"CEAT Limited Q3 FY-21 Earnings Conference Call"

January 20, 2021

MANAGEMENT:	**MR. ANANT GOENKA – MANAGING DIRECTOR, CEAT LIMITED** **MR. KUMAR SUBBIAH – CFO, CEAT LIMITED**
MODERATOR:	**MR. ASHUTOSH TIWARI – EQUIRUS SECURITIES**

Moderator: Ladies and gentlemen good day and welcome to the Q3 FY21 Earnings Conference Call of CEAT Limited hosted by Equirus 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 now hand the conference over to Mr. Ashutosh Tiwari from Equirus Securities. Thank you and over to you Mr. Tiwari.

Ashutosh Tiwari: Thanks Margaret. Good afternoon, everyone. On behalf of Equirus Securities, I welcome you all on the CEAT Limited's third quarter earnings call. From the management we have Mr. Anant Goenka – Managing Director and CFO – Mr. Kumar Subbiah, and also members of IR Team. Without further ado I would like to hand over the call to management for their opening remarks. Over to you Anant.

Anant Goenka: Thank you Ashutosh and good afternoon everyone. A very warm welcome to CEAT's Q3 FY21 earnings call and thank you for joining us today. I am Anant Goenka and we also have our CFO, Mr. Kumar Subbiah on call with us. I hope all of you continue to be safe and in good health.

As usual, we will start with the brief remarks from me and Kumar post which we'll be happy to take some questions. As we mentioned in the last quarter, we completed the CEAT and CSTL that CEAT Specialty Tyres Limited merger in Quarter 2 FY21, hence all our Quarter 3 FY21 and all comparable periods, standalone financials have been restated to reflect this. All the growth numbers that we will be indicated today, both financials and volumes will reflect growth on a like to like basis. FY21 has been an unprecedented year in every sense of the word. While due to the global pandemic the first three months of the fiscal were a washout. As restriction released, we saw strong and persistent demand pickup over the next 6 months. There was strong replacement demand recovery on account of pent up demand as well as increased preference for personal mobility in both rural and urban areas.

Further during the festive season OEM demand for the passenger segment also picked up. Though demand for new commercial vehicles has been soft economic activity has picked up and existing commercial vehicles are plying on roads with higher frequency which is largely indicated by increased toll collections. This has also led to increase in the replacement demand of CV tyres as well.

As a result our standalone revenue for the quarter stood at 2,212 crores a year-o-year growth of 26.4% and a sequential growth of 12.6%. The entire growth has been volume driven. On a year-on-year basis we saw strong growth across all channels, both our OE and export businesses grew by over 15% while replacement grew by over 35%. Our overall year-on-year volume growth was over 28%.

From a segment perspective, we witnessed maximum growth in CV tyres followed by PCUV and two-three wheelers. Our off highway tyre business recorded a sales growth of 42% in

Quarter 3 on a year-on-year basis. Domestic farm and export specialty segments witnessed strong demands.

Our overall raw material cost went up by about 1.5% sequentially on a per kg basis. Higher raw material price plus adverse product and channel mix led 213 basis point contractions on our cross margin. Given the current increasing raw material trajectory, we will monitor the pricing and margins closely over the next few quarters. We took a price hike at the beginning of December and then again at the end of the month to mitigate some of this effect. On a sequential basis, our standalone employee costs went up by about 20 crores, an increase of about 12% and this was on account of inclusion of employee costs of our recently commissioned projects. The second was some amount of higher sales incentive payouts and provisions. We believe that the productivity benefits of these people investments will come over the next few quarters. As sales and production activity picked up our standalone other expenses also went up by about 7.6% sequentially. However despite these increased expenses are standalone EBITDA margin contracted only marginally on a sequential basis and was at 15.3%. We ended the quarter with a standalone PAT of 128 crores.

On plant utilization, all our facilities have been operating at very high levels of utilization throughout the quarter and all our new capacities are ramping up well. As per our estimates over the last two quarters, we have been successful in improving our market share on the back of extensive distribution channel and strong supply chain management. However we continue to be cautious and monitor the market and demand situation closely. We continue to also make inroads into OEMs while cultivating strong relationships. During the quarter we partnered with Nissan to supply our securitized range of tyres for all models of Nissan Magnite. We also partnered with Hyundai to supply tyres for their I20 model. The Royal Enfield Meteor was also launched on CEAT in the last quarter. Our focus on investing in our brand continues and our investments around this have been consistent irrespective of the external environment. Last quarter, we had Amir Khan joining us as our brand ambassador. In the current quarters CEAT continued to invest in its association with sports. On lines of our IPL relationship we partnered with the Jio Women's 2020 challenge as their strategic timeout sponsors.

Going digital is also very important for us. Our digital initiatives have been well received. For example, we have a strong integrated fleet management module, a tool to track key accounts, tyre tracking and scrap tyre inspection was made live. Additionally online sales through e-commerce marketplaces for two wheelers and four wheelers have been also taken well in the last quarter.

