"Pennar Industries Limited Q2FY15 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Pennar Industries Limited Q2FY15 earnings conference call. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing * and then 0 on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Manish Raj of Dolat Capital. Thank you and over to you, sir.

Manish Raj: Thank you, Inba. Good morning all. On behalf of Dolat Capital and Pennar Industries, I welcome you all to the Q2FY15 conference call of Pennar Industries. We have with us Mr. Aditya Rao – Executive Vice Chairman of Pennar Industries to discuss the results and business outlook. I hand over the call to Mr. Rao for his opening remarks. Over to you sir.

Aditya Rao: Thank you. I hope I am coming through clear. To the investor community and other stakeholders of Pennar Industries, a very good morning to all of you. It gives me a lot of pleasure to be with you today on the second quarter investor conference call for Pennar Industries.

To start off, I will give you an overview of the performance for the company and its subsidiaries for the quarter in question and after that, sectoral outlook for each of the 6 business units. And after that is done, we will open the line for questions and any clarity or any further detail that would be required can be provided after that.

So I will start off with an overall performance:

For the second quarter of this financial year, the company had gross sales of INR 332.7 crores, EBITDA of INR 24.3 crores, and profit after tax of INR 7.1 crores that represents 21.4 % growth in gross sales and 30% growth in EBITDA. However, due to the new company law, our treatment of depreciation and deferred tax had to be a little different which has resulted in the profit after tax only showing a 8% growth. This is something we will explain over the course of the call. But from an EBITDA performance point of view, we are very glad to say that the consolidated entity has grown at double digits across all measurable indices including sales, EBITDA, margins, cash flow, and profit.

The standalone company had gross sales of INR 226.2 crores, EBITDA INR 15.9 crores, and profit after tax of INR 4.4 crores. Pennar Engineered Building Systems, our subsidiary, saw significant growth again this quarter. The gross sales is INR 104.8 crores, EBITDA of INR 7.9 crores and profit after tax of INR 2.7 crores, again lower because of the higher depreciation value that had to be taken into account because of the new company law.

To give you a segmental breakup of what we have achieved for the second quarter, we saw strong performance growth driven across all segments. All of our business units have grown with the exception of steel products on a year-on-year quarter basis and also on a quarter-on-quarter basis. Most of the growth has been driven by adding new customers, new businesses also to our business segments and we had substantially good order wins in our project driven businesses that includes railways, pre-engineered buildings and also environment business. We also continue to have a strong balance sheet and the CAPEX for all of the new products and businesses we are entering into is being driven completely through our internal accruals and the debt of the company on a consolidated basis and on a standalone company basis has come down over the quarter. No new debt has been raised and the performance improvement that you see has come on the back of our own internal accruals.

On a segmental performance basis, steel products had Net sales of about INR 100.2 crores. The Tubes business did INR 33.7 crores. Industrial Components recorded sales for the quarter of about INR 12.9 crores. Systems and Projects saw a big leap at INR 48.7 crores. Our Pre-engineered Buildings business was at INR 91 crores and Pennar Enviro had since it is a low base, it is a massive amount of growth, but it ended the quarter at about INR 6.1 scrores.

Going forward, our Pre-engineered Buildings business and Environment business and the Systems & Projects business share of revenue will continue to increase disproportionately since their growth rates are higher than the average growth rate for the company. The Tubes segment will also continue to see growth. On a revenue share point of view, it will more or less stay where it is because it will be near the company's average growth rate, but the margin improvement that comes in because of the focus on our new value-added products which are CDW and stainless steel will result in improving margins.

The Steel Products business will continue to have stability. So while the total sales that we have from that business will remain constant. As a percentage of a growing company in terms of revenue and EBITDA, that share will continue to decrease and this is in line with our expectations and our plan for this business. 10% of revenue for the Steel Products business has come from new businesses and we are now going to switch our focus to special grades. Again, we do not expect massive scalability in revenue and profitability to come in steel products, but what we do have, we will grow by a small amount, and the margins will be sustained because of our focus on special grades.

The Tubes business EBIDTA for the quarter has grown quite well, 50% compared to the second quarter of the last financial year. However, the sales have also grown by lot. The CDW tube business has grown quite well and the new CAPEX that we are doing will bring on increased CDW production over the next few months. So we expect this year to be a very good year for tubes with strong double-digit growth.

In our Industrial Components business, there was a lot of investment that went in last year. Some of that has started to bear fruit. We have added several high-margin products. Some of these products are the Wedge Barrier system which is an export product, we have started shipments in the last month of last quarter will have a disproportionate impact on the bottom line. Though the revenue will continue to be small, the margins on these are so high on the tune of about 35-40% that we will see significant improvement in this division's margins. We have also added new customers in Xylem, Firestone TVS, and also an order that we have received recently for water treatment components as well.

Our hydraulics plants remain in line. We have completed CAPEX, completed installation of the facility. The hydraulics business division is in the Industrial Components business and we have received a trial order from Bailey**,** a US based company. Once we are able to scale that business up, our goal is to use that as an anchor customer and increase India and export revenue in that business.

Systems & Projects, as I mentioned, has done quite well. While we open the quarter with strong order book, we have now grown that order book. More importantly, we saw the execution of wagon orders which we had not seen for a very long time. So while in the first quarter, entirety of railways was about INR 16 crores. In the second quarter, every month was INR 16 crores and we were able to consequently scale up that business substantially. We have supplied to major wagon integrators such as Texmaco, HEI, and BESCO and our ICF sales also continue to increase. There is new capital expenditure that is going on in this business division and with the expansion of our new plant in Chennai where we will be adding a bay and adding various fixtures spot welding and other equipment, we expect our Integral Coach Factory revenue to increase substantially. This is important because our ICF revenues are at a very high margin. So we continue to expect that this year's Systems & Projects revenue will increase at a very high level and we have high hopes for this business division in the next few years as well.

Our Solar business is usually depressed in the first half of the year. However, we did have some execution. In the second half of the year, we expect this to improve a lot. In the second quarter of this financial year, we have booked orders from L&T Solar; from Mahindra; from BE Solar, a German company and also from Azure Power. So we will continue to see this business doing quite well and Q3 and Q4 are usually good months for Solar and we expect revenue in this business division, Systems & Projects to be driven by both railways growth and solar growth.

That brings me the first subsidiary, Pennar Engineered Building Systems. The order book for the company stands at about INR 350 crores. We are not wanting to increase the order book a lot because of the inherent raw material risk this industry has, but we are ensuring that revenue growth does come in. In the Q1 of this year, we had gross sales of about INR 115 crores. In the second quarter too, we have sustained that. From a quarter or on year-on-year basis, we have increased sales from INR 80 crores at a gross level to INR 105 crores. EBITDA too has increased at a very high clip in PEBS. We had a 25.8% growth in EBITDA from Q2 of last year to Q2 of this year. Going forward, we expect the growth momentum in this subsidiary to continue. A lot of our revenue comes from new businesses. Another way of saying that is 50% of our businesses repeat customers and that is very important part of our business where people we had executed projects for, people we have completed projects for, their follow-up orders essentially create a critical mass of order book that we have which allows us to scale beautifully because we can count on half of our revenue this year coming in next year and even we can focus just on growth and new customers bringing in the remaining.

