"Vascon Engineers Limited 4QFY13 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day and welcome to Vascon Engineers Limited's 4QFY13 Earnings Conference Call hosted by Ambit Capital. As a reminder, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call, please signal an operator by pressing '*' followed by '0' on your Touchtone phone. Please note that this conference is being recorded. I would now like to hand over the conference to Mr. Nitin Bhasin from Ambit Capital. Thank you, and over to you, sir.

Nitin Bhasin: Thank you. Good morning, ladies and gentlemen. On behalf of Ambit Capital, we welcome you all to the fourth quarter FY13 earnings call for Vascon Engineers Limited. The company today is represented by Dr. Santosh Sundararajan, CEO of the firm and Mr. M. Krishnamurthi, the Chief Compliance Officer. I would like to hand over the call to Dr. Santosh and from there on possibly after his opening remarks, we will move to the questions and answers. Sir, over to you.

Santosh Sundararajan: Good morning everyone. A very warm welcome to Vascon Engineer's earnings call. I am Dr. Santosh and I have Mr. Krishnamurthi with me here.

You would be aware that the year 2013 was very challenging for the industry as a whole due to weak economic growth and weak consumer sentiment. The Indian economy of course has experienced one of its worst slowdowns in nearly a decade on the back of global context—headwinds from domestic macro-economic imbalances and policy reversals.

The year has started with the news that the previous fiscal's fourth quarter GDP has dropped to 5.5%. This coupled with low growth, macro-economic issues, and expanding subsidies worsening the current account balance have added to the slow down. Our industry is, we believe, at the cusp of a new growth phase and the demand is improving. Today, India is one of the most-favoured real estate markets in the world. The sector has not been only the largest contributor to the GDP of the country but it is also the fourth-largest sector in terms of FDI inflows in the country.

Recently, the rate cut has also been announced by the RBI, showing that it is taking in to consideration the liquidity concerns. The recent decision to cut the repo rate by 25 basis points has brought a big sigh of relief. This will not only help in mobilising liquidity in the market but will also help developers in reducing the cost of funds. Home loans are also likely to be offered at slightly better rates.

I will now take you specifically through our financial results for last year. The company on a consolidated basis has recorded revenue of Rs737 crores as against Rs728 crores in FY12. However, this year, we have had losses for the full year, amounting to Rs17 crores as against a profit of Rs16 crores in FY12. The company has been successful in reducing the current debt levels from Rs382 crores in the previous year to about Rs303 crores in the current year, resulting in a decrease of Rs78 crores in the gross debt levels. The company will continue its efforts towards cash flow improvement.

As discussed earlier, the company in its endeavours to reduce all non-core and non-profitable projects has taken a conscious call to exit from some of the projects which had been slow moving for a long period of time and were therefore economically unviable to continue on the same commercial terms. Therefore, we have now become very selective in accepting new orders on the EPC front. Our EPC order inflow during the year amounted to Rs354 crores which was mainly contributed by some prestigious clients like Godrej, Unitech, Dayanand Medical College, Sadhu Vaswani Mission and Gift City Ahmedabad.

We are now working on a much healthier order book, which will bring in better revenues and profitability in the future, thereby enabling us to avoid delays and improve the overall project execution cycle as well.

On the positive front, we have received the letter from PWD, Tamil Nadu, for the conversion of the Tamil Nadu Legislative Assembly into a medical college and hospital. They have asked us to commence the work and this is likely to commence as soon as we receive the payments from them. We have been registering a consistent increase in revenue in real estate in GMP which has been part of our strategy last year. In the real estate business, revenue has increased to Rs169 crores a year-on-year growth of about 48% compared to last year. The focus on this segment has been increased over the past few quarters and the same would be the strategy for the coming year as well. The cumulative area sold for the full-year FY13 for projects under-construction is 3.69 lakhs amounting to a sale value of Rs162 crores as against 2.55 lakhs, amounting to a sale value of Rs150 crores in the previous year.

