



SONA BLW Precision Forgings Ltd. (Sona Comstar)

Q2 FY23 Earnings Conference Call Transcript October 28, 2022

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<https://sonacomstar.com/investor/investor-presentations>

Moderator: Hi, Ladies and Gentlemen. Good Day, and Welcome to Sona Comstar Q2FY23 Earnings Conference call. Please note all participant lines are now in the listening mode only as of now and there will be an opportunity for you to ask questions after the presentation concludes. Please note that this call is being recorded and we request you to place your lines on mute except when you are asking a question.

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Here is a disclaimer for the call.

Some of the statements by the management team in today's conference call may be forward-looking in nature and we request you to refer to the disclaimer in the earnings presentation for further details.

The management will also not be taking any specific customer-related questions or confirm or deny any customer names or relationships due to confidentiality reasons, so please refrain from naming any customers in your questions.

Now I will hand over the floor to Mr. Kapil Singh, Nomura Head of Consumer and Digital Commerce Research India and Lead Auto Analyst. Kapil please go ahead. Thank you.

Kapil Singh:

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Thank you, Gigi. Good Day everyone and wish everyone a very Happy Diwali! To take us through the Q2FY23 results and to answer your questions with us, we have the management team from Sona Comstar led by Mr. Vivek Vikram Singh (MD and Group CEO), Mr Kiran Deshmukh (Group CTO), Mr. Sat Mohan Gupta (CEO of the Motor Business), Mr. Vikram Verma (CEO of the Driveline Business), Rohit Nanda (Group CFO), Mr. Amit Mishra (Head, Investor Relations) and Mr. Pratik Sachan (DGM, Corporate Strategy and Investor Relations).

I will hand over the call to Vivek for his opening remarks, followed by the presentation. Over to you Vivek.

Vivek Vikram Singh: Thank you, Kapil. And I hope everyone had a great Diwali. I have a slight, I actually got the flu a couple of days ago so I am not that well and my throat is a little strained so do not please misunderstand it for a lack of enthusiasm or optimism. Anyway, on behalf of Sona Comstar, I would like to welcome all of you to the earnings call of what has been our best quarter ever across all the financial metrics of revenue, EBITDA and net profit.

While we are understandably proud of that achievement, we believe that when talking to shareholders, bad news should take the elevator. So as we always do, we will begin with the negatives. First, one of our major erstwhile markets, Europe continues to remain under pressure from the demand perspective. On the cost side, like we predicted last quarter, raw material prices have started cooling but not by much, so pressure on margins from the input side is not completely alleviated. Additionally, there was a large one-time inventory correction at one of our major EV customers early on in the quarter. So while sales have resumed at the normal run rate, this has made our Q2 EV revenue percentage share lower than it would have been otherwise. There is also, and we do get questions around this a lot, a lot of macroeconomic uncertainty about the world in general. And instead of adding our voice to an already crowded field of opinions, I guess we just like to tell our shareholders that look, we built a solid resilient and diversified low fixed-cost business model and this is obviously good in good times but on a relative basis, we are quite brilliant in bad times. I mean you just have to look at our history. We have built a business which does relatively outperform in harder times and I mean just look at this quarter. EV sales were lower than the last quarter, so lower sequentially; differential assembly sales were lower, sequentially; Europe, which is one of our higher margin markets was much lower, continues to be weak; and yet we have delivered sequential as well as year on year growth in revenue, EBITDA and net profit. And not only that, we have also managed to improve our margin sequentially. So I think that is the thought I want to leave you with and not ask us too much about macroeconomic outcomes and forecasts because, to be honest, a lot of you listening in know more than we do about those things. All we can assure you of is how strong our business is.

With that, we move on to the good news part and there was quite a bit of that this quarter. We have added one new EV Program which is perhaps not so important because of its size, but it is fairly important directionally because ever since our IPO we have got a lot of questions on this trend of how much is in the OEM and how much is going to be outsourced. And I talk about this later. We have also added a new product to our portfolio, spiral bevel gears. It has taken us many years, I would say more than a decade. This project has been going on from before my time. Many years of engineering effort to get this product made through the forging route and because it opens a new market and a new revenue stream for us, it is an extremely, extremely gratifying outcome for Vikram, Mr. Deshmukh, and the entire driveline team. We have also updated our product roadmap. We have an annual strategy exercise every August and we have added some new and exciting future products that we intend to introduce in the next few years, and Mr.

Deshmukh will talk more about these later. As a company, we talk even in our board, even in our executive board, even in internal meetings, 90% of the time on technology. So I hope some of that reflects when we talk to our shareholders as well. Another good news, a lot of the programs that we launched last year and we won last year kind of started coming into production from this quarter which has contributed to revenue growth and will continue to contribute to the growth in the next couple of quarters. Lastly, the domestic auto market has been growing significantly year on year and that obviously, because we are dominant in our presence in differential gears in India, has added a tailwind to our numbers.

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Right, so to the numbers. Sequentially, we have had a double-digit growth across all the three metrics. However, what we will talk about on this slide are year on year basis, we have seen a robust revenue growth of 12% while EBITDA and net profit have risen by 7% and 5% respectively. BEV revenue in absolute terms grew by 6%, while the BEV revenue share was 21% due to the one-time inventory correction that I spoke about that happened in the last quarter. If we were to leave those few weeks of zero schedules out, the revenue share would have been much higher than this.

Also, quite importantly, our EBITDA and PAT margins have returned to our normal range of 25 to 27% and 14 to 16% respectively, after two quarters of unusual margin pressure. This is an encouraging sign for us and I hope input prices continue to cool in the quarters to come.

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Coming to H1 I am proud to report that we managed to increase our revenue, EBITDA and PAT margin by 15%, 5% and 5% respectively over what was a pretty strong H1 in FY22. And this is despite unprecedented inflation and both supply-side as well as demand-side disruptions in almost all of our key markets.

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Now coming to our strategic priorities; so first, electrification. BEV revenue share was 21% in H1 FY22. This has increased to 25%. In absolute revenue terms at 294 crores almost, the BEV revenue has grown by 33%. We continue to build on our EV order book. In Q1. We have added one new EV Program which is from an existing customer but this is for differential assembly.

