Escorts Kubota Limited
(Formerly Escorts Limited)

"Escorts Kubota Limited Q4 FY '23 Earnings Conference Call"

May 10, 2023

Escorts Kubota Limited
(Formerly Escorts Limited)

Emkay
Your success is our success

CHORUS CALL

MANAGEMENT: **MR. BHARAT MADAN – WHOLE-TIME DIRECTOR AND CHIEF FINANCIAL OFFICER – ESCORTS KUBOTA LIMITED (EKL)**
MR. HARISH LALCHANDANI – CHIEF OFFICER – AGRI MACHINERY BUSINESS DIVISION – EKL
MR. SANJEEV BAJAJ – CHIEF OFFICER- CONSTRUCTION EQUIPMENT BUSINESS DIVISION – EKL
MR. ANKUR DEV – CHIEF OFFICER – RAILWAY EQUIPMENT BUSINESS DIVISION – EKL
MR. PRATEEK SINGHAL – INVESTOR RELATIONS & ESG - EKL

MODERATOR: **MR. CHIRAG JAIN – EMKAY GLOBAL FINANCIAL SERVICES LIMITED**

Moderator: Ladies and gentlemen, good day, and welcome to the Escorts Kubota Limited Q4 FY '23 Earnings Conference Call hosted by Emkay Global Financial Services Ltd. 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 star, then zero on your touchtone phone. Please note that this conference is being recorded.

Before we start, I would like to add that some of the statements that the company makes in today's call will be forward-looking in nature and subject to risks as outlined in the annual report and investor releases of the company. I now hand the conference over to Mr. Chirag Jain from Emkay Global Financial Services Ltd. Thank you, and over to you, sir.

Chirag Jain: Thank you, Michelle. Good evening, everyone. On behalf of Emkay Global Financial Services, I welcome you all for Escorts Kubota Limited Q4 FY '23 Earnings Conference Call. I also take this opportunity to welcome the management team from Escorts Kubota Limited. Today, we have with us Mr. Bharat Madan, Whole-Time Director, and Chief Financial Officer; Mr. Harish Lalchandani, Chief Officer, Agri Machinery Business Division; Mr. Sanjeev Bajaj, Chief Officer, Construction Equipment Business Division; and Mr. Ankur Dev, Chief Officer, Railway Equipment Business Division. As well as we have Mr. Prateek Singhal, Investor Relations and ESG at Escorts Kubota Limited.

We would start the call with brief opening remarks from the management, followed by an interactive Q&A session. At this point, I would request management for their opening remarks. Over to you, sir.

Prateek Singhal: Thank you, Chirag. Good evening, everyone. This is Prateek Singhal. Thank you all for joining us on the earnings call for the fourth quarter and fiscal year ended 31 March 2023. Few highlights of the company's standalone performance for the fourth quarter ended March 2023 are as follows: Revenue from operation during the quarter was up by 16.8% at INR 2,183 crores as against INR 1,869.6 crores in previous fiscal.

On sales volume front, tractor volume was up by 13.1% to 24,765 tractors as against 21,895 tractors last year same quarter. On the construction equipment, volumes are up by 18.8% to 1,528 machines as against 1,286 machines in the last year same quarter. EBITDA for the quarter ended March 2023 came at INR 235.8 crores, down by 6.2% as against INR 251.5 crores last year same quarter and sequentially up by 23.9% as against INR 190.3 crores in Q3 FY '23.

EBITDA margin for Q4, up by 240 basis points to 10.8% as against 8.4% in sequential quarter and 13.5% last year same quarter. PBT before exceptional item at INR 271.4 crores as against INR 269.5 crores last year same quarter. Net profit at INR 185.5 crores as against INR 202.2 crores last year same quarter, impacted due to exceptional provision of INR 24.4 crores on account of impairment of investment in the wholly owned subsidiary, Escorts Crop Solution Limited. Company continue to be net debt-free with sufficient availability of liquidity for growth.

The Board of Directors has recommended a final dividend of 70%, i.e., INR7.0 per equity share for the year ended 31st March 2023.

On consolidated basis, company financial performance for the quarter ended March 2023 is as follows: Turnover is up by 17.4% year-on-year to INR 2,214.5 crores. EBITDA margin at 10.5% as against 13.2% in last year same quarter. Profit before tax up by 7.8% year-on-year at INR 277.6 crores. Net profit margin up by 13.9% year-on-year at INR 216.5 crores.

Moving on to the segmental business performance. Starting with the Agri Machinery business. The total tractor industry volume, domestic and exports, in FY '23 went up by 10.2% to 10.7 lakh tractor as compared to 9.7 lakh tractor in the previous year. This is a new record for the tractor industry, beating the last peak of 9.88 lakh tractor in FY '21. Our total volume went up by 9.7% to 1,03,290 tractors as against 94,228 tractors in the previous fiscal. Our total market share was maintained at 9.7%. Key to note that this is the second time that company has crossed 1 lakh plus tractor sales unit.

The domestic tractor industry went up by 12.2% to record number of 9.45 lakh as compared to 8.4 lakh tractor in the previous year. All macroeconomic factors, crop production, crop prices, good monsoon and availability of retail finance remained positive throughout the year. Our domestic tractor volume went up by 9.4% to 95,266 tractors as against 87,043 tractors in the previous year.

We ended the year with a domestic market share of 10.1% for FY '23 as against 10.3% in FY '22. The marginal drop in the market share was mainly due to drop in Q1 FY '23. Post that, we have taken some corrective actions in the last 9 months of the fiscal from July '22 to March '23. Our domestic market share improved to 10.4% as against 10.2% for the same period in FY '22. And in Q4, we ended market share at 10.9%.

