“ELGi Equipments Limited Q4 FY ’20 Earnings Conference Call hosted by Asian Markets Securities Private Limited”

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MANAGEMENT:	**MR. JAIRAM VARADARAJ – MANAGING DIRECTOR,ELGI EQUIPMENTS LIMITED**
MODERATOR:	**MR. KAMLESH KOTAK – ASIAN MARKETS SECURITIES PRIVATE LIMITED**

Moderator: Ladies and Gentlemen, Good Day and Welcome to the ELGi Equipments LimitedQ4 FY'20Earnings Conference Call hosted by Asian Market Securities 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 an operator by pressing '*' and then '0' on your touchtone phone. Please note this conference is being recorded. I now hand the conference over to Mr. Kamlesh Kotak from Asian Markets Securities. Thank you and over to you, Sir.

Kamlesh Kotak: Thanks, Bikram. Good Dayeveryone. On behalf of Asian Markets, we Welcome you all to the 4Q and full year FY '20 earnings conference call of ELGi Equipments Limited. We have with us today Mr. Jairam Varadaraj, Managing Director, representing the company. I request Mr. Jairam to take us through an overview of the quarterly and the yearly results and then we shall begin the Q&A session. Over to you, Sir. Thank you.

Jairam Varadaraj: Thank you very much, Kamlesh, and Ladies and Gentlemen, thank you very much for your time. Before we start, I hope that you and your family and all your dear ones are safe and well, these are trying times for us and I think the entire solution for battling through this process is squarely our responsibility and I wish you all the best in terms of continuing to practice safe existence so that we are able to beat this situation. Having said that, as per our normal practice I will take you through a reconciliation of our Q4 performance compared to Q4 last year and then talk about the full-year again in relation to the previous year and give you a context for how the business has done which are not necessarily fully reflected in the numbers, so if I compare Q4 of this year versus Q4 of last year, our revenue dropped by almost 733 in fact at the minimum we would have easily done this if not the shutdown roundabout the second or third week of March. We had all the products lined up, orders lined up, so we lost close to 75 crores of revenue in the month of March. As a consequence of that, our EBITDA impact was close to 32 crores and what was interesting for us this year is that our contribution margins have significantly improved and this is not an anomaly as you would have seen over the many years, we have consistently improved our contribution margin at the material cost level, so combining these two, the loss of revenue and the improvement in material cost at a contribution level we lost about 23 crores. Our EBITDA under these circumstances should have been about 380 million or 38 crores when in reality we had only **22** crores, so there has been a cost increase impacting EBITDA to the extent of 17 crores.

The largest impact of this has been our strategic investments in Belgium to the extent of 8 crores during the quarter and the fact that we had made three specific acquisitions; one was Michigan Air in December, the cost of that comes in additionally as a cost and we had the final payout in the case of Pulford's and we took over the portable business of our distributors in the US, so the combined effect was the reason why we had a significant increase in our fixed cost. The regular business as usual costs were well under control, in fact I will just step back here and talk about the third quarter. Up to the December quarter for the nine months, the Indian market was extremely challenging. We recognized it as early as August, sluggishness had already set in. We went through a significant cost optimization program as well as different a marketing going deeper into the market and aggressive marketing program, and the months of January and February we were doing exceedingly well and we expected March to be also a record month for us in India, but unfortunately that did not happen, so it is the combined impact of that and our strategic investments in primarily Belgium that has caused this impact in our EBITDA compared to last year.

Going into the fullyear, at a full year level our revenue drop is close to 34 crores and if we had not had impact of this virus, we would have actually exceeded last year's revenue and that is what I was telling you January and February was tracking very nicely for us, but unfortunately it did not happen in March and because of the revenue loss of about 34 crores at a full year level our contribution also dropped by about 15 crores, but like I said our contribution margins have been very positive and because of that we gained close to about 32 crores, so net-net we gained about 17 crores at the contribution level. At EBITDA, we should have been at around 210 crores, we came in at 130 so there is a gap of close to about 81 crores and our biggest cost again is similar to the Q4 explanation our biggest cost have been in our strategic investments in Belgium and in our acquisition. India, we had made an investment in people and in certain other fixed cost in the beginning of the year on the expectation there will be a close to an 18% growth in India, that did not materialize, so for a big part of the year we had to incur the cost. We are reigning those costs in now both on the people side as well as on the other fixed cost. We had started that process somewhere in November and December that is why we saw some good impact of that in Q4 and all those reductions we are continuing to benefit even now, so this is really the summary of the numbers. I will of course take specific questions later, but I would like to step back and talk about our business for the year '19-20, what were the highs and what were the lows.

