Date: 2nd March 2023

National Stock Exchange of India Limited,	BSE Limited,
"Exchange Plaza" 5th Floor, Plot No. C-1, G Block, Bandra Kurla Complex, Bandra (East), Mumbai – 400051	Phiroze Jeejeebhoy Towers, Dalal Street, Mumbai - 400001
NSE Scrip Code – SKFINDIA	**BSE Scrip Code -500472**

Dear Sirs/Madam,

Sub: TRANSCRIPT OF ANALYST/INSTITUTIONAL INVESTOR MEETING ON FEBRUARY 23, 2023.

Reference: Intimation Dated 20th February 2023 for Meeting & Intimation dated 24th February 2023 for Audio Link.

Pursuant to Clause 15(b) of Schedule III, Part A, Para A read with Regulation 30 (2), Regulation 30 (6) & Regulation 46(2) of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (as amended from time to time) ("SEBI LODR"), please find enclosed herewith transcript of Analyst / Institutional Investor Meeting on 23rd February 2023.

Transcript will also be available on the website of the company.

We request you to take the above information on record and disseminate the same on your respective websites.

Thanking you,

Yours faithfully,
SKF India Limited

RANJAN KUMAR

Digitally signed by RANJAN KUMAR
DN: cn=RANJAN KUMAR, c=IN, o=PERSONAL, email=ranjan.kumar@skf.com
Date: 2023.03.02 19:54:26 +05'30'

Ranjan Kumar
Company Secretary & Compliance Officer

“SKF India Limited

Analyst Conference Call”

February 28, 2023

MANAGEMENT:

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Ashish Saraf (SKF): Again to be honest, nothing much has changed compared to, I think what, when we spoke last six months back. I think we are on a similar trajectory. If you look at the environment at such still globally, it still continues to be volatile. So as a company I think we continue. We know that India is an outlier compared to the global market.

So, from an India perspective aspect nothing has changed. Again, the growth story continues to remain. We continue to focus on driving profitable growth for the company both in the industrial segment and the automotive segment. And I would say the challenges around inflation continue to remain as a company. So we continue to kind of work with our customers to make sure we kind of offset that with getting the necessary price increases from the market, if needed.

And definitely again, I would say 2023 based on the GDP predictions and the inflation, I think both of them are going to hopefully slowdown. So to that extent I think we should see some impact on the growth as we're going forward. But overall, I think we are on a right trajectory, if you've seen the last quarter results as well, I think the results with respect to all the financial parameters have been relatively good.

Mirae Asset: Just on financial note that we obviously have much on quarterly -- but last two quarters your gross margin has been have been very strong in an inflationary environment. I think in Q3 there were some other expenses that impacted the overall margin. But still gross margin has been very strong in the last two quarter, so…

Ashish Saraf (SKF): So as I said, primarily, the reasons why our gross margin has been higher is, one is, we've had impact on a lot of inflation. So as a company we are focused on making sure that we are offsetting those costs. So we are taking a lot of proactive steps since last year, where we are continuously looking at our cost, which is kind of helping us offset. Secondly as a company, I think one of the strategic decisions that we took in 2022 is that we want to drive profitable growth.

So lot of things that we are doing around portfolio management, looking at our mix, so looking at our customers, which are loss making, going back to those customers and asking for either a price increase or changing the mix of the products or exiting some of the loss making business if needed to make sure that we improve our gross margins. So adding all of these things have kind of helped us in terms of improving our profitability.

Mirae Asset: Okay, so mix which used to be typically 50:50 industrial/auto that has changed?

Ashish Saraf (SKF): That has changed, right. So, if you look at our mix currently around industrial is around 50%, automotive is around 42% and exports is around 8%. So we as a company see that our industrial is good. See typically if you look at SKF, globally, 70% is industrial and 30% is automotive. In India is an outlier because traditionally it was started off as an automotive company and gradually it became industrial. So that's where you see a lot more or a faster growth happening on the industrial side.

Having said that, we continue to have the same level of focus on the automotive market as well. So it's not that, we are moving away from the automotive market, but definitely India is a growing market across industry. All industry, all sectors are growing. So there is a lot more potential to grow in the industrial side compared to the automotive side.

Mirae Asset: But over here, I am really confused because industrial, a large portion is imported or either purchased from SKF Technologies. So in a way that should be a lower gross margin business for us, is that understanding correct?

Ashish Saraf (SKF): That is right, in a sense that because it's a traded product. So if you look at our industrial, 35% of our products are manufactured locally, 65% of our products are still imported. So we as a company, one of the focus is to localize and improve our localization effort. As we localize, our margins should improve. On the traded products, relatively our margins are lower because the larger business risk is taken by the manufacturing entity and not by the selling entity. So relatively the margins are lower for traded products compared to own manufacturing.

Mirae Asset: Within the 65%, how much do we source, let's say locally from SKF Technology and how much might be the imported?

Mirae Asset: Yeah, on the flip side of the question is, 35% includes, when it's a local sourcing, it includes sourcing from SKF Technology or it is like manufactured within SKF, the listed entity?

Ashish Saraf (SKF): See overall, if you look at SKF India, around 58% of our entire production is local and the remaining 42% is imported at an overall SKF India level. I was answering you a question specifically for the industrial business. For the industrial business, 65% is imported or either imported or purchased from SCLI and 35% is basically manufactured in SKF India.

Mirae Asset: So that was the point. I think that when you say within industry, 65% is trading within that, let's say how much might be the SKF Technologies portion and how much might be the direct portion?

Ashish Saraf (SKF): I don't have a number right now in front of me to tell you exactly that.

Mirae Asset: And but just overall perspective on this, when you localize a product in SKF Technology, so does it benefit the listed entity also in terms of margins or the entire benefit is retained by SKF Technology? Just trying to understand the thought process?

Ashish Saraf (SKF): There are two aspects to it. One is, its definitely helpful to SKF India from a perspective that once we localize a product in India, you are able to source better, you are able to manufacture it at a cheaper rate. Whether you are manufacturing it in SKF India or SCL IPL, it doesn't matter. The other entity of it -- the non-listed entity of SKF. So one is sourcing is better, you localize, availability for our customers are better because you are able to supply products to a customer.

We are far more competitive because the competition is manufacturing that product in India. We are insulated to the inflationary impact that we are seeing in Europe. So with that, we are able to grow well in the Indian market.

Now, in terms of margins, the margins will be similar from a perspective that what we have for an imported product, it will be similar to what we have with the local entity vendor because they are pretty much governed on the same routes.

Mirae Asset: But obviously, if cost of manufacturing goes down, that helps you in terms of increasing volume?

Ashish Saraf (SKF): That helps me increasing the volumes and getting a better market share. The other thing which you need to look at it is that, from an investment standpoint, SKF India is also like recently in the last quarter, we got an approval to do an intercompany investment. So we basically went and gave a loan to a sister entity, which is also where SKF India will earn interest. So it may not reflect directly in your PBT, but it will come in as another income. In terms of your -- it may not be a direct business income, but it will come in as another income on the total investments that we are making.

Mirae Asset: This through the SKF Technologies, how much is the amount that's invested?

Ashish Saraf (SKF): We have created a credit line, so it's not that we have kind of offered it as of now, but around MINR 2500 is what we have kind of – INR 250 crores. So that's what we've kind of got an approval for from the shareholders, as well as from the Board the last quarter.

Mirae Asset: What's sort of interest rate?

Ashish Saraf (SKF): So that is basically market linked. So I think its seven-year yield interest rate plus 150 basis points. So it's going to be roughly in the current market, I would say easily 9%.

Mirae Asset: I mean, this SKF Technology it has become profitable or its still in a loss?

Ashish Saraf (SKF): So SKF Technology is currently, I think at overall level, I'll have to check the numbers -- I would say it's currently at a breakeven level. It's not that it's not at an EBITDA level. So it's not that it's making a lot of money right now. It's got other businesses apart from the bearing business, got some other businesses as well. So they make lubrication products as well as seals.

Mirae Asset: Coming back to the core verticals and how much is the exports you can elaborate on that. But we have a good auto year in a domestic market and the base of going to high it's probably very modest growth from here. So is there any outlook or guidance you're suggesting next two years, let's say on this?

Ashish Saraf (SKF): See, we are not giving any outlook or guidance as such. But again, in the automotive sector also we see tremendous potential. One is, yes, two-wheeler is a market which is currently getting challenged from a perspective that exports are down for all the two-wheeler sector and that's kind of impacting the overall growth. But if you look at the only two-wheeler, two wheeler is almost 10% of our total business. So, it's not having such a significant impact.

We are seeing strong growth in passenger vehicles, we are seeing strong growth in commercial vehicle market and if you look at our VSM or automotive aftermarket that is also growing well from a perspective that, our strategy of reach, range and availability is kind of helping us. If you look at -- earlier our penetration in the aftermarket was probably 50% to 60% and the last one year we have kind of focused on increasing our availability by appointing lot many distributors across India.

So that's kind of helped us improve our overall reach to 70% and slowly and gradually it's increasing. So there is a lot of potential in terms of pure market penetration and what we are also doing is, we are trying to ensure that we increase availability, as well as range for our products which is going to kind of help us grow in the automotive sector.

Mirae Asset: So here after the replacement market, how are the trends of imports from China and is that also changing?

Ashish Saraf (SKF): Not really. I would say that overall the market remains like people who are typically buying SKF they are buying because the challenge for us is, more of counterfeit bearings and availability so we are kind of addressing that by ensuring that there is availability of our products. If you look at in the aftermarket what end customers or retailers are really constrained as to whether I need this type of bearing, is this bearing available for me to set? So that's what we are focusing on. Where we are kind of working with our distributors to make sure that we make availability, like create last mile availability for our network so that its kind of helpful. And that is where we are seeing signs of growth coming in in the VSM market and similarly on the industrial side as well.

Mirae Asset: Through this kind of background. You think autos can touch the overall thing, including replacement can touch double digit?

Ashish Saraf (SKF): See the way overall, I would say overall, considering the economic situation where we are in and we don't know how the future would be, typically if I look at our GDP is expected to grow between anytime between 6% to 7%. Inflation is going to be around 5%. So if you look at 12% is the bare minimum, I would say as a company that we are targeting at for next year at an overall level.

Yes. Again, internally we are even trying to aim higher. But it has to be like one of the things that we have kind of set a goal ask for ourselves is that it has to be a profitable growth. Unfortunately, in the past we had a good amount of customer base, especially in the OEM side where we're not making money, but we're still doing large volumes. We are kind of focused as to how we can turn that around for us, so that it's kind of return for us as well as for our shareholders.

Mirae Asset: Including industrial as well?

Ashish Saraf (SKF): I'm talking about overall in general for SKF. Again, it's not a formal guidance…

Mirae Asset: Mr. Bhatnagar was on television interview recently and he gave some sense about margins going forward. So, I mean, what's the internal thought process because Q1 and Q2, it was around 19 odd percent and Q3 was 17%...

Ashish Saraf (SKF): I saw that interview as well. It's a mix of, I would say, manufacturing margin and trading margin. And I would say the margins that you see right now is relatively what we as a company aim at. But for traded products, it's kind of governed by the transfer pricing rules as well. So, because of which there could be like a couple of percentage up and down on an overall basis.

Because what happens is that, it's kind of calculated on a transaction net margin method which is dependent on what price I've actually sold to the customer and then what is it that I should be kind of passing it on. And I cannot do that real time. It always happen in a lag. So because of that, you might always see a bit of a fluctuation in the overall margin. But our overall guidance is that we want to be in the similar range of 17% to 20%. It's not a guidance. That's what as a management, we are trying to come up with.

Mirae Asset: Transfer pricing calculation happens on a yearly basis, it is once in a year?

Ashish Saraf (SKF): That’s right.

Mirae Asset: So quarterly provision might be – so generally on this traded goods, let's say in your own manufactured portfolio, if you are ended up making 20%, so does the traded goods, you end up making 15% and that is how blended 17%, 18%?

Ashish Saraf (SKF): See the way in a transaction, net margin method as I said the risk for a selling entity is lower compared to manufacturing entity. So in that kind of environment, even if I sell a product at a loss, I will make a margin in SKF India. It’s so controlled because the major risk is kind of managed by the manufacturing unit or borne by the manufacturing unit.

So relatively the margins are lower compared to manufacturing margin, that's why our focus is to increase localization and that will help us kind of improve profitability for the business. The more localization we do, there will be a bigger risk as a company that we would be able to take and that will kind of help us drive a higher margin for us.

Mirae Asset: That's why we are trying to understand, what is that net margin that…

Ashish Saraf (SKF): I cannot give a fix number.

Mirae Asset: Give us range or some indication. It will be helpful in our modelling.

Ashish Saraf (SKF): See it varies. As I said, overall, I would say typically 6% to 8% is what is a transfer pricing guideline, which is there for a traded product. But it can go up as well because I cannot go if I have sold something at a higher margin, I will not go and reverse it on a full year basis. The tax rules doesn't allow me to do that. Because I am importing this product, so I cannot go and change the price of the product at which I imported.

Mirae Asset: The adjustment will happen next year?

Ashish Saraf (SKF): So that adjustment will not happen next year. Once the financial year is closed, it's closed. It's a start again from zero. So typical guidance is 6% to 8% but in some years we have done way higher than that. In some years you have done slightly lower, so its very, very relatively difficult. But typical guidance is 6% to 8%.

Mirae Asset: So for the balanced portfolio you are like 30% or maybe higher margin?