We have more than 1200-plus dealer count. We continue to focus on channel expansion to cover the white spaces for both Powertrac and Farmtrac brand. We have also initiated step to focus on the health of our channel and are taking a step to develop a strong and healthy dealer network.

On the export side, during fiscal FY '23, industry was down by 3.2% at 1.24 lakh tractors as compared to 1.28 lakhs tractors in the previous fiscal. However, our export volume went up by 11.7% to an all-time high of 8,024 tractors as against 7,185 tractors in the previous fiscal, driven by our continuous focus on new product development and expansion of our distribution network. Sales through Kubota global network is also gradually increasing and during the year contribute more than 30% of the total export volume.

Segment revenue was up by 13.5% to INR 6,316.1 crores as against INR 5,563.7 crores in the previous year. EBIT margin for the Agri Machinery business stood at 9.3%, impacted during the year by steep inflation in commodity price, adverse product mix and impact of price rationalization in certain products/geographies.

For the quarter ended March 2023, EBIT margin was up by 159 basis points to 9.9% as against 8.3% in the sequential quarter, led by a better product mix, improved price rationalization and softening of the commodity prices.

In Q1 FY '24, domestic tractor industry is expected to remain almost flat due to advancement of the key festive season to March '23 as against April last year, combined with unseasonal rain. However, for FY '24, we expect the domestic sector industry to do well and may register low mid-single-digit growth, led by positive macroeconomic factor, on account of good rabi harvest, improved crop prices and adequate water level reservoir.

Coming on to the Construction Equipment business, our served industry of crane, backhoe loader and compactor was up by 24.5% in volume as compared to FY '22, led by growth in backhoe loader industry up 28%, crane industry was up by 25%, whereas compactor industry see a degrowth of 5%.

Our total volume of manufacturing and traded products went up by 12.2% to 4,620 machines as against 4,117 machines in the previous year. Segment revenue went up by 19.5% at INR 1,179 crores as against INR 986.8 crores in the previous year. EBIT margin went up by 48 bps to 2.9% as against 2.4% in the previous year. There is a sustained demand for construction equipment industry supported by government continued trust across all infrastructure. We expect demand momentum to continue going forward for the current quarter and further accelerate in FY '23-'24. And margin for the segment to improve further, owning to softening of the commodity price and improvement in the product mix.

Coming to the Railway division. Revenue for the year ended March 2023 went up by 32.3% to ever highest yearly revenue of INR 841.9 crores as against INR 636.2 crores in the previous year. Sales from the new product contributes 65% of the total sales division sales. EBIT margin for the year ended March 2023 stood at 13.8% as against 14.8% in the previous year.

Order book for the division at the end of March 2023 stood at a healthy and ever highest level of more than INR 1,050 crores. With continuous focus on product diversification and export, we expect the Railway Equipment business segment to continue in the double digits in FY '24.

Now we request the moderator to kindly open the floor for the Q&A.

Moderator: The first question is from the line of Gunjan Prithyani from Bank of America.

Gunjan Prithyani: I have 2 questions. Firstly, on the outlook for the industry. I'm not sure if it was flat for F '24 or low single digit, if you could clarify that. And also give us some color on how did the recent festive go. Any color on the geo trends? Where are the inventory levels? Some color on the industry, what you're seeing on the ground.

Harish Lalchandani: Thanks, Gunjan. This is Harish. To give you our perspective of the industry, we expect first quarter of this year to be flat, given some of the adverse weather conditions, but overall, for the year, we expect the industry to grow by single digit. That's for F '24.

Going at the end of the festive season, the festive season in quarter 4 was -- if you were to split a quarter into 2 parts, the first part of the quarter was good for us because of good rainfall, good, what you call it, water supply, etcetera, good MSP prices. Last month, which was March, got impacted positively as well as negatively. The positive impact was because of the festival. Negative impact was because of unseasonal rain in few markets.

Gunjan Prithyani: And I mean on balance, how -- I mean did it go as per your expectation? Was it growth versus if you compare with last year Navratri festive? Did these balances out each other? Or was it more on -- skewed more on the negative because of the unseasonal rain?

Harish Lalchandani: If you were to ask us if the unseasonal rain hadn't happened, and if you see the trend versus the previous quarter, growth could have been better. But given the fact there was unseasonal rains, the market still grew 14%, but it is not in line with the growth in the previous quarters.

Gunjan Prithyani: Okay. And where are the inventory levels? Is there some higher inventory levels because it didn't go -- the festive didn't go as anticipated?

Harish Lalchandani: Actually not, because if you take a look at our quarter 4, our deliveries have been higher than our billings. Therefore, our net inventory at the end of quarter 4 stands lower than it was in the previous quarter.

Gunjan Prithyani: So less than a month, I should assume?

Harish Lalchandani: It is in line with the 4 to 4.5 weeks that we normally have.

Gunjan Prithyani: Okay. Got it. The second question is more around the margins. Now we've seen some sequential improvement given combination of mix, price hikes as well as the cost easing. But if I were to look ahead for -- going by the assumption that there's incrementally not much of operating leverage to play, if it's a flattish or a low single-digit volume growth, there's not incrementally much operating leverage as a lever.

So how should I think about the various push and the pull factors? Like do we have scope to take more price increases. Are we expecting more commodity easing to flow through? So just some perspective on how I should think about margins for F '24 for the agri business.