Let me start with the lows first, the low for us was that like I said, India started on a very positive platform. We were looking at everything pointed to a buoyant growth in India and because of that we had made certain investments to reach into new markets which meant additional people. Unfortunately, that did not materialize and because of that there was a significant effect on us. Belgium investment like I had explained to you in the past thing is a strategic, deliberate investment. In fact, today what we are spending in Belgium is far lower than we had earlier budgeted and the results that we are getting as a consequence of that has been very positive, so on the low side, it is really not a low, but it is an expense that I am bringing in. US, again there were certain additions to people because we took over the portable business and there was a transitionary kind of a lull from the distributor to us, it is coming back up, so during the year we had some dislocations which we have picked up and things are happening back now, that is a low. Patentswhich was an area that we looked at close to about 16% growth did not do well, we have specific reasons, we are working on putting those solutions in place as we speak, but that was the low for us last year.

On the positive side, on the highs is that if you look at again Belgium, we have been able to add distributors in almost all the countries and the rate of increase of distributors is extremely encouraging, and I will come and talk about what is the indication for us in April, May, and June and in that context, I will talk a little bit more about Belgium. The positive thing other highs are that in India we have gained share of the market in spite of a sluggish market, in specific verticals we have gained share, but it was not enough to compensate for the drop in the market that we experienced, the overall demand drop that we experienced. The other highs have been new products that we have introduced, they have gained very good traction especially in the oil-free segment in India, which is a very positive thing. We have grown very well in that segment of the market. Pulford in Australia, that acquisition has done exceedingly well for us, we have grown there, so these are all the highs and lows for what happened on the business side, so as usual let me give you a geographical rundown, starting from Australia, we have done well in Australia last year, Pulford and ELGi Australia combined entity has grown.

We are continuing to increase our share of the market, so it is a very positive thing. Southeast Asia has also grown, but nowhere near what we anticipated, but there has been a growth. India has been a challenge for us not because of our performance, it is just the general drop in the market, but specific verticals have done very well. Gulf, where we went through a direct model while we have grown, we have not grown enough to the extent that we had budgeted, I am not worried about it, it is not an issue with the market or our strategy, it is just a planning error in terms of how quickly we could have expected that kind of a growth that we have planned. In Europe, our regular business through Rotair of our industrial products has done exceedingly well both in Italy and in France, and with the addition of the manpower that we have done to reach into Spain, into UK, into the whole Benelux region, eastern Europe has also gained very good traction. We are beginning to see revenues beginning to ramp up. US, our direct business grew well, but not at a percentage that we expected, overall market in the US dropped, but actually we grew when the market dropped which means we have gained share in the market. Patterns like I said has been a challenge, we are on top of it, I am very confident that we will come around, I do not think there is an area of concern there.

As far as new products are concerned, our ABseries which is our new disruptive oil-free machine has seen exceedingly good traction in India. We are beginning to, we have already installed machines in Europe as well as in the US, so this is a very positive thing for the future and we are very confident and the whole team is very confident including our distributors all over the world that we have a good product in our hand. We have launched a range of piston compressors, very high-tech, highly engineered solution which will give us the ability to expand our share of the market in India where there is a high domination of unorganized players with lowcost. With our new technology and our machine, we are very confident that we can penetrate into these price sensitive markets, so overall while the financial numbers look very challenging, the business fundamentals look very solid, so I am very confident that the future looks good.

Now, I need to talk to you about the COVID situation. Now, specifically for us situated in Tamil Nadu, I will give you a context of what happened, we were locked down, by the March 21st or 22nd is when the lockdown happened. We anticipated that April and May will be a washout, but contrary to that we were able to get special permission from the Government. We operated our plant with very skeletal staff primarily to supply our overseas requirement which we did and therefore in the month of April, the revenue was not zero, it was nowhere near the run rate, but it was reasonable. Then in May when the lockdown lifted, our performance in international markets really has helped us. Many of the countries like Australia, Australia is almost running at the earlier run rate. Europe is contributing because they are starting from zero and that has been very positive. US was not locked down as much as India was, therefore, the US operations have also logged in, so the performance in May and in June has been very good, again I want to caution you nowhere near the run rate, but considering the situation, considering what I am hearing about the drop of other capital goods companies, we have done well and that has primarily because of our presence in the international market and this is something that is heartening for us. At this point in time, I am not able to say whether we have grown April to May, May to June we have continued to grow. At this point in time, I am not able to say whether that trajectory of growth will continue into July-August and the rest of the month, I hope it does, if it does then within this financial year, we should be able to get back to our normal run rate, so this is something that we are waiting and seeing. In the meantime, multiple cost reduction initiatives have already started, we are seeing the results of them, we have seen it in April, May, and June and we will continue to see more of them coming in, so this is really the situation as far as the COVID context is concerned, so I will pause here and if there are any specific questions, I will be happy to take. Thank you.

Moderator: Thank you very much, Sir. Ladies and Gentlemen, we will now begin the question and answer session. We have our first question from the line of Ravi Swaminathan from Spark Capital.Please go ahead.

