

# Varroc Engineering Limited

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VARROC/SE/INT/2022-23/57

August 16, 2022

To,

The Manager- Listing  
The Listing Department,  
**National Stock Exchange of India  
Limited**  
Exchange Plaza, Plot No. C/1,  
G Block, Bandra-Kurla Complex,  
Bandra (East), Mumbai-400051.

The Manager – Listing  
The Corporate Relation  
Department,  
**Bombay Stock Exchange Limited**  
Phiroze Jeejeebhoy Towers,  
Dalal Street, Fort,  
Mumbai-400001.

NSE Symbol: VARROC

BSE Security Code: 541578

**Sub: Transcript of Investor / Conference Call pertaining to Unaudited  
Financial Results for the quarter ended on June 30, 2022**

Dear Sir/Madam,

Please find Transcript of Investors / Conference Call held on Friday, August 12, 2022, in respect of the Unaudited Financial results for the quarter ended on June 30, 2022.

This is for your information and records.

**For Varroc Engineering Limited**

**Ajay Sharma**  
**Group General Counsel and Company Secretary**

**Encl:** a/a



## “Varroc Engineering Limited 1QFY23 Earnings Conference Call”

**August 12, 2022**



**MANAGEMENT:** **MR. TARANG JAIN – CHAIRMAN AND MANAGING  
DIRECTOR, VARROC ENGINEERING LIMITED  
MR. CHRISTIAN PASCHEL – CHIEF EXECUTIVE  
OFFICER, VARROC LIGHTING LIMITED  
MR. ARJUN JAIN – WHOLE-TIME DIRECTOR, VARROC  
ENGINEERING LIMITED  
MR. T. R. SRINIVASAN – GROUP CHIEF FINANCIAL  
OFFICER, VARROC ENGINEERING LIMITED  
MR. BIKASH DUGAR – HEAD, INVESTOR RELATIONS  
VARROC ENGINEERING LIMITED**

**MODERATOR:** **MS. NISHAT VAKIL – AMBIT CAPITAL PRIVATE  
LIMITED**



*Varroc Engineering Limited  
August 12, 2022*

**Moderator:** Ladies and gentlemen, good day, and welcome to Varroc Engineering Limited 1QFY23 Earnings Conference Call hosted by Ambit Capital 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 ‘\*’ then ‘0’ on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Ms. Nishat Vakil from AMBIT Capital. Thank you, and over to you, ma'am.

**Nishat Vakil:** Thank you, Nirav. Good evening, everyone. We have with us Mr. Tarang Jain, Chairman and Managing Director; Mr. Christian Päschel, CEO, Varroc Lighting; Mr. Arjun Jain, Whole-Time Director; Mr. T. R. Srinivasan, Group CFO; and Mr. Bikash Dugar, Head, Investor Relations.

I now hand over to Mr. Tarang Jain. Over to you, sir. Thank you.

**Tarang Jain:** Yes. Thank you, Nishat, for hosting the call, and good evening to everyone. I would like to thank all of you for joining the 1QFY23 earnings call of Varroc Engineering Limited. 1QFY23 has started with a stable outlook for the Indian automotive sector on the back of the forecast of a normal monsoon. The growth is visible mainly due to a lower base of 1QFY22, which was impacted by COVID Wave 2. The semiconductor supply constraints continue to impact the premium 2-wheeler production volumes, whereas the passenger vehicle manufacturers are seeing improvement in supplies.

In India, automotive production for all the segments in 1QFY23 rose on a year-on-year basis due to the lower base of last year, which was impacted by the COVID Wave 2. On a sequential basis, two-wheeler production grew by 8.4%, but other segments fell on a quarter-on-quarter basis due to the cyclicity which we generally see from 4Q to 1Q.

Against this backdrop, we are focused on completing the divestment of our 4-wheeler lighting business in Europe and America as per time line. As stated earlier, this divestment will help the company to strengthen its balance sheet and invest in identified focus areas to drive future growth.

In terms of operations, revenue from continued operations grew by more than 36.3% to Rs. 16,283 million, despite our top customer production only rising by around 1% on a year-on-year basis. We continue to improve our profitability on a sequential basis as gross margin improved by more than 340 basis points. The EBITDA margin also improved by 210 basis points for the continued operations, and it came in at 8.2%.

The operational PBT before joint venture for continued operations has become positive in the quarter and it is Rs. 138.3 million. The reported PBT was impacted negatively by mark-to-market on Forex items of Rs. 96.8 million and a JV loss of Rs. 45 million. The reported PBT is negative of Rs. 3.6 million.

