"Bharat Heavy Electricals Limited Q4 FY-20 Earnings Conference Call"

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MODERATOR: **MR. RENJITH SIVARAM – ASSISTANT VICE PRESIDENT, ICICI SECURITIES LIMITED**

Moderator: Ladies and gentlemen, good day and welcome to the BHEL's Q4 FY20 Earnings Conference Call hosted by ICICI Securities. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

I would now like to hand the conference over to Mr. Renjith Sivaram from ICICI Securities Thank you and over to you, sir.

Renjith Sivaram: Good evening all. Thanks for attending this call on a non-working day. We have with us the management of BHEL represented by Dr. Nalin Shinghal, CMD; Mr. Subodh Gupta – Director-Finance; Mr. S. Balakrishnan – Director-Industrial Systems & Products; Mr. Kamalesh Das – Director-Engineering & R&D; Mr. Manoj Varma – Director-Power; and Mr. Anil Kapoor – Director-HR.

We will have initial remarks by the management, post which we will open the floor for question-and-answer. Over to you, sir.

Nalin Shinghal: Thank you, Mr. Sivaram. Good evening friends. Thank you for attending this con call on a Saturday evening. I am Nalin Shinghal, CMD, BHEL and I have with me the directors and other officers of BHEL, whom Mr. Sivaram has already mentioned. Welcome to all of you.

Friends, the global economic crisis arising from COVID-19 pandemic is having an unprecedented impact on most sectors of the economy. As part of the industry, we too are facing disruption in manufacturing as well as project execution. The current crisis is adding yet another layer of complexity to an already challenging environment of an economic downturn coming on top of a long term decline in the traditional business of the company, i.e. thermal power.

In these situations, we have been focusing on transforming the company from a power sector organization to a global engineering organization with immediate focus on diversification of business and improvement in operational efficiency, with strict financial and quality controls. Some of the steps we have taken in this direction have been in the area of business diversification.

We have been working with one of the top-notch consultancy organizations and certain focus areas are identified and detailed business planning is going ahead. These include new opportunities in defense and aerospace as well as railways and some new business segments. We are developing a project centric focus ensuring sequential supplies and IT enabled project management systems among other things.

Our quality first initiative is well underway. We have fully shifted to e-office for improved efficiency and faster processing and the integrated project management software is also going live shortly. A number of changes have been made in our HR policies and systems to ensure a motivated and productive and engaged manpower. Further, a number of enabling provisions have been made in our policy frameworks for ensuring timely and quick response to the market requirements and our customer requirements.

In response to our honorable Prime Minister's call for an 'Atmanirbhar Bharat' and in line with our efforts to create and develop opportunities even in adverse situations, we have floated an EOI inviting global OEMs to leverage BHEL facilities and capabilities to set up manufacturing base in India. Besides helping in optimal use of our capacities, this will create new avenues of growth for the company.

We have received a very good response to the same and have a number of dedicated teams evaluating and processing these responses in a time bound fashion and hope to see results from this effort in the near future. Our manufacturing units have resumed operations at limited levels, strictly confirming to the guideline issued by respective local administrations. Though our project sector sites have opened, availability of labor continues to have an impact on resumption of normal operations. In this hour as a responsible corporate entity the company is taking all measures to ensure the health and safety of employees, associates and stakeholders.

I would like to highlight a couple of examples of our company's efforts in actively contributing to this fight against the current pandemic. We have developed a machine called BHELMISTER which can spray disinfectant liquid in open areas, which has been used for sanitizing open areas with over 100 such units being supplied to various municipalities across the country. We have also collaborated with CSIR to manufacture an electrostatic disinfectant spray machine for sanitizing indoor areas. These products and many others have been delivered to various civic bodies and corporates and we have earned widespread appreciation for the same.

During FY20 we have been able to nearly match the order inflows to that of FY19 despite sharp decline of nearly 14% in the IIP of capital goods. The total worth of orders booked in FY20 is Rs. 23,547 crores out of which power segment has Rs. 13,784 crores, industrial sector Rs. 8,757 crores and exports Rs. 1,006 crores.

Some of the major orders received in the power segment are 2x660 MW TG package for THDCIL Khurja project; FGD packages for about 10 GW capacity; boiler modification for about 3 GW capacity and ESP retrofits for about 2 GW capacity of power plants; Erection package for TG and reactor side equipment for 2x1000 MWe Kudankulam Units 3 & 4.

I am happy to inform that we have received notice to proceed for the 1x660 MW Sagardighi project just yesterday and our teams are well prepared to take up this job in a time bound manner with extensive ground work already having been done. This is a project valued at Rs. 3,480 crores which had been on hold since December 2018.

In the industry sector, which has been identified as a core area of diversification and growth for future, order booking has clocked a 25% growth over the previous financial year, with total order booking of Rs. 8,757 crores, which is the highest in the last 9 years. This includes highest ever order booking in the defence, solar and transmission verticals. Though margins are a challenge in the renewable sector, the company is working on the same.

In international operations, execution of Tishreen projects for 2x200 MW oil side boiler based thermal power plant in Syria had restarted in the previous year.