Ravi Swaminathan: Sir, my first question is in continuation to your commentary on current trends in terms of demand, what is the kind of run rate which is there in the domestic market say in the month of June or something of that sort, is it like 40%-50% of normalcy or higher than that, how is it?

Jairam Varadaraj: You mean in the current context, Ravi?

Ravi Swaminathan: Yes Sir vis-a-vis the usual run rate in the domestic market, how is it currently and if you can give a picture on the individual subsectors like infra, industrial, water well, which is relatively better off and which is relatively worse off?

Jairam Varadaraj: I will try to give you a breakup of our percentages in relation to the run rate in some of the major regions, so in India we are at around 55, I will take June as the latest because it is the best month of the three and it is a clean month in the sense that there was no lockdown and our factories were functioning, so India is about between 55% to 60% of the normal run rate. Now, if I have to look at verticals that have contributed, very surprisingly we thought it would be pharma, food, FMCG, chemicals, we thought these were the verticals that would continue to give us the business, but we were surprised to see even general engineering investing, so we have unlike our expectation that these five industry verticals will give us a bunched kind of a revenue for the month of June, it was actually quite diversified, so we also questioned whether this is pent-up demand from the past that is being ordered backlog that we are seeing, there is a certain percentage of order backlog that has contributed, but there is also book and bill that we have done in the month of June, this is India. As far as Europe is concerned, we are at around close to 70% of our run rate in both portables as well as our industrial machine. As far as the US is concerned, we are close to 75% of our normal run rate in all the businesses put together, and in Australia we are actually above our run rate.

Ravi Swaminathan: On a slightly longer-term question, a lot of the compressors in India in the lower end piston are Chinese imports, given the anti-China sentiment which is prevailing both in India and outside India, is there a possibility, a significant portion of that can be captured by us in the domestic market given that we are very strong in piston compressor and outside India also if you can give a flavor, it would be great?

Jairam Varadaraj: First of all, the presence of Chinese compressors in India at the moment is not a very significant presence, it is there but it is not very significant. At the max, I would say it is less than 5% of the market and they are playing in really the low-end, the bottom feeding, low performance, low price segments of the market and they do not have the marketing reach and the marketing presence that well-established customers would expect in terms of service support and training and all that, so to start with, their presence is low. Now, in terms of this anti-China sentiment mushrooming into behavior, it is too early to say that it is a turn of switch, everything will change, Ravi. How the world is going to react to China because of the virus and how India and India’s friendly countries are going to react to what China is doing in the borders, these are too early days to talk about in terms of a permanent impact. I think it is going to take some time, the world right now is struggling to deal with the virus, I think it has to settle down before any strategic decisions and maneuvers are made in that direction.

Ravi Swaminathan: Finally, in terms of cost, so basically on a blended basis both at an India level and outside India level, what kind of reduction would ultimately be in Financial Year ’21 and also in terms of other cost you had mentioned legal charges etc. which might not be there going forward, if you can give some inside on it will be great and CAPEX plans also, Sir?

Jairam Varadaraj: Our CAPEX right now is pretty much frozen, Ravi, so I do not think we are going to look at any fresh CAPEX. If at all there is going to be CAPEX of residual payments on machines that have already been either ordered or have been delivered and we have the final payments to be made, I do not see a significant amount of value there. As far as our goal is a 20% reduction in our overheads. It is too early to talk about what exactly we will achieve, but the entire leadership team is, their predominant focus is on looking at how to fundamentally reduce our cost and I am reasonably confident that we will achieve because I will give you an example for instance we are looking at shutting down most of our branch offices and we are changing to a model of working from home and there is a significant savings in rent, so these are all the things that we have already decided and it is a matter of rolling it out and every contract is being renegotiated, so where it will settle down it is too early to tell, but there will be reduction, so our goal is 20%, we will have to see how much we will achieve.

Moderator: Thank you. We have next question from the line of Kirti Jain from Sundaram Mutual Fund. Please go ahead.

Kirti Jain: Sir, first is on the motor manufacturing thing which you are doing for captive, how many models or how much of our sales mix we have been able to adopt in-house motor? Second thing is on the aftermarket business, how has been the momentum in the Q1 and how is the enquiry level for the aftermarket, and thirdly, are these cost reduction changes which you had highlighted in the earlier part to Ravi, are these structural or will they again come back in FY '22 or FY '23?

Jairam Varadaraj: Motor plant last year '19-20 was our investment as well as field validation program, we have got hundreds of motors running in India and the performance has been outstanding of this motors, but unfortunately this year the first three months the requirements have been low, so the motors are being supplied. Right now, we are focusing only on the India market and in the limited supplies that we are making in the India market right now maybe 25% of our compressors are going with our motors. By October, we hope that percentage will go up to 50%-55% and then we will look at expanding it to Europe and in the US, so that is really the plan that we have. Your second question was pertaining to the aftermarket, so aftermarket in these three months has done well, again nowhere near the run rate of our earlier run rate, but it has been one of the larger contributors to our revenue in these three months because a lot of plants are running and one is our ability to supply which we have built up fully now, we are fully geared up to supply.

