“Analyst Call of Cummins India Limited”

February 2nd, 2018

SPEAKER: **Mr. Rajiv Batra, Chief Finance Officer, Cummins India Limited;**
Mr. Sandeep Sinha, Managing Director, Cummins India Limited.

Moderator: Good day, ladies and gentlemen. I am Pragyat, your moderator of this session. Thank you for standing by and welcome to the Analyst Call. For the duration of presentation, all participants' lines will be in listening-only mode and we will have a Q&A session after the presentation. I would like to now hand over the conference call to Mr. Rajiv Batra, Chief Finance Officer of Cummins India Limited. Thank you and over to you, sir.

Rajiv Batra: Thank you. Good morning, ladies and gentlemen. On behalf of Cummins India, I welcome you to this call. I am joined in today's call by a Managing Director, Mr. Sandeep Sinha, and we would like to convey the results for the quarter just ended October to December and the nine-months ended December 2017 through this call. With respect to the sequential quarter, our total sales at 1318 crores, grew by 18% compared to the preceding quarter. Domestic at 899 crores grew 20%, while export sales grew by 13%. Net profit before tax at 220 crores, grew by 12% compared to the 195 crores recorded in the previous quarter.

It has been mentioned to you in our last analyst call our September quarter results were impacted due to the softness through the introduction of the GST, there were delays at some of our major customers as well as some certain supply constraints from our side. I am happy to mention that we've had for the most part been overcome, as you can see from the results and the numbers I just gave you. From the published results you would have seen strong improvement in our material margins. These obviously have been driven by our dedicated cost reduction efforts made by our teams and this has helped us take away this thing from some of the increase in the commodity markets. Commodity markets, as you are aware, have in the recent past been relentlessly going up.

Our employee cost and overhead expenses have seen an increase this quarter and this is primarily a true-up on our variable pay factor for our employees. A small increase in the donation expenses to take us to the 2% threshold as well as a true- up on our management cost charges. This has impacted our profitability in these lines for this quarter. Compared to the quarter a year ago our total sales at 1318 crores declined marginally by 6 crores. Our domestic sales, however, grew 3% at 899 crores, but our exports declined by 7 per cents points. Our profit before tax at 220 crores declined by 10% compared to Rs. 245 crores the same quarter last year. For the nine months ended December our total sales at 3746 crores declined by 1% compared to 3803 crores for the quarter at the same period last year. Domestic sales, however, actually improved by 3% to 2562 crores. Exports declining by 10 percentage points with the results recorded a year ago. Net profit before tax is 644 crores declined by 10 percentage points compared to 730 crores recorded at the earlier year. So with that, I would like to state that we are optimistic about the long-term impact rising from the domestic economy. Clearly, after GST and some of the circumstances which we saw in November of last year all there has been in the past, the industrial markets are robustly growing, so we remain optimistic about the medium to long-term future. So with that, I will open this up for questions.

Moderator: Thank you, sir. With this, we open our floor for Q&A. Any participants who wish to ask any questions can press "0" and "1" on your telephone keypad and wait for your name to be announced. We have the first question from Mr. Charanjit. The line is unmuted.

Charanjit: Hello, sir.

Rajiv Batra: Hello.

Charanjit: Yeah. Sir, if you can give us more colour on this, you know, rise in the other expenses while you gave an initial commentary, but what could be the quantum of, you know, the increase in different heads and how much of those could be, you know, recurring in number?

Rajiv Batra: Yeah. Our management the biggest item here is, in fact, about 2 large items. One is our R&D expenses; this is about 5 odd crores. Now, this number will keep fluctuating through the quarters based on what exactly programme we are pursuing for that quarter, right? So apart from that, the next big one is what I spoke about which is a true-up of our management cross charges. This really depends to the degree of services that we use from our parent who we have to reimburse. So in total for this calendar year we are running about 10 crores more than last year and that we trued up in the end of the calendar. So it's a kind of a true-up which has worked in this quarter.

Charanjit: Okay. And, sir, what would be the like, you know, what are the services which we are taking from the parent and do we see a similar kind of a number now continuing on a quarterly basis how we should, you know, forecast this?

Rajiv Batra: Charanjit, this number has been there always with us embedded in our financials. It's been there at least now for the last three years. These actually are services which we take based on certain markets that we approached in India. We have experts overseas, let's say, the mining markets, the marine market, the rail market. So across the world we are able to access this knowledge and for that obviously there is a charge. Then it also is our technical developments. Very clearly at times we live on the expertise of our worldwide experts. So its charges are VAT nature and purely based on what we consume is what we pay for. So these have always been there, except in the last quarter we've just trued this up to the actual extent of utilization. So in total for the year there is about Rs. 80 crores charge; last year it was 70 crores, but the true-up has happened in the last quarter. So again through the quarters this has always been there with us and we are talking about the true-up.