Pennar Enviro is a subsidiary that just started about a year and a half ago. Company has grown well. It has booked INR 65 crores orders in total. About INR 41 crores of that is currently going to be executed which has not been converted yet into revenue. The margins for this business are strong. The variable contribution levels for projects business at 15%, our Additives business at 60% and our Standard Plants business at about 30%. So we expect that the scalability options in this subsidiary are quite good. Once we have our pre-qualifications in and we have completed about 6 projects which we have handed over and received customer satisfaction certificates from them and these are good companies, these are companies such as Larsen & Toubro, Amtek Auto, Sanofi, Shantha Biotech, Hetero Pharma for whom we have completed 2 million liter desalination plant and others. Once our order book has been completely executed in Pennar Enviro, we believe the pre-qualifications that will give us will allow us to scale this business up much quicker, but we are quite proud of what has been achieved in a very short period of time in this business division. So that is the overall performance picture for the company. We expect all of our business verticals to continue growing.

Steel Products vertical was the one business which did not grow on a quarter-on-quarter basis. However, we have put a new team together on that and with a focus on special grades and on further formed components such as electrostatic precipitators, for which we have booked a lot of orders in second quarter which we will execute in third quarter. We have a lot of confidence in saying that we will continue to see consistent good double digit growth in the next two quarters as well across all business divisions. Steel Products which did not grow will also grow in the next division. With that, I would like to hand it over for any questions from the investor community. Thank you.

Moderator: Thank you very much sir. Ladies and gentlemen, we will now begin the question and answer session. Our first question is from Gaurav Maheshwari of Unilazer Ventures. Please go ahead.

Gaurav Maheshwari: Aditya, couple of questions. First is on Systems & Projects, we saw the margins going down as compared to the last quarter, but we can understand that last quarter could be 19% was not a sustainable number. So what is the sustainable margin in the S&P business?

Aditya Rao: The margin growth essentially came in because of the new wagon orders that came in. The wagon orders were at about 11% margin and that kind of pulled down the overall margin a bit and 11% is variable contribution. These are the first wagon orders we saw in a very long time. So we have also been conservative in our estimates of how we would compute the margin on this. There is a new wagon tender that is opening up in December where we hope to get a substantial chunk again further increasing our order book in this business, but the 19% is on the back of our ICF revenue which continues to grow in scale and will continue to have variable contribution margins of 30% plus. Our wagon orders as they keep growing in terms of the order book size and also the margin that we get, we will see a scale up in this business. I would not say 19% is unreasonable, but yes a blend of solar plus wagon plus coaches, I think will help us get to above 15% EBITDA is our target and we are confident of being able to achieve that overtime.

Gaurav Maheshwari: My second question pertains to our Solar business. So what is the order book over there which is pending?

Aditya Rao: Solar, we are treating in a different way right now. We are focusing on large customers and the order book that we have right now is well in excess of 100 MW and about INR 48 crores is the order book we have right now which comprises L&T, PE Solar, Mahindra, and Azure Power.

Gaurav Maheshwari: So basically INR 48 crores from solar and INR 71 crores is pending in the Systems & Projects in the Railway part of it for this year right?

Aditya Rao: Yes. Actually order book for Railways will be substantially more than that, but there is a lot of un-interest thing which will go into next year as well. So for this year, you can take that much yes.

Gaurav Maheshwari: So INR 120 crores should get added to our topline this year itself?

Aditya Rao: Well again, the December wagon order could also increase. We are also looking for more solar orders also, but at a very minimum is what you can take that number as. That order book has to be executed this financial year.

Gaurav Maheshwari: In terms of Pennar Enviro, so you said that INR 41 crores is unexecuted yet. So we would be ending this year at 60-70 odd crores number or higher than that?

Aditya Rao: I will not be able to give guidance. We expect the INR 41 crores to be executed in this financial year. That is what our order book calls for. This further order booking going on this month where we expect orders to come in from, I guess I cannot have the names until I get the orders, but we expect this month to be good in order booking. The revenue that has been recorded so far in Pennar Enviro is around INR 14 crores for the half year in question with the significant part or almost the entirety of the order book that we have and some orders that they are going to be get, going to be executed and there are also some non-order book businesses, we believe that there will be strong scalability in Pennar Enviro. Last year was about INR 18 crores. We will most definitely be growing at a very high rate over that.

Gaurav Maheshwari: So do we see the margins improving in that business sequentially as well because reaching at least 10% by the end of the year as far as exit quarter is concerned with the operational leverage coming in?

Aditya Rao: So the EBITDA margin in Enviro is all about scale. It completely has to do with scale. The orders we are booking right now are at variable contribution levels of 15% for the Projects business and our Additives business at about 60% and Standard Plants is somewhere in between that. Now as that converts to revenue with the fixed cost having been covered that has an impact on improving EBITDA. So we definitely expect good EBITDA improvement in Environment Treatment business. But to give you an indicator what that margin can be, the order book that we have right now is at an average operating margin of about 15%.

Gaurav Maheshwari: On the total debt side, you mentioned debtors reduced. But if I am not wrong, your total debt was INR 105 odd crores the net debt on March 2014 which has gone up to INR 152 odd crores in Q2. So if you can just correct me on that?

Aditya Rao: Our debt has actually gone down. I think what you would be referring to would be non-cash debt which would be inclusive of LCs. If you look at our cash debt alone, PIL has actually reduced debt by large number. PEBS is actually now storing of a growth in the next two quarters. So there is an increase in that, but that has been done through our internal accruals. We have not increased debt. There has been no cash debt increase in any of the companies. So the total debt utilization will differ based on noncash usage, but we do not have a choice. Now how much cash we have, they have to use LCs. That is the nature of the industry, but we haven't drawn on more debt.

Gaurav Maheshwari: So would you be able to quantify that number in terms of….

Aditya Rao: It was in fact and this could give to our CFO, he will give you the exact numbers of debt.

Krishna Prasad: Whatever is being reported in balance sheet, last year is around INR 105-110 crores. It is the same now also. As on date, there is no further debt than what we have taken during this year. So entire thing is only what we had at the beginning of the year and the same is a carry forward even including our utilization which is fund-based debt. So fund-based debt has not gone anything in excess of what we had at the beginning of this year.

Gaurav Maheshwari: So that is what I am saying. So INR 150 odd crores, would you be able to quantify. What are the fund based and what are non-fund based in March 14?

Krishna Prasad: In this, around a sum of INR 55-60 crores is going to be non-fund based.

Gaurav Maheshwari: And Q2?

Krishna Prasad: Q2 also more or less same is there, the utilization levels because we are not going for any enhancement as such

Aditya Rao: Essentially, Gaurav the debt picture for noncash changes on a day-to-day basis and has everything to do with what LCs are being opened, but if you look at the cash debt picture, we started the quarter at something approaching 70 crores to 80 crores and we are at that same level of utilization. May be little lesser in fact, about 3-4 crores lesser as we are right now.

