"Endurance Technologies Limited Q2 FY 2021 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good morning. And welcome to the Endurance Technologies Q2 FY 2021 Investor Conference Call, hosted by Axis Capital Limited. 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. Nishit Jalan from Axis Capital. Thank you and over to you, sir.

Nishit Jalan: Thank you. Good morning, everyone. Welcome to Q2 FY 2021 Results Conference Call of Endurance Technologies. From the Management Team, we have with us Mr. Anurang Jain – Managing Director, Mr. Ramesh Gehaney – Director and COO, Mr. Massimo Venuti – Director and CEO, Endurance Overseas, Mr. Satrajit Ray – Director and Group CFO, and Mr. Raj Mundra – Treasurer and Head of Investor Relations.

I will now hand over the call to Mr. Jain for his opening remarks, post which we can have Q&A. Over to you, Mr. Jain.

Anurang Jain: Thanks a lot. Good morning to everybody. I would like to share details of how we have done in the second quarter and the first half of this financial year FY 2021. In India, in the second quarter of FY 2021, as per the SIAM data, the two-wheeler industry sales de-grew by 2.4% compared to the previous financial year, scooters de-grew by 18.3% and motorcycles grew by 4.03%. The automotive industry in India had a de-growth of 4.1%.

The sales growth in Q2 was driven by demand in rural and semi-urban India, due to a good winter crop and due to a good monsoon. Also, we believe pent up demand and festival demand led to higher sales growth. Also, going forward, preference for personal vehicle ownership amid the COVID-19 outbreak would further boost the automotive sales, including the two-wheeler sales.

In Europe, in Q1, there was a decline of 49.7%, and in Q2, there was a decline of 7.2% in the European Union automotive sales.

On the financials, I will briefly talk to you about the second quarter of 2020-2021 and then the first half of FY 2021.

During Q2, as compared to previous year same quarter, our consolidated total net income de-grew by 0.3% from Rs. 17,827 million to Rs. 17,773 million. Consolidated EBITDA grew by 5.9% from Rs. 3,025 million to Rs. 3,203 million. Consolidated EBITDA margin percentage is 18%. The net profit was Rs. 1,672 million at 9.4%. The Q2 consolidated financial includes the Maharashtra state mega project incentive of Rs. 537.2 million. The consolidated ROCE was at

19.2% and ROE was at 18.5%. There was no net debt as there was positive cash available of Rs. 212 million.

During Q2, standalone total income de-grew by 0.6% from Rs. 13,005 million to Rs. 12,927 million. Standalone EBITDA grew by 14.9% from Rs. 2,051 million to Rs. 2,357 million, with an EBITDA margin percentage of 18.2%. Standalone net profit was Rs. 1,344 million at 10.4%. The Q2 standalone financial includes the Maharashtra state mega project incentive of Rs. 537.2 million. Our standalone EBITDA margin percentage for Q2, without the mega project incentive was 14.7% as compared to 14.2% in Q2 of the previous year. This is a result of our better cost control - on material costs and fixed costs, as well as a better product mix.

In Q2, our standalone business with HMSI or Honda Two-wheelers grew by 18.6% compared to Q2 of the previous year. Also, our business with Yamaha India grew by 13.7%, Suzuki by 28.9% and Tata Motors by 38.5% as compared to Q2 of the previous year. Within Q2 - July, August and September 2020 net incomes were at 71%, 104% and 123% as compared to the standalone India net income of these months in the previous year.

Also looking at our OEM schedules, Q3 in India is looking very good. Our unaudited October 2020 financials recorded the best ever net income of Rs. 5,564 million for Endurance's standalone operations, with a growth of 34.5% over the previous year.

The Q2 standalone ROCE was at 24.4% and ROE at 18.8%. There was no net debt as there was positive cash available of Rs. 285 million.

During the first half of 2021, our consolidated total net income was Rs. 23,913 million as compared to Rs. 36,986 million in the first half of FY 2020. Consolidated EBITDA was Rs. 3,739 million as compared to Rs. 6,506 million in the first half of FY 2020. Consolidated EBITDA margin percentage was at 15.6%, the net profit was Rs. 1,422 million at 5.9%. This includes the Maharashtra state mega project incentives of Rs. 637.32 million.

During the first half of 2021, our standalone total net income was Rs. 16,530 million as compared to Rs. 26,649 million in the first half of FY 2020. Standalone EBITDA was Rs. 2,424 million as compared to Rs. 4,539 million in the first half of FY 2020, with an EBITDA margin percentage of 14.7%. Standalone net profit was at Rs. 1,025 million at 6.2%. This includes the Maharashtra state mega project incentive of Rs. 637.32 million.

The detailed financials are available with the stock exchanges and on the Endurance website. I would like to share certain key points for the first half of this financial year.

