Eicher Motors Investor Conference Call Transcript Second Quarter FY 2017

Friday, 28th October 2016

Operator: Good day everyone and welcome to the Second Quarter FY 2017 Results Conference Call for Eicher Motors. Today's call is been recorded. At this time for opening remarks, I would like to turn the conference over to your moderator today, Mr. Arvind Sharma. Please go ahead.

Arvind Sharma: Hi. Thank you, Julian. Hello everyone. On behalf of Citi, I welcome you all to the 2Q FY 2017 Conference Call for Eicher Motors. From the management today we have with us Mr. Siddhartha Lal, Managing Director and CEO; and Mr. Lalit Malik, CFO. I will now hand over the call to Mr. Lal and Mr. Malik for opening remarks, post which we will start the Q&A session. Over to you, sirs.

Siddhartha Lal: Good morning. Good afternoon everyone. This is Siddhartha Lal here and thank you very much for joining us today for Eicher Motors Limited FY 2016-2017 Second Quarter Results. I will start with an update on EML's consolidated financial performance for Q2. Eicher Motors Limited has reported once again its best-ever total income from operations at 1,981 crores, which is a growth of 35% over last year. We've reported our highest-ever EBITDA at 542 crores which is a growth of 55% over last year. And as a result, our EBITDA margin has crossed 30%, is at 30.9%, as against 27% same quarter last year. And all of this resulted in the profit after tax of 413 crores, which is a growth of 45% over last year.

Moving on to the financial performance of VE Commercial Vehicles Limited, our joint venture with Volvo. For the same period which is Q2, 2016-2017, period ending 30th September, 2016. VECV reported a total income from operations at 1,972 crores which is a growth of 10.6% and EBITDA of 143 crores, which is around flat from last year, and then EBITDA margin of 7.2% as opposed to 8% same quarter last year. The profit after tax is 66 crores compared to 68 crores last year.

Moving on to business update on Royal Enfield Motorcycle segment, we sold nearly 167,000, so that's 1,67,000 motorcycles in Q2, which is a growth of 31% over the last year. We continued to have a very strong order book in Royal Enfield and are taking in much more orders than say even last quarter. In India, Royal Enfield continues to increase its retail footprint at a rapid pace and as available we've just crossed the 600 dealerships number last quarter and are at 605 dealerships now, as of September 2016. As part of our growth strategy in the mid-sized motorcycles globally, Royal Enfield has recently in the last quarter unveiled flagship store in Milwaukee in North America. This is our first standalone store in North America. We have also added two exclusive Royal Enfield stores in Spain, one in Barcelona and one in Valencia.

In other news, on accessories we had a collaboration with Happy Socks which is a leading Swedish brand which is where we launched a limited edition of apparel and accessories for men. That includes motorcycling jacket, sweatshirts, t-shirt, helmets, socks of course, and boxer briefs. So in addition to selling all of these through our Royal

Enfield Gear stores across India, we'll also be selling and displaying the limited edition motorcycle that we created as well as all the merchandise in Happy Socks exclusive stores across the world and in cities like London, Stockholm, Copenhagen and Mumbai. That expands our brand resources to different audiences and different markets.

We have many key projects which are going on, on the infrastructure site. We have two technology centers which are progressing very well. The one in UK is in advanced stage of completion and we will be moving in this financial year, so that in the next quarter which shall be, we should be actually getting into the premises which is in Bruntingthorpe, near Leicester, in Leicestershire in UK. We will soon be commencing work on our Chennai Technical Centre which will be operational by the end of next financial year so that by March of 2018, in that quarter that we have just had a groundbreaking ceremony on a third plant in Chennai which is called Vallam Vadagal, and so that will also be completed by the end of Q2 next year, so that in September timeframe, that's nine months from now.

In addition to that an update on Himalayan which is Royal Enfield's first adventure-tourer. And this has been extreme – received extremely well by our customers in India and it's been, while it is paving the way for accessible adventure touring segment in India which is – and we have a very strong positioning in people’s minds today as a very capable adventure-tourer the Himalayan and as well as the good all round motorcycle for daily use. So that's been established really well. We’re on track to our with volume progression, with expanding into all the dealerships in the country and we're considering, we're getting good growth in Himalayan. As part of our in addition to India, Royal Enfield has also launched the Himalayan in its natural habitat of Nepal last month, and we've also showcased the Himalayan as the Gaikindo Indonesia International auto show in August of 2016 which starts taking the Himalayan to other markets across the world. Our near-term basis, outlook for Royal Enfield remained extremely strong and we continue to work towards our expanding our position and growing our position profitably towards being the leading player in the mid-sized motorcycle segment globally.

