



“Minda Corporation Q1 FY 2016 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to Minda Corporation's Q1 FY2016 earnings conference call hosted by Edelweiss Securities Limited. Joining us on this call today are Mr. D. C. Sharma, Group CFO; Mr. Ajay Sancheti, Head, Group Corporate Finance & Legal and Mr. Vinod Bapna, Head Group Finance Controller. As a reminder, all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Siddhartha Bera from Edelweiss. Thank you and over to you Mr. Bera.

Siddhartha Bera: Thanks Melissa. Good afternoon everybody and a warm welcome to all the participants. We, at Edelweiss Securities, are very pleased to host the Q1 FY2016 earnings conference call of Minda Corporation. I would hand over the call to Mr. D. C. Sharma for his opening remarks post which we will have the Q&A session. Thank you and over to you Sir.

D. C. Sharma: Welcome ladies and gentlemen and thank you for joining the Q1 FY2016 earnings conference call of Minda Corporation. We hope you have had a chance to go through the earnings presentation and financial results which are also available on the Company's website.

I would start with an industry overview followed by key financial and operational highlights. Thereafter, we will open the call for an interactive question and answer session.

Automobile markets globally are witnessing a phase of slow recovery. During the quarter gone by, the Indian automobiles registered a growth of 1.6% y-o-y with the bulk of the growth attributable to the strong performance of medium commercial vehicles (MCV). The two wheeler segment remained sluggish and grew by 0.2% during the quarter. Overseas markets have showed more encouraging trends led by strong sales growth in the European passenger vehicles and the commercial vehicle segments. Various economic reforms undertaken by the Government of India are expected to bear fruit in the remaining part of the financial year which will help in improving consumer sentiments.

With this backdrop of slow recovery, I am pleased to announce another strong quarter for Minda Corporation. Total revenue for the company increased by

15.2% y-o-y to Rs. 5,281 million. The growth in topline can be attributed to delivery of new products in 'Wiring Harness', 'Die Casting' and 'After Market' segments. Domestic business continued its robust performance growing by 26% y-o-y.

EBITDA increased by 13.8% over same quarter of the previous year. Ongoing cost control measures and operational improvements helped in maintaining the margins and the overall business expanded. We also delivered a robust 16.5% year on year growth in PAT. This increase was driven by lower finance charges and fixed cost rationalization.

Continuous focus on value creation and superior client relationships have helped in generating incremental free cash flows, which in turn helped in reducing our net debt from Rs. 401 Crores at the end of previous quarter to Rs. 369 Crores at the end of this quarter. As a result, the debt-equity ratio has also gone down from 0.86x at the end of previous quarter to 0.75x at the end of this quarter.

We are also delighted to report an upward revision of one notch in our credit rating by the rating agency CRISIL to A/Stable for long term debt and A1 for short term debt. This is reflective of our strong financial position and prudent business management.

Our strategic geographic footprint and diversified product mix make us a global player in the automobile industry. Over the past few months, our strong relationships with auto OEMs have been strengthened as we have received a number of awards in various categories by global OEMs such as Kawasaki, Suzuki, Mahindra & Mahindra and Yamaha.

Going forward, we plan to leverage our strengths to further improve our international presence. To this end, we have formed a dedicated and experienced team of professionals to evaluate additional growth opportunities arising in both our existing and potential export markets.

This is all from my side. Now I would like to open up the floor for an interactive question and answer session.

Moderator:

Ladies and gentlemen we will now begin with the question & answer session. We have the first question from the line of Puneet Gulati from HSBC. Please go

ahead.

Puneet Gulati: Sir, can you give some more color on the growth in the wiring harness segment. Are you adding more customers or products? Also, can you elaborate on any additional market share you are getting?

D. C. Sharma: In the wiring harness segment, our sales have increased by about 33%, from Rs. 156 Crore in same quarter of the previous year to Rs. 208 Crores in this quarter. This increase is mainly in one of our JVs 'Minda Furukawa Electricals' where we have increased our SOB with MUL and started one new product with Nissan. Our other company 'Minda SAI' deals with non-Japanese customers where they have shown only marginal growth. There is growth in 'Minda Furukawa' where we supply the wiring harness to the passenger vehicle segment.

