"Tube Investments of India Limited Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to the Q1 FY'14 results conference call of Tube Investments, hosted by Axis Capital Limited. As a reminder for the duration of the conference all participants' line will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference call, you may signal an operator by pressing "*" and then "0" on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Kashyap Pujara of Axis Capital. Thank you and over to you Sir.

Kashyap Pujara: Good afternoon friends. It is a pleasure to have with us the management of Tube Investments. The management is represented by Mr. L. Ramkumar, Managing Director and we do have with us the new incoming CFO, Mr. Arjun and we do also have with us Mr. Balasubramanian who now is going to be superannuating, going forward, without taking too much time, I will handover the floor to you Sir. Over to you Mr. Ramkumar.

L. Ramkumar: Thank you Kashyap. Good afternoon to all of you and thank you for taking time off to attend this conference call. Tube Investments of India standalone, we ended with revenue of 826 Crores for the first quarter 2013-2014, which even though 4% more than the last quarter of last year was 10% low compared to the previous year. In the case of consolidated, we ended up with 2065 Crores as against 1793 Crores for the same quarter last year which is a growth of 16% over the previous year, slightly below the fourth quarter of 2012-2013. Now coming to the individual division, in the case of bicycles, we have seen the volume at around 10 lakhs which is 6.6% below the last year, however we had a good order load I must say. We could have actually grown marginally. We had to align our supply chain. We did see an improvement in the demand compared to the last two quarters of the previous year, which meant it took a little time for the supply chain to get aligned with the variety and the number of models which were available, so we are correcting the situation as we go into the second quarter. This has resulted in the turnover coming down from the previous year same quarter by 8% while we did grow over the last quarter of the previous year by 10%. We did improve our EBITDA and our PBIT in this business substantially from Q4 and still below the last year because of the volume we could have some pricing power during the quarter. We did increase the bicycle prices by Rs.35 progressively during the quarter. We are seeing the new models we have launched have been well accepted.

Going to the engineering division, as far as the numbers are concerned of volume, the strips was just 2% low than the previous year same quarter and the tubes were 5.5%, 6% less than the previous year in the domestic market. This is despite the slowdown in the automotive segment in two-wheeler, four-wheeler and trucks as well. Overall tubes we were down by 5% including exports, exports were roughly around the same level as the previous year. Here the accent has been on improving efficiencies, internal efficiencies in terms of yields, in terms of power cost and the throughput, this has helped us to somewhat maintain the profitability compared to the previous year and previous quarter of the last year. So you would see here the turnover has come down from the previous year slightly by 7% to the growth of 3% over the last quarter of the last year and the profit from operations has been below last year by 10%, but around the same level as the previous quarter in the year 2012-2013. Going forward in the case of metal forming, we have had reasonably good performance in the chain sector. We have had a growth in the auto chains as well as in the after market. We have had growth in the fine blanking segment, the exports have not grown, we have seen a slowdown from the second half of last year. There has been some pickup, but still it is much below last year. The major drop has been in the case of door frames. While we did have good business with Hyundai, which grew compared to the same quarter last year, the overall door frame numbers dropped by 12% and there has also been significant drop in the railway products which has dropped in volume terms by 70%. In the case of metal forming division we must know that railways have not been releasing orders for wagons, we are executing the orders of the previous year. They are yet to release orders for the current year, which is expected next month or so. Overall, we have also tried to control the working capital. The net working capital turned for the quarter compared to the same quarter last year has improved by two points from 10 to 12 and we have also managed our long term debt equity well in the sense of over the year end it was around 0.83, the debt to equity has come down to 0.78. We are pursuing our new project of the large diameter project at Tiruttani. The construction is on. We have ordered all the equipment, expected to get commission for trial production sometime in March. It is as per our revise schedule. In the case of automotive sector we have has some new LOI from Mahindra, from Hyundai for door frames. Our efforts are on to improve the new products in the tubular component section as well as in the fine blanking division. We have also commissioned our transfer press for making motor casings in the TI Metal Forming Division, which is required as an import substitution as well as to upgrade the current product range of the various automotive makers. By and large, this is summary of where we are today and we would be very happy to take any questions.

Moderator: Thank you very much Sir. Participants we will begin the question and answer session.We have our first question from the line of Mr. Prashant Shah from First Consultant. Please go ahead.

Prashant Shah: Thanks for the opportunity. Firstly, on your insurance business, Sir I want to know if you could provide some clarity on as to what valuation have we invested in Chola General Insurance?

L. Ramkumar: Around 270 Crores.

Prashant Shah: Sir I just wanted to understand the rationale behind this investment because it is basically a financial services industry whereas we are a kind of manufacturing, so how would this marriage work out, the merits and demerits?