It is heartening to see that all the businesses within our continued operations have shown improvement in EBITDA margin on a sequential basis. The India operations EBITDA margin improved by 20 basis points to 9.9% in 1QFY23. VLS remaining operations EBITDA margin improved by 290 basis points to 1.7%. For the remaining businesses, which is mainly the forging business in Italy, which is IMES. The EBITDA margin improved by 1,730 basis points and came in at 6.8%.

We continue to have strong order wins for new business in 1QFY23 across business units. This will enable us to continue to outperform the industry growth and in improving the profitability. During 1QFY23, lifetime revenue from new order wins is Rs. 14,673 million. And out of that, business wins from EV customers is Rs. 4,837 million.

Profitable business wins, appropriate capital allocation, sweating of our assets, commercialization of our R&D efforts, and control on costs remain the focus of the company. Mass production of traction motors, controllers and the telematics shows the capability of the team to industrialize a new product, first time right. The R&D team also developed the electronic fuel injection for an esteem customer in record time, and the production has started from June 22.

Our effort remains to move to a double-digit EBITDA margin in the next 2 to 3 quarters. The focus on operating leverage and expansion in gross margin across businesses will help us in achieving the same. We remain committed to take the EBITDA margin to 12% and ROCE above 20% over the medium term.

In our financials, the business, which we are divesting is now accounted as discontinued operations and only the profit and loss from discontinued operations is shown as a one-line item in the income statement as per the accounting standards. Please also note that as per accounting standard 105, the assets which are held for sale cannot be depreciated. Thus, the depreciation for 1QFY23 were discontinued operations was nil. Here also, sequentially, we have seen improvement in the gross margin by 210 basis points in 1QFY23 as compared to 4QFY22.

With this, I am now handing over the call to Mr. Srinivasan, our group CFO, who will walk you through the presentation, which is already uploaded in our website and also in the stock exchange.

**T. Srinivasan:**

Thanks, Tarang. Good evening, everyone. You already have the presentation with you, I presume. So I will just quickly take up on some key points. Starting with the highlights for the

quarter. So during the quarter, we started mass production for both traction motor and traction controllers for our anchor customer. And the value of these two products put together is more than Rs. 15,000 per vehicle. We also commercialized electronic fuel injection system for our largest customer in record time. Our R&D team was able to turn around this very quickly, which shows our technological capability. And so this will also lead to other businesses with the customer. So this is a big breakthrough for us.

In spite of, let us say, the market growth as well as the growth in volumes of our broadest customer not being so robust. We still managed to record a 36% year-on-year growth in terms of revenue, which is quite predictable. As Tarang mentioned, the EBITDA for continuing operations improved sequentially by 210 basis points to 8.2%. And during the quarter, we also won new business from various customers, totaling to Rs. 14.7 billion, out of which almost one-third of it was orders from 3 customers for EV 3-wheelers, both EV specific components and also other components like body parts, lighting and so on. So it is very heartening that the share of EV business in our new wins is going up, almost one-third now in the last quarter.

The second slide has overall industry performance volume performance. So the growth you see year-on-year is mainly because Q1 last year was impacted by COVID Wave 2, which is setting in good growth numbers for this year. But if you look at sequentially, slightly different, 2-wheelers still recorded a good growth, but 3-wheelers, passenger vehicle and commercial vehicles actually showed a decline, mainly because in Q4, typically, there is an uptick in volumes because of tax, in tax depreciation, many corporate customers do their purchases in Q4, but Q1 is comparatively especially slow. That is why it is replacing in that.

So 2-wheelers have started the year on a good note, which is very important for us as a segment. So we hope the festival season and going forward, the growth movement will pick up.

In the next slide, you will see a summary of the financials for continued operations. So you see revenue quarter-on-quarter was flat, but we are able to improve EBITDA margin because of our operational realization improved in this quarter. That is mainly because, as we all know, there is a one quarter lag normally between the commodity price increase and the price increase at some customers. So during the last quarter, commodity prices are more or less stable, but we got increases related to Q4 of last year. So this improves EBITDA margin.

That is why you see a better operational PBT. But during the quarter, we also recorded mark-to-market Forex loss of about Rs. 9.6 crores because of the weakening of the euro on the intercompany loan given to the VLS business to support them for the liquidity requirement. In the previous quarter, it was a profit of Rs. 11.9 crores with some mark-to-market at the moment notional.

And the China JV had some challenges in the overall performance still at a loss, but because of the lockdowns imposed in Shanghai and other places, the market volumes have not really picked

up yet. But overall, PBT level, we were close to breakeven compared to incurred in the last quarter and also last year.

In the next slide, you will see the revenue breakdown in a different dimension. From a business unit perspective or a product perspective, PBU or plastic components from the largest part, accounting for more than 30% of the revenue. Lighting, which is a combination of 4-wheeler lighting in India, 2-wheeler lighting in India as well as the global 2-wheeler lighting business, we have in Italy, Romania and Vietnam, together accounted for almost 24%.