The company is currently having a strong land bank of 52 million square feet which is completely paid for and available for development. Also, consistent growth has been registered in Clean Room Partitioning in the BMS segment, with revenue of Rs183 crores in the current year, which is a growth of 15% as compared to the previous year. The margins in this business have been stable and the company expects to post healthy growth in this segment going forward. The company is now focusing on cash flow improvement through various means. We are trying to monetise our completed project inventory and some selective land parcels. We have already sold three ready commercial buildings during the year and generated cash flows of about Rs58 crores, which were used for debt repayment.

An additional amount of Rs89 crores is expected in the current year through the sale of two commercial properties in Pune and Nasik and also two land parcels in Pune. The deals with regard to all of the above have already been closed and the monies are awaited. Advances have also been received in some cases. This inflow will facilitate our future planned launches. We are also trying to divest our stake in the hospitality portfolio; we currently have holdings in four hotels where our investment value amounts to Rs72 crores. We are in advanced talks with some buyers and we are hopeful of hearing some positive response on this front.

As a strategy for the financial year 2014, we would continue our focus on cash flow improvement. This will help us in real estate project development which is a high-growth opportunity area and where we plan to expand in a big way. The growth momentum in Clean Room and BMS is also likely to continue. We would now like to open the floor for the Q&A Session.

Moderator: Thank you very much, sir. Participants, we will now begin with the Question & Answer Session. Anyone who wishes to ask a question may press '*' and '1' on the touchtone telephone.

Nitin Bhasin: Operator, while we wait for others to ask questions, I will ask a few questions.

Moderator: Sure.

Nitin Bhasin: A very quick question then we will open the call for the others. Sir, you were talking about the cash flow management for FY14. We hear everyday from contractors and builders that liquidity is a challenge in the market and so what is the liquidity challenge? Is that the client payment? Whether it is a private client, whether it is a government client or whether it is a government state department; is everybody having a payment problem right now for the industry?

Santosh Sundararajan: Yes, you are right. See we have had projects both on the Government side as well as the private side where we have had a huge accumulation of funds which have not been paid by them. Of course the two main projects that have caused us these cash flow problems have been HDIL and TNLA in the past, where one is from the private side and one is from the government side. As EPC contractors when you are doing a huge amount of work, you probably delivering Rs8 crores to Rs10 crores of work in a month and by the time you realise that payments are not coming and you have to stop; at least 2-3 months of payments get stuck with the client. So it is not an easy decision for us to take when we slow down or when we stop because our overheads are running. So by the time we actually take the hard call of stopping, a good amount of money does get accumulated. So this is of course is a problem which we are facing. This is the exact reason why we are going through this cash flow crunch in the entire last year and we have to now look at other options of selling some of our assets to ease the situation for ourselves.

Nitin Bhasin: I think because traditionally it has been thought that real estate developers are pretty much an easy target on the holding. Easy target means that if you are not getting your payment, you can stop work immediately and the payment outstanding is typically not very large. So that causes large cash flow problems for contractors over there. Is that the right line of thinking or not?

Santosh Sundararajan: What happens depends on the pace of the project when the payments stop. So it is also a little bit of luck - sometimes the projects are slow and you are not doing much every month. So if it is only Rs1 crore to Rs2 crores work you are doing every month, then over a couple of months you accumulate an outstanding of less than Rs5 crores. You realise payments are not coming and you would stop and the risk is not too high. But every now and then sometimes the projects are going at a full pace and we are delivering Rs8 crores to Rs10 crores in big projects and then if the payment stops coming when you are delivering at that speed that is when your two month's accumulation suddenly is a huge amount of money which gets stuck.

Nitin Bhasin: And sir, have you seen on your debt any interest rate reduction in the last 3-4 months because as you have mentioned somewhere that the RBI has taken an interest rate reduction for the system as a whole. Is that translating into any benefits for you?

M. Krishnamurthi: No, the actual reduction has not percolated to the clients, so we hope may be in the future that we may get an interest reduction. So far we have not received any great benefit for that.

Nitin Bhasin: Sir, we will stop here and I will ask the operator to take questions.

Moderator: Yes sir, thank you. We have the next question from the line of Mahesh Bendre from Quantum Securities. Please go ahead.