1. In the first half of FY 2021, 69% of our consolidated total income, including other income, came from our Indian operations, and balance 31% came from our European operations. In Q2 of FY 2021, 73% of our consolidated net income was from Indian operations and 27% were from our European operations.
2. Our factories in India and Europe did not face any mandated lockdowns since August 2020. We continue to do our best to ensure a safe workplace for our people.
3. In India, in the first half of FY 2021, Rs. 3,618 million of new business was won from OEMs which did not include the Bajaj business. This business was from HMSI, TVS, Hero Motocorp, Hyundai, Suzuki and Yamaha. This business will reach peak sales in FY22. I would like to mention that we have Rs. 12,344 million worth of requests for quotes from OEMs.
4. About our new customer TVS, as mentioned earlier, we have been awarded Rs. 1,953 million of two-wheeler and three-wheeler brakes and suspension business. Further, Rs. 540 million of brakes business and Rs. 276 million of suspension business is being discussed.
5. As our combined braking system business is growing with addition of new TVS and HMSI brakes business, and also in order to de-risk operations in our Aurangabad brake assembly plant, we are setting up a capacity of 600,000 per annum CBS brakes at our Pantnagar, Uttarakhand plant, which will start operations from January 2021.
6. We are also setting up a cylinder head low pressure die casting plant at Pantnagar, for 720,000 numbers per annum, and operations will start in March 2021.
7. In October 2020, in our oldest die casting plant at Waluj, Aurangabad, our company announced a voluntary separation scheme for 86 confirmed workmen, with a one-time payout of Rs. 112 million. This will lead to an average wage cost saving of Rs. 48.7 million per annum, and additional savings in canteen, welfare and insurance costs related to these 86 workmen.
8. In 2021, we will also start supplies of brake assemblies, suspensions, and aluminium castings, including the battery housing castings for electric scooters and three wheelers.
9. I would again like to mention that Endurance is focusing on a more value-add and profitable product mix in its future business, which includes 200 cc plus motorcycle brakes and clutch assemblies, with the help of acquisition of Adler and Grimeca in Italy, Paper based clutch assemblies replacing the cork based clutch assemblies for motorcycles, Continuous variable transmissions or the automatic clutch for scooters, Anti-lock brake systems or the ABS for 150 cc plus motorcycles, Inverted front forks and Adjustable rear mono shock absorbers for both domestic and export OEMs - with the help of our collaboration partners KTM, and Fully finished machine castings as compared to semi-finished castings for two, three and four wheelers.

10. For our European operations, in the first six months, we have acquired EUR 10.83 million of new business from Audi, Maserati and Fiat Chrysler. This business will start from 2021 onwards.
11. Also, the consolidation of our foundry activities from two plants to one plant in Italy, which will lead to a saving of EUR 600,000 per annum has been completed.
12. Both the Adler and Grimeca acquisitions, which included all the knowhow, patents, brand and trademarks have helped our Indian operations in getting new business for 200 cc plus motorcycle clutch assemblies and brakes from Indian OEMs which will start in the financial year 2022.
13. I would like to especially point out that Endurance is actively involved in looking out for technology oriented and new product organic and inorganic growth opportunities.
14. I would also like to mention that in India, Endurance is entering two backward integration product areas, which are import substitutes also. First is the aluminum forging axle clamps required for our growing business of inverted front forks. Endurance has entered into a technical collaboration with FGM Italy, and production will start at our Aurangabad plant from April 2021. The second product is wire braided hoses, required for ABS brakes which will start operations in this quarter - Q3 of this financial year.
15. In the first half of FY 2021, our aftermarket business in India was almost at 5.3% of our standalone sales. The aftermarket sales were Rs. 883 million in the first half of FY 2021 as compared to Rs. 1,339 million in the first half of FY 2020. The aftermarket sales are growing very fast, both in India and overseas markets, and we hope to reach the average monthly 2019-2020 sales value in this quarter of this financial year.
16. I also wanted to update you that our new Vallam plant near Chennai for supplying machined aluminium castings to Hyundai, Kia and Royal Enfield, will start operations from next month. We are also happy to inform you that we have won Rs. 320 million of new business with Hyundai, which will start in October 2021 and will be supplied from this new Vallam plant. The net sales with Hyundai and Kia together are expected to reach Rs. 3,070 million in the year 2022.
17. We are also at an advanced stage of testing clearance for our ABS brake assemblies.
18. As far as the CSR activities at Endurance is concerned, we are focused on education, health and sanitation, livelihood generation and environment in the first six months of FY 2021. We have created a sustainable change in 25 village areas and partnered with stakeholders in 5 more. We have also started the renovation process for two Zilla Parishad schools, constructed 23 toilets, supported 70 farmers by training them on agricultural best practices. We continued our nala deepening and silt lifting activities, and planted 4,000 trees per acre in the forests of 3.75 acres across Kachner, Andhaner and Pimpri near Aurangabad. We have also started online classes for our vocational training students in English and soft skills. We have started running a 81 bed COVID

care center in Aurangabad for asymptomatic patients, and also given 5,400 food kits to the needy in Pantnagar, Chennai and Aurangabad. These food packets could sustain a family of four people for a month.