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So with this addition, we now have 37 EV programs across 23 different customers. The program which we won, like I said, is to an existing customer in India where we have been supplying differential gears for their ICE as well as EV variants for years. But we are now moving up to supplying differential assemblies for their next generation of born electric vehicles. And this is quite an important win as a trend because, like I said, I have often got this

question. So this is now the second customer and hopefully there will be a third in time to come where we have moved from being differential gear suppliers to differential assembly suppliers, which indicates that when it comes to the electric vehicle transmission, there is higher outsourcing than used to be earlier. Obviously, in commercial terms, it means our value per vehicle goes up by anywhere around 3 to 6 times depending on whether there is a final drive gear attached or not. And lastly, also, I should mention that this program that we won has a start of production in FY24 itself which also speaks to the increasing OEM urgency to launch new EV variants.

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This brings me to our net order book. Now we did consume some parts of the order book as some programs entered serial production or ramped up and that is the key reason for our sequential growth and the addition of 4 billion means that our net order book stays at 205 billion at the end of Q2. The only change worth mentioning here is the increased proportion of EV going up to 68%.

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With this, we come to diversification which is one of our key strengths. The weakness in European and Asian markets in the first half, and if you remember, in Q1 Asia was very very weak because of the zero covid shutdowns etc. It means that the revenue share from hybrid and micro-hybrid has been lower as compared to previous years which is quite natural as these are the two markets with the highest proliferation of hybrid vehicles. Stepping away from just the first half on a longer-term trend. The increasing share of BEV and decreasing proportion from ICE seems to be continuing unchanged.

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Geographically, things have been quite volatile as you can see Europe and Asia used to be 40% of our revenue in FY22 and this is reduced to only about 25% in H1. The gaps of course have been filled up by the US and Indian markets which continue to be quite robust. They have increased to 42% and 32% respectively. Now, relative market shares are always a little tricky, especially in the times of strong growth, right? Because in a growing thing relative has to be seen in the context of absolute numbers rather than just relative percentages. So, Europe also, you would notice that if you look at Q1, Q2 was better than Q1 at least. So that is an improvement. However, like I said initially, it is far far away from how strong Europe generally used to be.

Coming to product mix, the same geographic factor is visible as micro and plug-in hybrid starters fall from 26% to 21% in H1. And although just this quarter the numbers were reasonable. Again, the other notable trend that repeats here in the vehicle segment is traction motors are now 4%, which is also the electric two-wheeler percent, which is 4%, which is ahead of our own internal estimates so far.

So with this I will turn the call over to our Group CTO Mr. Deshmukh. He has some fairly important progress to report on the technology front. So over to you, Sir.

Kiran Deshmukh: **Slide 15:**

Thank you, Vivek. Good evening, ladies and gentlemen.

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We have been sharing this technology roadmap in every earnings call. And since the market conditions are dynamic and the technology landscape continues to evolve, we keep tweaking our tech roadmap to align with the changed realities. This time, for example, we have fine-tuned one product and added as many as six new products in the white area, representing the products under development that are being explored.

As I mentioned during our past earnings calls, our vision is to become a significant player in electric, autonomous and connected vehicles, offering integrated solutions to our customers. We are exploring partnerships and acquisitions of technologies such as sensing hardware and software solutions that address the burgeoning autonomous and connected vehicle space.

As a tweak to our technology roadmap, we have removed the DCDC converter from the chart and introduced an integrated motor controller that uses the available resources also to do the function of the DCDC converter. This way we believe we can provide a more efficient and cost-effective solution to our customers.

To augment our content in the final drive units for EVs, we are developing epicyclic gear drives consisting of several Helical Gears. We also have leveraged the competencies of our motor and driveline businesses to build an Electronic Locking Differential (EDL). This device located in the differential, electronically allows both wheels to turn at the same speed, providing additional traction should the vehicle become stuck.

We recognize that our metal-forming know-how can do much more than the net-formed bevel gears we are known for. We have been exploring how we can bring value to our technology while making the products in an EV drive train stronger, more durable and cost-competitive. As a result of this study, we are now developing three products where the bulk of machining will be replaced by forming. Our forming process will save the input material and provide additional strength to the products. So we have created two essential parts of the EV drive motor using this method: Steel Rotor Shafts and Non-Ferrous End Caps. We are also in an advanced stage of developing formed Park Gears. So all these products are now displayed into the white area, showing what we are developing and as they get developed and matured and get commercialized, they will move to the blue area.

Finally, I would like to share a significant breakthrough we accomplished during the quarter. Vivek mentioned it earlier. We have successfully

developed net-shaped spiral bevel gears. Perhaps, for the first time in the world, spiral bevel gears made by forming rather than cutting the gear teeth have been commercialized and we will soon be supplying these gears to global farm equipment manufacturers.

This development is big because it is poised to do to the automotive spiral and hypoid gears, what this technology did to the straight bevel gears several decades ago. Because net-shaped gears are made with lesser steel and have a more favorable grain structure than their machine counterparts, they offer an unmatched price performance pressure. With decades of expertise in designing and making net-formed straight bevel gears, we can now provide the same benefits for spiral bevel gears. Soon our customers will be able to get Spiral and Hypoid gears far superior to the current machined gears at a competitive cost.

We have always directed our R&D efforts towards creating groundbreaking products that give a unique value to our customers. This is one of those examples and we will continue to be on that path in the future. With that, I hand over to Rohit to cover the financial update.

Rohit Nanda:

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Thank you, Mr. Deshmukh. A very good day to you all. It is my pleasure to share our second quarter and first half results for the financial year 2023 with you.

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This quarter, we have clocked the highest-ever revenue, EBITDA and PAT, at 657 crores, 166 crores and 93 crores respectively. In terms of revenue, we had a growth of 12%, wherein BEV revenue grew by 6% year on year and non-BEV revenue this time grew by a strong 14%. While our top three geographies of North America, India and Europe grew by only 4% in light vehicle sales. A large part of this growth has come from the ramp-up of some new programs which strengthens the credibility of our diversified business model once again.

