



“Elecon Engineering Company Limited Full Year 2018  
Earnings Conference Call”

**May 31, 2018**



**MANAGEMENT: MR. PRASHANT C AMIN – EXECUTIVE DIRECTOR,  
ELECON ENGINEERING CAPITAL LIMITED  
MR. KAMLESH SHAH – CFO, ELECON ENGINEERING  
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**Moderator:** Good day and welcome to the Elecon Engineering Company Limited full year 2018 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing ‘\*’ and then ‘0’ on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Binay Sarda from Christensen IR. Thank you and over to you, Mr. Sarda.

**Binay Sarda:** Thanks, Janice. Good morning to all the participants on the call and thanks for joining this Q4 and full year FY2018 earnings call for Elecon Engineering. Please note that we have mailed out the press release to everyone and you can also see the results on our website as well as it has been updated in the stock exchanges. In case if you have not received the same, you can write to us and we will be happy to send this thing over to you.

Before we proceed to the call, let me remind you that the discussion may contain forward-looking statements that may involve known or unknown risks, uncertainties and other factors. It must be viewed in conjunction with our business risks that could cause our future results, performance or achievement to differ significantly from what is expressed or implied by such forward-looking statements.

To take us through the results of this quarter and answer your questions, we have with us the management of Elecon Engineering represented by Mr. Prashant C Amin – Executive Director and Mr. Kamlesh Shah – CFO. Mr. Amin will give a brief overview of the quarter gone passed and the full year FY18 results and then will open the floor to Q&A session.

With that said, I will now hand over the call to Mr. Amin. Over to you, sir.

**Prashant C Amin:** Good morning all. Ladies and gentlemen, a very warm welcome to our Q4 FY2018 conference call. Discussing the result at the standalone level, we have had a relatively healthy quarter from a margin standpoint with gear business reporting good performance. During the quarter, the topline grew by 0.1% year-on-year to 369.8 crores from 369.4 crores. The EBITDA on absolute basis stood at 76.1 crores as compared to 88.3 crores during the corresponding period of the previous year. This translates to EBITDA margin of 20.6% in Q4 FY18. We closed this quarter with a net profit of 50.2 crores, a significant increase from the previous quarters.

From a quarterly perspective, our performance has been consistently healthy, largely driven by improved product mix and traction in the gear business as a whole. On a yearly basis, our performance has been muted. Our total operating income was 911.27 crores in FY18 as compared to 923.36 crores last year resulting in a decline of 1.3%. EBITDA stood at 111.1 crore, a decline of 32.1% from the previous year. This translated to EBITDA margin of 12.1% for the year. We ended the financial year with a net profit of 8.1 crore. With the gradual pickup in economic activity and increased inflow orders towards the end of the year, we saw a gradual increase in performance during the year. Export revenues were at 66 crores compared to 49

crores last year. Despite the economic headwinds, we saw significant increase in the order booking with orders worth 555 crores book in the gear business and closed orders worth 286.3 crores in the material handling business. This translates to an order booking of 767.2 crores for the gear business and 469 crores for the MHE business for execution in the coming year.

Our overseas business Benzlers and Radicon registered a revenue of 277.8 crores with EBITDA of 5.9 crores. Overall, we saw headwinds across the industry due to slowdown in economy as well as muted activity in the engineering sector. With the change in strategy and reorganization done during the first half of the year, we believe that the performance will continue to improve in the medium to long-term future. With the pickup in economic activity, increase order inflows and positive demand outlook, we continue to remain positive on our business strategy and revival of macroeconomic activity.

Thank you all. We will be happy to address your specific queries about the business going forward.

**Moderator:** Thank you very much. Ladies and gentlemen, we will now begin with the question and answer session. We take the first question from the line of Sunil Kothari from Unique Investment. Please go ahead.

**Sunil Kothari:** Sir, basically we were giving the thoughts about selling or hiving off our international business sometime if there is a good buyer and if you can reduce debt by those hiving off. Is there any thoughts of further progress or nothing is happening?

