"Voltas Limited Q2 FY24 Earnings Conference Call"

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MODERATOR: **MR. DEEPAK AGARWAL – PHILLIPCAPITAL (INDIA) PRIVATE LIMITED**

Moderator: Ladies and gentlemen, good day and welcome to the Voltas Limited Q2 FY24 Earnings Conference Call hosted by PhillipCapital (India) Private Limited.

As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Deepak Agarwal from PhillipCapital (India) Private Limited. Thank you, and over to you, Mr. Deepak.

Deepak Agarwal: Thanks. Good afternoon, everyone. On behalf of PhillipCapital (India) Private Limited, I welcome you all to Voltas Limited Q2 FY24 Earning Call.

Today we have with us management represented by Mr. Jitender Pal Verma – Chief Financial officer; Mr Manish Desai – Head Corporate Finance; and Mr. Vaibhav Vora – Manager Corporate Finance.

I would like to thank management for giving us the opportunity to hold this call. Now I would like to hand over the floor to the management for their opening remarks, post which we will open the floor for Q&A. Thanks, and over to you, sir.

Jitender Pal Verma: Hi. Good afternoon. This is Jitender. Thanks to all the participants who have joined for the call. Before we get to the question-answer session, we just wanted to have a few words and explain our results, and then we can go on to the question-answer session.

As we all know, the second quarter of FY24 began with a slow economic recovery across major economies, but amidst sluggish pace. The action taken by the central banks across the globe on tightening of the monetary policy by increasing benchmark interest rate has helped tame the inflation to some degree. However, inflation still remains at higher levels. The key commodity prices have also shown a downswing given the overall supply exceeding the demand. Amid this slow recovery, recent geopolitical events may further cause some disruptions in the near future, and we have to wait to assess its impact on the economy.

In these challenging times, the Indian economy has remained resilient. High frequency indicators of GDP growth, GST collections and PMI point towards sustained economic recovery largely led by the urban diaspora. However, the rural economy is still having muted growth owing to high inflation. Given the lower economic growth in developed countries, recent geopolitical events and strengthening of US dollar index may impact the fiscal budget which will consequently impact the overall economic growth. There are still some positive offshoots in terms of manufacturing focus fueled by production-linked incentive schemes announced across various sectors and signs of receding inflation month-on-month that should support the growth going forward.

In this traditionally tepid second quarter of the financial year both for product and project businesses, Voltas clocked a considerable topline growth in both unitary cooling products and projects business. The financial results for the quarter have however been impacted on account of the provision of Rs. 86 crores due to delayed collection in the overseas business. Consolidated total income for Q2 FY24 was Rs. 2,364 crores as against Rs. 1,833 crores in quarter 2, FY24, growth of 29% year-on-year. The profit before tax and after tax was Rs. 85 crores and Rs. 36 crores, respectively. Earnings per share (face value per share of Rs. 1) (not annualized) for the quarter ended 30 September 2023 was at Rs. 1.11 against a negative EPS of Rs. 0.22 reported last year.

The consolidated total income for the 6 months period ended 30th September 2023 was higher by 25% at Rs. 5,794 crores as compared to Rs. 4,627 crores in the corresponding period last year. Profit before share of profits, loss of joint ventures, associates and tax was at Rs. 352 crores as compared to Rs. 340 crores in the corresponding period last year. Profit before tax was at Rs. 288 crores as compared to Rs. 174 crores last year. Net profit after tax was at Rs. 165 crores as against Rs. 103 crores in the corresponding period last year. Earnings per share not annualised for 6 months ended 30th September '23 was at Rs. 5.02 as compared to Rs. 3.07 last year.

The corporate balance sheet continues to remain healthy with the cash and cash equivalents and minimal borrowings at Rs. 2,590 crores as at the yearend. With the objective of conserving cash for the potential future growth opportunities, the Board in its meeting has approved issuance of listed unsecured non-convertible dentures to the tune of up to Rs. 500 crores for funding the capital expenditure plans.

You have already seen our snapshot of the results.

Segment A: Unitary Cooling Products:

The second quarter of a financial year is usually a lean period for the unitary cooling business through the initial period, but it is also the start of the festive period that continues for a period of two plus months across various parts of the country. The Onam festival in Kerala has witnessed a strong growth in the appliances business after almost three years of muted sales. This has given a hope of higher tertiary sales in the coming festival period across the rest of the country supporting primary billing to the trade partners that is reflected in the overall volume growth of the room air conditioners during this quarter. The focus on the inverter category and promotion of higher energy efficiency products has resulted in a healthy product mix contributing to the overall margins.