The other is many of the places are still under local lockdown, so one customer wants to service but we are unable to reach them in some locations and in many cases, customers do not want us to visit at all, so there are all these combinations that are happening. It could have been a lot more, but I do not think we have lost any opportunity in terms of what is there in the market. The third is in terms of overheads, if you look at all our overheads, there is the occurrence of the overhead and the cost of the overhead. Now, occurrence has come down by virtue of the current situation that is nothing that we have accomplished. Our goal is to reduce the overhead at a structure level, so when I talk about 20% reduction, it is not necessarily focused, it is not fully focused on occurrence, it is focused on the structure of the cost, so I will give you an example. Travel cost right now is almost zero, now that is no achievement of the management team, it is a situation that has created that reduction in cost, but we need to look at the structure of the cost itself, for instance do we need to travel, that is a structural decision, so our decision to wind down our branch offices, move sales people closer to customer pocket, these are all structural changes that will result in reduction in travel cost even after situation comes back to normal.

Kirti Jain: Sir, now when we see the win market, two win markets which have seen some positivity is the food processing industry there have been CAPEX plans and yesterday Government also told new plants have been laid by Government and second thing is on the pharma side, Government is also providing lot of incentives, so anything we are bringing new products towards that side to gain traction and gain market towards that side?

Jairam Varadaraj: There is nothing new for food processing, we have had a very strong presence in that vertical and we are seeing that vertical contributing in these three months, so we are quite happy about that. There are no new products per se, it is just a more focused attention that we are paying. As far as pharmaceuticals are concerned like I said, our new oil-free machine, our disruptive oil-free has seen very good traction in this segment and increasingly we are seeing all the large Pharma brands becoming our customers, so it is a very positive development there.

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

Bhavin Vithlani: Jai, it is more of a question like when we met last in Feb and once the lockdown was initiated and the current situation, are you more positive or negative looking at the current developments?

Jairam Varadaraj: Well obviously I am not very happy with the current development, our inability to go and engage with customers. The positive side is that it is giving us a lot of opportunity to introspect and clean up many of our cost structures. As you are growing, you tend to incur cost because you are so caught up in that momentum of growth or developing new markets or new initiatives, so this is given us a good pause to reflect back and say where do we take costs out, so that has been a very positive thing. The other positive thing that our international business even though it was contributing 50% has always been bit of a living-undertheshadow of the Indian business. Now, the fact that we have got our performance in April-May-June because of our presence in international market at a profitability which is far better is another positive sign for us to really push hard in growthose. I just want to say that our breakeven at an earlier run rate we were at 80, today our breakeven is at 60%, part of it is because our international businesses have higher profit margin, part of it is also because of the current situation, a lot of the overheads have gone away so that is true. Our cost reduction initiative will address some part of the overhead reduction will get to get sustained, but the fact is the international businesses’ higher profit contribution has been a very positive thing in these three months.

Bhavin Vithlani: We are just continuing on that, liquidity support that you would have thought maybe sometime towards the time of April, would you believe that the same is now required or you believe that the business is actually been back on the feet much sooner and that liquidity?

Jairam Varadaraj: It is a fair question, Bhavin, but the point here is yes, compared to what we planned would be the reality for April, May, June, we have done far better than that, there is no doubt about it. The expected impact on our liquidity that we had thought will happen, it has not happened, but my concern at this point in time is will we continue to follow the trajectory of growth of April, May, June. If we do not, then we will face a liquidity situation maybe not as extreme as we thought we will, but if we are not going to grow quickly to our earlier run rate, there could be some challenges, so we are continuing to pursue options on enhancing liquidity, it is very early days to talk about anything specific, but we are giving it enough serious attention, it is a priority that we are focused on.

Bhavin Vithlani: Just one last question from my side on the aftermarket, you already addressed, but like within the population of the ELGi equipments that we would have installed, what would be our wallet share within that and this is looking at some of your peers which may have a longer installed base and 40% of their revenues come from the aftermarket, if you could give some color maybe on a three-year basis as you said it is a much larger focus market now? When we look at some of your peers like Atlas Copco for them aftermarket share is about 40%, if you could give us three-year to four-year picture ignoring the current disruption, how the aftermarket can grow for us?