At Endurance, it will be a continuous endeavor to grow through organic and inorganic growth, with a focus on technology up gradation, quality improvement, cost and environmental health and safety. We will do our best to fulfil all our stakeholder expectations by following our five values of customer centricity, integrity, transparency, teamwork, and innovation.

With these opening remarks, I would like to invite questions from all of you. Thank you very much.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the question and answer session. The first question is from the line of Ronak Sarda from Systematix. Please go ahead.

Ronak Sarda: Congrats on a great set of numbers. First question is on the ABS supplies. How confident are we to begin supplies in the current financial year?

Anurang Jain: We have cleared the very important test related to about 11 types of test tracks, such tests which took us two years. So the good news is, we have cleared that. Now there will be an endurance test which will take place. We have been already allotted also an ABS brake for a vehicle, I cannot mention more details here. And we hope to start, if not in Q4, then in Q1 of FY 2022. But the main thing is, we have cleared these very important 11 tests based on the benchmark. So that's the good news. We are on the right track for the ABS.

Ronak Sarda: Does this even help you to expand client base now for ABS product?

Anurang Jain: We are in touch with all the clients - once we have got clearance from one client and we start, everybody else will follow.

Ronak Sarda: Second question was on the profitability, I mean, pretty strong EBITDA performance! How do we see that sustaining? And the VRS / plant consolidation impact in India and Europe, both - are these accounted in the other expenses or they have been treated as exceptional items?

Anurang Jain: In Europe, the gain of EUR 600,000 per annum will start in a significant way, from this month. I don't think that has been counted. Massimo Venuti can further. As far as India is concerned, the VRS impact will only come from this month onwards, because it was completed on 31st October. So, that impact which I mentioned will only come from the VSS, which is more than Rs. 47 million per annum will only start from this month onwards. So that's not included in the Q2 or the first half numbers. Payout of Rs. Rs. 112 million payouts to these employees will happen in this Q3.

Ronak Sarda: On the Europe side, margins have been slightly weaker than our usual trend - any specific cost item which has led to that impact?

Massimo Venuti: We closed the second quarter with 17.4% EBITDA compared to 20% of the previous year. There was an impact in terms of the product mix and inventory utilization effects. In the last quarter we have had a sharp increase of registration in electrical vehicles in the European market. We have seen reduction of the traditional existing internal combustion engine and related casting production. So, the mix included higher production of new parts for EVs. With stabilizing of production of such new parts, the profitability should increase. Components for hybrid and electric vehicles have an expected longer life cycle than traditional products that were subject to changes in emissions regulations. Investments can therefore be used for longer but the prices finalised with customers take this into account and therefore are lower resulting in lower EBITDA but also lesser investments, and consequently less depreciation, and similar free cash flows.

Further, cost of material was 37.9% of sales, compared to 31.7% of the previous year. In order to conserve cash in these unprecedented times and use inventories previously built up to allow the concentration of the foundry activities in Chivasso, we have reduced inventory during the quarter by producing less; and this had an impact on our consumption costs. In the third quarter, I believe, that this situation will change because now the volumes of production are going up, being more consistent to sales and we should be able to maintain or increase our stock. And for sure, the impact on EBITDA will be positive.

Ronak Sarda: That's helpful. We are seeing a second wave of COVID cases coming up in Europe - any impact on your operations in Italy or Germany?

Massimo Venuti: A lot of people are engaged in the automotive industry. While there have been a number of positive cases, so far governments and companies have chosen to control the impact without shutdowns. Also, in Endurance we have had some cases, but the situation is totally under control. We are working 18 shifts per week and we are meeting all the requirements of our customers. So, at this moment, I don't see a problem. However, it is uncertain if the government will place any restrictions in the coming weeks. The number of positive cases are high in Italy, France, Spain and also temporarily shut downs in order to do sanitation of affected plants are possible.

Moderator: Thank you. The next question is from the line of Aditya Jhawar from Investec Capital. Please go ahead.

Aditya Jhawar: A follow-up question on Europe. So, we see there has been a sharp contraction in gross margins, and in the past our gross margins were quite volatile as sometimes we used to outsource the manufacturing. But if you see the reduction in gross margin from 71% in Q1 to 62% in Q2, and considering we have done this consolidation of Grugliasco plant and we have arrived at a balance of outsourced manufacturing and in-house manufacturing, what could be the sustainable EBITDA margin in the next couple of years?

Massimo Venuti: As I told you before, in the second quarter, we have had a reduction of 3% of EBITDA compared to the previous year. But there is a different product mix compared to 2019, because we have had an increase of new EV/Hybrid components. Production of these parts started 6-12 months ago, and we have had a reduction of diesel and gasoline products which we have produced over several years with high efficiency.

Having said so on the overall EBITDA margins, we can go through the individual lines of the profit and loss statement - the Employee costs saw a reduction compared to the previous year and the same holds for the Other expenses. The major increase was only in the cost of material consumed. We have had a reduction of EUR 5 million of stock in Q2. During the month of August and September, in order to optimize our production, we shut-down the Grugliasco plant and closed our operations at certain key production centers for two weeks. In these two months, we reduced the stock. And we maintained such lower stocks till the end of September also to conserve cash. With inventory reduction, the indirect and fixed costs added to the valuation of previously manufactured stocks are charged to P&L as such stocks are now sold in the current period. This has an adverse effect on margins in absolute values and in percentage terms.