Our EBITDA grew by 7% to 166 crores. Our EBITDA margin for the quarter was 25.2% against 24.2% in the previous quarter showing an improvement on a sequential basis. Compared to the second quarter of last year, the margin was lower by about 1.2% which is largely on account of the arithmetic effect of material price increases despite material cost passthrough. Our PAT was 93 crores, showing a growth of 5% compared to the second quarter of last year.

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During the first half of the year, our revenue grew by 15% and stood at 1,247 crores. Our BEV revenue grew by 33% at 294 cr and it constituted 25% of our total sales. Our non-BEV revenue grew by 10% whereas light vehicle sales in the three key territories declined by 6% over the same period.

Our EBITDA grew by 5% to 308 crores. Though margin percentage was lower by 2.3%. But again, this is primarily due to the arithmetic effect from the RM price increase despite the cost pass through. Our first half PAT grew by 5% to 168 crores when compared to the adjusted PAT of first half of the last year. Last year, first half PAT, as some of you may recall, had an exceptional income on account of reversal of IPO expenses which had been adjusted to arrive at a fair comparison of the numbers. There was also an improved margin transmission from EBITDA to PAT during the first half, mainly due to lower finance costs.

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Moving on to the first half cash flow, the company generated 231 crores of cash from operations. An important takeaway from the cash flow summary here is that high organic growth of the company has continued to be cash accretive so far. As we have managed to generate 65 crores of free cash flow during the first half, even after deployment of 166 crores in Capex. Besides this, we also paid dividend of 45 crores during the first half.

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This brings us to the last slide of our presentation in which we report the key ratios.

The first one being value addition to employee cost ratio. It has further improved to 6.2 times which shows that marginal growth and value addition continues to improve relative to the growth and employee costs of the company. Our return ratios of RoCE and RoE continued to be strong above 25% though they are a tad lower than that of the last two years, primarily due to higher working capital and ongoing Capex expenditure. Return on equity also had an inverse base effect due to the primary equity raised in the IPO last year.

Our net debt continues to be negative, reflecting the balance sheet's potential to raise debt to support future growth. Working capital turnover ratio is also largely similar as earlier periods at 3.8 times, indicating that growth in working capital has been largely in line with the growth of the underlying business. Lastly, the fixed asset turnover ratio has come down a bit to 3.9 times, mainly on account of capitalization of our new unit in Pune which we have set up to support execution of the growing order book on the driveline business side.

This brings us to the end of our Q2 and H1 earnings presentation and I will now hand the proceedings back to the Namura team for the Q&A.

Moderator:

Wonderful. Thank you very much, management. We will now open the floor for the Q&A session. So if you wish to raise a question, please use the raise hand function located at the bottom right of the Webex page. We will unmute your line and prompt you to speak or you may submit your question through the Q&A chatbox addressing to all panellists. Please be reminded

to keep your questions to maximum of two questions. If you have more questions to ask please return to the queue. Thank you.

So first up we have Mr. Garvit, your line is unmuted, please proceed with your questions. Hi, Mr. Goyal?

Garvit Goyal: My question is basically from the demand side, actually how we are seeing that demand trends going on in Europe and America currently, and in the upcoming quarter, specifically from the EV side, Sir.

Vivek Vikram Singh: Although I did mention that; but to add our voices to macroeconomics, I will tell you what we see on 28 October at 4:25 pm and it may not be valid even a month out because things have become so dynamic. North America is quite strong actually demand wise. EV demand, like I said, continues to be as strong; India continues to be strong for off highway, passenger vehicles and commercial vehicles; Europe has been weak all through this year. I think ever since March this year, Europe has been weak and continues that way. Obviously, all of us read a lot, and we hear a lot but this is where things stand as of today as of now, this is what I see.

Garvit Goyal: Okay, okay, thank you. Thank you, Sir.

Moderator: Wonderful. Thank you for your question. So next up we have Mr. Jinesh. Your line is unmuted, please proceed.

Jinesh Gandhi: Hi Vivek, so a couple of questions from my side. Firstly, given that 27 programs are yet to get into serial production...

Vivek Vikram Singh: Can you speak a little louder please?

Jinesh Gandhi: Is it better now? Yeah, so given that 27 programs are yet to go into serial production, can you give some flavour on how many programs you expect to go in serial production in the second half and for FY24 and 25?

Vivek Vikram Singh: So I won't talk about the second half of this year, but a majority of them should enter production within the next six quarters, so the full next year, because there have been delays, I won't obfuscate that. There have been two or three programs that were supposed to actually start this quarter and they have not. Maybe they will start by end of next quarter. Maybe they will be delayed even further because, although and I think you remember we had this conversation, the semiconductor-led supply chain shortage is not a shortage anymore, it is a supply-demand mismatch; the right kind of chips for the right kind of component to the right kind of OEM. And those kind of things still persist. So it is such a weird thing to have that there are places where people have everything, all the means of production but demand is an issue while there are some people where demand is not an issue, but they cannot get the supply chain thing sorted. So it is still a little messy to try to pinpoint for extremely short term, but most of them, I think will start in the next six quarters.

Jinesh Gandhi: Got it. And second question pertains to the new product, net spiral bevel gears. Can you give some color on the size of the opportunity? And you talked about some orders in hand. So how big is the order? And by when do you expect commercialization of that?

Vivek Vikram Singh: So the first order is not that big. Like I said, we are first starting with a very specialized off highway vehicle product. We also want to make more before we keep taking it public, and for passenger vehicles, once we make the same thing in hypoid then it becomes passenger vehicle and that is where the big market is. I would say the market opportunity addressable is as big as the differential gear market in total size. However, I mean to get to where we are in differential gears to like 7-8% world market share. It took us 20 years. Now it won't take us 20 years to do this again because now we are somebody at that time we were a startup. But still I mean give us 5-6 years minimum to reach something of size. But yeah it is a big enough market and value-wise some of these products are fairly large.

And the same, I do not know if you got that point Mr. Deshmukh made that exact same rationale and USP or you know right to win what we did to straight bevel gears when we made it through the forging route, the exact same thing happens to spiral now basically.

Jinesh Gandhi: Right, Right, I got that. Thanks.

