our market position continues to be strong. Piston Rings and Seats and Guides, we retain our number one position and in pistons we are number two overall and number one in diesel pistons.

On next slide #9, the key driver remains pretty much the same, better fuel economy, low emission focus by the legislators and expectation of increase there from the end users. So, all are I would say good driver from our perspective and our product answers some of these in a very, very nice way.

Now, coming back to particularly performance focus, as we mentioned in the previous call reducing operational cost is a key focus for us. And we have been largely successful in fixed cost reduction and improving our operational efficiency. We have pretty good focus on the working capital and some of this is seen in the financial effect also, although we improved our cash but because of the inventory, of course, as we slow down the inventory, drive down the inventory does impact the profitability. But keeping in view the market situation, we believe that if we can really improve our working capital term ratios, it will be good in present scenario. And of course, on the growth opportunity, we continue to monitor the progression of our TGDI engines against some of this we will discuss. We are very happy with the market progression happening in favor of the TGDI engine. We have seen some of the bookings done in high end of vehicle, most of them have been TGDI, in general very good, I would say a signal which we have been discussing this. And as you know that from OEM perspective, we're claiming that nearly half a million which is five lakh passenger car booking is pending with OEMs and most of these booking is on the higher end of the segment, more than 1.5-liter engines actually. So that's pretty good news for product section.

And then on electrification, we continue to see a lot of announcement activities at the two wheeler level. Nevertheless passenger car and commercial vehicle level there is more I would say focus on the diversification of moving from diesel, petrol to more on I would say hybrid biofuels and CNG and LPG and those kind of fuels. So, there's very clear preference going into that direction. Electrification is on but still some time away at least on the passenger vehicle and commercial vehicle perspective. So, the immediate focus from the OEMs is more towards getting into I would say, more friendly fuels as considered in the market rather than going to pure battery electric vehicle.

With that, I will hand over to Manish Chadha who'll run through the financials of the quarter.

Manish Chadha: Thanks, Vinod and good afternoon everyone. This is a slide 13 where you can see the quarter ended result for 30th September 2021, there you can see the revenue of INR 3,357 million which is 22% better than the previous year and from the previous quarter it is 6% better than in the top line. So we can see some recovery happening but it has impacted as Vinod mentioned, it is a chip shortage in the last quarter. From the operational EBITDA perspective, we are 12% as against last quarter 11% and against last year we are 2% lower mainly because of the commodity price increase and the recoveries. So there is a net MCS loss for this quarter which we will be recovering in the coming quarter. So, the operational performance is 2% adverse from the last year as well as from the last quarter, it is 1% higher because the recovery has started happening, the gap is now shortening up. And profit after tax for the current quarter is 4.1% as against last quarter of 3.1%. So, overall, I think we have started seeing improvement, but, it is more depending as Vinod mentioned market is volatile and we can see some recovery happening from the chips.

Next slide. I've already explained the number, the top line is up from previous year 22% in the same quarter and from the previous quarter 7%. Operational EBITDA already mentioned we are 2% lower than the last year same quarter and 1% better than the previous year and similar impact comparison with EPS you can see from the financials.

Next slide, we have the 6% PBT for quarter last year, same quarter this year also. On the previous quarter it is 4% and same in case of PAT 5% for last year, same quarter and this quarter is 4% and PAT is better by 1% from the previous quarter.

Financial Result Overview: Already discussed about the revenue, is a growth of 22% from the previous year, last year was mainly impacted due to the COVID, market has started recovering but chips impacted this quarter. Operational profit we already discussed, it is 12% against 14% mainly because of the net and sales impact for the current quarter. And the PAT is already INR140 million for the quarter.

As we discussed in the financial overview and strategy we are focusing on working capital improvement and also operational improvement. So you can see the cash is generated almost INR550 million and the cash balance by the end of September quarter is INR1954 million. Vinod, over to you on the customer award deliberation.

Vinod K Hans: During this year particularly from April to now, we had awards from Fiat for Best Supplier for Quality. And Mahindra & Mahindra Automotive Division gave us the Best Product Development Award. Also, Commodity Award for Best Product Development, Spare Part performance. From General Motors, we got Supplier Quality Excellence Award. Although we are only now exporting to General Motors from here but the local unit of General Motors is closed as you know. But nevertheless this award from our global export potential perspective is still quite prestigious to the company. And also, we got a special acquisition for XUV700 product development because all our products are there in XUV700. And then we were also quite happy with Daimler, giving us overall most zero PPM award for their truck business.