L. Ramkumar: This marriage has happened many years back. Actually Tube Investments has been the promotor for the financial services businesses, Chola Finance and Chola Insurance. Chola Insurance is now 11 years old and when we had surplus cash and we also thought we need to diversify indeed from only the manufacturing sector. This is the idea with which we started it and I am glad to say that it is doing well and during the quarter they ended up with good growth over the same quarter previous year in terms of net earned premium going up by 56% and also the operating PBT going up by 86%.

Prashant Shah: From the investment perspective, I wanted to understand how much had the last capital infusion done at in General Insurance business?

L. Ramkumar: You mean in terms the value we put in?

Prashant Shah: Yes.

L. Ramkumar: During the last financial year, we did 34 Crores.

Prashant Shah: At what price sir per share?

L. Ramkumar: Rs.70.

Prashant Shah: Going to Shanthi Gears how are current integration plans and our growth plan for the next two years?

L. Ramkumar: I think it is going quite well. You must have seen the standalone results which we had published also. We have done a lot of work to clean up and streamline the operations there. We have fairly new senior management team in the last six months. We have also put in lot of systems and procedures. We have had an excellent response from the customers after we took over, we met all the key customers in cement, steel, and other segments which are key for the gears and gearboxes. Our order load is good. We are aligning our production as you know the capacities are not fully utilized even when we took over. We will be slowly increasing the capacity utilization and we would see going forward the numbers reflecting the growth in the business.

Prashant Shah: Any guidance on the utilization level Sir?

L. Ramkumar: It will be better is what I can say, from what it is.

Prashant Shah: Sir, can you please guide on the FY'14 and FY'15 capex numbers?

L. Ramkumar: We are in 2013-2014, I think I would rather wait, given the current situation, we have something, but I think everything is changing daily, morning, evening, so much of difference, we normally make our plan by say January, February for the next year, but right now I think we would like to complete our projects which we started, but in terms of regular capex will be there, but new capex I think we will have to really think hard.

Moderator: Thank you. The next question is from the line of S. Chellappa from Pari Washington. Please go ahead.

S. Chellappa: Could you tell me there is any capital expenditure required in Shanthi Gears?

L. Ramkumar: Nothing very significant, it is very marginal capital expenditure to spruce up things, but nothing very worth mentioning actually, may be a couple of Crores or something at the moment.

Moderator: Thank you. The next question is from the line of Nilesh Dhamnaskar from Religare Invesco. Please go ahead.

Nilesh Dhamnaskar: Sir, could you tell us the capacity utilization levels of your metal form division, engineering division and some sense on the capacity utilization at Shanthi Gears?

L. Ramkumar: Shanthi Gears may be around 50%. In the metal forming division, the door frames we make investments depending on the volume given by the car makers, so the utilizations will be very low in products related to TATA. We have a plant in Pune for Indica and in Sanand for Nano. The utilization may be 30% to 40% and we have a plant in Uttarakhand for railways, which is virtually we can say 10% to 15% average because we have not been getting orders. In the case of engineering division I think strips business our capacity utilization will be 75%. In the tubes business we will be very close to 85% to 90% actually.

Nilesh Dhamnaskar: As you are seeing the quarterly EBIT both consolidated and standalone so in terms of the metal form division the consolidated EBIT is lower than the standalone, so does it mean that the differential is largely explained by Sedis , has it made PBIT loss over there?

L. Ramkumar: There is no loss there, the metal form products are being 0.71 and 12.97 this is what you are referring to.

Nilesh Dhamnaskar: Though the amount is not that big, but it has been on the profit. It used to be a positive number in the earlier quarter.

L. Ramkumar: PBIT level, there has been a small loss due to foreign subsidiary.

Nilesh Dhamnaskar: How are things shaping up over there?

L. Ramkumar: They are largely Europe centric and that to France centric, the growth has not been good in the market, what we are trying to do now is, we are trying to get manufacturing of components done here in India, which will reduce the cost and do the assembly there and then address the market with some price advantage. This will happen in the second half of this financial year. As this program picks up I think we will get some benefits of working together plus we are also trying to attack some new markets with TIDC products and Sedis brand name, like US and some European countries.

Nilesh Dhamnaskar: My last question pertains to your CapEx though you have not finalized or frozen your capex for next year, but at least in this year segment wise capex though and plants remain underutilized, but anything which you will still continue?