Jairam Varadaraj: Let me contrast our aftermarket business in India and that to for certain products that are aftermarket conducive, so let me clarify that a little bit more. If you take an oil lubricated screw compressor, it is extremely conducive for an aftermarket business because these are organized customers who buy it, they need the parts, service, and support. Then there are piston compressors that are not very conducive because these are small customers who do not really look at repairing and maintaining their machine as per the recommended intervals that is good for the machine. Then you have the portable business where the aftermarket worldwide, it is not only for ELGi, but worldwide it is only the response of that market is very poor in terms of maintaining the machines to the schedule. Then you have the railway business, which is again Government-owned, the aftermarket piece is not as high as the regular industry, so if I take the industrial piece which is the oil lubricated screw and the oil free screw in India and I take the segment where ELGihas got a good installed base comparable to the other brands that you mentioned will be the oil lubricated screw compressor.

Now, if I take only that business vertical and if I look at only the aftermarket piece of that business vertical, we are already at a mature 35%-40%, so we are comparable at a global level of opportunity compared to the others for in India for markets for product segments where it is very conducive. Now, in the other markets for oil lubricated, our challenge and the opportunity is to create that installed base, the minute you create that installed base, you have a regular flow of aftermarket. Now, just to give you an example, just to give you a reference point, just on parts, I am not talking consumable parts without taking into account the opportunity and the replacement parts without taking into the opportunity in the service charges, I am just looking at consumer parts. If $ 1 of equipment sale is made, you have $ 1.2 of contribution level profit over a ten-year period from just consumable parts, so that is the profit opportunity of the aftermarket at a very, very conservative level, so which really means that 12% even in the first year on the equipment sale you are going to get as aftermarket and as the installed base keeps going up this becomes an annuity that will come.

Bhavin Vithlani: What could be the aftermarket as a percentage of our India business?

Jairam Varadaraj: At today's level if you combine everything as the denominator all the businesses and the aftermarket as a numerator, we are at around 24%, but if you take specific industry verticals like I said in some of them, we are at 35%-40%.

Moderator: Thank you. We have the next question from the line of Manish Goyal from Enam Holdings. Please go ahead.

Manish Goyal: Just to continuing from what Bhavin was asking like earlier when we had met in February, we had enumerated in terms of like the number of people we are looking to addin Europe and then associated cost implications over a period of next three years to the tune of some 160 odd crores, so now with evolving situation with things changing, so if you can like give us a perspective one is on your expectation on the revenue front, how has it changed and second on the cost front going forward how has it changed, if you can just give us a perspective on Europe and overall?

Jairam Varadaraj: On our Europe strategic plan, when this crisis hit, all the additional headcount increases have been frozen. Now, to what extent we have reduced in relation to that 160 crores that we had planned to invest over a three-year period, I would say about we have cut off probably around 20% to 25% and we are going to wait and see if the market starts moving and we are able to deliver on the numbers then we will incrementally add and these are all revenue producing headcount, these are not overheads. As far as the sales are concerned, today this period is not the right period for me to make an assessment, but if I look at April even earlier if I go back to even January, January onwards except for the period where Europe was locked down, we have consistently grown our sales of the Europe initiative in every country, so I do not want to give specific numbers, Manish, we had a run rate of machines already in Italy, we already had a run rate of our machines in France, I am not talking about that even though it is part of that initiativeand that cost that we are incurring is actually propelling additional sales in these two countries, I am not even talking about those two countries, I am talking about all the new countries that we have gone in. We are seeing significant increase in revenue, but nowhere near what we had earlier projected because of the current situation, but considering the current situation what we are doing this is a very positive thing.

Manish Goyal: So ideally the seeding of the market which we were probably planning now with the heading of new people is it that it probably gets postponed by a year or so and the incremental sales what we were probably looking may probably materialize but at a lower end?

Jairam Varadaraj: The annual cost that we had earlier planned as part of that 160 crores investment, the 160 crores investment is actually a loss, so the people cost that were contributing to that loss I am saying 75% is already baked-in, they are already there. It is that additional 25% that we would have spent more on adding people that has been frozen.

Manish Goyal: Also taking it forward from here like our annual employee cost is roughly 400 odd crores, so when you said we are probably looking at 15% to 20% cut in cost, can we expect similar number over here or how should we?

Jairam Varadaraj: The reduction in cost outside India is not going to be significant because these are all recent additions for a very small business relatively speaking. There are some increases we have gained, for instance we have participated in the payroll protection program in the US and we have got a grant of close to $ 2.5 million. Now, those are all Government supported effective reductions in our people costs there. Similarly, in Australia there is a pay check protection program, we have been eligible where we have got about 1.5 million, now those are all going to be cost reductions of a temporary nature in thehigh-cost economies where the number of people have already left, if we cut anything further then whatever business we are doing will go, so the focus is on India. Now, India we invested with a certain expectation of growth, but it is not because of our performance of the team, it is the economy that started tanking from August of last year, so we are taking cognizance of that and then saying what is it that we need to take out and under these circumstances, we have to do it in a very humane way. We have to be conscious of our cost, but we also need to be conscious of the likes of people and their families, so it is a fine balance that we are working on.