Charanjit: And, sir, the last question from my side would be on the overall, you know, market scenario both on the domestic and the export markets we've seen, you know, lot of issues in the domestic market now behind the GST and all, so how do you see the growth going forward, which segments can drive this growth and in the exports market, you know, how we see like has there been like you mentioned about maybe bottoming out and which geographies can see growth going forward?

Rajiv Batra: Yeah. I think on the exports market we've been consistently telling you the risk will go up and come down between the quarters and whereas we see a lot more optimistic about certain markets on a go forward basis. It is not something which will happen in the short-term. So, for example, we see the oil and gas reviving; it impacts some parts of our business. Our largest exports are into the power gen segment and that we believe we are seeing certain recoveries, but it will take time to come back. So that's on the exports and I think on the exports we have a low horsepower market which is extremely important to us which is really the Middle East which is down about 40%, the African markets which at this point are going through a currency crisis that is down about 50%. So these are our two major segments, the African markets and the Middle East market; the rest are doing well. So when these problems in these markets are resolved, we would expect that things would come back to normalcy.

On the domestic market, we are highly optimistic on the industrial markets. One is our teams are making dedicated efforts to get more share in these markets as well as there is tailwind from the government through the infrastructure initiatives which is the construction segment and the rail segment these markets have done very well for us. This quarter we had mining also come back very strongly. So if we would look as compared to a quarter ago, right, actually grown on the industrial markets quite handsomely at about 200 crores; last year the same number at about 180 crores. So there is significant growth over there and we've grown through the quarters as well. So our distribution, given the fact that there was slowness in the last quarter, at 360 odd around crores for this quarter we are up by about 46%. So we are optimistic about these markets.

The power gen market, however, this is somewhere the whole market has been slow for a while, slow for the last couple of years. We continue to maintain share, in fact, in some segments we've grown share but the market itself is soft. This will really depend on how industry comes back now. Manufacturing, real estate these are some of the sectors which have a huge impact on these markets. Sandeep, would you like to add something?

Sandeep Sinha: No. At least you've covered it all. Thank you.

Charanjit: Okay, sir. Sir, thanks a lot for taking my questions. Yeah.

Rajiv Batra: Thank you, Charanjit.

Moderator: Thank you, sir. We have the next question from Mr. Punit Gulati, HSBC. The line is unmuted.

Punit Gulati: Yeah. Thank you for the opportunity. First of all to start with, if you can, you know, just give a usual breakup for, you know, the segment-wise, revenues, power gen, industrial, distribution and others?

Rajiv Batra: This is for the quarter?

Punit Gulati: Yeah.

Rajiv Batra: So for the quarter our power gen on the domestic side was 330 crores, industrial business was about 206 and the distribution business was about 362, so that totals about 900 odd crores.

Punit Gulati: Okay. Exports?

Rajiv Batra: Exports was about 420 crores. So in total the numbers would come to 1318 crores which are the published numbers.

Punit Gulati: Right. And within the exports how much was, you know, various low horsepower made heavy and also for the domestic power gen similar breakup?

Rajiv Batra: Yeah. So for the exports side our power gen exports was about 170 odd crores and our high horsepower exports was about 224 crores and there's a little bit of here and there, so in total about 420 crores. Does that help?

Punit Gulati: Okay. Yeah. That's okay. And within the domestic power segment if you can give a breakup between low horsepower made heavy?

Rajiv Batra: Yes. So the domestic power segment is about 330 odd crores, low horsepower is 36, mid-range, heavy duty is 122 and high horsepower is 172.

Punit Gulati: Okay. Is it possible to share similar number for last year same quarter?

Rajiv Batra: Yes, it is. Last year? Okay. Sure. So last year is about 28 crores on the low horsepower, between mid-range, heavy duty is about 121 crores, high horsepower is 200 crores, so in total about 350 crores.

Punit Gulati: Okay. Great. And, sorry, last year upon the breakup of the industrial part as well, please.

Rajiv Batra: Okay. The industrial revenue for the quarter compressor is 44 crores, construction about 70, mining 25 and rail about 50 odd crores and there's small bits and pieces here and there in total [multiple speakers].

Punit Gulati: That's fine. That's it. Now, broadly on the strategy side, given that you also acknowledged that commodity prices are going up, is there a plan to take price increase and how are you seeing it from, you know, competitive intensity perspective?

Rajiv Batra: Yeah. So this is you are talking about overall or you are talking about any particular segment?

Punit Gulati: So power gen to start with, maybe, and then overall as well as [multiple speakers] always useful, yeah.

Rajiv Batra: Yeah. I think let's talk about the segments that are growing which are the industrial segments, there we have been taking a small price increases, right, nothing like a big-time increase but small 1.5%, 2-2.5% in that range we regularly keep taking price increases.

Punit Gulati: Okay. And is it good luck to cover cost?

Rajiv Batra: Plus, the fact there are engineering efforts and the efforts from our purchasing teams to get better value, all of that is maintaining margins, as we can see, in fact, we've grown margins, right?