L. Ramkumar: Broadly our new capex will pertain to the new project we are setting up in the tube area, it is largely an import substitution project, pertaining to the off-highway vehicles etc., not necessarily to the automotive sector to which we are catering, we are targeting something like 330 Crores of capex of the current year of which bulk of it will go for this large diameter project and there could be some capex for bicycle division it is around 50 Crores more to balance and also improve the capacities. I was mentioning earlier that we need to streamline our supply chain, even our variety if you want to quick deliveries in bicycles we need to keep a little more capacity is what we believe, so we will put up some capacity there and then some investments on the new LOIs we have received from Hyundai, M&M etc., 30-35 Crores, balance capex will be all regular capex.

Nilesh Dhamnaskar: So, a large chunk of the CapEx is going to come in the engineering segment?

L. Ramkumar: Engineering that will be around 150 Crores, balance some we have already spent last year on land and other things.

Nilesh Dhamnaskar: My last question pertains to your Shanthi Gears division, now the way we see it you have acquired stake in the company and through funding from your own sources, basically I was wondering the entire amount has been taken on debt and is it going to stay it that way or going to load up some debt on Shanthi Gears own books also because that is a completely unleveraged balance sheet with some amount of cash also, so what are your thoughts on these leverage part?

L. Ramkumar: If at all we need to restructure our funding structure it will be in TI standalone and we are not looking anything in Shanthi Gears. We bought Shanthi Gears with a combination of own generated funds and debt.

Nilesh Dhamnaskar: How much of debt within your books is associated to Shanthi Gears acquisition?

L. Ramkumar: Very difficult to say that, we can talk about the total debt which was for capex, Shanthi Gears and a couple of other things also.

Moderator: Thank you Sir. The next question is from the line of Ravi Purohit from Securities Investments. Please go ahead.

Ravi Purohit: I got two questions, one is on the railways business, you mentioned that there have been lack of orders for wagons from the railways and you mentioned that you expect them to come in the next month, but is there something that has been communicated by the railways or the clients because it has been in the limbo for very, very long time now, so if you could just throw some light on what are you hearing is it from the customer, or is it just expectation of the market that it will probably come next month or something of that sort, or have there been concrete indication from the railways?

L. Ramkumar: It is the latter; this is an expectation, there is no official communications in this.

Ravi Purohit: Second one is on Shanthi Gears, I think you had mentioned that we are expecting significant scale up this year, but in terms of given the current environment that we have how easy or difficult will that scale up be, because since you have taken over I think you had mentioned in your last call that there has been some cost rationalization, some one time hits that we had taken, now is all of those over and now it is just waiting for the market to pickup or if you could just throw some more light on how things are shaping up there?

L. Ramkumar: It is a good question, in particular sense all the rationalization etc., is over we do not have any major things to be done now, I meant good scale up, significant we will wait and see given the market condition, you answered the question in your own question itself saying it is easy or difficult, I think it is in today's condition is not going to be easy, but we have found that some of the customers whom we were not serving were missing us, so they may come back to us either they were importing or they go into sources which we are not happy with so to that extent we will have some growth despite the market condition.

Ravi Purohit: Secondly, may be initial days of our acquisition we had mentioned or may be our group chairman had mentioned about there could be some stuff that we can do which is complementary to tubes business likes sprockets and all or there could be additional new products that we might be working on or even exports could be an opportunity, so is there something, because I did not find many of these mentioned in the recent annual reports that Shanthi Gears released, so I was just wondering if those things still hold or those are still the opportunity that we are looking at?

L. Ramkumar: Sprockets is something which we will have to sell along with the industrial chains, we have already started the work on that, we have done some trial production, we will have to see how we make that and they will do it and give it to TI Diamond Chains. In the case of exports, yes I think there has been good inquires for Shanthi Gears and they are doing some exports now to US and some to Europe, but I think going forward there are many gearbox manufacturers themselves are looking to outsource from countries like India, probably they will buy some parts of the gearbox like gears or casings and then make the gearbox. We are talking to various people and this is also quite promising I must say.

Moderator: Thank you. We have the next question from the line of Vikas Garg from L&T Mutual Fund. Please go ahead.

Vikas Garg: Just a couple of questions, first is your requirement of funding for those capital guzzlers like the NBFC operations for this financial year 2014 and also to the insurance business?

L. Ramkumar: We may have some marginal investment for the insurance business. For the NBFC business, we are not planning any investment from TI at the moment.

Vikas Garg: I am just coming from the fact that Chola NBFC has been going at steady rate of 35% or maybe even higher, and they are already setting at a Tier I of around 10.5% which means they have to support some kind of growth to be supported by the equity infusion, so are we looking for some stake dilution in that front as to support?

L. Ramkumar: I think the capital adequacy ratio is around 18% now and probably they are well covered for the current financial year.