Sustainability has also emerged as an important agenda for us. As you all may know, we came out with our maiden integrated annual report in FY20 wherein we shared details on various activities CEAT undertakes to ensure high standards around environment, social and governance practices. We continue to make conscious decisions and investments to ensure that we promote sustainability across all our functions and processes. With this, I would like to close and handover the rest of the comments to our CFO.

Kumar Subbiah: Thank you Anant. Good afternoon, ladies and gentlemen and thank you for joining our call covering our Quarter 3 results. I will share some financial data points with you all first post which we can enter Q&A session.

Let me start with the revenue, our consolidated net revenue for the quarter stood at Rs. 2,221 crores, a growth of 26% versus the same quarter of last year and 12.3% sequentially over the previous quarter. The growth was largely driven by volumes. And gross margins for the quarter was 45.5% on the consolidated level and expansion of about 260 basis points versus the same quarter of last year while there is a contraction of 90 bps sequentially. The sequential gross margin decline was on account of increasing raw material costs, coupled with unfavorable channel and product mix. Despite the adverse environment, we have been able to manage our debt levels well in the last nine months of the current financial year. We continue to exercise caution while managing all our costs and also very judicious in spending our cash. We further optimized and brought efficiencies in our working capital during the quarter, as a result our consolidated gross debt during the quarter came down by Rs. 250 crores that is Rs. 1500 crores, which is after considering the total CAPEX of about 175 crores during the quarter which indirectly means that it was funded from our internal accruals. As a result of reduction in debt and also increase in our network, our consolidated debt-to-equity ratio improved further to 0.49 versus 0.59 as of the previous quarter.

For the full year, we expect our capital expenditure to be in the range of about Rs. 500 crores relating to projects and additional Rs. 150 crores are expected to be spent as a normal and routine CAPEX.

Now let me move on to our operational expenses:

Our consolidated employee expenses increased by 12% sequentially, as explained by Anant, this was primarily on account of additional employees that we had engaged in our new facilities at Chennai and also the expanded facility at Halol and Nagpur and in addition to that, we also incurred some performance and related incentives and bonus that was provided during the quarter.

With production ramping up across all our factories our consolidated other expenses went up by 8% year-on-year, largely on account of higher level of activities. During the quarter, we also incurred rupees 12.3 crores towards VRS to our employees that has been classified as exceptional costs. Now that all our expanded facilities have been slowly commissioned in a phased manner, our consolidated depreciation went up to Rs. 87 crores during the quarter as a drop in our debt level and also a reduction in interest rate on our borrowing, our consolidated finance costs were down to 42 crores for the quarter from 45 crores in Quarter 2.

I'm also happy to inform during the quarter credit rating of AA for long term and A1+ plus for short-term has been affirmed by both the credit rating agencies CARE and India Rating with the stable outlook. We ended the quarter with a consolidated profit before tax of 202 crores, which compares favorably with 82.6 crores of the same quarter of the last year and Rs. 132 crores of PAT versus about 53 crores in the same period of last year. Now let's open the floor for Q&A. Thank you.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Jai Kale from Elara Capital.

Jay Kale: My first question is regarding the demand scenario, how are you seeing it? In the year like this you have probably clocked the highest service revenues for ending the year and in that context going forward, how do you see the sustenance of this replacement demand? Since OEMs are on a yearly basis not yet back to the peak level. So going forward the sustenance of the replacement demand over the next 2 years how are you planning for it and in that context, how would your CAPEX outlay, any revisions in that since last two quarters back you had cut the CAPEX guidance but given the current moment and may need revision in that?

Anant Goenka: Yes, so demand scenario continues to remain quite positive. I'd say that replacement demand continues to remain on the current lines that have been seen in the last few months. With respect to OEM demand there's been a slight slowdown on two-wheeler OEM demand in the last month-month and a half time. But long-term we are very confident of OEM also being strong and CV commercial demand, which has been weak I am sure will pick up over the next few months' time as well. So over the next, 6-9 months, we feel quite optimistic with respect to the overall demand situation for tyres across categories, including exports, OEM, and replacement. To that extent we are comfortable in terms of our capacities also I think our timing was quite good. We were a little concerned in April last year but I think our CAPEXes have been timely and we are in a good position to utilize, the new plants that we've set up.

In terms of our plans, out of about 3,500 to 4,000 crores that we had planned, we should be doing, we finished about 2,200-2,300 crores of CAPEX already. About a 500 crores CAPEX is what we expect to do this year. We've done about 250 crores, balanced 250 will be happening over the course of the next quarter or so. The next couple of years, we will continue with our CAPEX plan of about 700 crores per annum is what we are looking at based on whatever has been agreed. Now after that there is no decision that we have taken on any CAPEX beyond that. But it will primarily involve completion of our Chennai expansion. We have a little bit of our truck radial and off-highway tyres that will undergo some expansion. These are largely the downstream equipment's that are pending as capacities go up.

Jay Kale: And the second question is on the raw material side, you mentioned that raw material basket increased about 1% to 2%. We were factoring in a little higher increase. If you can run us down, how it will shape up in the next couple of quarters and that would be my second question?