Punit Gulati: Right.

Rajiv Batra: So this is something which we've done right across the years. On the power gen markets which is fairly large to us the competitive intensity, as you are aware for the last 3 years, I would say, has remained high and it's very difficult to take very big increases here. In fact, as we told you in calls, we are market aligned and we make adjustments both ways, increase, decrease based on our assessment how market and competition is moving. So the market itself, like I told you, is flattish and therefore at this point in time to put huge increases through is just not possible and it would not be prudent either. So in this segment, again, our efforts at driving cost out of the product and getting the best from our suppliers this is where our efforts are. And we are taking other measures through operating of our products, the impact of which will be visible to you over time, but at this point in time I would rather not talk about those efforts.

Punit Gulati: Okay. And what would be your market share now in this domestic power gen segment?

Rajiv Batra: We are maintaining our shares and I think our shares in this segment so actually on the high horsepower side we will increase our share by about a per cent. So we were 61%, about 62% now. On the low horsepower side, obviously, the telecom market we are not very significant, so even there we maintain share at 40%. And on the medium range the image we see is about 54%, again flat, so flat market shares to a small increase of 1% in the high horsepower segment. So shares we take good cares and all the right actions to engage in the market and be market aligned.

Punit Gulati: Okay. And what would be our market share on the industrial side right now?

Rajiv Batra: It would vary because maybe depends it on what parts of the market it is, for example, in the railways we have a very high market share, but it is on the engines that we actually catered to. The railways have their own engine in private power market, so on and so forth. So it's kind of based on, say, the water well market we are almost a 100%. Portables we are running 58%, construction we are about 57%, so those are the kinds of market shares that we have. So I hope that answers your question.

Punit Gulati: No. This is very useful. Thank you so much for this. I will come back in the queue. Thanks.

Rajiv Batra: Thank you.

Moderator: Thank you, sir. I would again request all the participants, if you wish to ask any question, you can press "0" and "1" on your telephone keypad and wait for your name to be announced. We have the next question from Mr. Nilesh from Macquarie. The line is unmuted.

Nilesh: Hello, gentlemen. This is Inder here.

Rajiv Batra: Hi, Inder.

Inder: Hi. My first question is on this other expenses. You did talk about some reasons, but if I just look at numbers, you've gone from a 132 odd crore number to a 171-crore number that's practically a 40-crore increase, can you kind of talk about is there anything else in that which is either new expense or which is non-recurring something in that nature?

Rajiv Batra: I covered it actually. There are some expenses in line with volume, so those are actually variable-related cost. Then you have warranty again in line with volume. The two ones which we did cover was the true-up of the management cross charges, a little bit of donation about 2 odd crores, as we come back to a 2% threshold and the RTNE efforts, so in total that bucket is about 8 crores. So those are the real big ones; the rest are very small ones.

Inder: One question if I look at now for a very, very long period we used to operate in a margin band which was somewhere between 15-15.5 to 16.5, even stretching up to closer to 17 at times and now we have been at least for the last 4 quarters we have been very close to that 14.5%, is this you think a new operating band that we are going to stick to or is it just you still think that as and when the LHP exports start to come back, we have a potential to go back to our older margin regime?

Rajiv Batra: Yeah. I think it really depends on the mix that we are seeing and like you rightly said, exports is pretty significant in our business. So low horsepower exports when they start to pull back, high horsepower also starts to go back. There is a natural leverage which you will see on our manufacturing expenses and our SAR, so that leverage comes with the increased sales. In addition, I did talk about some efforts which would be accretive to our margins, but I don't want to talk about those as yet. So I would say we got upside from here, but for that upside volume is critical and for that the export markets to come back is also important.

Inder: Okay. That's it from my side. Thank you.

Rajiv Batra: Thank you.

Moderator: Thank you, sir. We have the next question from Mr. Rajni Shivram from ICICI Securities. The line is unmuted.

Rajni Shivram: Yeah. Hi, sir. Just wanted to understand after now it's nine months, so is there any thought in terms of our full-year guidance what we are giving in terms of exports and domestic is there any change in that?

Rajiv Batra: Yeah. Export guidance we will keep the same guidance which is if you recall, it's between negative 5 to negative 10. For the moment we will stay with the guidance. On our domestic side we would stay closer in the band of 0 to 5 closer to the 5. But we would like to maintain the band of 0 to 5.

Rajni Shivram: Okay. So it's 0 to 5% growth in domestic and negative 5 to negative 10% in the exports?

Rajiv Batra: That is correct.

Rajni Shivram: Okay. And, sir...

Rajiv Batra: That is basis what we can see today.

Rajni Shivram: Okay. And, sir, just wanted to understand like you mentioned there is a lot of pricing pressure in terms of increasing prices in the power gen and we are also seeing new players like Mahindra coming to the MHP, but the raw material prices will go up, so there might be some older inventory which is at low cost, but next year when this hike cost inventory coming to your raw material, then how will we able to maintain the similar gross margins?