Ashish Saraf (SKF): Again, as I said, it depends in a sense of what I am doing. And my traded product margin has been, to give you an example, has been actual margin has been way higher compared to what it should be for this fiscal year.

Mirae Asset: So when you say increase let say, localization manufacturing at an entity level, you said 58% is local manufacturing and with an industrial, obviously that proportion is lower. So are we trying to put more sort of capex or is it a function of certain threshold volumes and then only you can localize?

Ashish Saraf (SKF): So again, for the automotive sector it's easily to put in capex because you get a visibility of the volumes upfront. Like when you're manufacturing, say for Bajaj, you know what kind of volumes they're going to buy. So, it's much more easier to put in the capex. Whereas in industrial there are lot of SKUs. It's practically not possible to have 100% localized because for a certain bearing you might be only selling 5,000 quantities. So it may not make sense for us to put a full channel.

Plus, you also need to have a like typically industrial bearings require different grades of steel which requires vendor support infrastructure as well. So they have to go through a certain steel qualification. So we have to create a entire -- it's not just setting up a new channel, but we also have to create a entire supply chain to kind of support our industrial business.

So that is where it takes a lot more effort in terms of localizing an industrial bearing because we have to look at demand as to whether we'll have enough demand for us to cater to the Indian market and we have now in fact looking at an overall SKF Group strategy level we are also looking at Southeast Asia as to where can we cater to the Southeast Asian market as well.

So looking at those aspects, we are making a decision of whether to do capex investments.

Mirae Asset: Southeast Asia from India?

Ashish Saraf (SKF): Basically Manish, who is also responsible for Southeast Asia market as well. So wherever feasible, when we are looking at making investments, if there is a demand requirement for India, as well as a similar demand requirement for Southeast Asia, we are evaluating the total demand and then making a decision with respect to investments.

Mirae Asset: As a question, there are certain assumptions you might have had on capex, but is there anything you are suggesting?

Ashish Saraf (SKF): Yes, as I said. And the other aspect that you also need to understand is that SKF India predominantly has the capability to manufacture small size bearings. Whereas the other entity has capability to manufacture in mid and large size bearings. So the investments, when we're talking about industrial, most of the bearings would typically fall in mid and large size category. And that is where the investments are going in that because our Ahmedabad factory has capability to manufacture mid and large size bearings.

And that is where we can establish a credit line to make that investment there. So at an overall basis, yes, our investments are going up. You may not see that significant spike in SKF India, because SKF India, the investments would be predominantly for the smaller size bearings for automotive market or for industrial, where the size of the bearings are smaller in nature.

Even for SKF India, you would see a spike compared to last year, you would have seen there are the investments that slightly gone up. But you may not see such a significant spike, even though at an overall level we are making investments, if you combine both entities together, there is far more investments going in.

Mirae Asset: For the listed company, are you looking at somewhere around INR 100 crores?

Ashish Saraf (SKF): I would say somewhere between INR 100 crores to INR 150 crores is what we are looking at.

Mirae Asset: So any specific area where, let's say, some of these investments in, let's say, SKF Technologies, the other entity specific area which might help us…

Ashish Saraf (SKF): See our focus as a company, as a strategy in India, the way we are looking at industrial, we see growth happening in heavy industries. We see growth happening in construction sector. We see growth happening in drives. We see growth happening in railways and wind to a certain extent, because of the sustainability drive. Basically, the entire globe is moving towards sustainability. So these are the sectors. So typically our focus is to put in investments in these sectors from the industrial side.

On the automotive side, predominantly our investments are linked where we are working with our large customers and depending on the requirements and how their demand evolves. We are making more investments in automotive side.

Mirae Asset: Out of these four, five sub-segments, where lies the most opportunity where we can bring down overall cost and can let's try to gain market share or where, as of now, we might be weaker in there...

Ashish Saraf (SKF): As I said, our focus is on these heavy industry, construction and drives. These are the three sectors which we are focusing on because we feel India growth story will be infrastructure. And that is where the market will grow and we will grow along with that. And that is where we are making investments in those sectors to localize, so that we are equally competitive in the market and we are able to grow with them.

Mirae Asset: These four sectors, heavy industry, drives, rail and wind…

Ashish Saraf (SKF): Heavy industry, drives and construction.

Mirae Asset: Construction and rail is also in that railways and drive,,,

Ashish Saraf (SKF): Railway is definitely we are focusing on. In both these sectors, we have a bit of a challenge on profitability. Railways and wind. So that is where, as I said, the focus is to drive profitable growth. So we want to be really, really make sure that we are cost competitive in these two sectors and then drive profitable growth for the business.

Mirae Asset: But my question is for these sectors, these are mid and heavy. So, when you say capex, whatever investment is going to be done through technology?

Ashish Saraf (SKF): In the industrial side.

Mirae Asset: And not in the construction, not in the drive. Drives and construction will be through listed?

Ashish Saraf (SKF): Yeah. So say for example, drives would require smaller size bearing. So there the investments will happen through SKF India Company.

Mirae Asset: And what about you mentioning is the profitability challenge in rail and wind. So these are mid and smaller or are these…

Ashish Saraf (SKF): These are large sized bearings.

Mirae Asset: We are coming from the listed committee -- falling more is the domain and the economies of these…

Ashish Saraf (SKF): But we are selling through SKF India. So all of the sales happen through SKF India. So effectively it will come to SKF India. But yeah, in terms of manufacturing, currently either they are imported or manufactured out of Ahmedabad, which is through the non-listed entity.

Mirae Asset: Including for railways and the wind. So what's the way there; how do you get that economy…

Mirae Asset: Ultimately it's a two clear market. If I'm not Timken and you and still you are saying it's very competitive.

Ashish Saraf (SKF): It's not same thing with railway. It's a tender business. So railway will typically look at costs only while deciding on quality.

Mirae Asset: It's too critical for them to compromise.

Ashish Saraf (SKF): But it goes through a tender. See, they have their own process of validating whether the bearing will meet their requirements or not. So there's a separate exercise. But typically once you qualify then in terms of decision making as to whether they want to go with a particular vendor or not, it's always Ll, which is the lowest bidder. So it's all governed by that. So that is where we see challenges on profitability and that is where we are kind of having a lot of projects internally to drive costs.

Mirae Asset: And otherwise headline news would suggest that a lot of potential railways you have the Vande Bharat...

Ashish Saraf (SKF): That we are growing. I think it's not that all sectors of railway we are having a profitability challenge, but definitely some sub sectors within railways is where we see some challenges.

Mirae Asset: Overall, we will have what, 30%, 40% market share in railway?

Ashish Saraf (SKF): I think it will be lower. See, because there is not just Timken, there's NEI also and there is a Schaeffler also.

Mirae Asset: And this profitability wise you are saying some of the sub segment challenge is also because your extent of manufacturing and localization might be lower versus other players?

Ashish Saraf (SKF): That's right.

Mirae Asset: Just coming back on this nine-month number, 22% sales growth, what could be the bulk of volume growth for us?

Ashish Saraf (SKF): I would say 50:50

Mirae Asset: And 11% volume growth also. But pricing growth will also be so…

Ashish Saraf (SKF): It is again, I can't differentiate between price and mix. So when I say 10%, 11%, it's price and mix put together and remaining 10% is volume.

Mirae Asset: And growth across different vertical how it might have been, let's say during nine months, your automotive and industrial, just ballpark?

Ashish Saraf (SKF): We have seen growth across all our segments. But if you ask me, in the automotive sector, we have seen growth in our car division, trucks division, even two-wheeler division. And on the industrial side, we are seeing growth on metals, on wind, on distribution, on general machinery, as well as railways. So, again, in terms of sector, all sectors have grown for us.

Mirae Asset: Headline level, let's say automotive as a bucket put together might have grown out of, let's say this 22% is complete?

Ashish Saraf (SKF): No, both are equal. Both are equal. In terms of industrial and automotive, both are grown at around 25% each and exports have grown by 1%. Because as a company we've kind of relatively less focused on exports compared to the domestic market.

Mirae Asset: And aftermarket also have grown at around similar base 25%, let's say within both auto as well as industry?

Ashish Saraf (SKF): More for industrial, industrial aftermarket has grown at around 25%, whereas automotive aftermarket is grown by around 14%.

Mirae Asset: How is the progress on REP and how much it is contributing now?

Ashish Saraf (SKF): So, overall as a services business, our objective is that, it should become at least 5%-6% of our overall revenue. As a company, we are not just looking only at REP. Yes, REP is one of the products which has got a lot of potential. But as a company, at an overall level, we are looking at least having services business around 5% to 6% of our total revenue.

Mirae Asset: Which is as of now is 1% to 2%?

Ashish Saraf (SKF): I would say 2% to 3%.

Mirae Asset: And just on the export piece, so I know you have huge facilities in China as well. And yet sometimes we used to hear statement that you also kind of become bigger suppliers in the global ecosystem within this year. How is that panning out? Because on one hand you are saying that it's not such a focus area. And you know we hear of this China +1 and all those things. So is there any tailwind you are getting?

Mirae Asset: And just to extend this question, actually our competitors, they have talked a lot about India being a manufacturing hub. If I can name Scheffler and Timken in India they are really doing a lot of exports…

Mirae Asset: Last time Manish was saying that positioning or time position itself is a global thing. Is it that outcome is known that there is no go and therefore now you are saying no or are they not?

Ashish Saraf (SKF): I wouldn't say that there is no go. It's not that we are, but as a company, our focus, my focus or Manish's focus is to grow the local market which is India market and grow in that. Typically SKF has a regionalized supply chain given the volatility that we saw in the last few years. Group at a global level said that we will have a regionalized supply chain network. So when we say regionalized, India and South East Asia is one region. And that is where we are predominantly focused on in terms of growing our market.

So from India, yes, there could be export potential to South East Asian markets. And that we would be focusing on. But we may not focus outside of South East Asia at this point of time. If it happens, because we have excess capacity and they don't have capacity, yes it will naturally happen through that process.

But our predominant focus is to cater to the India market and with Manish's larger responsibility of South East Asia, definitely if there is opportunity in the South East Asian market we are looking at a regional level to see if we can cater that demand for South East Asia.

Mirae Asset: Southeast Asia, excluding China and Japan?

Ashish Saraf (SKF): Excluding China and Japan.

Mirae Asset: How big is that market as of now?

Ashish Saraf (SKF): It is as big as India.

Mirea Asset: And that is as of now, being catered from, let's say, a parent entity?

Ashish Saraf (SKF): There are other sister companies which are catering to that market, but they are sourcing products from predominantly Europe and China. They do not have a big manufacturing base locally in Southeast Asia market. So when we say that we will serve from India, we will probably export from India to those countries who will eventually go and sell in those markets. We will not go and directly sell to the customers.

Mirae Asset: And this automotive be a bigger piece?

Ashish Saraf: Automotive and industrial.

Mirae Asset: So industrial exports will happen, that also will happen through you or directly from SKF Technology?

Ashish Saraf (SKF): If we are manufacturing in SKF India, because it's not that we don't we still manufacture some products for industrial as well in SKF India. So that will continue to get exported from India. If it is getting manufactured in our other company, then it will get directly exported. So that will not come to this entity.

Mirae Asset: Just one thing this is a costing of manufacturing. The range you to do through the listed companies get India both for auto and maybe a little bit in the industrial, is there any reasonable advantage or differential versus the global cost of manufacturing or is it very similar?

Ashish Saraf (SKF): No, there is an advantage. There is definitely an advantage. Especially now, factories in Europe are far more expensive compared to what we can manufacture. So there is definitely a cost advantage that we are seeing and that is where our focus is, how quickly -- depending on our strategy, where we clearly see a visibility because it has to make a business case for us.

If there is only 5,000 bearings demand and I have a channel which can make one lakh bearing, I cannot go and even though, though it is much cheaper to make in India, it doesn't make financially any sense for me to set up that channel in India. So looking at those potential where there is enough demand in the Indian market and I can have a good utilization of that channel, I am going and setting up those manufacturing channels in India.

Mirae Asset: And similarly with China because the impression is that manpower cost has gone up many fold over the last few years is it providing any edge or is it still they've got other competitive edge on other costs?

Ashish Saraf (SKF): So again, China market, the way we are in SKF is predominantly their market itself locally is very big. So it's not that we are importing a significant stuff from China right now. Currently, most of our imports are from Europe. And where we definitely see a significant cost advantage if you localize it in India.

Mirae Asset: I'll definitely go to the South East Asia market, you are open to – so are these Chinese cost of manufacturing, the Chinese SKF opportunity reasonably similar or is it much higher giving you an advantage or a chance?

Ashish Saraf (SKF): I would say, similar to what we would say manufacture in India. They are much cheaper compared to Europe.

Mirae Asset: But in the rest of India you are saying the same thing. Because otherwise the impression we have that labor is now very has become costlier seeing it doesn't operate?

Ashish Saraf (SKF): So it's not -- if you I know I'm not sure if you've seen our channel, but it's not really labor intensive.

Mirae Asset: 8%, 9% of your labor.

Ashish Saraf (SKF): Yeah, but it's not labor. It's all management: plus labor. And everything is probably 8%, 9%. But if you look at our channel, it's not that it's a very, very labor-intensive industry. It's pretty much end to end automated. So relatively, it's not a very significant amount of our cost.

Mirae Asset: How big the Southeast Asian export opportunity have you evaluated…

Ashish Saraf (SKF): As I said, our focus is to focus on the Indian market. So, we have not evaluated Southeast Asia. The way we are looking at Southeast Asian market is only from an India perspective that there is a demand for this product. Does it make sense for us to localize in India and whether we have the volumes for us to set up that manufacturing facility.