I will hand over to Khalid for running you some of the CSR initiatives we had.

Dr. Khalid I Khan: Thank you so much, Vinod. So we continue to be engaged in the CSR activities helping the under-privileged people. So the company is building day crawls for lions and tigers at Shri Atal Bihari Vajpayee Zoological Park, which is also known as Hampi Zoo. And this is located in the Bilikal west river forest area and it spans around 141.1.59 hectares. It involves an amount of around 14.30 lakhs.

Apart from this, there are certain initiatives for which we were recognized. So Rotary Club recently recognized and honored our organization for our outstanding work in the field of basic education and literacy for our flagship CSR project at Bhiwadi, which is at Harchandpur School. Tenneco VSG plant, Bhiwadi was also bestowed with 'Contributor to Fight COVID-19 Award' by BMA. Then, the Patiala plant contributed around 17.92 lakhs for public construction of two rooms at a government girls senior secondary school. Around 700 girls attend this school and majority of them come from economically disadvantaged backgrounds. We hope that this school building will encourage more parents from marginal sections of the local community to come forward and enroll their children in this school which provides quality education to them. That's it from my side. I would like to hand it over to Ashish. Ashish, over to you.

Ashish Samal: **Margaret, we can start with Q&A session now.**

Moderator: Thank you very much, we will now begin the question-and-answer session. Anyone who wishes to ask a question may press dial * and 1 on your touchpad telephone .If you wish to remove your cell from the queue you may press * and 2. Participants are requested to use handset while asking a question. Anyone, who would like to ask any question please dial * and 1 at this time. Ladies and gentlemen, we will wait for a moment while question queue assembled. The first question is from the line of Manish Manchanda from Plaza Paints Private Limited. Please go ahead.

Manish Manchanda: Hello everyone, thanks for the opportunity, I would like to congratulate to the management for the wonderful results. I just wish to ask, Is the management concerned about minority stakeholders? Our share price is quite low in the current scenario and while I have been seeing that we have paid Rs.674 a share for the buyback and have been rejected two times. And in the past 10-years there is no substantial wealth has been made by the company. So, is the management concerned about the stakeholders? This is my first question.

Second, I would like to know that is there any dividend policy that we have made because over those years, although we are having a huge chunk of cash on our balance sheets, but still we are not paying any dividends to the stakeholders. So what is your view on that?

Dr. Khalid I Khan: We are a multinational company and we follow ethical values, integrity. As far as performance of our stock value is concerned, actually, our focus is to improve the performance of the company. So, we can't do much about the stock price. It keeps on moving right; it may be high, it may be low, right. So, I think our focus is very much on our performance, which you can see from our financial results over a period of time. We try to be consistent with the financial performance. As regards dividend policy of the company is concerned, yes, we do have a dividend policy, which is already available. If you go to our website, you'll find our policy. Are there any further questions?

Manish Manchanda: I have few more questions; I would like to know are there any other products in the pipeline apart from the piston and piston rings?

Vinod K Hans: We have a sintered metal product also, which is called valve seat and valve guides into our portfolio. There are about 12% or 13% of the total business and in fact, that is growing pretty, pretty nicely over there. So, as far as unit is concerned, our key focus is to really consolidate the product portfolios, and any related product which is coming for example, liners. We are at the moment to trading these liners wherever our customer are keen to get it done. So, we are getting through this other Tenneco entities globally. And once it reaches the certain sustainable, I would say, numbers, then we will look at the manufacturing of these liners. So, these are the commercial related components. We don't have I would say in near future any strategy to diversify into a very different category of components. Having said that, we already discussed the CNG, biofuels, and then hybrid coming in. So all these fuels have a direct implication and change in our products. So there's a change in metallurgy, there's a change in manufacturing, there's a change in ball geometry.. We will be pretty busy in supporting our customer on progression from diesel, petrol to CNG, LPG and these biofuels. It's a good news for us, because all these fuels, they have a special requirement on season guide piston and ring and we have pretty good solutions around that. So, again, I will repeat that we'll be busy in modifying our product portfolio rather than going into a very different kind of product, if that was your question.

