"Lloyd Electric & Engineering LimitedQ3 FY'17 Earnings Conference Call"

February 10, 2017

MANAGEMENT: **MR. NIPUN SINGHAL – CEO (CONSUMER DURABLE), LLOYD ELECTRIC & ENGINEERING LIMITED**
MS. ANITAKAKAR – VP (FINANCE) & COMPANY SECRETARY, LLOYD ELECTRIC & ENGINEERING LIMITED
MR. FILIP EISENREICH – CEO (OVERSEAS SUBSIDIARIES), LLOYD ELECTRIC & ENGINEERING LIMITED

MODERATOR: **MR. SALIL UTAGI – EDELWEISS SECURITIES**

Moderator: Good dayladies and gentlemen and welcome to the Q3 FY'17 Earnings Conference Call of Lloyd Electric & Engineering Limited hosted by Edelweiss. As a remainder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Salil Utagiof Edelweiss. Thank you and over to you sir.

Salil Utagi: Thank you. Good morning everyone. Lloyd Electric & Engineering Management is with us, represented by Mr. Nipun Singhal – CEO of Consumer Durable, Ms. AnitaKakar – VP (Finance) & Company Secretary and Mr. Filip Eisenreich – CEO (Overseas subsidiaries). Now I handover the call to Ms. Anita Kakar for her opening remarks. Over to you Anita.

Anita Kakar: Thank you Salil. A very good morning to all of you. On behalf of the management of Lloyd Electric & Engineering Limited I welcome you all to the quarter three FY'17 concall. I will take you through the financial highlight for the quarter and nine months under review and thereafter Mr. Nipun Singhal and Mr. Filip who would provide a quick overview of the businesses during the quarter and we will be open for the question and answer session. We will try to answer all the queries to the extent possible. In case any question remains unanswered due to time constraints we would get back to you soon.

Despite the temporary disruption caused by the recent demonetization drive which has impacted various sectors during the temporary cash crunch. The company delivered better performance during the quarter ended December 2016 with standalone revenue registering an impressive growth of 19% to 529 crores over the corresponding quarter of the previous year. This was primarily as a result of the proactive steps undertaken by the company to tackle with the currency crunch faced by the consumers and Lloyd was one of the frontrunners for having launched the cashless happiness which was zero down payment scheme with first EMI Holiday. This has led to consumer durable segment reporting a remarkable growth of 43% in revenue over the corresponding quarter of the previous year. The growth was also coupled with continued investment in brand promotional activities supplemented by delivering best in class after sales service which has resulted in Lloyd maintaining its market share of around 14% in the Indian Room AC market ranking among top 3 players.

I will now take you through the key financial highlights for the quarter ended December 2016. Due to the impressive performance of the consumer durable segment, the total standalone income from operation for Q3 FY'17 stood at 531.75 crores as compared to 443.77 crores in the corresponding quarter last year representing a growth of 20%. The operating profit excluding the non-operating income for the quarter was higher by 16% at 44.55 crores as compared to 38 crores in the corresponding quarter last year. During the quarter, other non-operating income stood at 0.31 crores as against 0.24 crores during the corresponding quarter of the previous year. The finance cost during the quarter under review was 28 crores as against 27.92 crores during the corresponding quarter of the previous year. The profit before tax grew multifold to 8.62 crores to 2.35 crores during the corresponding quarter of last year. The total comprehensive income after tax stood at 6.43 crores as against 2.52 crores in the corresponding quarter of the previous year registering an impressive growth. The basic EPS for the quarter stood at Rs. 1.59 as against 0.71 during the corresponding quarter of the previous year.

The financial highlights for the nine months ended December 31st, 2016. For the nine months ended December 31st, 2016 the company reported a total operating income of 1,938 crores as against 1,548 crores in corresponding period of the previous year registering a growth of 25%. The operating profit for nine months ended December 16 stood at 186.62 crores as compared to 153.80 crores in the corresponding period of the previous year representing a growth of 21%. For the nine months ended December 2016 the non-operating income stood at 1.01 crores as against 0.58 crores during the corresponding period of the previous year which is mainly on account of the interest and the dividend income on the investments.