The electrical and electronics components in India was about 18%, metallic component, which is transmission-related component for walls together was about 12%. The aftermarket business, what we have mentioned in the earlier calls as well is paying a much faster growth and the profitability margins there is also pretty good. So that has now reached almost 10% of revenue of continued operations, which is a good sign. It is also helping the overall margin improvement for the business. IMES, which is under others for our reporting contributed 4.6%.

On the product segment basis, two and three-wheeler account for 63%, 4-wheeler is 32% almost one-third and the rest is others. From a geographical perspective, India, with the continued operations account for 80% and 20% of the revenue coming from outside India. And from a customer perspective, Bajaj on a total basis contribute to be more than one-third. In India, they are about 50% and the rest of the customers together about 30%.

In the next slide, we are trying to give a blueprint of the performance between the different business units or segments we have. The India operation, which is basically a 2-wheeler focused business, improved EBITDA margin from 9.7% to 9.9% despite top line being flat. The overseas operations remaining in the past, which we are not selling, which is a global 2-wheeler electronics and so on, and also that 4-wheeler lighting business in India together improved the EBITDA margin from a negative 1.2% to positive 1.7% an almost 3% improvement. And other operation IMES also witnessed a turnaround. There we were able to pass on the commodity rate increase as well as the energy cost increase to the customer because compensation prices that also include improving the margins there. So overall, for the continuing operations that resulted in a 210 basis point margin improvement.

Going a bit to net debt level, it remain kind of more or less constant over the last 3 quarters. So maintain this Rs. 27 billion on a net debt basis. A lot this about Rs. 1,000 crores in India, the rest is abroad. That will be fully repaid excluding working capital like we have communicated. That is the plan.

On the next slide, we have given kind of some insights into the new order wins. The new order wins will contribute revenue of, let us say, Rs. 212 crores in current year and Rs. 780 crores coming from the subsequent year. And if you fix the orders between EV and ICE vehicle, one-third of the new orders related to from EV vehicle manufacturers and the balance would have

coming from ICE manufacturers. Bajaj accounts for about one-third, the non-Bajaj in line with the revenue share and the new order wins in the two and three-wheeler segment is about two-third and one-third is from 4-wheeler, which is an encouraging sign for the 4-wheeler with both the new businesses and revenue is going up, and 4-wheelers typically have a better margin structure than two and 3-wheelers.

Then the next 2, 3 slides, we have tried to give you an insight into all the components we have available we are able to offer to the customer specifically from the EV segment. Obviously, had gone through in the previous quarters as well. The main highlight was the commercial production of traction motor and controller switch started during this last quarter.

And the following slide gives a status on the divestment. So we are on track to close the transaction by end of September. The shareholder approval was received sometime back. Lenders approval is an ongoing basis, but all lenders have supported. So the documentation is in progress. From a regulatory perspective, we have got the regulatory approval in 3 out of the 4 geographies, U.K., European Union and Morocco. Mexico is a pending one, which is also expected to come through end of this month or early next month. So right now, we are able to close the transaction by end of September.

The following slide gives a big overview of the financials for the discontinued operations breakup. So mainly we see the improvement is because of that we stop depreciation on the assets on the discontinued operation under IndAS 105. Otherwise, performance comparable to the previous product. So that is briefly quick recap of the performance. Now we can go ahead with the questions.

**Moderator:** Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Aditya Jhawar from Investec. Please go ahead.

**Aditya Jhawar:** My first question is on VLS. So Srini mentioned that the transaction is expected to close in September. What about the cash flows by when we would see the cash flow coming to Varroc? And how much amount we have budgeted for cash burn? And is it in line with our estimates? And related question is that we also see that there would be a fundraise of about to the tune of Rs. 500 crores, what would be the objective of this fundraise?

**T. Srinivasan:** Fundraise part is purely an enabling resolution. So there is no specific plan to raise the funds at the moment. Specifically, if we do not take approval now in AGM then lead time to get approval at the time is more. That is why we are taking just an enabling thing. There is nothing more to it.

From a cash flow perspective, the money net of the escrow account and everything will come to us immediately, net of loan repayments and so on. So in sometimes early October can get the amount.