Moderator: Wonderful, thank you very much. So next up we have Anay. Your line is unmuted. Please proceed with your questions.

Anay Mittal: Hello? Mr Vikram can you hear me?

Vivek Vikram Singh: Hi Anay, I can hear you loud and clear.

Anay Mittal: Thanks. Vivek, I might go to this topic again on that Europe trend and demand, so sorry for that but I need some clarity, specifically one or two areas. Right? Are you seeing any trend where a customer has a budget for a particular EV project and they are putting those on hold because of ongoing whatever? It is like too many things are happening at the same time. So are you seeing trends on those lines? Number one.

Number two, when you said that other markets, right, like particularly India, you said that demand is strong and we have domestic consumption and stuff and infrastructure is booming here in India. So are you seeing any demand like those offsetting your near-term losses in other geographies?

Vivek Vikram Singh: So thanks. I will take the second part first. I mean this is the first time we have even crossed 600 crore revenue in a quarter, so we are actually at 650 plus. So this is the best we have ever done.

Anay Mittal: No no, first of all, I would congratulate you for that, Vivek.

Vivek Vikram Singh: Not for congratulations, just to give you the challenge of when you grow that much relative share is slightly misleading. So if you look at Europe's share even

now in absolute terms it is not that bad. It is just that on a relative basis where everything else is growing a lot, it has not grown at all. This quarter, so there is a bit of actually confusing signal even to us because we also go by our customers and what they are telling us and even more importantly, actions speak way louder than words. How much are they buying and how much are they picking up every month is the biggest indicator. This quarter was higher than last quarter for us. Although the commentary and tone seems not so optimistic, the numbers are not so bad in Europe. Other markets like I said, North America and India are doing fairly well. So nothing to say, but even you know the problem that you cannot stick your neck out for too long because you do not know what is going to happen in a month or two. The best thing we can do is be agile, be dynamic and act with, you know, alacrity. So there is no loss to make up because in a sense and I will be more realistic and slightly brutal, if sales are gone, they are gone, you know, you are not gonna get them back because if a guy has delayed their purchase decision by six months, it is not going to come in this time frame and if you lose time in pursuing anything as valuable as it may be, time is the most valuable commodity. So you have lost that. So I do not think anything gets made up because we cater to the global vehicle market, if enough global vehicles are sold anywhere we will be okay. But yeah, if something happens that affects the whole vehicle production, that is more challenging.

Anay Mittal: Thanks. Thanks, Vivek.

Moderator: Wonderful. Thank you very much for your questions. So next up we have Chirag. Let me just unmute Chirag's mic. Okay, can you try to see if you can speak? Yes please proceed.

Chirag Shah: Am I audible?

Vivek Vikram Singh: Yes Chirag, very much so.

Chirag Shah: Yeah. Hi, good afternoon everyone. Thanks for this opportunity sir. Two questions. One, last few quarters, if we see there have been series of disruptions happening, you know, be it OEM volumes and higher RMC etc. etc. So if we take a step back and if you have to assess where are we today in terms of volumes or like to like benchmarking. Where are we today? In terms of volumes, say a year back, where we were and where are we today? If you can give a ballpark understanding taking into account the geography mix issues, the product mix issue that we are going through. So that is the first question because we all focus on revenue for the company right there is so it helps us to understand where are we in terms of your benchmarking?

Vivek Vikram Singh: So Chirag, that is a very interesting question. I mean the whole presentation was the answer to that in one sense. The thing is, it is hard, it is not just the last four quarters by the way. I was given charge of this company in February 2019, so I have never seen a normal quarter, so I do not know what a normal benchmark is anymore. I think what that has allowed us to do is build a business which handles volatility relatively well. I would not say we are antifragile but fragility does not shake us as much as it would others, let's say

peers. Again, reasons: very low fixed cost, very high value addition upon employee costs. Do not choose products which are very commodity or market linked that one market goes down and suddenly you are out of business. And you have seen that all of those tests being applied. So I would say we continue to be focused on that, that as a business we are strong and resilient. Markets have not been great, I mean if you look at it and there are enough reports, I mean Nomura, BofA, all of them do a very fine reporting line by line of each market on light vehicle etc. No market has really done well. If you look into last six quarters, it is just now that we talk about a year on year, so we compared this quarter or this half with the corresponding half last year. But if we go back to 2018 and you being an auto analyst yourself seen all of this. Between 2010-2018 like clockwork the auto motor market used to grow by 4-5% every year. I think those days are just not there anymore and companies like ours which are fit and built to handle volatility and shocks, I think that is more important than just looking at trends and saying this market grows, I also grow. What can you do in a dynamic environment where there are many moving parts, I think that is what our benchmark is. Our benchmark is, how much money did we make? How much returns did we make? Did we deploy our cash properly? That is what our metrics is like I get the cash balance by the way, everyday we have very extreme metrics. We prepare for the worst literally. What is the worst? Your revenue goes to zero, absolute zero right? Every day we have a number that the executive board gets, which is how many months we can continue like we are today without a single paisa of revenue and Rohit obviously knows that answer well. We may not want to share it, but it is a long time and that is what we build our business for. That what is the worst that can happen and what do we do in those times and these are the benchmarks that matter to us, the others that we report of course they matter, the metrics that are that help analysts commonalize. People compare A to B, but for us, it is this: how strong are we because we believe the world will continue to be volatile and uncertain?

Chirag Shah:

Thanks, thanks for this. The second question was the new product, the white part of the product chart that you have. So I understand that proof of concept happens then after that you add a product over there. But if you can elaborate more on that, in general at what stage you add a product over there and how should we look at the development life cycle? I understand that you may have your own set of successes and so on and so forth. But internally, how do you look at when you add a product in that particular white area, if I use that word and what are your aspirations and how fast do you want to make it a commercial product or at least a product ready for approval stage from OEMs.

Vivek Vikram Singh:

Great question Chirag. So I will let Mr. Deshmukh answer it in detail. However you are right the variance is fairly high that there are products there which could enter commercial production in a quarter or two and there are products which frankly may never also enter. Even the spiral bevel gear by the way, like I said, it has taken us more than a decade from starting to actually getting it done. So it is a very good question, Mr. Deshmukh sir?