If we don't have sufficient volumes, can we go and look at Southeast Asian market and see whether they have the volumes and combined together whether it makes financial sense for us. So we are more so looking at it from that point. So, the resultant impact on the financials is something we'll get to know once we kind of set up that manufacturing facility. But it's not that okay. We're looking at it saying, okay, this is the market opportunity in Southeast Asia, so let's go and make an investment.

Mirae Asset: Then this will start from immediately or there is some time?

Ashish Saraf (SKF): We are already doing the evaluation. Typical timeline to set up a channel once it is approved internally from all our stakeholders. Typically 12 months, before you start production. So if I today decide to make an investment, it'll take 12 months. By end of the year through 2024, you will start seeing that.

Mirae Asset: How much capex the other entity might be doing. Any sense on their let's current growth…

Ashish Saraf (SKF): As I told you that we are giving them a credit line of INR 250 crores which we expect to get utilized in the next two years.

Mirae Asset: I mean, if you were to invest the money yourself, the returns are better or you give it a higher dividend payout, either. This seems like a lease preferred keeping that 8% -- financial opportunity.

Ashish Saraf (SKF): But it's not a question of just that. It's a question also that whether you have that expertise in house. For me to build that capability in SKF India will take much longer time. Whereas the other company already has that capability, has that infrastructure. So my investment as a company would also at an overall group level would also significantly increase.

To give you an example, there is a heat treatment plant in Ahmedabad factory, which is basically a requirement for large size bearing. That capability is not there in any of my manufacturing plants in India. For example, to do those kind of large size bearings. So now if I want to do manufacturing of that bearing in India, in SKF India, then I have to set up that heat treatment. So that also requires another level of capex investment.

So my capex investment as an overall level will significantly change. And it may not make financial sense then for the company to make that investment. So we have to kind of juggle between all of that and then take a decision as to where to make that capex investment.

Mirae Asset: Any reason to keep two separate entities in India and have you evaluated merger between them?

Ashish Saraf (SKF): At this point no.

Mirae Asset: Is Manish responsible for the Management: of the listed company only or both?

Ashish Saraf (SKF): So at an overall level, Manish is the Managing Director for SKF India. He is, since we buy industrial products from the other entity and all that. But he's not on the management of that entity.

Mirae Asset: Okay. It has his own separate CEO.

Ashish Saraf (SKF): It has a set of Board of Directors. So Manish works closely because they are part of the overall SKF group. So we work closely between both entities.

Mirae Asset: How are transfer pricing norms determined?

Ashish Saraf (SKF): Those are determined purely based on the tax laws which are there in India, as well as based on the OECD guidelines. So it is not something that is determined by us. It is purely the OECD guidelines, which is kind of-- you guys can go and read it.

As I said, it's kind of done based on the transaction net margin method, which is also an established process. It is kind of looked at by Big Four firms every year to make that assessment as to whether these norms have been followed, we are audited. Plus the tax officer in India also looks at it every year. So we have to comply with all the norms around that.

Mirae Asset: In this journey of further localization and capturing growth for the future, are you looking at it in organic way or ?

Ashish Saraf (SKF): We are looking at inorganic growth as well. But yeah, we have to find a right candidate

Mirae Asset: Any particular area, capability?

Ashish Saraf (SKF): Nothing as of now. And it has to be at the right price as well. A lot of in between when we were exploring, I think the prices that these players were asking, was not making financial sense.

Mirae Asset: Any moderated price?

Ashish Saraf (SKF): Again, difficult to comment at this point.

Mirae Asset: Are you evaluating introducing new products in the listed entity?

Ashish Saraf (SKF): We are continuously introducing new products. Because all our sales for other industrial or automotive happens through SKF India. So there is a continuous drive to introduce new products all the time.

Mirae Asset: So apart from bearings, which other significant products are?

Ashish Saraf (SKF): We sell a lot of non-bearing products. We sell seals, we sell mapro products, we sell power transmissions, we sell greases. A lot of those products are already sold by SKF India.

Mirae Asset: So what is ratio of sales?

Ashish Saraf (SKF): I have to look at the numbers.

Mirae Asset: But is it significant?

Ashish Saraf (SKF): I would say yes. At an overall level, I would think they would easily be 5% to 10%, if I'm not wrong. But again, very difficult. Maybe next time I think you will answer on this.

Mirae Asset: And just related to this whole move towards electrification. So your products, how well placed are they and can you break it up – 2W, PV, so on?

Ashish Saraf (SKF): And then we are very much there. If you look at we have all the products which are needed in the EV space. Right now the focus is predominantly two wheelers in the Indian market. Yes, we are already there with Ola, we are already there with Ather. So they are already buying from us and we are continuously working with them to expand our portfolio as well as with other vendors. We are working with TVS, as well, I was coming to the four-wheeler.

We are working closely with Tata's, Tata Nexon on other products. On the EV space we are pretty much there. We are pretty much working with all of them. Globally we have already built strong connect with Tesla and all that. We are supplying to them already. So we are very much there on the EV space. That is a big growth strategy for us.

Mirae Asset: And in China, not that it is relevant to India, but internally …

Ashish Saraf (SKF): I will have limited knowledge on that, to be honest, specifically on China. But globally I can say that at least what I've seen at a global level on the EV space, if I remember correctly, we are growing more than 40%, 50% quarter on quarter or year over year. There's a tremendous growth that we are seeing on the EV space. And globally we are tying up with all the large players. So it's a big growth strategy in the automotive space for us.

Mirae Asset: So India, two-wheelers is the faster growing. At this stage you are importing and supplying or what is the arrangement like?

Ashish Saraf (SKF): Again, we are importing as well. Plus, I think some of the bearings, even on the two-wheeler space we are locally supplying. So it's not that they are not getting locally manufactured because maybe the technology again, I have relatively limited knowledge on this, but maybe there is not much of a technology difference to that extent in some of the bearings and that's what basically getting locally manufactured because we already had a channel in place, but plus we continue to import as well.

Mirae Asset: So fair to say complexity of product is a bit lower for two wheelers EV and for four wheelers EV need more complexity?

Ashish Saraf (SKF): Yes, I think it's a long way ahead. It's more in the news right now. ceramic bearing, magnetic bearing I think the focus is on low friction right now is what I understand. Ceramic bearings and magnetic bearing are going to come. They are going to take some time before they kind of really evolve in the Indian market.

Mirae Asset: How much benefit be might have got because of this pruning of some of the lower profitable customers?

Ashish Saraf (SKF): Again, difficult to quantify in terms of value. What I can tell you as a company we are looking at each and every customer where we are making a loss or where we are not making money, we are going back and talking to them. So difficult for me to quantify in terms of what we have been able to turn around already. But the focus is pretty much like our day-to-day push is to go talk to each and every customer and basically negotiate a better price with them.

Mirae Asset: Because it is something very commendable. If I look into last 7, 8 years margin range 14%, 15% back and we are talking about 17 to 20 that too in an inflationary climate. So something fundamentally might have changed apart from maybe product mix here and there because still I think we haven't seen much…

Ashish Saraf (SKF): Fundamentally. as I said, one of the things is definitely portfolio management. As a company, I think, see, one of the things that we need to understand is that as a company, SKF, the way we used to measure performance internally, we used to measure performance based on standard costs earlier. And in the last couple of years, because of COVID happened and then the supply chain disruption happened, and then Ukraine Russia War happened, as a company and the group management, we decided that we need to move to actual cost.

And that has as a company brought in a lot more visibility within our organizations to see okay, which products we are making money, which products we are not making money, which customers we are losing money. And that insight itself has kind of helped us significantly to bring that focus in and that kind of help us improve you improve the processes within the company as well as brought in that insight because people used to think we were to grow our top line and profitability will automatically happen. Let's increase the utilization of our factories and the profitability will automatically happen. So I think that mindset shift has significantly helped us improve a lot.

Mirae Asset: Growth might not be most optimal, but hopefully…

Ashish Saraf (SKF): As I said, our focus is profitable growth. We will not sign up a customer unless it is very strategic. If it is a loss-making customer, we will probably not sign up with them. So we will be happy to compromise the growth if needed if not making money.

Mirae Asset: Sure. Just in this context, over the last three, five years, in terms of the intensity and pressure from other players, has there been similar or anything worst seen here, including imports?

Ashish Saraf (SKF): I think our competition is also under similar kind of pressure. Like whether you talk about Schaeffler or Timken, I think they are also feeling the heat of inflation and at least whatever insights that I have got, they are taking similar price increases the way we have taken in the market as well. So I think they are also feeling the same kind of pressure. I think Schaeffler still continuing to import a lot of stuff from outside of India. Timken is also, I believe, importing a lot of stuff they are, I heard that they're making a significant investment, but they still continue to import a lot of stuff.

So as such, we are not feeling that pressure. SKF as a product, we always sell at a premium compared to our competition. So as a company, we will always have that pressure. We will always have a pricing differentiation with our competitors, but we are okay with that because we know that our product and our brand is far more valuable in the market.

Mirae Asset: Just going back to that electrification question for two wheelers. So you might have had a certain market share with the two wheelers so far. And how is it trending in the new electric two-wheeler category? Is it similar to your legacy ICE share?

Ashish Saraf (SKF): As I said, I think the market share is again, I don't have a specific number of what is my market share within the EV space. But I would say, as I said, we are with them, we are in the process. Our strategy in the automotive sector is to focus on building strategic relationships, focus on key account management and expand our relationships across the automotive sector, especially in the OEM space. Having said that, we don't want to do business, you're not going to make money.

If Schaeffler goes and gives a very low price for a product, we will probably exit that business. So that's been a pretty much our focus. But in terms of making sure that we work with our customers, build relationship, create availability for our products, develop products jointly for them so that we can kind of grew along with them, that's pretty much our focus in the automotive space and in the OEM space.

Mirae Asset: And in the OEM electric space….. is it the same name of competition or is it lesser?

Ashish Saraf (SKF): There are many players in the OEM space. Like if you look at a lot of new names who are there in the market. We are basically working with all of them.

Mirae Asset: As suppliers besides you, is it the same cohort of suppliers who are there in the ICE or is it lesser or more?

Ashish Saraf (SKF): Again, difficult for me to answer. I would think it would be the same sort of suppliers like us because typically I would think that two-wheeler electric market requires much more technologically advanced bearing, in terms of friction and all that. So typically it will be with players like SKF, Schaeffler and all who would basically be gaining a bigger market share because they will have the right set of technology in this field set to support that. But this is more of me conjecture rather than giving you a clear data point.

Mirae Asset: Just a few couple of questions for my side. Can you give a breakup of automotive OEM, automotive export and industrial after market?

Ashish Saraf (SKF): Again broadly I give you in terms of percentage. So automotive overall automotive is 40%. As I said 30% is OEM or 10% is aftermarket. Similarly industrial is 50%, - 51%, 25% is after market, rest 25% is OEM and the rest 8% is exports pretty much.

Mirae Asset: And some sort of sense on the industry wise business within industrial like railway and heavy industries?

Ashish Saraf (SKF): As I said within that 7-odd percent -- I'm talking about overall out of 100% 7% is railways, Again similarly general machine, the same range wind also in the similar range.

Mirae Asset: Has wind seen a material slowdown?

Ashish Saraf (SKF): So wind I think last year was about growth story for wind. In terms of market there is a lot of potential for the wind in the Indian market. It's more of whether the market is giving us the right pricing for the products. So that's where as a company we have a strategy of wind turnaround where we want to make sure that we get the right pricing and then only sell. We don't want to sell at a loss. That's where the focus on wind is not really on growth, but on making sure that we do profitable business.

Mirae Asset: Just a last bit from my end next three five year do you see the current revenue shifting in a very big way? Let's say industrial is 50, automotive 40 to export 8. If I look into three five-year hence, how should I…

Ashish Saraf (SKF): As I said, see globally 70% is industrial, we are at 50%. So there is a lot of potential Indian market. Industrial is growing. So I would say that our industrial share will continue to increase compared to automotive and it may not become 70:30, but I would sure that over a period of time, it might become 60%-40%.

Mirae Asset: And in respective of that, margins should not get impacted a bit scale and not because the industrial typically being more traded is relatively lower market.

Ashish Saraf (SKF): But, over a period of time, we will also localize. So our strategy, as I said, is localization or regionalization, definitely, there is a higher potential for growth on the industrial side compared to automotive. So that mix will change over a period of time. Focus is on ensuring that we improve our working capital continuously, so that we are able to meet those investments effectively. So that's what pretty much our focus is.

Mirae Asset: Just one view outside of -- I mean, SKF, there is a supplier Rolex who supplies to you also. Just your view on their practices?

Ashish Saraf (SKF): Difficult for me to comment.

HDFC MF: How things are in terms of business?

Ashish Saraf (SKF): I think the business is -- you'll see the last quarter results. The business is fairly doing good. And I think for 2023 also, if the market and the economy remains as is, I think we are expecting again, not as high growth as what we achieve in 2022, but we are expecting good growth this year as well.

HDFC MF: Any specific pain points, couple of your peers have also talked about a little slowdown probably because of Vestas?

Ashish Saraf (SKF): See wind, I think the challenge is in the wind is more our focus, right away, on the wind is to drive profitable growth. So for us, the challenge in the wind business has always been profitability, because the market as such has not been paying us good pricing. So I think it's probably the similar challenge, which -- I'm not sure what competition is facing, but I think probably a similar change, where they are probably not getting the right pricing for the products. And that is where, as a company, I think we are pushing back all our customers to give us a better price. So that we can turn around the business as well. So the focus on wind is not really growth, but profitability.

