Transcript

Conference Call of Blue Star limited

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Presentation Session

Moderator: Good morning ladies and gentlemen. I'm Shirley, moderator for this conference. Welcome to the conference call of Blue Star Limited. We have with us today Mr. B. Thiagarajan, Executive Vice President and Mr. Vir Advani, Executive Vice President of Blue Star Limited. At this moment all participants are in listen only mode. Later, we will conduct a question and answer session. At that time if you have a question, please press * and 1 on your telephone key pad. Please note this conference is recorded. I would now like to hand over the conference to Mr. B. Thiagarajan.

B. Thiagarajan: Good morning ladies and gentlemen, this is B Thiagarajan. I have with me Mr Vir Advani and we will be giving you an overview of the results for Blue Star Limited for the quarter ended September 30, 2008.

The following are the financial highlights for the Company for the *quarter*

- We reported a Total Income of Rs 646.58 crore for the quarter ended September 30, 2008, representing 18% growth over the corresponding quarter in the previous year. Net sales for the quarter at Rs 646.54 crore were also up by 18% over Q2FY08.

- For the quarter, Gross Margin declined from 24.2% to 23.0%.

- Operating profit (PBDIT excluding Other Income) for the quarter at Rs 68.97 crore marginally increased as compared to the Operating Profit of Rs 68.41 crore earned in Q2FY08. The Operating Margin decreased from 12.5% in Q2FY08 to 10.7% in Q2FY09. The Company anticipated a decrease in Operating Margin in Q2FY09 due to the sharp increase in raw material prices, specifically steel and copper, in May 2008. This necessitated a price increase which came into effect towards end-July 2008. Therefore, margins in most of the orders executed in Q2FY09 were adversely affected. While the raw material prices are now under control, the sharp depreciation of the rupee is a concern area. However, we have effected the price increase for most of the products we are dealing in.

- Given the economic environment, it is the intention of the Company to focus on cash flow and efficient working capital management. It has been closely controlling the deliveries and job completion of projects rather than billings. Further, infrastructure projects have a longer execution time. Due to these factors, the billings are slower in comparison to the inflow of orders.

- Net profit for the quarter was Rs 44.95 crore, declining marginally over Net Profit of Rs 45.97 crore earned in Q2FY08.

- The Earnings per Share (face value of Rs 2.00) for the quarter was Rs 5.00 as against EPS of Rs 5.11 in Q2FY08.

- Carry Forward Order Book as on September 30, 2009 increased to Rs 1555 crore compared to Rs. 1031 crore as at September 30, 2008, representing an increase of 51%.

- Order Inflow during the quarter grew from Rs 591 crore in Q2FY08 to Rs 801 crore, an increase of 36%.

I will now spend some time on each of our lines of business and give you both financial as well as operating highlights for the quarter.

The central airconditioning and electrical contracting business, collectively called Electro Mechanical Projects and Packaged Airconditioning Systems grew by 19% during the quarter. Segment results declined by 4% in the quarter compared to the corresponding quarter in the previous year. While the difficult economic situation and the liquidity crunch in the market place adversely affected certain segments such as builders and retail, the Company witnessed enhanced demand from infrastructure segments such as airports, power plants and metro rail apart from hospitality, healthcare and IT SEZ segments. During the quarter, Blue Star booked the single largest order in its history from Delhi Metro Rail Corporation Limited (DMRC), valued at Rs 104 crore for the total airconditioning works including Environmental Control System and Building Management System for 7 metro stations and associated tunnel sections of Phase II of the Delhi MTRS Project. You may recall that Blue Star had successfully executed the airconditioning projects of 3 stations for DMRC in Phase I, and this repeat order is a result of the positive experience that DMRC had with Blue Star. The Company's eco-friendly range of VRF Systems launched in Q1FY09 continued to perform very well in the market place. The VRF technology due to its intelligence and energy efficiency is evoking a great interest in the country, over conventional systems. Blue Star is India's first and only manufacturer of VRF systems and has significant advantages over its foreign counterparts including its ability to handle high ambient temperatures and faster delivery. The Company registered significant growth during the quarter in this product category driven by demand from premium residences, offices, hotels and hospitals. Blue Star is steadily increasing its market share in this market which was a Japanese-equipment stronghold, and is now the No 2 player, with a market share of over 20%.

The Cooling Products segment registered a good growth of 25% driven by sales of the newly launched star-rated split airconditioners as well as commercial refrigeration products. Segment results grew by 35% during the quarter.

The Professional Electronics and Industrial Systems business has an innovative business model of a system integrator and value added re-seller. During the quarter, while revenues declined by 4%, segment results registered a healthy growth of 26%. The topline of this business is predominantly commission income and domestic value addition since most of the equipment is sold to customers on a high-sea basis by its Principals. Also, given the nature of the business, quarterly performance is not a true indicator of the overall performance of the business. The prospects of this business continue to be good.

In conclusion, the gloomy economic outlook and liquidity crunch have affected most companies across the globe. Considering the volatility of the market place, Blue Star has been selectively pursuing segments which offer profitable growth opportunities. In addition, the Company continues to focus on cost control measures and is managing working capital efficiently. Blue Star has demonstrated its ability to rapidly adapt seamlessly to the external environment in the past and we are optimistic of producing a good performance over the next few quarters.

With that ladies and gentlemen, I am done with my opening remark. I would like to now pass it back to the moderator, who will open up floor to questions. Between Vir and me, we will try and answer as many questions as we can. To the extent we are unable to, we will get back to you all as well. With that, we are open for questions.