- Kiran Deshmukh:** Yeah. So as in every R&D project the success is not assured. So we keep on working on it and of course we work on those projects where probability of success is quite high and probability of commercializing that product into something which will be a commercial success is high. That is what we look at. So there are products which in the white area today, which may come into the blue area next quarter. There are some more products there, which may not see the light of the day. Like, Vivek just now mentioned the spiral bevel that has entered the blue area now this quarter, we have been working on this for more than 10 years. So it is a long journey and a lot of products which we drop and there are a lot of products that will come into it. It is a dynamic chart and depending upon the technology landscape, how it shapes, depending upon the market conditions. We keep on, we have internal discussions regularly, we have strategy sessions and we keep on modifying this chart based on these realities.
- Chirag Shah:** Thank you. And if I can squeeze in one last question. So in general, Vivek, your view on demand, especially in China. How should we look at the ramp up? Because we read a lot of news flows coming across from China, but you are probably the right person to indicate, how should we look at the ramp up in volumes happening? What's happening over there?
- Vivek Vikram Singh:** So, I mean, this quarter has been exceptionally good in China as all the news flow will indicate. How sustainable it is? We will all have to wait and watch. I am not 100% sold that it is intrinsic and structural. I think there are other elements, there may be subsidies, there may be incentives, there may be other factors that play. Unsubsidized, latent demand, converting to actual demand, that's a real thing. Right? When you have a huge class of people who want to buy and then they eventually have the means to buy those vehicles. So again, I will be like slightly more skeptical about that.
- Chirag Shah:** But if you look at next few quarters, the next 4-6 quarters, can we assume that this kind of run rate that we have seen in the last quarter is sustainable in short term, say next four quarters or six quarters, is that the indication that you are getting from your OEMs?
- Vivek Vikram Singh:** So are you talking about us or are you talking about the China automotive market in general because we are very small in China and China is a very big market. So very different things.
- Chirag Shah:** Yeah, I was actually trying to figure out for both to be very frank.
- Vivek Vikram Singh:** Macro and Micro are very different, Chirag, because see micro growth can double when you are that small, right, you just have to win one new program and you can double. So that is and that is not very consequential to be honest. I would focus more on North America, India and Europe, in that order for growth.
- Chirag Shah:** Thank you. Thank you very much.

- Moderator:** Thank you Chirag for your questions. So next up we have Nitij. Nitij your line is unmuted. Please proceed.
- Nitij Mangal:** Hi, good evening, Thanks for taking my questions. Firstly I want to go back to the technology roadmap, it seems the range of components you are working on in current and legacy categories is way more than what you have in legacy. So let's say someone has to think of, what is the revenue potential from these components on a 3-5-7 year kind of basis. How should one think of that? And also in your order book, is there any contribution coming in from the current components?
- Vivek Vikram Singh:** Hi Nitij, so firstly Happy Diwali!. Good to hear you on this. Again, the black ones were legacy, this is what we started with when we let's say 2016, 2017, right. All the blue ones are the ones where we actually produce and have orders for they are in. So these are all products that we have and we offer. The white ones are the ones where there is a degree of uncertainty on when would they enter or add to our revenue stream? Right. That's the question?
- Nitij Mangal:** Yeah. And I do not know, I mean is there any way to quantify a bit in terms of, you know, you know, obviously there is, there are probabilities of successes and the farther you are in the commercialization the more uncertain it is. But let's see if you think of the blue part of the chart, is there a way to think of what is the total revenue potential and then you know, think of probabilities of success.
- Vivek Vikram Singh:** Yeah. You do not have to think of probability if it is blue, the order book is the value. So blue plus black is equal to the order book value.
- Nitij Mangal:** And how much of the order book is blue?
- Vivek Vikram Singh:** I would say a large part, right, because the starter motors and differential gears would not be that big. All differential assembly is in blue and yeah, I mean if you were to look at it, I think about 60 maybe 65-70%, would be in the blue. I know what you are asking, Nitij. You are asking in the left hand side in the excel sheet, how many rows and then how do I add the columns, right? But what I am saying is, probability is not there, that is order book only. The white is where probabilities come in because that is where you could be zero or you could be hundred and that is hard to predict because as you know, I mean we only add to blue when we get a purchase order. So blue is certain, probabilistic is all white. But you know if you had met me in 2015, 2016 and you come to our office, we made one product, differential gear. So this is all that blue is just last 6-7 years of work and our revenues would be perhaps, I do not know. Pratik, what is the revenue share from differential gears? 20%? less than that?
- Pratik Sachan:** In the orderbook?
- Vivek Vikram Singh:** No, what is today our revenue from differential gears as a product as a percentage? It is on the chart. Just go one chart back.

Yeah, this is it right, differential gears is white. This is 31% of our revenue. So like I said, All of this has been added in the last 5-6 years, so hopefully 5-6 years later all of the business that is there today becomes again 30-40% and that is exactly by the way, I was not being philosophical when I was responding to Chirag's question. That is how you build a business that can withstand stresses in a falling market and all of that. That whatever you have 5-6 years later should only be a portion of the revenue of that time. And that is the endeavor that we keep making new things and we keep gaining market share and the things we have. That is it. These are the two things.

Nitij Mangal: Okay. Alright, thanks. And secondly what kind of potential benefits you are thinking from the PLI scheme.

Vivek Vikram Singh: Large, but we have not quantified it and as we have spoken before, you know that the scheme outlay is fixed. the number of claimants and exactly what they are entitled to is kind of still up in the air. Right? So all of us, if I were to apply the percentage in a lot of our parts which are electrical and high tech which will qualify, they qualify them theoretically for the highest percentage but I do not think that is possible because that is a very very large number of incentive.

Nitij Mangal: Okay, thank you very much.

Moderator: Thank you very much. So before we open the floor for further questions. I will now pass to Sid to address some questions we received from the Q&A box. Sid over to you.

Siddharth Bera: On the road map, we had shared in the past on various technologies, like Enedym, IRP etc. on the motor side which we had done and we had planned to sort of start production in the next couple of years. So any update or any progress can you share about where are we in terms of the clientele and the plan to sort of start those?