Voltas continued its leadership in multi-brand outlets with YTD market share of 19.2% and exited August market share of 19.5% amidst an intensely competitive and fragmented market.

The commercial refrigeration vertical witnessed a muted growth on account of cautious investments by B2B due to lower demand of cold beverages, chocolates, and ice creams.

Nevertheless, the focus on the retail channel and product mix within the category supported the overall volume during the quarter on a higher base of the previous year. Within the commercial refrigeration category, the demand was buoyant for water coolers.

The air cooler vertical witnessed a strong demand in East and South India, whereas demand in northern region was tepid. Increased channel participation, network expansion, and product launch at competitive price points resulted in more than 50% volume growth over the previous year with an exit market share of 7.7% as of July and achieving the number two position in the industry.

In commercial air conditioning vertical, the quarter has witnessed a good demand for chillers and packaged air conditioners. The mandatory quality control order QCO compliance in few of the commercial air conditioning product categories and slowdown in projects will have some impact for the coming period. However, the focus on customer retention and retrofit jobs will continue to support the overall growth for the category.

Commodity prices have softened during the quarter. However, the volatility still continues. Various manufacturing initiatives undertaken, expanded sourcing base with expected stabilizing of commodity prices should help in containing product costs, thereby supporting the overall margin in the future.

To summarize, for the quarter ended September 2023, unitary cooling products segment registered revenue of Rs. 1,209 crores, a 15% growth in turnover from Rs. 1,048 crores in quarter 2, FY23. The segment reported an EBIT of Rs. 93 crores in quarter 2, FY24 as compared to Rs. 76 crores in Q2 FY23, a growth of 21%. And for the six months ended September 2023, unitary cooling products segment registered revenue of Rs. 3,723 crores, a 16% growth in turnover from Rs. 3,210 crores in the first half of FY23. Segment result was Rs. 300 crores in the first half of FY24 as against Rs. 243 crores in the first half of FY23, a growth of 24%.

In Segment B, which is "Electromechanical Projects and Services":

The segment revenue for the quarter was Rs. 924 crores as compared to the previous corresponding quarter revenue of Rs. 554 crores, a growth of 67%. These segment results, however, for the quarter reported a loss of Rs. 49 crores due to a provision of Rs. 86 crores made on account of delayed collection in overseas projects.

A healthy order book at the beginning of the quarter and scheduled execution has resulted in this attractive growth for the domestic project business during the quarter. The focus on collections and certifications has improved the overall working capital and return on capital. The domestic projects segment booked orders worth Rs. 673 crores largely in the electrical and MEP as compared to Rs. 475 crores during the previous quarter.

Commencement of new projects and planned progress in the running projects during the quarter resulted in higher revenue over the previous year. While top line has grown as targeted, the overall results in our overseas projects business have been impacted due to slow progress in the certification and collection of the receivables in few sizable and completed projects. Accelerated efforts are underway to expedite certification by engaging with the customers and thereby improving collection of the due amount. The order booking in overseas projects IOBG for quarter 2, financial year '24 was Rs. 449 crores as compared to Rs. 119 crores in a similar period last year.

The carry forward order book for domestic projects stands at Rs. 5,309 crores containing orders across water, HVAC, rural electrification and urban infra-activities. The international order book as at 30 September 2023 stood at Rs. 3,368 crores largely in the UAE, Qatar, and Saudi Arabia region. Total carry forward order book of the segment stood at Rs. 8,677 crores vis-à-vis Rs. 5,496 crores of outstanding orders as at 30th September 2022.

Segment C – "Engineering Products and Services":

The segment revenue for the quarter was Rs. 134 crores and EBIT for the quarter was Rs. 54 crores, respectively.

Our customer-oriented approach continues to support Mozambique operations contributing significantly to the result. However, a sluggish iron ore market and slower pace of infrastructure roll out has muted the domestic mining business performance.

In case of textile machinery business, capital machinery rolls out from the principal remained positive although a reduction in yarn price and deceleration in exports coupled with supply chain disruptions has lowered the momentum. Focus on sale of accessories contributed positively in the overall performance.

Voltas Beko:

During the quarter, Voltas Beko crossed a cumulative volume of 4 million units since launch of commercial sales becoming the fastest brand to achieve this milestone. The overall volume growth was in excess of 40% over the previous year against a muted growth for the industry. In line with the premiumization efforts, the overall revenue share of frost-free refrigerators and automatic washing machines has increased over the previous year. The intelligent spend on digital and social media has also helped the brand in connecting with the youth and targeting the consumers in an effective manner. Leveraging on the distribution reach of Voltas, the touch points have seen accelerated expansion over the last two quarters. The strategic tie-ups with modern trade and e-commerce partners in addition to the traditional channel has contributed in achieving much higher volume growth than the industry. Our market share stood at 3.3% for refrigerators and 5.4% for washing machines, representing an increase of 0.9% and 1.4% respectively over the same quarter previous year.