HDFC MF: And, what is this year's growth, I mean, say, 2022 growth? What was leading, I mean, was it more four-wheeler, automotives or...

Ashish Saraf (SKF): I think across all our segments, if you look at pretty much FY 2022, we had a 22% or 23% growth year-over-year. And pretty much, both industrial and automotive grew at similar growth percentage, almost 20% to 24%. So, and within that, I think in the automotive space, we saw good growth in cars, in commercial vehicles. Again, all sectors grew. I'm just giving you the top headline, which grew at a faster pace.

On the industrial side, we saw strong growth on wind, we saw strong growth on railways, we saw strong growth on metals as well as we saw strong growth in the overall distribution businesses.

HDFC MF: And two-wheeler might be a little like laggard?

Ashish Saraf (SKF): Right now, two-wheeler is growing at a relatively lower pace. One of the reason is exports. I think globally, we know the overall global geopolitical situation. And because of that, a lot of our customers -- exports are adversely impacted, especially the two-wheeler space. And that is where we are seeing a bit of a challenge. Even on the domestic side, I think because the petrol prices and all of that, the demand is low. But our sense is, I think, somewhere by end of Q3, when I say Q3, I mean a calendar year Q3, the late September, I think we expect the demand to pick-up on the two-wheeler side.

But if you look at two-wheelers, just 10% of our overall business. It's not that, okay, that is not growing, its impacting our overall growth, because we've seen strong growth on the passenger vehicles side, on the commercial vehicles side. So we still, at an overall automotive level, we are still expecting good growth this year.

HDFC MF: Passenger vehicle, how much is the percentage of revenue?

Ashish Saraf (SKF): Passenger vehicle is, it's around 6%.

HDFC MF: CV?

Ashish Saraf (SKF): CV would be around 5%.

HDFC MF: That includes both LCV and Heavy commercial. You have only -- you consider heavy commercial is commercial?

Ashish Saraf (SKF): No, if you talk about tractors, tractors is separate. But typically, all whether its light commercial vehicle or heavy commercial vehicles, its the same.

HDFC MF: Your exposure to tractor is good or?

Ashish Saraf (SKF): Its around – not really big, its around 2%. Its not a very big business.

HDFC MF: And automotive aftermarket, which I mean the last time when we met with Manish, also that time also, he said a lot of focus is on aftermarket, because there is a lot of countrified and...

Ashish Saraf (SKF): That's right. So if you look at -- in the aftermarket, our focus is on reach. Our focus is on increasing our reach as well as improving availability. So if you look at when we last met, we said we have probably our market penetration is at around 50%. So because of which we are not able to make sure that we're able to create good availability for our customers. So that's what we are focusing on. We have the Udhan program going on in the automotive market as well, where based on the high-level data that I got, we have already reached 65%, 70% in terms of our market reach.

So we continue to increase our market reach at an overall India level, and that's kind of helping us grow our reach our aftermarket in the automotive sector. As well as one of the big things that we realized as we are increasing that reach is, to grow our aftermarket, we need to have a strong availability. We are closely working with our distributor. We have streamlined our go-to-market strategy to make sure that the increased availability of our products for our customers, which is kind of helping us grow in the auto aftermarket.

HDFC MF: And when you say the penetration, so how do we measure penetration?

Ashish Saraf (SKF): So simple way is in how many districts we are operating. So to give you an example, there are around 733 districts in India and our distributor presence is at this point of time, around 500 districts. So its around 68%, 70%. So that's how we see that there's still a significant potential to increase our reach in the overall Indian market.

HDFC MF: And how does it mean I guess even in some of the markets where we don't have direct distributors and I mean the existing distributor might be supplying those products to non-directly penetrated district as well?

Ashish Saraf (SKF): They might be. So see, if a customer needs it, they might be sourcing it through some other -- but they're not may not be necessarily sourcing it from an authorized SKF distributor. So the big change which is happening is that we are appointing an authorized SKF distributor, authorized SKF retailer as well, which kind of helps us ensure that customer is getting a genuine bearing rather than a counterfeit bearing. As well as it is in the retail sector, especially availability becomes a very-very important play, because the retailer doesn't have enough cash to stock material. So they are looking at how quickly they can kind of get an SKF bearing when the customer is asking for it. So we've spent a lot of time in the last 1.5 years in terms of creating that distributor network, so that the distributor is carrying enough stock to supply at any point of time in a shop.

HDFC MF: So that comes to the point of distributors' ability to stock also, financial health of the distributor, It's also important right now.

Ashish Saraf (SKF): Correct. That is right.

HDFC MF: And so when we say the reach is also, I mean, so the availability of whatever the SKF bearings and components. So is it like a number of SKUs has to go up substantially high to have or -- you just study the market typically that this market is typically, maximum consumption is of this kind of two-wheeler bearing or four-wheeler bearing or something like that?

Ashish Saraf (SKF): See, right now, there is a big science, which is kind of working on this in sense that we have worked with a third party, where we have kind of created an entire supply chain market, in a sense where we know depending on what we have sold in the market in the past, what's an optimum stock level that distribution should maintain. And we have kind of enabled an automated replenished method where as soon as a distributor stock for a particular SKU comes down, he gets an automatic supply from us. So that's the whole Udaan model, which we have kind of enabled. And so that distributor is never out of stock, in the automotive space, so that we ensure availability at a retailer side.

HDFC MF: So you know basically, how much is left with that guy. So we can have...

Ashish Saraf (SKF): Yes. So we know, what's the optimum level that the distributor maintain all the time. And whenever see stock replenish, we don't wait for a distributor to place an order on us. The arrangement is such that we will supply automatically to the distributor to replenish stock to a certain level, so that's kind of helping us, especially on the automotive side in terms of making sure that we have the right availability.

HDFC MF: And how big is auto aftermarket right now, in terms of sales?

Ashish Saraf (SKF): It's around 12% of our overall business.

HDFC MF: Overall, domestic or that includes top line total including exports?

Ashish Saraf (SKF): No. this is just domestic.

HDFC MF: And when you reach from, say, it's probably 65% to 80% or 85%, I guess that we will be the optimum number, you might be looking at, you might be 100%, I don't know. I mean...

Ashish Saraf (SKF): See, our focus is definitely too continuously increase reach, but definitely currently, at 65%, 70%, there is a lot of potential. And where we are going to stop, I think, difficult to say at this point of time. But the idea is to make sure that we have strong penetration and stronger availability across the market.

HDFC MF: And when you say from 50% to 65%, when you have moved from that number, so what kind of extra benefit in terms of top line or reach or volume you mentioned?

Ashish Saraf (SKF): It's kind of helping us grow our automotive space. So if you look at -- to just give you an example, our automotive business has grown year-over-year, I am talking nine months to around 15%. So that's kind of helping us grow our top line, because most of it is predominantly driven because of volume in the automotive space.

HDFC MF: This year, the pricing would also be there, because quantity has…

Ashish Saraf (SKF): Not so much in the automotive or aftermarket. There is some bit of price increase, but the price increase has been far more higher on the industrial side.

HDFC MF: So why it's not a pass-through? Is it not a pass-through, the commodities should be passed through, right?

Ashish Saraf (SKF): It should be, but we have to kind of see what our competition pricing is right in the market as well. We don't want our demand to be adversely impacted because of price as well. So we are looking at both. It's not just that you need to pass on the cost. It's a mix of competitive pricing as well as making sure that we are passing that cost.

HDFC MF: And mostly, you might be competing with FAG and some of the Japanese guys, I think…

Ashish Saraf (SKF): Predominantly, FAG, in the automotive aftermarket.

HDFC MF: Not with the NBC...

Ashish Saraf (SKF): No, there are others as well, but I'm saying predominantly like when we talk about quality, I'm talking about quality as well as pricing, typically, the competition is FAG.

HDFC MF: Your pricing is 15% premium, if I'm not wrong?

Ashish Saraf (SKF): That's right.

HDFC MF: That's what I've seen in aftermarket. I don't know...

Ashish Saraf (SKF): No. You're right.

HDFC MF: I think, your pricing might be similar, because you can't change too much. So when -- probably, you move to say roughly 80% or 85%, do you think there will be a bump-up in aftermarket contribution in overall?

Ashish Saraf (SKF): Naturally, if your reach is going to increase, then there should be increase in our volumes as well as the mix should improve.

HDFC MF: So two, three years back, it was same 12%, auto aftermarket, of course.

Ashish Saraf (SKF): I don't have that data with me to comment upon. But definitely, our VSM has been continuously growing. And I would think they've been growing at a faster pace compared to the OE space. So our mix would have improved.

HDFC MF: And localization in this part of the business is...

Ashish Saraf (SKF): Most of it is already localized.

HDFC MF: So it's at the back-end side, the supply chain is also mostly localized in this…

Ashish Saraf (SKF): That's right.

HDFC MF: So now coming to the industrial, which is this year, how much was the industrial for nine months?

Ashish Saraf (SKF): As I said, 25%. So the growth in industrial and automotive was very similar at 24%, 25%.

HDFC MF: But in terms of the total contribution?

Ashish Saraf (SKF): So see, industrial is around 50% of our business. Automotive is around 40%, 41%, and export is around 8%.

HDFC MF: So, 50%. And so within that, which is the biggest segment?

Ashish Saraf (SKF): See, the biggest segment in terms of industrial, I would say, aftermarket is the biggest in the industrial. So 25% is aftermarket. And remaining 25% is the rest of all the OE business basically that we do across our sectors. In that, I would say, railway is a big segment for us, then I would say, general machinery is big, which is basically drives, pumps, motors, fluid power, those textiles, all put together, they are similar, right around 7% to 8%. And then others are relatively smaller.

HDFC MF: Railway is also 7%, 8%?

Ashish Saraf (SKF): As I said 50%, 25% is distribution, 8% is your drive, which is pumps, motors, fluid power, rest, 7%, 8% is your railways and rest of the other segments.

HDFC MF: So, 7%, 8% is general machinery. That includes the drive, or that...

Ashish Saraf (SKF): That is drive, basically.

HDFC MF: So, 7%, 8%, 7%, 8% and 7%, so broadly 24%.

Ashish Saraf (SKF): So, 7% general machinery, 7% railways and 7% rest.

HDFC MF: And there has been a lot of talk on -- I mean, we have seen the wagon procurement etcetera, is quite increasing in India. So what kind of railway growth you are envisaging in, are you...

Ashish Saraf (SKF): So railway is basically what passengers, metro and freight. So we are there in all the sectors. Definitely, freight has a lot of potential, because of the 90,000 wagons order, which the railways have placed on the private wagon builders. And we are basically working with all the private wagon builders. So we are already fully approved both for Class E and Class K bearings. And we are working with private wagon builders to basically win orders with them.

So definitely, there is a potential for growth in the railway sector, in the freight sector, passenger and Metro also, there is a lot of potential with Train 18 coming in, we're already there in Train 18. So we are closely working with ICF to grow in the passenger side, similarly on the metro side, so many metro projects happening. There is a lot of focus on railways.

On railways, the challenge is always profitability. So as a company, our focus is driving profitable growth for the business. So if the business is at a loss, we would probably not do that business. So that's been our, as I said, on the wind side, we are doing profitable growth, similarly on the railway side, the focus is stood at profitable growth of the business.

HDFC MF: And most of these bearings are manufactured in India, or do you have still importing so...

Ashish Saraf (SKF): For railways, we are localized, then for freight, we are localized, for passenger, I would say, we have localized as well as we are importing stuff. So there is still some -- for railways, most of it, we are localized. We are still importing a bit, which we are in the process of localization.

HDFC MF: Metro also?

Ashish Saraf (SKF): Metro also.

HDFC MF: So I think last time, we also spoken on the localization front. So where are we in terms of capex, right now?

Ashish Saraf (SKF): So again, we continue to invest. If you look at our capex, it's increased from last year. A lot of our capex investments are going in our sister company, which is the non-listed entity. Because a lot of investments are happening in mid- and large-sized bearings, where the technical capability to manufacture lies with that entity. So that is where you do not see a significant jump in our capex spent for this entity as such, because on the automotive side, we are almost 85%, 90% localized already. It's only in the industrial large-size bearings where we are not localized. So that's where the significant portion of our capex investments are going there in other entity.

HDFC MF: But how is the transfer pricing between the two entities is...

Ashish Saraf (SKF): It's governed by the standard, we see the guidelines depending on the Transaction Net Margin Method. So it's pretty similar to what any other company would have. It's not anything different that we are doing.

HDFC MF: And any thought on, say, some of the segment or I mean, some of the larger bearing also getting manufactured in this entity?

Ashish Saraf (SKF): In SKF India?

HDFC MF: Yes

Ashish Saraf (SKF): See, in SKF India, we are also localizing. Say, for example we had UC inserts, which is basically required at the distribution business. And we saw a lot of potential there. So we are in the process of setting up a channel where in this entity. So we are continuously evaluating. If it is a smaller size bearing, where there is -- the skill sets are there in this entity, we are making investments through this entity. If it is medium or large size bearing, then we are making investments through the other entity.

HDFC MF: So basically, what you are saying is, just correct me if I'm wrong. So mostly the ball bearing that we -- ball bearing and all this will remain in this entity. And probably this is a spherical…

Ashish Saraf (SKF): SRBs, TRBs, will -- because you require a different kind of skill set, like the technical capability, the grade of steel, the supply chain network, which is needed is completely different for a spherical bearing compared to a small DGBB. So that capability lies in the other entity. And that is where we will -- as a company at an overall level, it makes financially more sense for the company to manufacture it in that entity rather than building that capability from scratch in SKF India. So localization opportunities will probably happen in that entity.