Vivek Vikram Singh: Thanks Siddharth. I will ask Mr. Deshmukh to respond to that. I think three - IRP, Enedym and C-Motive.

Kiran Deshmukh: IRP, Enedym, C-Motive. With IRP and Enedym the projects are in very late stage I mean they are at very advanced stage of development and they should be ready for commercialization in next 2 quarters, next six months. Again it depends upon the final results, final test results and like I said before R&D projects are binary. You succeed, you do not succeed, depends upon what results you get. You may have to do some tweaking, you may have to take one more iteration, in which case it may take longer time but if everything goes fine then we should have products coming from these two partnerships which is IRP and Enedym. Both are magnet free motors; should be ready for commercialization in the next six months. C-Motive is a third company with whom we are working, it is a completely new technology.

Vivek Vikram Singh: I will take that. It is a bit of a moon shot to be honest because it is an entirely different way of making motors through electrostatic technology. So that I

do not think you should consider for any forecast estimates. Even for us, it is one of those things that if it works out, changes the way motors are made and if it does not, well the option value is not that high. It is like an option that we put in about \$1 million behind that research. It is trying to eliminate all of it, the rotors, even the copper I think will go. So it is a very different way. Hence the probability is obviously lower because the closer you are to the way things were made, the probability is higher. So Enedym is obviously higher because it is a way motors have been made earlier. But they had a problem called torque ripple which is that the torque literally rippled if you made a graph instead of being a very steady way, which was a rippling way. And I think the work we are doing with Enedym is trying to solve that problem. And if we do solve that it becomes a very very proficient magnetless motor. Hence the higher degree of certainty. Electrostatic means through static charge it is trying to develop magnetic current which is obviously much further away from how things are normally done right now.

Siddharth Bera: Got it, and for the existing motors like BLDC and PMSM in which we are already supplying, and given the strong preference we are seeing for some of these electric models, would it be possible to share any numbers in terms of capacity? How you are, you have built currently and depending on the sort of because you are getting how much do the capacity will touch in the next couple of years.

Vivek Vikram Singh: So Sat, if you could touch upon installed as well as capacity utilization. Siddharth wants to know the capacity that we have for BLDC and PMSM, you know 2 wheeler, 3 wheeler motors.

Sat Mohan Gupta: So, right now we have a capacity of around 250K for hub motors and around 75-100K for PMSM motors in our Chennai plant.

Siddharth Bera: And the utilization levels will be?

Sat Mohan Gupta: Utilization levels as you know, it depends upon quarter to quarter and right now around 35 to 40%.

Siddharth Bera: And lastly sir, on the Capex side, if you look at it again for the next couple of years what is the number you are looking at, any change in that and broadly in which areas you are planning to sort of do the capex. That will be all for me.

Vivek Vikram Singh: So Rohit?

Rohit Nanda: So next 3 years we are estimating the capex to be 900 to 1,000 crores to take care of the existing order book.

Vivek Vikram Singh: So Siddharth, it only goes up and down depending on, you know if you see that in the near term something is not going very high or whatever. Then you kind of push out the cash flow. So cash management of Capex is a different thing from commitment of Capex. So we are fairly actively monitoring that. I think in the second part, Rohit, he wanted to know which areas. So I will answer that, most of it is actually towards, I would say, the largest would be

differential assembly and final gear and other EV transmission parts that we also showed in white, some of it will obviously start doing. The second largest would be towards the IMCM, the integrated suspension module product. The third largest would be towards adding more differential gear capacity which also serves by the way the differential assembly business and fourth would be the traction motors. Obviously there is zero capex deployed for starter motor.

Rohit Nanda: So it will be 80% for the driveline business and about 20% for the rest of the business.

Siddharth Bera: Okay thanks a lot sir.

Moderator: Thank you very much, Sid. Thank you. So next up we have Basudeb. Just a reminder to investors due to limitation of time please refrain to two questions per person. Thank you.

Basudeb Banerjee: Yeah my thanks. I have a couple of questions sir, one as in your presentation also you have explained and earlier also we discussed that the optical effect of metal inflation impacting margin, so with metal prices correcting since what almost June how much of the revenue is reflecting metal deflation this quarter and what part of the potential optical reversal in margin is already there in the numbers?

Vivek Vikram Singh: Thanks Bhaskar. Not much has happened for alloyed steel actually. Only Rs 5,000 per ton was the reduction that we got, so not that much as we were expecting. But yeah it is already in the margins. Rohit, Vikram, if you want to add to that or if you are seeing anything more.

Basudeb Banerjee: Just expected to understand how much potential of that reversal is still pending compared to the 300-350 bps of negative impacts.

Vivek Vikram Singh: Huge, I mean we are still at almost the second highest steel prices we have seen, in perhaps a decade.

Basudeb Banerjee: And this Rs 5,000 per ton is on a base of how much, sir?

Vivek Vikram Singh: So, Rohit, do you want to share, you have a slide on the build up, on how it has kept going up? I mean 5,000 gets us to what the prices were in March 2022.

Rohit Nanda: In April, we had a large price increase, in fact July price decrease does not even take care of the price increase that we had in April actually. So it is higher than the March price.

Basudeb Banerjee: So broadly speaking, with operating leverage not being that substantial huge scope for this reversal in the base effect. Definitely, plus PLI being unaccounted so the margin has a huge scope to move up, per se.

Vivek Vikram Singh: Yeah, and like I said before to you also that the largest variable is steel price, that is the biggest variable. If you remember, in 2020 our margins had reached almost 30% because the steel prices became quite low and since

then it just kept climbing climbing climbing to this level. And like Rohit rightly pointed out, this is actually not even the price increase that happened in April has also not been reversed. So this is the 2nd highest price point in the last I do not know how many years.

Basudeb Banerjee: Sure, thanks.

Moderator: Wonderful, Thank you, Basudeb. Next up we have Jay. Jay your line is unmuted. Please proceed.

Jay Shah: Hi, can you hear me?

Moderator: Yes, loud and clear.