Moving on to business performance and sales performance for our joint venture with Volvo which is VE Commercial Vehicles Limited. The industry declined by 7% last quarter, whereas Eicher grew by 15% last quarter – I was talking about 50 tonnes and above commercial vehicle segment, giving us a market share increase from 11% to 13.6% that was very robust market share growth in the quarter. That's 2.6% over 11% that we had last year. 2.6 additional, so it's a very strong market share growth.

Even in – and right now I'm talking about 5% above, but even in the segment below where we have just very recently entered, that is a 4.9 Truck the Eicher 1049, we were exceptional performance. Eicher sold 513 units in the last quarter versus – and the industry was 2409 units. As a result we have a market share of 21.3% in a market that we've just entered. It thus shows the exceptional brand that Eicher enjoys in the light and medium duty segments where in the market we've just entered we have now got over 20% market share immediately.

In segment performance in light and medium duty trucks, we maintained our sales from the same quarter last year whereas the market grew by maybe 3%, so there's a slight reduction in market share to 32.3% from 33.2% last year. Maybe due to the fact we had a strong growth in market share from 3.2 to 5%. We grew by 21%. The industry dropped by 21%. In buses, the industry grew by 8%. Eicher grew by 48%, making the market share grow 11 to 15%. In exports, we grew at 5%. The industry grew at 27% last quarter. And in Volvo trucks, we declined by 25% to 259 units, largely as a result of the coal mining segment shrinking of the trucks, and the coal mining segment shrinking in the last quarter. Our medium duty engine sales volumes, which are the engines that we sell to Volvo Group globally for their Euro-6 base engine requirements. We crossed 6,000 units for the first time and had a growth of 26%, so we're pacing at over 2,000 units per month which is a good growth now for us. and good volumes in the Euro-6 base engines.

Moving on to a joint venture with Polaris, we continue to expand our retail presence. We have presence now across eight states and in around 60 locations. We had – we continue to expand our sales, expand our footprint in the Polaris – in the Multix product which is India's first 3in1 personal utility vehicle. So yeah, that's the news from us last quarter.

We've had as we said a very good quarter once again, best-ever quarter for Eicher Motors both at the top line and bottom line level. And we're open for questions, now.

Operator: Thank you. If you would like to ask a question please press * followed by the number 1 on your telephone. Again please press *1 to ask a question. We will now take our first question from Raghunandan[?] from Quant Capital. Please go ahead.

Raghunandan: Hello. Good morning. Congratulations on a wonderful result and –

Siddhartha Lal: Can you keep your phone away from the mike because I think that's what –

Raghunandan: Congratulations on a very good set of results and season's greetings to you. Sir, my question was on the results part. Other expenses seem to be high this quarter. So was there any one-off items there which led to that increase?

Siddhartha Lal: So generally it is in trend with the – I think it is in trend with the growth of the business of course we got a – we got some. We got good news on the material cost [inaudible] where the [inaudible] cost is at a all-time low. Some of the other expenses [inaudible], but it's only one time. If you're going to call it one-tenth of the quarter will be some of the marketing and the promotion expenses which is for the Himalayan motorcycle, so that can be classified as one-off.

Raghunandan: Understood, sir. On the waiting period for the Royal Enfield, how is it currently, sir? I mean I heard the initial comments and the press release which says that last quarter the new order bookings were higher than that of the dispatches, but how is the waiting period? Is it still anywhere between one to two months?

Siddhartha Lal: So for Classic, it's more than that at a gross company level I'm taking about. It's close to the three months like it was the same time last quarter as well. But for some of the other models, it could well be between 30 and 45 days.

Raghunandan: Understood sir. And on the VECV side, can you – would it be possible to share the engine realisations and also the current touch points for the – on the CV side?

Siddhartha Lal: Current touch points are about 280-285. But the engine realisation, no, we don't break out product level or component level pricing at all. It's a single segment reporting that we do, so we don't break that out.

Raghunandan: Fair point, sir. Thank you sir, thank you very much.

Operator: We will now take our next question from Ashish Nigam from Axis Capital. Please go ahead.

Ashish Nigam: Hi Siddhartha and Lalit, congrats on a very good set of numbers. Just a couple of questions on both on Royal Enfield. So if you can just walk us through your capacity ramp-up again in Royal Enfield. I believe you are looking at an exit capacity when we spoke last of around 720,000 by end of FY 2017. So is that any change to that, and also the ramp-up towards 900,000 you know, how does that really play out?