Bharat Madan: Gunjan, this is Bharat Madan. So, as you currently mentioned, operating leverage, we are not really banking on too much. But if you look at the trend in the last 2 quarters, so we are getting the benefit of the softening of the commodity prices. And it looks like the trend will continue in the coming quarters, too. So, price increase doesn't look like the feasibility in this scenario when the commodities are softening. So that is something which we are still keeping a watch. It will all depend on how the competition plays out, and it is a possibility. So that will be explored. But right now, it looks difficult looking at the way commodities are moving.

But as we mentioned in the last quarter, that was a bottom quarter from a margin perspective, and we're only looking at better margin coming in going forward. So, this commodity cycle, obviously, is giving benefit going forward, too. So, we expect that trend should continue, and that should actually lead to some better margin.

In addition, there are also some cost control measures which company had put into place for this year. So that will also start playing out. So that also should act to the overall bottom line. So at least by the time we exit the year, we should be at least back to what it used to be the normal level of margin for tractor business.

Gunjan Prithyani: The normal, you mean the low to mid-teens because we've gone through a huge range in the last 2.5 years, right, 13%, 14%, then we touched even 20%.

Bharat Madan: I think COVID year, you should exclude. So, I think pre-COVID level, which used to be just 14% sort of range. So that is the sort of number which we're targeting to end the year this year as an exit.

Gunjan Prithyani: Okay. Got it. Just last question if I can pitch in this Construction segment margin at 8%. Is this sustainable? Is it one-off this quarter? Any clarity on that?

Bharat Madan: So, Construction, as you know, I think the demand started picking up only from December last year. And only second half in Construction Equipment business is good. And you've already seen the margin historically also. The last quarter used to be the best in terms of margin. Whether the same numbers will sustain, I think difficult to say, but the demand momentum is continuing. We've seen good numbers coming in April also. There's some spill over of demand, which was there.

So, industry is right now struggling with capacity issues, but very good demand coming in both domestic as well as an export front. I think the demand scenario for this year, we expect the momentum should be good. The price increases have been absorbed in the market. So, the idea, the margin should continue to be better than last year, whether the same level is sustained, I think it's difficult to say at this point in time.

Moderator: The next question is from the line of Chirag Jain from Emkay Global Financial Services.

Chirag Jain: I have a couple of questions. On the market share front, within the tractor space, we have seen a decline last year. So how do we see that shaping up this year? And any major initiatives that you can call out, which can help in terms of boosting our market share?

Harish Lalchandani: Chirag, thanks. This is Harish. Chirag, again, if you take a look at the full year and if you take a look at the sequential quarter-wise, quarter-on-quarter, we have increased our market share from Q1 to Q2 to Q3 to Q4. Biggest drop that we had was in Q1. Subsequent to that, we have always grown in our market share. So that is point number one. Two is, this has -- already some initiatives have been taken. Key among -- is the focus on digital. Second is our focus on the 31 to 40 HP, our focus on 41 to 50 HP, and our focus of greater than 50 HP.

Second, just in terms of geography, our focus on the strong as well as the opportunity markets, which is leading to a significant growth of share in this strong as well as the opportunity markets across quarters. The third is our focus on the haulage segment. So, we see haulage segment as an opportunity for us going forward. And even in the last year, we have inroads into the segment.

Chirag Jain: Okay. Second question is, with respect to the product mix or, let's say, the segment-wise, let's say, growth profile within the tractor space, let's say, Agri and nonagri, how do we see that, let's say, in this financial year? And this could have some implications on the margin profile as well. Maybe if you can discuss that as well.

Harish Lalchandani: Two bits. If you were to take a look at the market today, if you were to take a look at the pure nonagri, our estimate of the nonagri market is approximately 15% to 20%. And if you take a look at that specific market, that is predominantly driven by investments into infrastructure. Given that the government has the stated intent to double the spend in infrastructure this financial year as compared to the actual spend last year, we see this segment showing a significant growth. That is part one. I agree, if you take a look at it, given the current quarter levels that we have and the positive trend that continues into this year, we also see a positive momentum in that segment.

Chirag Jain: Okay. Sir, just last thing and then I'll come back in the queue. In terms of Trem IV for regulations, any update do we have? I think in the last call, we mentioned that it might come probably in September '24. So, any final notification or any update that we have?

Harish Lalchandani: So, no further update. It is just that as part of the TMA, we have submitted a recommendation to the government to try and keep a 5-year gap between the Trem 4 and the Trem 5 but is yet to get back.

Bharat Madan: And also, again on last call, we had mentioned in the original emission norm for more than 50 HP, then got delayed by almost 18 months. So, we expect similar delays should be there for the lower HP segment also. So earlier, the initial change of emission you saw was supposed to happen from 1st April '24. Now if you look at 18-month delay, it would have been September '25, not September '24. So -- but right now, obviously, there's no notification being issued. So, we're still waiting, and we'll come back once the discussion is out and the notification is out.

Moderator: We have the next question from the line of Devika Jain from Ratnabali Investment Private Limited.

Devika Jain: So, we have grown our exports by nearly 12%. I just wanted to understand how our players have performed and also the reason for our outperformance as against the industry.

Bharat Madan: So, industry has actually declined by almost 2% last year. So, exports in India have not done well. So, the industry total was roughly 125,000 this year against 129,000/130,000 a year before. So, in our case, the exports have grown because, obviously, we have started exporting to quarter network also, which was also one of the reasons. So, it's almost 30% export in our case, actually, this year or through quarter network. And that's the trend we are seeing probably will continue. So that's why we are more bullish on the export number going forward, too.