Regarding the sustainability of the profitability, if we will be able to come back at the same level of turnover of the previous year, I don't believe we will have a problem. There will be an impact due to the different mix compared to the previous year with higher EV/hybrid components and lower internal combustion engine components. I am not saying that electrical component has the profitability lower compared to our earlier products – In electrical components, EBIDTA may be lower but it would be accompanied by lower depreciation. In addition it is also a question of stabilizing the production of a newly launched part. It is normal that the level of efficiency in a product that you produce for over five years will be higher compared to level of efficiency in a product that started a few months ago.

Aditya Jhawar: So, this mix change that you mentioned could continue for the next few quarters. And that essentially means that there could be a pressure on margin over the next few quarters, until and unless the volume ramps up for the new products?

Massimo Venuti: I believe, yes, and I explained to you why. Newer products will gradually see improved efficiency as the volumes ramp up. Also, on the investment front, there would be an impact. In the past, as you know, when we invested for transmission and engine components for internal combustion engine business, we invested a lot of money for a smaller product life cycle. Continuous changes in the product was the norm especially considering the changing environment related regulations. Our product had the life cycle of 3-5 years. Now, with the electric platform, we are expecting a product life cycle of 10 and more years. And this means that the investment will be less compared to the past.

We will invest less and we will have an impact in terms of depreciation that will be less compared to the past. And so, in terms of net result and medium term cash generation, there will be no adverse impact. Probably we will have a benefit due to the fact that we will optimize the utilization of our machines.

Aditya Jhawar: Okay, that's quite helpful. Moving on to India Business, considering that the inventory level of two-wheelers is relatively higher on the ground as compared to passenger cars, what is the outlook, that your customers would have shared with you in terms of production schedule?

Aditya Jhawar: This month, though technically there are 22 working days, we have to work for 24 days. And the per-day requirement with some of the OEMs is higher than even October, where we have had the highest growth of 34.5% ever in India. So, of course, the end of the calendar year is always down. But I believe that two-wheeler sales, as per my major OEMs, are quite good in the Q4 this year. Quite good means lower than this festive demand of September-October, but I would say much higher than the corresponding months of 2019-2020. This is the expectation that we have at Endurance, after hearing our OEMs.

But having said this, see, as far as Endurance is concerned, I would like to make it clear that industry growth is a big factor in growth but we are also taking a lot of new business. We are not only growing with Bajaj but also with many other OEMs. I also mentioned about low pressure die casting cylinder heads, and brakes plant which are coming up in Q4 this year.

But say to take Honda for example, Last year, we did Rs. 6,080 million. This year our focus is to achieve the same in nine months. Next year, we want to go to Rs. 9,000 million. We have got additional brakes clearance and the first inverted front fork business with them. Our scooter suspension business with them actually peaked only in January 2020, and will reach almost Rs. 3,500 million next year. So Honda is just going great guns. As I said, we have grown 18.6% over Q2 of last year.

If I talk about Hero Motocorp, we did Rs. 2,100 million last year. This year we will cross Rs. 2,600 million only in nine months. And next year, because we have got new orders for brakes, inverted front forks, and the Halol plant will reach from 2,300-2,400 to 4,700 sets of front forks and shockers a day. Next year we are expecting turnover to go to Rs. 3,500 million with Hero.

If I talk about Yamaha, we did Rs. 2,070 million. I am expecting Rs. 2.500-3,500 million next year because we have got brakes business, new alloy wheels coming up, and we make a fair amount of money in these products.

Then we come to fourth OEM, which is TVS. We had no sales with them last year, though we started in Q3 with some suspension business, which was practically zero. But next year, this business will be minimum Rs. 1,650 million because of the brakes and front fork shocker business.

So point is, there is a lot of new business coming in for Endurance. It's not a question of two-wheelers sales growth- that of course is important. I mean, if external factors would affect the two-wheeler automotive growth, it would affect us. But we are taking a lot of new business. And I have not even mentioned about the new machined aluminum castings business growth for the four-wheelers.

So our focus is to get new business, that is the main focus. Secondly, we are upgrading our products. Like I mentioned in my opening remarks, because of the acquisitions of Grimeca and Adler, for the first time we will get into the 200 cc plus category in a major way for our clutches and brakes business, from FY 2022 onwards. That's a big addition to the business we are doing today. I have told you about slight increase in the alloy wheel business for both Yamaha and Bajaj. Also, the Pantnagar new business. So we are taking a lot of these incremental businesses. So for as I am concerned, and I have always maintained since the IPO days - I have no control on external environment. I am focusing on new business and cost controls. That is my job here. And that's what we as a team at Endurance are trying to do.