Siddhartha Lal: Yeah so, actually the monthly level we are closing on in a bit around 60,000 a month now. I know that is that's already at the 720 level. We will be maintaining approximately this number of 60,000 a month. We might, can be marginally up and down and trying to improve some productivity. But from a capacity standpoint this is going to be at around 60,000 a month till our next plant such so our Vallam Vadagal Phase I gets into production, that's in Q2 of next financial year. So we will be approximately maintaining this number till that time, so it's stabilising our volume, stabilising our processes, our supplier base of it's all of that in the coming two quarters or two and a half quarters with the view to also then start working towards the ramp-up when Vallam Vadagal Phase I comes in. Vallam Vadagal Phase I along with Oragadam Phase I and II along with Thiruvottiyur all put together will give us delivered capacity of which we will be able to deliver 900,000 units in the year 2018-2019, so that continues to be our outlook for the coming period in capacity.

Ashish Nigam: Okay, so just with Phase I of the new plant it will go to 900,000?

Siddhartha Lal: Yeah, Phase I of new plant plus, Oragadam and others – but they're all very interrelated because you would have [inaudible] from one place, [inaudible] from another, tanks from another and basically if it all works, all our three plants work together as one delivery unit as opposed to… no segregation between the plants as such. We jointly use them to deliver this capacity.

Ashish Nigam: Okay that's helpful. Okay secondly, if you can just talk about the changes in the profile of the Royal Enfield buyer and also how the spares and accessory business is trending?

Siddhartha Lal: So the Royal Enfield buyers coming recently more in line with the motorcycle buyer, but of course, is generally a step-up to us in affluence. But in terms of age, it has been trending down. In terms of first time buyer of a motorcycle has been increasing for us which is all positive as far as we're concerned. We of course have still the majority of people gearing up from commuter or 150 cc motorcycles, but it is – our buyers are still like buying us for leisure purpose and weekend and long distance ride. Over 90% of our users are still using on a daily basis as well for everyday motorcycling. Accepting that they're still a young nascent business, it's growing very well for us, but it's still a small in the larger scheme of things. Spare parts is growing rapidly. It's now facing similar or – as in growth, as our motorcycle side because the population has also been increasing over the last few years. So we're getting good and we've actually improved our entire spare parts delivery and warehousing and all of that, so that's really helped us in delivering better spare parts for our customers and through our dealer. So numbers of spare parts we breakout only at the year-end our annual report.

Ashish Nigam: Yeah that's fair. That's fine. That's very helpful. Thanks. Thank you and all the best.

Operator: We'll now take our next question from Kapil Singh from Nomura. Please go ahead.

Kapil Singh: Hello.

Siddhartha Lal: Yeah Kapil, go ahead.

Kapil Singh: Hi sir. Sir, my first question is, could you give us a sense of growth in order inflows, like September quarter how much would it be on a year-on-year basis?

Siddhartha Lal: Kapil, we don't talk about the order book, order inflows and all the stuff. All I can say is that, like I have told you 40 times, it's month-on-month. It's higher then the previous month. And that clearly is going to happen in October as well.

Kapil Singh: Okay. Okay, secondly on the emission cost, if you can give us some colour like what kind of emission and safety-related costs are expected? And would you expect those to be – when do you expect those to be passed on?

Siddhartha Lal: So the change in the material cost have – when the new products are out, I think that's a good time to speak about it. We're still a few month away.

Kapil Singh: Okay. But I believe you would start launching them in the Jan to March quarter itself, right?

Siddhartha Lal: In Q4, of course, yeah, in Q4, we'll have to launch it because you have to be compliant as on 1st April 2017.

Kapil Singh: Okay and on the material cost side, what was the price hike and did we see a further decline in the material cost this quarter?

Siddhartha Lal: Yes, we saw further declines on a – for sure on a year-over-year basis, but also on a quarter-over-quarter basis. Price hike, we took one price hike at the middle of August so not a large part of that is visible on the P&L because it is fully referred in half the quarter. But on the material cost, we continue to expect [INAUDIBLE].

Kapil Singh: And it's largely stable, going ahead?

Siddhartha Lal: Well, I hope it is not stable because we do plan to extract as much as we possibly can.

On the outlook perspective, some of the commodities might just go up a little bit, but that's on a outlook side. Nothing has happened as of this point in time given the commodities that we use.

Kapil Singh: Okay and the last question –

Siddhartha Lal: But we have old aluminium's and steel. Yeah, go ahead.

Kapil Singh: On the revenue, there's a minor difference between standalone and consol, I mean consol is slightly lower than standalone. So just wondering why that may be happening?