Manish Manchanda: Just last question. Can you just clarify on the capital allocation of that reserve which we are having right now with us? And are there any plans to monetize the land bank of around 80 acres which we are having in Bengaluru?

Vinod K Hans: In Bangalore, we have about 55 acres overall size of land, almost similar size in Patiala, and about seven or eight acres in Bhiwadi. So that's a total land we have.

Manish Manchanda: Last question, Can you just specify me what will be the capital allocation of our company for the cash reserve which we are having right now with us?

Manish Chadha: So, you're talking about the cash availability? So the current strategy is to use this cash on the growth opportunity due to change in the emission norms, we are spending on innovation and modernization of the plant and machinery and also technical application. And we are also monitoring the global customers because they also need your credit viability. So, that is the current strategy for cash utilization.

Vinod Kumar Hans: On the dividend part I mentioned last quarter also that we are looking for really these transition to get you know stabilize and once we have passed through this, the company will be reviewing the dividend very favorably, but we have to pass this cycle of changeover to Euro-VII consolidation and some of the global difference getting settled around actually.

Moderator: Ladies and gentlemen you may press * and 1 to ask next question. The next question is from the line of Nitin Gandhi from KIFS Trade Capital. Please go ahead.

Nitin Gandhi: Continuing the previous question where you said your innovation, modernization, upgradation will taper but that won't be taking more than 10%, 20%, maybe 5%, 10% of the cash on hand 195 crores which you have. So, aren't any CAPEX plans to incur some bigger amount or use for better production efficiency, because you can't do buy back, you are already at 75%, so, that is ruled out.

Manish Chadha: First of all, this technology upgradation or renovation won't be Rs.10 crores to Rs.15 crores. So, first of all, these plants, this company is very old, 1954 in Patiala, and somewhere in 1980 in Bangalore. So, it requires quite handsome amount of money. So, maybe just to give an example, if we are spending, say, the CAPEX, maybe 2/3 is going into this and 1/3 we are spending on capacity increase, etc., It's a big amount and also as Vinod mentioned, if you see in our previous slides on this performance forecast, we are also evaluating the growth opportunity with this TGDI engine and also the steel piston which is very much in China. So, it will require huge investments. So, we are just evaluating on those and that is the reason we are keeping cash.

Nitin Gandhi: Will that be beyond Rs.100 crores?

Vinod K Hans: Close to that range, Rs.90 crores to Rs.100 crores as Manish said, two-third of that is going into the technology upgradation because as we said that Euro IV to Euro VI and the TGDI engine is really calling for not on the line chain, this is a work-in progress getting complete, but at the same time, if you recall last meeting, we did mention that our focus is to make our lines more flexible, say, for example, at the moment, the situation is that if we take a passenger car vehicles, at the moment, most of the OEMs they are sitting at a backlog of nearly five lakh vehicles, which are booked by the end users, but the companies are not able to deliver mainly on the semiconductor issue. So, that is on the passenger vehicle. However, on the two wheeler, I have to also concede that it's not a good situation that production is ahead of the demand actually. So, you might have noticed all the major two wheelers have reported a lesser sale during this quarter. And one reason which all these OEMs are claiming that a typical two wheeler today with the Euro VI norm, with ABS requirement, with also a lot of cash and other requirement on the lighting and speedometer and all, that's taken average price of two wheeler beyond Rs.80,000, Rs.85,000 is the base and with the Rs.100-plus petrol, the affordability of this is under question. So, why I'm taking this as the reference is that for us the focus is that our two wheeler and passenger cars, lines, we are making them really flexible so that we don't run into the risk that that we have a backlog of passenger vehicle or we have idle demand on two wheeler. So, all this flexibility does require a lot of transition and it will help us. So, going forward, the fluctuation you might see in the market. But we may not have to fluctuate in this manner. So, that's why I think two-third of investments of that magnitude which you refer to, we are almost ballpark on the same number is going in this direction and one-third is toward expansion actually, and this expansion we should have invested more but because of this market, we are really pushing this investment to next year as well then the new business which we mentioned in the last meeting of some of the export engines which that PSAs is now commissioning their plant, they're starting their engines, trial runs and another export opportunity. So, we are readying ourselves for that expansion as well, which is taking 1/3 of our I would say CAPEX in this financial year. But this will continue maybe in first quarter of financial year '22-23.