HDFC MF: And if the localization happens, within that entity, does it benefit anywhere?

Ashish Saraf (SKF): Yes, it benefits us in a big way, in a sense that -- see, whatever we are manufacturing in that entity, predominately, the focus is India market. So it helps SKF India to sell at a better price. It helps increase availability of the products. It increases cost competitiveness at an overall level for SKF, which will help us get better volumes from the customer. So from that perspective, it kind of enables SKF India to cater to the market in a much, much better way. And yes, we will buy it from the other entity as a traded product, but we will still make money at reasonable margins under the transfer pricing guidelines, but we'll have higher volumes.

HDFC MF: Basically, operating leverage will help in this in entity. The gross margin is whatever predetermined transfer pricing is, the gross margin will remain as it is?

Ashish Saraf (SKF): That's right.

HDFC MF: And any new trend, etcetera, you're seeing in terms of -- what is the outlook for industry?

Ashish Saraf (SKF): See, outlook for industry overall, the way we are looking at 2023 is if you look at the GDP growth for 2023, 6% to 7%. Inflation is going to be around 5%. So overall, 12% pretty much. So, I think that is something which we are -- it's not a guidance, but I would think that, that is something that we should be driving for, which is basically a combination of price mix and volume put together.

Internally, we are even driving a higher target, as a company. But I would think that if the market remains the way it is, we should expect a double-digit growth this year.

HDFC MF: And this will be predominantly driven by industrial? Because I think auto, this year might be a little...

Ashish Saraf (SKF): Two-wheeler is a challenge, as I said, which we believe should improve from Q4, from October to December should improve. But in the automotive sector, as I said, we are increasing our reach. So we're trying to gain volumes through that in the aftermarket. In the OEM side, we are trying to build strategic relationships with customers with whom we didn’t relationship with. We are trying to build together with them in terms of innovate together for the new products. We are trying to increase our range, improve our availability. So that's kind of is going to help us on the automotive side.

On the industrial side, the focus is infrastructure led, which is drives, which is heavy industry, which is construction. These sectors, we believe in the long term are going to grow. Because India is significantly right now focused on infrastructure as a country. So there is a lot more focus on these specific sectors. This is going to kind of help us to grow in the market. But as a company, what we have also said is that we want to grow profitably.

So if there's a customer in wind who is giving us a big order, but if we're losing money there, we'll probably not do that business. We will focus on driving profitable growth. We'll focus on portfolio management as a company. So we are focusing a lot more on looking at our internally, our entire customer base to see, are there customers where we're losing money? Are the products which we are selling at a loss? So looking at those areas to see how we can improve the overall margin for the business.

HDFC MF: And in terms of OE, I think you are the oldest company, which is present in India in terms of bearing space. So is there some ways where you are still at a very primitive stage in terms of volume, etcetera, or?

Ashish Saraf (SKF): Yes. So there are many OEs in the sense, we have relationships, but at times where financially didn't make sense for us, We would have probably exited the business at some point of time. So there is a constant connect with all the OEs in the market on the automotive side, where we are trying to continuously peg our products against the competition and build that relationship, Create that value proposition for our customers. So there's always that push. To give you an example, we have a big relationship with Bajaj, but not so big with TVS or Hero. So our focus is to build that relationship with TVS and Hero to kind of grow our business.

HDFC MF: Honda is a more working with the Japanese companies?

Ashish Saraf (SKF): That's right. So they have been like, and that's been our challenge on the passenger vehicle side, I would say, where they have been sourcing like, buying bearings from the Japanese vendors. And I think that is not something that we have been able to crack yet. But the good thing on the passenger vehicle side is that we have with players who are growing big like Tata and all, so we are with them, we are with Mahindra, whose market share in the passenger vehicle side is continuously increasing.

HDFC MF: And the same is the case with Koreans, or Koreans you deal with?

Ashish Saraf (SKF): Not so much.

HDFC MF: So basically, your canvas size is actually limited, because of the geographical mix of the OEs?

Ashish Saraf (SKF): That's right. Like, especially on the Japanese side or the Korean side, I think they traditionally have a preference to work with their global mandate or with the global relationship at a local level. So our SKF presence with them is relatively low.

HDFC MF: As last two years, I think India has particularly has grown faster. In terms of the pricing, industrial, you have completely passed on whatever you have got in terms of the commodity...

Ashish Saraf (SKF): I would say, at an overall level, we have fairly done. And that's where you see our margins improving. We've been able to pass on, or if I talk about on an overall basis, we have been able to pass on the costs back to the customer. It's been fairly, I would say, much easier on the aftermarket side and relatively a lot more difficult on the OE side, both on the industrial as well as on the automotive side.

HDFC MF: But, who is better? Industrial OEs or Auto OEs?

Ashish Saraf (SKF): I think it's similar in a sense that I think of the auto is, it's a lot more easier, because there are long-term contracts. So and the price increases are kind of already built-in. They are linked with steel prices and all that. So it's a lot more easier to kind of go back to them and get a price increase, because it's kind of built-in our contracts.

Where as in the industrial side, the contracts are not very long term, with most of them. It gives us an opportunity to give a quote a higher price, but we have to also look at competition, because every order is in new order for us. So we have to look at what competition is quoting and whether our pricing that we are quoting is competitive and it's making value for our customers. We have to always keep that in mind as well. So on the industrial side, it's slightly more difficult, I would say.

HDFC MF: And how does it work in some of the tender businesses, like say railway have used to have a tender business?

Ashish Saraf (SKF): They still have tender business.

HDFC MF: And so how -- I mean, once you quoted the price, can you increase the prices, or no? So you have to focus, you have to block the commodity also for every supply for one year later, right?

Ashish Saraf (SKF): So that's always the challenge in railways that whatever price we commit to the customer. One is that's all L1. So it has to be the lowest bidder. And second is at whatever price we quote now is basically effective for the next -- for the entire duration of the tender. So you might execute the tender in the next 12 months or six months. So you have to hold those prices even though the prices might go up in the market or the -- basically, your input cost might go up, that's the risk that you'll have to carry.

HDFC MF: Working capital, the railway and all does it have a problem?

Ashish Saraf (SKF): Yes, it's a bureaucratic process. You need to really manage that process better. But working capital as such is not a challenge. We continue to collect pretty much from railways on time.

HDFC MF: So I think globally, we have 75%-25%, I guess, in terms of industrial and auto?

Ashish Saraf (SKF): 70%-30% industrial and auto, whereas it's 50%-40% in India. So we see that continuously. We expect industry to grow at a faster pace compared to automotive. So that mix gradually should change and industrial mix should increase.

HDFC MF: How is it changing over period, say, five years back, was it like…

Ashish Saraf (SKF): I would say, earlier it was 50%-50% if you look at industry and automotive. So now it's become 50%-40%. So you can see that shift already and that shift should -- I think in India, it cannot be -- we may not reach 70%-30%, but might become 60%-40% over a period of time.

HDFC MF: And I think globally, we have 8% CAGR guidance. I think the SKF global guidance as SKF said. So what should be our guidance?

Ashish Saraf (SKF): Again, very difficult for me to give a guidance. But I already told you, that GDP is growing at 6%, 7%, inflation will be around 4% to 5%. So that itself ties at more. than 10%. So I would think at an overall SKF India level, if the economic situation remains as is, and there's no significant disruption, and we should at least be growing at that pace.

HDFC MF: On competitive intensity, are you seeing increasing, decreasing how is the prices?

Ashish Saraf (SKF): Yes. It is always there and I think, it is increasing. One of the things that we always see with our customers that they might be okay buying a local bearing, but when it comes to critical applications, they always prefer SKF against competition. So wherever they see a strong value proposition as our customers, they are always -- they are not willing to go and bet on a product, which is selling at a much lower price. So that is where we see that there's always going to be a price differentiation and there's always going to be a pricing pressure. But as a company, I think we need to create value for our customers and show them the benefits of buying SKF over the long term. And that's what as a company we are focusing.

HDFC MF: Imports from China is still very high?

Ashish Saraf (SKF): Counterfeit bearings? again, difficult for me to comment. As I said, our focus is that our counter measure is to increase our rates. So that if the customers are going to get genuine bearing from SKF, they would irrespective of the price differential they will prefer to buy SKF.

HDFC MF: Because, why I'm asking this is because a couple of like, small textile mills and all what we have seen is a lot of guys get those bearings from China also?

Ashish Saraf (SKF): There will always be the case. But again, that is not something that because anybody is free to import, and whatever they want to import. So it is difficult for us to control. But what we are ensuring is we create strong availability, strong penetration, strong reach. So that customers know whom to reach out to. A lot of times customers struggle to reach out to the SKF authorized distributor. That's where they kind of land up buying a counterfeit bearing. And we have seen cases where customers have paid premium as well for a counterfeit bearing, which they didn't realize it's a counterfeit bearing, but they paid premiums in the market compared to a genuine SKF bearing as well, because they needed that bearing urgently and all of that. So as a company, our focus on reach is kind of helping us get a bigger market share.

HDFC MF: So what is the capex you will do in next two, three years? I mean I think it's already given I think INR 100 crores, INR 150 crores that is what...

Ashish Saraf (SKF): Yes. So typically, again, it might go up, as we localize, you may not see such a significant spike in SKF India as such. But as a company, will we invest in India, we are investing in India. Through the unlisted entity to be able to capture this market better. So you may not see a significant investment in terms of capex in SKF India, which is a listed entity. But if you probably look at the unlisted entity financials, you will see a significant jump in the overall capex.

HDFC MF: And your distribution for this -- the lubrication and all business is separate?

Ashish Saraf (SKF): Yes. That's all separate. It's not with SKF India, so it's the same unlisted entity. So we sell lubrication and seals through the unlisted entity.

HDFC MF: But bigger bearings, we sell it through here.

Ashish Saraf (SKF): Yes. So all bearings, which we sell in the Indian market, are sold through SKF India.

HDFC MF: So on this unlisted entity what this kind of capex you are doing?

Ashish Saraf (SKF): See just to give you an idea, I will just give you a reference point. We just opened a credit line between SKF India and SKF Engineering for INR 250 crores. So I would think we should be making that kind of investment in two-three years in that entity.

HDFC MF: Any change you're seeing in the marketplace, some new trend, if you can?

Ashish Saraf (SKF): No, not really, I would say, I think the sense that we realise is that SKF was the first mover in terms of taking the price increases. I think what we are realising now is that competition is following in. They are also probably having a similar kind of cost pressure, just like us. So the good thing is that we are not feeling that pressure on demand, because of the price increases that we have taken in the market. On the EV space, we are working closely with all the players. So whether it's Ather, whether it's OLA, we are there with them, as well as the current players, we are already there with them. So I think we are in the right position, and that is also our automotive key strategy to make sure that we are part of this EV revolution. So I think that's growing, doing well.

HDFC MF: So how do you see the content moving…

Ashish Saraf (SKF): Right now, the EV share is only 6% of the overall in the automotive space. So it's not a very, very big market in that sense. But the good thing is we are there with them. We are jointly developing products with them. So and we are working with all these players on wheel end, on other aspects of the two-wheelers and the four-wheeler as well. So we continue to work with them and grow in this space. But still, in terms of, if you ask me revenue share, it's relatively very small, so it will take time.

HDFC MF: Revenue share 6%?

Ashish Saraf (SKF): That's right.

HDFC MF: But I mean in car also?

Ashish Saraf (SKF): We are there with Tata. We are working closely with -- so the good thing for us in the passenger vehicle side is that we've been with these Indian players, Tata, Mahindra and we’re jointly developing products for them. So say, for example, Tata Nexon Electric, we are there. So in that way, we are their key partners on the bearing suppliers both on the combustion engine as well as one electrical vehicle engine.

HDFC MF: And overall exposure to engine or transmission related bearings?

Ashish Saraf (SKF): It's difficult for me to answer. I don't have the data.

HDFC MF: But our presence was more on wheel-end side, if I'm not wrong? Because you don't manufacture needle roller, right?

Ashish Saraf (SKF): That's right. So we are there on the wheel-end. We are there on power train, I think these two, we are there, and we are seeing strong growth in both these areas.

HDFC MF: And how is the content change, does it increase your content in terms of...

Ashish Saraf (SKF): You to talk about electric vehicles also. So what happens is that the number of bearings which are required in an electric vehicle definitely come down. But from a cost perspective or a pricing point perspective, that goes up. So overall, at an overall value proposition level, it remains very similar. It's not that our volume -- our volumes might come down in a total when you compare the ICE to EV. But in terms of the overall value proposition, it will remain the same.

HDFC MF: And value wise is -- is it also because as of now, the volume is smaller, where electric pricing is high?

Ashish Saraf (SKF): No, not really.

HDFC MF: And in terms of internal cost efficiency and all these things, any thoughts? And do you see room for improvement in terms of production, and overheads, etcetera?

Ashish Saraf (SKF): No. There is always a focus on becoming more efficient as a company. So for our manufacturing locations, we continue to monitor our costs on a month-on-month basis to see what are cost levels are for a particular factory. So we monitor that at a factory level and sometimes also at channel level. So one is that. So we kind of are continuously looking at how we can kind of bring down that overall cost level for all the manufactured products that we made. We look at cost optimization. We at times look at volumes also because factory cost is also dependent on – certain extent on economies of scale where you can increase your volumes, you can get a better cost for the products that we need.