Puneet Gulati: Which one did you say was the first customer?

D. C. Sharma: There are mainly three customers in Minda Furukawa - Maruti Suzuki, Nissan and Honda.

Puneet Gulati: Secondly, how do you see the interior business for the Company?

D. C. Sharma: Our car interior system business is largely concentrated in Germany, with only marginal business in India which we started last year. In India, we are supplying one model to Maruti Suzuki and total sales is about Rs. 20 Crores

While in Europe, we have a total business of about Rs. 400 Crores in Europe spread mainly in Germany, Poland and Czech Republic. During the quarter, the interior business remained largely flat, growing by just 3%.

Puneet Gulati: Who are your main customers in Germany?

D. C. Sharma: In Germany, we supply to major OEMs like Volkswagen, Audi, BMW and Daimler

Moderator: We have the next question from the line of Sanjay Satpathy from Merrill Lynch. Please go ahead.

Sanjay Satpathy: Firstly, what kind of margin you have in various segments like wiring harness and plastics? Secondly, what are your future plans of growth in case of wiring harness and other divisions, i.e. new customer acquisition etc.?

D. C. Sharma: Our EBITDA margin at consolidated level is about 9.5%. In Rupee terms, our

EBITDA margins increased by about 38.8% compared to the corresponding quarter of the previous year. Overall, margin in security systems is higher at about 12%, while margins in wiring harness are slightly lower at around 9%. In car interior system, it is about 10%. We have relatively lower EBITDA margins in wiring harness but there is strong growth and we are in the process of improving the margins. We have outlined a detailed plan and are taking action as per the plan. Hopefully, our margins in wiring harness will improve to the levels of other segments in the coming quarters.

Sanjay Satpathy: Considering that you have just entered into Maruti, what kind of market share you have? Is it going to see some sharp changes from now on?

D. C. Sharma: In Maruti, our current share of business is around 16% and this is expected to increase. We have certain commitments with Maruti to reach a particular level of SOB during the next two years. So we are working on that plan and we already have a couple of new products. Once these new products start, our SOB will be increased.

Sanjay Satpathy: Understood. Sir, lastly if you can just tell us whether you are getting these orders on the back of pricing or it is more because of the product that you offer through Furukawa?

D. C. Sharma: When we start a new product, the margins are definitely in a tight situation because there is more imported content in our materials but we have a localization plan in place. When we start the localization, over the next six months to one year, the margins are expected improve gradually. As far as pricing is concerned, there is no impact of the pricing on our margins because we have back to back arrangements for major raw materials. For forex risk, since previous quarter rates for raw materials and the foreign currency are applied for deciding the price for the next quarter, there is no price impact in as it is fully hedged.

Sanjay Satpathy: Lastly can you just tell us what the level of your localization in wiring harness and various other segments is right now?

D. C. Sharma: See, right now we are looking for localization of about 6% to 7% over the next one-and-a-half years. There are a couple of new products and we have our own internal component shop; the JV partner has designed the drawings and know-how; there has to be localization. Localization will help in reduction of

import duty and forwarding cost.

Sanjay Satpathy: Correct. Sorry I couldn't get the level of localization right now, is it 6% to 7% you said?

D. C. Sharma: Yes, 6% to 7% in the new product. At the beginning, we always target 6% -7% localization.

Sanjay Satpathy: Understood. Sir, though the number looks very small, your jobs looks like it is more restricted towards assembly at this point of time. Is it the right conclusion to make?

D. C. Sharma: Can you repeat your last sentence? I could not hear properly.

Sanjay Satpathy: You were saying that it is only 6% to 7% localization so what it means is that, virtually you are getting everything imported and only assembling it here?