Rajiv Batra: I don't think the inventory, in fact, is very significant. Our inventory terms are pretty high, so that is not the cause which would be of concern. We have to continue our efforts to do what we can on the product, give more value to the customer and therefore at least keep our power gen margins where they are. And market alignment is very essential today because there's a certain premium that we obviously deserve and customers are very happy to give us that premium, but beyond the point you just cannot price yourself out of the market. So this is something which we continuously have to work this and there are various means to provide more value to the customer which we do a very good job of.

Rajni Shivram: Okay. And, sir, in the railways in the current budget also we are seeing the diesel locomotives procurement have been halved and the push for electrification and electric locomotives, so in success scenario are we worried about the business in railway coming down going forward because of the electrification drive?

Rajiv Batra: Yeah. I think that's, first of all, all of those are directional in nature and it take years to happen. But closer to us we are in a segment of the market which is not likely to be impacted. The government's efforts are rarely on the main line traction which are diesels which are built by themselves and earlier on on the call like I told you we don't have the complete play of the rail market because the bigger lines in the pipe power on those bigger lines are built by the railways themselves. Where we operate is not likely to be impacted on the short-term. In fact, that's a segment which is growing very, very fast.

Rajni Shivram: Okay, sir. Thanks.

Rajiv Batra: Thank you.

Moderator: Thank you, sir. We have the next question from Mr. Venkatesh from CITI. The line is unmuted.

Venkatesh: Yeah. Sir, please bear with me on this question because it is slightly kind of a long kind of a question. When I actually look at your numbers, for the last 4 years we have not basically grown our profits, so I am wondering is this business getting into a situation where Cummins India's whatever businesses it is operating it is getting structurally challenged because of the changing environment, I mean, you would agree that, you know, the power deficits and all those things are less of a problem today than it was maybe 4 or 5 years back. So as the quality of the great power keeps improving, people using engines and gen sets for primary power go away. Yes, there is a need for backup, maybe, close in line with GDP, but a part of the business is getting structurally challenged because of that and secondly it looks like, you know, we believe that we've read there is Mahindra Susten which has put up a solar backup, battery backup-based power in Andaman where they've got a subsidy with a subsidy the cost is Rs. 8 per kilowatt hour, but they claim that without subsidy the cost of power is Rs. 12. So if you can get Rs. 12 solar-based power with battery backup, what is the need to put up a diesel-based generator, so isn't that a structural challenge for your domestic business?

Last, but not the least, it looks like over the last 3-4 years there have been a lot of global Cummins Inc. factories which have shut down and a lot of that manufacturing has come to India, but it really does not look like any of that business seems to be new product lines are started in Cummins India, so isn't it a fact that Cummins India's growth per se looks structurally challenged?

Rajiv Batra: Okay. So we have three different points which you have made, so let me try and answer that and I will also call on Sandeep, our MD, to help us out on this. So first thing is on the power gen markets, right? The power gen markets over the last 3 years in response to how the economy has been doing has been flattish. Now, as you yourself said that you don't create airports, hospitals, high-rises without backup, so whereas power in the US is very stable but it is the biggest backup gen set market. So I think, as economic activity hits back to the 8 percentage points which our Finance Minister indicated yesterday, so that impact clearly will start to show. What really happens is, as gen sets run less, it's the distribution business or our customer support business which starts to get impacted because the gen sets run less. Our customer support business, however, has been very positively growing between 7 to 9% every year. So the way we manage is working closer with our customer, right, distribution business and lots of it.

Now, the second part is exports, right? Exports clearly in these markets have underperformed and they are nowhere close to where they used to be. Whether you take Europe, in fact, now for the last one and a half years, in fact, last 2 years the Middle East and the Africa are about 50% what they used to be and I think we are struggling a bit with the end user markets or our destination markets on the exports and that is clearly reflecting in our top line as well as on our bottom line, there this the leverage which we used to experience that clearly has been impacted because of the exports in a major way.

Now, on renewable very clearly ultimately it's going to be how you store that power to meet with sudden demands from your equipment when you really need that, right? Today battery technology is not supportive of anything beyond a small steady-state power requirement. So if you were to really bring on a certain load, there is no known substitution of diesel today. But here I will hand this over to our Managing Director, Sandeep, and he could analyze it on this.

Sandeep Sinha: So thank you, Rajiv. And hi, Venkatesh. Sandeep here. I think I am just going to add on what Rajiv said. If you think about CIL, CIL is driven by, you know, one in the domestic market predominantly by three businesses, one is the power gen which I will talk in a bit, the other is our industrial market which is something again I will talk and then our customer support part of the business and then it's dependent a lot on exports.