Question and Answer Session

Moderator: Thank you sir. Ladies and Gentlemen we will now begin the question and answer session. If you have a question, please press * and 1 on your telephone keypad and wait for your turn to ask the question. If your question has been answered before your turn and you wish to withdraw your request you may do so by pressing # key.

Our first question comes from **Mr. Nirav Vasa of Gupta Equities.**

Nirav Vasa: Hello?

B. Thiagarajan: Yes, good morning.

Nirav Vasa: Good morning sir. Sir, can you throw some light on the order of 1555 crores, how much of it would be from the domestic and from the international?

B. Thiagarajan: Predominantly you can take it as 99% from domestic market.

Nirav Vasa: Okay. And rest would be from the international market.

B. Thiagarajan: That is right, very negligible.

Nirav Vasa: Okay. And sir I would like to know what has been the interest rate for the company, for the working capital?

B. Thiagarajan: You are asking the cost of capital.

Nirav Vasa: Yes.

B. Thiagarajan: No, we do not disclose that actually. All I can tell you is that, the interest has gone up substantially, which is basically due to capital employed increase predominantly in debtors and the inventory.

Nirav Vasa: Apart from that, sir, this…

B. Thiagarajan: Apart from that interest rate also is up by around, in Q2 it would have been up by at least 4% to 5%, in Q2 alone.

Nirav Vasa: Okay. And sir, this order book of close to 1500 crore rupees, in how much time will this order be executed?

B. Thiagarajan: Very difficult to say. Normally it used to be around six months of time, but right at the moment our decision is to focus on the efficient working capital management and not create any doubtful or bad debts. So we are making sure the customer has got money, the project is fully secured. So our primary task now is to focus on cash flow. It is quite likely that it will be, my guess is that it can be even 12 months of time. Moreover, infrastructure projects like Metro Rail and all, have got a long gestation period.

Nirav Vasa: So approximately sir, would it be right to conclude that around nine months it will take for the execution of these orders?

B. Thiagarajan: Yes, 9 to 12 months you can say.

Nirav Vasa: Sir, and apart from that sir, can you please throw some light on your strategy for hedging of metal components, because there have been quite some volatility. Copper prices as of now is at an all time low. So any specific strategy that the company is pursuing in order to insulate from the volatility in metal prices?

B. Thiagarajan: Not exactly. Right at the moment we are more concerned about the volatility of rupee rather than metal prices. The metal is coming under control, we have a feeling that it will further go down, and we are in the process of putting in place a policy with regard to hedging against foreign exchange fluctuation.

Nirav Vasa: Sir, but as of now, you just informed that you have just 1% of your order, which is from international. So as of now, if just 1% of the orders are from international aspect…

Vir Advani: It is largely because we are a net importer of raw materials and input, so which is why foreign exchange hedging is very important for us.

Nirav Vasa: Absolutely sir, I get your point on that.

Vir Advani: It is not about orders in hand.

Nirav Vasa: Okay sir, I get it. And sir…

Vir Advani: And as far as metal hedging is concerned, you know, we buy steel locally, steel and GI and it is not advantageous to hedge locally and therefore we have to give an open position on that. The issue around metal hedging is actually because we don't buy that much pure raw material, there is of course copper pipes which is LME connected, which we can look at, but we don't buy steel in large volumes. What happens is that most of the components we buy are connected to steel, whether it is compressors, motors, pumps, things like that. And that obviously you can't hedge from a commodity perspective. You can only do it from a foreign exchange perspective. For the company, foreign exchange hedging is more important right now.

Nirav Vasa: Sir, as of now, what is your forward cover that we have, approximately can you throw some number on that?

Vir Advani: No, we can't. We have just put some procedure in place, just about three weeks ago, and we were actually unhedged until now. So we have been negatively impacted by that with the rupee moving up to 50, but going forward we are going to be locking in. We just got board approval to do certain things on that, so I am not at a liberty right now. Probably by the next quarterly review, we will be able to tell you our hedging policy.

Nirav Vasa: Okay sir. Apart from that sir, these orders which are there on hand, are you facing any request for delay from any of your customers?

B. Thiagarajan: As of now, No. See, as of now two things are through. One is, we do not have any cancellations so far, two, there has not been any request formally from the customer to delay the delivery, except in case of some telecom shelters - very, very negligible amount of telecom shelters. But, proactively we are making sure that the payment pending against a project is released or for a proforma invoice the payment is readily available with the customer. Unless that is there, we are not going ahead and delivering. But the fact of the matter is, there is a money problem with most customers.

Nirav Vasa: Absolutely..

Vir Advani: So as far as our builder work is concerned, we are being very, very cautious about delivery and therefore it is an automatic slowdown as it were all slowing of the projects. Corporate customers are still in better shape, but even there we have to manage delivery to cash, so that's what we are focused on right now.

Nirav Vasa: Okay. And sir while taking new orders, are there any additional steps which are being taken by the company to ensure that the payment by the customer is prompt?

Vir Advani: Not prompt, but we have made payment terms much more stringent. We are asking for more money upfront and at least the orders that we are booking now, we are being very careful about what orders we accept. #1 point being, in terms of payment, we are willing to let go of margin if required, but control the cash. And most customers are willing to give us, if there are corporate customers, they are willing to give us better terms of payment and that's what we are focused on. But you can't, there is only so much you can do to guarantee, there is no way to guarantee your payment obviously.

Nirav Vasa: Okay. And sir in the second business division that is cooling products, you just informed that you had launched new products and sir, going forward any new product launches are there in the pipeline?

B. Thiagarajan: Not exactly. See, at this point of time we will not be interested in launching any new product, at least in Q3. Before summer, in cooling products, there maybe certain new products. So right at the moment, the environment is not conducive for launching any new initiatives or new products at all. Our focus will be to improve the operational efficiency.