With this, the total order book as on 31st March 2020 stands at Rs. 1,08,443 crores out of which power sector is Rs. 86,914 crores and industry sector is Rs. 13,346 crores with Rs. 8,183 crores from export projects. In addition to the above, we are favorably placed in 2x660 MW NTPC Talcher main plant package and many orders for FGD and boiler modifications. Tendering is in progress for 2x800 MW NTPC Singrauli; 2x800 MW NTPC Lara and 1x800 MW SCCL Adilabad extension and 2x660 MW Pench, MP. Tenders for FGD for around 34 GW, mostly from government utilities are also in advanced stage.

During the year the company has focused on timely and sequential project execution as its top priority, since we believe that the topline is a derivative of the same and the mantra for sustainable growth. To mitigate the negative impact of turnover due to customer recognition for only sequential supplies in the current scenario, the company has aligned its revenue policy in line with requirements of Ind-AS 115. This has not only ensured optimum shop capacity utilization but also resulted in savings on unnecessary and untimely incurrence of costs and cash outflows.

Coming to the financial performance:

The turnover for Q4 2019-20 is Rs. 4,594 crores against Rs. 9,910 crores during Q4 2018-19. Turnover at the end of Q4 FY20 stands at Rs. 20,491 crores against Rs. 29,423 crores during the previous year.

In spite of lower topline and value addition, which is lower by about Rs. 4,700 crores as compared to the previous year, the company has been able to contain and limit its loss at Rs. 662 crores due to initiatives such as disciplined budgetary controls and efforts at provision withdrawals. The company has focused strenuously on cash collections, addressing the concerns expressed by stakeholders on the receivables management. The cash collection to billing ratio achieved in FY20 is 114%, the highest in the last 10 years.

The collectable debtors have gone down by more than Rs. 3,400 crores, which amounts to a 22% reduction on FY19. The elevated levels of contract assets are primarily due to skewed payment terms (in projects from TANGEDCO and NTPC, Railways etc.), non-sequential executions, and delays in verification of documents by certain customers. It is also pertinent to mention that receivable management is a concern across the industries especially infrastructure and for other EPC players also.

The focus of the company has been on controlling and reducing overheads by monitoring each and every line item of expenditure. As a result, I am pleased to share that operating expenses in

FY20 are lower by more than Rs. 2,300 crores, a reduction of almost 47% as compared to FY19. The company is committed to carry on this momentum and generate better returns through institutionalized cost reduction efforts in a competitive environment.

The company's material cost has seen an increase during the year going to 67% as compared to almost 61% in the last year. The higher material cost has impacted the gross operating margins mainly due to lower volumes because of COVID in the current year, and to some extent due to depleting margins. However, the company has initiated steps on multiple fronts to tackle the increase in material cost through value engineering and design optimizations as well as pre-bid tie-ups and seeking rate reduction from vendors.

The company has been following prudent factors of provisioning with respect to amounts not likely to be realized and at the same time also focusing on withdrawal of provisions already created so as to ensure better quality of receivables and a healthy balance sheet. The withdrawals during FY20 have been more than Rs. 2,200 crores which is the highest in last many years. The net provision creation during the year has been only Rs. 255 crores against Rs. 1,836 crores in the last year.

The company had also focused on increasing the other operational income during the year, which has been maintained at elevated levels similar to last year despite lower overall volume of operations. The vendor recoveries and liability write backs of Rs. 532 crores have in fact exceeded the net provisioning requirements of Rs. 255 crores.

As mentioned earlier the company during the year has mapped its operations to cash flows especially for topline. This has enabled the company to sustain its operations and end the year with positive cash balance. The operating cash flows have been higher by Rs. 1,000 crores from last year. FY20 operating cash deficit at Rs. 2,875 crores vis-à-vis the deficit of Rs. 3,855 crores in FY19. Cash focused operations ultimately have helped the company retaining its debt free status in the times of overall liquidity crunch especially when the company is also channelizing timely liquidity for MSME and other vendors. Due to this, the creditors have gone down by Rs. 2,100 crores as compared to the previous year. It is worth mentioning that BHEL is among the few companies which despite all odds enjoys a debt free status due to better treasury management.

Thank you once again for joining us in this conference call. We will take questions now.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. We take the first question from the line of Mohit Kumar from IDFC Securities. Please go ahead.

Mohit Kumar: Sir, you have quantified Rs. 4,000 crores as the impact of the COVID, but the COVID impact I think started from 23rd or 24th March. It lasted only for seven to eight days. And sir, do you have any revenue target for FY'21 and how is the work proceeding in this quarter?

Nalin Shinghal: Well, you see the COVID impact actually is not just 23rd March onwards. We had started facing supply problems right from January, from suppliers from China, then from Italy, then from various other European countries etc. also. So that impact in our case has been much longer than just that one week's impact.

As far as the current quarter is concerned, yes we have mentioned that we have only started with very limited labor. The first almost one to one-and-a-half months was a complete washout. So there is lot of stress in the current quarter and I think the performance will be affected.

Mohit Kumar: Is there any revenue target or execution target for FY'21 which you are committing to?

Nalin Shinghal: You see the FY'21` targets are now under revision. Some targets had been formulated, but the budget is under revision given the situation. There is a very drastic change from the previous situation. So I think we should be coming out with the revised targets very shortly.