So there is a constant focus on that. We are internally driving a lot of projects, cost savings projects, because as a management, we have a mandate to reduce our costs every year to a certain extent. So we are also internally working with a consultant as well as with a larger team to identify areas where we can kind of bring down overall cost for us in the manufacturing space.

On the traded products, this is relatively less opportunity to reduce costs. Because it's a function of the transfer price, which is determined based on basically what price we are selling in the market. And also what cost the manufacturing company is incurring. So it's relatively we can control that less as a company. But our focus is to make sure that we do profitable business, so we are continuously looking at that and even for the traded products, we do not want to sell product at a loss to improve our overall margin. But cost efficiency is a challenge for traded products, there's not much of an opportunity that we can do to bring on cost.

What we can do is to localize, so that we are not adversely impacted, because of the adverse inflation, which is happening in Europe. So that's where the focus is. If there is an opportunity to localize, we look at localizing them in the listed entity or the non-listed entity depending on the kind of bearing that we are manufacturing. There is a lot more focus on, I would say, improving our cash flows as a company. So if you look at our working capital, it's continuously improved quarter-over-quarter. And our focus is to make sure that we are able to fund our investments on our own. So whatever cash flow that we generate during the year, we should be able to fund our capex investments that are needed apart from paying a standard dividends.

HDFC MF: So working capital, I think it has improved. But is there any room for improvement, because you will have to pay 45 days advances?

Ashish Saraf (SKF): See, typically, if you look at -- I just give you an example, our working capital in December '21 was around 21% of our sales, 12 months rolling sales. Now it's come down to around 17%. So you see a 4% improvement. So that's a significant cash flow release that we have done for the business. Like in last one year, we have generated around INR 2 billion of cash. If you look at our balance sheet, we're sitting with almost after paying dividend. So we're sitting with INR 2 billion of cash compared to what we were sitting last year in December '21. It's a significant jump in our cash flows.

And on working capital front, there's still some opportunity on the AR front where we can collect better. On the inventory side, we are trying to continuously optimize and see if we can kind of further reduce our inventory. I mean these two opportunities still exist. Yes, it may not be as high as what you've seen already an improvement. But it is still maybe we can improve by percentage or two on an overall basis. And that's what we're kind of internally aiming for.

HDFC MF: And just from a traded product, if your volume increases, so leverage comes into the listed entity in terms of -- so is that extra benefit which you get in terms of top line is also passed through to the manufacturing entity?

Ashish Saraf (SKF): Naturally, because you'll buy more units from the manufacturing entity. So that could still pass on the share of the margin to the manufacturing entity, the cost plus the share of the margin that the manufacturing entity should get.

HDFC MF: So cost part which -- that is understood -- cost whatever?

Ashish Saraf (SKF): The margin also has to be passed on, because the whole transfer pricing is governed on a margin basis. And you kind of say, okay, what should be the share of the selling entity, what should be the share of the manufacturing entity. I should say, for example, what do all margin on a particular product is 10%. You say, okay, how much margin should be retained by the selling entity out of that 10% and all how much should be reatined by the manufacturing entity. So that's a constant split, which is basically the transaction net margin.

HDFC MF: So is it like, say, 2/3, 1/3, what?

Ashish Saraf (SKF): Typically, the margin for the manufacturing entity is higher compared to the selling entity. Because they take a much bigger risk, under the transfer pricing norms vis-a-vis the selling entity. That's where the focus is more on localization.

HDFC MF: So if their margin also increases, then our margins should also increase in that with because if the share remains same, say, 60%-40% or 50%-50%, whatever…

Ashish Saraf (SKF): It all depends, in a sense that if you are making a much higher margin as a business, yes, the manufacturing share will increase as well as the selling entity share will increase. If you relatively make a lower margin on the product that you sell, you would probably still make a reasonable margin on the selling entity. Because you are taking much lesser risk, whereas the manufacturing entity might land up making a loss. Because they take a much bigger risk.

So being a selling entity, I have to make a reasonable margin at overall business. Irrespective like, see, take an example of COVID year, we're probably made a loss on a traded product. Being a selling entity, I will make a reasonable margin. Because I'm taking a lesser risk, whereas a manufacturing entity might end-up make a loss. Because the overall, like a manufacturing entity might be not just producing for India but for the other markets. So at an overall level, when they have looked at their P&L, since they didn't produce enough in a COVID year, they actually landed-up making a loss. So that's how this whole thing works.

HDFC MF: So there is no fixed formula as such?

Ashish Saraf (SKF): There's no fixed formula. It's always every year, you look at what's the overall margin. And you look at comparable companies, who are in similar kind of business, what's a typical share that a selling entity should make, what's the typical share that manufacturing entity should make, and if we go with a reasonable assessment where we see a minimum, this is what we should make. But eventually it comes down to what has happened during the year and whether that margin is falling in that reasonable bucket or not. If it is falling the reasonable bucket is less analytic, if it is not, then there has to be some two of adjustments, which had to be done.

HDFC MF: So is there a scope for going from, say, 17%, 18% to 20%-plus?

Ashish Saraf (SKF): I would say, the margin that you see right now at this point of time, there could be some possibility of improvement, but it's not going to be significantly changing. You might see some blips in the quarter, some quarters you might see it coming down. And -- but I would say, between 17% to 20% is in the current economic situation, however if things change, then difficult to say.

HDFC MF: Understood. Thank you. I think I am done. What's your number? Because I was looking for that time when the resolution has come, so that time we wanted to speak, because we engage with all the companies.

Ashish Saraf (SKF): I was, in fact, trying to meet some of you guys as well to just explain. Sorry, I'm not carrying my card, but I'll give you my number.

HDFC MF: I didn't have your number. Because typically, in any resolution, if there is some adverse comment made by some of the proxy agencies, then we typically engage with companies.

Ashish Saraf (SKF): So I spoke, because I was trying to get in touch, but I didn't have a number, so I couldn't. Actually, I don't know, if Manish spoke with any of you guys. But we were trying get in touch with you just to explain the transaction.

And I think that's beneficial from a market standpoint, it is going to help SKF India sell more. Yes, I think from your perspective, you would ideally like SKF India to manufacture. But again, we have to look at it from an overall perspective as to whether financially some of the investments that we are trying to make through that entity, will it make sense for SKF India or not, if we had done it on a standalone basis?

HDFC MF: We have been doing good. So I think we have been holding on to at 8% or 8.5%, I think we can't move beyond 10% because that's the regulation.

Ashish Saraf (SKF): I think you guys are holding the maximum, if I'm not wrong, right? Between all the funds that you have.

Ashish Saraf (SKF): Okay. See you. See you on the 11.

HDFC MF: Sure. Thank you.

Kotak MF: Company is very well known to us and we have been large shareholders for a very long time. So basically, just wanted your sense on the overall industry dynamics both on industry and we are getting different comments on different things. Some are saying slowdown is happening, some are saying it’s okay, replacement market is seeing some kind of a problem. Can you just help us understand the reporting time and the way you are looking at it? And then we will go into specifics on what the every level company, we have lot of questions.

Ashish Saraf (SKF): See, if you look at 2022, you'll see what, 24% growth for SKF India. So if you compare that with 2023, definitely overall GDP growth for the India market is slowing down. The overall impact of the geopolitical situation and the inflationary environment which exists outside of India, that impact is kind of coming and to a certain extent will impact India. So to that extent, I think our growth definitely will get moderate, in the current environment.

But are we expecting growth year-over-year? Yes, we are expecting growth. I would say our GDP is expected to grow at 6%. Inflation is going to be somewhere around 4% to 5% in the current environment. So I would think somewhere around 10%-plus is something definitely we are aspiring to grow at a much faster pace than that. But I would think in the current environment we should grow at 10%-plus. Again, it's not a guidance, but that's a typical high level view.

Kotak MF: Normally your multiplier has been better than your GDP growth?

Ashish Saraf (SKF): Yes, so that is what we are aspiring for as well as a company. But I would say that internally, the way we see as an indication is that what's the GDP growth projected to be, what's the inflation projected to be, and we should be growing at a faster pace than that.

Kotak MF: What will be the drivers of growth, if you can just help us on that?

Ashish Saraf (SKF): Sure. If you look at industrial, we believe that long term India root story is going to be infrastructure led. So as a company, we are focusing on segments which are going to be infrastructure focus, sectors like heavy industry, sectors like construction, drives, which is basically pumps, motors, fluid power, textiles. So these are the sectors which we believe will grow at a much faster pace compared to other sectors. And that is where we are making significant investments in the industrial space. And we believe that that will drive growth for the industrial business in '23 and going forward.

In the automotive space, two-wheeler, is definitely slowing down, what we are seeing. Right. But two-wheeler is around 10% of our overall business. So even though two-wheeler is slowing down, we are seeing good traction in the passenger vehicle. We are seeing good traction in the commercial vehicle. So we believe that that should be able to kind of offset and drive growth in the OE space.

In the automotive aftermarket. I think our strategy of reach, range and availability is kind of helping us grow in the automotive aftermarket in a big way. Our penetration in the automotive aftermarket was earlier around 50%. Our whole focus on increasing our reach, increasing our presence in the overall market is kind of helping us drive the overall growth, as well as one of the things that we've realized is that availability can play a very important role in the aftermarket. So we are closely working with our distributor network as well as retail network to create a strong availability at the distributor end. So that we can kind of improve our market share. I think that's what's pretty much driving the automotive space.

Kotak MF: And automotive aftermarket would be how much total in the number of your overall sales?

Ashish Saraf (SKF): So, overall our sales, if you look at around 50% is industrial, 41% is automotive. And rest around 8%, 9%...

Kotak MF: And automotive aftermarket will be…

Ashish Saraf (SKF): In industrial, the aftermarket is 25%. Out of 50 25% in industrial comes from replacement. And the balance, 25% is OE. And similarly, on the automotive side, around 12%, 13% is automotive aftermarket. And the rest, 37% is through OE.

Kotak MF: So aftermarket in automotive are still…

Ashish Saraf (SKF): No. actually, 13% of 40%.

Ashish Saraf (SKF): 13% of overall sales and 27% is OE.

Ashish Saraf (SKF): Yes, 27% is OE, not 37% in automotive.

Kotak MF: And the way we have seen Schaeffler ramping the exports, and now they have 15%, 16% of sales on export. And this was a conscious, whenever we have shareholders in both that may be introduced, in fact, there was clear focus that was they have to drive exports, and that was 7%, 8% as you are. Any thoughts on that?

Ashish Saraf (SKF): Our strategy is a little bit different to Schaeffler here. As a company one of the things that we realized when COVID happened and substantial supply chain disruption happened, we said that we need to have a regionalized supply chain network. And somewhere in the beginning of 2022, we created an ISEA region, in the industrial business, which is India and Southeast Asia. So we said we have four regions EMA, ISEA, Americas and China and Northeast Asia.

So basically our focus is predominantly to cater to the Indian market. Now, with Southeast Asia coming in, definitely when we are looking at localizing, we are also looking at Southeast Asian market, because Southeast Asia predominantly they have very little local manufacturing presence. They are predominantly either buying from China or from Europe.

So when we are investing in, say, a new channel in India, we are looking at, is there an in terms of potential, we are looking at not just Indian market, but we are also looking at Southeast Asian market. So to that extent, you should see some, over a period of time, some growth in the export side. But as such, we are not focused on in it the way probably Schaeffler or other competitors are.

Kotak MF: Schaeffler is transferred the production line also to India, Europe to India.

Ashish Saraf (SKF): So, as I said, we are also looking at it specifically for those products where we have enough potential for the Indian market as well as for the Southeast Asian market, not for Europe. We are not exporting from here to Europe or to America. But if there's an opportunity that comes up through a natural progression. In a sense that we set up a line, it turns out to be cost effective for overall SKF and it makes business sense for them to buy from us, then it will happen through a natural progression. But predominantly, when we are setting up a new channel, we are setting up a new channel to cater to the domestic demand as well as to Southeast Asia demand.

Kotak MF: So would that I mean, when it comes as an opportunity, would it be sourced out of China? Would it be sourced out of India? How would that be decided? Because ultimately, Southeast, if it's a Southeast Asia opportunity, would that be sourced out of China or would it be sourced out of India?

Ashish Saraf (SKF): See, when we are looking at investing anything in India, I'm talking specifically industrial. If industrial, typically when you set up a new channel, you have to look at a lot of things because the volume for a particular bearing is relatively much lower compared to an automotive bearing. So what we typically do is that, okay, if I want to set up a channel, it has to make financial sense. There has to be a reasonable utilization of the channel for me to make that investment.

So whether I have that growth potential for that product in the Indian market to meet that requirement if, say, for example, it is not meeting the India requirement and the volumes that I can produce is significantly higher financially, it will not make sense to make that investment in India. Then at that point of time, I look at Southeast Asian market to see whether for a similar product, there is a demand in the Southeast Asian market which is probably currently getting served from Europe. Can I serve it from India?

So in that kind of the situation, we go and do that overall evaluation and make that investment. I don't look at European demand and decide here. My predominant decision is first based on whether there's a demand in India and whether that I'm the investment that I'm making, whether it is giving me a payback with purely the demand in India. If not, can I look at Southeast Asia? If I look at Southeast and combined India and it makes financial sense for me, then I make that investment. If it doesn't, then I don't. So I don't predominantly look at exports other than Southeast Asia to decide whether I should localize or not.

Kotak MF: My point was, I agree Southeast Asia is the market. If that has an opportunity, then India would be looked at as an investment. But the follow on question was whether that investment option would be looked at India or could be also serviced out of China. And how do you decide between investing in India vs China?