Nitin Gandhi: So, effectively what we mean is whatever cash flow we are generating in next two or three quarters equal amount will be spent on CAPEX in next two or three quarters, right?

Vinod K Hans: I don't know equal amount, but basically, you saw a figure of Rs.190 crores and Manish did mention a figure of 90-100 crores in CAPEX. So, we are talking about that kind of amount.

Nitin Gandhi: We are generating 40, 45 crores cash flow every quarter. So, after three quarters will be same back to the 195, 200 levels?

Vinod K Hans: Absolutely.

Manish Chadha: So, at the same time, we are also saying we are evaluating the dividend distribution because as you rightly mentioned, we have the estimate now, the CAPEX as well the generation. It's like that market is volatile, so, we have to keep an eye on that also and also as we mentioned global customer being served from India and we are looking with this technology upgradation, we are looking for that business, for that we need this credit viability. But I think we are also on the same page that with the CAPEX and cash generation, definitely we are evaluating for dividend in the coming years.

Nitin Gandhi: Can you share something on global export side because of Tenneco actually should substantially shoot up subject to semiconductor but you also need to spend time to set up the facility. What could be that additional business – can that be another 400, 500 crores business in three years? Right now, we are already Rs.1,300 crores business.

Vinod K Hans: It's difficult to put down the numbers right now, but as Manish mentioned earlier, that two-thirds of this technology transfer is the flexibility we are readying ourselves for some of the global business which either in terms of engine export from India or direct export. So, we are progressing very nicely in that direction. If we talk about the semiconductor this quarter, COVID has impacted the US and Europe more than what it has impacted say India, for example. So, there could be one or two quarters where these kind of seasonality will be there into our books, but directionally you can imagine that we are readying ourselves for that and it will have a good traction which should start coming once this cycle of semiconductor is gone, and probably I would say that second half of next calendar year, you'll see a major traction in that direction, a) because of the situation getting improved and b) some of the global programs will start hitting on the ground for us.

Nitin Gandhi: Can you enlighten with reference to post 1/3 expanded capacity, what is the peak potential revenue which will be possible?

Vinod K Hans: I think this will be a graded one, but Manish will be a better one to answer. Graded means, there will be some expansion in '22 and '23…

Nitin Gandhi: Assuming that whichever year happens, maybe '25 but what is the peak revenue potential based on the expanded capacity?

Manish Chadha: We are talking about 10% to 12% increase from the current capacity, say 125 and 130 crores.

Nitin Gandhi: How much utilization we are doing right now?

Vinod K Hans: We are talking about 1,400 crores on an average. I'm not talking about this fiscal but in general, earlier in January to March we did hit the number which was close to 1,500 crores annual run rate actually. What Manish is saying that probably 120 to 150 crores whatever, will be our additional on top of that actually once all these investments start producing for us.

Moderator: We'll move to the next question, which is from the line of Lakshmi Narayanan from ICICI Mutual Fund. Please go ahead.

Lakshmi Narayanan: One suggestion is that when we announced our results, maybe we can have a conference call subsequently within a day or so, otherwise it becomes, difficult for investors to track, right. So, it's a suggestion if you can incorporate that.

Vinod K Hans: Yes. Dr. Khalid is evaluating that and hopefully, we'll have a positive outcome of that.

Lakshmi Narayanan: Thank you so much. It'll be wonderful if you can deliberate and give a good conclusion. So, on the export side, is there any potential line getting shifted to India or any potential projects which you will see which will give you a kind of a leg up in exports? While there is always business as usual, is there any specific projects or something which you think can materialize over the next few years or so? Not asking for names, but any broad guidance would be helpful.

Vinod K Hans: We discussed in our last call also that into our investment. I would say a significant portion of this investment is shifting up for some of the key equipments. So we are not uprooting the whole line from Europe or US and installing it here because that is not an efficient way in our opinion, because these lines were tailor-made to a specific business. So, what we are doing is we are seeing what's more suited locally for us and in that manufacturing, what are we missing and then we are picking those equipments from there rather than copy pasting the whole model itself. It is a combination of, For example, if a standard equipment to uproot and replant in India with all these logistics issue and customs and other evaluation, complexity. It's better if the same equipment is available in India to have a new equipment; however, there is a specialty equipment which is not available in India. So, those equipments we are shipping from double rather than getting the whole total. And also we have been little mindful that rather than taking out the full automated robotized handling, we are trying to find our own local way of how to handle a product and we save a lot in doing that, I mean, fully automated robotized, I would say material handling line is not a right answer for a product.