Mohit Kumar: And my second question pertains to working capital side. Sir, how much is the debtors right now and what is the breakup between the State and Central PSUs?

Nalin Shinghal: I will ask the Director Finance to answer that.

Subodh Gupta: Right now, talking of the net debtors, it is Rs. 36,471 crores. Last year, at the same level, it was Rs. 38,615 crores. So there is a reduction of almost Rs. 21 crores as compared to last year.

Mohit Kumar: Can you give the breakup between the Centre, State and Private?

Subodh Gupta: If it is a trade receivable, right now we are disclosing two categorizations in our balance sheet because of the new Ind-AS 115, that is trade receivables and contract asset. Contract asset is un-billed revenue. If I give you the number of trade receivables last year, it was Rs. 15,796 crores, this year it is Rs. 12,378 crores - a reduction of almost Rs. 3,418 crores, which the CMD has already mentioned in his opening remarks, a reduction of almost 22% over the opening.

Secondly as far as contract assets are concerned which we call as unbilled revenue, because of the deferred payment terms and the delay in the verification of bills or the documents not approved by the customers, which goes to unbilled revenue. So the contract assets have gone up by Rs. 1,274 crores, so there is a growth of almost 4% to 5%. In March 2019 it was 22,819 crores and March 2020 it is 24,093 crores. So basically when CMD was referring to the cash collection to net billing ratio, it is the highest in last 9 years at 114%. It means basically whatever is due for collection, there is an improvement over collections. So collectible debtors have gone down. But the contract assets have gone up because of the kind of payment terms in the new orders, what we have across all the business sectors, that is a hit on the company.

Mohit Kumar: Right sir, and my question was it possible to give a breakup between Central PSUs, and State PSUs of this entire receivables?

Subodh Gupta: Shall I tell in percentage or what you need?

Mohit Kumar: Percentage is good enough.

Subodh Gupta: So state utilities if I see, last year it was 50% now it has come down to 47%. Centre PSUs it was 33%, now it is 34%. Private customer 12%, it has come down to 11%. Exports 6%, it has gone to 8%. So the state share has come down from 50% to 47%.

Moderator: Thank you. We take the next question from the line of Jonas Bhutta from Phillip Capital. Please go ahead.

Jonas Bhutta: My question is again on the receivables part and it is slightly a convoluted question. So if you can tell us what is the amount of retention within contract assets, the retention amount, and the comparable number?

Subodh Gupta: Retention amount as on March 2020 is Rs. 15,700 crores.

Jonas Bhutta: And what was it last year sir?

Subodh Gupta: Last year it was Rs. 14,900 crores approximately.

Jonas Bhutta: So the question is this number of almost Rs. 16,000 crores has remained at these levels almost for four years?

Subodh Gupta: **A**ctually, whatever we are executing, we are collecting money annually, but at the same time it is getting added also, whatever withdrawals happen at the same time with the same rate also. During this time in fact what we have done on the retention part, the billing was Rs. 3,256 crores. This means Rs. 3,256 crores is what we put it in from the last year opening and further there is a reduction in the deferred billing because of the skewed payment terms about which I told you.

Earlier 10% used to be the deferred portion, now in most of the contracts, it is 15%, 20%. The customers are demanding financing indirectly from BHEL. That is the whole stress. It is because of that reason the whole stress has come on our cash flows. And those are zero deviation tenders. So we are managing with that. Our company is working towards liquidation of these debtors, and things should improve in future.

Jonas Bhutta: But my question is between FY'17 till '19 which was that 3-year period, which is when the terms of trade were not as poorly skewed to BHEL as they are now. So the company commissioned almost 17,000 MW. One would have assumed that after two to three-year period of lag of warranty of provisioning, this number should have reduced because your sales number between FY'19 and FY'20 is down by almost Rs. 10,000 crores, Rs. 9,000 odd crores.

So at some point sir what we are not able to understand is despite having commissioned 17 GW of power in the last four years, our retention numbers still remain high despite sales being lower than what it was two years ago. You know we understand the accretion to retention in FY'20 because of poor terms of trade. If you can help us understand?

Subodh Gupta: I am coming to the point what you have raised. This retention amount basically is towards two activities, towards the trial operations and the performance guarantee testing. It has been noted that there is a reluctance on the part of customers not to offer the plant for performance guarantee test, because the customer also knows the moment he offers the plant for **PG** test, he will have to pay the money. And ultimately he makes one or the other excuse to try to link also with the delayed execution.

Ultimately the level of provision what we are doing so that our balance sheets maintain at least a quality, as CMD also has mentioned in his remarks regarding the quality of debtors in the books. So at least on prudent and qualitative basis, we are provisioning such debtors. The numbers, which I have told you basically, we are also factoring all these things into the provisions also.

So that is helping the company rather and at the same time parallelly, we are taking all appropriate action to recover this money. I would request Director (Power) if he can throw some light on this particular aspect, what efforts we have made and how the money has come during the year'19, & '20.

Manoj Varma: So just to supplement what Director Finance was telling, in fact the capacity addition confined to the commercial operations declaration, that is a factor which all customers prefer to have, and then they add the capacity. But definitely the performance guarantee test they are not pursuing or not allowing us to proceed with, for some or the other reason because lot of dues are to be paid by them on those accounts.