The favorable product mix coupled with localization of the fast-moving SKUs has resulted in the improvement of overall gross margins. The profits have remained at the previous year levels despite higher advertisement spends and spends on BTL activities. Various cost reduction efforts coupled with increased in-house production of SKUs will improve the overall gross margin leading to better profitability for rest of the year.

Outlook:

The early indicators of tertiary sales indicate a strong demand during the upcoming festival months. The downtrend of inflation, stagnant interest rates, and a fulfilling monsoon season may help in reviving rural demand during this auspicious period. The general elections may slow down capital spending by the central government over the next few months. However, the long-term commitment of government towards improving infrastructure remains intact. Private capital spends are expected to continue on the back of the production-linked incentives announced across sectors. We, therefore, remain optimistic given the various supporting factors for the business we operate in.

Thank you. That is the end of my introductory message, and we may open the floor for the question-answer session. So, we will request to take it forward. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. Our first question is from the line of Natasha Jain from Nirmal Bang. Please go ahead.

Natasha Jain: Sir, my first question is regarding the EMPS segment. Sir, are these delays in collections happening because we were possibly a little negligent in terms of screening these orders or are these more geopolitical related specifically in the Middle Eastern belt? And how are the margins in the newer orders that we are taking because the order book is quite strong? So, does it mean that in order to get surety of payment, we might bid for the new project that's probably a lower EBIT margin than historically taken?

Management: If you look at the slowed collections, it's basically a trend which we are seeing in our international operations and because of that over the last few quarters, we have changed our strategy and for our new order booking, we are being extra careful. However, whatever the previous orders are there, one has to complete them because, one, there is a contract. Two, there are guarantees given. So, we have to manage that.

We mean, at least in this case, we do not see any major bankruptcies as such but following a conservative approach to taking provisions, we take the provisions. So, as and when these collections will come true, which we are very hopeful, we should be able to reverse these provisions.

However, going forward the margins also we are targeting to improve which kind of reflects or will reflect a risk premium in the region. We remain committed to continuing with this business and looking at the profitability in a big way, because we do have a large presence over the, we would say, last four decades and that would help us in getting projects of our choosing and which we would continue with that and hope to not having to face the similar situation.

It's basically a selection of good customers which we have to focus, and that's what we are focusing while taking the new projects. On the domestic project side, where the bigger focus is there, we are also having the similar controls and strategies being followed.

Natasha Jain: So, should we assume that the newer projects will come at similar margins?

Management: Yes, similar margins

Natasha Jain: And sir, my second and last question is, so you have been mentioning that along with market share protection, you will also ensure that your margins are protected, and then in the recent times we read Noel Tata's narrative that market share loss may be on account of not getting discounts or add in than promotional spends and therefore losing a bit of volumes there. So, just want to get some clarity as to what's the long-term strategy going to be for us from here on?

Management: Natasha, the long-term strategy remain intact. Sorry, this is Manish over this side. Long-term strategy remain intact to have the balance view both on margin as well as on the market share. The market is becoming more fragmented and is becoming more concentrated now with the top seven to eight brands fighting for the piece of the market share. So, some kind of volatility or some kind of intensity can be seen in the market but the long-term objectives will clear to remain leader in both market share as well as margin.

Moderator: Thank you. Our next question is from the line of Siddhartha Bera from Nomura. Please go ahead.

Siddhartha Bera: Sir, my first question is on the UCP Side so we have talked about a 20% volume growth and our overall revenue growth has been 15%. So, can I just tie where, how is the growth in RAC and if you can break into the remaining segments like CR and CAC, how the growth has been?

Management: So, Siddhartha, our growth in the AC we have a growth of around 15% or so. The overall growth what we talk about the 20% is largely laid by the air cooler and the sub-commercial refrigerator category like water cooler and water dispenser. Commercial refrigerators remain almost having a muted growth over the last year. So, this is a composition we have. Since the growth in air cooler is an excess of what we have given in our investor spill result tilting towards a higher turnover, higher overall volume turnover for that matter.

Siddhartha Bera: So, overall volumes include air coolers as well as ACs in that?

Management: All categories have seen a growth largely, but in that among all, the air cooler is the biggest one or the highest one for that matter.