Jay Shah: Congratulations team for a great and a superb quarter and hope you guys had a great Diwali. So I want to ask you this question Vivek, as we have seen in the last few quarters and even prior to listing, majority of our order book used to be you know maybe 6-8 quarters or maybe in that range down the line and like you just said FY24 we will see a lot of ramp up. So, in a way can you say that you know last 3-4 years the industry itself has been adopting the standards to EV and hence now the shift will be much more quicker even when you get order like I think in the last quarter, I asked you this questions, where from the time you finalize the deal and when it goes to, you know production, how much time does it takes and now you see a majority of our 205 billion order book is coming into production in FY24, so would you be able to say that now? Okay, the curve of production can be much steeper?

Vivek Vikram Singh: So Jay, look very astute of you, number one and also Happy Diwali, I did not have that good a Diwali because I fell ill but still. So yes, in a way if I were to kind of to draw a visual analogy, the end time for ICE and the starting point for new EV models was actually drawn a couple of years ago. So the people who were late to that point, let's say who were launching new models or who are starting a new model now, they have very little time to go to SOP. So yes, the pressure on us though obviously increases a lot for these customers, that I think I mentioned today and good I think you caught it. I said that there is this Program we won they want to start next year. This is not usual, you know, 18-24 months is the usual time. So I think a lot of OEMs are now under pressure to catch up and this trend will accelerate and I think Europe has already passed, 2035, is now a hard cut off. ICEs have to drop off if you have to now start doing new model launches. Let's say you are a car maker and you have a car launch in 2027, how many people would think of launching a diesel or petrol car in 2027? Outside India of course. That number is very low, so when you know that already and you know that it is inevitable that you have to launch only EV variants. Now you are getting into a hurry, so yes, yeah the urgency is increasing however and this is a note of caution for the people to also read this and other supplier, there is a time period beyond which we cannot crash these processes, these are all safely critical things, there is an amount of time that one must put in testing, and samples, and validation before we go to market, we do A sample, B1 sample, B2 sample, B3, C... before we go to production, so it cannot be cut down beyond a point also

but you are absolutely bang on right, the urgency and the tone has shifted to you know, one of those everything is needed tomorrow.

Jay Shah: Got it, got it. And just the last question now that we are seeing more adoption, I would not name the OEM, but yeah they have come with another variant where the price of the variant is just half of their actual variant which was doing so great so would it be that you know your wallet share per car as you know if you if you can say it rightly like if Moore's law is applied and if the cost of car keeps coming down, your wallet share per car might go down but obviously your product will go into more number of cars, can that be a possibility?

Vivek Vikram Singh: It is right, I mean if you have seen that chart in which we defined our strategy, we started with very low volume but very high value and very few number of cars, very high performance and then we kept moving down to when EV becomes mass. See still whatever saying that EV is not that mass, it is still most of the successful EVs are relatively expensive for most markets. It will become mass one day, so there is a point which will come, but that is I think 10 to 15 years later when EV is the vehicle, there is no other power train, there is no competing power train. At that time, which sector do you want to specialize in etc, because right now for us it is how much value total and how much can that be done balancing 2 things returns and profit, that is it. There is some things which will have higher EBITDA but lower return some will have slightly lower EBITDA but higher return and you got to balance those two. But yeah, exciting times, the next 2-3 years will be exciting. Yes, they could be, you know, a couple of quarters here and there, with uncertainties and geopolitical stuff, but I think the direction is pretty clear and I think it is also getting pretty linear.

Jay Shah: Okay. Okay, thank you so much and God speed recovery to you Vivek.

Vivek Vikram Singh: Thanks. Yeah. Thanks

Moderator: Wonderful, thank you very much. So due to the time concern we will end the Q&A sessions here. If you have any follow up questions, please feel free to email your questions to your Nomura sales representative or corporate access team. So now I will pass back to call to Kapil. Kapil over to you.

Vivek Vikram Singh: Actually, I am okay with more questions by the way. I know some of you have to go and attend some other earnings call perhaps but I am okay. We are here. It is only five. It is not that we are going home.

Kapil Singh: Okay, sure. Gigi do we have any more questions in the queue?

Moderator: Earlier we had a question from Afin, but I think Afin just dropped off. Let me see if he is still around.

Kapil Singh: Ok, anybody else.

Moderator: I think Afin dropped off just now. So for those who had raised your question, who had pressed your raise hand function if you have any follow up please

just raise it again, so I know you have a follow up question. We have got a new raise hand from Deepak. Deepak over to you.

Deepak Yadav: Hello, can you hear me?

Vivek Vikram Singh: Yes, Deepak

Deepak Yadav: Congratulations for a good set of numbers. I have two questions. The first is, I believe you were looking for some acquisition opportunities for a compatible sensor based company, if I am correct. So, how far are we in this endeavor or process and what products in your portfolio, I believe in the white region would have synergies if such acquisition will ever take place? Is it your controller or invertors or next generation motors we are working for?

The second one is we are seeing kind of boom in electric two wheelers segment in India. Recently I was in my village where my grandfather, he bought EV like electric scooters so it was quite nice. So what Sona Comstar is basically doing to proactively capture this opportunity. Thank you!

Vivek Vikram Singh: Thank you for those interesting questions, Deepak. So first one I will take, all M&As are binary till a deal is done, nothing is done, once we do and if we do, we will of course inform everyone. You have very astutely already observed that the right inverter and the controller we control using inversion, so that is why it is an inverter. Basically anything. What is the sensor capability we are looking to add or we are looking to develop that capability is around the software end. We will not enter the chip or the hardware control of it. It will be, how do we get software to control these electronic sensors to perform a function that makes vehicles better for their consumer. That is the objective here. So yeah, the capability alignment will be more towards software driven products.