So this is being taken up. In fact, we have discussed at our Board level also yesterday and we are preparing to go to the Ministry along with MOP and then CEA to have a common guideline on these things, that limited timeframe should be allowed post the COD so that obligations on both the sides are met even to the extent of realization of funds. I think that attempt will ease out the position in one or two years' time.

Jonas Bhutta: What is the amount if these PG tests go ahead out of this Rs. 15,700 crores how much of it can be recouped, can you quantify that and that will be my last question?

Manoj Varma: As of now, around 5% to 7% in the next one year.

Jonas Bhutta: Just about Rs. 750 crores?

Subodh Gupta: No, not Rs. 750 crores, I think he is not asking the percentage. No he is asking how much amount what is the question, can you repeat it again?

Jonas Bhutta: Out of Rs. 15,000 crores, how much out of Rs. 15,700 crores how much is stuff for the want of PG test, so if these PG tests go through?

Subodh Gupta: How much we are targeting for the current year?

Jonas Bhutta: How much is stuck and how much are you likely to get?

Subodh Gupta: We will share this number afterwards, you can take this number from corporate finance, they will share with you. Right now we do not have the exact breakup.

Manoj Varma: As of now it will be around 30% but exact we will share.

Nalin Shinghal: In fact, in this current scenario this is a major target we are looking at: how to make sure whatever pending works are there or whatever else is there to be completed and to get this revenue, go after this revenue collection. This is a very major target for us for which specific teams have already been set up.

Moderator: Thank you. We take the next question from the line of Abhishek Puri from Axis Capital. Please go ahead.

Abhishek Puri: Sir, my question is on the prospects list that you have given. Some of these projects have been in the pipeline for quite some time. Just wanted to understand what is the status for some of these projects like Singrauli, Lara, Adilabad and Talcher and what are some of the conversations with clients who are telling you in terms of like NTPC has not even ordered a single plant in the last 3 years apart from maybe Patratu?

Nalin Shinghal: I will ask Director Power to take that one.

Manoj Varma: You have rightly observed there are many projects which are to be finalized and they are getting deferred over last year also. In these meetings also we were quite hopeful for Talcher 2x660 MW. While Government of Orissa had cleared with NTPC, though they had taken it currently in their March Board meeting but it is still to be finalized and converted to regular purchase order. So still some considerations at their ends are going on and we are hopeful that it should happen in at least if not in this month, at least in next two, say by Q3 of this current fiscal year.

For Lara, Singrauli, NTPC have already taken a pre-bid review in the month of April and that also should fall in the H2 of this year. In fact, Singareni project is, 1x800MW, while talking to the management, they were indicating since they are going for brownfield projects of Kothagudem and other places, Singareni also is to be decided.

So we are quite hopeful that by the end of this financial year all these things should be in a quite favorable stage as far as tenders and finalization is concerned. And besides that I had a recent conversation with their Energy Secretary, Mr. Suleman some two months back. They are also quite hopeful to float this tender, if not by Q2 definitely by Q3. We expect a lot of tenders to be finalized in this current fiscal.

Abhishek Puri: Sir, as a follow up to this, is there a rethought with NTPC also in terms of thermal power projects given some of the round the clock bids for storage plus renewable have come and very competitive somewhat similar to or lower than that of thermal power plant?

Nalin Shinghal: So as of now we do not have any such indications, but if something does happen then yes we will all get to know. But in fact you know the figures are actually a little bit misleading if you look at the 2.90 rupees or whatever, they are actually at the end of the day not the real figure. So we are also looking at that figure in detail.

Abhishek Puri: Secondly in terms of the diversification as per the expression of interest that we had put out, you did mention that there is a good response. So could you indicate in what segments we are looking at, which companies are there in terms of and what are the kind of deals that we are offering in terms of whether we will do land, lease out, whether it will be a JV, whether it will be a sellout of some of the factories, if you can just throw some light on that please?

Nalin Shinghal: So we have, as I was saying, over 50 responses already and two major areas that the responses are falling into are defense & aerospace, and railways and which is actually in line with what our own objectives are. There are a number of other responses also in various range of areas but these are the two which we are very positively looking to take forward. There are number of responses also for contract manufacturing.

We have been very open as far as the model for collaboration is concerned and in terms of locations and model for collaboration, we are quite open and this discussion is progressing quite rapidly. I think in the near future, for contract manufacturing, for shorter ones we should have things moving very quickly, and thereafter the longer ones. That should happen. So as far as companies are concerned, we have very big names also internationally, but however I am not at this point in a position to give you names, which you can understand, I am sure.

Abhishek Puri: Yes, sure that is helpful. My last question is on the industry segment. You have seen quite a big dip in the margins, so what is this related to and the solar business or the other segments that we are operating on, are they really profitable the way we are getting orders today given the competitiveness is pretty high in the market?

Nalin Shinghal: So I will put it this way that lot of these areas are, as you said yourself, very competitive, but going ahead we are looking at more niche areas which would not be that competitive. We are looking at defense, we are looking at aerospace, we are looking at railways. We are looking at areas which would be less competitive going ahead, understanding and learning from the fact that we have been in areas which have become extremely competitive and we need to move into areas which are not that cut throat.