For the nine months ended December 2016, the finance cost stood at 80.20 crores as against 73.20 crores during the corresponding period of the previous year. The profit before tax grew by 41% to 83 crores as compared to 59 crores during the corresponding period of the previous year. The total comprehensive income after tax for the nine months ended December'16 stood at 62 crores as compared to 46 crores in the corresponding period of the previous year registering a growth of 36%. The EPF for 9 months ended December '16 stood at 15.61 as against 13.25 during the corresponding period of the last year. I will provide you the highlights for the segment performance. The consumer durable segment, the revenue from this segment during the quarter stood at 306.14 crores as against 213.36 crores registering a robust growth of 43% over the corresponding quarter of the previous year. The segment results stood at 16.77 crores as against 13 crores during the previous quarter of the previous year registering a growth of 29%. The OEM and the packaged air conditioning segment; the segmental revenue and the results for the quarter under review stood at 135.18 crores and 6.49 crores as against 208.43 crores and 7.87 crores with respectively to during the last year. After excluding the inter-segmental sales to other segments, the net revenue to outside customer has reported a marginal decline of 7%. This was primarily on account of currencydemonetization which has impacted the AC manufacturing company. During the year, the company has developed and launched new range of highly efficient ecofriendly inverter AC meeting with 2,018 energy efficiency norms for the residential segment. The heat exchanger and the component segment; the segment revenue and the results stood at 130.70 crores and 14.64 crores as compared to 131.64 crores and 13.24 crores respectively during the corresponding quarter of the previous year. This segment caters to the manufacturing of the heat exchangers and evaporator coil for the HVAC and refrigeration industry and copper and brass heat exchangers for railways, heavy automobiles and other industrial applications and component business of sheet metals. The segment revenue during the quarter was marginally lower due to the lower demand intake from HVACR players.

During the quarter, the total income from the operations from all the subsidiaries put together was €12.30 million as against €11 million during the corresponding quarter of the previous year registering a growth of 12%. The third quarter being the traditionally off season period due to the lower sales volume and order intake on several markets the subsidiaries put together had reported a negative EBITDA of €0.05 million during the quarter ended December'16 as against negative EBITDA of €0.28 million during the corresponding quarter of the previous year. Consequently, the subsidiaries reported a negative PAT of €0.32 million during the quarter under review as compared to the negative PAT of €0.72 million during the corresponding period of the previous year. However, for the nine months ended December 2016, the subsidiaries reported positive EBITDA of €1.3 million as against the negative EBITDA of €0.10 million during the corresponding period of the previous year.

As a main effort, Janka continues to focus on cost saving initiative. So far major portions of savings has been achieved through reduction of personal costs which decreased by about 10% from the last year. However, implementation of several engineering actions has been delayed from the targeted time schedule due to various manufacturing obstacles. As a consequence of the ongoing actions, though the financial performance has significantly improved from the last year but still remains in negative figures. More organizational and engineering actions are therefore planned for the coming months which would result in further reduction of product cost as well as head count. In the upcoming quarter the company would secure two larger AHU projects in domestic market and is close to reaching agreement with large rolling stock manufacturers in Poland regarding future deliveries of AC units. In respect of the newly acquired Noske-Kaeser rail and vehicle business, the sales volume has been slightly better than the previous period due to the full ramp up of deliveries for the Bogestra project to customer Stadler. As a strategy all new projects sourced by the NK-Germany are planned to be outsourced to the sister company Janka in order to benefit from the internal manufacturing within the group. Now I would request Mr. Nipun Singhal to provide a quick overview of the operations during the quarter.

Nipun Singhal: Thank you Anita for giving us a detailed snapshot. Good morning everybody. I think she has read out the top line number but I will just repeat it to everybody. The top line has again been wonderful and despite some fears of slowdown in demand which did happen we have been able to post 43% growth as against 213.36 crores. We were able to post 306.14 crores as revenue in this quarter. The nine months' picture is even better as against 839.15 crores. We are at 1242.28 crores for the nine months which is 48% growth in this current financial year for the nine months. I think we have been talking earlier in investor calls and the dream of how this brand is moving forward and the momentum moving forward is essentially driven by 2 philosophies that we have very close to us, one being after sales service and talk in the past about what we have done in terms of the KKG code, Khushiyon Ki Guarantee code which ensures happiness to customers. Let me talk about the app, the MyLloyd app which is a real unique feature for customers who wants service from Lloyd. So that theme of delivering after sales service continues and the second has been to give world class products and maintain our leadership in gaining market share in all segments. I will just take you through the segmental breakup now. In AC, our growth was 63% versus the previous corresponding year.

In LED TV it was 19% and in washing machine it was a whopping 79%. So all categories have contributed and I can see this trend going ahead that we will see growth across all categories. So the nine months, the air conditioner growth was 41%. For LED TV it was 67% and for washing machine it was 74%. What we really would like to see is how the market share can increase in LED and washing machine as in air conditioners we command a very respectable market share of about 14%. Likewise, in washing machines and TVs also we have a new line up which will be ready for the festive season. I think that is it from me. I would request Mr. Filip to provide a quick overview on the overseas subsidiaries. Over to you Filip.