Gaurav Maheshwari: My last question pertains to our working capital. As a percentage of revenue as compared to March year end, it was 23% which has gone up to 29% which is primarily led by the inventory increase. So is there any PEBS order which is expected to be completed in next quarter and this is one-off inventory increase which will get normalized because QoQ, it remains almost constant.

Aditya Rao: Yes, that is correct. It is actually very good analysis. So we have received a very large order from MRF for their factory which has to be executed by December. This is the INR 62 crores order and we have to suddenly improve our current assets to ensure we supply for this order. Supply has already started. We will complete shipments and complete the project by December. That is one of the strengths of PEBS that it has very quick conversion cycle. You will see the inventory levels go back down after, but I do want to stress that this increase in current assets has been met through our internal accruals and our own cash reserves. We have not increased yet.

Moderator: Thank you. Our next question is from Sanjeev Panda of Sharekhan. Please go ahead.

Sanjeev Panda: I guess part of your commentary you said PEBS, if I understand it correctly, you said you have been selective in bidding or ordering to take order because of the competition environment. If you can throw some light, is there margin pressure that you see or is intensifying competition. How is the scenario?

Aditya Rao: I will try to answer the question the best I can. So when we say PEBS, it itself is a blend of businesses. In the core Pre-engineered Buildings business, if you look at our results for the last 4 years, we have been very disciplined in ensuring that we do not have any margin decrease in that. So when we started off, we are at 20-22% and we are the same level now as well. There have been times we have dipped down to 19%, but we have always found our way back. It is more because of certain orders we are taking from L&T and others, they are excellent customers for us, and so we may have to compromise a bit. But on a regular basis, we do not respond to margin pressure from the market. We are okay with not taking orders, but our order book is right now quite healthy. Our plant is actually full until February now. We cannot even feed the plant if we wanted to and we feel that at this point of time for the Pre-engineered Buildings business, scalability options will exist. We have only tapped into the West and South markets. The North market is even bigger according in our opinion and when we start exploring that market, we have already started looking at growth options. We feel that once we turn into the North market, our addressable market size almost doubles and that will ensure that we can continue to source orders at the margins we want. The other segments are high-rise buildings, engineering services, cold form buildings and solar which we have in PEBS are also is consistent in their margins. There is no true competitor because there is no company which does everything that we do. Pre-engineered buildings or metal buildings only comprise 50% of the sales of PEBS. So in high rise buildings, there is only one or two companies in India I can think of who does what we do and in solar structures, there is only about one or two others and this margin pressure angle is not something we would respond to. The way we think of strategy and growth is we think of geographical expansion. So what we are doing already do it in other geographies such as in North India, such as in other geographies such as Africa and others. What we are not doing, so I guess get into newer products, new services which will allow us to record growth and scale growth there. And the third thing is enter and look at exports, look at new geographies and allow scale to build up which will allow us to improve margins. So going forward, our margin picture will remain consistent. We do not anticipate decreases in EBITDA margins in PEBS. The fluctuations that you see on a quarter-to-quarter basis are there, but if you look at it on an annual basis, you will not see too much movement in terms of margins for PEBS.

Sanjeev Panda: You said part of your commentary, just wanted to get an explanation on that. If I listen it correctly, you said you would not wanting to take order in PEB, did I listen it correctly?

Aditya Rao: I think what I had mentioned was that we have an order book worth INR 350. One of the questions we often get is we have had a INR 300-crore order book about for a very long time, almost a year. So for a company that is growing at 30-40% or more, stability in order book or a static order book may not be looked at as a good thing, but in our case that is something that we see as a positive because we cannot afford to take a lot of orders and go very deep into 6-month, 7-month order books. Steel prices are typically very volatile at this period of the year. So when I mentioned that we are sticking to that order book that was in reference to ensuring that we do not bite up more than we can chew and when we need to have orders, we have gotten very good at getting orders at the margins we need. It was a reference to that. It wasn’t to indicate that we see growth moderating or margin growth moderating in PEBS.

Sanjeev Panda: Another question is toward the Tubes, can you help us to understand the new capacity, the kind of product that you are planning for. How it will frame out, when it will frame out and how much could be margin accretive this new line of CAPEX?

Aditya Rao: Our Tube business is based out of Isnapur. We have capacities in ERW and CDW. The new capacity that has come up is set out to increase the production and output of CDW which is the high margin product, 15-18% margin. The amount of capacity that will come on line and we have done the CAPEX that will come on line in December will allow us to increase CDW revenue by close to 40%-50%, but the overall Tubes division revenue will increase by something approaching 20%. Since this is at higher margin, this will have a disproportionate impact on the bottom line and EBITDA and we will see this coming in Q4. Q3 is we will have more or less in line with, whatever growth we have seen in the last quarter, you will see that continuing, but we will see more growth coming in Q4 when the new capacity comes on line. We are also looking at stainless steel tubes, another very high margin business with 20% plus margins and EBITDA and we think that is an entry we can make now. The Tubes business is now self-sustaining. In fact as I have told you before, we have not drawn a debt to do our CAPEX. Every business division fund its own funds, its own growth. So the Tubes business division has the ability now to make a strong entry into the stainless steel tube business and that will also be a powerful booster of margins. So we expect strong double digit growth this year in tubes and going forward our concentration on higher margin products will result in margin growth, but if you are looking at a target or something, we are expecting from where we are right now which is closer to I think 8%-9%. We will see stronger growth, then that we will obviously see getting into the double digits our goal as soon as possible.

Moderator: Thank you. Our next question is from Vikram Suryavanshi of Phillip Capital. Please go ahead.

Vikram Suryavanshi: One thing you said that you will give explanation for this deferred tax thing that is one. And second, can you just elaborate on what our CAPEX plan and what kind of CAPEX if anything revision or something on that side?

Aditya Rao: So there is a big non-cash component to this quarter's results. If you look at PEBS while EBITDA has grown by 25.8%, the bottom line have not grown. Compared to the quarter, the reason for that is because of the new company law, the depreciation of the company changed in a very significant way and for Pennar Industries standalone also because of the difference between our book depreciation and income tax depreciation, there has been a very big deferred tax liability that has also come in. It is actually equal to PAT, the amount of difference that has come in these things. So that has resulted in EBITDA across both companies growing strongly, but net profit only showing a 9%-10% growth. So that was what I was referring to. I am requesting our CFO to elaborate on that as well.

Krishna Prasad: Earlier, the depreciation was based on fixed rates. Now, the depreciation is changed to the balance period of the life of that particular asset. So now it is coming through period, not therefore the percentage. So there is a change in calculation of depreciation as per Companies Act. But as per IT act, it remains the same. So whatever the depreciation is there between those two, definitely it has to be reflected in a DTL.