Abhishek Puri: So any cost cut initiatives that we have taken I mean apart from what has already been achieved because we have cut costs in a meaningful way in the last couple of years in the last 3 years and a large part of that has also been due to the provisions being coming off? So any such efforts in the current year especially given this disruption that we have seen in the first half? This is my last question.

Nalin Shinghal: Cost is a very major challenge for us, as you pointed out. For the current year, this is the major issue and we are looking at cost cutting across the board. Major focus areas will have to be material costs, because that is the biggest chunk of our cost. So we would be looking in terms of procurement cost as well as design, so we have specific teams working in areas for design for FGD, for various other areas where we face cost challenges. So that is the most important exercise going ahead.

Subodh Gupta: Actually shall I even contribute, in addition to what CMD said. It is not only on the provision number, even the other expenses. Last year it was Rs. 2,140 crores, this year it is Rs. 1,896 crores. So almost a reduction of Rs. 250 crores in other expenses mainly because of the budgetary discipline as mentioned in CMD's opening remarks. So the reduction is in provisions also, in other expenses also, in power and fuel, indirect materials also. So there are many areas; on each and every line item, work has to be done.

That is the reason that despite a heavy reduction in topline as compared to last year, and we have missed on gross operating margins, but at least we are able to reduce and minimize the losses and that is one of the reasons that we have brought the losses to the level of Rs. 662 crores. So ultimately that is one of the factors. Net debtors are almost lower by Rs. 2,000 crores as compared to last year. That is a very important factor. So as CMD has explained, the work is still continuing. We will be more aggressive during the current year also. The strategy of cost reduction has to continue, it cannot stop.

Moderator: Thank you. We take the next question from the line of Renu Baid from IIFL. Please go ahead.

Renu Baid: Sir, my first question would be to understand a bit from a long term perspective, specially to Dr. Shinghal. It has been over a year that you have taken charge and the market outlook has actually worsened with respect to the power sector. So you have highlighted few areas of diversification but they will take time.

So can you just highlight a bit more in terms of the medium long term strategy on which you were planning to work to help the profitability of the company to improve, anything more concrete to talk about in terms of specific cost actions or programs or in terms of revenue drivers that we are looking at beyond just the current environment that we have seen through?

Nalin Shinghal: So I have largely covered the issues that we are looking at when we said that in terms of revenue drivers, first we are looking at diversification in a big way. New product areas, and in the existing areas also, we are looking at increasing our share of services business, even in the power sector. We already have technology development program for high efficiency power plants also because that is the very major area for the country going ahead.

So if you look at new growth areas, we talked of railways, we talked of defense and we are also looking at areas like EPC in oil and gas. In addition to that we are also looking at asset management. First focus is on sorting out issues with regard to the execution and collection of receivables. So this entire area of commissioned projects which was just discussed, that is a very major focus area we are looking at, going forward. We have more than Rs. 40,000 crores of BGs, so we are looking at BG vacation in a very major way.

And so ultimately these areas have to be taken up in a very focused manner with teams dedicated to these jobs. And underlying this whole thing I think going forward, we are looking at development of people down the line, and a very close linkage between performance and rewards and involvement and motivation. So that has to be the driver of this whole thing. And in addition to that, I already mentioned about the quality initiative. So these are the various initiatives that we are looking at going forward to get us out of this situation and actually set us on the road to becoming an engineering organization.

Renu Baid: Sure sir, now being a bit more specific. EPC execution has been painful to us in the last couple of years especially when we have looked at projects in Telangana, mere situations of getting LD imposed etcetera. Now that we have two large NTPC projects, be it at Maitree or Patratu under execution, how are we, as in what actions have we taken to ensure that there would not be similar slippages on the EPC side and the profitability on some of these projects could be contained and within control? So what has been the corrective actions on the EPC side which we are planning to undertake for the new large projects in pipeline?

Nalin Shinghal: On the EPC side as I mentioned the integrated project management software, that is the first and the most important initiative, so that we are able to establish a real time control on our project execution. The second thing is advance preparation. So for example, for Sagardighi a great amount of ground work is already done even before the notice to proceed has been received, the geo-technical engineering has been done, the teams are already working on taking off from the ground level on this project itself.

And for example, for Maitree project, we put in place a Project Director to improve the local level of control which we are again doing at Yadadri which is a very major project coming up. So it all comes back to what we said about more effective project focused performance.

Manoj Varma: I would like to supplement what CMD sir has just summarized. Besides this, in the ongoing projects, to absolve ourselves of the penalties of the LDs, we have already taken up with most of the customers in the first week of April itself for the entire projects which we are taking care to support us with the idling charges and definitely give us time extensions on account.

While there is a stretch on the migration of labor but they are also being reviewed and trying to curtail. Despite all these conditions also, we have been successful in adding the capacity of first unit of 4x270 MW Manuguru and resurrection of Kothagudem 1x800MW also besides Namrup. So these activities are going on. There are certain pain points but I think gradually in a month or two, we should be in a position to resurrect ourselves in the existing projects also.