Aditya Jhawar: Performance on gross margin front has been pretty impressive. In this quarter also, there was almost a 220 bps expansion on the standalone gross margin. So if you can help us understand to what extent it is driven by higher share of proprietary business and what could be the benefit from raw material prices? And essentially, that will give a good understanding of sustainability of the gross margins?

Anurang Jain: Fixed cost saving is almost Rs. 2.5 crores per month, which is not bad. We are going to make full efforts to sustain this. Secondly, like you rightly mentioned, the product mix is improving because of upgradation mainly happening due to proprietary business and machined castings business. As you know, bulk of our products for Hyundai and Kia are fully machined. The business with them is going to reach Rs. 3,070 million in FY 2022. This business started and we are making a fair amount of money there. So it is definitely product mix improvements as well as cost controls leading up to better margins. And I have always said in the last four years, we maintain our focus on these two actions. Unfortunately, lockdown was not good for us. First quarter was a washout. We did only 26% of last year's sales. But this has been a good opportunity for us to introspect, to focus and go into attention to detail of how to control costs. So this actually has been an opportunity and that's why you are seeing these margins also.

Moderator: Thank you. The next question is from the line of Vimal Gohil from Union AMC. Please go ahead.

Vimal Gohil: Sir, you had given some growth rate on HMSI, Yamaha, Suzuki. If you could just help me with what has been the growth rate with Royal Enfield this quarter?

Anurang Jain: Royal Enfield, there has been actually de-growth. The shares of Royal Enfield and Bajaj Auto in our total sales have decreased. We have made up in Honda, Suzuki, Yamaha, and in Fiat Chrysler overseas.

Satrajit Ray: Royal Enfield sales Q2FY21 vs Q2FY20 has been lower by Rs. 12 crores. Last year quarter two was 7.7% of total standalone sales, this year is 6.8% of total standalone sales. And the decrease over last year is about roughly 12%.

Vimal Gohil: And what was the decrease in Bajaj Auto this quarter?

Anurang Jain: Bajaj Auto was minus 6.5% from last year's base particularly because of degrowth in July. It's share in our total sales has gone down by 3%. But yes, this 3% SOB loss of Bajaj has been made up by Honda and Yamaha and Suzuki, and also in Tata Motors we have 38.5% growth.

Vimal Gohil: Right. And sir, the decline in Bajaj Auto would largely be because of we are not present in some of the models or what is the reason?

Anurang Jain: With others we have grown more, thus Bajaj share in our sales has become less.

Satrajit Ray: Also, it must be noted that Bajaj production numbers went down by 12% in Q2, YOY.

Vimal Gohil: You said that you are putting up a CBS facility in Uttarakhand, I missed out the number of units that would be made there.

Anurang Jain: We expect 600,000 per annum and it will start from January 2021.

Vimal Gohil: Right. And sir, what is the total capacity that we have there?

Anurang Jain: Right now we are not doing brakes in Pantnagar; we are only doing some finishing operation of brakes like oil bleeding and all. But now we will start to assemble brakes in Pantnagar. It was only being done in our Aurangabad plants. But like I mentioned, we got new orders from Honda and TVS. Also, we don't want to risk everything in one plant. So this will be a new order. I mean, we are taking this business from others.

Moderator: Thank you. The next question is from the line of Jinesh Gandhi from Motilal Oswal Financial Services. Please go ahead.

Jinesh Gandhi: Congrats on a good set of numbers in testing times. So, first clarification on incentives which you have received in India business. You indicated Rs. 537 million incentives for second quarter. Does this include Rs. 279 million for the prior period?

Anurang Jain: Yes, it does. Just to explain this in a little more detail. Until we received this additional Rs. 99 crores this year, we had got about Rs. 367 crores of eligibility for mega project incentives. So, the additional amount due to inclusion of financial year 2018-2019 was another Rs. 99 crores, which takes the total to Rs. 466 crores. So, against this new eligibility of Rs. 99 crores, for prior years of FY 2019 and FY 2020, we booked Rs. 27.9 crores. For Q2FY21 the booking is another Rs. 25.8 crores. So, that makes it a total of Rs. 53.7 crores booking in Q2.

Jinesh Gandhi: Right. And we have one more instalment coming in 3Q, right, given the increase which has happened?

Anurang Jain: Yes, now the numbers will be booked based on Rs. 467 crores. That will be booked appropriately in the books of account based on recognition as per eligibility and SGST sales recorded in the state of Maharashtra.

Jinesh Gandhi: And these 467 crores would be over 5 years or 7 years?

Anurang Jain: It will follow the original 7 years - not additional 7 years from now.

Jinesh Gandhi: So effectively you have the 5 years left?

Anurang Jain: Yes correct. But GST compliances might lead to part of the recording beyond the original 7 years.

Jinesh Gandhi: Secondly with respect to India business, we have seen increase in depreciation, any reason why depreciation has gone up in India business?

Anurang Jain: Previous year there has been lot of CAPEX. Depreciation has gone up on capitalization.