Manish Goyal: Just couple of housekeeping question is in terms of what is our gross debt and net debt as on March?

Jairam Varadaraj: The net debt as on March was about 260 crores, I do not have the gross debt, unfortunately Manish working from home I do not have easy access to information, but I can share this off-line with you, I will have Raghu send that information, but I can tell you the net debt right now is lower by about 50 crores.

Manish Goyal: Right now, as on date?

Jairam Varadaraj: Yes.

Manish Goyal: Just last question, I wanted also a data point on other income which has shot up in standalone in Q4 to 30.6 crores, so is it that dividend from the automotive subsidiary has come in?

Jairam Varadaraj: We did not take any dividend from ATS, like I explained in the dividend decision that we had made in February-March, see this year there was a one-time provision that the tax paid by the overseas subsidiaries if they pay a dividend, the tax could be set off in India only for the Financial Year ’19-20, so these dividends came from our Indonesian and the Gulf subsidiary, we did not take dividend from ATS.

Manish Goyal: So this is basically a reversal of tax which is paid on the dividends received from Indonesia and Gulf subsidiary?

Jairam Varadaraj: Correct, that is that 30 odd crores that you see as other income. Now, in the consolidated, you will not see it because it is within the thing it is consolidated and the tax on that has been taken out of reserves because when you consolidate you do not have income, but you have to pay tax, so just like dividend distribution tax which is taken out of the reserves, this has also been taken out of the reserves.

Moderator: Thank you. We have next question from the line of Renjith Sivaram from ICICI Securities. Please go ahead.

Renjith Sivaram: Sir, this employee cost of 400 crores, how do you see that, we understand that given the scenario, is it like we will stop any incentives and bonuses and keep our workforce for the long-term, so will that sustain around the same number or you see a reduction in that?

Jairam Varadaraj: We are working on reducing that like I just explained to Manish for the focus more is on in our Indian headcount because the headcount outside of India is very small and if we touch that in any significant way, it is not that we are not going to but if we do touch it in any significant way, it is going to paralyze our business there, so it is an India focusthing, so in India what we have done is there are no increments for this year, there is no performance bonus for this year, and we have also looked at the first stage of cash flow optimization for certain levels of people and above, we have deferred a certain percentage of their salary. Now, we are going to watch this very carefully to see whether we should convert this deferral into a salary cut. We will take that call in the next couple of months, this is on just optimizingthe costs, but we see opportunities to reduce the head count like I said we had invested in India on the premise that the Indian economy will continue to grow and we had invested in people last year and that has not happened, the Indian economy did not grow, it is not that we did not perform to that potential, so we do not see the Indian economy coming back to the growth path of 7%-8%-9% anytime soon, so therefore there is an opportunity for us to look at these costs, which is what we are evaluating that will be a reduction in the cost.

Renjith Sivaram: What is our target for debt for the full year?

Jairam Varadaraj: If we had done to our budget which is close to a 15% growth than our debt levels would have been half of what our current level is, but I am not able to say how our top line, because without a top line there is absolutely no way we can manage our debt very well under steady state condition, so like I said right now our debt has come down, we have managed our cash flow very well as the debt has come down, but if the top line does not support and grow, it is going to be very difficult to sustain it at these levels, so Bhavin's question earlier I said we are looking at other forms of funding which will help us during this time, but we are evaluating what could be the scenario that we need to plan for.

Renjith Sivaram: Sir, I think in one of the major section, the water well last year we had lost some market share so has that seen any improvement because we are seeing at least the farm sector is doing well, the number of sectors which are being?

Jairam Varadaraj: Farm sector is certainly doing well, but the water well segment has not picked up yet, we have lined up some great products for that market, very optimistic about when this market comes back, we are going to regain our share of this market. This time I am very confident because the products that we have developed are just outstanding. Now, is it going to happen in one year probably not, but in two to three years' time I am very confident we will regain our dominant position in that segment.

Renjith Sivaram: Sir, lastly you seem to be a bit more optimistic compared to our last con call, so if you can say which segment like you told it is a broaddiversified, in that if you want to pick up two-three particular segments which are the ones which are driving this optimism?

Jairam Varadaraj: During the last call which was sometime in April we were kind of just at the start of this entire pandemic and the impact and nobody really knew what was going on and what to expect because nothing was happening on the ground, but in the three months of April, May, and June, we have got a little bit more confidence that the future may not be as bleak as we thought it would be, but still I want to caution here, it is early days like I said the trajectory of growth has been very good in April-May-June, whether it will continue down that trajectory for the balance nine months is something that I am not able to say for sure, so with that caution in mind, the positives that I see is our international business has really done well. The drop in run rate in our international market has been significantly lower than the drop in the run rate in India, so the verticals that have done well in international markets cuts across all, it is not specific to any specific industry vertical, we are seeing it across. In India, we anticipated only these five segments which is chemicals, pharmaceuticals, food and beverage, FMCG, and textiles these are the things we thought will continue to have a good run rate, but what we are seeing in the three months, we are seeing a much more broader spectrum of industries buying our machine.