As far as Maitree is concerned, definitely it was at the foreign land. There were certain conditions or things which were beyond our control as the law of the land prevailed so there with the help of MEA and the Government of Bangladesh, we have tried to support the manpower to evacuate, but simultaneously we are taking a review to rebuild the manpower availability from nearby projects, and also by the nearby countries also which our contractors are now being advised to. So I think that also will be on track quite soon.

Renu Baid: Sir, in terms of the shortfall utilization levels, so I understand until May it was more impacted. So currently as we speak for June, July and the coming months, what is the current utilization levels that we are seeing with the required people on shop floor and how are you expecting the activity level to ramp up in the subsequent quarters? So by when are you expecting you should be back to a 90% or 100% at normal activity level, what is the expected timeline based on the situation on ground across projects?

Nalin Shinghal: Not just the social distancing, but then there are issues regard to supplies, overseas supplies as well as local supplies. There are number of issues which are being faced in the shop floor while our units started functioning right from April onwards, as various units have come back on stream. If you are looking at an 80% to 90% operational level, I think that will still take some time to come to that level. It is not going to happen immediately.

Manoj Varma: More so I would again like to supplement what CMD has replied. While we are taking up all these activities, we are addressing the works in progress, which were left unattended due to the onset of COVID, and the finished goods, which we are trying to now send as per the site requirements. But, definitely the raw materials which have to come from the vendors ranging from ABC category, they are getting affected. Till the time our ancillary units and other bought out items suppliers are fully stabilized this process will take time to bring us at the 90% plus efficiency.

Nalin Shinghal: But the effort at the same time is to ensure that whatever project execution is happening will not suffer on account of anything on the shop floor. So that we are ensuring a very close coordination between our production units and our project sites to ensure that there is no mismatch there despite any other issue that we may be facing.

Renu Baid: Right, because last year we had sufficiently topped up in terms of the factory output in anticipation of site work. So this year that cushion should be available so broadly would it be right to say it would take at least 6 months for you to get the site level activity up and running to close to 80% plus levels?

Nalin Shinghal: It is not actually very clear at this point in time. So, at this stage it really becomes very difficult to forecast what is going to happen. But yes, all efforts are there to do that as quickly as possible.

Manoj Varma: I will prefer to supplement again here like CMD sir has informed, it is precisely geographical domain wise. If you look into the Telangana projects, Bhadradri and Yadadri, there yes, the government has also been quite positive, and they have supported the retention of migration of labors. As far as the U.P. is concerned, there also they have come up quite positively while in Maitree as I said it was beyond our set being a foreign land and some of the other sites being in Tamil Nadu, yes we have been adversely affected.

So while the two input channels for any project, whether it is shop capacity which is being taken care by the units even on the revenue and storage basis, that thing is being taken care for optimizing the shop capacity. But the bought out items definitely, it is pertaining to most of the vendors. So now it becomes only the manpower as one of the key elements which has to be ensured back to the sites to take care of these things.

Renu Baid; And if I can ask one last bookkeeping question. There has been restatement of cost items for FY'19. The staff expenses have been restated from Rs. 6,200 crores to Rs. 5,500 crores. So is this adjustment just for the Rs. 760 crores of the wage provision impact which was there in FY'19?

Subodh Gupta: Earlier what was happening, this was shown as a provision. Actually it was not a provision, and from provision, we have removed and put it to employee benefit. There was a withdrawal of some Rs. 760 crores of provisions last year, actually the withdrawal should happen from the employee benefit expense, but it has gone into provision heads.

Renu Baid: No, last year we had added this as staff expenses and hence it was Rs. 6,200 crores so in the restated numbers now they are back to Rs. 5,500 crores?

Subodh Gupta: Yes, last year it was Rs. 6,261 crores, the revised number is Rs. 5,502 crores.

Renu Baid: So this is largely for the provision impact of Rs. 760 crores?

Subodh Gupta: Yes, Rs. 760 crores, whatever provision for reason we have created in earlier years, last year it was booked under provisions head, now it is under natural head of expense.

Renu Baid: Got it. And just one clarification of the Rs. 760 crores?

Subodh Gupta: So that the personal payments are comparable like-to-like basis. Without any impact on bottom line. It is a reclassification in the category.

Renu Baid: Right I got that sir.

Subodh Gupta: And that we have disclosed also in the notes.

Renu Baid: Agree and last year in the fourth quarter '19 conference call you had also clarified that of the Rs. 760 crores, about Rs. 540 crores was pertaining to financial year '19 itself. So that becomes more like a recurring cost. So just wanted to clarify, does that number also still stand good.

Subodh Gupta: In that year itself it was booked to natural head, at that time because the wage agreement was concluded for supervisors. It was that Rs. 540 crores was already forming part of special payment. This is basically the withdrawal of provisions, last year basically when we show the provisions, provision means impairment provisions, not for the liabilities. So last year liability provision was also classified here. This year we have put it at appropriately at right place so you are able to compare the personnel payments on like-to-like basis without any impact on bottom line.

Moderator: Thank you. We take the next question from the line of Lavina Quadros from Jefferies. Please go ahead.