**Prashant C Amin:** Are you talking about the overseas subsidiary?

**Sunil Kothari:** Yes, overseas subsidiary sir.

**Prashant C Amin:** To be very honest, I do not think we are really looking for hiving it off. As a matter of fact, our export outlook is not looking better. Eventually with the increased effort put in and if we bifurcate our exports division or overseas divisions, two of our divisions have actually come into very positive figures. They are seeing net profit. The only reason you see on overall burden on the EBITDA or pressure on EBITDA is because of the strategy that we have followed in USA which has actually started paying off. So, two subsidiaries out of the three subsidiaries have actually shown very impressive turnaround and we believe that this year we have taken the necessary action in the US working and that will also produce some results which will give an overall positive response. Our trust on export is very high and we believe that we have a better place to work on the export market with lot higher margins compared to the domestic market.

**Sunil Kothari:** Because the current margin is very low and with little bit fluctuation in currency, we go to loss. So, is it possible to give some, maybe in the near future double digit margin of this Radicon and Benzlers segment?

- Prashant C Amin:** If we really go at our UK and Sweden subsidiary, I think we are at a very close to double digit EBITDA margins. We have almost achieved 8 to 9 and 9.5% in both the subsidiaries for this year. So we do expect roughly 10%-15% growth coming up in both those regions, the European as well as the UK subsidiary and with an improvement in the US with the cost restructuring that is already into effect, we believe that we will go forward the double digit, but I think double digit is about I would say 2 years away from today and as a whole.
- Sunil Kothari:** So, what we are losing in this third subsidiary?
- Prashant C Amin:** The third subsidiary is the US subsidiary that we are talking about. It is the US market.
- Sunil Kothari:** So, US market, is it negative or positive?
- Prashant C Amin:** This year was negative only because we have put in an informed strategy of putting in sales activity. We have expanded, so it has only covered the market which is now directly coming to us.
- Sunil Kothari:** So hopefully this year is to turn positive?
- Prashant C Amin:** Yes, actually our target is to make it not loss making this year and breakeven in the US. But this is a strategy that can really pay off once we start getting some large project orders from US.
- Sunil Kothari:** And sir second point, in this MHE division, we were saying that all the loss-making projects will be completed by June which is just a month or two away. So how much we are on target and what is the outlook for MHE division because now we will be focusing on MHE product business only which should have at least very reasonable good margin.
- Prashant C Amin:** See, our target of completing this loss-making project by June was derailed a little bit by a strike at I think in one of the projects. So out of the two projects, we are sure of completing the project where there was no strike by June and the second project is likely to just maybe extend another couple of months or so. But the biggest negative impact of those cost overruns are always included in the March results because we have been following the project reporting and so we have already estimated what is the expected cost of completion.
- Sunil Kothari:** So, what is the outlook sir, growth and margin for MHE?
- Prashant C Amin:** For MHE, we expect to reach roughly about 400 crores turnover in the coming years with achieving a positive result.
- Sunil Kothari:** That is after interest depreciation you mean to say?
- Prashant C Amin:** Yes. We do expect to do that.

- Moderator:** Thank you. We take the next question from the line of Arvind Joshi from Bateleur Advisors. Please go ahead.
- Arvind Joshi:** I just had a couple of questions. One is we have been interacting with our competitors like Shanthi Gears and Premium, they are quite buoyant in their outlook. They are saying this is a beginning of a recovery and their visibility for 18 to 24 months. Do we also concur on similar thinking or you feel product mixes make a big difference in the outlook?
- Prashant C Amin:** We have definitely seen some traction in the gear business in the last quarter or two, but the projects are still far and few in between in general, but we are expecting to deliver roughly at about, between 12% to 15% in the gear business for the coming years for sure.
- Arvind Joshi:** With better margins?
- Prashant C Amin:** Of course, yes.
- Arvind Joshi:** And sir one more thing I wanted to know. This global recovery is helping our subsidiaries to do well or is it global recovery plus our strategy that we have undertaken for our export business?
- Prashant C Amin:** It is very interesting. Europe is definitely showing some sign of recovery. When I look at our numbers, I think it is probably because of our continued focus and staying on course in those markets have started now paying us the results. European market which is traditionally very tough to enter. Our persistence of last 7-8 years in the market and having a say in it is definitely have started showing denting into the revenue over there now.
- Arvind Joshi:** So once the recovery picks up, we could participate on a much larger scale, you mean to say over the next couple of years?
- Prashant C Amin:** Yes. We are seeing that positivity definitely is coming in.
- Arvind Joshi:** And sir I also wanted to know are we selling any of our products under Elecon brand in either US or EU?
- Prashant C Amin:** No. Our larger industrial reducers are mostly growing with Radicon.
- Moderator:** Thank you. We take the next question from the line of Ritika Garg from Equitas Investments. Please go ahead.
- Ritika Garg:** Sir I wanted to know what is the sales we expect in the MHE division for FY19?
- Prashant C Amin:** We have already given that number out. We are expected to touch roughly 400 crores.