Filip Eisenreich: Thank you Anita. Good morning everybody. Greetings from Prague. First of all I need to congratulate my colleagues in India because they results are really fantastic and I would love to havealso such a good news for everyone and hope as time goes I will be able to present some more positive figures. However, in Europe one of our main challenges for the quarter is continuing trend of weaker market. This was particularly the case for our coil business, heat exchanger business where sales has suffered drop of more than 10% from the last year levels. So since beginning of financial year we have intensified our customer acquisition efforts in order to get a new prospects into a regular customer base. This activity has started to deliver tangible results towards the end of year 2016, soon as all qualification requirements have been fulfilled. With the new calendar year we are now starting serial deliveries to couple of new large OEMs in Italy, UK, Germany which shall partially offset the lower sales volumes from our traditional market. Certain encouragement has been recently arriving also from Russia as you probably know as we have reported in the past. The Russian market during the last two years plummeted by 60%-70%. So it basically disappeared and in the last few weeks, thanks to the stabilization of Russian currency and also slight increase of oil prices we start to observe mild recovery of the market there. Other focus area as was already mentioned by Anita has been the cost saving actions at Janka where we achieved different results. The highest savings by far are coming through reduction of personnel or improved labor productivity. So in this chapter we say we are fully reaching the target. Quite successful has been procurement savings. Although in few cases the full effect has been delayed due to stock of previous inventories. So far our most difficult implementations are the actions in the area of Engineering improvements and savings through design. In this section we have identified the largest potential we are working on it by the executions slower than planned due to necessary adjustment to production process or in some cases also requirement of customer approval. So here I must say we are on the right track, but so far we seem to be in the slower line. All in all, during the nine months we have seen good progress in the process of cost reduction although implementation has been slightly delayed and therefore did not contribute as much as planned. But at the same time we have concentrated on new customer acquisition and we currently started to see gradual improvement of order intake which shall result into growing sales revenue in the coming period. That is it from my side. Thank you for attention.

Anita Kakar: Thank you Filip. So we will be open for the question and answer session. Can we have the first question please?

Moderator: Thank you very much. We will now begin with the question and answer session. The first question is from the line of Harsh Vijay Shah from Creseta Investments. Please go ahead.

Harsh Vijay Shah: My first question is on consumer durables. Can you just throw some light as to what percentage of our sales was from the new scheme of yours regarding that zero down-payment?

Nipun Singhal: Yes, good morning. The thing is that normally our consumer scheme was at about 13% of our total sales. Consumer finance was about 13% which almost doubled to 25%. So if you look at the trend for the 9 months, January to September about 13% of our turnover was through consumer finance. But in the quarter October to December we found that it doubled to 35% of the total gross revenue was through consumer finance.

Harsh Vijay Shah: And can you just throw some light as to this quarter after the impact of demonetization what happened in at overall AC industry as a whole, your company had specific, we did see that there was a pressure but did we also take some production hits or so or did we have inventories withusat the end of the quarter?

Nipun Singhal: For Lloyd Electric I will start first. In Lloyd Electric we have had 63% growth in air conditioner for the quarter October-November-December. So we have done far better than our industry peers. Yes, there is some problem for few brands and we have had sluggish sales and this stock levels have gone up, but in our case, we were able to maneuver very well. We spent more money by giving ads to our dealers so that they could liquidate their materials.

Harsh Vijay Shah: The last question is on foreign subsidiary. Can you just throw as to how is the growth trending especially in the last call you had mentioned we are gaining some market share in the Germany area. So apart from Germany other European market, how are we doing and what is the plan?

Filip Eisenreich: Sure. In general, for the heat exchange of market, yes Germany is one of the region where we see a growth potential for two reasons. One is generally better economy development than in rest of Europe and second reason is also our so far, the lower market share that we had in this market before. That I must say we have the highest growth throughout the year in Germany so far. Thanks to very hard sales effort that we have in this market and basically we have started and if you look in our distribution of sales throughout Europe always the leader for us was France. France was representing 1/3rd of the market and sorry, need to correct it, 30% of our turnover whereas our market share in France was estimated to be close to 20%. In Germany, our market share was let us say under 3%. In the recent months and years since we have our own establishment in Germany we believe that the market share has about doubled, so we are currently patching 6%-7% of the market share in Germany and the trend is growing, just as a picture, two years ago we used to have about 5 single customer accounts in market in Germany. Currently we have about 30 active customers in Germany and of course as we are ramping up the production the market share is increasing. You had also rightly mentioned the large coil manufacturing which is typically the segment of cooling of data centers. It is the most promising segment in Europe so far and I am happy to say that we are currently serving all largest players in this market. In international it is Emerson Group. Schneider Electric Group, Molding Group. All these largest manufacturers are among our customer pool. So definitely we are full benefiting from a growth on this market.

Harsh Vijay Shah: Second is one last question to Mr. Nipun. Sir from the date of demonetization till date that is February, after this demonetization, how is the movement of our raw material pricing has been across the sector?

Nipun Singhal: This is an open information. Steel prices have gone up considerably. Copper prices have also gone up. So about 20% has been the increase in copper, steel, aluminum, plastics. So there is a huge pressure to increase prices and we will be looking to increase prices once the season is in full swing. So we are looking to increase prices in the near future.

Harsh Vijay Shah: And still that was the main thing, are you looking for any price increase because of the increase in raw material?

Nipun Singhal: The entire industry will have to. It is not only for us, the entire industry will have to increase prices. In January we were all worried about how the demand would react to increase the prices. So we reined in, and still you know winter in North India etc. So we just held back, but I think very soon we will be all increasing prices.