Lavina Quadros: Sir, I just wanted to understand directionally how are payments moving from the Centre and State utilities. I mean are the government entities little reluctant and delaying payments for the given Corona or are you seeing collections which possibly should have come in the March quarter coming through in April and May. Just wanted some color on that?

Nalin Shinghal: Director-Power will take this.

Manoj Varma: Indeed, we have two major customer clienteles. One is the Central utility and others state utilities. So while our major debtors are on account of 3 major customers deep down south, it is Telangana, Tamil Nadu and the Andhra Pradesh governments. So while most of the projects are funded through PFC and REC they have been until now supporting us in spite of certain constraints.

But when it comes to their equity payment to the extent of roughly 20% on each project they are unable to meet and I think that can be supplemented by their ratings also in the market. They themselves are struggling for most of the fund management and sometimes some of the funds on account are also being pruned. So as of now if you put this, it is roughly going to a five-figure digit on account of these three customers only.

So State utilities on these accounts are we are suffering while states like UPRUVNL or Maharashtra Genco they are quite okay, they are quite able to meet our fund requirements. So the major contribution of state utilities debtors is from major three customers.

Lavina Quadros: And sir, just to understand this expression of interest for using your facilities by global companies, I know it is very early in terms of timeline but would it be fair to say this might fructify logically only over 12 to 18 months and earlier it will be a little harder or how are you looking at it especially given the whole Corona environment?

Nalin Shinghal: Actually that will really depend on the nature of the engagement. There are some requests for contract manufacturing for example, that could happen very quickly. But if you are looking at setting up a JV for a major new area, that will certainly take time. So it really depends. Some of the smaller ones will come through quicker, the bigger ones will certainly take some time to come but may not be as long as 18 months, it may be faster than that. That is our target.

Moderator: Thank you. Next question is from the line of Darshan Mehta from Ambit Capital. Please go ahead.

Darshan Mehta: In terms of FGDs can you throw some light on what margins do we enjoy and how is the competition now as I initially understand that the competition was quite high and then it dropped a little. So are the Chinese players who are also bidding or is it more restricted to Indian companies?

Nalin Shinghal: Director Power will take that.

Manoj Varma: Indeed, for the FGD equipment being associated with the main power equipment for emission control, almost 125 GW tenders have been in the market of which 80 GW have been finalized and 30 GW we have won. Another 32GW odd are being finalized and some 12.5 GW are roughly in the advanced stage of ordering. While we maintain the major chunk as of now at roughly 38% or so, but there has been some competition. GE is also there, L&T is also there, and BHEL is also there. In the current year only we have been able to get an order from NLC and another we have been placed favorably from MPPGCL just last week. So that way we are targeting on contract basis and attempting it.

Darshan Mehta: Okay so it is more like big companies who are basically going for bidding so but then are the margins like sufficient enough or still there is like cutting edges in terms of margins?

Nalin Shinghal: As I had mentioned in the beginning, you see this is one of the key areas, you see we are all aware that the margins are very thin on these projects and this is therefore a very major area for redesign and cost reduction. There is a very focused and targeted project that we have taken on for cost cutting and redesign in this area.

Manoj Varma: To supplement, while we have taken them on these thin margins, but we are quite hopeful to develop most of the items now in-house. We have been pursuing NTPC as one of the major central utility who has ordered roughly 70% of these tenders already and rest are going to the state who always look upon as a big brother to the Central utility. So once these specifications of in-house items are agreed upon by the Central utility, I think we will improve upon our margins also. So that will also add on to the bottom line for these products.

Moderator: Thank you. Next question is from the line of Ankur Deora from Bank of America. Please go ahead.

Ankur Deora: Thank you so much. My questions have been answered previously.

Moderator: Thank you. We take the next question from the line of Viraj Kacharia. Please go ahead.

Viraj Kacharia: I just had a follow up on the FGD what the earlier participant asked. So the projects which we already have in hand, how is the execution taking place, if you can just provide some color how has because a lot of these projects have a certain deadline which the utilities have to meet? So how is the execution happening or the implementation happening on ground? That is first. And second is say from central utilities or are we seeing any support in terms of more lenient working capital terms or relooking at the overall margin structure because of the kind of impact one may have of COVID on the project execution cycle. So if you can just provide some color on that?

Manoj Varma: Yes, definitely. In fact, the very first project which is coming in the country is Dadri 2x500 MW and the unit I which we are executing in fact was slated for roughly 25 months initially. But then our Honorable Minister for Power had taken a review on the 12th February, even the central utility NTPC was a part of that team, wherein it was brought to his kind attention that the timeframes, which have been given for FGDs, were too tight.

While Dadri had to get completed by May, but because of these conditions, the customer is also extending equal amount of timeframe on that. Rest of the projects also, the drawings and the placement of POs is already under progress. So I think whether it is Karanpura or whether it is for Telangana customers or for these standalone contracts which we have won, they will fall in line and we are quite hopeful to be on time on those things.

Viraj Kacharia: So basically what you said is there is six month extensions which the customers are given for execution of these projects?

Manoj Varma: That is being considered through CEA now, they have themselves given because it was considered for Dadri but when it was reviewed at customer level also he also in fact endorsed that these time lines were too skinny. So now it is going from 36-37 months they are going for these.