- Ritika Garg:** And sir on a PBT level, the subsidiaries have broken even and what do we expect going forward like I know the US subsidiary is the one that is holding us back.
- Prashant C Amin:** Our projections are that we will have the US subsidiary breakeven this year and the European and the UK subsidiary to grow at about 10%.
- Moderator:** Thank you. Next question is from the line of Sunil Kothari from Unique Investments. Please go ahead.
- Sunil Kothari:** Prashant bhai, any strategic decision to reduce our debt, any possibility in near future or medium term?
- Prashant C Amin:** We are definitely looking at increasing some capital in the system. We are evaluating various options available to us and hopefully within next few months, we might be able to come and focus or maybe strategize that.
- Sunil Kothari:** And divestment of any asset or any business is on the horizon or first is capital raising?
- Prashant C Amin:** It will be mostly on the capital raise. On the divestment side, we are consolidating the material handling division. So, we will have to take a call on how that business goes forward, but we are very confident that on a product-based strategy, we will be quite successful.
- Sunil Kothari:** Just to clarify this MHE division, you said will be breakeven at PBT level?
- Prashant C Amin:** At PBT level, yes.
- Moderator:** Thank you. Next question is from the line of Rohit Potti from Marshmello Capital. Please go ahead.
- Rohit Potti:** Sir, just wanted to understand what is the capacity utilization in each of the business segments today, gears, MHE and global businesses?
- Prashant C Amin:** We would put in on an overall basis at 50%.
- Rohit Potti:** That is interesting. Could you detail a little more on the capital raising? What will capital be raised for, primarily it is a paid down debt, or you need it for further working capital?
- Prashant C Amin:** Mostly, we would be focusing on reducing the debt burden. We do believe that on an ongoing basis going forward with the business plan we have for this year; the working capital would rotate quite well.
- Rohit Potti:** Sir, going forward which business do you expect to pick up sooner, domestic or global?

- Prashant C Amin:** Domestic is definitely expected in terms of number wise, lot larger than that. We are counting on the export market to give us also better margins.
- Rohit Potti:** So, one last question from my end. At this position, how long do you think you can continue without increasing capacity for the next 24 to 36 months, is it?
- Prashant C Amin:** I think that is a very good guesstimate. I think 2 to 3 years we should be able to manage growth coming in without adding any more capacity.
- Rohit Potti:** So just trying to understand the capital allocation thoughts of the management. Once the balance sheet is repaired, its buyback or increased dividends in the thought process of the management going forward if the business does well.
- Prashant C Amin:** Unfortunately, we cannot comment on that. I think we will have to take it as it comes in the next couple of years.
- Moderator:** Thank you. Next question is from the line of Venkat Subramanian from Organic Capital. Please go ahead.
- Venkat Subramanian:** Not very long ago, our EBITDA margins even at utilization levels of about 65% used to be closer to 20%. With some uptick actually in domestic demand, how long do you think we need to wait to probably see that direction?
- Prashant C Amin:** I think we are very close to that in our gear division right now anyway and with increased capacity utilization, it will definitely go and cross that within next 12 to 18 months for the gear division. On the material handling division, we will have to see as it comes in, once we go over the breakeven point, then obviously the EBITDA margins will start improving on that. Obviously, it is very difficult to go to 20% level in the material handling division. At best, you are able to get into about 12 to 15% range at an optimum level.
- Venkat Subramanian:** In that context sir if we are fairly close to those kind of margin levels, what will capital infusion be required for?
- Prashant C Amin:** Actually what you are looking at, our debt restructuring whatever the past debt raised to be settled, that is what we need. With that kind of margin as I had already mentioned that we will be quite comfortable in rotating our money.
- Venkat Subramanian:** And do you have some disputes and some customers not taking our material etc., have we found the resolution for that because that also can probably help in that reduction, right?
- Prashant C Amin:** That can definitely help. All the legal requirements are being followed very rigorously. It takes a little while before the resolution comes on the legal side.
- Venkat Subramanian:** How close are we sir with respect to that?