Mahesh Bendre: Our gross rate has come down significantly during the current year from Rs382 crores to Rs303 crores. By this current year-end, what do you think about this number?

Santosh Sundararajan: We are still continuing to reduce our debt levels because the interest burden is something which with the current market situation and with the current turnover that we are doing, the interest burden is still a little bit higher than our comfort levels. We have taken very active steps in the last year, as you said, we have brought down Rs80 crores. Going forward it might not be another Rs80 crores but yes, another Rs30 crores to Rs40 crores we would target to bring it down a bit further by the end of next year.

Mahesh Bendre: Sir, majority of our real estate projects and land bank is associated in Pune, so how do you see the Pune market behaviour over the next 12-18 months? There have been some cases of oversupply and price reduction in that particular geography and so what is your view on the Pune market as a real estate market?

Santosh Sundararajan: See the Pune market now has stabilised to the extent that it is now clearly behaving as a demand-based market where at the right price in the suburbs the projects are selling at not necessarily very exciting volumes of sale but steady volumes which we have now been seeing for the last year. So we have not had to reduce prices as such and we have now seen that there is an increase in demand compared to last year but this is again, as you said, this is not investor-driven. So it is not necessarily in very highly priced prime projects. This is in the project for the masses which you see more in the periphery of the city.

Mahesh Bendre: Sir, if I look at your full-year financials and gross profit margins, real estate is the one segment which has seen a significant decline in the margin, if I compute on a year-on-year basis. Any specific reason for that?

Santosh Sundararajan: See actually the reason for that as we said is we have had this cash flow situation this entire year which we have been focusing on and we did take some conscious calls to exit from a couple of old real estate investments that we are holding on to if we see slightly lower rates which we had to do here to ease the cash flow situation. So while the total turnover of real estate has increased, some of those sales especially in the commercial sites have been at lower rates.

Mahesh Bendre: So have you booked those in the below breakeven point?

Santosh Sundararajan: More or less as break even; yes one or two sales are slightly below the break-even point, you are right. So that has pulled down the total average profitability of real estate.

Mahesh Bendre: And sir, in your opening remarks, you have mentioned that you are holding four hospitality entities for a divestment—two in Pune, one in Goa and another in Coimbatore. So when you do you think this will materialise?

Santosh Sundararajan: See again these investments in hospitality for us have always been non-core with always an intention exit at some point of time. Now this current year, of course, we have started putting these assets on the block and looking for sales from an angle of generating cash flows; however, going forward if the cash flows are generated from other sales and we are more comfortable on a cash flow situation then the expectation of prices from these hotels also would increase from our end. We do not want to be obviously just selling beyond a point for generating cash flows. So if this answers your question, how likely any of these sales will happen this year is difficult to predict and it depends on the market, the prices we offer, the prices we get from prospective buyers and our situation at that point of time.

Mahesh Bendre: It is not necessary to have these assets, am I right in my understanding, sir?

Santosh Sundararajan: No, you are right. It is not necessary unless the price is right and if the right price is of course a combination of the market and our situation at that point of time. So the right price for us last year we did take a call, as I said, to have a couple of assets which did not happen in the hospitality side but on the real estate side where we did not take a call to do it at break even points because we were in need of cash flow. But going forward we have eased our cash flow situation quite a bit and as we have said we have already signed deals on four or five other real estate projects where the monies are expected in this coming quarter. So we do expect that we will be in a much better cash flow situation three months from now. So we the right price would therefore be slightly higher than what the right price was six months ago for us on the hospitality deals.

Mahesh Bendre: Sir, last question is during the quarter you already have monetised 6 to 7 assets. Are we going to further carry out this exercise in the current year also?

Santosh Sundararajan: No, as I said we have already struck deals on another four assets which should generate about Rs80 crores to Rs 90 crores over the next 3-5 months maximum. So if those monies do come in given our current situation I think we would not have a cash flow issue with our bank payments or statutory payments and the running of the business. So if we get this Rs90 crores then I do not think we would want to continue selling assets at slightly lower prices. We would then ready for sales of these hospitality assets, provided we get the price we expect because these are anyway non-core and we do not want to hold them for the sake of holding them; if the price is right, we would exit.