Anant Goenka: Raw material has run up quite a bit in the last quarter, rubber prices have gone up to about Rs. 160 per kg from 130; crude has also been consistently going up from $42 to over $50 a barrel. To that extent, both our key raw materials are going up. I think from Quarter 3 to Quarter 4, we can expect an average increase of about 10% on the entire or material basket. By the end if you were to look at our March end buying prices, it could be over 10%.

Moderator: The next question is from the line of Basudeb Banerjee from Ambit Capital.

Basudeb Banerjee: Just to continue with the previous questions. You said, there were a couple of price hikes in beginning of and end of December, so if you can quantify them?

Anant Goenka: They were approximately 3% so, early December it was about 1% and then again towards the latter half was around 2% to 3%, so slightly around 3% price increase across all categories except two-wheeler.

Moderator: The next question is from the line of Siddhartha Bera from Nomura.

Siddhartha Bera: First question was on the replacement side, you indicated 35% growth but could you help us with what will be the growth at the retail level? That will be the first question and do you think the similar tonnage we can do in Q4 also given that it is usually a seasonally strong quarter, so your thoughts on this?

Anant Goenka: For us, this is a largely retail level growth itself. We don't have any difference between a retail level of growth and there's been no inventory accumulation out here. To that extent, I would say the retail level and our sales would be similar. Current demand situation in the market continues to be positive. So I don't see a major difference between this quarter and next quarter in terms of volumes, so trend seems to continue to be positive.

Siddhartha Bera: And inventory levels, how are they, I mean, are their normal levels or still lower and what will be that level if you can help us?

Anant Goenka: Our FG inventory levels are very low. We've been short of tyres. Even if we could manufacture more, we would have sold more. So inventory levels are uncomfortably low and yes, if we continue to sell this way, we may continue to fall short. But yes, we will be more comfortable with some more FG inventory, maybe 50 to 100 crores more.

Siddhartha Bera: How many days of inventory do normally do the channel keep on a normal basis?

Anant Goenka: About one month.

Siddhartha Bera: So now it's still slightly less than a month is what you are indicating?

Anant Goenka: Yes.

Siddhartha Bera: Second set is on this CAPEX side again, so if I'm correct, you indicated 500 plus 150, 650 crores of CAPEX for this year, out of which we have done 250 crores in the first nine months, is it correct?

Anant Goenka: That's right. A little bit more than 250. I think we'll be doing maybe about 200 in the next quarter, 200-250 range.

Siddhartha Bera: But if we have done 250 only then for the next quarter, we should be doing more than about 350, so the total CAPEX is around…?

Anant Goenka: No, this is project CAPEX.

Subbiah Kumar: 250 crores are against the project CAPEX of 500 and against the normal routine CAPEX proportionate amount, about 100 crores has been spent already in the first nine months. Balance amount would be spent in the quarter.

Siddhartha Bera: Understood and lastly on the price hike side, you indicated near about a cumulative 3% increase, across passenger car and TBR segment till date. So do you think this is sufficient or do you think you will need more price increases to offset the cost pressures? Any thoughts on that and why two-wheeler we have not taken any hikes, is it demand is weak and any specific reason if you can highlight?

ANant Goenka: Yes, so we do need to take another 3% odd price increase during this quarter to offset the entire raw material price hike. That will be decided based on competitive situation in the market, so we will be evaluating it during the course of this quarter. And on the two-wheeler side again because of the competitive situation, our pricing was considerably higher than our benchmarked SKUs or products of competitors. So to that extent we have not taken a price increase yet.

Siddhartha Bera: Last question, so the CAPEX of 700 crores you indicated for next year, this is the project CAPEX and maintenance CAPEX will be on top of that.

Anant Goenka: That's right. We do about 150 crores of maintenance CAPEX every year.

Moderator: The next question is from the line of Nishit Jalan from Axis Capital.

Nishit Jalan: My question is primarily on the replacement demand. What according to you is actually driving such demand or in other ways, are you seeing that such strong demand partly because of import ban? And if you can give some color in terms of how our two-wheeler and PV and PVR segments doing because we used to have a lot of imports PVs and PVR but two-wheelers I put used to be much lower. So just wanted to understand how much of this demand you are seeing is because of import coming down and domestic players benefiting, so some sort of color on that because the replacement demand is clearly surprised on the upside in the last few months.

Anant Goenka: That's right. So replacement has been particularly strong. I think one is, we feel because of personal mobility requirement going up amongst consumers and that is affecting the passenger car segment, two- wheeler segment particularly. Second is rural as I said, has been strong. If you look at farm segment, even replacement demand has been strong, OEM demand, so farm has grown very nicely. CV as I said had grown amongst the fastest of all categories. We are also seeing across category group and import restriction has also been a boost to a certain extent. Maximum imports were coming in on the passenger car segment. Two-wheeler, there was very little import, so to that extent, two-wheeler did not really get affected. But approximately I would say, 3% to 5% of the market would have at least got vacated because of further opportunity came up because of import restrictions that have come in.