- Aditya Jhavar:** Okay. My second question is on new order wins. So it is encouraging to see that we have one order for electric vehicle from other than our anchor customer. So for the 2 new customers other than our anchor, if you can highlight that what is the order win? Is it traditional product, existing product or there are EV components?
- Bikash Dugar:** These are our traditional product only. But the encouraging thing is that we have both incumbent as well as new customers on the EV side. So new and both incumbent customers are there for our product. So we have started engaging with them for our EV product related. So sooner or later, we will get orders for those also.
- Aditya Jhavar:** I just wanted to check on one thing. So we also mentioned that the traction motor and controller for our anchor customer, we will be ramping up production. But when you look at Slide #13, where we have quantified that total revenue from EV could be at about Rs. 1,000-odd crores. Here, we do not see mention of traction motor and controller?
- Tarang Jain:** It is mentioned out there, traction motors and controllers on next slide.
- Aditya Jhavar:** I mean, the order that you have quantified Rs. 700 crores and Rs. 300 crores, it is not against traction motor and controller?
- Tarang Jain :** No, I think that is just a combined number.
- Moderator:** Thank you. The next question is from the line of Ashutosh Tiwari from Equirus Securities. Please go ahead.
- Ashutosh Tiwari:** So firstly, if I look at this IMES operations where margins are improved YoY, QoQ, while revenues have dropped. Is it sustainable? What do happen over the year?
- Bikash Dugar:** So yes, the margins are more or less we would like to sustain it because we have got some customer price increase of last year in related to the energy cost and the metal prices, which have gone. Unlike in India, where the pass-through happens on a quarterly basis, in Europe, it is on an annual basis. And now we have got that price increase and we would like to sustain this kind of EBITDA margin and see that how can we utilize our capacity further to further bring the efficiency into that business.
- Ashutosh Tiwari:** But does this EBITDA also include some compensation for last year or this is normal for this quarter only?
- Bikash Dugar:** This is normal for this quarter.
- Tarang Jain:** That is something which is normal. It is a normal margin.



**Ashutosh Tiwari:** And secondly, so VLS remaining operations there also, like, say, 1.7% margin this year despite almost a season higher revenue versus last year. So how should we look at those business? How should the margins improve over a year?

**Tarang Jain:** So see, the revenues here are coming basically from our lighting business, our two-wheeler lighting business abroad, which has got plants in Italy primarily and Vietnam, which continues to have a double-digit EBITDA. Our electronic business in Romania is on a ramp-up stage. And going forward, I think once it has capacity I mean we will see EBITDAs going up, up to probably up to 8%. And this is something which will mean also PAT positive can operate performance from the EBU, and this is something which should happen probably in the coming months.

And thirdly is our VLS 4-wheeler lighting business in India, which also, I think we will see improved numbers. Here also, our target is that in the coming quarters, few quarters that we reach a double-digit EBITDA. So I think with all these together, I think going forward in the next quarters, we will be striving that we take this EBITDA up closer to a double-digit kind of a number for the VLS remaining operations, which are going to be our continued operations.

**Ashutosh Tiwari:** Okay. And in India, is there a possibility of margin improvement from here?

**Tarang Jain:** So we will be going up because we see our revenues increasing in the second quarter right from July. So here, we will be definitely at a double digit, a double-digit EBITDA. And here, of course, like we have said before also in the medium term, we will be reaching this 12% EBITDA.

**Ashutosh Tiwari:** The point is that despite this EBITDA improvement because of higher depreciation charges that we have now in remaining operations still, I think at the PBT level, the margin is not very good. So depreciation will also increase going there and how should we look at it? Like from the PBT margin improve significantly from here?

**Tarang Jain:** Yes. So for sure because see here, the way I see it is that the EBITDA margins are going to grow across and especially in the bigger businesses of India as well as the continued operation of VLS, we will see significantly improving margins. We will see from a PBT point of view, we will see there are interest costs both the transactions will drastically reduce, which is quite high today. So that is something which we see going down kind of considerably. So therefore, we are looking at obviously a good PBT performance post, I think, the transaction this thing happening.

And here also, even in this June quarter, as you can see, we had a foreign exchange loss of about Rs. 97 million, which also was the reason why we had a small loss of Rs. 3.6 million for this quarter. Otherwise, we were actually our performance, gross of that Forex loss was positive.

**Ashutosh Tiwari:** And lastly, I have missed the initial part of the call. But in terms of net debt after completion of dimension, how should we look at it, like say, considering whatever losses you are making right now and realize discontinuing the operations?

**Tarang Jain:** So we have already mentioned earlier that we will be net debt negative. So that is clear. So we are not just so we are going to be net debt negative if we have to take of a repayment of all the loans and also if we do not repay 100% loans because there is some working capital loans, we will have cash in the books. So we will be net debt negative on the whole as a balance sheet.

**Ashutosh Tiwari:** Yes. But will the cash be like say, higher than Rs. 300 crores, Rs. 400 crores or it will be just getting net cash position?