So, in the industry scenario, with some of the countries have started facing decisions especially in EU countries. So, we are seeing some sort of decision condition are prevailing because of geopolitical issue. And the U.S. also is expected to get into this decision mode. So, on exports, demand may get impacted slightly. But in our case, since we are banking more on the export to Kubota network, so maybe we'll not see that sort of impact for the industry.

Devika Jain: Okay. This quarter, our excludes through Kubota was more than 40%. What is the number going forward? Is it expecting through Kubota channel?

Bharat Madan: So right now, we are projecting a similar level as we have seen in the last year. So, once we open more countries -- and there's a lot of work needs to happen on the product side. So once the product is steady, then obviously, we'll see the numbers going up. So that will take some time. But definitely, I think the trend product portfolio, what we have, which we are already exploring, and there's certain new markets which are opening this year. So, we expect the number should gradually continue to improve. It will be in the range of 30%, 40% in annually going forward.

Devika Jain: Got it. And one last question, sir. So, I also wanted to understand the reasons for our poor volume uptick in the Construction Equipment segment this quarter.

Bharat Madan: Poor volume uptick. Why do you say that?

Devika Jain: As compared to the industry, the growth of our volume...

Bharat Madan: So essentially, because of the product mix which we have, if you look at -- we are -- our main product portfolio is in the pick-and-carry crane segment, where we have done almost at par with the industry. The issue is on the backhoe loader, which is the earth moving segment. Here, we're a very small player with about 1.5% to 2% market share, and the maximum growth in the industry has happened in that category.

So, it's more in terms of the issue, in terms of mix that the industry has and where segment has grown, where we are not a very strong player. So, they're saying the service industry looks like as if we have been dropping the market share. But if you look at our own pick-and-carry segment, I think quarter -- this quarter, we almost gained our market share back to 40% plus, which is the largest segment for us.

Moderator: The next question is from the line of Mitul Shah from Reliance Securities.

Mitul Shah: Sir, I have question on your yearly guidance of single-digit growth for the industry. Sir, in view of festival being not there in April this time, in March to last year, April had a festival, so the base was high. Even for this quarter, also base for the coming months, May, June remains high. Overall, climatic situation is still adverse and untimely monsoon. So, despite all those negative factors fundamentally right now, what are the factors you see could help driving single-digit growth?

Bharat Madan: So, Mitul, if you heard the commentary from Prateek, I think he mentioned in this quarter, since you've already seen April has declined, the industry has declined, and May, we expect to be almost flat industry, and June early, we'll see growth coming in. So overall for the quarter, we are anticipating flat industry this quarter. The low single-digit growth we were talking about is for the full year basis. So, it's...

Mitul Shah: My question is on full year only. I asked that this quarter, we are seeing flat, and full year, we are seeing growth. These are the negative factors even -- in fact, inventory level is also high for the industry, which probably may come down slightly. So adjusted for that wholesale growth, you are indicating single digits. So that's what I want to understand.

Harish Lalchandani: No, no. So, Mitul, if you take a look at it, there are 3 positive factors that are impacting the industry today. One is the good MSP prices that we have as well as the crop prices. The second one is the water reservoir, which are significantly better than what we have in the last year. The third one and the most important one is the fact that it is an election year.

Therefore, we expect infras trend, as I indicated, is doubling this year as compared to the previous years. So, the haulage plus the mix segment, which accounts for close to 30% of the total industry, is expected to give a big boost to that particular entire space, that combined -- so that infrastructure growth, and hence, a significant boost in the 30% and 35% of the market, plus growth in Agri because of MSP increased as well as irrigation. That is expected to give you that single-digit growth.

Mitul Shah: Okay, sir. Second question, again, on the same in terms of -- as for the commentary, it seems that the second half would see the growth, first half may not be very great. In terms of region-wise, where do you see high growth coming? Or which of the regions do you think still have some weakness? Because this monsoon impact seems to be more in the north and in central belt, where we are relatively stronger compared to south.

Harish Lalchandani: I think the growth we are expecting is going to be pan India. That is one. And second one is monsoon is -- if it comes, and I'm not sure what the outlook is going to be, but I think it will impact most of the geographies, if it does impact. In fact, irrigation in the northern and the western zones are actually better than some of the other areas, if you see the historical trend. So, we feel a lesser impact would happen in our strong markets.

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

Hitesh Goel: Sir, first question is on the tractor margin, which has improved 160 bps Q-on-Q. You had highlighted in the last con call that there's not much commodity cost benefit, which you are expecting in the fourth quarter. But the commentary seems to be you've got some benefits, and that will flow through in the next quarter. So, is it mostly commodity benefit that has helped margins, or it is also the mix to some extent?

Bharat Madan: So, it is the 3 reasons we mentioned. One, we also mentioned last quarter since we've taken the price increase after the festive season was over. So, the full impact on the last quarter was not visible, which we've got the full impact in this quarter, which still is almost 0.75% in the margin improvement.

And then second, the softening of commodity price had happened. So still, some decline is happening on the last time, which was not visible. But during the quarter, when the rate got settled with the competition, the leader who actually take the lead in settling those rates on the commodity side, so we did get some benefit, which happened towards the later part of March. And that's why we got the impact on the full quarter, and that basically will continue in the coming quarters, too.

And third is product mix, which was also positive. Because you look at the trend, the more than 48 sales number into the percentage has gone up by almost 3% in this quarter. So that also contributed to the better realizations. So, all 3 factors were this module for the improved margin trend in the tractor business.