Nishit Jalan: So, Anant do you mean that if import ban would not have been there instead of 35% you would have still grown at 30%-32%?

Anant Goenka: Yes. Maybe about a 5% impact approximately.

Nishit Jalan: But what according to you, is it because that after lockdown and things not moving, your truck tyres, basically there were lot of replacement which was required because these kinds of growth, we have not heard of or we have not expected. I'm sure even you would not have expected this kind of growth. So what according to you could be could be the sustainable growth once we catch up the base, will we go back to the 7%- 8% kind of a growth which we used to see in the industry or do you think something really different has happened in the industry because of which we can see a higher replacement growth for maybe 1 or 2 years?

Anant Goenka: See, I think this kind of growth, right now demand is continuing to be strong. So I can tell you for the next quarter we are quite optimistic. You look at quarter after that also we're talking about a very low base effect that will come in. Most companies have shown (-30%), (-40%), (-50%), so to that extent Quarter 1 will also be very strong and possibly some of that will also go into Quarter 2. So I can tell you that the next nine months are looking to be relatively positive, a lot because of the low base effect as well. Beyond that it is a little difficult to see. If you look at the last 2-3 years have also been relatively muted. Last 2 years average growth would have been under 5% CAGR. So to that extent also, we're talking about a longer term relatively lower base that has been there.

Nishit Jalan: That has been helpful. Secondly, on the RM cost and price increase side, on the price increase side what we understand is that MRF probably has not gone ahead and taking a price increase. Is it because of that in two-wheeler side, is the competition really different because of aggressiveness of MRF and Max is coming into play? I just wanted to understand what is the reason or what is the difference in two-wheeler segment that you have not taken a price increase despite such strong growth despite are really struggling for capacity and stock, so just wanted to understand that part.

Anant Goenka: We like to maintain some kind of benchmark pricing differential with competition on certain key sizes or most sizes in a way. That is a differential that we don't want to overprice our product versus competitors, even if the market may be able to absorb it. To that extent, that is a call that we've taken. Let's say, for example, you decide you will price certain 2% higher than competition. We don't want to change that gap. To that extent, we try and maintain that approximate benchmark.

Nishit Jalan: Any details in terms of, what sort of market share gains would have seen in the replacement market or do you think in that industry growth itself is so good that industry itself is also growing at close to 30% on a YOY basis?

Anant Goenka: Yes, so industry also has grown well. I'm aware of that. But I would also say we have gained market share. I don't have Quarter 3 data but I would surely say that in the first two quarters of the year, we would have gained at least 2% market share across all categories, passenger car will be even higher, maybe 3% to 5% market share increase, at least in the passenger car space.

Moderator: The next question is from the line of Mukesh Saraf from Spark Capital.

Mukesh Saraf: My first question is regarding the mix between your replacement and OEMs. You'd mentioned that replacement was over 70% in the first half and you would expect it to kind of come off to the usual 60% levels but where are we now in that mix?

Anant Goenka: To that extent, of course that has got adjusted because if you look at OEM demand was quite strong in October-November festive season. We have come off to close to our normal mix. We don’t share generally exact data but approximately it is 60-25-15, 60% in replacement, 25% OE and 15% exports are our average and we will be very close to that kind of mix.

Mukesh Saraf: So we're back to normal there and so going forward in terms of gross margins, the mix shouldn't really have an impact. It'll just be raw material costs and whatever price hikes we are able to take?

Anant Goenka: That’s right.

Mukesh Saraf: Secondly, again on the expenses side, if I look at your employee cost is up 33% where you did mention it included some bit of incentives as well. But if you could give some sense on where you can stabilize in terms of employee costs, I remember you also mentioned last time that you do kind of look to add employee costs 3-4 months ahead of time. But some sense on where we can stabilize on how much do you see the ramp up, further in terms of these plants coming up and how do you see this going forward?

Anant Goenka: A large part of this is variable as volume is growing; we need to have more people. So some plants we were operating for example 6 days, we've taken that up to 7 days. Our Chennai plant is ramping up. Sp as we take up that, we will continue to see further increase in at least employee cost in that space and some amount were provisions which has been slightly higher than we expected, numbers being a little better. We have done some provisions for bonus payouts and other kind of sales incentive payouts that would be happening.

Mukesh Saraf: So we can expect the absolute employee costs to continue to kind of rise from here as you ramp up the facilities?

Anant Goenka: Yes, possibly. Kumar would you like to add on that?

Subbiah Kumar: Employee cost for the quarter was approximately about 178 crores. If you look at the same period of last year, we were around 145 to 150 crores and if we continue at current level of operations and it could be around 170 crores kind of a quarter level but if we operate at a higher level, there'll be an increase in employee cost in line with the increase in volumes.

Mukesh Saraf: In terms of advertising expenses, I think on a normalized basis it's about around 2.5% of sales. Are we back to those kinds of levels, that is our other expenses? Are we back to those kind of advertising expenses or do you think there is much more to be ramped up there as well?