**Tarang Jain:** No, last time, we had said that we will be about Rs. 200 crores-plus, but there will be a little bit of a cash burn because that we do see because of the inflationary conditions in Europe. So that is something which should be there. There will be some adjustments. So probably a Rs. 200 crores could go down to Rs. 150 crores or things like that. And so we have to see how things pan out. It is a question of another 1.5 months. So it is not that long also at the moment.

So we do see some this thing. But the main thing is that we will be net debt negative. That is our statement. A little bit here or there is something we can experience and we will come to know September end really where we are. But we already know our situation where we are today.

And going forward, obviously, the focus is going to be a lot on the India side because that is going to be our major revenues. And there, we will see and there we have a strong growth potential going forward. We have a lot of business wins. And here, I mean, unlike probably maybe global markets, but in India, we continue to do kind of well. And here, we will see definitely improving margins also as we go along.

**Moderator:** Thank you. The next question is from the line of Abhishek Jain from Dolat Capital. Please go ahead.

**Abhishek Jain:** So what is your revenue guidance for the FY '23 and '24?

**Tarang Jain:** See, we have said like this year for our perimeter, we have said that not counting China because China is still in a JV that we will be at about Rs. 7,000 crores. And then we have said for the coming years, I mean, whatever the market growth is, we are going to be 8% to 10% more than the market growth. So we are going to perform better than the market by at least 8% to 10%. So that is our guidance for the coming 3 years.

**Abhishek Jain:** Okay. And the VLS remaining operational, which revenue stands at around Rs. 30-35 million on a quarterly basis. So what is your outlook for the revenue and the margin going ahead? As you have mentioned that you are looking a margin of 8% versus the 1.3% right now. So what is the road map for that?

**Tarang Jain:** So there the roadmap is that we will reach between 8% to 10% in the coming 2 to 3 quarters, we will achieve that percentage to EBITDA percentage to revenues.

- Abhishek Jain:** And what would be the revenue size for FY '23 from the VLS remaining operations?
- Tarang Jain:** So here India, I think we had said close to about Rs. 5,500 crores and the balance without China was Rs. 1,500 crores. That is the breakup.
- Abhishek Jain:** Okay. And overall margin would be at 10% to 11% for FY '23?
- Tarang Jain:** Yes. So double digit is what we are trying to push for.
- Abhishek Jain:** Okay. And sir, currently, 4-wheeler contribution is around 33%. So what mix you are targeting going ahead? If you can throw some more light on the winning new business in the 4-wheel lighting system and other part like in the polymer and metallic side?
- Tarang Jain:** Yes. So see, our focus is definitely when it comes to the India market, definitely, we expect future growth towards our India lighting business and also on the plastic side, the plastic interiors where we do quite a few products. We have also a lot of new technologies here, like 2K molding. We have some very unique parts like the roof rails, which are there for SUVs in the growing SUV market. Here, both for lighting as well as for our plastic interiors business, we see a huge growth. And it will be double-digit growth in the car market under these two segments.
- Other than that, we are also looking at some of the transmission parts, which are engine agnostic, even something to do with the EV whether it is two-wheeler shafts or there are other parts. So we are discussing with various customers on the export side, which is also a higher-margin business. And here, we are looking at, of course, the domestic market, but also more importantly, in the export market where as metallics is concerned. So probably going forward in the metallic side, we could in the coming years, see a shift more towards 4-wheeler as compared to the 2-wheeler as we move along.
- Abhishek Jain:** So recently, you have won the business for the 4-wheeler lighting system in India. I think it is for the Mahindra & Mahindra and for the Tata motors. So if you can throw some more light on the winning new business in the lighting system and what is your revenue right now from the lighting part only?
- Tarang Jain:** So India lighting business, you can say we will be Rs. 500 crores-plus in revenues in this financial year. Our major customers in 4-wheeler lighting business today are the Volkswagen Group, Mahindra & Mahindra and Renault Nissan. and also Tata. Tata is smaller.
- So here, we are presently focusing on these customers. Of course, we are also looking at winning business with a few other 4-wheelers where we are strongly engaged. So today, actually, frankly speaking, we are very well utilized in both our plants when it comes to both Pune, Pune being a larger plant 80%, and 20% in Chennai. And here, we are very much engaged with our customers for future business wins.

And like I said, in lighting business also with these customers and a couple of other new customers whom we are talking to, which I cannot name at the moment, we are looking at a double-digit growth also in our lighting business going forward in India.

**Abhishek Jain:**

And sir, my last question is related with your CapEx plan for the next 2 years?

**Tarang Jain:**

So I think that when it comes to India, I think we are going to be at probably approximately about Rs. 200 crores or Rs. 2,000 million year-on-year. That is what we are looking at for the kind of growth I have mentioned. And abroad also, there will be a certain level of investment for the continued operations, which also could be another probably maximum it could be about probably up to probably Rs. 50 crores to Rs. 500 million, up to.