I will probably start with the last one first, exports. I actually beg to differ on the point you made about declining exports opportunity coming to CIL. We have actually added new product lines what is not visible to you evidently is because our base business has fallen down dramatically. As Rajiv said in many parts of the market, those markets are down 50% of peak volumes, but our business in export are not down to 50% or 60%. So I think what has happened is we have at the new product lines which has helped to keep in this range of minus 10% or so, so clearly we've added new product lines. So I think it may not be evident when we have the profits storm in terms of all the markets, you know, peaking up especially Middle East, Africa, the continent of Africa, Europe I think you will see that there will be, you know, good export growth in those periods for CIL.

On the industrial market I think we have done really, really well. We are growing very strong in this market. We are growing structurally strong because we are adding tremendously higher value to our customers than ever before. We have in the past you could have looked at us as purely an engine supplier; today we have transformed our organization into a system supplier. So think about us giving an engine for a power car application. In rail today we supply the entire power car integrated product, so we've moved up in the value chain which improves profitability and top line growth, both. Now, this business also helps our after-market sales support business because these particular engines run much longer than a standby gen set. What you will see is more growth in the coming years in the distribution business triggered by all the engines that we are putting into the market today.

Now, we will touch on the last part which is, of course, the biggest part of our market which is the power gen market. Power gen market in India has been impacted because of two or three major reasons, one being the real estate, I think, I don't need to educate you on what has really happened to the real estate market especially the high end real estate which is where we were very, very strong because of our high horsepower power gen business. And it's anyone's guess when it will come back, but certainly we feel that it still is about a year before the high end real estate market starts to come back.

And the other one where you require time the gen sets which we are very strong has been in the manufacturing segment and for many years manufacturing has been over capacitized. We believe that market when we bottomed out and we are optimistic in the coming years seeing growth in that particular end.

As far as technology is concerned, I can assure you that Cummins is, you know, we have invested a lot as a parent in new battery technology. And if we feel that the TCO for the customer becomes feasible, we will bring those technologies, right now, we do not see that. But we do have the access to that technology and CIL will be able to sell those products in India as the market matures to that point of time. I hope I've answered your question.

Venkatesh: Yeah. You have answered most of it, but this small part, I mean, there is always that fear that if there is a technology shift in India, Cummins as a group definitely has a technology, but there is always that fear from the perspective of Cummins India shareholder that will this get introduced through Cummins India or will Cummins Inc. Independently on its own, so...

Sandeep Sinha: So I just want to assure you that in all the markets that Cummins India plays in, in the domestic market of India they will continue to be the interface with the customer and no other legal entity of Cummins will do that. So please be rest assured about that.

Venkatesh: Okay. Thanks for the detailed answer. The second question was on once again on this other expenses, I think, this quarter it was around 171 crores, it was 132 crores odd in second quarter, it was 146 crores one year back. Now, while we understood, you know, what are the reasons why it increased, but how much of this, you know, 30, 40 crore increase is recurring in nature and how much is one-off in nature, I mean, like, for example, are we expecting this to remain at 170 crores on a quarterly basis or this will go back to that 140 odd crore level next quarter onwards?

Rajiv Batra: I think I answered that twice since morning, but I will answer that one more time. There are certain catch ups which I told you is growing up and then there are R&D expense sitting out there. The R&D expense I cannot tell you whether it will go up or come down, maybe, it depends on what programmes have been pursued and from quarter to quarter it will change. The management concern, like I said, was a true-up and clearly that 10 crores is not something which you will see again. It would be on a more regular basis prior to the quarters. So hopefully I've answered your question.

Venkatesh: Yeah. Okay. Just one final question, sir, from my side. Recently, there was a clarification given by Cummins India on the stock exchange that this news of Cummins India being interested in the Kirloskar group promoter stake is more of a speculative kind of a news which has appeared in Livemint, but is it possible to also clarify that whether Cummins Inc. is looking at Kirloskar oil engines or even that is not something we need to be bothered about?

Rajiv Batra: Yeah. I think we clarified, I mean, we didn't say it was speculative in nature; we clarified that. At this moment in time we are not looking at that. So we will stay with that.

Venkatesh: So when you are saying we, you are basically talking about Cummins India; I was asking you this Cummins Inc. looking at it.

Rajiv Batra: I don't think there is any interest at this point in time. But all I can say is at this point in time we would reserve our right if our plans were to change.

Venkatesh: Okay. Thank you very much, sir. All the very best.

Rajiv Batra: Thank you.

Moderator: Thank you, sir. We have the next question from Mr. Bhavin from Axis Capital. The line is unmuted.

Bhavin: Good morning, Rajiv.

Rajiv Batra: Hi, Bhavin.

Bhavin: Hi. At the outset, congratulations, Sandeep, for your new role.

Sandeep Sinha: Thank you, Bhavin.

Bhavin: My question, one, is book-keeping question, can you give us the breakup of the exports and you said power gen was 170, how do you break between the mid and the low horsepower, that's my first question?

Rajiv Batra: So you are kind of asking for the exports sales breakup?