Vikas Garg: Secondly on the total debt number, I missed the number, I am not sure if you gave the number, what is the total debt that is sitting on the standalone book as of now?

L. Ramkumar: Standalone book total debt is 1280 Crores.

Vikas Garg: This also includes the working capital loans that you have?

L. Ramkumar: Everything long term and short term.

Vikas Garg: Any guidance on the peak number which could be possible let us say by March and financial year 2014 and or 2015 on the debt number?

L. Ramkumar: I wish I could do this, it is very tough.

Vikas Garg: Out of this 1300 odd Crores how much would be the kind of working capital loan as of now Sir?

L. Ramkumar: Around 350 Crores.

Vikas Garg: Do you see any pressures on this number going up given that we have seen the working capital intensifying for many of the companies?

L. Ramkumar: We are saying so far our working capital management has been good, we have been improving the turns of sales to networking capitals by tight control of inventory and better collections, it may not happen due to working capital and we may have some borrowings to meet the capital expenditure apart from whatever we generate as profits, we need some gaps to be bridged.

Vikas Garg: One last question, which is like more so on the broader perspective, if I want to just look at the balance sheet strength of the company for the past many years the going has been well below 1 and so last year because of the acquisition and all it has gone a bit marginally above 1, so any guidance or any thought process like what kind of level would you be comfortable with going forward sir?

L. Ramkumar: What you are saying is right, we have been well below 1. You are talking about total debt equity or long term debt equity?

Vikas Garg: I look at total debt equity including working capital?

L. Ramkumar: We don't have any guidance, I think we are really looking at as the need arises I would think up to 1.5 is fine and long term debt equity of up to 1 is fine, but we would like to keep it to the minimum and see if we can conserve more by getting more cash flow from operations.

Moderator: Thank you. The next question is from the line of Mr. Paras Nagda from Enam Holding. Please go ahead.

Paras Nagda: Thank you for the opportunity. Sir I joined a bit late, I wanted to know if you mentioned the motor pool account losses and how is that shaping up Sir?

L. Ramkumar: I think we have provided some more in this quarter. We have provided 13.73 Crores P&L of the insurance company for the quarter and after the motor pool charge the profit before tax is at 30.7 Crores.

Moderator: Thank you. Kashyap you may go ahead with your question.

Kashyap Pujara: Just as an extension of the last question asked, basically which imply that we are already at a PBT run rate of 44 to 45 Crores on the insurance front, so what is the balance amount of losses that need to be provided now?

L. Ramkumar: Another 40 Crores.

Kashyap Pujara: So that would be provided for in this year itself?

L. Ramkumar: Yes, correct.

Kashyap Pujara: So basically apart from our own generation of third party pool I think from next year onwards the profits from the insurance division will really be reflective of the actual potential.

L. Ramkumar: Yes.

Kashyap Pujara: Can you just also throw some light in terms of what is the kind of price hike, because I think general insurance per se there have been 20 to 20% price hike which have happened over the past couple of years on more than two occasions, are we seeing any move to de-tariffing in the near term or there going to be further price hike before we go for de-tariffing?

L. Ramkumar: We have been on the hearing of pressure on the pricing, but we will get back to you on this specific question with correct data what happened in the last two years.

Kashyap Pujara: Could you also throw some light on the recent Tsubamex tie up that we have done and what is really the plan in terms of exports or local, what is the kind of capacity we are looking at, if you could give some more light on that?

L. Ramkumar: Tsubamex is the dye maker for the body and white parts sheet metal which is used in the body building of the car. They are a reputed manufacturer in Japan supplying to various tier I manufacturers and the car manufacturers, they have been in business for I think more than 40 years. Most of these, I heard 80 to 85% of the tools and dyes are imported into India, all the makers here, be it the Japanese companies or local companies, either they import from Japan, Korea or elsewhere, so there is a need for import substitution, this will also give them deliveries locally. The broad idea is this, that there is a market for this, that there is a technology involved in this in terms of design and precision tooling, so what we have done by this joint venture is we have set up company which will be like a design house, we will have to start with some 12 employees who already we have recruited three, we are getting another four people, they are getting trained in Japan in design areas, in software of this company, with this we will approach the customers here and we will be at the first level be able to translate this in terms of design, initially we will use the Japanese facility of Tsubamex for catering to this, during the next 12 to 18 months, we will assess the Indian market about the kind of investment required locally to make these tools and dyes, the quantum and the timing of this after which we will commence the manufacturing of dyes, to start with it will be interaction with customers design and also servicing of tools if that is required, so the customer feels that there is somebody to look after this in India. We will also have couple of Japanese closely working with us when we meet the customer or when we have to setup the design facility here in India.