Siddhartha Lal: So basically the performance is basically EML standalone plus our market country operations in North America, plus Brazil technically, but Brazil is not even started in operation. So when knock out the inter-company sales and stock that's where the numbers tend to fall down because if the North American company is not able to sell all its stock that we have sold, then the number will be correspondingly lower.

Kapil Singh: Got it. Okay thanks a lot, sir. That will be all from my side and wish you all a very happy Diwali.

Siddhartha Lal: Thank you and same to you.

Operator: Okay our next question from Pramod Kumar from Goldman Sachs. Please go ahead.

Pramod Kumar: Yeah thanks a lot for the opportunity and congratulations on a good set of number. Lalit, you have – or rather Siddhartha, you mentioned that Classic 350, the wait list remains three month same as last quarter and dispatches have been growing at a fairly robust pace for the Classic 350. So does that imply that the order intakes of Classic 350 remains fairly robust because you don't want to quantify the order book growth rate. But just is that a fair reading given that the waiting period haven't shrunken with capacities increasing between the quarter? Is that fair assumption that even now for Classic 350 continuing to see strong order inflows?

Lalit Malik: Yes absolutely, and it's continuing to in fact despite being by long shot the largest, the biggest model in our range. It's continuing to increase even as a percentage within our range so the order intake is very strong. The and it's the Classic 350 which is growing faster than any other model in our range, even now.

Pramod Kumar: And going by the historical what do you say calls and in terms of the order book size, I'm just trying take a – trying to gauge the order book size. Because if I'm not wrong, I think the order book in absolute terms has not only keep inching up, probably it has expanded considerably. So I'm just wondering is the three-month wait list a bit conservative on the average company side? I'm just trying to – because the way the numbers have shaped up or your commentary shaped up looks like the wait list is well in excess of three months.

Siddhartha Lal: So you know what I'm saying is that in the overall country level, but very honestly there will be pockets in the country sales where it will be more than three months. But there will be some pockets in the country which you know very old stores, very old establishments over there where there would be slightly less than three months because there will be slightly more stable in that sense.

Pramod Kumar: That leads me to my next question, Lalit, that in the major markets like say Bombay, Bangalore, Pune, Delhi NCR market. How's the growth rate there because those are markets where you already have probably market share higher than the premium bike manufacturers? So how is the growth rate on the same store – not on a same store basis, on a same city basis?

Lalit Malik: Well I think same city basis, and this was the same store. It's not exactly the same so you're right, because in some of the places we may have added stores and all that. But generally speaking in all the top 20 markets, top 20 cities, markets in the country we – year-over-year we're 15% plus.

Pramod Kumar: 15, that's excellent. And thanks a lot for that and my second question is related to VECV. Siddhartha, given the way we look at the share of profits on that, business it has come down during the quarter. There has been some bit of operating deleverage, but I think looks like margins have taken a bit of a hit. So if you can throw more colour, is it got to do with the mix in terms of higher HD sales. Is that related to that or the discounting intensity has stepped up in the HGV market?

Lalit Malik: Yeah most of those, most of the above which is its still nascent in our product range, and we certainly not pulling it as much margin as like a medium [inaudible]. So, and that has increased as a percentage of – so the product mix factor is of course there. Also we've entered new segment in 2.9 tonne. So all of that there is some product mix going on there. On the other hand of course, on heavy duty in particular there is a continued that is nascent enormous discounting going on by the market leaders, and that puts us in the spot. So even though we've been gaining, and in fact it's because we were gaining without that the – that at the discounting level, it's so super high, with the old view of fighting you know as last resort with price, which is what big competitors do perhaps in the future they might have more profitability concerns from their board. So maybe they'll also start working towards profitable growth like we do, but till then there is a price war in the market and we have to participate in it.

Pramod Kumar: And the last question on the –

Lalit Malik: And this is –

Pramod Kumar: Yeah Lalit.

Lalit Malik: So just on Q-on-Q front, the Volvo trucks was higher in Q2 as opposed to Q1 so that also leads to a just in the profit.

Pramod Kumar: Right, and finally on the industry side on head CVs in particular September was a weak quarter for the investing given the high base. But how is demand shaping up in this month on the industry basis. I'm not looking for specifics, but generally is the demand kind of coming back or are we still in a weak patch?

Lalit Malik: Industry is, we expected, I mean, there was a large decline on the last quarter. So we expect and believe that it should not, certainly not decline by those numbers, but still uncertain whether it will start growing again as we'd hope. So we're still – the jury is out on that. But it will certainly not be the depth that we had in the last quarter, the large dip in the industry.