D. C. Sharma: No, it differs from product to product. For example, in security systems, we do complete manufacturing: We have a die casting shop, plastic moulding shop, engineering department and assembly department. So, over there, it is complete manufacturing. In case of wiring harness, we have a component shop, where we do our own manufacturing of certain components additionally. We also import certain other components. To complete the process of manufacturing, there is an assembly shop. When we decide the price the customers, we look for the average contribution over a period of three to four years. And for the average contribution, we plan the amount of localization and cost saving we will do over the period of time. So, we don't do only the assembly here. We have other departments like the production engineering department which constantly work towards improvement in margins. It is based on the product.

Moderator: Mr. Bera, would you like to continue with the questions while we wait for participants?

Siddhartha Bera: Yes sure. I had a couple of questions. First is about the expected growth across various companies like Minda SAI, Furukawa and after markets for this quarter. If you can throw some light on this?

D. C. Sharma: Okay, I will share the growth in terms of products; performance of one or two companies is not as important as the growth of the product itself. In case of security systems, there has been a growth of 15% from Rs. 152 Crores in June

2014 to Rs. 175 Crores in June 2015. In case of wiring harness, as I have already mentioned, the sales increased from Rs. 156 Crores to Rs. 208 Crores, representing a growth of 33%. The car interior system remained sluggish with a de-growth of (8)% which is due to an adverse effect of a change in the forex rate; the Euro rate was Rs. 69/Euro at the end of June 2015 which was Rs 79/Euro in June 2014. The decline in the Rupee rate was 11% and our growth rate was about 3%, resulting in an overall de-growth of (8)%. In the after-market segment, our sales have increased from Rs. 36 Crores to Rs. 45 Crores, translating to a growth of about 26% y-o-y. In the ASEAN region, we achieved sales of about Rs. 150 Crores last year. With the new Government, the Indonesian economy is going through a depression and we estimate that this may impact our sales by about 28% or 29% over the year. For example, last year we had about Rs. 50 Crores and this year, it may be about Rs. 100-105 Crores. During the month of July and also August, the demand from customers is usually good and we feel that the sales will improve in the ASEAN region. Our target will be more than 15%. In the ASEAN region last year, we had sales of about Rs. 37 Crores and in this quarter the sale is Rs. 30 Crores. It means that in the ASEAN region we are down by about 19% and overall we have done sales of about Rs. 528 Crores against Rs. 458 Crores last year; so there is growth of over 16% overall.

Siddhartha Bera: Sir, you highlighted that there was a 15% revenue growth in the security system segment. Do these numbers include the security system business from VAST also?

D. C. Sharma: Absolutely right. This includes both the two wheeler and four wheeler segments.

Siddhartha Bera: Does this include the entire 100% or only 50%?

D. C. Sharma: Only 50%. We have considered Minda Vast joint venture for four wheeler products and we have considered only 50% of the sale.

Siddhartha Bera: Okay. And for Furukawa also it will be like 51%?

D. C. Sharma: Yes, we have considered only 51% but in the case of Minda Furukawa, we own 51%, which makes it a subsidiary company and we are the holding company. So consolidation in the topline is for 100% along with complete consolidation of all the expenditures. Only the minority interest is reduced at the profit level.

Siddhartha Bera: The RM costs have inched up sequentially both in the standalone and

consolidated businesses, while we are hearing about commodity costs coming down for most of the OEMs. Is it not getting reflected here? Is it that we are not receiving any price hikes or they are yet to come?

D. C. Sharma: At the consolidated level, our raw material cost is higher by about 2% - 2.5% during this quarter which is mainly because of the high raw material cost in the wiring harness business. As there was a growth of 33% in the wiring harness business, the product was impacted leading to a slight increase in raw material cost. Secondly, we target a 2% reduction in cost every year which in this case has been delayed slightly; the benefits are expected to accrue in the second or third quarter. By the end of second quarter or beginning of third quarter, our material costs will come down by some amount.