Moderator: Thank you. The next question is from the line of Ankur Sharma from Motilal Oswal Securities. Please go ahead.

Ankur Sharma: Couple of questions on the Room Air Conditioner side, if you could tell us what is the proportion of investor ACs to your overall mix and on a related note we understand that LG is completely moving to inverters in the split segment. So what is your strategy there and how do you see the share kind of moving up over the next few years?

Nipun Singhal: It is an excellent question. Thank you for that. I think the inverter AC definitely help in saving power and that is why that is a technology which is a future technology. But at the moment if you see the price gap between a 3-star AC and a 3-star inverter AC the price gap is almost to the extent of Rs. 7,000 – Rs. 8,000. So the pay back to the consumer is going to take about 2-2.5 years. So at the moment in current year 17, we are not going to find a huge switch to inverter ACs. Next year as you know the star rating is going to be revised downwards in two steps. So what is 5-star today will become 3-star in 2018. At that point in time when the gap between the next year 3-star fixed speed and inverter narrows, it is at that time that customers will probably choose to buy inverter. Currently, I think fixed speed 3-star will be dominant. I have had several dealer meetings and I have taken feedbacks from the dealers who are interacting with customers that the market will still be almost 70%, 80% fixed speed.

Ankur Sharma: So you do not expect radical change towards inverter at least this year. May be starting next year the pace gets faster?

Nipun Singhal: Absolutely. Then there are some other issues. In inverter ACs you have a very sensitive component called the PCB, the PCB failure is being reported very high even in the past, that is principally towards our power supply. So in metro cities may be you can use inverter ACs, but in Tier-2 and Tier-3, the PCBs have a high failure rate. So the customers are even weary of that problem. Because if you have a PCB failure you will spend Rs. 10,000 – Rs. 12,000 in replacement of PCB which is going to clear savings completely for the next 5-6 years. So all in all. I think this year people are still going to be dominant in fixed speed. Which is why no other brand expect LG has taken this gamble. Whether it will take off or not we will come to know in 4-5 months times. My bet is that this year we will see 70%-80% fixed speed still remain.

Ankur Sharma: So conversely does that also mean that LG is exiting the fixed speed, players like yourself and some of other players like Voltas would actually gain share at the expense of LG, is that a fair assumption?

Nipun Singhal: See, I would not like to comment on LG's strategy. All I am saying is that, my view is in this year for sure, I do not think we will see inverter ACs becoming 50% of the market. I think it will not be more than 20%-30%. What is LG strategy, how are they seeing the market, that is something that I cannot comment on.

Ankur Sharma: Understand. That is very helpful. And secondly sir, just trying to understand little more on this very strong growth that we have seen this quarter, 63% in the Room AC side, now what we understand is that Lloyd traditionally has been more focused on the Tier-2, Tier-3 cities where what I would believe is that EMI schemes etc. may not be that popular. Now despite that we have shown some strong growth. So this if you could just tell us, just trying to kind of get a sense of how this has come through? Is it primarily the market share gains for you, that would be very helpful if you could elaborate a little bit more?

Nipun Singhal: I think you answered the second part of the question already. The industry is not going at 63%. Which means that we have gained market share. It is an obvious assumption. Now come to the point of being strong in Tier-2 – Tier-3, we were strong in Tier-2 – Tier-3, that is where we started off from 2008-2009 but in the last 2 years I have said on several calls, all our investments in marketing has been targeting towards gaining market share in the metros and in Tier-1 cities and that is what started to play in. That is exactly the fruits what we are reaping today. Our focus is on brand spends in metro cities. So this growth is not from Tier-2, Tier-3, this growth is all from metros, places like Delhi, Bombay, Bangalore, Hyderabad, these are the markets which have given us this phenomenal growth, where we were weak. And going ahead I will tell you, the growth for Lloyd will come from these markets, it will not come from Tier-2 – Tier-3 going ahead. Which is why all our marketing spends are aimed at these metro cities. I will give you examples. Look at the investments we do at airports. If you go to Hyderabad airports you will see beautiful display of Lloyd. Delhi airport we have the largest square foot area of Lloyd branding. Bombay airport we do festivals every 3 months in Bombay airport. So the entire investment is on metro cities. Our tie up with The Times of India group, The Times of India is focused at customers in metros, not at Tier-2, Tier-3. So this was a weak point and I said on calls earlier that I think from a year and half that we took this call, that look we have done very well in Tier-2, Tier-3, now the time to come into the metros.

Ankur Sharma: Understand. And sir just one last thing on your proportion of inverter sales in your overall Room AC sales?

Nipun Singhal: We are at single-digit currently for Lloyd, but I think we will grow as well in this quarter and in this season. Yes, maybe certain brands may have 20%-30% inverter but that is because of their design, that is because they are focused on that segment. And LG will probably have 100% inverter just because they do not have the fixedspeed. In our case, we have a very large bouquet of products, right? We have right from floor standing,cassette, portable window, many brand do not even do window ACs. We still have a very high proportion of window ACs. So our percentage therefore of inverter looks much smaller.