**Abhishek Jain:**

So Rs. 250 crores sort of the CAPEX will be in the next 2 years, right, sir?

**Tarang Jain:**

Yes. I mean, per year investments.

**Abhishek Jain:**

Okay. Per year. And as you are targeting around Rs. 1,000 crores kind of the revenue by FY '25 in the EV segment. So most probably, the CAPEX would be at the higher side. to get this business?

**Tarang Jain:**

No, we have already created a lot of capacities in our electronics factory on the SMT lines, and we also have a good capacity on the motor side. But yes, I mean, what I am talking about the growth, even if it is for the EV side, it will be within this investment. So it is mostly I think more of our investments will go more towards our plastics business and our electronics business. That's where we see major investments going.

As we go along, it will be little bit less on the metallic side, we will leveraging more existing capacities to kind of utilize the capacities better, including for 4-wheeler components in India or for exports. So we have still enough capacities available.

**Abhishek Jain:**

Okay. And sir, after the closure the deal, so you are talking about that you will be a net cash company. So there would not be any debt on the books, right, sir? I mean in India business as well.

**Tarang Jain:**

On a net debt basis, yes, on a net debt basis. Now we are not going to stop out of working capital lines. The working capital line will be there but I am saying to the extent cash available in the system. But we are not going to eliminate all our working capital limits. That will continue.

**Abhishek Jain:**

Okay. And what would be the size of the working capital you would be required?

- Tarang Jain:** I mean out of that, let us say, we have a net debt of the working capital continues working capital. I think it is normally Rs. 300 crores or so. Overall, I do not think it is going to be more than Rs. 300 crores or Rs. 400 crores that is the max I am saying on an overall basis.
- T. Srinivasan:** So adjustment between enterprise value and?
- Tarang Jain:** No. This is on a continued basis, what is the working capital.
- T. Srinivasan:** This is typically our receivable front, between 46 to 50 days. The inventory level in India is around 30 days on average, and payables are around 60 days. So that is the normal working capital cycle we have. So you can adjust to the last thing.
- Moderator:** Thank you. Next question is from the line of Sachin Kasera from Svan Investment. Please go ahead.
- Sachin Kasera:** I just had two, three queries. One was you mentioned that while the net cash would be Rs. 200 crores post the transaction. The cash on the balance sheet will be a little higher because you will have some short-term working capital debt. So consider that normally, the yield that we get by putting it in treasury is normally lower than what you will pay on the negative carry. So do you have any perhaps because you mentioned that CAPEX is only Rs. 250 crores, which you may be able to fund from internal accrual? So this Rs. 400 crores, Rs. 500 crores of cash that will be remain on the balance sheet post the transaction, what is the thought process?
- Tarang Jain:** I mean that is something we will come out with some kind of a policy, I think, probably.
- T. Srinivasan:** First of all, last 3 years, we have not paid any dividend. I think it is time that we pay out some dividend, give some cash back to shareholders. So we will to have to access this from the cash what we have is number one. And secondly, some way it is a good idea to keep some liquidity in the balance sheet. We do not want to be cut to cut come to the cash in the liquidity, which we learned the hard way during the COVID time. I think some liquidity buffer because you can never be sure what is around from the industry perspective, market perspective, from the economic perspective so some contingency buffer is always good.
- The immediate focus is to now close the transaction so that we can move on with a strong balance sheet. And then we are parallely working on our strategy 2030, which also we had hoped to be ready in the next 2 to 3 months. And then we will have a clear road map of how we are going to deploying the, let us say, the capacity we have on the balance sheet to invest.
- Moderator:** Thank you. The next question is from the line of Saurabh Jain from Ambit Capital. Please go ahead.

**Saurabh Jain:**

Yes. Sir, I just wanted to understand about the industry outlook. So if you could shed some light on how is the demand right now in the industry? Do you see the demand coming back strong or the uptick in the volume is largely due to the pent-up demand? And also, if you could shed some light on the European demand scenario, given that we are seeing high inflation and other political headwinds over there, so any color on those fronts would be helpful.

**Tarang Jain:**

So on the India side, we definitely see a kind of a strong demand pull is there. Today, the limiting factor, frankly, is only the chips. And that I can say for a 2-wheeler sector and even the 4-wheeler sector. We see a strong demand for whichever customers, if their volumes are down is largely only because of the chips.

And I see that in this year, provided the chips are available for the various electronic products. I do not see really a problem in achieving a double-digit growth for the industry. So this, I clearly feel. So even in the first quarter, if there were issues in the growth in volume, it was largely overall because I feel because of chip shortage, not because of the demand. That is our view and going forward, we will have to see how things pan out.