Moderator: Thank you. We have the next question from the line of K C Suri from Span Capital. Please go ahead.

K C Suri: Sir, firstly, talking about the cash inflows, the balance of Rs81 crores from the four deals have already closed. What about the real estate side. I mean we still have to recognise about nearly Rs200 crores of our share of those projects which we sold. So how long would those be realised and what about the cash inflow for the same?

Santosh Sundararajan: You are right. See most of the projects that we have already launched and we are working on we do have to realise about Rs200 crores of cash and most of it except for Windermere which would continue to FY14-15, most of the other projects would get completed and the monies would be realised in this coming year, which is FY13-14. So there would be some free cash flow generated from that as well which will help us.

K C Suri: So I mean Windermere is approximately about Rs40 crores including the duplexes of about Rs60 crores. So barring that is about Rs140 crores is what you will realise this year and that is the amount of cash flow in addition to the Rs 80 crores, is my understanding correct on that?

Santosh Sundararajan: Yes, your understanding is correct but just to point out, the Rs80 crores of cash flow that we generate from this sale from project-to-project, the expenses behind those sales does not exist anymore. So these Rs80 crores can be used for solving other issues like our bank repayments, debt reductions, little bit of statutory payments whereas on the real estate side the Rs140 crores that we would generate is not entirely free cash flows. They would also be used partially to complete the projects, but yes, the margin will be there. So we would generate may be 25% of that as free cash flows.

K C Suri: So about Rs35 odd crores will be free cash flows just from the project itself in addition to the Rs80 crores which may or may not be used for the other commitments?

Santosh Sundararajan: Right.

K C Suri: And once this situation is cleared out by the end of this year and at the most by the early part of the next financial year, what is the trajectory in terms of how do you plan to take the company forward because your clean room business is also doing fairly well. So how do you position the company going ahead? What percentage of the business would be probably pure EPC, Clean Room and Real Estate; how would that split look like?

Santosh Sundararajan: Clean Room and BMS is a separate subsidiary which we own and then also they will be growing independently; they are targeting a growth of about 20-30% year-on-year. So we have also been cautious with them. Actually specifically for this year and the next one year, we would stick to that focus on both the BMS and the EPC side as we are not focusing on order booking and the top-line just for the sake of the top-line. We have been very cautious in order booking on both these sides. So if we are getting our terms and getting our profit margins and we are going ahead with the order. Otherwise we are not too aggressive on the order booking. Whereas on the real estate side we do hope to continue this growth by starting a couple of other projects and increase the contributions of real estate to our total turnover. So that is definitely a strategy which we are focusing on.

K C Suri: I mean EPC is now 50% and real estate is probably 25% of the overall turnover. So going forward you will see that probably real estate is about 50% and EPC 25%?

Santosh Sundararajan: We hope so but not in one year.

K C Suri: Yeah, of course I mean not. I am taking a three-year view down the line. I mean your real estate from a current Rs170 crores and another Rs200 crores this year on a basis of Rs200 crores would that actually grow up to Rs400 crores over three years?

Santosh Sundararajan: It should, yes.

K C Suri: And just to understand what is BMS? I am not too clear on this part of the business? I understand Clean Rooms.

Santosh Sundararajan: Actually it is just term we are using. It covers a whole lot. BMS is Building Management System. But we have also HVAC and they in fact even do some electrical works. So we are basically from the services side of buildings.

K C Suri: Sir, do you see probably a potential for that part of the business to be say a regular annuity business in terms of annual management and maintenance contracts?

Santosh Sundararajan: Little bit and a portion of their business is annuity based, so but a good portion is also projects for building volumes in terms of numbers coming from projects annuities that do not give you huge top-line but they always help you because of their continuous guaranteed inflows which take care of certain fixed overheads. So there is a combination of both.

K C Suri: Could you just provide a split of your EPC order book now? You took the Rs1,100 crores write-off in the previous quarter and so how does that split stand on as on date?