Siddhartha Bera: Sir, for the standalone business, which we believe is purely locks, the raw material cost have increased by 50 bps to 62% in the current quarter as compared to 61.7% in the last quarters. Can you please explain this increase?

D. C. Sharma: There is a special reason for this slight increase in RM cost. In June 2014, the raw material cost was 60.1%. For the quarter, RM cost was 63.4% as against 62.9% in the same quarter of previous year. This 50 bps increase in RM cost is partially because of the product mix and partially because of delay in the cost reduction project.

Siddhartha Bera: So should we expect some benefit going ahead if the price reduction comes through?

D. C. Sharma: Yes. Also, if you see some other areas such as 'Other Expenditure', there is a good reduction. This is owing to reduction in costs related to manufacturing expenses, and 'power and fuel'. Additionally, finance costs have also come down. Secondly, in terms of product mix, the material costs are slightly higher in case of two wheelers. For example, in HMSI, wherein we are working to reduce the costs, the material costs are slightly higher. Some benefits from cost reduction plan are likely to come in during the second and the third quarter.

Siddhartha Bera: Sir, finally, I understand that the company was in the process of getting some new business from OEMs like Hero. Can you please share the status on that and when we can expect revenues to come through in the P&L?

D. C. Sharma: For Hero Motors, we have already started doing business in the wiring harness

segment in this quarter.

Siddhartha Bera: Okay, and sir, what is the status in case of locks?

D. C. Sharma: In the locks segment, we got an order for three new bike models from Hero Motor Corporation but the development will freeze only by November. We expect to start the supply in the last quarter of this year.

Siddhartha Bera: Sir, I understand that we were also planning to supply to the new Honda plant?

D. C. Sharma: We have already been supplying to HMSI where we have a share of about 17% of their business and this is gradually increasing. We have already got some business for their new plant in Gujarat; and in the north, we are seeing good increase in SOB from the Manesar plant, where one model is about to be launched.

Siddhartha Bera: Can we understand if the delay from the OEM side in launching new models is creating a delay on your side also?

D. C. Sharma: Yes. In case of Minda SAI, wherein we have been supplying wiring harness to Mahindra & Mahindra and Tata Motors. There is a delay in the launch of two models because of which Minda SAI's sales this quarter are lower at about Rs. 113 Crores as compared to last year's sales of about Rs. 119 Crores. Our sales here have been lower because of Mahindra & Mahindra and Tata Motors but at the same time, we are expecting a sizeable increase in business for Ashok Leyland. In fact, there is good growth in Minda SAI's Chennai plant which supplies mainly to HMSI and Ashok Leyland. But overall, sales are lower because of delay in projects.

Siddhartha Bera: Okay. Sir, will the company be supplying products for the new model of Mahindra compact SUV that is planned to be launched in September?

D. C. Sharma: Yes.

Siddhartha Bera: And for S-Cross, Have we started supplies for it?

Company speaker: Yes, we have started with the supply of products for the S-Cross.

D. C. Sharma: Though there has been some delay in the launch of S-Cross but as you know, there is a big market available for S-Cross and this is Maruti's dream project wherein they are pushing very hard. They are going to open new showrooms for

the S-Cross and have dedicated teams for selling the S-Cross, so we are expecting that there will be good growth. We expect good amount of business from the S-Cross model of cars.

Company speaker: And this is a good time to supply to Maruti as we are supplying the products for Alto, DZire, Swift, Celerio and S-Cross. These five models of Maruti are practically the first case right now.

Moderator: We have the next question from the line of Bhavesh Jain from Envision Capital. Please go ahead.

Bhavesh Jain: Sir how much capex are we expecting for FY2016?

D. C. Sharma: Capex for the full year FY2016 would be about Rs. 50-58 Crores.

Bhavesh Jain: And how much will be the maintenance capex out of this?

D. C. Sharma: We were operating at about 70% capacity last year and have already done a capex of about Rs. 55 Crores to build up the capacity by opening a new plant in the wiring harness business. We have good capacity in the security systems. For the maintenance capex, we don't target more than one third of our PBT so within this range our maintenance capex would be about Rs. 48 Crores.