Hitesh Goel: And sir, my second question is on this, which Harish also highlighted, actually. Irrigation intensity has improved quite dramatically, especially in states like Madhya Pradesh and all that. So, I did an analysis that only, I think Maharashtra and Karnataka and to some extent, Gujarat is the areas where monsoon can have an impact on tractor volumes, if the water levels are quite high. Is the analysis, right? So, we should not worry too much about monsoons at least because it's – reservoir levels are only -- they are lower in UP, Bihar where anywhere the irrigation intensity is very high. Is the analysis, right?

Harish Lalchandani: Broadly in line with what we are also thinking that we don't feel there is going to be a significant impact of monsoon this particular year because of the reservoir levels across most areas, which are key markets for us being reasonably good. And plus, as I said, the infrastructure growth, which is happening because of the election year.

Moderator: We have the next question from the line of Raghunandhan N. L. from Nuvama Research.

Raghunandhan N. L.: Congratulations on the strong margin performance, both in Agri and the construction equipment space, and very heartening to hear the improvement expected by end of the year. Sir, a couple of questions. Firstly, on Kubota Agri Machinery, if you can share your thoughts on the timeline for merger? And also, how is the progress happening on the localization part? Would you see that exercise completing within the 2-, 3-year period and seeing EBIT margin of 15%? And again, on Kubota Agri Machinery, how do you see the component exports to global Kubota? What are the efforts there? And on a pilot basis, have you started exports?

Bharat Madan: So, Raghu, on the merger front, right now, the -- we are waiting the approval from SEBI. So, we had filed our application, and all the stock exchanges have given the -- all the queries were resolved, and the matter has been referred by stock exchanges to SEBI now. So, we have yet to have received the approval. It's almost now close to 3 months since spending with SEBI. Once we get the approval from SEBI, then it will be filed with NCLT for the necessary processes. So, it will take another 6 months' time.

So right now, the way things stand, it looks like the process call gets delayed by another 3 months. Earlier we're expecting it should happen by September, October. But the way I think things are today, so SEBI has already delayed this whole process. So, it looks like it may go somewhere around December, January types, assuming everything comes in line in future.

On the localization front, so obviously, the localization in the JVs is essentially for the Indian manufacturing, which is a major part, which right now is getting imported, and also other products which are right now traded was in the manufacturing JV. We are only doing 2 models for them right now. And the balance of the models are actually imported from Japan. So that localization will happen once the more product gets introduced in the portfolio, which will happen I think over the next 2, 3 years, as you mentioned. Because we have already factored that in our midterm business plan, which was unveiled to the investors and analysts last year in November. So that obviously is very much on. So, the work is happening on that front.

On the component export, it's already -- the manufacturing JV is exporting to some of the countries, including Thailand and U.S. market. And as they grow and develop more components and do more indigenization, so the opportunity for export will also further increase. So that is also already indicated, and that will continue. Obviously, the visibility to numbers will only happen when the merger happens. So right now, they are still stand-alone entities, and we only consolidate the bottom-line numbers there. So that is not really reflected right now. But since the -- the integration happens and the merger happens, we'll get to know more, I think, about them.

Raghunandhan N. L.: And the effective date will be from 1st April, right, sir?

Bharat Madan: Yes, I appointed it as 1st April 2023. So as and when it happens, so we'll do the consolidation of results from 1st April and produce consolidated results.

Raghunandhan N. L.: Kubota tractors are selling in the network of 300-odd outlets. Any thoughts on cross-selling using the Escorts Farmtrac or Powertrac network?

Bharat Madan: Yes. So, like we mentioned, so this is one of the key synergies which is there. So, when the integration happens, so definitely, there will be an opportunity for the dealers of both the companies to do cross-selling. So, the good dealers and Kubota can also sell our products maybe through a different showroom, not in the same showroom. And same thing can happen with our dealers also. So especially in the northern, central India where we are strong. And Kubota is not very strong. So that will give them also an opportunity to represent it to our network.

Raghunandhan N. L.: And on the Construction Equipment and Railways, if you can talk about outlook for FY '24?

Bharat Madan: Sanjeev, you want to talk about Construction, then Ankur can take the Railway.

Sanjeev Bajaj: Yes. Thank you, Raghunandhan. So, this is Sanjeev Bajaj. I want to talk about the Construction Equipment outlook for this year. Now last year, we've seen that the first half was very subdued. And second half only, we saw that the demand came up. And we expect that the speed at which the projects are moving at present and the demand from the infra projects is very, very high. So, this year, it is expected that the same level of demand will continue.

Although there was some backlog, which was to be covered in the last quarter for the first half of the year. Second half of the year -- I mean this year; we expect that the industry will continue to grow. Our served industry will grow at about 10% to 12% is what we are expecting. And we see that until the end of the year. This demand should continue except for the small period of monsoons when the projects actually went to a halt.

Ankur Dev: Yes. Raghu, this is Ankur Dev. So, regarding Railway business, so as of now, we have a strong order pad of INR 1,000 crores plus, as we mentioned in our opening remarks. Most of this will be executed in current financial year only, financial year '24. Additionally, we are going to commercialize 3 more products, which were in field trial in the last financial year. And obviously, these -- commercialization of these 3 new products will add to order pad and the revenue in the current financial year. So overall, I can say that we are -- we will continue this growth momentum in the Railway business, and we are hoping that we will be able to grow by double digit in the current financial year also.

Raghunandhan N. L.: And to Ankur, sir, if you can talk a bit on the localization efforts of new products and how the margin trajectory will go ahead on railway.

Ankur Dev: So, regarding localization, as of now, mostly, it is in the brake side for the LHB coaches. And we have already done the localization of the components which we are importing as of now. So, all those localized components are put into the field trial as per the Indian railway's regulation. So, we expect that this localization benefit will flow into our margin in financial year '25, basically the next financial year.