Moderator: Thank you. We have next question from the line of Aditya Bagul from Axis Capital. Please go ahead.

Aditya Bagul: Sir, my question is on a slightly longer-term basis that to with respect to our overseas business, we have five key geographies where we operate, we have Middle East, Southeast Asia, Australia, Europe, and US, on a sustainable basis can you help us understand what is the kind of growth rate that we expect in these geographies and if you could probably split that between what is the overall industry growth rate and what is it that we are targeting?

Jairam Varadaraj: Strategically, our markets are Australia, Indonesia, Thailand, India, Europe, and the US, these are our strategic markets, Aditya. If I look at Australia, the Australian market is probably growing at less than 1%, but our growth rate, I do not want to give the exact percentage but it is a low double-digit. Now, why is that happening, when you are a bottom feeder I keep giving this anecdotal thing as a referral, when you are a fish at the bottom on the floor of the ocean, if there is a storm at the top of the water, it does not make a difference, right, so there is so much of headroom for us to grow, so that is really what is happening for us in Australia. Now, we have a very clear plan to double our revenue in the next three to four years in Australia, and we are tracking to that part, we are very confident that will happen. Now, as far as Indonesia and Thailand, we continue to have challenges, it is more a talent level challenge rather than a market level challenge. We have grown but our strategic traction is still not as strong as it is in Australia, we are working on that. India, I have explained it over and over again in this call, we are present, we are there, we have got multiple initiatives runningin spite of a suppressed market. I am not talking on a regular on a run rate basis, I am not taking the COVID situation, I want to keep the COVID situation out, we are working on multiple initiatives to deepen our presence and our penetration into the market, we are quite confident that we will start seeing results in India, but a percentage of growth will be a function of how the economy supports us, this is something that we do not have any visibility into as to what is going to happen. As far as Europe is concerned like I explained in the past thing, our investment we are talking about 160 crores over the next three to four years, now at the end of the fifth year we expect to breakeven, recover our losses and post the profit and at that point in time, we are looking at a revenue of close to 500 crores and that is the plan. If we had to acquire a business of that size, it would have cost us probably more than double of what we are investing to grow that business. As far as the US is concerned, we worked with BCG two years ago to build a very clear strategic plan, we are tracking to that plan and our goal is in the next four to five years, our combined revenue in the US will be close to $ 120 to $ 140 million, so that would be an another close to 700-800 crores.

Aditya Bagul: Sir, my second question is on some of your opening remarks, you mentioned that in Q4 specifically we had a revenue drop of 75 crores, but then in the same breadth you mentioned that your EBITDA impact was about 32 crores?

Jairam Varadaraj: We lost 74 crores and the contribution that we lost was 32 crores because of that 75 crores.

Aditya Bagul: So this was on the contribution?

Jairam Varadaraj: Contribution level, yes. We gained contribution because our contribution margins at material cost level was higher than the previous year.

Moderator: Thank you. We have next question from the line of Harshit Patel from Equirus Securities. Please go ahead.

Harshit Patel: Sir, my first question would be you have spoken at length on your expansion plans in to Europe, could you tell us what is the amount that you have already invested in FY ’20, I think earlier you had indicated about 30 crores kind of a number, so could you give us an update on that?

Jairam Varadaraj: Our investment has been about 30 crores right now in the year ’19-20.

Harshit Patel: The overall revenue earned on this investment will be very minimal I would expect?

Jairam Varadaraj: It will be marginal for '19-20, but like I said we are beginning to see a good growth happening from January onwards.

Harshit Patel: On my second question Sir, I would think that India's overall air compressors market would be around 4000 to 4500 crore, so out of this market what would be the share of oil-free market, if you could throw some light on that?

Jairam Varadaraj: I know the numbers of machines, I do not have the value in front of me right away.

Harshit Patel: Sir, even if you could give us some idea on the volume front, as you say you have the overall numbers in front of you then it would also help us a lot?

Jairam Varadaraj: Our estimate is for the year '19-20 the total marketnumber of machines was approximately around 300.

Harshit Patel: What would be our share if you could highlight?

Jairam Varadaraj: Our share right now be about 20%.

Harshit Patel: Sir, globally how would be the dynamics, I mean globally overall oil-free market would be greater in size than the oil lubricated one?

Jairam Varadaraj: No, our estimate of the global oil free market which includes both oil free screw and centrifugal is anywhere between 20% to 25% of the total air compressor.

Harshit Patel: Total market would be around $ 15 billion approximately?

Jairam Varadaraj: Yes, correct.