Nirav Vasa: Okay sir. Majority of my doubts are cleared. Thank you very much.

B. Thiagarajan: Thank you.

Moderator: Our next question comes from **Ms. Kirti Dalvi of Enam AMC.**

Kirti Dalvi: Good morning sir.

B. Thiagarajan: Good morning.

Kirti Dalvi: Sir I wanted to know, we have booked 18% top line in this quarter, were there any execution issues on that front? We had the order book of almost 1422 crores, if I am not wrong, at the beginning of the quarter.

B. Thiagarajan: Yes, so your question is whether there was any execution…

Kirti Dalvi: Issues, I mean, we could have, let's say in Q1FY09, our top line booking or the segment one booking was higher than 30% around, so and in the second quarter the booking is around 18% odd. So, any execution issues or something on that front?

B. Thiagarajan: In the sense that we are making sure the payments are fully secured, the customer will be able to pay. So we have been basically slowing down on billing. Unless and until the money is coming, we have not been delivering. Or we want the assurance that the payment will be done. So therefore the billing growth is lower than the booking growth.

Kirti Dalvi: Okay. So going forward in future, I mean, in Q3 and Q4, we can expect a higher billing?

B. Thiagarajan: I am not very sure about that, probably, I wouldn't know. We have to watch the money situation in the market place. Two is, as I had mentioned in the remarks, infrastructure projects, there is a clear skew, like the Metro Railway, airports, etc, they take a longer time for billing to take place, not like the IT and other segments, which have been experiencing a shorter turnaround time.

Vir Advani: The issue is not on execution, just to be clear, as you know we have been billing growth at the north of 30% for few years; obviously the infrastructure is in place to execute. The issue is cash in the market. So as the credit situation improves, and we are hoping it does over the next couple of months, at least a little bit, at least the credit situation should improve, hopefully our billing should accelerate, although we are unclear right now, simply because we are not chasing billing right now.

Kirti Dalvi: Okay. And sir the second question is, in terms of your order book, can you give us a breakup in terms of how much is IT related or infrastructure related, a ballpark figure.

B. Thiagarajan: Roughly you can say 30% to 40%, you are asking about IT and infrastructure together?

Kirti Dalvi: Yes.

Vir Advani: Together will be more. I think IT is about 30% and infrastructure is about 20% or 15% right now.

Kirti Dalvi: And the balance is distributed among?

B. Thiagarajan: Many segments, like hotels, hospitals, and normal offices, banks, many things.

Vir Advani: Retail, etc.

Kirti Dalvi: Anything greater than 30% of order book? Any of these segments, like hotels or hospitality?

Vir Advani: IT is the largest at 30%.

Kirti Dalvi: Okay. And sir what are our exports in Q2FY09?

B. Thiagarajan: Exports in Q2, it is predominantly product exports, which will be something like 30 crores in Q2.

Kirti Dalvi: Okay and sir the last question is on the margins. We have always been benefited because of being a net importer. Considering this rupee depreciation, do you see that whatever the margins we achieved in last year are sustainable this year also?

B. Thiagarajan: As of now, if I have to pass a judgment, yes, it should be, because the price increase has happened, raw material prices are coming under control. Obviously the one issue is with regard to the foreign exchange. Taking all into consideration, both gross margin and operating margin, we aim to basically hold it at last year level.

Vir Advani: Just a little more clarification on that, based on the volume of purchase as well as what we are projecting, broadly the foreign exchange or the dollar moving up, is largely offset by the raw material prices coming down. However, there is a time lag on that, because what's happened is that, inventory has increased, obviously because the growth slowed. To that extent there is a lag between the impact of the two. Now because we are stuck with the inventory at better dollar prices, there is an advantage there, but however today you can obviously procure raw material at a lower price. So you understand, how I am saying that they largely offset each other. So, although we weren't hedged purely on foreign exchange for example, there is somewhat of an unnatural hedge there between what's going on with prices and the foreign exchange. So, which is why we feel that we should be able to maintain margins on an overall basis. Of course, the billing growth has slowed, so that naturally has a negative impact on margins. But that, we hope by the end of the year, will be offset by all the operational efficiency effort that we have been putting into the company for the last 12 months. So therefore, broadly there is, I will just repeat it, as raw material price is going down, there is the dollar having a negative impact on margins, there is billing slowing, which is a negative impact, and there is the operational efficiency that kicks in. So we are hoping that all four of these net each other off, and we land up at similar margins as last year. We had originally thought before this slowdown that we could actually get better margins this year- that was the plan. That is not going to happen, which is why we are hoping we land up at same margins as last year.

Kirti Dalvi: Okay, and sir, in segment 2, in cooling products, what is the proportion of our Split AC to Room ACs? Is it the same what we had in Q1?

B. Thiagarajan: Split ACs to…

Kirti Dalvi: Room ACs.

B. Thiagarajan: Window AC and Split AC, combined is called Room AC. Out of this room ACs, split should be around 70% now.

Kirti Dalvi: Okay, and sir the last question, would it be possible to get the balance sheet figures?

B. Thiagarajan: No, we do not publish anything on Q2.

Kirti Dalvi: I mean, cash or something like that.

B. Thiagarajan: No, not exactly.

Kirti Dalvi: Okay, sir then the inventories, I think in segment C, we had some large inventories across, in the market, all the players. What is the situation today?

B. Thiagarajan: Segment C?

Kirti Dalvi: Cooling sir, sorry, segment B, cooling products.