Raghunandhan N. L.: So, you see margins going back to the historical price of 18% to 20%?

Ankur Dev: It is difficult to say exactly to those high levels because we have been impacted by the inflation in the metal cost in last 2 years. But obviously, we are working towards that.

Moderator: The next question is from the line of Pritesh Chheda from Lucky Investment Managers.

Pritesh Chheda: Sir, my question is with the Escorts Kubota tie-up in place. What kind of opportunities has opened up from a product perspective or what kind of gaps gets plugged from a product perspective? And over the next 3 years, alongside exports, these 95,000 or 100,000 tractor volumes that we see, what kind of volumes are possible on a 3-year basis, if you could just give a small recap on that?

Bharat Madan: So, Pritesh, we already unveiled our midterm business plan, so maybe you can have a look at that. It's already available on our website. It gives the overall picture in just how our aspiration is to go, not exactly 3 years, we're talking about 5 years there by FY '28. And it's both on the domestic front, export front, the outsourcing opportunity, which exists for EKL, which Kubota intends to use, both on the component side as well as on the finished goods side.

So, I think all those questions are getting addressed over there. So, it's difficult to put a number right now and what will happen. But obviously, the idea is to make sure wherever the white spaces exist in the product, so that gets addressed. And there's also what we do. Obviously, do a joint development of growth, which there's a plan. So, most of the first introduction will happen by FY '26, as I think it stands today, and the projects are on, and I think with both the growth on the domestic side as well as for the export market.

Pritesh Chheda: Most of product introduction will happen by FY '26?

Bharat Madan: For the new products, which is totally under new development, but there are many opportunities which will be in terms of tweaking the existing product platform. So that will happen sooner. We will see some new products coming into the play.

Moderator: The next question is from the line of Manoj Bhatt from Motilal Oswal. As the current participant is not answering, we move on to the next question, which is from the line of Kapil Singh from Nomura Group.

Kapil Singh: Sir, just a follow-up on the Trem 4 norms. How much was the cost increase that we did for more than 50 HP segment? And were we able to fully pass on this cost increase? And did that have any impact on volumes for this segment?

Bharat Madan: So, Kapil, the impact is roughly 10% to 15% of the total cost of the tractor. It's on the high 50 HP and above tractors. So obviously, emission has already been put into place. So last purchase that once become effective only from 1st of January, and most of the manufacturers were carrying inventory. So really, the impact has not been seen. However, whether this gets absorbed in the market now, I think we'll come to know in the coming quarters. So, I think it's difficult to say at this point in time. But definitely, no one would like to keep the costs on the P&L. So, everybody would like to pass it onto the market.

Kapil Singh: So, we have already taken 10% to 15% price increase?

Bharat Madan: Also, like you mentioned, most of the manufacturers are carrying inventory of the old tractors with the old engine. So once the new emission on tractors start coming to the market and start getting retail, so really, we'll come to know. But yes, the price increase will happen based on this cost increase.

Kapil Singh: Okay. And by when is it expected that the new tractors will start coming into the market?

Bharat Madan: I think from this quarter, you should start seeing the impact.

Kapil Singh: Okay. The second question was on exports. April saw a pretty sharp decline. Any particular reason? Was there a one-off? Or do you think that exports could be soft this year?

Bharat Madan: No. So, export will not be soft. We have order book. We had more than 800 tractors order likely, but it could not be completed with some model mix issue and supply chain issues were there. But they will get addressed in the coming months. So, there's no shortfall as far as the order book is concerned for export. I think it was the only temporary issue in the line and some quality issues which are getting addressed. So that should actually get taken care of in the coming months.

Kapil Singh: Okay. So, is it already addressed, or it could -- like by when do you expect that this would be addressed, the issues basically?

Bharat Madan: Most of them have been addressed. So, you will see the impact coming from the coming months.

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

Jinesh Gandhi: A couple of questions from my side. One is the RM cost savings you expect to continue in coming quarters. And what materials are we seeing further operations from where we are today?

Bharat Madan: Yes, we expect the softening will continue. So, we are seeing -- I think we've only seen the news clippings on the sheet metal, the steel companies are talking about reducing the prices by about INR1,500 to INR2,000 per ton. On the casting also, we think some softening is happening. So, both on the coke prices and then this big iron, both are going down. So, we'll see some softening happening on the casting, too, which is a major component for the tractor industry. We've also seen the level prices going down. So, where you've seen the results of the tire companies, most of the companies are seeing the margins going up in last quarter. So hopefully, since we get the impact with some lag, so that should also start benefiting the company.

So, to your question, yes, broadly, we see the trend is downward on the commodity side. So, we should continue to get that impact as the quarters pass by.

Jinesh Gandhi: Okay. Okay. And in that context, we would not have taken any price increase in fourth quarter or till date in 1Q.

Bharat Madan: Yes. So, industry hasn't taken any price increase because the prices are coming down. So, net-net basis, if you look at whatever the inflation has been there, it's been fully passed on to the market by the industry, including us. Yes, the margin on that increase has not been absorbed by the market, and no one has been able to pass it on. So that is why we're seeing the -- cost-wise, percentagewise, the material cost is looking very high compared to what it used to be 2 years ago. So, I think as the softening happens, we'll see the gradual increase will start happening on the margin front, too.

Jinesh Gandhi: Got it. Got it. And lastly, with respect to the merger of those 2 entities, can you clarify what kind of impact segment have on margins and profits based on FY '22 numbers or other indicated on a F '23 basis?