Ashish Saraf (SKF): We said we will have a regionalized supply chain. So we might decide to invest in India or in Southeast Asia. Depending on where it makes sense for us to make that investment. But it may not like, we will not go and set up a channel in China, say for example, of a China entity to serve the Indian market…

Kotak MF: So, you all don't have any large operations out of China?

Ashish Saraf (SKF): SKF, globally has a large operation out of China. It's a big market for us. But SKF India doesn't operate in China.

Kotak MF: So export per se, Europe and all is not a great priority for us, the way its…

Ashish Saraf (SKF): For us, if it happens in due course, because we have capacity, we are making at a lower cost, then it might happen as a natural progression. But our focus is predominantly Indian market, that's it.

Kotak MF: And this 8% revenue, which is from export. Any ambitions, any aspiration?

Ashish Saraf (SKF): For export, as I said, it's more of a filler for us.

Kotak MF: Export is a filler?

Ashish Saraf (SKF): Export is a filler for us. The focus is predominantly domestic market.

Kotak MF: And between India and the SKF technologies, where the name has now been changed. So the Southeast Asia opportunity can also be catered to buy the unlisted company or…

Ashish Saraf (SKF): That's true. So it depends on the kind of – see, we have two separate legal entities with two separate capabilities. The non-listed entity has capability to make medium and large size bearings, whereas the SKF India manufacturing competency is making smaller size bearings, automotive as well as industrial.

So, depending on the kind of investment that is needed, if it is for a smaller size bearing, then the investment will come in SKF India. If it is a larger size bearing or a mid-sized bearing, which is predominantly for industrial market, it will go into the other entity.

Kotak MF: Presumably, given that, obviously, Southeast Asia are more advanced compared to India in terms of infra spends, disproportionate beneficiary could be the unlisted, right?

Ashish Saraf (SKF): I couldn't relate. I couldn’t understand.

Kotak MF: What is saying that SKF tech could benefit from the localization of Southeast Asia more than SKF India because of the…

Ashish Saraf (SKF): Not necessarily. I would say, SKF India is big in automotive. Southeast Asia has got a big automotive market. So we can supply a lot from SKF India in Southeast Asia in terms of exports. Yes. The Southeast Asian market is also getting, like I'm talking about market, not SKF, is also getting served by a lot of Chinese players. Definitely there is a lot of competition in the automotive space from the Chinese players in the Southeast Asia.

Kotak MF: So there's 9% export how much would be automotive or industrial?

Ashish Saraf (SKF): I would say mostly is automotive. Obviously for automotive. Because most of like say for example, industrial products which are unique, which are large size bearings are being done out of Ahmedabad factory, which is the other entity, and they are the ones which is not their exports are not coming.

Kotak MF: In industrials, which are the sub-segment which would have done well for us in the last nine months?

Ashish Saraf (SKF): See, all our segments in the industrial space have done well. All of them have grown here, out here. Most of the big ones -- the big ones last year or in the last nine months, which have grown is railways, wind, distribution, metals, railways, distribution.

Kotak MF: Distribution is aftermarket. And on the wind side, have you seen some slowdown? Because we are….

Ashish Saraf (SKF): See on the wind side, what we are seeing is the market itself slowdown. And it would be true in order for SKF, I presume for the entire market, where the market is not right pricing in the market for the products. So pricing itself is an issue. Traditionally, SKF has been doing a lot of business on loss and we realize in last one year that we need to focus on driving profitable growth. So as a company, we are focusing on looking at all our customers and all our products which we sell at a loss.

And that's also kind of significantly help us in improving our profitability. So, example is wind, say for example, wind, our strategy is not growth, our strategy is driving profitable growth. So say for example, this year we are not focusing on driving growth of the wind business, but it's really focusing on turning around wind and making sure that wind as a segment becomes profitable for us.

It's in the process. As I said, there is an overall market challenge where the customers themselves are not giving the right pricing, the pricing levels are not right. There is a lot of discussions happening with our customers and some of these are global customers, to correct the pricing in the Indian market. And that's the challenge not just with us, but globally, I think all players are facing.

Kotak MF: And how big will be wind for us, in the industrial portion, I remember 7%, 8% used to say…

Ashish Saraf (SKF): Overall out of 100%, wind is around 7% to 8%.

Kotak MF: Now, even if it turns to breakeven…

Ashish Saraf (SKF): I would say, it's not 7%, it's 5%. So out of high level, I have to say 50%, as I said, is industrial, 25% is distribution. Your 7% to 8% is railways, 7% to 8% is general machinery, 5% is wind. And rest of this pretty much smaller segments.

Kotak MF: So where is the growth coming from in industrials…

Ashish Saraf (SKF): So railways, railways have grown, distribution has grown, wind has grown. Last year, wind has grown, wind last year, 2022, wind has grown. And see, because wind has long lead orders. Long lead time orders. You take orders, like 2022, what we executed, most of the orders came in 2021. So even though we're not making money, we couldn't really cancel those orders. We did had a lot of discussions with our customers to get a better pricing, but we couldn't really cancel those orders.

Whereas in 2023, we are being very conscious in terms of taking orders. it is going to be a significant impact on the overall business. Because again, it's difficult for me to quantify in terms of value, but -- just to give you an idea. We were making a loss of 9% to 10% on wind business.

Kotak MF: So till when it will be breakeven?

Ashish Saraf (SKF): See as I said, from our perspective, incrementally, that the orders that we are taking is we are making sure that they are positive margin.

Kotak MF: And in railways, we're making money, now?

Ashish Saraf (SKF): Railways is making money, definitely. Having said that, not great margins for us. So it's mostly a tender business. It's relatively a bit more challenging to make money there. But yes, our focus is also to turn that around in terms of improving our margins.

Kotak MF: What should be threshold, like we see Timken and all they are making decent and then we see a couple of other guys like Amber and all, providing air conditioning, they are also making money.

Ashish Saraf (SKF): Again, difficult for me to give you a numbers – because railway is mostly, from an SKF India perspective is mostly a traded product. It's not a product that we manufacture in SKF India. We manufacture out of the other non-listed entity. And only sales margins are booked.

But see, even if you make a marketing margin, you are assured of that margin. In the sense that even if you sell a product at a loss, you still make a good margin. Being a marketing margin, you have to make another transfer pricing norms of minimum margin.

Kotak MF: Given that now railway is also moving of the value chain, be it on the DFC high quality bearings there. Even on the passenger side, we are seeing electric locomotives as well as that. So does that open a new opportunity for us or we are still back or we are still behind in the curve for servicing these markets?

Ashish Saraf (SKF): We are very much there, in terms of servicing this market. In the freight business, the bearings are already localized. We are already supplying to private wagon builders. Because when you talk about localization, it's not just that you manufacture the bearing locally. You need to have the entire supply chain network also localized. That takes time. So there are a lot of initiatives happening on that in the railway front, where we can ensure that the entire supply chain network, it's a big market for us. It's a very important market for us.

Kotak MF: Just a follow-on to this would be that as a function of this change, will this 60% being traded reduce because of this transition to the new set of products that are coming?

Ashish Saraf (SKF): It will definitely reduce. You may not see a significant reduction, because a lot of it, if there are medium or large size bearings, it will continue to get manufactured in the sister company of SKF in India. But even if it gets manufactured in the sister company of SKF in India, there are a lot of benefits from an SKF India perspective. Because it creates cost competitiveness for us. It creates better availability for our customers. We are able to cater to the market in a better manner and we are able to get higher volumes and get a better share in the market.

So from that perspective, you may not see that, okay, railways or wind, I will swing from trading to manufacture. But just because there is a significant cost down, there will be better availability. You will be able to gain a better market share on both these areas and overall better profitability for those.

Kotak MF: We have a paly in Vande Bharat, Metro?

Ashish Saraf (SKF): Yes, we are already there in Vande Bharat. The bearings which are getting supplied in Vande Bharat is of SKF, we are there. We are closely working, with Metro is now becoming big, because so many Metro projects are coming across.

Kotak MF: We were not there in Metro earlier?

Ashish Saraf (SKF): No, we are very much there in Metro.

Kotak MF: Have you supplied to the Alstom?

Ashish Saraf (SKF): Yes, we supply to Alstom.

Kotak MF: Recent win of Alstom has gone to Timken?

Ashish Saraf (SKF): See Timken relatively is a much, much bigger player. Especially, I don't know, maybe you're referring to the freight business, which is…

Kotak MF: No, they said, Andhra, Indore and one more metro – from Alstom, they said entire order is with us…

Ashish Saraf (SKF): No, but we are working with Alstom as well. I may not have specific details with respect to this specific order, but we are there, we are closely working with them and both in Metro and passenger as well as in freight. But Timken is a much bigger player in the overall railway market compared to us.

Kotak MF: And we use to have a K grade bearing?

Ashish Saraf (SKF): We still have. So right now I think the railway is more focused on planed business. They have still not gone big on K class bearing. They're still not gone.

Kotak MF: Remember, four, five years back you were so bullish on K grade bearing?

Ashish Saraf (SKF): So again, the key differentiation is that a K class bearing can take a higher load. And E class can take a much lower load. Both the bearings are approved by railways and we are there with them. But right now their focus was more on making DCF operational and they wanted to make sure that there are enough wagons, that's why they have floated 90,000 wagon order in the market, but they're not moved to high load carrying capacity wagons yet. They are still focused on they're continuing with the old wagon structure. The demand is not…

Kotak MF: Is this something to do with like, I was hearing that earlier railways in passengers were moving to the LHB coaches. Now they are looking at some much future technology on coaches, which is where their transition to K class…

Ashish Saraf (SKF): No, this K class is for freight, it's not for DCF.

Kotak MF: And on distribution business, which is cash cow for you, 25%. I was speaking to a lot guys from SKF and others, your spurious bearings have all over the place. Thus the Chinese intensity has gone up very high and a lot of those guys are saying somebody takes it from saying it's SKF, but it's not original. Lot of spurious products and that's hurting the SKF dealers a lot. And these are large dealers in Chennai, Bangalore I spoke to recently and this is the biggest fight we are having is this market only, because everybody is selling with SKF name, but we only know what is right, what is wrong, but clients take it then they abuse SKF. So it's becoming a big challenge.

Ashish Saraf (SKF): See, that's always a challenge. And I don't think from a company standpoint, we can go and stop counterfeit bearings, that's why our focus is always creating strong penetration, creating reach. And that is what we have done both in the automotive distribution network as well as industrial distribution network where we are focusing on increasing our reach. Just to give you an example, 1.5 years back, our reach was only around 50%. So when you say, high level, just to give you an idea, like, in India there are around 730 districts.

And we were present in only 50% of the district, our official distributor were working only in 50% of the district across India. In the last one year, we have increased our reach to almost 70%, where our presence have gone up to 500 districts across India. And we are building a strong supply chain network to make sure that we create strong availability in the retail network. So that's kind of helping us grow our market both in the industrial side as well as in the automotive side.

Kotak MF: And the same dealer is for both automotive?

Ashish Saraf (SKF): No, they are different for industrial we have a different set of distributors, because the market is different. The automotive dealer is working closely with mechanics and even the players who are there, they are concentrated in an aftermarket vehicle market like, if you go to – like in Bangalore, if you go to Peenya, there is specific market for OEs, and for industrial, it's a different market. So we have a complete different network for industrial and automotive.

Kotak MF: But what we understand is that some of these areas where you are penetrated new was because our supply chain issues in terms of availability from China and all. But now all that material has now started to come back again. So are there repeat orders from these new distributors, or?

Ashish Saraf (SKF): Yes. We are seeing like wherever we have deployed our Udaan model, we are seeing that our growth is at much higher percentage compared to where we haven't been able to deploy it. So, sector or certain geographical areas, where our new model and the new supply chain network is we are seeing a much higher percentage of growth quarter-over-quarter vis-à-vis what we have seen in an area where you're not deployed the model.

Kotak MF: So, you are seeing already that…

Ashish Saraf (SKF): Yes. We are already seeing that.

Kotak MF: And has the import density again gone up from Chinese segment?

Ashish Saraf (SKF): Difficult for me to comment.

Kotak MF: What's the fear on the ground level when you say to the aftermarket head, its just the sense…

Ashish Saraf (SKF): See on the aftermarket side, what I hear is that the demand remained strong. When I say, strong is and then do not see a drop in the demand. What I also hear is definitely in the automotive aftermarket, there is some bit of a price pricing pressure, but it's more of a temporary. I think the sense that I get is like our competition, which is a much bigger player in the automotive sector, they have high volumes and they're not getting the share in the OEM, so they are dumping it in the aftermarket. It's more of a temporary phenomenon. What we are noticing, but in the long run overall, our growth remains strong on the auto.

Kotak MF: Last year, on the total aftermarket distribution or industrial plus automotive what would have been in your growth …

Ashish Saraf (SKF): See, industrial distribution has grown at a much faster pace.

Kotak MF: How much will be that?

Ashish Saraf (SKF): Almost 25%. And whereas the automotive grew at a relatively slow, because we were in the process of deploying.

Kotak MF: So how much will be?

Ashish Saraf (SKF): Its around 14%.

Kotak MF: There is the highest margin?

Ashish Saraf (SKF): These two businesses are the highest margin.

Kotak MF: FY'22 you said?

Ashish Saraf (SKF): No. CY '22, CY '23.

Kotak MF: Nine Months?

Ashish Saraf (SKF): Nine months.

Kotak MF: That's why the gross margin has gone so high to like on 40% 41%, life high margins?