Pramod Kumar: Thanks a lot guys. Take care. Thanks a lot.

Operator: We will now take our next question from Pulkit Singhal from Motilal Oswal Asset Management. Please go ahead.

Pulkit Singhal: Yeah. Hi, this is Pulkit. Firstly, wish you a very happy Diwali Siddhartha and Lalit, and congrats on a great set of numbers. Just a couple of questions firstly on Royal Enfield. How do you decide on the price hike decision? I mean, we have raw material prices coming down and you also have price hikes happening. And I'm just wondering how do you take care of the fact that you don't price yourself out of the market compared to the next 150 cc bike below you? So how is the pricing decision taken?

Lalit Malik: We have a very sophisticated model on pricing and how we look at it. We certainly consider competitive motorcycle. We consider our source of growth in terms of where our customers are coming from. We map over the years, we map as a percentage on all of these including our models, as one data point we map costs on a different data point. And with all of that, we are able to like fully gauge how much we are doing so essentially at the end of all of this, we've actually increased I would say only by 1% this year. It's not a substantial increase. Most of us EBITDA growth from 27% to nearly 31%. Obviously, nearly all of it is actually comes from operating leverage because given the price increase is not really – it's given only partway through the quarter. So we are very cognisant of that. We are certainly not in any form or manner we believe [inaudible] the market in any sort. We are making sure that we maintain a very strong price positioning for our products, which is evident and which continues to be evident.

Pulkit Singhal: Yeah. One of the concerns is that at least what I get from some of the dealers that I've spoken to is that it is really the Classic that has picked up or the 350, but the other bikes are not selling as much. And the other point they say is that the management focus is also not as much on say is trying to sell a Thunderbird, etc. Now this is the feedback I'm getting from the ground. So what is the management doing to try to push some of the other brands? I mean Himalayan is new so that's fine. But what about say Thunderbird and what the – kind of how do you look at it from the next two years in terms of getting a new brand? I mean how do you want to position it? Will it be an entry level or an upgrade level? How you're looking at it?

Lalit Malik: So the Classic, as you know what happens is that there is some products or brands or get into a virtuous cycle. So today Classic is in that position where it has, where there is very good visibility of the Classic in the market. There is a very good resale value of the Classic even better than of our other motorcycle. So all of our motorcycles have a good resale value, but Classic is even better. So customers think of it as a nearly as a very safe investment thing. Today when they're buying a Classic and from the margin what happens is that some of our customers who are contemplating other brands such as let's say Electra or Thunderbird are because the waiting period of Classic has come down now to let's say two or three months maybe four in some cases. But the waiting period has come down.

They're willing to wait for a Classic now. So that's why the market is shifting even a bit more towards Classic. We are doing a lot of work on all of our other models. In fact, what goes really unnoticed is that 500 CC range which is our Bullet 500, our Classic 500, our Thunderbird 500 and our Continental GT put together are in the order of over 5,000 a month in the Indian market. Now think about it so the 500 cc range as a franchise of 60,000 units a year, which in itself has a standalone business if it were really it's a strong business proposition. It's a very valuable business that we have in our 500 CC. So we of course understand that. We work on improving it and we're doing many things in currently and in our future organisation or within our future product plan. But also in our dealership experience so there's a lot of work going on the right selling products.

So when a customer comes in it's not just basis looks or belief, but actually basis the usage pattern. So we're selling so there's a lot of changes happening in our distribution network also to support other models, but actually it is not the issue. The positive issue really is that the Classic has such a strong pull right now that everyone is sort of riding that wave and moving on to that bandwagon. It does sometimes affect some of our other models, but and we're doing a lot to keep them up. But at the end, we’re not overly worried about that as long as some products, you know as long as it's within our portfolio that people are moving.

Pulkit Singhal: So therefore it would be fair to assume that your future launches would be trying to answer what next after Classic because you already have a strong entry level Royal Enfield positioning with Classic and Bullet?

Siddhartha Lal: Yeah certainly, I mean there is, Himalayan the outcome of that is exceedingly different from Classic. It doesn't get more different at least from our product portfolio standpoint and it's starting to build a very strong reputation in the adventure segment. People are really enjoying the benefit of the specific aspects of adventure touring that we've been able to bring in. So yeah, we're certainly going to do certainly do more of that in the future which is open out new sectors.