B. Thiagarajan: In cooling products, there was an inventory pileup in the month of July and it was true of the whole industry and between July and September. Obviously, we are not a big player to be unduly worried. But the industry piling up the inventory got a different connotation, because they will not increase the price, they will end up dropping the prices, though our desire was to increase the prices. And our production is tuned to what we will be in a position to sell. But on the whole, compared to last year, probably we are holding 10% more inventory.

Kirti Dalvi: Okay..

Vir Advani: And again in light of what we have seen with the dollar, because you understand in cooling products, there is a heavy import component, much more than in the other segments. So to that extent, actually this inventory pileup is somewhat of an advantage, because they were all procured at much better dollar prices. Prices of components for cooling products had still not, sort of turned down inspite of the commodity prices dropping, because those vendors are also facing huge slowdown on a volume basis, so they are dragging their feet on renegotiating prices. We expect that prices will be renegotiated down by January, but to that extent actually while, of course, holding inventory is not something that we like to do and that is not our aim and it has ballooned the working capital and we are paying the price from an interest perspective for that, we feel that net-net we are probably going to be better off and it is not by design, it is actually by fault. We are going to be better off because of having procured at better dollar prices.

Kirti Dalvi: Okay. And what is the proportion of fixed price contracts in our order book?

Vir Advani: Proportion of fixed price, practically everything we do is fixed price. What is your definition of fixed price?

Kirti Dalvi: What I mean by that is, if the commodity prices goes up or goes down, do we get the advantage of it, having an escalation clause in that?

B. Thiagarajan: Say roughly around 25% of the orders should be having an escalation clause- predominantly infrastructure or the government public sector projects. Most private orders are all firm price contracts.

Kirti Dalvi: Okay sir. Thanks a lot and wish you good luck.

Vir Advani: Thank you.

B. Thiagarajan: Thank you.

Moderator: Our next question comes from **Mr. Nirmal Shah of Alchemy Shares.**

Nirmal Shah: Sir, my question has been answered, thank you.

B. Thiagarajan: Thank you Nirmal.

Moderator: Our next question comes from **Mr. Munzal Shah of ICICI Prudential.**

Munzal Shah: Hello?

B. Thiagarajan: Good morning.

Munzal Shah: Good morning sir. How are you?

B. Thiagarajan: Fine, thank you.

Munzal Shah: Just wanted to know, this other expenditure in this quarter, has grown up by almost 37% YOY.

B. Thiagarajan: Yes.

Munzal Shah: What would be the breakup and is there any one time or would this be the trend going forward?

B. Thiagarajan: I will have to verify this. You are talking against 27 crores, why it is 37 crores.

Munzal Shah: Yes, exactly.

B. Thiagarajan: I will have to verify and come back. I do not have the answer right away.

Munzal Shah: Okay, fine. Thank you sir.

Moderator: Our next question comes from **Mr. Nainesh Rajani of Tata Mutual Fund.**

Nainesh Rajani: Good morning sir. Just a couple of things I wanted to understand. If you can give us, of the total raw material used, what is the total import component? Can you quantify that amount sir?

B. Thiagarajan: Imported out of the total…

Nainesh Rajani: Total raw material requirement that we have, what is the total amount of imported items, if you can quantify that for this particular quarter?

Vir Advani: The quarter is difficult, on an aggregate basis, roughly 30%.

Nainesh Rajani: Okay and how does this cycle work, just wanted to understand. For example, lets say you are executing orders in this particular quarter itself, by when will you have to order the inventory for that execution of the project is something that I wanted to understand sir?

B. Thiagarajan: Different segments it is different, say for example, let us take electromechanical projects, obviously, the lead time of big equipment like chiller, if it is imported chiller, it will be at least four months of time. So we will make sure depending on the project plan, to order four months earlier. Let us take a product which is manufactured by us, like cooling products segment. For items like a compressor, we will not be importing order to order, right? It is based on the total production cycle. Normally, it will be three months ahead; the order will be placed, roughly.

Nainesh Rajani: Okay, just another thing I wanted to understand, you were talking about the fact that you will be impacted as far as your FOREX is concerned. Now, in this particular quarter, did we have any extraordinary losses on account of foreign exchange fluctuations?

Vir Advani: No, because we don't hedge, we don't have any losses, right?

Nainesh Rajani: Alright.

Vir Advani: You are asking about notional loss or, I mean, financial, there is no P&L…

Nainesh Rajani: No, notional loss, which you might have to write down in the next few quarters, in I think your balance sheet or P&L depending upon the entry that you make sir.

Vir Advani: No.

Nainesh Rajani: No? All right. Just last question from my end, can you give a breakup of your clients for IT, ITES, maybe top two to three clients, a few clients, IT, ITES, infrastructure, hotels, especially the ones wherein you are actually slowing down the billing payments. Just to get a sense as to what is happening in the industry sir.

B. Thiagarajan: As far as the customers are concerned, where we have received orders or executed large orders, it is given in the investor update, which will be circulated this evening or tomorrow. But it is very difficult to say which customer, for whom we are going slowly, it is unfair, right? It maybe due to number of reasons, so I won't be able to tell you which customers we are slowing down the billing.

Nainesh Rajani: Can you give us an idea on the industry that you probably are slowing down on your billing as you mentioned earlier.

B. Thiagarajan: All builders. For most of the builders, we are making sure that the payment is available.

Nainesh Rajani: Okay. But that would be across all categories, it would include IT, ITES, infrastructure, maybe hotels, because you would be doing projects for these builders who are actually building up these IT parks and infrastructure.

B. Thiagarajan: Many IT SEZs are directly done by the IT companies. Builders do for IT or hotel or hospital and it is irrespective of this. If my end customer is builder, we will be seeking a specific confirmation that the equipment can be delivered, money is secured, money they will release, and then only we go ahead and release.