Anant Goenka: No, we want to maintain 2.5%. In fact, we went above that. Quarter 1 was of course zero advertising but Quarter 2 we were up over 3% as a percentage of sales but overall for the year and going forward also we will maintain the same advertising as percentage of sales.

Mukesh Saraf: And nine-months we should be around the 2.5% right now.

Kumar Subbiah: In nine-months it would be little higher but on a full year basis it will be in line with 2.5.

Moderator: The next question is from the line of Shyam Sundar Sriram from Sundaram Mutual Fund.

Shyam Sundar Sriram: My first question is on the pricing environment, per se. While the RM inflation has been quite strong, we have shown a lot of confidence in picking up prices. Is it also a reflection of the import restrictions that has squeezed the supply side that is giving more confidence to take up the prices and do you see more leeway in terms of picking up the 3% increase that you talked about in the next 1-1.5 months to completely offset the cost inflation?

Anant Goenka: The price increases have not been sufficient actually. While we take in a 3% price increase, it's not enough to offset the raw material price increase. We need to do some more price increase over the next, this quarter to make up for the increased raw material prices.

Shyam Sundar Sriram: The leeway to take up prices is also because of the supply squeeze that has happened due to the import ban and is there any other supply constraint from the domestic tyre makers or there is no supply constraint from the domestic tyre supplier manufacturer per se?

Anant Goenka: Overall I think the industry has enough capacity to serve the market. I believe everyone has done a fair amount of investments. In our case I can say that in certain categories we have been short of supplies, particularly in the passenger car space.

Shyam Sundar Sriram: On the replacement growth that you spoke about specifically personal mobility driving up growth because these vehicles part additions has been coming down over the last several quarters because of the new vehicle sales are being lower but still we are seeing currently a very strong replacement growth. Does it mean that a lot of people who had not gone for replacement earlier in the last year, there is an accumulation of those, that demand that is now playing out, we shall then start easing after 8-9 months into going forward.

Anant Goenka: The question was not very clear to me.

Shyam Sundar Sriram: The vehicle park addition. The population increase has been coming down because of the new vehicle sales being lower over the last several quarters, in LTV and PV, total OEM sales, new vehicle sales but we are seeing a very strong replacement growth a 35% growth that you mentioned. Is it because some of the earlier replacement that should have happened last year which got postponed is all now coming into, which is getting replaced now and because of the need for personal mobility and will this taper down going 8-9 months after from here on?

Anant Goenka: I think people are replacing more because they are traveling more on personal transportation. As a result, I don't think it has as much to do with new vehicle demand. New vehicle demand has also been positive but the replacement is happening because people are using more of their personal vehicles. As a result of higher usage that is also helping. I was talking to one of our customers and OEM customers so they were like, during the lockdown, people didn't have much to do because they couldn't go out so they would go for drives for example. Now you go for a drive your car is getting well-utilized, tyre is getting well-utilized and that's the only outing which people had. I'm just giving you an anecdote but I'm saying that the utilization of vehicles, personal vehicles has gone up and as a result, people need to replace tyres more than what we've had to.

Shyam Sundar Sriram: Between truck bias and truck radial how has the demand trend been, is there a greater preference for TB deals over TBR or any such shifts that you're seeing?

Anant Goenka: No, both segments have seen high growth surprisingly. We always thought truck bias is going to show negative or flat growth for longer term but I think with strong demand in CV segment also both have grown very well. Truck radial has grown more than truck bias but both are showing (+30%) kind of growth numbers.

Moderator: The next question is from the line of Prateek Poddar from Nippon India Mutual Fund.

Pratik Poddar: Two bookkeeping questions. One is on your debt. If you can just help me understand how much of the debt reduction was due to working capital release and how much was due to FCF generations in the first nine-months? Second question is, is this the peak level of debt now? Whatever debt levels we end up within year FY21; is it fair to say that, that would be the peak debt and from here on if at all either the debt would remain flat or will come down?

Kumar Subbiah: Overall if you look at, for the current year, our debt level came down by about 370 crores if you start from 1st of April till May and working capital production is also closer to the number, around 300 crores kind of a reduction and working capital that we have managed to do it in the first nine-months of the year. If you look at overall our capital expenditure is around 450 crores in the first nine-months including routine operating CAPEX for specialty business. There is no one-to-one correlation but it's correct to say the debt reduction is very close to the reduction in working capital. Therefore, that way internal approval has been utilized to repay the debt and cash profit is very close to the CAPEX that we have incurred during the year. Both of them we had managed to match and the differential amount is kept in the form of a cash. That's one way of looking at it. The second question is whether we have reached the peak, no. As Anant had also indicated, so far project CAPEX that we have incurred in the first nine-months is around 250 crores only. Our total CAPEX for the year is going to be little less than what we had initially indicated in terms of range. We indicated up to 500 to 600 crores. We are now looking more at the lower end of that range and as we incur CAPEX next year and the balance part of the quarter, in the next quarter and depending on how much CAPEX that we incur, got our cash profit that it may move up, also depends on the working capital. It is unlikely to be substantial there could be some increase in debt level and in the next 2 years, if we manage to keep our CAPEX around 700 crores, that Anant had also indicated earlier. Ideally if you are able to generate enough cash, then we should be able to sustain the debt or increase it only to the extent of working capital. That's the way we are looking at debt at this point in time.