Aditya Rao: So the capital expenditure portion, each business division, as I said, runs its own CAPEX plans. Currently, capital expenditure is underway in our Tubes business as I mentioned. Our Railways business for ICF, Pennar Engineered Building Systems and also some incremental maintenance CAPEX for the other business division. The total amount that we have spent in the quarter is quite small. They have committed to spend about close to INR 6-7 crores, being met completely through our internal accruals. For the year in question, it will be slightly higher, but again I stress that this CAPEX will be met through our own internal accruals and we do not have any plans to raise debt as of right now.

Vikram Suryavanshi: So for full year, how much amount we are looking for?

Aditya Rao: Across all companies and all business units, I expect that we would look at about INR 50 crores this year.

Vikram Suryavanshi: INR 50 crores?

Aditya Rao: 50 and every bit of that investment is going into new products which have more than 15% margin.

Moderator: Thank you. Our next question is from Chirag Shah of Edelweiss. Please go ahead.

Chirag Shah: Clarification on this deferred tax. So is it an accumulative impact of past years or how it is and how this number will look going ahead?

Krishna Prasad: The thing is that whatever the past, the impact is being adjusted against the general reserve, free general reserve that is there. So the impact is going to be only for the current financial year and from now onwards whatever life is left for that particular asset.

Chirag Shah: So going ahead, your effective tax rate, deferred as well as current tax that you would be paying. Would from now from third quarter would stabilize at 30-33% levels or it would remain at such a high number.

Krishna Prasad: No, it will stabilize.

Chirag Shah: Second, just on the debt portion, if you can help us understand because if one looks at purely from 31st March to 31st September debt number and the reported stuff which has gone up, but you are highlighting that you have not borrowed incremental money during the first half. So I just missed that particular portion because if I look at your short term borrowing is up by almost INR 30 crores in that sense and even your long-term borrowing is marginally up.

Aditya Rao: Let me give you the picture we have right now of debt and we can go from there.

Chirag Shah: Or if you can also help us understand what is the current level because it is a particular date entry. So how is debt looking currently?

Aditya Rao: So I will start with that. I will give you current levels of debt right now and we can go from there. So on a standalone basis, Pennar Industries has a term rate of about INR 38 crores, mostly for the solar power plant that we had built up in order to get power security. That is the only long-term debt in the group. Pennar Engineered Building Systems has no long-term debt, Enviro has no long-term debt. The CC limits that we have in usage, they fluctuate on a day-to-day basis. As of this morning, our current CC usage is around INR 70 crores.

Chirag Shah: Sir, it has come down from INR 130 crores to INR 70 crores.

Aditya Rao: That is for Pennar Industries standalone.

Chirag Shah: At a consol level?.

Aditya Rao: At a consolidated level, our total CC usage as of right now is about INR 110 crores.

Chirag Shah: So it has come down from that level?

Aditya Rao: It has come down and very significantly come down, I think. So I will look at the number again for what we had reported, but I expect to see nothing other than a decrease in terms of our debt usage. Now there is also a non-cash component - LCs and BGs. Typically, over the course of our business we give BGs for advanced bank guarantees for our projects business where we get some money and even ABG for that and once we have executed a project, we give a PBG for a period of a year which freeze up our cash flow. The reason we do that is pretty simple. BGs actually are a very cheap instrument. It only cost us 1% per year whereas if you look at standard contract definitions of retention money. Since we have taken a CC hit, we would rather have a BG limit. So this reported as debt, but I would encourage you to not to see it as such because if we have a BG, we have the cash for it as well.

Chirag Shah: The part of short-term debt probably and the corresponding cash has not reported as a part of cash, that is how your reporting structure behaves. Is it right?

Aditya Rao: So to clarify your question, our term debt level as of right now is INR 38 crores for a solar power plant and some internal CAPEX we had done and that has not increased. In this year, it has not increased. CC that we use, the short-term capital that we use, cash credit we use is around INR 110 crores approximately, actually a little less and definitely much lesser than what it was at the beginning of the year.

Chirag Shah: So it is largely similar level where it was in the March?

Aditya Rao: I would assume it is actually significantly lower, but I am afraid I do not have the exact number in March.

Chirag Shah: Because as per the balance sheet details you have put out, secured short-term borrowing is INR 106 crores consolidated. So it is largely similar. Fair point.

Moderator: Thank you. Our next question is from Ankush Mahajan of KR Choksey. Please go ahead.

Ankush Mahajan: Sir just wanted to understand this Pre-Engineered Building business. Currently order backlog is INR 350 crores, what is the breakup of that backlog and what is the scope of work in different segments and what is the execution period and how do we see the order inflow growth in this business in the next 2-3 years as the economy takes shape in the uptake in the economy?

Aditya Rao: At this point, it would not be right for me to mention that any future projections of PEBS. I have been advised to be very careful in giving forward statements on PEBS as we are exploring the possibility of an IPO for PEBS. So, I am sure you will understand that I will not be able to give future guidance.

Ankush Mahajan: I mean to say is with the improvement in economy, how the business can take shape, that is just I wanted to know and what is the breakup of INR 350 crores of business in different segment?

Aditya Rao: Okay, that I can provide. So INR 350 crores comprises of about INR 180 crores of metal buildings. It comprises of about INR 40 crores in solar business. PEBS provides engineered module mounting structure. So that business division has an INR 40 crore order book and our high rise buildings and cold form buildings order book which we typically take together is about INR 100 crores. Structural steel is another segment which will have the remainder, but for that we are expecting some orders next month but as of right now we do not have.

Ankush Mahajan: That is the remaining?

Aditya Rao: That is the remaining, yes.

Ankush Mahajan: And what is the execution period for this order backlog?

Aditya Rao: All of our order book is always executable within 6 months. We do not take anything more than 6 months, in fact the vast majority gets executed in three months.

Ankush Mahajan: So, how do we see sir this business, the development in the business with the recovery in the economy.

Aditya Rao: So PEB, the key sectors that its services are construction, infrastructure, process industries such as cement and steel, warehouses, retail, commercial buildings, high rises. It is a very versatile product which can be used for wide variety of end users. Essentially, it can be used as a guidance factor for what is happening in the larger macro economy, but a life blood for the business so far has been industrial buildings. That is changing very slowly. With whatever is being happening in the market, we are quite bullish for further growth. It is definitely better than it was has been in a long time. So as the tide lifts up, we want to be ready with increased capacity to scale up further. So we are very bullish in for PEBS and we are also looking internationally. The export business of the company across multiple business units in fact has grown quite significantly in this quarter and will increase in the third quarter as well. We also believe that lot of opportunities for PEBS in other geographies.

Ankush Mahajan: So in 350 crores of order backlog, what is the export order backlog?

Aditya Rao: I will actually not be able to give that number. We do not actually report that number but it is a small number, it is not very high.

Ankush Mahajan: Sir, can we take a ballpark number if the economy will grow by one time so this business will grow by two times.