Siddhartha Bera: And sir, going ahead in terms of the commodity benefits which you have talked about, can you highlight, I mean, in general, do we sort of factor in and get back to that earlier levels of double-digit margins at some point with the benefits or do you think given the competitive intensity in the market that may take longer even with the commodities softening now?

Management: No. So, what we have written, what we talked about is we have seen some kind of softness in the commodity price, but the volatility still continued. So, in a way the benefit which the brand or the manufacturer should get on a long-lasting basis is still not there.

However, given these situations wherein we are, the market consensus says that the supply is going to exceed demand at least for some period of time. Thereby we are presuming that the commodity price should soften out, and if that happens, it should support to the product cost wherein we are using the critical commodities like your aluminum and the copper.

However, that question doesn't get ruled out by giving the passing of this benefit to the end consumers, but that we have to play around in the market looking into the dynamics prevailing across country for that matter.

Siddhartha Bera: Sir, lastly, if you can break out the UCP revenue mix into the particular segments, like how much will be RACs and CAC and CR?

Management: As we said, the growth in air conditioner at 15% overall in terms of volume and in case of commercial refrigerators, subcategories like water cooler, dispensers are in double digit and air cooler being the highest in excess of 50%.

Siddhartha Bera: Sir, I am looking for the mix. How much percentage of UCP revenues would be RAC?

Management: So, if the percentage almost remains the same because we have to take, if we go quarter by quarter, then you find that the AC contributes highest to it because of volume being on a higher side, the value per unit on a higher side. So, in Segment A, over 25% odd is coming from the CAC business, rest all from my traditional AC and the commercial refrigerator, and the air cooler business. And within that you find that the ratio between them is 75% is 55%, 15% and balance 5% between air conditioner, commercial refrigerator and air cooler.

Moderator: Thank you. Our next question is from the line of Pulkit Patni from Goldman Sachs. Please go ahead.

Pulkit Patni: Sir, I want to better understand this 86 crores provision that you have taken for delayed collection. Can you tell me how does it works? Is this ECL? Because a delay in payment would not provide you to take a provision. And can you also tell me what is the balance revenue pending in this customer? Because if there is a delay here, what more could we see in future quarters? And I think just continuing with the same question, can you also better explain, like we have been speaking about, or we have been taking these provisions for quite a lot of quarters now, as a management, when do you see things turning for us in terms of better profitability for this segment? Any sense on that would also be helpful.

Management: So, Pulkit, if we answer in two phases, the provision which we had, yes, if we talk about the ECL following the policy what we follow, it would not have amount to the provision what we have taken in the current quarter or as well as in the last quarter and in some of the periods. However, when we see some kind of stress happening on some of the projects, we go on a higher side following the cautious and the conservative policy.

So, in addition to the ECL, we go for a specific provision on some of the projects where we are seeing the stress continuing for some more time, and that's why we have done this specific provision in addition to what we supposed to follow the ECL provision in normal norms, and that's why you may find many times our policy is much more conservative compared to the other project companies operating in the similar kind of industry or similar kind of framework.

Now having said that, the second question is how long it will take into it? We are seeing stress continue over there. There are certain projects which we are watching very closely. Hopefully, we feel that situation should not arise because there are the commitments coming out from the customer side to have the collection or the payment plan given on the outstanding and hopeful we should not see such kind of provision coming back or coming or getting into in the future period, but it all depend upon, honouring of the plan which has been submitted today or the commitment kind of discussion or during our discussion with the customers.

We have to monitor Pulkit, in a quarter-by-quarter situations. These all provisions are pain to us as a management as well as to the investor fraternity. That's why in the last call also we said we have changed certain terms of doing the business in the overseas market and the consequences of that can be seen in my order inflow. It has come down in a quarter basis less than 1,000 crores. Probably, it will still have an impact, further impact as we move forward in the balance part of the year, but that's where we have to structure our business in the international operation till such time, we feel that or till such time we see recovery in the outstanding or in the overall collection process.

Pulkit Patni: Sir, I will take the liberty to maybe just extend this. So, there are other peers of yours also who have problems in these provisions, but they have some, they give some visibility that okay, these orders will get over by X quarter of X year, after that things should get better. Anything on that sort? Because this has been a continuing thing. So, as an analyst it becomes easy if we can get some direction on when we think the worst could be over.

Management: Pulkit, this provision we are taking not because of the running project. These all are coming into either project which are completed or maybe in the last leg of completion. To give you, if we want to go on a much conservative way, the way in which we are standing today, probably you can see such kind of pain may continue for the next two or three quarters. May not be as aggressive or as accelerated what we are seeing today, but if we want to follow the conservatism and you asking me that on giving what kind of time zone you are looking for into it, so the next two three quarters we are feeling that some stress will continue in the international business.