Pulkit Singhal: Good. So I mean I have always believed that may be say motorcycle growth will also impact the kind of demand for Enfield and how is your assessment of the impact of this festive season? I mean are you, do you see because I mean what we're reading from the other competitors is that rural has not been as strong. But most of the growth say 11 to 12% growth in motorcycles year-to-date has probably largely been from the urban side or the town side etc. where I would think that Enfield is well present. So do you see a festive cheer happening on the Enfield side as well or is it just that the three month the waiting period itself just pushes people off because they want a bike sooner than later?

Siddhartha Lal: You're quite right. I mean there is the capacity constraint, so we don't get that, we can't get that immediate bump-up in sales because of capacity because we're anyway limited bike as well because of the festive because we're already limited by capacity. And to some extent there is a market that we miss out on which is people who want immediate delivery, like I said, whether it's for festive period you know people wanted new motorcycle for Diwali or for other occasions whether it's for marriage season where people want a new motorcycle immediately to gift or something like that. So we do miss out on some of those and over time as the capacity increases and our waiting comes down, it should on the one point for that market it should certainly help us.

Pulkit Singhal: Good. I'd just like to share an anecdote that one of the dealer said in UP that even though the guys are not able to get a Classic bikes. He actually lend his showroom bikes to those guys so that they can use it during the marriage day. So it's still building a brand in that market. Nevertheless my last question on the raw material side. I mean we've seen a commendable increase in gross margins. I mean so it does every single quarter keep surprising on the upside. So I'm just trying to understand how much is this is just raw material price decline versus what the management can do because of higher volumes? I mean one of the competitors did say that there's a one quarter lag in raw material prices and therefore next quarter would be a higher raw material price. Is that something we should expect with you and also over a longer term is there more scope for as you double the volumes to kind of get more leveraged?

Lalit Malik: So look, the raw material costs are clearly concluded after the quarter is through because that's when we know what are the level [inaudible]. So clearly there will be lag which mean what we will report and what actually what will happen to that quarter in all. So what you should expect from us really you know that's going to the future and now let's wait for the next quarter and next subsequent quarters to know as to how the raw material price have changed and how do we react to it. Clearly, we are getting the benefits and we have been getting for a while now. Clearly, we have been getting the benefits of the volume entries which also means ability to rationalise the vendors much better than we're more able to done it in the past. So on both the levels; we continue to extract some reasonable amount of benefits. You know to let up on that it's a continuous exercise. It should happen every month.

Operator: Thank you. Again as a reminder to all participants please limit yourselves to two questions. We will now take our next question from Sonal Gupta from UBS Securities. Please go ahead.

Sonal Gupta: Hi, good evening. Thanks for taking my question. So just on the capacity side, so first is the Vallam Vadagal would be what 300,000 units?

Lalit Malik: Sonal like Siddhartha just said a while ago the peak capacity of the present plan to do Phase I of Vallam and all the rest as the company is deliverable capacity of 900,000. Now how much each plant does it's a very competitive thing therefore.

Sonal Gupta: Right. I was just –

Lalit Malik: Also said that –

Sonal Gupta: Hello.

Lalit Malik: I mean to say and not withstanding that what happens is each phase of Oragadam is was 25,000 or 30,000. But like the benefit is deeply integrated with the rest of the supply chain or in general of plating, trains, [inaudible] as in different places. So all of that is the combined capacity, but yeah, it will be in the order of 25 to 30,000 for Vallam Phase I as well.

Sonal Gupta: Okay, and just on coming back to the question on top 20 cities what portion of your demand in first half would have come from top 20?

Lalit Malik: A lot, but I don't have a number off-hand. Sorry about that. But a very, very sizeable portion.

Sonal Gupta: So it still be around 50% or?

Lalit Malik: I don't have a number, but it's probably much more than 50% of the top 20 cities. So basically means out almost I'm saying almost one-third of our network distribution. Yeah maybe so some cities are even 13 dealers, 15 dealers. I mean, the top few cities. So top 20 would be – has been 200 plus dealers. I'm sorry I don't have numbers with this, but yeah, it's a very large number of our sales.

Sonal Gupta: Okay. And do you have any sense then in terms of what is the market share in the premium segment in these top 20 markets? I mean top 20 cities or however you look at it?

Lalit Malik: What is premium market? And how do you define it?

Sonal Gupta: I mean like whichever way you would – I mean you'd – I think above Rs 75,000 or whatever above 150 cc and above or whichever way I mean.

Lalit Malik: If you see 150 cc and above, we're on, we're over 20% market share. If you see overall motorcycle we're above to 5% market share down. So 150 cc and above we're over 20%. Our market share in some cities is 30-35% as well in – yeah.

Sonal Gupta: No, so I understand that you're above 20 over in the 150 cc plus segment. But I was just saying that in top 20 would your share be like 40% or something of that sort? I mean just to get a sense of there how high is it, can it go because that's obviously the main chunk of your I mean catchment as of now?