Pratik Poddar: Basically then whatever levels you end up with in FY21 of debt mostly you're there. From there on the increase should not be substantial, it could be slightly at max.

Kumar Subbiah: Working capitals, we currently are at finished goods inventory is quite low and it’s important for us to increase it and even raw materials inventory also needs to go up at this point in time, it's a very tight supply situation for even raw materials. Those things will take up and when you sell more, your receivables also increase. There's some amount required to meet the increase, the working capital requirement in due course of time. It won't be substantial; it may go up but it won’t be very substantial.

Moderator: The next question is from the line of Kashyap Javeri from Emkay Investment Managers.

Kashyap Javeri: Just one clarification, when you say there is additional price increase of about 3% needed, that's on the total portfolio, right?

Anant Goenka: That's right.

Kashyap Javeri: For the Quarter 4 any indication on the cost index? Should it be equivalent to the gross of amount of that 3%?

Anant Goenka: Can you repeat again the second question?

Kashyap Javeri: Based on that 3% needed, the price increase needed, the cost increase in the Quarter 4, or cost index in the Quarter 4 should rise by about roughly about 1.6%-1.8% types?

Anant Goenka: If I'm answering your question right, I am saying that from Quarter 3 to Quarter 4 we expect about a 3% price increase. That is equivalent to say about a 6% price increase at 10% raw material price increase, it is about a 6% increase needed in net realization. That's about 3% is done. We have another 3% left or we need to do but by the end of March; so this is the average of Quarter 4 raw material price increase that I am talking about. There can be more than 10% impact going on to say Quarter 1 of next year also because March exit raw material will be even higher.

Kashyap Javeri: In terms of natural rubber, we have seen some cooling off happening probably because of the new production would have started coming in. Any view that you have over there, how has been the inflow or production in this particular season and what bearing could it have on the natural rubber prices? Because even in the month of January, they're still hovering about Rs. 150-155 a kg kind.

Anant Goenka: What is your question?

Kashyap Javeri: In terms of rubber production and consequent…

Anant Goenka: These are the peak starting months that are there right now. Rubber prices are largely dependent on, it's a global commodity. It doesn't affect as much as what is happening in India. There can be some impact but it is a lot because of what is happening in China in terms of demand in other global numbers and weather patterns say in South-East Asia, in terms of any floods or crop disease etc. To that extent I think output has been quite okay. Kumar, would you like to share anything here?

Kumar Subbiah: I think Anant you have largely responded Indian rubber prices normally mirror the international prices. Therefore unless the international prices cool down, we don't expect the local prices to significantly change. One of the other reasons for the local prices to be higher or international prices to be a higher is also on account of steep increase in the freight rates and some premium over the published SICOM prices. The local prices have marginally come down but when we indicated our average cost for the quarter and also exit cost for the quarter, it is based on Rs. 152-153 per kg kind of a rubber, natural rubber level. Even if the production goes up in India because if demand is higher and the international prices are still firm, the local prices may not come down unless international prices come back.

Moderator: The next question is from the line of Hitesh Goel from Kotak Securities.

Hitesh Goel: Can you tell us nine-month volume growth numbers for replacement demand, OEM, and exports?

Anant Goenka: On average we would be at a positive growth across on average but we won't be able to share the nine-month data specifically. We don't share the exact data points so I have given you approximate data points. Maybe you can just compute it out of that.

Hitesh Goel: Because I think over a volume growth in nine-months is 3%-4% only, am I right?

Anant Goenka: Yes. It's just moved into positive territory in the last quarter.

Hitesh Goel: OEM would be a decline, right? I mean, it's a replacement which should have grown in double digits because you said OEM, they were also positive growth in nine-month.

Anant Goenka: I can get back to you on that. I don't have the data here but yes, replacement has clearly surpassed. So yes, OEM would be negative.

Hitesh Goel: Was there a growth in export segment also? Just trying to get nine-month data (46.04) you're projecting forward?

Anant Goenka: I think exports would have been negative as well marginally. Net-net replacement is far exceeded and it is a much larger category.

Moderator: The next question is from the line of Jinesh Gandhi from Motilal Oswal Financial Services.

Jinesh Gandhi: With respect to this VRS scheme which we are running so by when do we expect benefit to reflect in P&L? And what could be the saving because of that? And secondly looking at the tax rate in this quarter does it mean that entire benefit of CSTL accumulated losses is now accounted for or we would take it in the subsequent quarters?

Kumar Subbiah: As far as VRS is concerned, it's an ongoing activity for us. We have some high cost for factories and particularly in bias plants except in the last quarter otherwise in the previous quarters we were not able to utilize that capacities fully. It's important to keep those factories cost competitive and from long-term perspective, we continued to run some Voluntary Retirement Scheme options, we may give it to employees and that will go on. Every year a certain number of people when they opt for it, those benefits will not be visible, it will reduce the impact of any increase in overall salaries and wages for those particular factories so it's going to continue in older factories, in the next few years or so. So that is point number one and the next question was on?