But anyway, even in the coming years, I do feel, I do feel that there will be a growth in the Indian market of at least 7%, 8%. This is the way I am quite optimistic about the market growth going forward, both in 2-wheeler and the 4-wheel sector. We should not compare the India situation with the global situation is very different. We have our own demographics here. We have our own situation here, which is quite positive. So irrespective of the issues, we have inflation in India also.

Yes, it might affect a certain segment. But then overall, we do see a good growth because there is a demand, and I think that the monsoons also this year are quite good. And this is also going to help demand in the coming season. So I do see a good double-digit growth in this year in the remaining quarters. The first quarter was little muted. Yes, there are chip shortages still there, but it is improving.

So I do see a good growth in the Indian market, which will be for us the major play. When it comes to the European market, yes, I mean, it is impacted, I would say, I mean, by the Ukraine war. But there I do not really see and maybe Christian can also elaborate. I do not see really any softening of any volumes there or demand because of the moment at least I mean, I do not see it but there is inflation. So there are cost pressures there. But I do not see really at the moment a problem of demand, at least in this year, in spite of so many things taking place, especially the war. Maybe Christian, you can maybe elaborate on the volumes in Europe?

**Christian Päschel:**

Yes, so as you are saying, so the global situation, especially in Europe as well depending on the chip shortages. We are improving here but we have high inflation costs. We have to absorb the OEM as well as the war in Ukraine is intensifying.

**Saurabh Jain:** And secondly, on the margin front, you did mention that we had a good 340 bps improvement on the gross margin front. And the primary reason, as you mentioned, was the further inflation pass-through that we received in this quarter. But if you could just help us out quantifying as in how much of this reported is slightly due to the pass-through effect? And have you seen any material improvement because of the correction in the commodity prices as well?

**Tarang Jain:** See, basically, as you know, we had got an overall 8%, 9% increase from January of '22 from all customers for VLS. Now in fact, what has happened is that so that has, of course, resulted in an improvement in the gross margin. But in fact, the gross margin should have been better than what we have actually achieved so far, but the problem was that there has been an inflation in the commodity prices. So in spite of that, there was an improvement in gross margin, otherwise, it could have been much better in our view.

And also, after the gross margin also, there was an impact mainly because of some labor cost increases and importantly, energy costs. They have gone up quite a bit because of the war. And that has resulted in the kind of performance in the VLS discontinued operations. They have been a little bit impacted, but we are not seeing really a problem in the overall volume. The demand has still been there. It is just that there has been the price increase, which we are expecting, if there was no war, I think the performance would have been better because there will be not so much of inflation, which we are experiencing.

But having said that, we have again asked some of our customers for some price increases from April, and we do expect a settlement of some price increases from April onwards in the month of September because unfortunately, August is a holiday period in Europe. And of course, all our decision makers are also on leave at the moment.

**Bikash Dugar:** And in India, the gross margin has also improved because of the internal efficiencies, which we are trying to bring in the system, be it our sourcing, be it addition value engineering. So that we are continuously doing and that we will continue to do for the rest of the year so that our gross margins further improves from this level.

**Moderator:** Thank you. The follow-up is from the line of Sachin Kasera from Svan Investments. Please go ahead.

**Sachin Kasera:** Yes. Just one question on the lighting part of the business. So if we both in 4-wheeler and 2-wheeler, if you could tell us where do we stand in terms of the LED part of the Lighting business? How do we see the market evolving? And what is the type of market share gains we are looking there in the next two, three years?

**Tarang Jain:** Yes. Maybe Arjun, you can answer that.

**Arjun Jain:**

Yes. So I think from an India specific standpoint, I think really today, if you look at whether on the 2-wheeler lighting side or the 4-wheeler lighting side, I think in the premium segments of the market, I think we are doing very, very well.

Now when I say premium segments, what I really remain is if you look at 250 CC plus, where you really have full-fledged Class D homologated headlamps, today, we occupy all Bajaj, KTM, or other KTM brands as well also. And I think we do fairly strong volume there. Even the new Pulsar that have launched, we supply the bi-functional LED there as well.

So from a passenger car standpoint, I think a lot of the new models that have launched over the last 12 months, especially the XUV700 and all the Skoda and VW models that have launched, we do a very large portion of the lighting. So XUV700, we do almost all the lights that are around that vehicle.

So when we think about the technology that we already have on the road, I think it definitely places us in a very good position as more and more vehicles move towards LED. Ultimately, today, we are fully localized whether in terms of design, development, manufacturing for these technologies, we are also vertically integrated with the electronics manufacturing, which is really around 50%, 60% in the now. So we feel we are in a very competitive place and I think that is really what we would have moving forward as well.

**Sachin Kasera:**

You mentioned three customers. So these are probably three, right now we are working on the LED? Or are we also working with some newer clients? And hence, the client addition could be there for two and four-wheeler as you go ahead.