Moderator: Thank you. The next question is from the line of Yash Matai from Vibrant Securities. Please go ahead.

Yash Matai: I want to understand something. Sir, OEM and packaged air conditioning business why the revenues and margins are so volatile, like if you see in some quarters we have around 300-350 crores revenue and some point we have around 81 crores revenue, what is the reason for volatility of revenue in margin in this segment?

Nipun Singhal: Are you talking about margins or you talking about revenue or both

Yash Matai: Both.

Nipun Singhal: Okay. So we will address one by one. I think first we will talk about the revenue. I think we are manufacturers, which means that we will be following the demand of our customers and how they fair in the market. We have no control like in consumer durables we have no control in pushing materials without their orders. If certain customers of ours have weak demand or they do not want to build up inventory or some other compulsion, the volatility will be there in revenue. Although I would say that if you look at corresponding quarter which is under review, there is only a 6% drop. That is what very volatile. So first thing is the nature of OEM business is we are dependent on the fortune of our customers or the strategy of our customers. Sometime the customers are very bullish. They may prepone their purchases and they may want to stuck up looking at buoyancy in demand. Sometimes they are little pessimistic and they say let us not keep any inventory at our end, let us hold the purchases. So that is the nature of the business. The second thing is in this quarter per se, there is only a 7% drop. It is not 30%-40% drop. Move into the margin side, we just heard one of the questions where we talked about volatility in the commodity price. Now steel, copper, aluminum all have shot up by 20%. There is some time which is taken to pass through that increase because I cannot have a daily rate to my OEM customer. I can change my scheme on a price to the dealers on a weekly or a monthly basis. But for OEM customers it is a process. You have to sit with the purchase team. You have to go into the costing and… There will be some product which will flow out at old prices despite that you are buying at new prices.

Yash Matai: Sir my next question is on the corporate restructuring that you were talking about a quarter or two back that you had E&Y this thing. What happened to that?

Nipun Singhal: We are still in active consideration. I think sooner than later we will be coming back to you and making an announcement on that very soon.

Yash Matai: Sir, and last question is, sir can you speak more about the competitive scenario in TV and LED and basically washing machine segment how is your competition like that because two quarters back we spoke about it and you said that Micromax and other players have come in and their competitive prices is lower than yours, so how is the scenario now shaping. Can you speak more about it?

Nipun Singhal: See, if you look at what we found it, but you know the company is in the mobile business, like Micromax, like Intex, they had a lot of money power from their mobile business to enter into LED TV business. What happened is that, I see for Micromax for sure they have lost considerable market share in their home turf. You know Vivo, Oppo, Gionee, all these brands have become very aggressive in India. So Micromax currently struggling to hold its turf, where it was strong in mobile phones. You can take industry data in mobile phones, their market share is dropped. So in the last 3 or 4 months I find less number of ads to Micromax, less aggressive prices for Micromax. That is now reduced because I think they are probably trying to save their home turf.

Yash Matai: So what is your market share in washing machine and LED right now and have you gained market share?

Nipun Singhal: Absolutely. In my initial remarks, I said that in washing machine our growth has been 79%. So we have really gained a lot of market share in washing machine and I think going ahead, I have said this in the past as well, LED TV market share and washing machine market share is low-hanging fruit for us. In ACs, at 14%-15% we are probably number two, number three brand in India. So yes, we will grow in market share there as well but there is not much head room to go there. But in premiere washing machine where we are sub-5% there is a lot of head room and I think this is what is going to be the driver of revenue in the next 3-4 years because currently the customers have started accepting, yes, Lloyd TVs are good. Customers are accepting that Washing machines are good. Earlier were perceived only as AC company. Lloyd is a 60-year-old AC company. From repeated campaigns, repeated efforts, significant dealers, customers' own experiences, now we are slowly gaining acceptance in LED TV and washing machine as well. The numbers are indicating that. Quarter-on-quarter you see the numbers are indicating just what I am saying.

Moderator: Thank you. The next question is from the line of Yash Agarwal from Crest Wealth. Please go ahead.

Yash Agarwal: Yes. I have a question on this, finance cost has moved up sharply quarter-on-quarter, so has the working capital situation deteriorated from H1 because in H1 there was a tremendous improvement.

Anita Kakar: During Q3 we start building up the inventory for the quarter four. So that is the reason the finance cost is high sequentially as it includes the bank charges.

Yash Agarwal: And second question I had on the margins of your consumer durable business, so despite such strong growth in AC, the margins are down year-on-year by about 60%-70% basis, so what is the outlook ahead going on your consumer durable business margins?