Kashyap Pujara: Initially what would be the total capital commitment?

L. Ramkumar: Is in 5 Crores.

Kashyap Pujara: So it is negligible basically?

L. Ramkumar: It depends on who is looking at it.

Kashyap Pujara: One more point regarding the overall state of the economy that we are in what is the kind of growth that you are envisaging on the automotive front for the full year, when you are working on expansion plans or basically setting your own assets as well what are the growth estimates that you are building in, in terms of automotive growth for the full year?

L. Ramkumar: We are not very bullish about this, we are looking at growth in our products largely through a market share gain, the growth could be I do not know 2 or 3% whatever max, in two wheelers also come down, passenger cars, trucks also, we are looking at various methods where we may be giving new products or we can get the higher share of business, so we will be targeting some single digit growth in our product volumes, overall we are not very hopeful that it will be significant. We will be very happy if it does not come down.

Kashyap Pujara: Just lastly, margins in cycle really came back as expected hopefully going forward most of the one time related write off have been done with, so these margins should really be sustainable right?

L. Ramkumar: Definitely we do not have anymore of one time and none of that has been reckoned in Q1 now. So I think what we are looking for is even probably as I said we did lose some volumes because of supply constraints which you should separate now and hopefully things will be on this note or even better than what we have reported.

Moderator: We have a next question from the line of Taral Shah from Kitara Capital. Please go ahead.

Taral Shah: Can we maintain the volumes in engineering segment or not this year compared to last year?

L. Ramkumar: We are hoping we will maintain the volumes.

Taral Shah: Whether we can maintain the price or not we have to sell our product with some discount or something like that because of the slowdown?

L. Ramkumar: We may not sell at a discount, but we may have trouble if the input cost go up too much, they are talking about the steel price increase now, so far we have not had anything in the first quarter, then the recovery takes time, we may lose one or two months or we may get part of the increase so there could be some issue there otherwise we are not going for any discounting of any products.

Moderator: Thank you. Kashyap you may proceed with your questions.

Kashyap Pujara: Couple of followup questions. One is related to the overall power situation in Tamil Nadu, I think in the first quarter due to the wind generation I think there would be some amount of receding in overall power cost, but what is the current situation that you are looking at going forward and do you think that the availability is slated to improve in the second half overall?

L. Ramkumar: The expectation is going forward this year should be better than last year, because we have been informed about many of the power plants which are getting refurbished and they will start becoming more productive, then we also looking at the nuclear energy coming in some portion of that into Tamil Nadu, so the total supply side the expectations have been increased over the previous year.

Kashyap Pujara: So hopefully our power cost to sales progressively should taper off at least it should not move forward going from here.

L. Ramkumar: Yes.

Kashyap Pujara: One more aspect which I just wanted to get clarity on was related to your large diameter tube facility that is likely to be commissioned probably in the fourth quarter or the first quarter of next year and this is largely an import substitution product, so hopefully get the client traction and generate the relevant volumes would that be much of an issue would you have to go through the concept testing and the entire trial phase or all those things have been done with and you can really start shipping out the product and you achieve optimum utilizations in FY’15?

L. Ramkumar: For the same sector up to a particular diameter which is well within our range now we are supplying but this will be a smaller portion of the total requirement for this application. The large diameter tubing will be done here, there is some level of approval process, it is not the first day itself you start selling, but we have already studied how long it takes and where we can do it during the commissioning stage and all that our endeavor is going to be to cut short this process in less than three months, so that the approval process is through and then we start manufacturing for the sales.

Kashyap Pujara: Is it fair to assume that the new capacity that would come up would at least be utilized to the extent of 50% to 60% for the first year.

L. Ramkumar: Correct, you are right.

Kashyap Pujara: Just overall one more point was related to the expansion of the bicycle facility that would be coming up in the North East region? Correct me if I am wrong?

L. Ramkumar: We may do couple of things, one is we may do some marginal investment in existing plants in Nashik or elsewhere, it is a marginal investment, we can improve some capacity, second may be a new plant somewhere in the north because you already have a plant in Noida which is catering to the North and East, so we may want to supplement the capacity there for which we may have to setup in the northern part of the country, which will be more efficient.

Moderator: Kashyap would you like to make any closing comments here.

Kashyap Pujara: Thank you so much to everyone and including the management of Tube Investments for taking time out to participate in this call. Thank you so much.

L. Ramkumar: Thank you Kashyap and everybody.

Moderator: Thank you Sir. On behalf of Axis Capital Limited that concludes this conference. Thank you for joining us. You may now disconnect your lines.