Nainesh Rajani: Sir, actually that’s it from my end. Thanks a lot sir.

B. Thiagarajan: Thank you.

Moderator: Our next question comes from **Mr. Dhimant Kothari of Lotus Mutual Fund.**

Dhimant Kothari: Good morning sir.

B. Thiagarajan: Good morning.

Dhimant Kothari: Sir, would you please give me the net sales and the EBITDA included for Naseer Electricals for this quarter?

B. Thiagarajan: No, it is not disclosed here. It will become a selective disclosure. It is part of the electromechanical projects. All that I can tell you is compared to what it was, last year it was not there, right?

Dhimant Kothari: Right.

B. Thiagarajan: Compared to their figures, when it was Naseer Electricals it is growing at around more than 50%.

Dhimant Kothari: Okay, and secondly on the employee cost at quarter-on-quarter reduction it is mainly because of reassessment of the retirement benefit liabilities?

B. Thiagarajan: That is right.

Dhimant Kothari: Could you quantify that?

B. Thiagarajan: It is there given in the results itself, right. If you see the notes…

Dhimant Kothari: Yes, it is included at around 10 crores, had the reassessment not been done, what would have been the number that would have been included?

B. Thiagarajan: Yes, you have to simply reduce that 10.

Dhimant Kothari: Okay, thank you sir. That's it from my end, thank you sir.

B. Thiagarajan: Thank you.

Moderator: Thank you sir. Our next question comes from **Mr. Sanjeev Zarbade of Kotak.**

Sanjeev Zarbade: Good morning sir.

B. Thiagarajan: Good morning.

Sanjeev Zarbade: Sir, my question is on the professional electronics segment. Although I understand that this is a seasonal kind of a product segment, but just wanted to understand the impact of depreciation in rupee on this product segment?

B. Thiagarajan: See the thing is it doesn't affect much as far as the billing or the booking value is concerned, because what will happen is the customer opens the LC directly on the foreign principals and he pays, so we are not in the picture. It affects to the extent of our commission income, like for example, let us say, Nuclear Power Corporation placed an order on its principal, who is our principal for 100 crore or 100 million or 25 million USD. They will open a LC, they will execute that order. We may be entitled to 10% of the order value or 7.5% of the order value as commission payable in Indian rupees or payable in USD; it depends on the principal, depends on the customer. Sometimes the principal pays, sometimes the customer pays. To that extent, if we were to get in USD, we will benefit. If the dollar goes down we may be losing - that is about all. So, in other words foreign exchange fluctuation is not going to greatly impact this part of the business.

Vir Advani: Just to qualify that, obviously this is an import distribution business and to the extent that USD moved up to 50, obviously is much more expensive for clients, so there is obviously a demand impact. However, having said that, the competition of comparative products are all imports themselves. There is very little local or indigenous alternatives available for these segments that we represent. Because this is all complex equipment, electronic equipment or industrial equipment for whom there is no local competitor, so to the extent that our prices have gone up, so has the competition. So customers have to now budget a much higher CAPEX, which is obviously a demand dampener, which is the only impact, but like Thyag said, from our P&L perspective or operation perspective, there is no impact.

Sanjeev Zarbade: And these products basically go to a very diverse range of industries and not a particular industry is that…

Vir Advani: Yes, I would say about 7 or 8 industries would contribute about 80% of the business. But it is a broad range, there is banking, steel, power, broadcasting and satellite, defense… so there is a wide variety of industries.

Sanjeev Zarbade: Okay, but would Blue Star be interested in changing the terms so that we are completely insulated from the fluctuations of forex, in the sense that we get commission directly from the customer, in that case our rupee receivables would be more or less fixed?

Vir Advani: No, what we are going to do, like we told you is, put in a new foreign exchange policy. It is very difficult to change terms of doing business, it is easier obviously to protect ourselves from a hedging perspective.

Sanjeev Zarbade: Okay, sure. That's it sir, thanks a lot.

Moderator: Our next question comes from **Mr. Mahesh Bendre of HSBC Securities.**

Mahesh Bendre: Good morning sir.

B. Thiagarajan: Yes, tell us.

Mahesh Bendre: Okay, sir I have two questions, one is in the last con call you had mentioned the CAPEX of around 100 crores this year and that we will have more clarity by September year end, what is the outlook towards that?

B. Thiagarajan: See, as of now, we have in the first half, incurred around 65 crores already, because there was a work in progress in Wada, which was around 26 crores and in other factories put together around 10 crores. And the normal CAPEX equipment is around 3 crores and for some commitments we have made, you can say that already committed and what definitely will happen is 60 crores of rupees and it is very much likely that we may touch 100 crores. We are not, because of this slow down trying to cut down our CAPEX at all, because there is a need.

Mahesh Bendre: Okay and sir, just one broad question, sir. What is the outlook for FY10 in terms of growth in order booking and may be on margin side?

Vir Advani: I think, you should tell us, because we can't really see that far right now. There is too much uncertainty in the market as you know, we are directly linked to real estate. So I think as it becomes clearer what is going to happen in the real estate market, we will be in a better position. As far as we are concerned right now we are very much focused on this year and like we said, we are being very selective about projects we take. We have been very selective about how we bill and what we collect, so that’s really where we are right now.

Mahesh Bendre: But sir, airconditioning market, which has been growing more than 25-30% for the last two-three years, do you expect that growth might come down to sub 20 or sub 15?

B. Thiagarajan: As of now, the industry exchange data I am telling you, the domestic central airconditioning market everybody agrees that at least it will be 25%. I think this month particularly is a bad period to predict that, but so far the understanding is, indeed it will grow by 25%. I am talking about central airconditioning.