Bhavin: Yeah.

Rajiv Batra: Yeah. The exports sales for low horsepower is 70, the mid-range is 100.

Bhavin: Okay. Yeah. Thank you so much. Second is if you can help us more directionally in terms of if you put your business into different buckets like domestic power gen, exports, mid and low horsepower power gen, high horsepower power gen, industrials and distributions, which of these are, I mean, at this point in time in terms of margins you would rate highest to the lowest and if you can ignore the operating leverage negative part looking only on the material margin basis?

Rajiv Batra: You know, Bhavin, we don't get that detailed analysis discussions on margins, so you will have to excuse us on that.

Bhavin: Not an issue. Then the other question is on the power gen, while I really appreciate your detailed answer, if you can throw more light on because we are seeing infrastructure as a sector coming up where you need onsight power that's something which your competitors have been highlighting has been the driving force, so are we actually seeing this as a driver? Secondly, on the power gen what we have been seeing is data centres has been another growth driver, so how large is the data centre business and how is Cummins's position in the data centre business for domestic power gen?

Sandeep Sinha: Yeah, Bhavin. This is Sandeep here. I will take these two questions. I think you are very right. I think our position in this infrastructure market is strong and it continues to be a growth area for us. I think just the sheer size of the real estate business for us was extremely big, so I think that's where my comments came from.

Specifically on the data centre it is a significant growth market for us and we have a dominant share in that of close to 75%. So we feel very, very good about our position in data centres with our global partners because most of them have experienced Cummins in some other part of the world and have now come in to India and we are well positioned with them and our market share in India is a testimony to them.

Bhavin: Sir, would it be possible to give a broad user industry breakup on the domestic power gen like how large will be data centres, the infrastructure, real estate, as you said, was large historically but now come down significantly due to the end market?

Sandeep Sinha: We can bring it next time and will share it with you.

Bhavin: No problem. Afterwards, just a data centre how large it could be for Cummins?

Sandeep Sinha: In India?

Bhavin: Cummins in India, yeah, for CIL you said 330 crores in power gen how large could be the data centre out of this?

Sandeep Sinha: I will come back to you on that.

Bhavin: Yeah. Sure. Just last question. We have seen a change in the US taxation regime and based on that I understand it is too early, but would it impact the sourcing strategy of the parent of moving to low cost like India, China?

Rajiv Batra: Bhavin, I don't think taxation has ever driven the utilization of factories anywhere in the world as far as Cummins is concerned, right? So clearly we have certain products in the high horsepower space and in the low horsepower space. So when that demand comes anywhere in the world, that's something which we continue to service. Otherwise, if there is any other business which has been moved out from the US or anywhere from Europe, it clearly would be a territory we should have to win that business and the business has to be one of the cost quality deliveries. So if we align on that, then most certainly but apart from that I don't think there is anything as yet which we can talk to.

Bhavin: Sure. Yeah. Thank you so much for taking my question, sir.

Rajiv Batra: Thank you, Bhavin.

Moderator: Thank you, sir. We have the next question from Mr. Surjit Jain from HDFC Securities. The line is unmuted.

Surjit Jain: Congratulations, Sandeep, on his new role. Sir, I have a question on the – now that we have a 3% growth in 9 months in domestic business and we have revised the guidance downward from 5 to 10% domestic growth to now 0 to 5% and here it's almost over going into FY19, what kind of guidance we can think for your domestic business?

Surjit Jain: At this point in time we don't want to give you a specific number, but our endeavour would be to win this the 5 to 10% range, right? But as the year starts, maybe, in the next call we will be in a better position to see how is the infrastructure markets in response to all the initiatives starting to behave. So for now we can say 5 to 10%, but give us a quarter.

Surjit Jain: Sure. And the recovery that is taking place in global economy, as you've mentioned in the press with the result, would that make you a little more optimistic about the exports and therefore could there be a chance going forward to tinker with the guidance there in FY19?

Rajiv Batra: Yeah. I think we are seeing certain markets start to come back, right, and we should see some of that come back in about 6 months back. So again next quarter is something where we feel more confident about that, but to the point is that recoveries have started; it probably was a lowest point now.

Surjit Jain: Okay. And one last question is on the gross margins and correct me if I am wrong here is that they have been down by more than, I mean, close to about 160-170 odd bips y-o-y, so is that the assessment correct and so therefore and like you mentioned about the pressures on pricing a 63-64% is this a kind of a new normal in terms of the raw material cost and therefore gross margins of about 37 odd per cent?

Rajiv Batra: Our material margins for the nine months are actually up; they are up by 0.3 percentage points. And, see, operating profit which is impacted by about 1.8 percentage points and that is because of some of the extraneous cost primarily around the employee cost line, right, where we did have to take increases that is about 1.6 percentage where you are seeing the increase. And, as you are aware, we align ourselves to market trends. So we don't see any significant increases that will happen because we are market aligned and it now really depends on the growth where the top lines is. So on the material we are, in fact, better than where we used to be.