Nipun Singhal: See, we have taken a hit in this quarter, yes, definitely as against 6.09% we are at 5.48%. So you are absolutely right that about 60 basis points has been a drop in the margins. So it is basically on account of two things. One because we saw demonetization we went into the finance scheme and as I said earlier, the total financed products jumped from 13% to 25%. So those were extra pay out for the company. The second thing is increased in advertisement costs. Not only our regular corporate advertising, we spend almost 8 crores in giving dealer advertisements to liquidate their material. So eventually when there is a situation like this, where there is a sudden drop in demand, the companies need to push product and liquidate the material. If I had not done that, in November December, January-February-March would have been affected which is a much bigger quarter for me if the pipeline has been full at the start of January, I would have had a problem in pushing material in Jan-Feb-March. What has happened is that by sacrificing a small amount of margin we were able to clear the pipeline in the inventory in the last quarter itself. So the pipeline and inventoryis clean as of 1st January. So you see a very good growth in January- February-March.

Yash Agarwal: And sir now is the raw material price increasing and also what is the outlook on margin, do you expect it to revert back to the former levels, last year levels?

Nipun Singhal: I think we should be at around last year. That was because a) with the growth in turnover which I am confident of, we will find that the base effect will come in. So, we should end up at last year levels, I mean, despite the commodity increase, I do not think there is any effect in this quarter. You should compare the last quarter of '15-'16 versus last quarter of '16-'17 we should be at similar levels.

Yash Agarwal: And sir in this financing scheme, what sort of pay out do you do? You just mentioned right now. So in this 0% finance scheme do you pay the NBFC or anything?

Nipun Singhal: The finance team has two parts – There is something called as DBD, which is the dealership and the other part is called MBD, which is the manufacturer buy down. The scheme that Anita spoke about 'Cashless Happiness' this scheme was a very expensive scheme. The total cost of the scheme is 9.5%.

Yash Agarwal: Of your selling price?

Nipun Singhal: Yes, 9.5% is the selling price to the total scheme cost. Now out of this 9.5% we gave only 2.5% to our dealers and the company took a hit of 7%.

Yash Agarwal: But that is a pretty substantial hit. So what are the pros of this scheme, just to clear inventory?

Nipun Singhal: Absolutely. If I had not given the scheme, the sale would not have happened. See we took a call, that let us liquidate material. Let us not keep material and stock, just to hold on to margin. Let's give this scheme, let us give ad support and then liquidate stock. There is no point in keeping stock and then suffering in January.

Yash Agarwal: And this scheme is offered by only you or is it there by competitors also like BlueStar, Voltas and all?

Nipun Singhal: I think 2 or 3 competitors also did react after that but much later. We were the first to come out. My ad you can see was in the 15th of November. 8th November, 8 pm Mr. Modi announced it, 15th my ad was there in the newspaper.

Yash Agarwal: And sir any new consumer products that you are planning to launch apart from these three right now?

Nipun Singhal: In this quarter, no. In this quarter, we are going to continue with our current range. Of course there are very new models of air conditioners that we have launched, the big campaigns which are mentioning from March is going to talk about 21 models that you have introduced with WiFi. So you have 3-star ACs, you have 5-star ACs and inverter ACs, that is common, across all competitors. We are the only company who will be offering you 3-star with WiFi, 5-star with WiFi, inverter with WiFi. Now what is WiFi. WiFi basically is AC is now connected through the internet through WiFI to the World Wide Web and this will result in the AC developing artificial intelligence. So not only can you control your AC through your smart phone, you can also get all the data from your AC on the smart phone like power consumption, like the number of hours that it worked and eventually it will also communicate directly the error codes to the service center without the customer even realizing. So this is a trend which we are seeing globally of IoT.

Yash Agarwal: So basically, the beneficiary the power consumer data will be as a consumer or will it be with a company to assess the products, or with both of us? The power consumption rate and all, I am sure as a consumer I would not want to know what the power consumption of my AC is, but how would it benefit I mean?

Nipun Singhal: See, the first benefit is, the control of the AC will be now on the Smartphone. So you do not have to reach for the remote, change the batteries and so and so forth. Also you can control the AC from your car. So let us say you are driving back home and you want to switch on the AC, you can switch on there. So this is the first benefit. The second benefit is to understand the data of how many hours is AC being used. You know, many times children don't switch off the AC and you can see suddenly that the AC has been on for 19 hours in the day. So why the hell is AC on for 19 hours in a day. Then there are customers who are conscious that they do not want to have a very high energy bill because ACs do give you very high energy bill. So, they want to track that. This is an added benefit. The big thing is going to be when the error codes will be transmitted to the service center directly. Today what happens is when you have a problem with the AC, you have to either use our app or you have to call our toll free number and register a complaint. Going ahead these futuristic ACs will directly talk to the service center through WiFi. If you see what is happening in Las Vegas, the CES show, Consumer Electronic Show in Las Vegas which happens every year. The whole theme this year was about IoT. So all devices in the future, not only ACs, will be connected to internet. And I think Lloyd is the only company who have taken this leap in this season, where they are not talking about 3-star, 5-star inverter. We have everything here. Everybody has inverter. What is the big deal about inverters. We have got 3-star 5-star inverter with Wi-Fi. What I want to clarify is the extra pay out has elevated margins to drop by the 100-135 basis points during the quarter.