Aditya Rao: Over the last four years, we have typically grown at an average CAGR of twice the market growth rate. The market growth rate is completely contingent on what we call non-residential construction. So that typically grows at 2 or 3x the GDP growth rate. So you have 15%-16% growth over the last few years in this business and there is also regular demand transfer from regular construction to this form of construction because of the more modern methods of construction. So that adds another 3-4%. So the market growth rate is about 20% and if you would, maybe we can take this conversation offline also. We also have market surveys that they have conducted with a company called Feedback Ventures, a very good infrastructure advisory firm. We can give you good lead points on how the market has evolved, but as I said future we will not be able to talk too much about it.

Ankush Mahajan: Last one is that we are seeing about INR 50 crores of CAPEX. Could you give me a breakup of how much for the Tubes, how much for PEBS and how much for the steel product and industrial component?

Aditya Rao: Yes, absolutely. So out of the INR 50 crores, Railways will be about INR 10 crores, Tubes business will be about INR 6 crores, our ICD business which I did not mention is about INR 3 crores, PEBS will have about INR 20 crores and the remaining is maintenance CAPEX which is used across a wide variety of businesses in our plants.

Ankush Mahajan: And what kind of CAPEX we are looking in FY15 and FY16, next-to-next year?

Aditya Rao: I will remove PEBS from that. PIL will continue to have a steady state CAPEX of about INR 30 crores and Environment business will not require CAPEX. It is a technology company, Pennar Enviro. So its capital expenditure is more in the realm of IP generation, technical tie-ups, and technical collaborations. We have tie-ups with Total of France, we also have an exclusive tie-up with a Veolia group company, and also UK based company where we have an exclusive tie-up with Tech Universal which is a very old, very successful water treatment company. So that will be me more CAPEX in PIL, but you will not see that number across a few crores.

Ankush Mahajan: So on this 50 crores of CAPEX, we are looking of 20% of sales growth in consolidated basis?

Aditya Rao: We will definitely beat that. This is not guidance, but we expect more than that. This quarter itself we have grown at more than that.

Moderator: Thank you. Our next question is from Rahul Kohli of IndiaNivesh. Please go ahead.

Rahul Kohli: Sir, my question was regarding the gross margin of the company like if I see the consolidated results, the YoY gross margin has come down even on quarterly basis and for the first H1FY15. So why is that the gross margin has come down?

Aditya Rao: When you talk of gross margin, I will talk of contribution. Contribution for the company compared to last year to this year if you were to look at an overall picture, I do not actually see a huge decrease in terms of margin. EBITDA was you seeing a marginal decrease in standalone but a growth in consolidated basis. So if you could just verify the number that you are exactly looking at?

Rahul Kohli: Like consolidated number if I see, H1FY15, the net sales has grown by 15% and the material cost has gone up by 21%. I am taking material cost I am talking inventory also into the inventory change and the actual material consumed?

Aditya Rao: Raw material cost, is it? Is that what you are asking?

Rahul Kohli: Yes.

Aditya Rao: So the raw material cost having gone up is actually, it also has to do with the way we record consumption. We also have two kinds of inventories. Steel inventory and non-steel inventory and for Enviro, it comprises of a lot of what we call other than raw materials, bought out items as such. So anytime the businesses are gearing up for growth, you will see an increase in raw material. So the way accounting standards called for, the moment we removed it from stores it is consumed. So it will sit as current inventory in our books, but valued at cost but you will not see the sales in fact. So you would have seen a raw material increase on that basis, but even then we do not have a massive increase in raw material. Can you comment on this also?

Management: Compared to Q2, the raw material consumption is around 63% and now it is at roughly around 66% that is somewhat 2-3% is only the increase with the change in inventory. It is depending on what is the mix of products what we are going to sell and also what is changing inventory we are going to carry, but the impact is no so big as such.

Rahul Kohli: And sir in the EBITDA margin level, what are your expectations segment wise, like long term what you are targeting EBITDA margin?

Aditya Rao: We expect continual EBITDA growth because of topline growth. As the topline continues to grow, we will expect to see what we call the variable contribution dropped directly down to EBITDA. So we have expectations that EBITDA will grow for PIL Group Companies. PEBS, I will not be able to give you much thing on that.

Rahul Kohli: Company used to have higher EBITDA margin in 11 and 12 in double-digit also.

Aditya Rao: Yes, EBITDA margin growth in this financial year compared to last year yes, we expect growth.

Rahul Kohli: So, your target is to reach double digit in EBITDA margin, at least in standalone.

Aditya Rao: Absolutely.

Rahul Kohli: I am asking is like double digit margin you used to…

Aditya Rao: Yes, go ahead. Also, let me just say this. All the new orders we are getting, all the revenue growth that is coming in the businesses, we are growing the business divisions that are growing are all high margin businesses and we define high margins are anything over 15% operating margin. So as we scale that up, that 15% operating margin drops down to your EBITDA, leading to EBITDA growth. That is the fundamental plan behind our EBITDA growth and EBITDA margin growth. We think that so focusing on higher margin businesses will result in growth. We have seen this bottomed out and we think this will continue.

Moderator: Thank you. Our next question is from Vishal Sharda of Athena Investments. Please go ahead.

Tushar: Aditya, my question is your overall margins are 8.5% EBITDA margin and you keep referring to operating margin. So what is the meaning of operating margin?

Aditya Rao: Good question. I think I should have a better job of explaining that. So EBITDA, we are concerned is an output of first year sales minus your RM costs from what we call spread, from that we remove other variable costs such as bought out consumables, labor, electricity, water all of that and we have it a number called contribution. Now after contribution, they just add fix cost which is salaries of management people, rent-related administration, and all of that. So typically, when we evaluate whether a business is good or bad or when we look at growth in a business, the number we look at is the variable contribution what we call operating margin, the word we use.

The reason we do that is sustainability of growth of a business has to be looked at completely on the basis of the operating margin. Anything else that responds to growing sales is not a fixed cost, it is a variable cost. So our fixed cost has now been totally compensated for and our EBITDA margin of 8.4% comes after you remove the fixed cost from a 14%-15% variable margin. Now as we grow and as we add revenue, you are adding it at (+14%) – (+15%). So that number, additional revenue. We had 100 crores in revenue at 15% margin, then 15 crores should drop to EBITDA. So very small increase in revenue can result in massive increase in margin if you focus on variable operating margin and that is what we do. Does that explain the question?

Tushar: Yes, I understand the concept of that. But if I look at your number, you have raw material cost which is approximately 66%, employees are 6% and other expenses are probably 16-17%. So this other expenses have fixed and variable component and the employees you treat it as fixed or as variables because this will also include your planned employees right, specific. I am not talking of the head office management. So there will be lot of workers and other people.

Aditya Rao: Yes, so other expenses are variable expenses. The salaries that we have, the labor cost, the factory worker labor is a variable expense, we net it out. Management salaries are fixed.

Tushar: So you are saying you have 15% operating margin and around 7% fixed cost.

Aditya Rao: Yes.

Tushar: That is how you arrive at 8% EBITDA.

Aditya Rao: I think I would put that as 6% fixed cost, but yes.

Tushar: 6% fixed cost and that is how you arrive at EBITDA of 8%.

Aditya Rao: That is correct.