Surjit Jain: Sure. All the best to you and that's it from my side.

Rajiv Batra: Thank you.

Moderator: Thank you, sir. We have the next question from Ms. Renu from IIFL. The line is unmuted.

Renu: Yeah. Hi. Good morning, sir.

Rajiv Batra: Hi, Renu.

Renu: Yeah. Sir, first question is on the power gen space coming back here, though if we see the last couple of quarters, on a year-on-year basis the growth has been on the negative territory and as your commentary suggested it might take still couple of more quarters for the gold mark to come back for us, so would it be right to presume that probably the segment in the next 12-15 months would be in mid-single digit growth at best or you think probably in the next couple of quarters we should start seeing sequential growth in the segment coming back?

Rajiv Batra: Yeah. That's what I was kind of telling you in our overall guidance also it would be in the 5 to 10% range, which is really what you are saying in the single digits.

Renu: Right. Because industrial and [mute audio] both of them are growing in mid-teens.

Rajiv Batra: Yes. So they've grown 2 years in the mid-teens and power gen should start growing in the single-digit again. So you are very right on that. It's not going to be at least based on what we can see a hockey stick recovery; it's going to be very gradual.

Renu: Okay. Right. And, sir, if you don't mind, can you share with us, A, this split of 220 crores exports power gen between heavy duty, HHP and also the last year's industrial number as in the last year's domestic sales split was somewhere I think the growth numbers were not tallying through, so I just wanted to re-clarify on those numbers?

Rajiv Batra: This was for the quarter?

Renu: Yeah. As in for 3Q 2017 can you share the domestic sales split between power gen, industrial, distribution and for 3Q FY18 if you can share the split between 220 crores of exports between mid-range and heavy duty?

Rajiv Batra: Well, low horsepower is 70 crores exports for the quarter, mid-range is 100, heavy duty is 27, high horsepower is about in total including the spare parts, as we have said, is about 207 and there's a bits and pieces here and there, right, so that comes to about 420 crores, right? Your next question was?

Renu: Last year's 3Q17's domestic sales split between power gen, industrial and distribution.

Rajiv Batra: Okay. So that is power gen is about 350 crores, our industrial business is about 200 crores, right, and our distribution business is about 324 crores.

Renu: Okay. As in last year I think that was about similar 10 crores from autos, so here at the moment [multiple speakers] industrial?

Rajiv Batra: Yeah. This has combined as part of our industrial, so if you take that all, the industrial is 190.

Renu: Right. Sir, because the point that I was trying to come here is on the industrial side if we see, though that has been among the key core drivers for us, but for the last two quarters on a y-o-y basis comparing only industrial to industrial, the growth has been single-digit levels, high single-digit 9 to 10%, so is that was more of a GST-related issue that customer had gone slow and now we should expect the year-on-year growth to come back to mid-teens or high-teens 15 to 20% range or probably there is a base effect in the industrial side as well?

Rajiv Batra: No. Certainly last quarter GST had an impact on our industrial business obviously, so that was impacted. And if you were to look at the industrial businesses compared to the quarter which is a previous quarter, our industrial business actually has grown 23%. So our compressor business has gone something like 61%, right, so there has been increases. And your point is if you look at quarter one, our industrial business was about 167. So from 167 if I were to look at this quarter which is about 182, in the following quarter we should be at the same level, so there is growth.

Renu: Okay. Right. All right, sir. That's it from my side. Thank you so much and all the best.

Rajiv Batra: Okay. Thank you.

Moderator: Thank you, ma'am. We have the next question from Mr. Deepak Agarwal. The line is unmuted.

Deepak Agarwal: Hello? Yeah. Good morning, gentlemen.

Rajiv Batra: Hello. Yeah. Go ahead.

Deepak Agarwal: Yeah. My first question is on we've seen a very sharp increase in both mining and within industrials, you know, in this quarter. So from a more 12 to 18-month perspective like given the base revenue as we are, how do you see these two segments within industrial like they are going to outperform in access of 20-25% plus kind of revenue levels?

Sandeep Sinha: So this is Sandeep here. I personally believe that we should see continued growth in rail. Mining is a little bit more tender-based and we have a couple of partners, so it's not that are business is spread across; it's a very, you know, coal India driven market. So I would say that mining will be probably more stable growth versus rail I think we have continued high end growth.

Deepak Agarwal: Okay. And my second question is if you can, also, help us understand in terms of overall CapEx that we have incurred so far and, you know, how much we plan in FY19?

Rajiv Batra: This year's CapEx on a forecast basis is about 250-300-crore mark. Next year would be around similar levels about 300-350-crore levels.

Deepak Agarwal: In FY19?

Rajiv Batra: Yes.