Ashish Saraf (SKF): That is true. See, as I said, there are a lot of things, but definitely one of the big things is price corrections that we have taken in the entire '22 -- because of the significant cost pressure.

Kotak MF: Inventory gain must also have come in this, right? You would have low-cost inventory, you increased the price?

Ashish Saraf (SKF): Not necessarily. See, it's more of the price increases that we have seen in Europe and not all costs came to India, because they are transfer prices. So that's where you see a margin increase at an overall level.

Kotak MF: Will it sustain?

Ashish Saraf (SKF): See, from an overall margin perspective, we feel that we will probably, we will continue to monitor our costs closely and if need be we will pass on more cost to our customers to make sure that we are not compromising on the margin.

Second thing is that there are a lot of business, historically, which SKF has been doing, which was relatively either a very low margin business or a negative margin business. So in the last one year, one of the big focus areas has been portfolio management, where we are looking at each and every customer to assess as to whether we are making money or not. Look at what our product portfolio, which are the products where we are making losses, going and having that conversation with the customer to give us a better price or if need to we exit that business as well. So that has also significantly helped us improve our margin. And that is something that we will continue to do in 2023.

Kotak MF: Is it safe enough to assume that the range will be 38% to 40%? Because this transfer pricing had created a lot of distortion. If you remember last year's September quarter, suddenly the margin just shot up like crazy and then you guys also kind of through sell side send us the message that was there was one-off kind of a transfer pricing distortion. So don't take it as a…

Ashish Saraf (SKF): See broadly, the way you need to look at it, is that the traded product margins are relatively lower than a whole manufactured margin. There is a reasonable guidance which is given under the transfer pricing rules, which is relatively a single digit margin on a traded product. So in an ideal scenario, you would not make more than a single digit margin ….

Kotak MF: This is a bottom line, because there's very little cost attached to it in the transfer pricing, you will have actual cost and all that but not other costs related to manufacturing?

Ashish Saraf (SKF): Yes. I'm talking about our traded product. So typically, what happens is that's what you make. But when you are going to the market and you know that the costs are increasing, you are going and asking customers for a better price. That cost that comes in might come in at times at lower end, because you set prices under the transfer pricing rules way before you sell, so because of that there is always a differentiate.

Now when you close the year, say, for example, I close the year, whatever has happened during the year has happened during the year, because these are imported products, I cannot go and change the pricing of the product at which I imported. In March and say that I have imported at a lower price. I should have probably put it at a much higher price than that. So, I live with that. I close the year. I probably book at a relatively higher margin in the books. And then I start the year next year refresh. And see how it plays out. So that's why you will always see a bit of fluctuation on the traded products.

Kotak MF: And that also changes your gross margin?

Ashish Saraf (SKF): That also changes my gross margin and also my net margin.

Kotak MF: And traded as a company as a whole will be on much?

Ashish Saraf (SKF): Traded as a company at an SKF Group level will be definitely much higher.

Kotak MF: Indian, listed entity?

Ashish Saraf (SKF): In terms of the mix?

Kotak MF: Mix.

Ashish Saraf (SKF): So, the mix is around 58% is what we manufacture, 42% is all traded.

Kotak MF: So, this 42% is at a single digit margin, if I understand correctly?

Ashish Saraf (SKF): Should be relatively at a single digit margin. But at times it might go up as well.

Kotak MF: And this thing, when you do your transfer pricing, it's normally December end, and if I remember…

Ashish Saraf (SKF): No, it's an ongoing process. It’s a continues ongoing process.

Kotak MF: Every new contract will have a different transfer…

Ashish Saraf (SKF): No, it's not like that. See we have a lot of factories in SKF through which we import. We constantly look at what is the margin that we are meeting on transport pricing on a month-on-month basis. We look at what is the cost. And we continuously, like at a group level, at SKF, not we and not SKF India, but somebody at a group level constantly look at what is the cost at which SKF India is importing that product and what is an overall margin that it is making. If that margin goes outside of, say, the single digit range, then they go and change the cost, on a continuous basis…

Kotak MF: Will not allow money to be wasted?

Ashish Saraf (SKF): Having said that, retrospectively, they cannot go and change.

Kotak MF: It is only our prospective.

Ashish Saraf (SKF): Obviously it is always a lag, because there's a two-month transit time for an imported product. So, what I sell now, I have probably imported, plus there is a lag time also to manufacture. So, what I import is probably three, four months down the line when I place the order is what I've imported now and sold now. So, my price, when they have decided to cost, they have looked at my previous pricing in the market and if my pricing has changed my margin will increase or decrease, depending on what is happening because…

Kotak MF: This margins of yours will be very big, wont it?

Ashish Saraf (SKF): Because I have taken a lot of pricing increases.

Kotak MF: Inventory is also – two months inventory also…

Kotak MF: Now they will correct, and then that future…

Ashish Saraf (SKF): Over a period of time. If it becomes stagnated, definitely my traded margins will stagnate and it will come down.

Kotak MF: Then there will be inventory loss?

Ashish Saraf (SKF): Not inventory loss.

Kotak MF: Its not inventory loss. Now what he saying that suppose they have made 12% margin in traded product, now they will come down from 12% to 8% by normalized, they will not take back in prospective order. And beyond the point, he can't pass on to customers indefinitely…

Kotak MF: Out of this SKF, how much will be the traded from your unlisted company?

Ashish Saraf (SKF): Overall there is 42% as I said. I don't know the exact numbers….

Kotak MF: But to a greater extent ……

Ashish Saraf (SKF): We will do it, but the methodology is same.

Kotak MF: Their revenue is INR 700 cores, right?

Ashish Saraf (SKF): You are right. They also sell, also externally, they make lubrication products and seals as well. So they go and sell that also.

Kotak MF: So, lubrication is I think 40% of their revenue? That is all external sales.

Ashish Saraf (SKF): That is all external.

Kotak MF: And 60% which is left up for industrial and seals, we can assume majority is to you?

Ashish Saraf (SKF): Industrial is also sold externally.

Kotak MF: But how much?

Ashish Saraf (SKF): I don't recollect the number.

Kotak MF: The reason, I am asking is that your overall EBITDA margin in that business is just 8%-9%, despite 46% gross margin.

Ashish Saraf (SKF): In that business.

Kotak MF: In that unlisted business. 46% gross margin in SKF, so the name has changed.

Ashish Saraf (SKF): No. If you look at that entity doesn't make money.

Kotak MF: Yes, exactly. Because it is not scalable. It is a sub-scale. It has its own costs. I don't think so it is economical to run two businesses under the same roof.

Ashish Saraf (SKF): I have to check whether your gross margins numbers are correct or not. But see, typically, lubrication and sales are relatively much lower margin business compared to a bearing business, that is one of the reasons. Second is the Ahmedabad factory which is the industrial factory, the utilization of that factory is relatively at a low end compared to what it should make. So that is also a challenge in terms of making an overall profitability for them.

Kotak MF: Where has the estimate gone wrong? When it was put up?

Ashish Saraf (SKF): That was put up in 2008-2009, at that point of time they took certain business decisions looking at a significant opportunity in the wind market. As I said, wind is not a very profitable business. So a lot of investments were made for wind. Railway, again not a very profitable business a lot of investments were made for railway. So that's what basically has impacted the margin of that factory.

Kotak MF: Is there a possibility to merge both?

Ashish Saraf (SKF): As of now, we are not looking at merging.

Kotak MF: Given that we have 42% being traded and the fact that now on the European side there is a reasonable amount of manufacturing cost escalation, would that have any kind of bearing on our ability to be price worthy in our market? Because that escalation. Even we are highly leveraged to a traded portfolio and cost from global standpoint has gone up.

Ashish Saraf (SKF): Definitely that is a challenge. That's a challenge that we've been dealing with. That is where we came up with a strategy of regionalization and localization. There is a lot of investments going in terms of localizing, a lot of stuff which we are currently importing from Europe. You do not see all of that in this listed entity, because a lot of it is as I said, medium and large size bearings, which basically are going to get localized in the non-listed. But having said that, the cost pressure that we are facing we understand and you guys are tracking Schaeffler and Timken and they're also, I understand facing a similar kind of pressure.

Kotak MF: The reason that we asked this question is, because they are kind of being very proactive in moving the plants and moving and shifting all of that and making a lot more…

Ashish Saraf (SKF): That is a similar focus that we have. You probably don't see that so much. Just to give you an idea INR 250 crores worth of intercompany loan, we gave, only in the process of giving, we came to shareholders approval last quarter and all that and it kind of went through. So we are making a kind of around to INR 250 crores of investment in the non-listed entity which is being funded by SKF India.

Kotak MF: Why do are doing so?

Ashish Saraf (SKF): So let me tell you, see, there are benefits of that. One is there is a capability difference. Understand that the factory that I have in SKF India, has a different set of capability versus a capability which I have in Ahmadabad, because they can make large size bearings, whereas these factories cannot. See, even if, say, for example, I decide to manufacture those bearings, large size bearings in SKF India, I cannot do or if I want to do, I have to put in lot more money than what I would put in the Ahmadabad factory, because they already have the capability. So from that perspective, it made business sense…

Kotak MF: Why put INR 250 crores? It might not be looked positively by the investment community.

Ashish Saraf (SKF): And it's going to be helpful. End of the day, we are going to cater to the same Indian market…

Kotak MF: I'll tell you, I have been a Schaeffler holder for the nine years, and the only thing, when the global CEO, visited and asked, what should we do? I said, make one Schaeffler. There will be no questions. You will have a peace of mind of one legal entity in the country, and trust me, within six months, the announcement was made on one Schaeffler, you have the opportunity to…

Kotak MF: I am just saying that, it is business of INR 700 crores, there is loss in the P&L. There is tax benefit for you. Whatever transfer pricing is there, sell it on less, but the bigger market size which will be create, which will be much more than the SKF group. Now you globally you are trading at 5 to 6 % there, you are getting 30% here. Keep your balance sheet clean

Ashish Saraf (SKF): Our balance sheet is clean. We have gone through all the right approval processes and all that. We have given a credit line at 9%. We have not given money.

The money would be given only as is when the capex investment happens. It is not that I have said, okay, take INR 250 crores and that's it. The money has been given specifically for investment purposes, and it is being given to do capex investment. As and when they will do capex investment, they will draw from us.

Kotak MF: But where is the capacity? What are the products you are localizing?

Ashish Saraf (SKF): But I told you that there are different kind of bearings. I talked about wind and railways where we have excess capacity, but there are other products which are also medium and large size, where there is a tremendous demand. And we are predominantly talking about imports that we are doing from Europe, which we would like to utilize. TRBs, CRBs, SRBs etc.

Kotak MF: What exactly are we looking? What new segments which will be substituted? What will be scale, how big is the investment? What new capacity addition?

Ashish Saraf (SKF): There will be multiple investments. We are not setting up new plant, we are setting up new channels within the same plant. So the channels would be for specific products like SRBs, like medium sized DGBBs. Those are the kind of investments that we are looking at, which makes financial sense for us. Right? So it will be the purely it will go by specific products, a specific segment. And I talked about segments already, which is high growth segments, like heavy industry, construction, which is our strategy, where we are seeing growth. It's all inter linked. It is not that, okay, let's just give money because you want to pass on money. Whatever we will start manufacturing locally in India, we will start supplying from this entity to SKF India then subsequently sell it in the market?

Kotak MF: If there is an input of INR 100, it will become 50 in 12, 24, 36 months, given what we are doing investment, or it will be 70 of 100?

Ashish Saraf (SKF): As I said, we have 42% traded. Some of them are from India, naturally, that percentage which we are importing from Europe as well as China it will come down. For me to give you a number, it's very difficult because it's a journey, right, that we have started. It's not that I have given the entire and I have a clear roadmap of what all investments will make. It is a continuous evaluation process for small, small investments that we are going to make over a period of time to cater to the Indian market, right. And to that extent that investment will be deployed and to that extent that we import from Europe or other parts of the world, we will become competitive in India market…

Kotak MF: What is the downside to the 40% gross margin?

Ashish Saraf (SKF): See, as I said, from a margin perspective, our margin is sustainable.

Kotak MF: Sustainable….

Ashish Saraf (SKF): Right. Right.

Kotak MF: Because on wind you are rationalizing, also in railways.

Ashish Saraf (SKF): We are rationalizing overall business portfolio. That will be a tailwind which will probably offset some of the transfer pricing…

Kotak MF: After 4 to 5 years industrial growth which is 50% it can be 60% to 65%?

Ashish Saraf (SKF): Globally, we have 70% industrial and 30% automotive. Here in India will be probably one, one and a half years back, we're 50:50. So it's already changed to 50:40. So over a period of time, we believe industrial will grow at a faster pace than automotive.

Kotak MF: And that bulk of that growth will be traded?

Ashish Saraf (SKF): See, in the long term, our focus is that we will localize in India.

Kotak MF: How much do you think the localization should be? 58% I have been looking for a long time and I used to hear that is focus?

Ashish Saraf (SKF): As I said, when I say from our perspective, our focus is to localize in India. It may not necessarily all of it may not necessarily happen with SKF India, our focus is to localize from 58%. It may not go to 100%, but our focus is it should go to 70%, 75%, 80%. Some of it will get localized in SKF India. Some of it will get localized in SKF Engineering. How much it will get localized between that very difficult for me to answer.

Kotak MF: Any visibility on that?

Ashish Saraf (SKF): Difficult to say

Kotak MF: How are you making sense of the INR 250 crore credit line?

Ashish Saraf (SKF): It made financial sense.