Jinesh Gandhi: Coming to the European operations, there we have seen quite a sharp increase in staff cost from Euro 8m in Q1 to Euro 11m in Q2 - is there any one-off in that or does Q2 contain anything pertaining to Q1 or is this the new run rate?

Massimo Venuti: We closed the second quarter 2020 with Euro 11 million of the overall employee costs compared to Euro 11.8 million of the previous year. The reduction due to the shutdown of the plant in Grugliasco is recorded in the Other Expenses, not in the cost of labor, as we were able to reduce the number of indirect leasing people with this action. With the reduction of turnover of only around 10% compared to the previous year now, we are not eligible for the free of charge short time working benefits from the government as we were in first quarter 2020. Only those companies with reduction of 20% compared to the previous year are eligible for these full free support from Government. But this quarter, compared to the previous year Q2, there was, in any case, a reduction of Euro 800,000.

Jinesh Gandhi: So the current quarter staff cost run rate is more a normal run rate to follow about INR 900-950 million, is that the right way to look at it?

Massimo Venuti: The total employee cost is less as compared to the previous year. Going forward, we do not expect the government support that we got in Q1. The savings from Grugliasco consolidation will persist in future quarters also but as reduction in Other expenses.

Satrajit Ray: Also, it must be noted that the euro has appreciated by 10% Q2 this year versus Q2 last year.

Jinesh Gandhi: We had talked about potential revenue coming from CVT - any update on that? Where are we in terms of the development cycle and how far we await from commercialization of that?

Anurang Jain: On the CVT, we are definitely working with two OEMs. This COVID19 has pushed back the final testing. Our focus is to continue to try and see that these tests are cleared with both the OEMs.

Jinesh Gandhi: So would it be fair to say this looks more likely towards FY23 kind of opportunity and not FY22?

Anurang Jain: It could be partly FY22 and partly FY23. Our focus will be to start something in FY22 but some business can go to FY23 also.

Jinesh Gandhi: Lastly with respect to the passenger vehicle as a segment, how much does it contribute to the India business now and given the ramp up which we are seeing with Hyundai, Kia and Tata Motors, over next 3 years how do you see this share changing?

Anurang Jain: It’s about 6.5% of the India business. Our overseas business has all passenger cars and commercial vehicles customers. This percentage depends on how well we do with two-wheeler business, where we are growing very rapidly with new business, with new product upgradations. Our focus is mainly on machined castings. Hyundai, Tata, as well as Kia, these three are the major customers which are emerging. Like I mentioned, Rs. 3,070 million should be reached in FY22. I mean, that should be the run rate by last quarter of FY22. That's why the new Vallam plant is being set up. So, we will focus on getting more and more machined casting orders. But as we speak, we are also getting into new clients, new customers. I can’t name them; maybe on the next call I will. We are working with 3 new OEMs. We are trying to get more machined casting business. Casting and machining of large and complex parts is our strength. To answer your question, the absolute amount will go up. But as a percentage I don't know, it depends on how the other business grows.

Jinesh Gandhi: How much would Kia and Hyundai be contributing - roughly 5% now?

Anurang Jain: Right now, it's not much. They are together 2.2% of our India business. So it's very small, so it's a long way to go.

Jinesh Gandhi: Of the 6.5% PV, Hyundai and Kia are just 2.2%, so balances is what, Tata motors?

Anurang Jain: Our total sales to PV in Q2FY21 is actually 5.2%. 2.2% comes from Hyundai, Kia. The balance are largely from Getrag and Tata. Tata is a very old customer, and we are growing very fast and they have done very well. That's why I said we grew 38.5% with them and plus we have exports of Machined Castings to Getrag for their plants in UK and France.

Moderator: We will move on to the next question that is from the line of Niket Shah from Motilal Oswal Asset Management.

Niket Shah: Two questions from my side; given the cost initiatives that you mentioned, what is the standalone margin that one should expect for the next 2 years? And also if you can just highlight your strategy on how do you plan to derisk from your two-wheeler business and expand more into four-wheeler business - which might include some M&A thought process also - over the medium to longer term?

Anurang Jain: Like I've always said, we will keep focusing on increasing the margins. Even without mega project incentive we had done 14.7% based on our costs focus - on fixed, variable and materials costs. We will target more economies of scale, so that the fixed costs go down. So I would say that one should target a similar margin. I would like to have a 15% margin at least for India which we will try to deliver and sustain. This is without the mega-project incentive, obviously. It's very difficult to say conclusively because product mix upgradation is happening, and at the same time, we are looking at the new business which we have to secure against the competition we have. We have to keep working harder and harder to try and sustain these margins. As you are seeing we are improving. I can only tell you we will keep improving but if you want to figure, I just can't pinpoint a figure. I would like to be at 15, right now I'm at 14.7 without incentive. So let's see how it goes.