Tushar: Now, what is the plan to increase this EBITDA from 8% to say in the range of 12%-15%? We in the market understand EBITDA or gross margin because we have to analyze based on information that you disclose. So what is available to us is really sales and raw material cost and we do not really know the breakup between variable and fixed cost.

Aditya Rao: I know and I think it is fair to treat on the basis of EBITDA. EBITDA growth in the future will come from what I will call our variable contribution percentage sustaining at the level on even growing at where it is. Any additional revenue coming in should fall down to EBITDA, thus leading to revenue EBITDA growth.

Tushar: Now from what you are saying, I do not think the margins would increase very much from this 8% level, may be it will go to 9%, but from whatever you described if you are targeting 15% margin at operating level less 6% fixed cost, then you are probably talking of 9% kind of margin.

Aditya Rao: 6% will not increase. 6% will come down right. Let us say that you increasing revenue by 30%, then your fixed cost also comes down by 30%. The 6% comes down to 4.5.

Tushar: Okay, so what is your target for say FY15 and FY16 in terms of margins?

Aditya Rao: I will not be able to give guidance. But as a previous gentleman had asked, our target is to reach double digit EBITDA margin very soon.

Tushar: Okay, because if I look at your PEBS business which is fairly well established which has size and scale, there also you are doing 8% EBITDA. You are not doing really very high EBITDA, in spite of high growth.

Aditya Rao: It is about 9% this quarter. What typically happens is the Q3 and Q4 numbers of PEBS are scale up a lot more. So every year what happens is we go through a period of some fixed cost increase, we do want to incentivize our people to do more. So that typically kicks in at the beginning of the year, but by the time the end of the year comes through, Q3 and Q4 we actually see EBITDA margins which are much higher. I am not again giving guidance and saying our Q3 and Q4 of this year will be much higher, I am saying that is what has happened in the previous years and if you look at the year overall, then you will see us touching double digit and in fact growing along with scale.

Tushar: And one more question. What is your turnover guidance for the whole year? I read somewhere you have guided around 40% growth and first half is only 15%.

Aditya Rao: Yes. I will not be able to give guidance for the whole year. I think what I will definitely be able to say is for next few quarters continuing, we will continue to see strong double digit growth. We do not see that declining. Exact guidance for the year, I do not know where the 40% number came from, but that is not something that we would have provided.

Tushar: I think it is one of the analyst reports which must have come from the management. So what would be your turnover this year, will you do…?

Aditya Rao: Again, I really will not be able to give you a number but I am very confident of strong growth.

Aditya Rao: We will revert back to you on that particular aspect sir.

Moderator: Thank you. The next question is from Harshad Gujrathi of Athena Invest. Please go ahead.

Harshad Gujrathi: Can you just give the average ticket size of the order book which is in the PEBS segment and the Enviro segment?

Aditya Rao: Since that is the past, I can. The average ticket as in the average order size, is that what you mean?

Harshad Gujrathi: If you bid for any order, so what is the average ticket size you generally look it out when you are going for any orders?

Aditya Rao: There is a minimum order size of about INR 3 crores which we have, that changes per the year. When we first started, it was INR 1 crore, now it is INR 3 crores. But the average order size that we get is typically around INR 7-8 crores.

Harshad Gujrathi: That is for the PEBS and for the Enviro segment?

Aditya Rao: Enviro segment, it is actually substantially similar. It is about INR 5 crores.

Harshad Gujrathi: So here you try to maintain your 15%-18% of operating margin where you can easily catch that,

Aditya Rao: So, how I would put it is, we have a contribution target internally to the company. That is what we used to measure. It is the best measure according to us. We have a contribution target on PEBS of 20% and about 15% for projects for Enviro which would be the most relevant number right now because of the scale and by the time those fall to EBITDA, they should be (+10%) because of differences in inventory, consumption, stocks and that you can have some differences but overall we do not aim to be less than 10%.

Harshad Gujrathi: But this 20% PEBS will get increased further in going ahead in terms of well bidding to the orders or this will remain the same?

Aditya Rao: I would like to say a lot about that, but I cannot. I will not be able to give you PEBS guidance.

Harshad Gujrathi: Also one more thing we would like to ask on the PEBS that who is one of the competitors in terms of listed and unlisted companies which are similarly doing same kind of business, which we are in Pre-Engineering business.

Aditya Rao: I think the closest thing that comes to our competitors, but they only compete with about 40-50% of what we do which is industrial large scale buildings. They are not present in cold formed buildings, they are not present in solar, they are not present in high rise buildings, they are not present in green silos or telecom towers and others. I guess there is no listed entity or unlisted entity which would do everything that we are doing. I think the closest thing you can look at is the combination of companies. For our Metal Building business, you can compare us with Kirby.

For our High-Rise Towers business, you can compare us with JSW, Severfield they are not listed. For our Engineering Services business, you can compare us with any ITES company.

Harshad Gujrathi: Okay, as far as if I ask about the total market size of a PEBS where we stand in terms of the depth of the market if he can show on this, any idea on this front?

Aditya Rao: So could you say that. The market share is what you are talking about.

Harshad Gujrathi: No, I am talking about as far as total market size of the Pre-Engineering Building segment.

Aditya Rao: So the market size for PEBS currently is about INR 6000 crores. So it is about billion US dollars growing at about 14% year-on-year.

Harshad Gujrathi: Sir also would like to know that since we are planning to come out an IPO on PEBS segment, so is there any target for the same. Have you decided or….

Aditya Rao: I really would not be able to say anything about that.

Moderator: Thank you. Our next question is from Jagdish Bhanushali from Florintree Advisors. Please go ahead.

Jagdish Bhanushali: One thing, earlier you mentioned that we execute PEBS orders within 6 months of timeline.

Aditya Rao: Yes.

Jagdish Bhanushali: So right now we have stand an order book of about 350 odd crores in PEBS. So is it fair to assume that the coming quarters we will have a revenue of at least 160-160 crores from PEBS business?

Aditya Rao: Again, that would be a kind of giving guidance which I will not be able to do. I can tell you that you can look at, if you have a previous quarter number, one interesting exercise would be look at what happened in Q1, Q2, Q3, Q4 in the previous years, you have the full year history and because there are public companies that is reported information, but you can see what our growth has been and typically over the previous years, Q3 and Q4 tend to be very big quarters. Q4 tends to be a much large quarter than….

Jagdish Bhanushali: Another question comes as because we have been having orders of about 300 crores since three quarters, so if we are able to execute in 6 months, I think our PEBS business should report revenues of about INR 150 odd crores at least?

Aditya Rao: INR 150 crores for what, for Q3 is what you are asking?

Jagdish Bhanushali: That is what for Q3 or even for Q2 because in Q1, we had order book of about INR 280 odd crores or INR 300 crores.

Aditya Rao: Yes.

Jagdish Bhanushali: So basically if we are able to execute in 6 months, our revenue reporting should be about INR 150 odd crores from the PEBS business right?