Lakshmi Narayanan: Got it. We have seen a lot of auto ancillary companies or tier one suppliers be it Tapco or Sundaram Fasteners, etc., Talking about taking advantage of PLI and setting up separate lines, is that something which the global parents have deliberated upon or anything that you'd like to mention, because this is something which we see as a common pattern among some of the best auto ancillary companies including Bosch?

Vinod K Hans: So, we have had a couple of meetings already with all the stakeholders on this PLI. As still the policy is not in a fine print, but we are on top of it, we are evaluating with all the stakeholders and also consultants and we are also reaching out to our peers to really understand, because there's still a dilemma on the fine prints the way it is coming out. So, we are doing all these consultation at the moment and trying to see how we can fit it. But at the same time, I would say our first focus still remains how to capture these low hanging fruit of TGDI engine which Manish mentioned and really shifting some of the global businesses here and we support our customers there. But having said that, PLI, that is very much on the table for evaluation.

Lakshmi Narayanan: One last question related to the little long term trends like heavy weighting of engines or anything like that which will help us because what there is also we hear is that from 12 speed people are going to higher speed gearboxes, etc., Do you see any such things or even vehicles are moving towards I hear that a heavy commercial vehicle either the fuel is changing to a different kind of fuel or indeed CNG or it could be government is talking about ethanol, some of these larger trends, how they are going to help us from the increasing the component value of products that are going in maybe heavy weighting or it could be these high speed better tonnage vehicles, any immediate trends we are seeing or you think there is a high component value can be added for us?

Vinod K Hans: Yes, exactly, that was one of the high points of our presentation if you see our slide #9 or #10 where we have mentioned these two areas. So TGDI we are very happy with the trend. Frankly, when the Euro VI came, we had estimated a higher loaded engines like it happened in China, for example, but that was not the case because the cycle was too short for OEMs to jump from Euro IV to Euro VI. So, while most of the OEMs met the target, but the solutions were mostly gravitated towards the lightly loaded engines. You might have noticed the new bookings which are happening in the market space, whether you talk about some of the Toyota vehicles, some of the Mahindra, even Tata vehicles, the higher end vehicle with the loaded turbo engine are getting more share of booking than the base variants. So, that is a very, very good news for us. And the moment from I would say petrol to CNG or similar fuel is again a very good moment for us, because it does increase our value content overall. So, CNG, we have a pretty good, I would say, handle on the sinter product, our materials are pretty much secured and well accepted by our OEMs. And there's a good chance that these moments will really help us not only from the content point of view, but also from a market share point of view.

Lakshmi Narayanan: I just have one more question, In last call, you mentioned that there is a delay in material price movement correction which you can pass through, etc., And of course, our gross margins have actually come down a bit. Now, what is the status there, what kind of corrections we are able to take and what is the broad margin at which you like to operate a year from now assuming that things get normalized, EBITDA margin or gross margin contribution margin level, what is the band in which you like to operate?

Vinod K Hans: Maybe Manish can answer with the more objective numbers, by and large we have a spread of say about 30-plus customers actually, and we have these commodity escalators agreed with the majority of our customers, and the way the contracts are, they vary from one quarter, six months and yearly. So, there are customers with early correction of prices than with six months and there are a few where this correction happens every quarter. So, on an average, our typical lag is coming to nearly about seven to eight months actually when you sum total the whole cycle. So, for example, if we're buying something in this month of November, and if it is say 5% more you're buying off this commodity, this will get covered maybe on the seventh or eighth coming month actually. That's the lag we are talking. Having said that, we are approaching our customers to really reduce the cycle, for example, wherever we have one year contract with some of our customers, we are asking them, can we do it six month basis, so that this lag of seven to eight months is really hitting our financials or cutting our cash from that perspective. So, the way we are looking for example, these quarters there is a lag definitely. As you know, most of our commodity which we are buying whether it is aluminum, nickel, mostly our suppliers are attached by. That's the immediate hit you see on our financials and the recovery is coming only seven to eight months later. Unfortunately, the money which we are recovering now, for example, from our customers, which we were paying in, January, February, so we are much better off that we got our money recovered, but at the same time between February, March period to now the commodity also have moved up significantly and the material margin which we track, Manish can share with you some more details of how we are tracking that. Manish, over to you.