- Prashant C Amin:** Positive results in our favor have started coming in. Now, we have to realize them as it happens.
- Venkat Subramanian:** Can you kind of quantify that sir? We remember that figure to be about 50 to 70 odd crores.
- Prashant C Amin:** At this point in time, it is very difficult to quantify that numbers, but we can say that whatever results have so far come, they have all come in our favor and as you know that it gets into an arbitration and then negotiations and all those things, so it takes its own time. But all we can say is that they definitely have started trickling in.
- Venkat Subramanian:** I am saying this has been lingering for more than a couple of years. Do we also get penal interest and delayed interest etc. in situations like this?
- Prashant C Amin:** Well, it goes on a judgment to judgment cases. Most of the cases, people are willing to give your capital back.
- Moderator:** Thank you. We take the next question from the line of Nitin Gandhi from KIFS Trade Capital. Please go ahead.
- Nitin Gandhi:** Can you guide me what are your existing debt and what are the cost of borrowing them? You have debt of 357 crores.
- Prashant C Amin:** The current debt is 496 crores.
- Nitin Gandhi:** And cost?
- Prashant C Amin:** The cost is about 11.5% to 12%.
- Nitin Gandhi:** Can you give guidance for your transmission equipment, you have shared some thoughts on material, but if possible what are the margins on those likely to be, it is 806 crores turnover, right, transmission equipment?
- Prashant C Amin:** Transmission is the gearing equipment, yes. Your question is at what margins are we working on? We are working at target EBITDA towards 20% in the transmission business.
- Nitin Gandhi:** I am asking what is the revenue growth you are expecting for FY19 and 20?
- Prashant C Amin:** We are expecting about 15% growth in FY18-19.
- Moderator:** Thank you. We take the next question from the line of Abhishek Bhardwaj from Green Lantern Capital. Please go ahead.
- Abhishek Bharadwaj:** Sir, we have few orders from Navy on the gear business. Any update on that? When do we execute?

- Prashant C Amin:** We start executing and supply starting this year. We will be doing billing of that in this particular year and then the balance over the next 3 years as per the schedule and we are on schedule on those orders.
- Abhishek Bharadwaj:** Any further orders in pipeline from Navy?
- Prashant C Amin:** They take long time, but yes, we are preferred supplier for Navy on quality gearboxes. So, we do expect that as they go out and require more ships and may build them in India.
- Abhishek Bharadwaj:** Few months back, there was some news item wherein government had directed power plants which were close to coal mines to invest in covered conveyors, some 50-60 kilometers of covered conveyors and I think DVC and NTPC were to put up some 7 or 8 covered conveyors. I understand we are in that business, in the MHE we do covered conveyor belts. So, would we be bidding for that?
- Prashant C Amin:** Yes. We are in the bidding for all what we call the pipe conveyors. We have already executed 2 to 3 orders in the pipe conveyors and as they come about, I think we are binding ourselves well placed on those kinds of tenders.
- Abhishek Bharadwaj:** So how many players do covered conveyors in India?
- Prashant C Amin:** I think there are about 3 to 4 players.
- Abhishek Bharadwaj:** If a typical covered conveyor is 50 kilometers, how big is the project size?
- Prashant C Amin:** Depending upon the size, it can be anywhere between 100 to 300 crores.
- Abhishek Bharadwaj:** On the export front, I remember you were suggesting that there could be some traction and there could be some orders coming in from US on the gear side. Any update there?
- Prashant C Amin:** We have improved our export billing last year and we will continue to do that at hopefully little better pace than last year for sure.
- Abhishek Bharadwaj:** But any large orders that we expect from US or it will be small increase only?
- Prashant C Amin:** No, most of the US as well as the European economy is not doing very large projects. We do have a few in the far East, but they are coming slowly, but we are seeing good enquiry level on our catalogue type of products, our standard large gearboxes.
- Moderator:** Thank you. We take the next question from the line of MS Arun from Capital Markets. Please go ahead.
- MS Arun:** What is the export number for FY18 sir?