Aditya Rao: Again, I will. Let me answer this way. As I said, vast majority of order book gets executed in a 6-month period. So if your question, you are starting the year with INR 280 crores, so you should do in 6months. Yes, ideal situation yes, but there is a little bit of a difference to that. During the monsoon, not too many orders get executed. In fact construction industry as a whole usually tanks during the second quarter. So that has to be priced in. So if you remove that, then I would qualify what I said before by saying 80-85% should translate over. So an order book if you want to look at the order book we have resulting in what will convert into turnover, I think that much should typically converts in 6 months time. But again I am not saying that our revenue for the next two months is going to be the number yet to be mentioned INR 150 crores.

Jagdish Bhanushali: Alright, now because if the Q2 has a weak performance due to rain that means INR 90 crores gross is what we have executed. So then definitely it would be fair to assume that you will be clocking about at least INR 150-160 crores in the coming two quarters now.

Aditya Rao: I have very strict instructions from our board to not say anything about PEBS. So you want to get me into trouble. But I am very confident that PEBS is going to do well. That is what all I can say. We have a good strong order book right now. We have a record of proper execution and it is a debt free company which is well-poised for growth that much I can say.

Jagdish Bhanushali: Okay, another thing is one year back we had a private equity buying a stake at about INR 50 odd crores. That means they had valued the company at about INR 200 crores PEBS business.

Aditya Rao: That is correct.

Jagdish Bhanushali: Okay, because in the previous con-call somewhere I read it was about INR 230 crores of valuation is what they had counted for.

Aditya Rao: Well, it depends on pre money and post money. It is a little over 200. It is in between the two numbers that you mentioned - INR 210 crores.

Moderator: Thank you. The next question is from Anand Bhawnani. He is an individual investor. Please go ahead.

Anand Bhawnani: I have a pretty basic question. In most of our businesses, you mentioned order book is executed within 6 months. So could you please explain us how do we mitigate the risk of not being able to bag sufficient orders when a slowdown happens. So how do we ensure that we consistently have ability to acquire order even in downturns?

Aditya Rao: When we expect a certain percentage of order book to convert, certain percentage to get delayed, a very small percentage also gets cancelled. It is very small like 2-3% on over the last four years we have seen of our total order book tends to get cancelled as well. Across multiple business verticals where we have order book such as Railways, Solar, PEBS and Pennar Enviro, typically the metric we use is, do we have enough revenue for the next three months four months. If we are able to have enough what we call clearances, then we are in a good place. If we are not, then there is an immediate feedback, look that goes into our business development saying we need to book more sales. So typically what happens is we tend to have our order books reach their maximum level at the end of the year and over the course of the next couple of quarters, they do tend to either come down or moderate a bit. Not all business divisions would see this. But overall you would see this is the picture. Then we spent Q3 and Q4 again scaling up for the next financial year. So we have not yet run into a position because they are all growth companies. Pennar Enviro has been growing at 200%. Our PEBS has grown at 44% CAGR for the last four years. Our Railways business has grown at 100% this year. So far, more than that I think, 200%. So, we do not typically have this problem, but going forward as we continue along the growth curve ensuring that we have revenue to feed to our plants, will essentially consists of a 2-3 month plan. We do not think more than that. We honestly do not think more than 3-6 months.

Anand Bhawnani: Just to make sure I have got you correct. We try to get orders at a 3 months short of time horizon and how much time does it take for us once we decide that we need more orders, what are the typical period it requires us to bring in orders?

Aditya Rao: So we have an enquiry bank for all of these businesses with the exception of Railways. It is one customer or in case of wagons, where we have limited set of customers but the other business divisions do maintain a steady enquiry bank. So the amount of time it takes us to close and to quickly put more pressure on our sales to go is actually quite short. I would say, a short as a month reaction time. One thing we will not do is for example lot of times taking orders means comprising on margins. That we will not do. We are okay with lower turnover, but we would not compromise on margins.

Anand Bhawnani: No, because as an investor I look at more of return on equity. So whether you do at a low margin with a high asset turnover or low asset turnover with a high margin, assets we are indifferent. What we focus more on is how much at the equity level the company can earn? So can you explain to us why exactly has chosen a higher margin. Why we focus more on margin and not on the ROE itself?

Aditya Rao: We focus on a blend of numbers; we focus on return on equity not so much, balance sheet size is about 400 crores. We do not focus on return on equity. What we do focus on is return on capital employed and margins and cash flow. Those are the two or three boundary conditions that we have. So our line between whether we have taken order or not taken order goes through several approval process. One of the process that finance looks at and again marketing looks at and engineering looks at is any order that we take should be in line with the expected margins and expected something is defined over a period of so many years of experience and we look at how the order cash flow is like. So if we gave us a 50% margin order but you will pay a year from now, return on equity will look great. Your EBITDA margin will look great. But your cash flow looks bad and we will not take that order. Whether we can finance it or not, it depends. So we will just not take that order. The reason for this is pretty simple. We believe in quick cash flow businesses. We have brought in good double digit growth without increasing debt at all and we are going to continue doing that. We will not be increasing debt and the only reason we have done this is because of complete focus on cash flows. So the most important thing for us is cash flows. The next in line comes return on capital employed where different divisions have different ROCEs. We go all the way from 40% ROCE for some businesses to less than that for our steel products business. So our focus will be on maintaining and growing ROCE and making sure the cash flows of the companies stay intact. Typically, both of those things being okay, means results in higher EBITDA margins as well.

Anand Bhawnani: Okay, and my second question was more macro oriented. This Made in India theme that is being pushed by government of India, do you see our company in anyway getting impacted positively by developments on ground?

Aditya Rao: I think so because every major sector that you can see, infrastructure, construction, environment, pollution control, water treatment, all of those are end use customers for us, automotive, general engineering. They continue to be sectors we have strong presence in. We have a general move up in Indian infrastructure, Indian automotive, Indian construction, Indian engineering, will have to affect us quite frankly.

Anand Bhawnani: Let me be a bit more specific. Have we seen an increase in the enquiries, has our enquiry book gone deeper because of the current…

Aditya Rao: Our enquiry bank has definitely gone up. Absolutely, yes.

Moderator: Thank you. We will take the last question from Chirag Shah of Edelweiss. Please go ahead.

Chirag Shah: Just trying to understand two things about your business. So the return on capital employed is what you focus on you highlighted. Can you just share us across businesses, what are the broad, you may not specify each, but what is the bottom in, what is the kind of ROCE business beyond which you will not look.

Aditya Rao: So, last year was especially bad for the company. That is something that we are very cognizant of, but ever since I started looking into operations from the beginning of this financial year, the ROCE target we have set this year is going to be quite high. We want to be (+20%). PEBS has been (+30%) and has not come down below. That we do not anticipate a problem with the ROCE being defined as either on EBITDA or PAT I do not think we will see a problem there. Enviro is a growth business, so we think it will take time for it to mature to the point it is, but even for Enviro because the capital employed is so small I mean its cost us INR 4-5 crores to put the business up frankly and it will have revenue multiple times that and it should have good EBITDA margins by the end of the year. So even Enviro, we will not have a big challenge, it is showing good ROCE, but the target below which we have less than 20% we will not look at it any more.