Manish Chadha: As Vinod mentioned, the recovery has a lag and now if you see from the Q1 to Q2 operational improvement is happening though raw material prices are up, but we are reducing the gap in the MCS increase and the recoveries. So, answering your question on the EBITDA what would be the number, today we are at 12% and I can tell you the net impact of MCS and recovery is 3%. If I will add in the normal scenario, it will add to 15% and then the volumes are also less and operational productivity which we achieve say I would add 1.1%-1.5%. So, it will be somewhere in the range of 16% we will say in the normal business scenario when the volumes are there, and there is no gap between MCS and recovery is somewhere around 16% is operational data. And as far as recoveries are concerned, we are tracking the customer wise recoveries and you will see the recoveries coming in the next subsequent quarters. And we can see whatever the forecast or projection we have, we see in the next year if prices remain the same, we will be recovering the money and overall MCS recovery stay within the range of 70% to 75% from the customers.

Vinod K Hans: Just to add on the aftermarket side where wherever we are, having a direct business with our end users or retailers. So, we increased our prices in July and we are evaluating how much should we transfer into the direct market where we have a direct business. So, ultimately, it has to be borne by some of the manufacturers and some by end users. So, we are testing that as well actually. We gave one increase in July and then we're probably re-looking because if this trend continues, we'll have to pass on the price increases in the aftermarket as well.

Moderator: The next question is from the line of Avinash Gupta, an individual investor. Please go ahead.

Avinash Gupta: Good afternoon. The cash available with the company is of the order of Rs.200 crores and another Rs.400 crores is the kind of borrowing capacity actually points debt-to-equity ratio of 0.5, so, that is something like Rs.600 crores which is more than the total value as on date. This gives me an impression that the company whereby have to change the business totally and put in a lot of money or you're sensing there are a lot of good opportunities coming somewhere which you're not ready to share at this point in time.

Manish Chadha: So, first of all, as we mentioned that the technology is changing, emission norms are changing, upcoming TGDI engines, first of all, we don't want to use any debt for that, but we have generated cash and we wanted to use that cash for this technology upgradation, emission norms, whatever with the new engines coming in. So, that is one. And secondly, as we already mentioned, this technology upgradation, the global customers are looking to be supported from India and we want to keep that financial credibility here, so that it will be a good strength for us to be in those businesses. We are not evaluating any major shift in the business what we are currently doing. We are just trying to be in line with the market, how market is behaving, with the change in emission norms and new engine program which are coming.

Vinod K Hans: I think one thing I would like to add for the benefit of the shareholders family is that, again and again, Manish is claiming financial credibility in front of our global customers is that we have to be mindful that Tenneco globally has still a lot of debt as a global company. So, that is foremost in our global customer mind. So, some of these perceptions do get carried away when we are discussing the business to be conducted from India. And that's where this cash and no debt situation is really helping in winning over the global business. So, in a way what we are trying to say is having a parent company in a significant debt, and if some business is to be moved to India… having a debt in India will really become impediment for a decision for our customers. In fact, our customers are very happy to see a debt-free in India.

Avinash Gupta: Okay, again, what I'm seeing is that the last dividend was paid in somewhere 2016 and whereas Tenneco has been paid somewhere around about two, three years ago. This policy that we have to conserve cash has been going on for a long time, and it's not something new. And it is much…?

Vinod K Hans: I agree. That's what Manish also mentioned that once we have stabilized with technology or a production cycle… I don't want to confuse you, right now, Europe and US is working on Euro VII. So it's a matter of one or two years that Euro VII will be in India and it will be a great differentiator for us. So, we will not probably even wait for that to happen, but we were really waiting for this cycle to be over. And once this is behind us without taking that whatever additional cash, as Manish already mentioned that there is evaluation going on, on dividend in coming years anyway. We did mention this before.