Moderator: Thank you. Sir. Our next question is from the line of Dhananjai Bagrodia from ASK. Please go ahead.

Dhananjai Bagrodia: Wanted to ask you now regarding Voltbek. How are we seeing in terms of A, demand? And B, how do we see the year and next year along those lines? And when do we think, we will start seeing a profitable number in this in market share?

Management: So, if we look from the profitability perspective, if we want to go in a straight-line method or basis, the loss would have been quadruple because of higher volume which we have done in the current year.

However, if you can see our results, it has almost remained at the same level at which it was there last year despite our aggressive spend on some of the service initiatives as well as on the advertisement expenditure which means that we are earning or we are balancing our cost or we are optimizing the cost to the fullest extent in order to achieve our targeted breakeven year which is '24-'25 on a EBITDA front. And that's what our efforts continuing over there and we are hopeful that we should be able to get to the particular break even by '24-'25.

Having said, you ask about the market share. Market share has seen growth over the last year. Since our focus is also going more on premiumization, the frost-free refrigerators to start with has seen some improvement in its overall volume mix or the value mix over the last year. With this we should be able to start gaining in the frost-free market share as well which got impacted and the market share which we are driving earlier was purely based upon the direct cold refrigerator which means that going forward, although 10% what we kept ourself as an objective in the year '24-'25 may not be attainable and that's what we clarified in our previous call as well. Probably we have to wait for some more two, three years before we get into a 10% market share, and this has largely been affected by the COVID two years, which has disrupted the overall distribution as well as on the targeted path what we kept for ourselves.

Dhananjai Bagrodia: Then maybe I will follow it up with the easier question, different question. So, what would be our detailed touch points, let's say last year and this year now, this quarter, year-on-year?

Management: So, if we look into it, we used to have in the range of 6,000 to 7,000 which has now gone beyond 10,000.

Dhananjai Bagrodia: And lastly, what is the CAPEX amount we are seeking for this year?

Management: Current year there is not much CAPEX. We would say the marginal or the normal CAPEX will be there at a plant, but the following year may see some kind of CAPEX given that we are going for more and more capital, more and more localization of the units in our Sanand factory for

Voltbek. I hope your question more was on Voltbek because you continue to the Voltbek front, but for the Voltbek CAPEX

Dhananjai Bagrodia: No, CAPEX for the company.

Management: CAPEX, so since you are continuing in Voltbek, so we gave reply on the Voltbek side. On the Voltas side, yes, the CAPEX plan is in excess of 500 to 600 crores covering both capacity expansion for our air conditioner as well as commercial refrigerator along with PLI led investments which we factored in.

Moderator: Thank you. Our next question is from the line of Abhijit Akella from Kotak Securities. Please go ahead.

Abhijit Akella: Just on the EMP segment, if you could please just help us with the total maybe quantum or the value of the projects that are currently under stress, if that's possible to share that? And also, how much provision have we taken so far on this?

Management: So, as we said, Abhijit, we would not be able to provide any quantum on this matter. What we are trying to say over there is and the amount of provision what we have taken is anyway reflecting in our financial. Going forward, we just answered Mr. Pulkit over there is for the next two to three quarters, we anticipate some kind of stress given the current situation. However, the efforts are under way, we would say, to reduce the impact of such kind of provision as we move forward, and we are hopeful that our engagement with the customers on this ground should yield the favorable results as we move forward.

And again, sorry, Abhijit. Why we am saying it's difficult to provide a quantum, because some of the events which are taking place are not in the ordinary course of business, right? Like, guarantees invocations and all are not in the ordinary course of business. So, it is difficult today to provide, if we want to take the entire my receivables, it will be too conservative. If we take part of it, maybe we give more kind of optimistic view on that. So, that's why we said very difficult to provide quantum. Otherwise, we do not have a reservation any which way for that matter.

Abhijit Akella: And on the UCP side, just within this 15% growth that we have reported revenue growth, how much would just RAC growth have been? And given that the market share that we have reported about 19 odd percent, I believe last year it was about 22 odd percent for the corresponding period. So, should we assume that the MBO sales are basically what have declined for RAC and that has been offset by growth from say e-commerce and EBOs and other channel outlets? Is that how we should understand it?

Management: So, if we look from the, you ask for the first question on the value growth, the value growth is also at 15% for air conditioner and the volume growth is almost equal. That's why we say since there is no across or uniform price action which took place over there, the volume and value growth collaborates to each other.