Moderator: Thank you. The next question is from the line of Ashish Kumar from Infinity Alternatives. Please go ahead.

Ashish Kumar: I had one query in terms of relation to your margins. So if you look at the margin profile, over the last 3 years we have seen the margins peak out at 13% and this year, every year, or some reason or the other we see a margin drop. As the brand based acceptance which we can all observe, one would expect that the margins would start increasing. By when do you think that we would start seeing a growth in the margins back again at the company level as well as the CD (Consumer Durable) level.

Nipun Singhal: Okay, I will first talk about the company level. The company level is basically a change because the blend has changed. As you can see the margins in the consumer business are lower than what we have in our traditional heat exchange and components business. So as the blend changes, as consumer durable in the last 3 years you can see consumer durable percentage has increased year-on-year. So at the current blend of about 64% consumer durables, you will find that the blended margins will drop. So on the overall company, I think it is a change in blend which is resulting in the lower margins be more specific consumer durable which is now 64% of the business. I have said this in the past, as we grow more and more in television and washing machines we will have to spend more money to gain market share. Our advertising expenses are very high compared to our peers. If you compare what we spend versus your peers, we spend much more money. Our service costs are more than double of what is spend for half year because this is the platform on which Lloyd was based, '*Khushiyon Ki Gurarantee*'. So I spend almost double the money in our after sales service than what my peer spend. I am new, I am yet to gain that acceptance in TVs and washing machines, so I have to spend a lot of money. My schemes, my bigger margins are higher than what you will see with Voltas and Hitachi. Those are the established players for the last donkey's years. So these are 3 reasons, my pay out to the dealers, my advertising expense and my service cost, which is why my margins are lower than my peers. And to answer the part, when it will start growing up. I think I have said this earlier, when we have approximately 10% market share across all categories, that is the time then we will be like all the established player and then you can see a gradual uptake of margins.

Ashish Kumar: Thanks Nipun. But the thing is on the AC side we are already a double-digit market share. So are the AC margins now comparable to what we see for let's say some of the peer groups or does that also still is some time away for us?

Nipun Singhal: No, it is not. Even the AC margins are still not away because it is still early days, if we look at our growth in the last 3 years from being not even in the top 5 we are probably at number 2 right now in India. So it is still early days. You have to cement your position. You do not want to have a flush in the pan that one year you have done well and next year you start increasing prices and the whole trade is unaligned with you. So I think let us sustain out here. We are in this business for the long haul. I am looking at doubling or tripling this revenue. I am not looking at 20%-30% growth. In the next 5 years, my guess is that we will double this revenue and that is when it is going to be fun.

Ashish Kumar: So you believe that you will continue kind of trading the margins for the growth at least for the next couple of years.

Nipun Singhal: I would say that we will maintain, I would not say trade margin, we will maintain. We will not grow margins but we will not even surrender margin, we will keep our margins at the current level.

Ashish Kumar: So the current levels of around 6%-6.5% consumer durables at EBIT levels that would be sustainable?

Nipun Singhal: Absolutely, that should be the sustaining thing and maybe like I said after two years or so when we find that 2-3 years, when we find our position in air conditioning is cemented. We are gaining traction in washing machine and in TV towards(+5%) market share, that is the time when we can gradually stop picking it upwards.

Ashish Kumar: And in terms of the ROCE, do you expect that inventory tightening which we saw in the first half. I know in this call you mentioned that some of the inventory build-up this quarter that we have seen is because of the season. But do you expect that the working capital intensity in the consumer durables business let us say over the next couple of years, will that trend line what we saw in September will that be continued or will we see further dips, what is the guidance you would have on the net inventory days let's say for the full year?

Nipun Singhal: Actually, we will continue with that trajectory. We will be tightening and that is something which is more important than margins because eventually when you look at ROCE, I think that is a more important number than the EBITDA margin, especially for a growing company like ours. So, that is something which will continue. You will see tightening on the less number of days in quarters going ahead.

Ashish Kumar: So what will be your target let say if I were to look at the inventory days for FY'17 and '18?

Nipun Singhal: I wouldn't like to speculate, but it is not about the absolute number, it is not the direction, what I am giving you guidance on is that the direction is going to be tightening on the net working capital days and that will continue. The absolute number does not matter. As long as you are moving in the direction it is going to keep on improving our ROCE that is for sure.

Ashish Kumar: That is true. The question is base of the improvement, so can we look at scenario where we would be flat inventory despite a 30% growth or will that be too aggressive?

Nipun Singhal: It is a very difficult question and I would not like to….Youare putting me on spot. I think I would not be in a position to give you an accurate answer and hence I won't give you an answer.

Ashish Kumar: Okay. Anyway all the best and hopefully you will get your inventory days.