- Prashant C Amin:** Export numbers, I think we did 69 crores last year.
- MS Arun:** So, could you give the breakup of gears, what is the standard thing and what is the custom made?
- Prashant C Amin:** At this point in time, I will not be able to give you those breakups, but they all come in all mixed quantities. This is not as a result of any one particular large order.
- MS Arun:** Could you see the demand, which segment is showing some signs of traction for gears in these two segments?
- Prashant C Amin:** In the domestic market, obviously we are seeing cement more than steel. On the overseas market, it is a mix. The results are because of our being there for long time and sales force taking efforts right now.
- Moderator:** Thank you. We take the next question from the line of Abhilasha Satale from Dalal & Broacha. Please go ahead.
- Abhilasha Satale:** Sir, you mentioned that you will be completing some loss-making budgets by June. So, I wanted to understand that with improved outlook for MHE division, how do we see a receivable cycle moving up? Do we see further improvement in terms of debtors?
- Prashant C Amin:** When we complete this project, which are burden on the sales numbers, we are focusing on the products where the receivable cycle is not an issue. Those are mostly on supply basis and erection commissioning. So, this particular type of product orders do not put lot of burden on receivable in the long run.
- Abhilasha Satale:** So, can we see our working capital cycle improving in FY19?
- Prashant C Amin:** Yes, obviously because the biggest drawback, the positive side would be that we will be entering into the positive numbers.
- Abhilasha Satale:** And is there any retention money? How much could we able to recover post completion of these projects?
- Prashant C Amin:** The retention money is directly related to the completion of the project and the terms of the contract. So, we keep working at it and finished them. As we finish and clear the large EPC type of contracts, they obviously reduce because they are getting completed and the product orders do not have a very significant portion of that and if it is there, it is a very short cycle compared to the large projects.
- Abhilasha Satale:** So is there any number on this like how much.

**Prashant C Amin:** No, that exact number is very difficult to say. It all depends on the project as they get completed.

**Moderator:** Thank you. The next question is from the line of Arvind Joshi from Bateleur Advisors. Please go ahead.

**Arvind Joshi:** Sir you mentioned like our capacity utilization has been in the 50s for quite some time now and now with the business picking up, once we hit say 70%-75% capacity, will it lead to very disproportionate improvement in margins? How do you see? I think that should be the obvious outlook, right?

**Prashant C Amin:** Yes. Once we start hitting those numbers into 70-75, likely to see a vast improvement in our EBITDA working.

**Arvind Joshi:** Sir on the MHE side, we have been in the good old days have got margins around 25% on product, they fallen as low as 4%-5% in those days of very high competitive wars that were going on in the market. Now what is the kind of realistic margin that one can look with the slight improvement in the scenario and considering there are not too many players left in the game, would you be looking at 10%-15%?

**Prashant C Amin:** At this point in time, we are looking at between 10%-15% at utilization.

**Moderator:** Thank you. Ladies and gentlemen, that seems to be the last question. I would now like to hand the floor back to the management for their closing comments.

**Prashant C Amin:** According to us, we are looking at a fairly positive trend going forward into the coming years both coming from the gear domestic as well as the export market and the material handling division which the strategy change has started now coming into effect, we do believe that we will stabilize that division in the coming year and then if the market on the project side improves, it will probably show some large number increase in 2 years going forward. But the general outlook for the next year is positive. We should improve by anywhere between 10%-15% on the topline and the EBITDA margin improvement should come quite substantial in the coming year. With that, I think we will close. Diwakar or anybody else, any more other questions, I think we will close the call. Thank you. We appreciate all the questions and participation in this investors call.

**Moderator:** Thank you very much. Ladies and gentlemen, on behalf of Elecon Engineering Company Limited, that concludes this conference. Thank you for joining us. You may disconnect your lines now.