The second question you talk about the channel participation in terms of the MBOs and all, we would say that not much significant change took place between the channel participation. Yes, the trend reflecting the distributor's strength is going down or distributor contribution is going down, getting replaced with the organized and the modern trade channel partners including EBO as well.

Abhijit Akella: Just also to just clarify, so within UCP, RAC sales have also grown by 15%. Is that correct?

Management: Yes. And it has both volume as well as value growth.

Moderator: Thank you. Our next question is from the line of Aniruddha Joshi from ICICI Securities. Please go ahead.

Aniruddha Joshi: Sir, in one of the earlier calls, you had indicated the steep increase in capitalization post PLI is going to impact the overall ROC of most of the players. So, just wanted to delve deeper on that and understand so how long do you see the impact on ROCE, whether it will be short lived, or do you see the impact on ROC sustaining beyond three years or so?

And also, what would be the quantum probably that you would have internally worked out, if you can share maybe what will be the impact on ROCE, maybe 200 bps, 300 bps or how much the impact will be? So, that is question number one.

And question number two is, now we are going to reach up to 2 million units in case of RAC capacity. So, is it completely backward integrated or what will be the product that we will be manufacturing component wise? So, excluding let's say motors and compressors, what are the total capacity for each of the products, like say cross flow fan or plastic molding, sheet metal, copper tubing etcetera? So, is it also 100% backward integrated or what is the extent of backward integration?

Management: So, let me answer your second question first. When you say about the fully backward integrated, yes, in terms of the heat exchangers and the crossflow fans, some of the plastic molded components, it will be a backward integration. We just wonder what you mean by 100% backward integrations to these components because we are not going to manufacture the copper or we are not going to extract copper from the mines and neither not going to manufacture plastic to have these components in place. Leaving aside these two components, all manufacturing value addition will certainly take place as a part of our backward integration.

In terms of you talk about the ROCE impact, the expenditure will go in a phased manner as we build up the capacity, and we have already clarified earlier that the overall capacity what we are planning is around 1 million. And if we want to cater the South and West Market for the same, unlike other players, we may not see an under absorption of the capacity to a high extent. Yes, but it is difficult right now to give any impact on the ROC assuming that if we are fulfilling this condition of the PLI, it may not have a significant impact on the ROCE definitely since our capital expenditure will be higher and the recovery payback time is going to be 7 to 8 years. To that extent, it will have some kind of impact but get partially compensated by the PLI benefits which government is going to give.

Aniruddha Joshi: So, sir, means any number you would like to put, let's say, 200 bps or you don't see that or it's too difficult to see?

Management: We would not be able to quantify the impact currently. Let construction get over and let's start a commercial production from the factory and that point of time we should be more clear in terms of what impact will be there on the ROCE side.

Aniruddha Joshi: Sir, lastly, what is the total industry capacity right now? And where do you see the industry capacity, let's say, after a period of two years when most of the announced projects get over? That's it from my side.

Management: Aniruddha, we are not sure because people are talking about capacity addition, are they taking, doing in two phases or they are going to come up in the first phase itself? So, very difficult to find out what is the industrial or the industry capacity is for that matter. We can talk about our own capacity which we are looking for it. The question then comes with how the PLI scheme will benefit or will have the general question is any excess supply than the demand from the consumer side? Probably, we have to wait and watch because we are sure the industry is going to align the manufacturing plan based upon the demand what they see in the relevant period.

Moderator: Thank you. Our next question is from the line of Shrinidhi from HSBC. Please go ahead with the question.

Shrinidhi: Sir, on the project business, may I ask what percentage of your project business comes from the government funded projects and how much it comes from the private market, and if you can tell it for both domestic market and exports market separately?

Management: In international business, generally, we have a quasi-kind of government structure, so not like clear that we have in a domestic scenario. In a domestic business, we would say electrical and water projects what we carry normally are funded by the Central and the state governments. In MEP, it's a mix. If we are doing Metro, you can say is again an entity being funded jointly by Central and state. And for the private consumers, it will be a non-government entities.

Shrinidhi: And in all these projects what we do in the domestic market, how much of the contracts wherein Voltas directly have contract with the authority which is spending and in how much of the cases it is somewhere there is a large contractor, and you are a subcontractor to it?

Management: Leaving aside water and the few electrical projects, probably we will be acting mainly as a subcontractor both under the domestic as well as international market.

Shrinidhi: So, there will be one major contractor in between you and like eventual party who is investing.