Vir Advani: And when we talk about growth from the industry perspective, it is all order booking. So that’s typically how people talk, they don’t talk billing. So while booking will continue to grow, we have to see how that translates into billing and revenue.

Mahesh Bendre: Yes, sir another question about the cooling product side, last two quarters we have been growing more than 20-25% when industry is struggling to put any growth, do you think this growth will continue for the next two quarters, or would the slow down might affect these kind of consumer durable segment?

B. Thiagarajan: That is definitely on the cards, it will affect.

Mahesh Bendre: It will be a negative growth or it might improve?

Vir Advani: We are not able to comment on that, as you know.

Mahesh Bendre: Okay, thank you sir, all the best.

Vir Advani: Thank you.

Moderator: Our next question comes from **Mr. Rahul Bhangadia of Lucky Securities.**

Rahul Bhangadia: Sir, my question was basically on the absolute number of inventory, debtors and working capital, which I believe you are not willing to share, would you be able to share?

B. Thiagarajan: No, I can broadly share for the benefit of yours and others, though…then it doesn't become selective. The debtors went up for the…, I am talking about September to September, okay. Debtors went up by around 150 crores.

Rahul Bhangadia: September to September or, sir if you could talk in absolute numbers, what are these numbers as of now, that would be easier?

B. Thiagarajan: No, I do not have that with me here, but I can always tell you that. But our interest component is nothing. That's what I keep saying. The concern is not the interest cost at all because our capital employed is very negligible and interest is very negligible. But I can tell you September to September indeed the debtors went up by around 150 crores, inventory went up by around 20 crores, this is what it is. The debtor is predominantly in segment 1; inventory is predominantly in segment 2.

Rahul Bhangadia: Okay, I think that should help, sir. Thank you.

B. Thiagarajan: Thank you.

Moderator: Our next question comes from **Mr. Abhinav Khandelwal of Systematix Shares.**

Abhinav Khandelwal: Hello sir, I just need to understand that, you said that around 25% of the total order book is fixed price contracts, if my understanding is right?

B. Thiagarajan: No, the other way around, 25% only will have the price variation, 75% will be fixed price contract.

Abhinav Khandelwal: Okay, so if the raw material prices come down, so we have to pass on this 25% order book benefit to the customers?

B. Thiagarajan: Correct.

Abhinav Khandelwal: But we will not be benefiting because we are not hedged for the foreign exchange?

B. Thiagarajan: Very difficult to say that way. First of all, in the last conference call I had mentioned that there is a RAMA price variation formula which we want to implement. That is still under implementation, it is not going to immediately translate into anything. Probably it will happen in the next quarter or the last quarter. The general price variation clause, is in case if the raw material prices have gone up, it is supposed to be paid for plus or minus, but in both the cases there will be a ceiling that will be there, right. Like if the customers agree, I will pay up to 5%, +5% or –5%, but as of now those price variations, if we are to look into, it is also linked to many conditions that the project was delayed or there was no…

Abhinav Khandelwal: Hello.

B. Thiagarajan: Yes, as I mentioned it is subject to customer has not delayed it or I have not delayed it… so on that 25% as of now, we do not see any loss of revenue just because the raw material prices have come down It is also related to the time when we have quoted, the time when the order has been booked and the scheduled delivery date. As of now we do not have any loss on that account.

Moderator: Our next question comes from **Ms. Bhavana of HDFC Securities.**

Bhavana: Good morning, sir.

B. Thiagarajan: Good morning.

Bhavana: I just wanted to understand our PBIT margins in the professional electronics segment have increased substantially this quarter, is there any reason for that?

B. Thiagarajan: See, you should not see the margin percentage there, because the top line and the bottom line cannot be directly correlated. The top line reflects commission income or local value addition that is done, so don't read much into that at all.

Bhavana: Right, so when we are doing some sort of value addition, which has seen some increase in demand or something like that?

B. Thiagarajan: No, not at all. It has got no correlation. You have to look at in this segment, the absolute amount only.

Bhavana: Which is pretty flat?

B. Thiagarajan: Yes, where are you reading?

Vir Advani: That is 19% growth for the half, right?

B. Thiagarajan: Yes, so, it is not flat, so you have to see the absolute amount only here. Don't ever calculate the segment result to segment revenue as a percentage at all.

Bhavana: Right. In our cooling product segment, the types of seasonality factor and the debtor factor that we explained, our sales are down 40% on a quarter-on-quarter basis.

Vir Advani: Where, which quarter?

Bhavana: If I compare Q1 with Q2.

Vir Advani: Q1 of this year with Q2 of this year?

Bhavana: Of this year, right.

Vir Advani: Yes.

Bhavana: It is down about 40%.

Vir Advani: Yes.

Bhavana: So, besides the two factors that I mentioned, is there any other reason for that?

Vir Advani: No.

Bhavana: Okay and overall our tax rate should be about 28%, because in this quarter we have only provided about 25% or so?

B. Thiagarajan: We do not expect any change in that on the full year period that is at least our rough assessment.

Bhavana: Right, so the full year basis, we expect it to be about 28%?

B. Thiagarajan: Yes, like last year.

Bhavana: Okay, all right. That will be all. Thank you.

Moderator: Our next question comes from **Mr. Ankit Sancheti of Birla Sunlife**.

Ankit Sancheti: Hello.

B. Thiagarajan: Yes, sir. Good morning.

Ankit Sancheti: Good morning sir. Last couple of quarters has been pretty robust in terms of order inflows. Till September we have seen significant order inflows for Blue Star and for the industry in general. Just wondering, the last 2-3 months has been quite challenging for the industry as a whole. Have you seen significant slowdown in inquiries in the last one or two months and what are your plans going forward for at least next couple of months. Do you see that order booking will be a significant challenge for you?