Bharat Madan: So, I think it's already there in our investor presentation on our website. So, we have given the consolidated view of FY '22 numbers based on the -- both the JVs numbers. So broadly, if you look at the last year's number, there was a dilution happening in the EBITDA margin of about 1.5% to 2%, where they were just -- they were still almost breakeven sort of operation. So, I think once the merger happens, there are a lot of cost synergies still flowing.

So, as you keep cutting down the cost, the margin will continue to improve going forward. So, an objective is they should also continue to come back to the same level of margin, what we are doing in EKL on the tractor business. Obviously, there'll be some difference with the positioning because Kubota brand is different than what EKL has. So, to that extent, there will be some -- some difference should be there. But overall, blended margins should be actually in the same range as the tractor industry enjoys.

Jinesh Gandhi: Okay. And given that this is happening in FY '24, impact might be much lower than 1.5 to 2 percentage points or can be similar. Would that be fair?

Bharat Madan: It will be similar.

Jinesh Gandhi: You mean similar dilution of 1.5 to 2 percentage points because of...

Bharat Madan: Continue to be in the same range. So, there's no major change their related to margin profile.

Moderator: The next question is from the line of Jyoti Singh from N Capital Markets Limited.

Jyoti Singh: Sir, as most of my question got answered, so I just have one query. So how is the traction we are seeing on the nonautomotive side?

Bharat Madan: Nonautomotive means?

Jyoti Singh: I mean, sorry, nonagri side.

Bharat Madan: Nonagri. Okay. Tractor uses for nonagri, you're saying?

Jyoti Singh: Sorry?

Bharat Madan: Are you talking the tractor uses for nonagri purposes?

Jyoti Singh: Yes, sir.

Harish Lalchandani: Okay. Okay. So, 2 parts to it. As I mentioned, the tractor uses for nonagri purposes is going to see a boost this year, at least that's our estimate. Given the increase in infrastructure spend, which is a doubling as compared to last year, point number one. Two is, starting from Q2 of last year, we have had an increased focus in this particular segment, and we are consistently seeing a growth of share within that segment, and we continue to focus on the segment for F '24.

Moderator: The next question is from the line of Sameer Deshpande from Fair Deal.

Sameer Deshpande: So, Bharat Madan, congratulations, and welcome on the Board of Escorts. You really deserve the seat, and I'm happy that you are there. I hope the company prospers even better under your stewardship. Now the question is, actually, we have a capacity utilization of 90%, and we have sold 1.03 lakh tractors this year. So, we have, I think, around 101/110 or something as the capacity. Now we -- earlier, when we had -- with Kubota, we were planning to increase the capacity by about 50,000 tractors. So, what is the status of that at -- the level of that?

Bharat Madan: Yes, Sameer, you're right. So, our own capacity in EKL was close to 120,000 tractors. And with JV, we have another 50,000 tractors capacity, out of which roughly 30,000 capacity was available for users by EKL also. So overall, we had about 150,000 tractors capacity. So right now, we are at 103,000 this year. So, capacity-wise, we don't see an issue on an immediate basis.

And as we had indicated in our midterm business plan, there is a plan to double this capacity in the next 5 years, and this is one of the key projects as part of our midterm business plan. So, we'll be increasing the capacity from 150,000 to 300,000 tractors by setting up another greenfield venture within this next 5 years period.

So that will be on. So obviously, we'll ensure there's no shortage of capacity in terms of what we need in the sales requirement. This 90% capacity is only in this quarter of March. So overall, the utilization level is not 90%. So that's why it's more seasonality, which comes into play. So, there are options to keep the inventory build-up if the requirement is there for any particular season -- quarters of season months. So that can be done. So overall, so we don't see really from capacity perspective will be an issue. But yes, there are already plans to expand the capacity further.

Sameer Deshpande: And now with this -- regarding margins and tractor industry outlook, I think it was mentioned that mid-single-digits growth is possible this year. Despite this El Nino sector, etcetera, because of the good water levels and overall irrigation improving, etcetera, that is good. We are -- and even in the nonagri segment also, expected to have a good sales boost with the election year as good. But the margins you mentioned, that currently, we have about 9.8% in this quarter for tractor segment margin. So, you mentioned that earlier, we are about 14%, 15%, about 1 year back, 1.5 years back. So, are we likely to return to those levels by the end of the year?

Bharat Madan: Yes, that's what I indicated. So, both I think we're expecting the commodity prices continue to soften and then also some benefits which will flow in from some of the cost initiatives that we have undertaken this year. So, both put together should really lead us to a situation where we end the year with this sort of margin profile, which used to be there for the tractor business for us.

Sameer Deshpande: And it will keep on improving sequentially. Margins -- when margins will go on increasing sequentially...

Bharat Madan: The cost impact -- whatever cost initiative can we take, the impact will be maximum in the last quarter, because every quarter, it will keep on accruing. So definitely, in the last quarter, you'll see the maximum bit coming in. So, we think when we end this exit, we exit this clear in the last quarter. So, we should be in that range.

Sameer Deshpande: And then last question. Is this -- in our balance sheet, we had last year under current investment INR 4,587-odd crores, and now that has -- almost INR 2,785 crores have shifted to noncurrent investments. So, what actually does it mean?

Bharat Madan: So, Sameer, it is only a classification issue because the investment which is held for more than 1 year has shifted to noncurrent. Otherwise, the overall investment portfolio remains the same. So, we have close to INR 4,800 crores of liquidity on the balance sheet, which is invested in mutual funds. And that's excluding the escrow account. So -- well, if you include escrow account balance, it will be more than INR 5,000 crores at the end of March.