Moderator: Thank you. We have next question from the line of Aman Shah from Jeetay Investments. Please go ahead.

Aman Shah: Sir, in some of the earlier interviews actually you highlighted that in era of COVID, people will now look to players like ELGiwho give a better value proposition from a quality as well as price and that should sort of be beneficial to us in this era actually, would you please elaborate on that and how are we seeing in last two to three months?

Jairam Varadaraj: The fundamental logic is that under these conditions everybody is looking at managing their cost and cash, now which means that when you are buying a compressor earlier you may have bought the compressor, compressor like I have always explained is not a production machine. It is not a machine that earns the customer money, it is a utility that supports the production in a factory. Now, typically people do not pay too much attention to the purchase of a compressor, but under conditions like this, earlier they may have just bought it on the basis of a brand and a little bit of negotiation and say okay fine, let us just focus on the production. In conditions like this, brand as long as it is competitive, if it is not I do not think people are going to pay a premium just for the brand or the premium that they are willing to pay will be significantly lower, so that is the logic from a pure customer behavior point of view, so on that basis we believe that there will be opportunity. Is it going to transform and make a switch overnight, no, and to answer your question are we seeing this result in April-May-June, no it is too early and the impact we will see more in countries like Europe, America, and Australia where we are not a known brand, but our performance is as good if not better than the well-known brands.

Aman Shah: Sir, my second question was we developed a revolutionary product on the oil-free compressor where we shrink the inefficiencies to this 5 to 7 percentage, my question is in case like we are competing to all the global leading compressor players and the market is very mature. The R&D budgets are much higher than us, what sort of keeps this growth perpetuating over a level because in case tomorrow even they would be putting all their efforts in revolutionizing their products, so it will be a constant catch-up game on both sides, but what will be our perpetuating growth strategy?

Jairam Varadaraj: Let me rephrase your question to the extent that I have understood, are you saying how is it that we are able to develop these products in spite of not having a big R&D budget, is that your question?

Aman Shah: That is true, Sir.

Jairam Varadaraj: Now, this R&D as a percentage of sale is a very tricky number, so if you take one of our competitors, they may be spending 2% to 2.5% of their revenue on R&D. Now, we are also spending around about 3% on R&D, but you got to understand the cost of their people which is also calculated into the R&D spend is probably five-six times more than what we pay to our people to our engineers here, so if you factor that in our R&D percentage on revenue is not 3%, it is significantly higher in a normalized sense, so that is one part of it. The second part of it is innovation is not the domain of only large company, in fact innovation happens more if you look at all the literature of innovation, it is small individuals and small companies that are more agile and innovative. Now, large companies if you look at the failure of large companies, it is because you look at the classic case of Kodak, even though they came up with a digital camera, their revenue was so much dependent on selling these film cartridges, they did not move to digital camera, right so large companies have the disadvantage of their installed technology, which is earning a lot of profits to break it is a big thing, so it is not that large companies are more innovative, history has shown repeatedly breakthrough innovation comes from individuals and small companies.

Moderator: Thank you. The next question is from the line of Kamlesh Kotak from Asian Markets Securities. Please go ahead.

Kamlesh Kotak: Jai, couple of points I just want to understand in railway business did you see any material change way up or down because of the current situation that is prevailing?

Jairam Varadaraj: There is definitely a pause their Kamlesh because I think the Government is also evaluating their budgetary allocation to deal with the financial situation in the country, so it is still early days to see how much of the railway budget is going to get a cut so that they are able to release funds for other to handle the current situation, they have cut the defense budget, they have cut a lot of other budgets. In Railways we are waiting to see, therefore, there is a pause so we do not know whether they are going to continue to make that.

Kamlesh Kotak: Same way in the other two pockets which were still in pain, construction and mining and automotive, do you see that the pain will be elongated and we may see the recovery only in the next year?

Jairam Varadaraj: What we are seeing is interesting, construction and mining, there is some activity starting. There are some specific verticals like mining specifically where there is a Government conversations about allowing private mining for all minerals, so we are seeing some mining-related businesses picking up, but construction of course is very, very low.

Moderator: Thank you. Ladies and Gentlemen, that was the last question. I would now like to hand the conference over to Mr. Kamlesh Kotak from Asian Market Securities for closing comments. Sir, over to you.

Kamlesh Kotak: Thank for this very elaborate and insightful discussion, participants also thanks for attending the call.

Jairam Varadaraj: Kamlesh, thank you so much for as always for organizing this. I have tried to be as candid as possible, but the current circumstances are so fluid and we will try to reach out as much as possible when material event happens, we will try to reach out to the investor community to communicate and share our thoughts.

Moderator: Thank you very much, Gentlemen. Ladies and Gentlemen, on behalf of Asian Markets Securities, that concludes this conference call. Thank you for joining with us and you may now disconnect your lines.