**Arjun Jain:**

Okay. So if I talk about passenger car, our customer base is quite competitive. So I spoke about Mahindra and VW because they are the largest customers. But we also do LED headlamps and tail lamps for Renault Nissan. So both magnite and Kiger. We also have LED contract with Tata, especially in terms of DRLs like on Harrier and Safari.

We also have other non-LED businesses also with all of these customers, right? But from a 2-wheeler perspective, other two-wheeler, let us say, we do Bajaj, KTM, Ducati, Hero. So we truly have a very comprehensive portfolio across technology segments. The question was more specific about LED. So I spoke more about the customers where we are supplying high-end LED product.

**Sachin Kasera:**

Can you assure your LED market share in 2-wheeler and 4-wheeler? And how do you see that in the next 3 years?

**Arjun Jain:**

So honestly, I do not have numbers on the top of my head. Again, I think when you think about the LED market I will absolutely share that.....





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**Sachin Kasera:** Are you in the top 2 or top 3 players or how many players are there if you can just. And how are we positioned if not a specific market? We are #2, #3, #4 in LED lighting today in both 2- and 4-wheelers?

**Arjun Jain:** So I think 2-wheelers, especially if you think from a value perspective rather than a volume perspective, I would say we are definitely in the top 3. Passenger car, we are basically the high supplier. So where a top 5, the exact number, I would not know the top of my head right now.

**Sachin Kasera:** Okay. But do you even especially on during internal budgets where we are looking at some significant market share gains in this segment in LED two and 4-wheeler segment?

**Arjun Jain:** So I think for us, again, I would repeat, right? I think we are in a good place because we have been early entrant and a market leader in terms of bringing this technology to the Indian market, right? And I think when we look forward, we would expect that customers will trust the supplier, we have already done it rather than the supplier whom we are hoping to do.

So that is a trend that we hope to find a product on the road back to whether we read in all these magazines like Autocar or Overdrive, et cetera. We have all the lights we supply are be extremely, extremely well whether from a performance standpoint or reliability standpoint, again, we do very well. So the expectation is that, that is a trend we will be able to capitalize on further.

**Sachin Kasera:** Sure. My second question is regarding the overall evolving of the auto ancillary architecture in India and globally. As we see the world ahead, it is becoming more and more about engineering technology software. And hence, it has also become imperative for all the auto ancillary players to spend a significant portion of their revenues on R&D and innovation. So where are we in that journey today? How much do we spend or intend to spend on R&D and innovation as a percent of sales in absolute number? And how do we see that number in the next 2 to 3 years?

**Arjun Jain:** Should I take this also or?

**Tarang Jain:** Yes.

**Arjun Jain:** Okay. So I think I can speak more specifically about India and I think anybody else on the call can also add about the rest of the world and the continued perimeter. But I think in terms of engineering, I think really as we have always spent on engineering. It is not a new thing, right? We have always been self-sufficient when it comes to technology.

So almost all the products we see in the road, all the products that we supply is technology that we have developed in ourselves. Now of course, over the last few years, whether as a result of BS-VI and Euro-VI coming to 2-wheeler and also now with EV, there has been a need to drive further investment. But in my view, I think we have already done that.



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And so in a lot of ways, this investment has already been driven. Of course, as technology continues to evolve, we will stay with it because for our customers, ultimately, we are the supplier. And I think both our CFO and our CMD talked about how we were able to ramp up a fuel injection system in 3 months, and we supply 50,000 a month now. So definitely, I think the technology capability is something that we have always had. We built on further and something like by our customers.

**Sachin Kasera:** That's fair. But I was looking more for some numbers first. So if you could tell a number of engineers in R&D innovation and how much do we spend yearly and what is the intent next 2, 3 years? That would be more helpful.

**Arjun Jain:** So number of engineers today, I would say, at the Indian Engineering Center for electric-electronics alone would be somewhere around 450. I think globally we will continue perimeter add approximately 750 engineers. In terms of the total R&D spends, I would not know that number on the top of my head.

**Tarang Jain:** It will be about 2%. I think in our perimeter, now it will be around 2% to 2.5% of revenue.

**Sachin Kasera:** And we intend to keep it there? We intend to increase it as a percentage of revenue going ahead?

**Tarang Jain:** We do not need to increase it. I think this is enough.

**Moderator:** Thank you very much. I now hand the conference over to the management for closing comments.

**Tarang Jain:** So I just want to thank all of you again for joining in, listening to us and asking your various questions. The trust and faith of our stakeholders is what motivates us to pursue excellence in our day to day life. So thank you very much.

**Moderator:** Thank you very much. On behalf of Ambit Capital Private Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.