Sameer Deshpande: Okay. And in Construction Equipment, really, after a long time, we are seeing very good results. So, 35% of the capacity utilization had a volume of around 4,600 . We have been in a position to turn around and make some 3-odd percent on margins. So, if the capacity goes up by around 30%, 40% more during the election year, maybe 20%, 30% more, can we see the margin grow 5% to 6%?

Bharat Madan: So, Sameer, capacity depends on what product we are selling because there is a demand maybe for different products. So, some of the products, we are facing shortage of capacity today. So, there are capacity constraints, especially on the safe crane part, which is one of the key components, which is a high margin product for us. So there, we are actually not able to produce, which is why we saw some of the spill over happening from last quarter to this quarter of some volume.

So overall capacity looks like there's an issue because backhoe loader, we are not doing much. So there, we have suppressed capacity, but where we need capacity there, we have some shortage. So don't look at the overall number, but that is for the combined capacity, which is reflected in the presentation. But in the early basis, it's something what we need to really track and thus seeing how much we can grow.

Moderator: We have the next question from the line of Deepak Jain from Enam AMC.

Deepak Jain: Sir, you were having some product mix issues a few quarters back. So, are they being addressed? And in context of that, this 14% EBIT margin for the exit quarter, will it come entirely from the cost moderation or some other price hikes or some product mix improvement that eventually will also be there?

Bharat Madan: So, it will be a mix of both, I think, multiple matters. So, like we mentioned, the cost initiative on which we are looking at, then there's also some softening of commodity prices, which we are expecting will happen. So that will also lead to improvement in the margin.

And on product mix, I think it's -- compared to what we were earlier, we think some improvement which has happened in last quarter also, and same trend was there in April, too. So, we hope if that continues, so that will only help us in getting the earlier than probably in the last quarter.

Moderator: The next question is from the line of Aayush Agrawal from Molecule Venture.

Aayush Agrawal: I wanted to ask about the commodities. The commodity prices you said are expected to go down. So, in that, which commodities are you expecting the prices to soften in, rubber, castings and?

Bharat Madan: Casting, sheet metal and rubber prices, as I mentioned.

Aayush Agrawal: Okay. And could you please give us some more idea about how much of the cost of our company would be coming from castings and rubber?

Bharat Madan: So, I think we indicated in last call also last quarter, so it's almost 50% to 60% cost comes from these 2 commodities within rubber and tires and castings for tractors, which is why you did not see the impact of what we saw in the auto industry. We didn't see that impact coming in the tractor industry.

Aayush Agrawal: So, casting, separately, could you give us an idea?

Bharat Madan: Sorry?

Aayush Agrawal: Casting -- you said casting and rubber is 50% around. So, casting alone would be around?

Bharat Madan: Almost 40%, 35% to 40%.

Aayush Agrawal: 30% to 40%. And over the past also, in the current -- in FY '23, how is the -- how has the prices stand?

Bharat Madan: In FY '23, as you all know, I think when the geopolitical issue happened, so in March, April, we saw a very steep increase in the commodity prices. In a single quarter, we had seen almost 4% to 5% increase happened in this material cost for us. And only the prices coming -- started coming down from Q3 onwards very marginally. It only happened in sheet metal likely first. In casting, the price cut has only happened now. Some of them we saw in Q4. And then probably, something will happen in this quarter, too. But it's not a major change. This has happened in the casting front. So that's why you're not seeing major impact coming on the commodity savings in the tractor industry.

Aayush Agrawal: Castings, we have more than 3 suppliers? Or are they consolidated?

Bharat Madan: No, no, there are multiple suppliers for casting. There are many suppliers.

Moderator: We have a follow-up question from the line of Devika Jain from Ratnabali Investment.

Devika Jain: So, I wanted to understand how and by when we will we deploy the cash balance and where exactly -- where primarily?

Bharat Madan: So, Devika, you can refer to our mid-term business plan. We've given a capital allocation strategy there, how the money will get utilized. Because obviously, the capex planned by the company, there is certain money which we got from Kubota is meant for using the business only. It's not meant for distribution. Because that was the purpose of that money, which was being raised. So, we had given the indication how much will get spent on capex and how -- where the greenfield project has to come up with regional capacity that's created. And then within the existing capacity, a lot of changes are happening and relay out is happening there. And the product development, which is another major spend which will happen on the multiple products, which we then introduced both for domestic market as well as for export market.

So, net-net, we have given the overall indication, what will be the capital allocation strategy the company will deploy, including in the sort of distribution and the pay-out ratios, the buybacks. So, everything, I think, is spread out there.

Devika Jain: I basically wanted to understand, when will we see -- when will we start seeing some movement?

Bharat Madan: Yes, it will happen gradually. You can't expect to happen overnight. So obviously, as you see the improvement, I think, of the performance also and the numbers are moving up, so these things will also start getting better. So, you've seen the dividend itself this year. We have maintained the same issue as last year. The pay-out actually has gone up compared to what we had last year. So, idea is to gradually move up to the level what we had indicated in our mid-term business plan.

Devika Jain: Okay. And if we have any inorganic opportunities that we are exploring.

Bharat Madan: So, if something comes to us, definitely, we'll look at that.

Moderator: Ladies and gentlemen, due to time constraint, which was the last question for today. I would now like to hand the conference over to Mr. Bharat Madan for closing comments. Over to you, sir.

Bharat Madan: Thank you, ladies, and gentlemen, for being present on this call. For any feedback and/or queries, please feel free to write into us at investor.relation@escortskubota.com. Thank you very much and have a good evening.

Moderator: Thank you, sir. On behalf of Emkay Global Financial Services, which concludes this conference. Thank you for joining us, and you may now disconnect your lines.