Jinesh Gandhi: Tax so primary CSTL merger is accumulated? Loss has been fully accounted for in nine-months FY21 or we expect some spillover of benefits in FY22?

Kumar Subbiah: It's been fully accounted in Quarter 3. Since the merger happened on 1st of September and as of 1st of September in that quarter accumulated losses as per the books has been adjusted against and accordingly the tax benefit was also accrued in the last quarter to the tune of around 50 crores odd. We don't have anything more from the merger in terms of tax benefits.

Jinesh Gandhi: Constraint that we have taken already 3% kind of price increase, you are saying full absorption of that already in the market, demand not getting impacted by that? How confident are you of picking another 3% kind of price increase given the demand environment?

Anant Goenka: Yes, the 3% has happened and there's been no impact on the market at this point of time; demand continues to be strong. The balance is tough to say, I don't have an answer as to when we going to take it. I hope we are able to take it during the quarter.

Moderator: The next question is from the line of Chirag Shah from Edelweiss Securities.

Chirag Shah: First question is a continuation, when I look at your EBITDA per ton, it seems to be flattening out over last two quarters and given the raw materials cost pressures that we are witnessing and there is a fact that employee cost can incur from here on if activity improves. How do we look at EBITDA per vehicle? So what are the levers to improve EBITDA per vehicle for us?

Anant Goenka: No, we don't have the data point. We won't be able to share that with you. I think it'll have to be computed by you itself.

Chirag Shah: According to EBITDA per ton is not really changing much, will it continue to improve?

Anant Goenka: Yes, one is you look at our margin. So margin is also reflection of EBITDA per value in a way or so to that extent, EBITDA is flat between the last two quarters. Employee cost while it will go up as we ramp up our factories, it will not go up at the same rate because here we are only adding feet on the street in a way, the people who are on the shop floor. The overall if we grow by say 20%, it doesn't mean our employee cost will go up by 20% it so the employee cost will go up every year based on the normal increment cycles that are there. And the factory will show equivalent growth to a certain extent for that one factory.

Chirag Shah: And over on this German R&D center that we have, can you indicate at what stage of operation it is and when can we expect meaningful contribution from that R&D centers and is it functioning across all the segments like PVs, two-wheelers and trucks or its primarily for PVs?

Anant Goenka: The German R&D center has been operational now for (+3 years) and it is fully operational. We are doing a lot of testing that happens in Europe. These are primarily focused around the passenger vehicle segment but also does other categories. Over time as we look at entering into Europe for other categories, it helps us there. We get a lot of market intelligence and information on what are future tyres that are emerging. We get global capabilities and results. We have people from all over the world who are there in our German office. The capabilities that we get are a lot more diverse. So to that extent, it is fully operational and it will ramp up based on the needs of expansion in terms of other categories as well.

Chirag Shah: It is not meant for India perspective? It's more for products for European market?

Anant Goenka: No, it is for European markets, is a large part of what it does but it also adds a lot of capability to India. We learn a lot on how do you take decisions on which patterns, for example you introduce, how is testing done, do we need to do certain different types of tests in different test tracks around the world? So you will have something in Norway that we may do, Germany that we will do even for Indian market, Indian tyres. To that extent there is a lot of knowledge transfer and capability transfer that happens for India.

Moderator: The next question is from the line of Nishant Vass from ICICI Securities.

Nishant Vass: Anant a clarification on the price hike. You mentioned that 3% hike, ex of two-wheelers, right? So effectively two-wheelers are one-third of revenue. Effective pricing for the portfolio is around 2%-2.5%. To come to a 6% portfolio pricing fees, you would have to do potentially, nearly 4% increase on a blended portfolio basis. Is that understanding correct?

Anant Goenka: Yes, the overall price increase that we would have done would be 3% on average across categories, including two-wheeler, while you've not taken two-wheeler. What I'm saying is we would have taken 1.5% full part of December and about 3% to 4% in the latter part or about 3% in the latter part of December so that may be 3.5% on other categories, which would kind of average out to just around the 3% level on average.

Nishant Vass: You're saying on a portfolio basis, you're at 3%, but you've done higher price increase in other categories and not done a price increase in two-wheelers?

Anant Goenka: That's right.

Nishant Vass: This is a slight confusion. Is then effective requirement of price increase higher on a product basis and just because you're not doing on two-wheelers and you're doing a higher increase in other categories or SAP increase at 6%, is that understanding correct?

Anant Goenka: On average, across all categories, we would need another 3%. Now whether it happens in two-wheeler or it happens something higher across other categories, that's still to be seen that's what's happened in December but I think we will, I mean if there is any price increase then we may look at two-three-wheeler also in this quarter.

Nishant Bhat: My second question is more of a clarification. You mentioned replacement, which has come back to normal level. So, I'm really confused here because replacement has grown double then OEM and export. How has it calmed down or how is that happened? Because the growth obviously is 2X though even the exports.