Santosh Sundararajan: See we have an active order book of about Rs1,200 crores on EPC. We are not considering order books which are stalled or which we do not see a future in. These are active running order books of Rs1,200 crores. If you look at the bigger ones, I think we have about Rs100 crores order in Delhi. The Dayanand College is about Rs100 crores order and the Godrej project is a new Rs100 crores order. In Chennai with Unitech, we still have our order backlog of close to Rs100 crores in the three projects that we are doing with them which are all running. In ESIC, we still have about close to Rs80 crores odd to complete. So these are all projects which are running. These are active order books.

K C Suri: So these are amongst the bigger ones and none of the orders are really beyond Rs100 crores in size, and so in case anyone of them really stalls, you would not really take a bigger order going forward now?

Santosh Sundararajan: Absolutely right. There is no single order of Rs500 crores and Rs400 crores.

K C Suri: In the conversion of the TNLA to the medical college and hospital post clearance of dues, how much dues are outstanding there which you expect to receive?

Santosh Sundararajan: The dues of approved bills are of about Rs6 crores only. And then we have unapproved bills which will come in after that they will initially pay us the approved bills and then once we start work we would have another Rs4 crores to Rs5 crores of unapproved bills from the past which would then get. We also have a claim for these delays with them which we are negotiating with them which also they would pay soon.

K C Suri: In terms of the margins profile, your clean room and BMS is now about 5.8-6%; that is what they earn on the segment and then EPC is also earning about less than 6%. Do you see any prospects for these margins improving and by when?

Santosh Sundararajan: Yes definitely. See that has been the focus and also what has happened in the last year on the EPC side is we have been doing a little bit of cleaning up and we have gotten out of some projects where we do not see any margins coming in the future. In some projects, our exposures in terms of the assets that lie in the site of the client, the bank guarantees that we have supplied in some projects, these risks are too high for us to just take an exit. So there are some order books we are carrying especially in Ahmedabad and a little bit in Chennai where we know that we are not making good margins but prudence tells us that we need to continue and complete this. So we will make our order book a little unhealthy but a good proportion now is a much healthier order book; we are having much higher margins and the terms are much friendly. So in the coming year we would be executing a higher percentage of these newer projects and lower percentage of these older projects. So we will see overall margin improvement for sure.

K C Suri: I mean you said that few older projects are not enjoying those healthy margins. What would you term as healthy and what is the kind of margin in newer projects?

Santosh Sundararajan: See when we take jobs, typically the margin we can expect on paper, the net gross profit margin at the project levels is 15%. Now if we do a decent turnover and we achieve 15% of the gross of this, project margins add from at the project level then we would see more than 8-9%. But by the time some of these projects are now running at 5% or sub-5% at the gross project level itself due to labour escalations and delays, and they are below 5% ideally if the client is not willing to help us out for his delays. Most of these delays of course are both from the side of the client and a little bit from our side because of labour mobilisation. Labour in the country has been a major issue and what happens typically for a period, the client does not pay all of a sudden; when he has mobilised his cash flow, he pays and we take a while to get up and mobilise labour. So I think the game keeps going on in these projects. In most projects there is always a significant fault lying on the client side and technically we do have a claim. Now it all depends on how the client reacts. Some of them are understanding, and they are willing to listen and pay a bit more, but some of them are adamant. So then we have to take a call whether we exit, depending on the risk we carry on the project.

K C Suri: So I mean from what I understood of this conversation is that anything which earns less than say 6-7% as gross project levels is actually lost to you on the corporate level, right?

Santosh Sundararajan: That is right.

K C Suri: And what proportion of the order book will be at sub 6-7% levels?

Santosh Sundararajan: Out of the Rs1,200 crores, I think we only have about less Rs250 crores now, which is unhealthy at those levels. The rest are all good now.

K C Suri: And over how long is this EPC order book executable?

Santosh Sundararajan: Technically, none of these orders on paper give us more than two years to complete them. So theoretically I should be finishing all of these in the next 24 months maximum. It should give me Rs600 crores EPC top-line but as we see that does not happen; there are always delays somewhere; there are issues and some projects are stalled. So this Rs600 crores that we expect might come down to Rs500 crores. But if we book some new orders may be we will be able to catch up on that as well.