Lalit Malik: It's really difficult to – I don't have numbers so I can't answer you directly. I don't know if it's 28 or 27 or 30s. I don't have a number so I don't want to just guess and say what it is because I don't even honestly have a list of our top 20 right on front of me and what the market shares are. So I don't have it directly, but it is fair to see that clearly in bigger cities, we have a bigger share. And in richer city and states we have a better share. So in states like Kerala, our market share is extremely high. So our market share in motorcycle is probably 20 plus per cent in Kerala right? Above 20% in motorcycle so in premium it will be much higher. Our share in Punjab is very high still in terms of premium motorcycle market and in big city. So basically in a nutshell in the richer parts of the country we have a higher market share. It's as simple as that.

Sonal Gupta: Okay, great. Thanks for answering my question. Thank you.

Operator: We will now take our next question from Chirag Shah from Edelweiss. Please go ahead.

Chirag Shah: Yeah thanks for opportunity and congrats for the set of numbers Siddhartha and Lalit. As question in capacity just sorry for coming back to that. So we are anywhere 50,000 per month and you're saying by end of FY 2019, you would be at around 75,000 a month. So is this a right understanding the way we look at it? Then it means that given the growth opportunity and economic cycle, we are where we are, the demand cycle in the economy. You would be missing out on a lot of opportunities. Is it the right understanding because if I divide 900 by 12 you get 75 per month volumes? And over in that there would be export business which would now hopefully would start coming in given the efforts of last two years?

Lalit Malik: We think that that's our current outlook, Chirag. So if you see upside we have a, obviously, we can [inaudible]. But right now this is the trajectory that you're seeing in terms of the Indian market and it's still, I mean, you're right exports should kick in. But to be fair exports is or let's say significant exports is probably just beyond that horizon. So we don't know how exports will pan out right now. We just believe that the work that we've been putting in the last couple of years in the next couple of years, we should start seeing solid traction in the medium term. Not withstanding exports, we do certainly have current outlook. But we're a pragmatic bunch of guys so if we find that demand continues to grow at the pace that it is and we'd certainly work on it and I'd leave that to certain capacity it's not that long. We can certainly expand on that, but this is really what we're working towards at this point.

Chirag Shah: So this is more of your capacity can be expanded if the demand keeps on going up. So that's the way to understand the capacity outlook that you're sharing?

Lalit Malik: Yeah, I mean this is our current outlook for what capacity we will like to build then what we will be able to effectively use in the year 2018-2019 which is our current outlook. If our outlook changes if we do a planning then we will work towards updating that so that is which of course affects us our entire supply chain, so, yes.

Chirag Shah: Fair point. The second question was on other expenses. And now if I look since last 12-14 quarters are other expense as a percentage of sales for Royal Enfield I'm talking is around 10-11%. So in a sense the operating leverage benefit which is actually filtering in, in the gross margin, failed to appear in this other expense line item, and that is a concern. Can you shed some light at what inflection point we can see this number going down?

Lalit Malik: So there are future outlook will be decided by the future. As of now between this on the fixed cost, so with other expenses unfortunately, half of that is fixed and half of that is variable. So don't please treat other expenses as all fixed. But the way whatever SEBI has formatted the whole thing out, that's the way it is, number one.

Chirag Shah: Even is half is been –

Lalit Malik: Number two, sorry I'm just giving you broadly split. It's not all fixed. Between staff cost and the fixed part of all of our Opex as there are Opex. We continue to drive leverage. So if you, if, you know, once in a while one-off that we have and I can say one-off for the quarter that it won't be one-off the year for the level of bike launch expenses. I mean for the next one or two years we do have a bike to be launched every year. Then for the year it's not a one-off. So I think as to – to do all those kind of things also. So there is a leverage that is going back to –

Chirag Shah: Because even if I take 50% as fixed even then there should be some leverage visible in other expenses. Fair point over this. And last if I can squeeze in last question is on product launch outlook, so new launches as well as upgrades of the existing models if you can share some light over next one to two years, how are you looking at?

Siddhartha Lal: So right now, our entire focus of normalisation is on expanding the new Himalayan segment the adventure-tourer segment as the new product. And we're making a lot of headway. It's a very interesting product. It's an absolutely new category which never existed in India. So the fact that – so just getting that into people's mind, getting them interested in the segment, enormous amount of number to be done to grow this into a very strong franchise over the next year, so really all of our efforts are on that.