Management: Eventual party may be either investing or maybe building for its own captive use. Say, for example, data center, right? Whoever constructing data center is putting it for the use. He appoint a main contractor to whom which we associated for carrying out a specific task.

Shrinidhi: And on the provisions, sir, like over many quarters, we have seen that for the very same reason company has been providing and the reason which typically we give is that there has been a delayed collection. So, over time, but we rarely get to hear that reversing of these provisions. Maybe it's the cycle, but what I want to understand is that in last few years, have these provisions turned out to be real cash cost and rather than delayed collection, it was maybe the underestimation of cost overrun that you basically calling it as a delayed collection, but it turned out to be cost overruns?

Management: Generally, what we state is what we mean. So, when we are saying we are providing for the delayed collection, it's the provision is coming on account of that and not the cost overrun. We just want to clarify the very first thing on that.

Second thing is the provision been started taking into the account for the last, accelerated provision, we would say, for the last three, four quarters and the results attributable to maybe the onerous one in few of the quarters and the few of the quarters because of the stress what we are seeing in this market. The reason what you said is we keep talking about the delayed collection, but yes, the fact is that we are seeing those kinds of situations, and that's why we are going with the reason of delayed collection and not anything else for that matter. The question is how long it will continue? Probably, as we said to the earlier participants, we hopeful that the pain may not last for long.

Shrinidhi: And just if I can build on to this question, is there a kind of a like a cumulative provision number that set in balance sheet which can eventually come back if things improve or the cumulative number is not very different from what we actually book annually?

Management: No, no, cumulative numbers year-on-year will definitely be higher than what we are doing in here now. But the question is that the other question, the earlier question what you asked, are we having a reversal? Yes, we have reversals, but while quoting to the investors, we are more transparent and we always talk about the numbers which we are taking the provision, but otherwise, there is a reversal which is happening on quarter-on-quarter, may not be in quantum the way in which we are taking the provision, but the overall P&L talks about the net number, but being transparent to the investors, we always talk about any specific projects or the cross amount which we are taking in the provision.

Shrinidhi: And last one, if I may, sir? You talked about being more cautious in terms of international projects how you take those projects, but apart from being selective, are there any other things that you have changed in terms of way you do this international business so that one can be confident about in future we may not have such episodes of a significant high provision cycle?

Management: Obviously the learning came from our past mistakes and what we realize that and we keep saying that we have to change. We have already initiated the way in which we have to carry out the business. To give you one example, guarantees which have been earlier unconditional, now it will have conditions suitable to the project which we are taking over there or depending upon the customer or the project risk which we you are witnessing over there.

So, we are replacing those unconditional guarantees with a conditional one. Like this, there are various changes we have introduced in the contractual terms between the contractor and to certain extent we have secured, we would say, to the main client as well into the overall contractual terms to ensure that the risk on such kind of events gets mitigated to a great extent.

Moderator: Thank you. Our next question is from the line of Keyur Pandya from ICICI Prudential Life Insurance. Please go ahead.

Keyur Pandya: Sir, just want to understand as far as the room AC is concerned, so what is the situation of inventory with the channel as well as with the company?

Management: Generally, if we look from the festival period time, definitely channel partners will be more optimistic in having this because he is witnessing or he is going to see a good amount of the consumer demand in the festival period. So, it won't be appropriate to talk about channel partner inventories because festival period will decide or the secondary during festival decides about the inventory which is going to have in his hand. If we look from the trend on the primary side looks like the inventory at the channel partner is much comfortable position, and we are seeing good amount of indents coming from the channel partners for the festive season.

As far as the inventory with the company is concerned, yes, it is in the range of 75 to 90 days, but it generally need to be considering the supply chain disruption which we have seen in the past and to safeguard future sales because we don't want a situation that we are losing sales on account of not having inventory with us in the opportunity time.

Keyur Pandya: And on the project side, the way the difference is there in say domestic and overseas order book, similar is the execution. I mean, how are the domestic projects doing? And will they be enough to offset all these kinds of one-offs with net any outlook on the project side net of all the provisions?

Management: So, we would say domestic provisions are doing much better and probably they are inching towards the targeted both for ROCE as well as on the EBIT margin. Hopefully, in the next year we can see reaching closer to what we kept ourselves as a target to be there in the project business as far as domestic operation is concerned.

Moderator: Thank you. Our next question is from the line of Bhavin Vithlani from SBI Mutual Fund. Please go ahead.

Bhavin Vithlani: So, this question is on the total provisions on these projects done because when I am looking at the cash flow statement for six months it is about 180 crores and whole of last year, that number was about 360 crores. So, want to understand how much of this is the total provisions pertaining to the projects business? And what percentage of this would you believe can get reversed as these are provisions for delayed payment?