Viraj Kacharia: That has nothing to do with the COVID impact?

Manoj Varma: No, the COVID will go separately like Dadri was to get completed in the month of May but having been in that same overlapping slab of time, this will get definitely this extension.

Viraj Kacharia: Okay and is there any waiver of penalty because the timelines one, so typically there is a 31 months contracts and it gets delayed by 6 months. So is there any cost escalation with the customers are also allowing and any waiver of any penalty because of delay?

Manoj Varma: No, I will tell you because Dadri being the first project, it is yet to be affected so there is no question of penalty as of now it is yet to happen and for most of the items where POs were placed, so these terms are agreed upon. Now once we get relaxed from the current situation and the tenders in the offering, which are yet to get finalized, there we will see the trend and then we will see what is to be taken care.

Viraj Kacharia: Okay and any extension of working capital term say from NTPC or the likes for FGD projects?

Manoj Varma: While we have put a request to them I think there is another meeting scheduled in the next week so let us see in the apex level meeting if these things can be taken care favorably by NTPC.

Moderator: Thank you. We take the last question from the line of Ashwini Kumar from Nippon India. Please go ahead.

Ashwini Kumar: My question was, you have 447 sets on the coal powered plant with 125 GW of capacity. So there the spares retrofit and modernization opportunity, what is that opportunity and how are you exploiting that? And my second question is that Indian Railways is embarking upon significant CAPEX in the next 5 years to 7 years or 10 years the way they are projecting it to be. So what kind of opportunities do exist for BHEL in this sector?

Nalin Shinghal: Let me take the second one first. Indian Railways we are looking at a range of opportunities on the rolling stock front where we are already manufacturing locomotives as well as traction equipment, as well as for EMUs. And we are also looking at, in fact the coach itself, whether we can do that, and then there are opportunities in the diesel to electric conversion. We see opportunities arising in the signaling front. So there are number of opportunities that we are looking at going ahead in the railway front. And as far as the coal power plants, the modernization opportunities, I will request Director Power to take that.

Manoj Varma: In fact, you were talking about the R&M, indeed lot of scope is coming as far as the lifecycle of these existing thermal power plants is being pruned out now. Whether it was Panipat or whether it was Kothagudem or whether it is Bhusawal, Panki, Patratu so all these are brownfield projects and many more to follow to the extent of 48 GW. So while the time is being taken to get these effected from respective state or central utilities, we have taken up regarding the R&M which used to be roughly 3% to 5% earlier of our contribution say in the 12th plan. Now it has grown to roughly 8% to 10% of our contribution as far as the order book is concerned.

So even last year also, there is a jump of almost 10% over the order booking in the spares business. So this year also we are quite hopeful but we are targeting it to grow to from Rs. 3,100 crores to Rs. 5,000 crores. While we have taken up with all respective state utilities also, even we are attempting for some rate contracts with some central utilities, so this definitely has a better margin and a faster pace of execution and it will definitely add to the bottom line in the current fiscal year, we are quite hopeful on those lines.

Ashwini Kumar: Sir, just one thing to Mr. Shinghal. Sir, you had highlighted that raw material cost reduction is one major area. Now given that the scale of operations are roughly half or 40% of what they used to be in the peak, so how will this raw material or the component cost reduction happen because everybody who is a supplier Tier-1, 2, 3 is down to the extent of 40% or 50% of peak volume.

So how do you get it done from 67 to 61 or 67 to 63, 64 wherever you intend to take it to, because the scale is not in your favor, so it has to be an internal exercise, it has to be an external exercise with the vendor. So can you help me understand that what is your thinking on this aspect?

Nalin Shinghal: So if you are looking at the 61 and 66, 67 they are on a similar scale. You know we have been on a similar scale for some time. In fact, what we are looking to do is a number of areas we are looking to further aggregation, centralized ordering negotiations, whatever process we can look to long-term contracts. So contracting is a major area we are looking at. I had already mentioned that procurement is one area and the second is design.

Because we find that in number of areas we have margins in the design itself. We have been over designing as compared to all our competitors. So without any of the quality performance suffering and not allowing any reduction in that aspect, there is a very major exercise going on, on the design part. So between these two, we expect to bring our costs into the ranges that you know all of our competitors are also able to achieve. So that is what our efforts are.

Ashwini Kumar: So this looks achievable in 12, 18 months or will it take more in terms of your design efforts?

Nalin Shinghal: Should be, actually the ordering cycle is such so this is going to happen in line with the ordering cycle.

Moderator: Thank you. Well, ladies and gentlemen, that was the last question for today. I would now like to hand the conference over to Mr. Renjith Sivaram from ICICI Securities for his closing comments. Over to you, sir.

Renjith Sivaram: I thank the management of BHEL for taking out time to answer all the questions and I thank all the participants, despite being a Saturday to participate and thanks for your time.

Nalin Shinghal: Thank you everyone for your patient hearing and this interactive session and your interest in BHEL. And again for being on a Saturday evening. Thank you so much.

Moderator: Thank you. Ladies and gentlemen, on behalf of ICICI Securities, we conclude today's conference. Thank you for joining. You may now disconnect your lines.