On new product introduction pipeline, we have product certainly in the pipeline. We will likely have one launched new product next year, next financial year and – but that's you know, these things are until they happen it should have you know we're just working on them. So that's the current outlook. But we certainly you know are planning more new products as we speak, but our focus is on expanding existing products at this point.

Chirag Shah: Fair point. This was really helpful and all the best and wish you a happy Diwali.

Operator: Pardon the interruption. Again as a reminder to all participants, you will have to limit yourself to two questions. If you have further questions you will need to requeue again. We will now take our next question from Binay Singh from Morgan Stanley. Please go ahead.

Binay Singh: Hi Siddhartha. Hi Lalit.

Lalit Malik: So moderator this will be our last question. We have got out of time now. Yeah go ahead Binay.

Binay Singh: Hi. Thanks for the opportunity. Actually just like the third plant that you are ramping up, incrementally threading around 15,000 which is around 180,000 units per annum. So is that the Phase I of that plant because we thought that the Phase I was more like 300,000 units?

Lalit Malik: So the Phase I is indeed on that number. It's about 25k to put as a 1,000 there about per month. It's not 15,000.

Binay Singh: Okay, so those basically when you say 900k, you're basically saying that the Phase I may not be fully ramped up by that time?

Siddhartha Lal: It's a bit more complex than that because when we're talking about capacity right now, 25 or 30,000 per month, that's to do with vehicle assembly and paint capacity. But there might be a some lag in engine capacity, in supply capacity, in train capacity, in tank capacity, in plating capacity which are all capacities that we're building in different parts of either internal manufacturing or external supply chain. So other things have to also catch up. In fact, the module of paint and vehicle is what we're referring to right now, but there are other aspects that we – of the supply chain that we're ramping up. And of course if you're able to ramp those up quicker they will be able to get bigger capacity earlier. But that's only if the need is there, right. So if we see the need for more volume we can certainly increase the pace.

Binay Singh: And sir, like basically because the reason now I guess this question is coming back is from 60 to 75,000 that's around to 12% CAGR growth in capacity right? The industry itself during this time could do high single digit. So what kind of lead time will you have in case you realise that you know actually FY'2019 demand driven by industry growth and your core franchise strength can be strong. So what kind of lead time do you need? Is it six months? Is it one year?

Lalit Malik: So the lead time we put up – actually it's for plant like Vallam the lead time is slightly more because it's a brand new plant. So that for Phase II Oragadam, the lead time was there because interesting infrastructure are available so for Vallam you know they've been – that's on the vehicle and paint side we'll get up and running like Q2 of next year.

On the other aspects, the lead time is probably a shade less, so more in the 9 to 12 month range for other modules with for training or for plating or other aspects. That's the kind of lead time. So we will certainly, I mean these are – which numbers that we're talking to you about from our last year's estimation for three or four years out. They're going to get into a planning sectors and extra month and we'll see if we have any revision in any form or manner on these numbers based on what we foresee is the market demand or maybe – and it's all to do with our view on the market if we have a stronger growth in the market then we should be able to increase our volumes for sure to add capacity volume.

Binay Singh: Right. And sir, just last question on the VECV slightly more on the industry role. We've seen your market share grow in HD. We've seen discounting being pretty aggressive. In fact, when we speak to dealers, they generally point out that Eicher and Tata are the two most aggressive guys in the industry. So do you think this aggression in discounting that we've seen in HD in the last three, four months, is more market share grab or is it more reflective of the fact that the demand has slowed down very sharply?

Lalit Malik: It's to do with – I would certainly say the incumbents worrying about new entrants like us in heavy duty from a market share perspective because it was the same situation the quarter before and the quarter before where actually there was a lot of growth. So it's not to do with the growth or degrowth as such. It's to do with trying to dissuade the new new entrants like us in getting good share. So a lot of the focus of the deep discounting is also on deals where newer players like ourselves and a couple of others are involved. That's where the incumbents are deep discounting and, yeah, it's – but it's really the incumbents that are setting the trend. As you can imagine as a small, as a relatively smaller player, so if you see the behaviour in light and medium duty it's – there's also discounting which is not as crazy as heavy duty because there we like to keep a better price position, and we're one of the absolute leaders there. So the leaders drive the – certainly the behaviour on discounting.

Binay Singh: Great. Thanks a lot.

Operator: I will now hand back to –

Siddhartha Lal: Thank you. And is that all then?

Siddhartha Lal: Arvind, we'd like to close call now, so…

Operator: That will conclude today's conference call. Thank you for your participation. Ladies and gentlemen you may now disconnect.

[END OF TRANSCRIPT]