K C Suri: If we stay with this order book then the worst-case scenario is at the most in 36 months you will still have had executed all of this?

Santosh Sundararajan: Right.

K C Suri: Sir, what is your cost of debt right now?

M. Krishnamurthi: 16.67%.

K C Suri: Somehow the math does not fit in terms of Rs33 crores finance charges on the Rs330 crores of debt you had?

Santosh Sundararajan: No, some of the interest is also capitalised.

K C Suri: How much will that be?

M. Krishnamurthi: About Rs23 crores.

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

Sagar Parekh: Sir, you mentioned that Rs1,200 crores of your order book, and so is that your third-party order book or it is a mix of both?

Santosh Sundararajan: No, it is a third-party order.

Sagar Parekh: What would be your guidance for your EPC revenues for FY14?

Santosh Sundararajan: As I said, nearly half of this should be executed but we could say Rs500 crores.

Sagar Parekh: And in terms of this Renaissance and HDIL project, both of them are not included in the order book?

Santosh Sundararajan: No, they are not.

Sagar Parekh: Have you terminated the contract with them or is the labour or material or everything still lying at the site?

Santosh Sundararajan: No, with Renaissance, we have communication to the effect of termination and we have demobilised and we are just settling final issues with them in terms of payment. With HDIL, they have never asked us to stop work and we had had to stop work because the payments were not coming in. So the situation in terms of the paper work is the same that it was a year and a half ago or two years ago. There are some of our assets lying at the site which are below the slab which has not been concreted. So that we have not been able to demobilise but most other things are demobilised from the site.

Moderator: Thank you. We have the next question from the line of Swapna Ghosh from Sushil Finance. Please go ahead.

Swapna Ghosh: I would like to know about the real estate segments. Are we planning any new launches in FY14?

Santosh Sundararajan: We are planning some launches. The Talegaon project that we did start off with a year ago has run in to some issues with the land which we expect will get cleared in this quarter and then so we expect to formally launch that project which is a big project. We do expect to launch that in this year. We also expect to launch project both in Chennai and Coimbatore and Madurai, all three places, we will be launching the first phases of our land bank over there in this year and we do also hope to launch a project in Kalyani Nagar which is now having some issues with the new environmental rule on the road width and building height but once that is sorted then we would launch the Kalyani Nagar project as well.

Swapna Ghosh: Sir, Chennai and Thane are the two major properties in our real estate portfolio, correct?

Santosh Sundararajan: Right.

Swapna Ghosh: What is the status of the development of the already launched projects there?

Santosh Sundararajan: See in both Chennai and Thane, we do not have any already launched portfolio. In Coimbatore we have a project which we have launched which will be completing phase-2 in this year. In Chennai and Thane we have these big land banks that we have signed up on but we have not started anything in either of these cities.

Nitin Bhasin: Sir, I have just two questions here. The first question was basically about the BMS business and the embedded HVAC business. In that, are standalone opportunities out there, or it is becoming very competitive, and margins are coming under pressure? Are payments the same as that in construction?

M. Krishnamurthi: No, this business we acquired in 2010 then after acquisition we have given new directions to that. So now we are exporting to more than six countries. We are exporting food print, we are increasing and eventually next year and next of next year we are looking at more than half should come from exports. So we have done a lot of ground work towards it and so the margin has come down because of a lot of worthy advertisements and other areas, ground work has been done. So we are expecting margins to improve and basically they are all on LC basis and so cash flow should also automatically improve.

Nitin Bhasin: So when you say that international - is it for Clean Room or is it for BMS?

M. Krishnamurthi: No, it is Clean Room and BMS together. So the Clean Room supplies the materials and BMS executes.

Nitin Bhasin: If I am not mistaken you compete in the HVAC business with Voltas and BlueStar and if I look at their HVAC project business in the recent quarter, the numbers were nothing to write home about. Both the companies have been saying that the orders are missing?