Moderator: The next question is from the line of Saket Kapoor from Kapoor & Company. Please go ahead.

Saket Kapoor: Firstly, the PAT margins are at the bottom. So, what steps are in the anvil? And what are the current utilization levels for us? I think we took a plant shutdown also at the end of the quarter. So, I think that was around 27th September. If you could explain the impact on PAT numbers and the way forward how H2 is shaping up depending upon the OEMs deliverables?

Manish Chadha: I have already mentioned that we have almost 3% net impact of MCS recovery for the current quarter. So, that straight away go to the PAT. And of course, there are capacity or I would say fixed cost absorption also impacting in the current quarter. So, PAT would be better if you will have a better fixed cost absorption and the MCS recovery. So, maybe we are seeing a 4% gap in the PAT in the current quarter. If volumes are there and MCS recovery and gap is not there, which we will be recovering in the subsequent quarter, and I already mentioned the overall total recovery is in the range of 70% to 75% with the cycle of one to six month and one year. Regarding capacity utilization, for the current quarter it is between 80% to 85% and different value streams for the current quarter. And as far as the impact of chips for the current quarter, I would say, somewhere around 10% of total FMG value and majorly coming from the light vehicle segment because of the chip shortage.

Saket Kapoor: We are already two-thirds of this quarter also. These lingering impacts are still continuing, that is what understanding is?

Manish Chadha: You're right.

Saket Kapoor: So this quarter also we will be in these utilization levels of 80% only as the best case?

Manish Chadha: First half and second half at this moment we see almost on the same level and we do have impact of chips with the OEMs and we see that trend also.

Saket Kapoor: We have seen an increase in employee cost quarter-on-quarter also.

Manish Chadha: As a percentage, it has not changed. So, we are keeping close eye and that will be one of our focus area apart from MCS and MCS recovery, labor productivity, but as we already discussed, the market is very volatile, we just came out of COVID and then this chip shortage and then also we are seeing uncertainty. So, I think once we will have the volume, we are already accessing players we are working towards that, but if you can see this is at least variable at this moment even with the flexibility of the volume. So, we have work to do, which we are focusing, but answering your question, percentage to revenue is almost the same.

Saket Kapoor: Could you explain the reason for the shutdown for the four days in holidays and its impact on the volume?

Vinod K Hans: So, this shutdown is in response to our customers actually, in a sense that if our customers are closed for nearly a week or 10 days, then we have two choices, whether to have workforce in a plant or distributed over 30 working days or total number of days in a month, or should we not also shut down and save on this cost of transport for our people, cost of canteen, cost of buses. So, I think it makes sense that if we can have also a shutdown in line with the market, then it will be good. If we're operating on 80% utilization, it makes sense to close down the plant for three to four days in a month rather than working those… and by the way, those three to four days closing of the plant is to use for ready upgradation of the line for us also. So, that's how we are modeling ourselves. So, this shutdown is more in response to the efficient working in the market condition rather than setting our labors 40% and then calling them back when the market comes back and having trained and skill them does not make a lot of commercial and operational sense for us. Your company is lucky in a sense that the way we operated on a model which we operated during this whole cycle of COVID, where there were a lot of issues relating to migration of labor, at least our customers told us that we were one of the companies where we were not impacted and at least our customers did not have to chase us because the labor were not migrating, we were able to really sit with our labor and workout shutdown days with them and trying to share the pain with them actually.

Saket Kapoor: The promoters reclassification if you could explain and the court matter also, any update on the same?

Dr. Khalid I Khan: We had a high court order in Bangalore directing us to make the payment to almost 50% to the former employees by 30th November and the remaining by 31st of January 2022. So we have started making the payments, so that is already in progress, and we don't foresee that the payout would be more than the amount already provided for. Hope that answers the question.

Saket Kapoor: We were firstly contesting it. Now there is no contest as such and that amount is now to be paid to them?

Dr. Khalid I Khan: Yes, we filed the curative petition and then we filed an application for early hearing. But unfortunately that didn't happen. And we don't have any control on how the Supreme Court of India proceeds, right. And we have to honor the order passed by the High Court of Karnataka. So that's what we have been doing.

Manish Chadha: Just to make it more correct that earlier in the call, we were informed that we have a strong case. So that was not the one and now we have accepted the judgment in totality and we are making the necessary payment. So the accounts that get set off going forward.