Deepak Agarwal: Okay. And my last question is you commented on this material margin which is an improvement in the nine month on 0.3%. Now, based on your procurement and the engineering efforts that you have been doing for last few years and depending on the revenue mix that we are expecting how far do you think this can grow, you know, from in the next couple of years or so?

Rajiv Batra: Because essentially material margins is also driven via mix, mix between exports and domestic. And then like I said, improvements have been making on our products. So I would believe that over the years on material margins has made significant progress, so those efforts continue. It's very hard to say that it will grow by 1%, 1.5% I don't think we would like to commit to that, but we would like to commit to our ongoing efforts and making all the right moves on the product themselves and we've substantially and successfully demonstrated that in the past.

Deepak Agarwal: Okay. Fair enough, sir. All the best. That's it from my side.

Rajiv Batra: Yeah. Can we take the last question, please?

Moderator: Sure, sir. We have the last question from Mr. Abhishek Puri. The line is unmuted.

Abhishek Puri: Yeah. Thank you for the opportunity, sir. Two things, first, if you can tell us a little bit more about this power generation space? We've seen your revenues remaining, you know, constant for the last 5 years, I think, you've spoken about high end real estate and buildings and airports, manufacturing segment, which should be the two key segments that we should be focused on which can lead to a double-digit kind of, you know, growth here or is it that the solar plus battery revolution has taken away a large part of this market share and hence this business cannot grow double-digit?

Rajiv Batra: Yeah. First question is easy to answer. The social business has not been material at all, not at least for now all the four seasons in the future, right? The second question is what is likely to give us significant hit back. Clearly, manufacturing investments for the last 2-3 years had been subdued because if you go into the past, there were huge investments, which, as you can now see from the economy, are not doing too well. In fact, all these large companies which are now realigning the brands become viable again; all there is idle capacities. So until that gets sorted out and the capacity utilizations come back in the economy, that's a strong move or fresh investments being made.

The second thing here especially in the power gen space your question was which are those markets, so one is manufacturing, the other is we've seen strong traction in the data centres because, as we all get busier on our mobile devices and all become huge users of storage capacity, right, it needs to get stored somewhere, so that is something which is consistently being growing for us. And that's the market like Sandeep told you earlier we have a very high percentage in that market. So that clearly is going to help.

The real estate I think and again we shared this earlier a little while away from recovery. So when that starts to happen, but what will happen in the interest is the government initiatives are around infrastructure that should start happening build out over the next 6 months to one year, so that will give you a positive weather. These really are the sectors that we are looking at which would take us into an improvement now whether it will actually get double-digit how fast only time will tell. Actually you can see of how smart cities are built out and all the government initiatives that again [multiple speakers].

Abhishek Puri: Right, sir. Sir, thanks for the detail. Sir, just a clarification here, if data centre is growing strongly for you, is the real estate business seeing a decline right now which is why your revenues are kind of flattish for the couple of years [multiple speakers]?

Rajiv Batra: Yeah. Real estate has been declining.

Abhishek Puri: Real estate and manufacturing?

Rajiv Batra: Manufacturing, like I told you, there is no fresh investments, so that's not increased. Real estate has been declining.

Abhishek Puri: Fair enough. Sir, the traded goods have gone up 70% on a y-o-y basis, what has led to that and is that the reason why your gross margins have improved?

Rajiv Batra: To some extent, yes. Traded goods really is our B-series engine which we used to do a lot of improvements on them, you know, fitting to that in-house. We are now actually buying through Tata Cummins Limited which is our own company, so that way the product is more viable for us. So all of that sourcing model chain that have been done on the shareholder's interest. Okay?

Abhishek Puri: Okay. Great. And my last question, sir, for the distribution business, the revenue for distribution business is now higher than the power generation segment, I think, this has happened for the first time and if we look at your parent company, you know, global, you know, other companies also when I compare, distribution segment typically or service business typically is almost 40-50% of power generation plus industrial put together. In India I think it has touched almost 70% for you in the current quarter, what is driving this strong growth in distribution and whether this kind of proportion of services business versus the actual equipment sale is it sustainable?

Rajiv Batra: See, this quarter like I explained to you distribution in this business has been like huge catch up model and that's because GST had impacted the revenues of service contracts in the previous quarter, so the distribution business this quarter at about 325 crores, significant growth for the previous quarter. So that is not something which is going to repeat itself, but the fact is that, as you put more engines in the market, as the industrial businesses keep growing, right, industrial businesses in those segments of mining, rail and compressor there are huge users for the distribution service. So, yeah, it will grow. But don't take this quarter as a benchmark because this quarter was a big catch up, right, this quarter [multiple speakers] something like 46%. Okay? So thank you so much.

Abhishek Puri: I understood. Thank you. This is very helpful. Thank you and all the very best.

Rajiv Batra: Thank you.

Sandeep Sinha: Thank you.

Moderator: Thank you, sir. Thank you, participants. That does conclude the conference call for today. Thank you all for your participation. You may all disconnect your lines. Thank you and have a wonderful day ahead.