Vir Advani: Order enquiries are slowing, order finalizations are slowing, most people are waiting and watching the credit situation, so, Yes, we are expecting, I wouldn't call it challenging, we are not sort of predicting doom and doom, there will be growth, there will be good orders coming in, also some of the sectors where there is more robust buying we are obviously spending more time on, so government jobs is one, any infrastructure related jobs, as well as there are certain segments, for example IT SEZs continue to be sort of moving ahead, especially when the IT company or the corporate is the one that is investing directly, so there are clearly segments of the market that continue to buy without any issues and that is where we are focused.

Ankit Sancheti: Sir, in your overall order mix, can we presume that since infra related projects will have increased dominance going ahead, does it impact anything in sense of either working capital or in terms of margins, is there any correlation between that, private sector projects and some more infra projects?

Vir Advani: Yes, infrastructure project tend to be L1 projects as you would imagine, which may not be the case in corporate customers where we get a premium for our brand, so to that extent there is. But having said that we don't see in general lower margins per se in the infrastructure space where we are seeing fairly good margins there. Terms of payment are also okay, the issue is that they tend to take much longer to execute. So, to that extent the cost of delivery does of course increase, so there is a little element, but it is not substantial, it is not significant enough to affect the overall margins of the company and in any case, like I mentioned it is only about 15% of the order book right now. We don't, given that we are focused on HVAC and Electrical, it's unlikely that infrastructure as a segment will become 40% or 50% of the order book. You just can't, because the other segments will always buy cumulatively much more than the infrastructure segments. I think if we were a pure civil contractor that might be different because infrastructure is a very much larger percentage as compared to commercial, but for HVAC and Electrical, commercial will always be larger than infrastructure.

Ankit Sancheti: Okay and just wondering since there is a general slowdown in enquiry levels, do you presume that competition is becoming more aggressive at current levels or no…

Vir Advani: Of course that is true of any industry and we should expect that here as well.

Ankit Sancheti: Are you seeing new people coming into this market apart from you and Voltas and one other guy, three guys are predominantly commanding this industry, apart from that are you seeing some other guys entering in this sector?

Vir Advani: No we haven't seen anyone come in for a while.

Ankit Sancheti: Okay and just wondering exports have been largely a very small part of our overall portfolio, it is predominantly product exports, are we looking at Middle-east market or you are feeling pressure out there also and it doesn't make sense to venture out in Middle-east at this point of time?

Vir Advani: No, we have only one operation in the Middle-east on a project perspective, which is in Qatar, where we have booked some business; we are executing that right now. We will be increasing our presence there, but again as the company grows, it is still not a significant enough piece of the overall business, so we don't have plans, for example of entering the Dubai market or anything right now. I think we are very much focused on India and to a certain degree in Qatar.

Ankit Sancheti: Not entering Dubai and these markets is more due to margins being lower out there or you…

Vir Advani: No, margins are not lower there; I don't think that is the case. It is just…

Ankit Sancheti: No, it's your capabilities to handle those projects are still lagging, that's the reason, I am just wondering?

Vir Advani: I don't think that's the case either, it's just about where you focus your energy. We have been very much focused on the domestic market, which is why we have a leadership position here with the margins that we do. There is a certain lead-time required to get going in a market. It could be three to five years and some of our competition has been doing that and it is benefiting from that. We had chosen not to because we had wanted to get all our businesses profitable, which we have managed to do including the refrigeration piece, so it is just choices, it is just strategic choices that we made and in today's market I think that, Dubai for example is also coming under pressure in spite of the Middle-east supposedly being insulated. So I think at this stage in general as you would agree, businesses, you stay focused on where you have a leadership position in a slowing down market and that is what we are doing,

Ankit Sancheti: Sure and just one last question, this CAPEX of 100 crores, which is to be getting over in this year, this is largely for what?

B. Thiagarajan: The largest item is actually the Wada project.

Ankit Sancheti: Which project?

B. Thiagarajan: Wada manufacturing unit, which is coming up in Wada. See actually last year it was due to the delay in execution it was a work in progress, that's about all, that is why it appears to be much higher CAPEX this year. Wada itself will be close to around 30 crores and in the other manufacturing units we normally incur close to 20 crores every year, replacing equipment and other stuff. We are into a SAP ERP implementation this year.

Ankit Sancheti: Okay, so next year again the CAPEX will be say 30, 40 odd crores, not more than that, that won't be as significant as….?

B. Thiagarajan: We have not planned, we decide normally in the month of January, February.

Vir Advani: But it is unlikely it will less than 50 crores.

Ankit Sancheti: Okay, it's unlikely to be less than 50 crores.

Vir Advani: Yes, we haven't planned yet, so it is a little early. We should be planning in January, but at the size of operation we are at now, just maintenance CAPEX tends to be a certain size, so I don't think we are in the 30-crore range anymore.

Ankit Sancheti: Okay, thanks a lot sir and best of luck.

Vir Advani: Thank you.

Moderator: Our next question comes from **Mr. Mehul Mehta of Standard Chartered.**

Mehul Mehta: Good morning sir.

B. Thiagarajan: Good morning.

Mehul Mehta: Yes, in terms of absolute number of working capital and fixed assets employed, I believe working capital has gone up to as high as 325, 350 odd crores at the end of this quarter?

B. Thiagarajan: No, where did you get this from? Are you guessing?

Mehul Mehta: Sorry?