Dr. Khalid I Khan: Actually, so if we are making the payment, then our curative petition becomes redundant. We make the payment, then it doesn't hold any ground. So we are still maintaining that we have a good case and we are still expecting that we might get a date of hearing from the Hon'ble Supreme Court of India and we tried that, we have filed an application for urgent hearing, but that has not happened and we don't have any control on how the courts proceed. We cannot be in a suit for contempt of court.

Saket Kapoor: I think earlier that it was a strong case for the company, that is not to be considered and we have accepted, whatever have been the judgment and we have to go ahead with it?

Dr. Khalid I Khan: Absolutely, absolutely. Because we had contempt proceedings started by former employees.

Saket Kapoor: On reclassification of promoters, can you throw some light?

Dr. Khalid I Khan: Maybe you would recollect that IEH FMGI Holdings, LLC acted in concert with Tenneco Inc. and bought the shares in the open offer. Subsequently, it sold all the stake and it is not holding any share as of now. So we have complied with the minimum public shareholding of 25%. So public shareholding as on date is 25.02%. So, as on date, IEH is not holding any shares. Earlier, they were classified as promoters. Now, they have to be reclassified as non-promoters as per SEBI regulations. That's what we are going to do.

Saket Kapoor: This court part issue, we investors were not separately informed that the company is making payment, we were of this opinion that it is to be contested and all, no mention of the same in the press release, nothing.

Dr. Khalid I Khan: If you see the note to the September quarterly results, we have been updating the investors, because it is dynamic, as the situation changes, we have to inform and that's what we have been doing, in a note to that effect that we have a high court order which was passed on 27th of September and it directed us to make the payment to some of the former employees by 30th of November and to the remaining former employees by 31st of January. So, we have started the process now. We have to go as per the order, right, because we had contempt proceedings already filed by former workman against the company.

Saket Kapoor: Just to conclude that the teething problems which the industry and our company in particular facing, these factors would get linger away only post six months from now. And the impact of the chips shortage and other issues are still going to linger around for the coming two quarters and the performance of the company in the first half we are proceeding to replicate somewhat in the same vicinity only, there is no other signal of an upward revision in utilization level depending upon these factors, so this conclusion is correct sir?

Vinod K Hans: As Manish mentioned, for us the first half and the second half look pretty much the same, because if you talk about this particular quarter since you mentioned, so, this particular quarter the impact of the semiconductor will be worst, let me put it like that. But having said that, now with the current indication for our OEMs that they are now getting better visibility from December onwards. So, when we say having better visibility, will that knock off the five lakhs booking backlog with all the OEMs have claimed in the market, no, this five lakhs booking will not be going straight away because this semiconductor problem as we learn from them will be solved, it is not going to be zero or one, it's not that in January, if there's a demand, say company, Maruti make more than two lakh vehicle, they will get chips, I don't know, I mean, the answer is it will be step-by-step improvement. The good news is that this is consistent across the OEMs. So there's a better visibility of the chips for sure. So that's the reason the coming four months could be better than the last four months. That's the way to look at. Whether these coming four months, we'll be able to remove the backlog? Our estimate is no, this backlog will continue till mid of '22. Although we are not buying direct semiconductors, but we also, like you, are very much interested in understanding what's happening and we are getting into very close communication not only with our customers, with all our companies within Tenneco. So fortunately, we have more than 100-plus locations and there is a meeting around that. So we do what's happening in China, what's happening in Japan, what's happening in Brazil. So that gives us a little bit better idea as to what's happening. Regarding the performance part, as Manish also mentioned that there is a lack of recovery. So assume that next five months if the commodity price do not go up, but our recovery will be better. So obviously with that situation, the performance definitely would improve in the second half. But if the commodity prices really become out of control, then this lag can be there. I don't know if I answered your question or not. The simple answer is if the commodity remains stable at the moment they look like, then there is improvement in performance because we'll get the recovery due to lag which Manish mentioned six to eight months.

Moderator: Ladies and gentlemen, due to time constraints, that was the last question for today. And with this we conclude today's conference call. On behalf of Federal-Mogul Goetze India Limited, we thank you for joining us and you may now disconnect your lines.