Anant Goenka: No, sorry. I didn't understand the question.

Nishant Bhat: You had mentioned to a participant that the replacement mix has now normalized back to last year level, in each one you were at 71% and even this quarter, you've grown in replacement by 35%, which is more than two times OEM export. So, how has the replacement mix come down?

Anant Goenka: No, I said that, we would not be able to share data, but in the longer term, what we are seeing is our mix will continue to be at this kind of level. OEM on a year on year basis would have gone back up to normal growth levels. We saw strong growth in OEM; this is year on year growth.

So, last quarter OEM would have been for example, at negative growth levels this year on a year on year basis, both replacement and OEM have shown a strong group. One is at about (+15%) levels, one is at about 25%. So it has moved more towards replacement. The skew that you saw on a quarter on quarter, Q2 versus Q3 that would have got adjusted because on a quarter-on-quarter, we would have shown a higher growth. In the longer term, there will be, we will go back to a normal mix.

Nishant Bhat: One small clarification if I may a squeezing, in terms of the price negotiation OEM has that passed being done, completed, or is there any delay on that account.

Anant Goenka: Sorry

Nishant Bhat: On the OEM side, on the commodity price too, is that seamlessly working?

Anant Goenka: Yes. That is working normally.

Moderator: The next question is from the line of Abhishek Jain from Dolat Capital

Abhishek Jain: How was the revenue mix for the Trucks, Two-wheeler, and PCR for the nine-month FY21?

Anant Goenka: So, category mix, approximate again we wouldn't be able to share with your exact information. We share it on a six-monthly basis, but approximately our truck would have been about close to 35%-40%, two-wheeler is about close to 30% and passenger car is about 15%. So that's the approximate break-up between and the balance would be farm and of heavy tyres.

Abhishek Jain: In a T&B segment, how is the change in its fleet, especially in a TBR versus TBB?

Anant Goenka: TBR has shown higher growth. So, we would be having about 60-40 kind of a mix, 60% bias, 40% radial.

Abhishek Jain: What kind of the growth in the TBR segment in last nine months because, you have added a new capacity, so what is the growth in TBR segment? Because, TBB must be degrowth for India but what is the growth in the TBR?

Anant Goenka: On a year-on-year basis, for Quarter 3, I'm not giving you the nine months because Q1 skews everything. On a year on year basis, we would have grown by over 35% between both the categories, over 45% in TBR and over 30% in TBB approximately.

Abhishek Jain: My last question is related with this dealership strength. How much dealers you have added in last nine months and how's the mix in a rural versus urban?

Anant Goenka: No, so dealers difficult to really give a number because it varies across categories. In two-wheelers you have very small mechanics, small dealers who deal in tyres. So, the numbers there would also be very skewed. But, on average, we would have added even more than 300 dealers plus.

Abhishek Jain: What is the total strength right now?

Anant Goenka: Maybe about 5,000 dealers and then there'll be a large number of sub dealers. What we call them a sub dealer, these are a small, a two-wheeler dealer. That would be a very large number.

Moderator: The next question is from the line of Achal Jain from JP Morgan

Achal Jain: I would like to know that whether CEAT is ESG compliant or not. One more thing that I was to ask was about the replacement and the costs that you are telling us that the raw material costs has been going up and up. So, one question that just came into my mind was whether or not, like the replacement, if there could be recycled or not.

Anant Goenka: As I shared in the latter half of my opening remarks, ESG is very important to us. According to us in governance, we are of course at a very high level. We give a lot of importance to even the social aspects, so areas like diversity, getting people from various backgrounds. We have over 50 people who have people with disability for example, women recruitment or gender diversity is very important. We have over 20% people in our new factories, not only Chennai, but even Halol etc., who are women operating on the shop floor. We also look at people with background diversity. Not only CAs, MBAs and engineers, which is typically what one would look for, but what about people from a liberal arts background etc. and people from different nationalities and backgrounds. To that extent, diversity is something that we invest a lot. On giving back to society through our CSR needs we invest on providing English education to various schools, municipality's schools. We have partnerships with a few thousands of schools around Maharashtra where we train teachers. We look at doing activities around our factories, so just some examples of social work that we do. On the environment front, we have very clear targets that we've taken. We are at the highest level of reporting disclosure but we want to do good for society. It's not just a compliant aspect that we want to do. We want to do the compliance plus-plus because we see the earth deteriorating every day and we want to play a role in making a difference to societies. Whether it is working on how we make our factories more energy efficient, our products, having better rolling resistance which is more fuel efficient, tyres using greener raw materials. So, we have plans across each area that we can impact the environment on ESG.

Moderator: Thank you. Ladies and gentlemen due to the time constraint that was the last question. I now hand the conference over to the management for closing comments.

Anant Goenka: Thank you for hosting the call, Ashutosh and team and thank you all for your time and interest in CEAT. We look forward to catching up with you once again next quarter. Stay safe, stay healthy. Thank you.

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