Chirag Shah: And is there a scope of improving the working capital cycle in the business or not really the nature of business is such….

Aditya Rao: I believe there is. I think we are currently at 2.5-month working capital cycle. Our goal is to get it to 2-month working capital cycle.

Chirag Shah: But would it be driven by your business mix in that sense or is the business mix also a factor of higher or lower working capital cycle or generally for each business you are targeting to bring it down. So how should we understand that?

Aditya Rao: Yes, each business has its own. Tubes for example, it is 3 months, PEBS is less than 2 months, Eniviro is 1 month. So, each business has its own working capital cycle. The broad base is 2 months for the entire company that I mentioned is based on a blend of businesses. It is what we believe should ideally be achievable and we will be glad to share this with you to give you why we think too much on important number. But essentially let us say that we are at revenue run rate of about say 1400-1500-1600 crores, then we expect the one-sixth of that as the working capital. I think the question around we think 6x your working capital usage should be end up with.

Chirag Shah: And coming back to that debt question, apologies for repeating that. I am still not able to understand that your cash based debt because your bank guarantees and CC limit, etc., would be a part of your contingent liability right? So, is that your working capital has gone up slightly because you did highlight that some of the businesses you are required to execute and that is why your debt has gone up in the system?

Aditya Rao: The contingent liability is part of BG, yes. LCs and BGs are common limit, so it is hard to delineate it. **Chirag Shah**: So the balance sheet debt has gone up, just wanted to understand that. Is it more of a working capital funding intermittent that you are highlighting that some businesses which are ready to execution.

Aditya Rao: I think there has been an increase in LC usage because we are gearing up our growth in some of our businesses.

Chirag Shah: But that would not be part of your reported debt, right? That would be a contingent liability.

Aditya Rao: It would be part of our reported debt.

Moderator: Thank you. Our next question is from Riken Gopani of Infina Finance. Please go ahead.

Riken Gopani: Sir just two things that I wanted to understand. One is on the railway side of the business. Who would be our largest customer there and I am just trying to understand may be you have answered it previously, but just I am trying to understand is that why would there be so high volatility in terms of margins in that business, if you could help me understand that.

Aditya Rao: The largest customer we have in railways is ICF, the Integral Coach Factory where we will have over INR 100 crores of revenue. May be one of the larger customers of Pennar Industries, we have good margin in that business too. To answer your question why this marginal volatility, it has a lot to do with the revenue breakup. Now Railways when we speak of that as a thing, we also have wagons and coaches both and also if you look at Systems & Projects business unit as such, solar also gets included in that. So wagons had a significantly lower margin than coaches. So any time you see wagons and coaches revenue there that being disproportionate, you will see margins swings and there can be tremendous margin swings. We hope to moderate this somehow by improving our margin on wagons.

Chirag Shah: And is there some seasonality to the deliveries between quarters on wagons and coachers or are the growth rates any different from each other if you could highlight that.

Aditya Rao: What has happened is actually if you do not count the last quarter, there have actually been no wagon orders for 18 months. There was a big lull. That is something that has picked up now where we have received multiple orders now and also there is another tender opening up in December which also we intend to be part of. So there is no seasonality per se that I can define, but what we would expect is there seems to be a general trend where both coaches and wagon production seems to be on the way up compared to the last two quarters, last two years also. So consequently, we believe that both revenues should go up. We are scaling ICF revenue and wagon revenue right now and it will be burst….as and when the orders come in, they will be executed over the next few months as such.

Chirag Shah: Okay and sir out of your various segments that you report, could you highlight which of these businesses you would carry any raw material volatility risks?

Aditya Rao: I think pretty much all of them do except for Pennar Enviro. The core raw material that we use is various grades of steel. Steel is a very volatile raw commodity which can go up or down, swings are 16% per year and not uncommon. Over the past few years, we have seen a lot of stability in steel prices. So for PEBS, steel price was 50%, for Pennar Industries is close to 70%, so obviously it is a big driver of cost for us. But because of the relationship we have with major raw material vendors JSW and others, we found ways through the quarterly rate contracts, through pass-throughs to ensure that we do not suffer inadvertently to this. In fact in Pennar Industries, the gap between a steel price increase and ability to pass it through is very short. It can be measured in weeks.

Chirag Shah: Any which way it is given that you would be having short cycle orders 3-6 months is the max duration for the most of your divisions. So you can hedge it as well. I mean, do you do anything on that or you would just enter into a contract immediately once you get the order?

Aditya Rao: So that is a very good question. So for where we do not have rate contracts or we do not have tonnage contracts, so all the previous orders for example are lump-sum contracts. So the moment we book an order, we book the raw material so to speak which does not mean we buy it but we enter into an agreement to buy the raw material. Which is another reason why we cannot have an order book which crosses more than 6-7 months. The raw material price goes up, then if you have booked raw material, if it goes down then you are in trouble.

Chirag Shah: And one last point, as you mentioned that your target should be to look at any new business at or any incremental revenue at (+20%) in terms of ROCE. As of now of your segments, which are the segments which are sub-par in terms of your performance as compared to the target.

Aditya Rao: Largely Steel Products business which comprises of our cold rolled steel stripes and cold rolled formed sections that is the legacy business of the company that is at under par ROCE and par EBITDA. Our goal is to move into specialized products in those businesses. So we will have, so that we can see some growth in those businesses and sustainable margins. But what you are seeing across all other business divisions which is near double digit growth. You are not going to see more than double digit growth across in all verticals. You will not see that happening in Steel Products. Our plan is not to grow that business. We will require a lot of CAPEX, a lot of spending, we would have to fundamentally rewire at whatever we are as a company to grow those businesses.

Moderator: Thank you. Our next question is from Jagdish Bhanushali from Florintree Advisors.

Jagdish Bhanushali: Could you give me the contribution margin breakup in each of the PEBS segment verticals that PEBS, Solar?

Aditya Rao: The core metal buildings business is about 22% contribution, higher also some times, but an average of 22% contribution. For the structural steel business, it is closer to 18 to 19%. Solar is the worst coming in at 12% and cold form and others is at close to 25-30%. It varies a lot depending on orders, 70% contribution, and EBITDA because fixed cost is already covered.

Moderator: Thank you. Ladies and gentlemen that was the last question. I now hand the floor back to the management for closing comments.

Aditya Rao: Thank you for your questions. We endeavor to give you a good picture of the ocmpany. I have taken note of the comments you have had. There seems to be some clarity we need to provide on the debt picture. We will provide this through our investor relations team. Also, I apologize for not being able to give you some of the information on PEBS, but as the potential listing is being considered by the board right now, we are unable to give you those numbers. I do want to conclude by giving you a picture that we are a growth company with very efficient use of capital. We believe that we are going to continue to see good strong double-digit growth going forward. We have been able to scale up across all measurable metrics and I am confident of further improving the performance of the company in the coming quarters.

Moderator: Thank you very much sir. Ladies and gentlemen on behalf of Pennar Industries Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.

(this document has been edited for readability purposes)