The second question is regarding the focus on four-wheeler versus to two-wheelers. Now if you see our past history with the last 33 years since we started in 1985, we are focused on two and three wheelers in India, and within that product range, on process and product technology and an aim to become a leader. We are the top two in all of our products - suspension and casting we are number one in the country in terms of growth, technology. The point is that you should do business from a position of strength. Now our strength is in two and three wheelers largely, in the proprietary products. In castings, we are doing two-wheeler three-wheelers and four-wheelers and with the help of our technology and expertise of our professionals in India and overseas. If you see the last 10 years, two-wheelers in India have grown at 6.4% CAGR compared to passenger vehicles which has seen 3%. We believe two-wheelers is a good space to be in.

One can talk about strategy of going into electric vehicles for example. For electric 2W/3W, OEMs are going to use our brakes and suspensions and we have got a lot of castings starting in FY22 as far as electric vehicles are concerned. Let's see where that goes in terms of volumes. Today volumes are very low.

They're here to stay for a long time in a country like India and for us in Endurance two-wheeler will be definitely our major focus and so will the passenger cars be for castings.

But having said this, we're looking at organic and inorganic opportunities in the passenger vehicle space. We are actively looking at products, which I cannot state right now till these projects are cleared. We can talk whenever we are ready. So it's not as if we have less focus on PV. But if you talk about our four product areas, the opportunity in suspension, brakes and clutches is not much in the passenger cars. There are too many players and volumes are very less - only 4 million in a year. So there are not many opportunities in our product areas. Maybe for a new product area, the opportunity can be there in passenger cars. But in machined casting, we see a huge opportunity with Hyundai, Kia and exports. So we will focus on what we can do well and also look at organic/inorganic opportunities which makes sense in terms of potential growth, which are also EV agnostic and where we can make a good profit margin.

Moderator: The next question is from the line of Shanti Patel from Shanti Patel Investment Advisors.

Shanti Patel: My question is, what is our share of different segments in the industry and what is the return on capital employed and return on equity as on today and what you think about next 2 to 3 years?

Anurang Jain: If you go to through our financials even since the IPO, we have generally been always near 20% in ROE and above 20% in ROCE. The consolidated ROCE was at 19.2% and ROE was at 18.5% for Q2FY21. If I take the standalone, ROCE was 24.4% and ROE was 18.8 and we had positive net cash in both consolidated and India.

Shanti Patel: Also, share our market share in respect for different products, if possible.

Anurang Jain: In scooters and motorcycles, if I take Q2, we are more than 40% of the front fork market. In shock absorbers, maybe we are around 36%, transmission we are at 14% which is our clutch assemblies and in brakes we are at 27% of all the motorcycles / scooters, which are sold in India.

Shanti Patel: What is your thinking about increase the return on equity and return on capital employed in the next 2 to 3 years?

Anurang Jain: We are always focusing above 20%. A lot depends on kind of opportunities we get and the external market conditions. We have been very stable in delivering these two ratios. We're a highly focused company as far as financials and technology is concerned. I've always said that and we believe in higher than industry growth and profitable growth only. So I would say both these should be above20%. That is always our target.

Moderator: We will move on to the next question that comes from the line Arvind Sharma from Citi.

Arvind Sharma: We keep on hearing about the news saying that there is a big inventory buildup at the dealers end specially in two-wheelers. Secondly, on the three-wheelers part as well given the social distances norms, sales have declined. On both of these aspects what is your view?

Anurang Jain: I saw the figures of FADA - which is the dealer's association. They talked about a 27% down in two-wheeler retail versus what they bought from OEMs. Now I don't know who are these OEMs and who has given these figures. I only know our sales per day this month is higher than even October which is the highest ever in Endurance. The outlook I'm getting – I would say at least from top three major OEMs is that next month also will be much better than the previous years.

We discussed all these capacities that we built-up and they're very clear. They do not want us to let our guard down in production activities, because the volumes will be good. They won't be like our festival demand obviously - like September and October or this month but definitely it will be higher than 2019-20. So that is the sense I get from OEMs, but now only time will tell what happens.

Arvind Sharma: And, on Three-wheelers…

Anurang Jain: As far as three-wheelers are concerned you are aware that this category is badly down. Maybe it is due to COVID19, and people not wanting to share three-wheeler taxis. So I don't see three-wheelers improving till the COVID19 vaccine is found.

The export markets have really opened up for Bajaj. Exports are doing quite well. But I feel personally, in India, till there is a vaccine I don't see three-wheelers market improving.

Arvind Sharma: Is it possible to share the European revenue EBITDA and PAT in euro terms like you shared last quarter?

Massimo Venuti: The Q2 EBITDA was €9.8 million, 17.4% on €56.3 million of total income. Net result €3.8 million, 6.8% of the total income compared to 6.7% in the previous year.

In Q2 '19 the turnover of 61.6 so we are at reduction of 8.6%, EBITDA was €12.4 million with 20.3% of EBITDA and the net result was 4.2 million with 6.7% net margin.

Moderator: We will move onto the next question that is from the line of Ashutosh Tiwari from Equirus Capital.

Ashutosh Tiwari: You mentioned about this Yamaha order and the sales next year number, what is the number for last year and how much we are looking at in the next year?