Management: Bhavin, just wonder where you are seeing 360 crores of collection last year?

Bhavin Vithlani: No, no, no, the provisions for doubtful debt were 360 crores last year, whole of last year, and for the six months in your cash flow statement, that number is 179 crores.

Management: Yes. So, what's your question, Bhavin?

Bhavin Vithlani: So, the question is of the cumulative provisions that you have done over the last 18 months of roughly about 540 crores, how much of this is the provisions for the delayed payments and where you believe that there is a good chance of it being written back and how much of this is actual loss which has been already incurred for?

Management: if we take out the 250 or 260 odd crores of provision which we picked up because of the onerous condition wherein the project got either cancelled by the contractor and or maybe under the DLP period, the main contractor has encashed our bank guarantees - these are the provision probably which will take slightly longer time to come back because it will go into a legal way of settlement.

However, just to inform to the investors, the last quarter or the quarter of the similar period last year, the provision what we have picked up for the project wherein the main contract, the client has terminated the main contractor, the same project has been awarded to Voltas as the subcontractor.

So, hopeful that we should be able to recover may not be the entire provision amount but should be able to mitigate or should be able to recover some of the provision what we carried out for the said project, because when we carry out the provision, it was outstanding against the main contractor, not to the main client. But we hope that as we progress on the project, some loss may get kindly mitigated, but it will take some more time in terms of recovery because these are the litigation cases which probably take longer time than what we expected.

In terms of the other provisions, we are hopeful that the collections should start flowing into it in the near future. We would not like to give, Bhavin, any timelines to it, because the efforts are in a much accelerated way to source or to do this collection, and we are hopeful that it should be done in a near future, but definitely the way in which we are giving information about the provisions, we will definitely provide you the information about the reversal as well when any substantial amount gets reversed in the future period.

Bhavin Vithlani: Just one last follow-up on this is just to understand our ECL policy, when is it that we book a provision and, like, what is that outstanding number of days threshold so after that we kind of book a ECL provision?

Management: So, we would not like to narrate the policy, Bhavin, because every company has a different policy and different look or outlook on the receivable side. What we need to do in a summary way is we follow a very conservative policy, even a minor stress in the overall collection triggers the assessment on the entire outstanding on the client side and accordingly, based on the assessment, we start providing a specific provision and not the ECL provision which otherwise follow in an ordinary way.

Management: Hopefully, this is the last question because we reached to a closing time.

Moderator: Yes, sir. Our next question is a follow-up question from Keyur Pandya from ICICI Prudential Life Insurance.

Keyur Pandya: Thanks for the opportunity again. Sir, just one follow-up. I think last year all the project business, domestic project business subsidiaries were consolidated into one subsidiary, and I think similar arrangement has been done for say overseas business as well. So, what is the future plan of action, I mean, post all the, say, project businesses are into one or two subsidiaries? Do we plan to demerge it or so any thoughts on future plans on this demerger?

Management: So, Keyur, the primary objective is to consolidate the business in the subsidiary company and have the management bandwidth released for focusing upon the consumer facing business. So, that was a prime objective when we start doing this transfer of the some of the verticals to 100% subsidiary company. Domestic transfer what we carried out started giving some kind of positive results. In the last six to nine months, our orderbook has gone up. The execution is taking as targeted or as planned, and the results are also showing or affecting out of it.

International business we just announced the one quarter before. The process regarding that has already been initiated, and hopefully should get over in the near future. But the entire objective, as we said, to release the bandwidth time of the current management to focus more on the consumer side business. If the opportunity arises in the future, in order to value enhancement to the stakeholders, definitely it will get evaluated in a much deeper way and considering in the mind or keeping in mind the shareholders' overall interest into it.

Moderator: Thank you. Ladies and gentlemen, that was the last question for today. I now hand the conference over to the management for closing comments.

Management: So, we hope we have answered to most of the questions. We do understand there is a kind of more anxiety or kind of concern on the provisions which we are taking up in the international business. Let me assure you that the management is taking all necessary steps to reduce or to mitigate the risk to a great extent. As we said, there are some pain area which is still continuing it. However, hopefully as we move forward, such kind of impact shall be mitigated to a larger extent. If anything, remain unanswered on the participant side, we are just a phone call away. We wish all the participants a happy weekend and a Dussehra, which is coming in the next week. Have a great evening. Bye.

Moderator: Thank you. On behalf of PhillipCapital (India) Private Limited, that concludes the conference call. Thank you for joining us, and you may now disconnect your lines.