Second and very interesting one. And thank you for sharing. I have also always believed that our rural India has a great potential for electric vehicles for one of the biggest reasons obviously electricity being subsidized when your TCO goes down dramatically. What we are doing as ourselves we cannot do much because you have to understand that we are B2B2C, so we cannot solve end consumer problems directly. However, we are working with a lot of our customers on electric tractors, electric 2-wheelers and 3-wheelers, which can be used for both passengers and goods carrying for rural India and I genuinely believe rural India has a humongous untapped potential for electric vehicle. I mean just think of electric tractors because you are not going too far from home range anxiety is not an issue. The TCO is phenomenal here. What it does to reduce pollution etcetera is just a byproduct, just economically, it makes so much sense. So we are working with a couple of our customers on electric tractor products and I think it is quite exciting and hopefully all my best wishes to your father and hope there are many more who purchase this. I think the problem currently with vehicles are they are not made for rural roads. I think you need a much wider tread of the wheel, you need better suspensions to take those uneven roads,

etcetera. But it will get that there, there is a great market opportunity waiting to be found.

Deepak Yadav: If I can add a small question. So recently there was a company, I would not take a name. They acquired an electric tractor manufacturing startup. Right? So can I say that in future, Sona Comstar can use their expertise to go into this end product or they are only focused on supplying motors or other mission critical parts?

Vivek Vikram Singh: So Deepak that I will clarify, I know who you are talking about. We will work with such people and supply them the parts they need, we are never going to invest in or buy a vehicle maker, because that is not our business and it provides a direct conflict of interest. We can be in the best intention that whatever we do, but our actions must be above reproach, if we want to be the leaders in our field. So there should not be an iota of a doubt in my customers mind that whatever product that we codesign or we designed for them, I am going to use for something else because of a vested financial interest in owning a vehicle company. So that that day we will not let arise, we will help all our OEM customers develop the best products they possibly can but no we will not go and make vehicles.

Deepak Yadav: Thanks and that answers my question. Thank you very much.

Moderator: Thank you very much. So Vivek just want to know if you are okay on time, would you like to take one more question?

Vivek Vikram Singh: 100% and actually Kapil has not even asked me a question, which is usually used to be the first question so I have to at least answer his question.

Moderator: Okay, so we have Sunil next, Sunil your line is open. Please proceed.

Sunil Bhojwani: Hi Vivek and team, thank you and congratulations for the great numbers. So I have two questions. One would be pertaining to China and Europe. What difficulties are you seeing in your plants in China and Europe? And is there any margin dilution happening because of higher input costs like power and other things due to China and Europe and on the overall consolidated basis. What capacity utilization are we at? I will ask my second one later.

Vivek Vikram Singh: Sure. So capacity utilization is because we have multiple products and multiple processes. Quite a tough one. So what I try to do is give you product. I think gears we're running at about 70 odd percent because we just added a lot of capacity. That is why the fixed asset turnover also you would have seen gone down because we just had a lot of capacity; differential assemblies, etc. I think we are running about 80-85% and starter motors about at about, I would say 45%, traction motors around 35-40% like Sat said. So these are the broad things.

We do not have a plant in Europe actually, we only have warehouses. So, I know what you mean by the increase in input prices, etc., but since we do not manufacture there, it is not consequential. Our China plant is also not very very big. So of course there are challenges, there were challenges in

the last quarter, but this quarter has been relatively smooth. But Sat, anything you want to add on our China plant?

Sat Mohan Gupta: No Vivek, I think you covered it very well. Right now we are not seeing a big change in our forecast in the numbers.

Sunil Bhojwani: So any lockdowns or anything else is not really hampering the plant in China, okay. And my second question was with pertaining to the customers and also due to the high growth in the BEV and EV segment, is there any cannibalization possible? And do you have a lot of overlapping customers? Because what I see is you have close to 37 customers in the Nov EV and about 19 odd customers in the EV segment, so is there a lot of cannibalization which could kind of take the growth away?

Vivek Vikram Singh: Not that much actually. So if we can, I think I know you're talking about the order book slide right?

Not much because if you look at it, passenger vehicle, everyone has an EV variant and usually we are there, so that is where cannibalization can happen. Off highway and commercial vehicle there isn't much two wheelers we were not in and three wheelers, two wheelers are added only recently after we made the traction motor. It is not really cannibalization and I think I mentioned this trend when I spoke in my opening remarks that for the gear guys, we are actually moving up. We have already done so for two customers like I said, hopefully we will do it for one more instead of cannibalization, it is actually value addition is increasing for us. So that is what is happening for us so far.

Sunil Bhojwani: Okay. That helps, if I could just add on one thing. How do you forecast the next few quarters on overall basis. I know you do not give out any guidance or numbers but a little view of yours, and your management.

Vivek Vikram Singh: I mean it should be good and strong, you know our track record, it should continue to be good. We just do not know how the macros would be, because what is harder to estimate is, you know, the base that you have already, you know which new order books, how much you land, but what happens to the base you have not had, does that shrink? And if yes, by how much, I mean in just the last three years we have seen the industry go from 96 million vehicles producing industry to 72 million. So that is the variable that we do not know but yeah, growth should be there and it should be robust in the near term, in the medium term, hopefully also in the long term, but at least we can answer till the near term and medium term.

Sunil Bhojwani: Okay, great, thank you so much. Thank you. That was it from my side.

Moderator: Thank you Sunil for your question and thank you Sir Vivek. Thank you. Just a kind reminder for clients online if you have any further questions, please feel free to use the raise hand function we will help you to unmute your line. Alternatively, do submit your question to us through the Q&A box, we still

have a short time left before we conclude the call. So do take the last opportunity to ask any questions you may have.

Moderator: Hi so Vivek, seems we do not have any follow up questions as of now, would you like to end the call slightly earlier with the closing remarks.

Vivek Vikram Singh: Sure, unless Kapil wants to add anything, we must take our host's permission before ending things.

Kapil Singh: No, I will hand it back to you Vivek for any closing remarks. Thank you so much.

Vivek Vikram Singh: Nothing, as always thank you to all of you who attended and gave us your valuable time. I know there are many things you would maybe rather be doing on a Friday evening but your questions help us understand our business also better. We do not look at it the exact same way the outside world looks at it. So it makes us better. Learning is iterative and we hope to continue learning and continue to do better in the future. So thank you and see you again next quarter.

Kapil Singh: Thank you very much everyone for attending the call and I thank the entire management team of Sona Comstar for taking out time as usual. Thank you.

Vivek Vikram Singh: Thank You

Moderator: Thank you everyone. Thank you again for your time. Happy Diwali and now you may drop off the line. Thank you.

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