Bhavesh Jain: Okay. And what would the debt repayment be for this year?

D. C. Sharma: Debt repayment was approximately Rs. 42 Crores. Our net debt which was about Rs. 401 Crores as on March 2015 has now been reduced to Rs. 369 Crores as on June 2015. This is because of availability of surplus cash and the repayment of loans.

Bhavesh Jain: And Sir, how much top line growth are we expecting for this full financial year?

D. C. Sharma: For the full financial year, we are expecting a growth of about 20%.

Bhavesh Jain: And what will drive this 20% growth- new products or the existing products?

D. C. Sharma: Both new products and SOB in case of the wiring harness business. But in case of security systems, we have a couple of new products which will be started this year.

Bhavesh Jain: Sir, somewhere you have mentioned that you are rationalizing the product

portfolio by stopping the manufacturing of non-profitable products and closing down units where the margins are below comfort level.

D. C. Sharma: Absolutely right, this was the story till 2014-2015.

Bhavesh Jain: So that exercise has been completed?

D. C. Sharma: That exercise is already over. For example, someone asked the question on the higher material cost in the standalone business this year. Last year, we had some business of electroplating and the plastic business which were not profitable. We decided to close these businesses; June 2014 was the last quarter of the closing process. Now all loss making businesses have already been closed down.

Bhavesh Jain: Okay. And Sir, you said that you are targeting operating margins of around 10.8-10.9% but for FY2015 we ended at 9.4%?

D. C. Sharma: Our consolidated EBITDA margins in this quarter were 9.5%, in fact last year also the margins were about the same at 9.4% or 9.5% for the full year 2014-2015. This year, we are expecting to increase that by at least 1.5%.

Bhavesh Jain: Sir, what will be your asset turnover if you do a Rs. 40-50 Crores capex? How much revenues we can generate?

D. C. Sharma: On an average, we have an asset turnover ratio of about 4.5 times but in case of wiring harness this is much better because there is low application and in case of security systems also it is higher.

Bhavesh Jain: And what will be our sales of control cable for this particular quarter?

D. C. Sharma: We started control cables only last year. It is a new product; earlier we had the strategy of starting first with OEM and then onto the after-market. But last year, we adopted the reverse strategy. We started with a couple of key products in the after-market and then once these products are established and we are satisfied with the products, we will take it with the OEMs. This year our target for control cables is of about Rs. 30 Crores.

Bhavesh Jain: Rs. 30 Crores versus Rs. 26 Crores in FY2015 I guess?

D. C. Sharma: In FY2015, it was about Rs. 20 Crores only. Now, this year, we are expecting more than Rs. 30 Crores. We have shifted our manufacturing rates of the control

cable because of the margins and capacity expansion which will take about two to three months.

Bhavesh Jain: Sir at Rs. 30 Crores, we will be break even?

D. C. Sharma: Yeah, it is already break even. In fact, we have some marginal profits in this and we are in process of localization for two wheelers and four wheelers. We are starting with little manufacturing and then gradually we will increase manufacturing and localize many other areas of the cable. This year we will be operating at about 40%-45% of capacity and next year we are look forward to a good increase in control cable.

Bhavesh Jain: Sir how much we have invested for this?

D. C. Sharma: About Rs. 14 Crores.

Bhavesh Jain: And you said we will be operating at 40%-45% this year?

D. C. Sharma: Yes.

Bhavesh Jain: So that means we can generate around Rs. 65-70 Crores?

D. C. Sharma: We expect about Rs. 55-60 Crores.

Moderator: As there are no further questions I would like to hand the floor back to the management for closing comments. Please go ahead.

D. C. Sharma: Great. Thank you very much.

Moderator: Thank you. Ladies and gentlemen, on behalf of Edelweiss Securities Limited that concludes this conference call, thank you for joining us and you may now disconnect your line. Thank you.

Note: This transcript has been edited to improve readability

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