B. Thiagarajan: You are estimating, right?

Mehul Mehta: No, you shared the number in terms of your CAPEX incurred. If I look at that, and if I deduct that gross block part, then like you know, working capital, so broadly if you can share in terms of 515 crores of capital employed, what would be, say gross block part and what would be working capital part?

B. Thiagarajan: No, I do not have the figure. As I mentioned earlier to some other question, the CAPEX in the first half of this year we would have incurred somewhere around 60 crores of rupees.

Mehul Mehta: Sir, based on that only I have calculated, so may be, if you don't have those figures, but otherwise like…

B. Thiagarajan: I don't have it, debtors compared to September last year had gone up by around 150 crores. Inventory had gone up by around 20 crores, that's all I have. Otherwise I do not have the absolute capital employed or the balance sheet for that period.

Mehul Mehta: Okay, thank you.

Moderator: Our next question comes from **Mr. Shalabh Agarwal of Sundaram BNP Paribas.**

Shalabh Agarwal: Good afternoon sir.

B. Thiagarajan: Good afternoon.

Shalabh Agarwal: Sir, I logged in a bit late. So I am sorry if I am repeating this question, but will it be possible for you to share the broad breakup of your HVAC segment in terms of, which industries it caters to, like in real estate and whether it is a commercial building or a hotel, will that be possible for you to share those numbers?

B. Thiagarajan: Yes, I suppose you are in the mailing list, you will get the investor update today or tomorrow and we cater in the electromechanical project segment to practically every corporate and commercial establishments, starting from airport, railways or IT SEZ, banks, offices, convention center, hotel, etc, etc and we mentioned right now the infrastructure projects are on, power projects are on. By infrastructure we mean the metro railway or airports. In steel industry, power industry, all these, the projects are on. The order inflow is good, the execution is happening and IT SEZs are indeed happening. The builder segment or the retail segment practically it has come to a stand still, in the sense that many projects are getting delayed.

Shalabh Agarwal: Okay and you are seeing the broad breakup between these would be there in the slides, which you would send us?

B. Thiagarajan: There won't be a breakup, but you will be able to say the order inflows are from which segment. It indicates during the quarter, so that will give you an idea.

Vir Advani: But we had mentioned was about 30% of the order book is IT.

Shalabh Agarwal: Ok.

Vir Advani: Largest, and then after that will come retail and offices. We don’t have the numbers here, but it will be in the range of around 15% or so each.

Shalabh Agarwal: Ok, each?

Vir Advani: Each, Yes and then there is infrastructure, about 15%. I don’t know how much I just added up, may be about 75% and then the rest would be shared between hotels, hospitals, that kind of things.

Shalabh Agarwal: So, whatever we do in the power side also will get clubbed in the infra side?

Vir Advani: Correct,

Shalabh Agarwal: Within infra?

Vir Advani: Correct, infrastructure includes airports, metro and power.

Shalabh Agarwal: Okay and when we say office is 15%, it is commercial offices besides IT?

Vir Advani: Yes, commercial offices including banks and all.

Shalabh Agarwal: Okay, great sir, thank you. Thank you and all the best.

B. Thiagarajan: We will take one last question.

Moderator: Sure sir. We have one follow up question coming from **Mr. Nirav Vasa of Gupta Equities.**

Nirav Vasa: Hello, sir can you throw some light that after what percentage of contract gets completed, it gets billed to the customer and it starts ticking in the revenue of the company?

B. Thiagarajan: I am not able to follow, see we follow AS7 or the Accounting Standard 7 guidelines, so even if you deliver any equipment, you reckon the revenue actually for that pro-rata value, okay.

Nirav Vasa: No sir, actually what I want to understand is that assuming that you have an order of 100 crore rupees and what percentage of this 100 crore rupees would get completed till the time the revenue would not be booked, so assuming that even if one percent of this 100 crore rupees order gets booked in, it will be reflected in the revenues of the company?

B. Thiagarajan: Yes, Yes accounting standard 7 clearly indicates that as soon as you start delivering anything, you will start recognizing the revenue, but on the cost part of it also there is a specific guideline. Long ago, about 10 years ago there used to be a practice of unless and until 90% of the job is executed, it won't be recognized in revenues, that is no longer applicable from AS7 point of view. Anything, even if you deliver one small cable, there it is the revenue.

Nirav Vasa: Okay and sir apart from that while taking an HVAC contract, what percent of the contract is taken as advance from the customer?

Vir Advani: It varies between 10% and 20%.

Nirav Vasa: Between 10% to 20% and sir, how many people are employed by the company as of now?

B. Thiagarajan: As of now around 2700.

Nirav Vasa: And sir can you give some breakup in terms of blue collar and white collar between both of them?

B. Thiagarajan: Say, roughly around 700 are blue collar.

Nirav Vasa: Okay and the rest would be white collar?

B. Thiagarajan: That's right.

Nirav Vasa: And attrition rate of the company?

B. Thiagarajan: Roughly around 12%-12.5%.

Nirav Vasa: 12%?

B. Thiagarajan: Yes.

Nirav Vasa: Thank you very much, sir.

B. Thiagarajan: Thank you.

Moderator: Now I hand over the floor to Mr. B. Thiagarajan for closing comments.

B. Thiagarajan: Thank you very much for your interest. We will be circulating the investor update this afternoon and if you have any specific queries or some of the questions, which I have said that I will respond separately, I will indeed get back to you. Thank you very much.

Moderator: Thank you sir. Ladies and gentlemen this concludes your conference for today. Thank you for your participation and for using Door Sabha's conference call service. You may disconnect your lines now. Thank you and have a pleasant day.

Note: 1. This document has been edited to improve readability.
2. Blanks in this transcript represent inaudible or incomprehensible words.