Anurang Jain: Last year with Yamaha we had done Rs. 2,070 million and we are expecting next year to be Rs. 2,500 million because we have won a brakes business which will start in first quarter of FY22. Also, alloy wheel is also going up but this is an approximate figure. Yamaha sales at Rs. 2,500 million next year is our estimate.

Ashutosh Tiwari: Any plans on increasing alloy wheel capacity?

Anurang Jain: At present we have increased our capacity in our existing plant to about 135,000 sets which is about 270,000 wheels per month. Beyond that, we can add more capacity if we have good commercials. There is a lot of demand for alloy wheels but till I know we can make money we will not take the orders.

Ashutosh Tiwari: On the HMSI side you mentioned last year sales was Rs. 6080 million and you are looking at Rs. 9000 million in the current year or next year?

Anurang Jain: It will be next year. This year, I am targeting to do the same Rs. 6080 million in nine months. In Q1, HMSI was practically closed this year. The suspension business is really going up. We are doing already one type of brake; we have got another brake clearance. We have got the inverted front fork clearance. Clutch volumes have gone up. I am assuming a business of Rs. 6 billion for HSMI which is not much higher than 2019-20 actuals. That much we should do because even scooters are coming back now. You can see from September scooters are coming back after being down for 2 years.

Ashutosh Tiwari: So your two major drivers are HSMI and Yamaha. In TVS, how much you did last year and how much is planned for next year?

Anurang Jain: Last year was practically zero. We had just started in a small way with suspensions. This year we should do around say about Rs. 500 million as we are just starting off with brakes and suspension, but next year we should do close to Rs. 1650 million. If volumes increase then this figure goes up because we work on SOB, share of business.

Ashutosh Tiwari: On the European operations you have mentioned that because of this higher mix of EVs the margins have come down. So like say is it a new normal margin or maybe from the second half of next year we can assume that probably margin will be higher than what we did about in Q2?

Anurang Jain: A lot depends on volumes. In a situation like this when volumes are down, to make 17.4% is not easy. The consolidation of our foundry will help us to get another € 600,000 per annum that has started may be from this month, that's a good sign. But then there are other challenges with this COVID outbreak in Europe.

Massimo Venuti: On 2020-21 volumes, the sentiment is positive considering the last 6 months and the incentives available. Nevertheless in the European market, car makers are still reducing inventories. We had a reduction of 8.6% in our total incomes in the last quarter while in terms of registration, for the same period, the EU had a reduction of about 7%. For instance, Germany had a reduction in registrations of 6.7% in Q2, while the production of Passenger cars was down more steeply by (-)7% in July, (-)37% in August and (-)11% in September.

There are a lot of problems in terms of volume but you have to consider that the major problem faced is with respect to the abnormal period, as COVID19 impacted our productivity and efficiency. Once we are back to normal production schedules, with normal foundry utilization levels, we can come back to the same profitability.

With higher sale of electrical vehicles compared to internal combustion engine vehicles, for the reasons already mentioned it means that we will invest less compared to the past and so even if we will have a contribution margin that is less compared to the past, in terms of net result and in terms of payback of the investment the situation is expected to be better compared to the past. Our business is currently very capital intensive. Probably with these changes in the market, there will be less investment requirement compared to the past.

Ashutosh Tiwari: With higher EV volumes the CAPEX requirement will come down, so your asset turns can improve. Secondly if the volumes go back to FY20 level, then the margin will be very slightly lower than the earlier level?

Massimo Venuti: In the month of October, for the first time in the history of the European market, we had more or less 25% of the total vehicle registered as electric/ hybrid. OEMs like BMW, Volkswagen, Tesla, Renault are moving Die Casting production capacity for internal combustion engine to external suppliers and they are installing or utilizing their lines for the development of the first versions of the electrical vehicle components. This problem might persist for the next 2-3 years. This is the history of the automotive business. For the first period of time when OEMs develop a new technology and up to a certain volume, they produce the parts inside. After 2-3 years, when the volumes grow they get the benefit from outsourcing the activity to the suppliers to produce those parts. This is the normality of the history of the automotive markets. By the time volumes for these models go up, it is expected that the outsourcing will increase.

Moderator: Thank you. Ladies and gentlemen; that was the last question. I now hand the conference over to Mr. Nishit Jalan for his closing comments.

Nishit Jalan: Thank you Lizann. On behalf of Axis Capital, I would like to thank Endurance management and all the participants for joining the call today. Mr. Jain, I will hand over to you for any closing remarks after which we can conclude.

Anurang Jain: I just want to say that looking at my interaction with OEMs, I am very optimistic about the future. I am quite optimistic the next financial year will be a good year because 2019-20 was a bad year and in the current year, the first 3 months were very bad due to COVID. So looking at the whole situation, I am quite optimistic. This is a thought I want to leave with everybody.

Moderator: Thank you. Ladies and gentlemen on behalf of Axis Capital. That concludes this conference call. Thank you for joining us and you may now disconnect your lines. Thank you.