Nipun Singhal: That trajectory is going to move in tightening direction. Like I said ROCE is going to increase which is of great interest to you.

Ashish Kumar: That is right. That is the bottom line.

Moderator: Thank you. The next question is from the line of Agam Shah from KDS Trading. Please go ahead.

Agam Shah: Can you just give a brief about like going ahead. So when do we expect the demand to be normal in the OEM segment after the demonetization like. What do you expect going ahead like?

Nipun Singhal: I do not have a clear picture on that because I handle the consumer business, but from what I hear from my colleague, Mr. Roy, who handles the OEM business that the demand again has started to pick up. So in yesterday's Board meeting we had a little discussion and he is saying that the other brands also have started showing an increase in demand which was not there in November-December. We were really just skeptical in November-December, people were cutting their targets for calendar year '17. But yesterday's board meeting he was mentioning that there is a renewed interest and increased buying.

Agam Shah: And on the consumer part?

Nipun Singhal: On the consumer part, we are very bullish. I am 100% confident that we will have a fantastic quarter, like we did in the last quarter we will have a very good Jan-Feb-March.

Moderator: Thank you. The next question is from the line of Shiv Reddy from Mergers India Info.com. Please go ahead.

Shiv Reddy: My question is, is the home appliance segment contribute into the bottom line. What is the rationale of foray in appliances segment, are we spreading our resources too thin or we are expecting to gain critical mass in this segment?

Nipun Singhal: A very good question sir. What happens is, the moment you become a single product player you find that your grip on your channel is greatly reduced, for example if I only have air conditioners then my channel partner he has to go and buy washing machines and refrigerators and TVs from other brands and then they arm twist**.** If you want our washing machine, if you want our TV, then you have to sell our AC also. So your grip on the trade becomes weaker. I am not saying that there is a great example of Voltas which is only an AC player. But I am told that even Voltas is foraying into newer segments. So first reason is from the point of view of channel control. The second reason is that, in today's 20 player industry if you are only talking and communicating to customers in the season, the AC season then post that you are out of sight, out of mind. If you have products which are relevant throughout the year, then you will be communicating to customers in the AC season for cooling products, in the monsoon season for washing machine and of course in the festive season for electronic products. So you have something throughout the year. The last reason is, we do not want to see Q4 and Q1 are very big quarters and then Q2 and Q3 are very shallow quarters. The peaks and thrusts are very steep for the AC business and our fixed expenses are almost constant throughout the year. Salaries, warehouse cost, everything is almost constant throughout the year. So by adding these products, like if you see Television sales are reverse proportion to the AC sales, they will peak in the festive season.

Shiv Reddy: I heard your reply. But I am specifically referring to this brand extension. It should not dilute the brand if you are going Iron box and stuff like that, I do not know where it is really going to add critical mass?

Nipun Singhal: No, the steam irons and all are not something which we are focused on. They are basically products that are added, bundled with the prime products.

Shiv Reddy: My last query, how is your railway business shaping up?

Nipun Singhal: We have to get back to you on that because I do not handle the railway business. So I do not have a clear picture on that.

Shiv Reddy: No issues. Appreciate it.

Shiv Reddy: Because almost all, government is spending a quite a bit on this railways, so it should give lot of traction?

Anita Kakar: We are in the process of developing protocol for the Toshibha orderwhich has been bagged recently and once approved the dispatches will start soon

Moderator: Thank you. We will take our last question from the line of Sayali Gandhi from Torero Capital. Please go ahead.

Sayali Gandhi: Could you help me with the ad spend figures for the quarter?

Nipun Singhal: Yes, the ad spend that we did for the quarter was about 13.06 crores which is about 4.24% of the top line.

Sayali Gandhi: Okay. And for the last quarter and the corresponding quarter?

Nipun Singhal: The corresponding quarter was 11.5 crores and the previous quarter I do not have with me right now, I will have to get back to you on that. What I have is, this quarter and corresponding quarter.

Sayali Gandhi: Okay alright. And also could you help me with the volume figures for AC, LED and washing machine for the quarter?

Nipun Singhal: We have stopped giving the volume figures for the last two conference call. We do talk about our growth in percentage term and I can give you the value figure?

Sayali Gandhi: Yes, that will be good.

Nipun Singhal: You want the value figure?

Sayali Gandhi: Yes.

Nipun Singhal: Okay. So the value of air conditioner sales in the third quarter was 134.74 crores and the LED was 122.94 crores and for washing machine it was 44.96 crores.

Moderator: Thank you. Ladies and gentlemen due to time constraints that was the last question. I will now hand the conference over to Mr. Salil Utagi for closing comments.

Salil Utagi: Thank you all on behalf of Edelweiss for attending the call. I also want to thank Lloyd management on behalf of Edelweiss. So we can end the call here. Thank you.

Moderator: Thank you. On behalf of Edelweiss that concludes this conference. Thank you for joining us and you may now disconnect your lines.