M. Krishnamurthi: Our business is a niche business and so we do not directly compete with them though some portion of the business may be in competition with them.

Nitin Bhasin: And sir, the other one was about the building orders because we see in Mumbai pretty much tall buildings are constructed by you. The real estate business is doing good right now for Mumbai launches and launches happening but at the same point in time a contractor like Larsen & Toubro is outbidding many of the other competitions. So your views on that, is there that much demand for tall towers? How is competitive landscape on tall towers buildings shaping up right now?

Santosh Sundararajan: Yes, you are right. There is a demand for tall tower construction in Mumbai and L&T is viewed as a favoured contractor. Traditionally, L&T rates used to be a good percent higher than most of our rates and that gap helped us compete. You are right that as the landscape is unfolding in Mumbai today, L&T has become very aggressive and bagged a good amount of these tall building orders by competing at rates even with people like us. So having said that, there is a limit to everybody’s capacity to absorb work and execute. We are playing the waiting game to see how much aggression L&T is going to display and then how are they are going to deliver these having competed with rates which are not exactly at par with the kind of overheads that a company of that size has. So going ahead we are playing a waiting game. We are not desperate to now further compete and bring the prices down and grab orders as I have been saying.

Nitin Bhasin: As you know related to this, are these developers in Mumbai who construct these tall towers there are handful of them about 6-7 of them, not more than that, are they good payment makers? Do they make timely payments or not? What is your view on that? And second , is there such an opportunity out of Mumbai also?

Santosh Sundararajan: See tower construction when we talk of buildings of more than 30 storeys, these primarily today across the country are primarily concentrated only in Mumbai. Delhi is in the high earthquake zone and NCR as such is much more spread out and so they still do not have this kind of a demand. Mumbai of course has a huge amount of 40-storey and 50-storey towers that are coming up.

Nitin Bhasin: And related to this, are these clients good pay masters or you are saying that even the good guys are becoming questionable right now?

Santosh Sundararajan: See the good guys did become questionable for us as I said and we would not expect the Government of India to be a bad guy when it comes to payment but even they have become questionable; so it is all about the business environment. Being real estate players ourselves, we do sometimes understand and we cannot empathise when our builder client does not pay us but we do understand because there are so many issues; sometimes the Government comes up with rules in the middle of a project and there are so many stages of approval. You start a project with part approval then expect to get the next set of approvals on time. The construction catches up and you do not get those approvals. So you have no choice but to stall the work. And adding to all of that, the real estate prices have not been in a great boom scenario. So the real estate project if it gets delayed, our builder is also going through his own issues. So he is obviously then going to delay payments to us. So I do not think it is specific to anyone and we cannot say that somebody is a good pay master and somebody is a bad pay master; it depends on too many factors.

Nitin Bhasin: And the cost of construction, how is it behaving because since I cover cement also and I see prices are higher. The cost of construction is rising for the individual or a small contractor. How is it behaving for you? Is it a concern or not?

Santosh Sundararajan: It is definitely a concern in terms of risks; we never take cement and steel risks as an EPC vendor. These risks are always on the other side of the table with the client but the labour risk, the sand, the bricks; even these prices have increased drastically in the last two years. So that is why we have to take lower margin than we expected originally in a lot of our projects because in the last two years there has been an unprecedented rise even in labour rates because of the supply-demand issue. So you are right, construction prices have increased drastically in the last 2-3 years and real estate prices have not exactly, at least in the suburbs in economical housing, increased.

Nitin Bhasin: But just to get a sense because you said drastically and significantly what kind of a gradient one should look at is that 100% increase in labour rates and a 100% increase in brick and sand or it is a bit more?

Santosh Sundararajan: Labour rates are very funny. They have very time specific supply-demand in a local location. In fact we now have data on labour rates across the country and you are right, as compared to three years ago I would even say labour rates have almost gone up 100% if you talk about the rates at which you can really get the labour in. We can talk about rates where the labour really does not come in and you do not get your required labour. If you really want to get the 1000 labourers is the project that you need then the rates have doubled; labour rates have doubled in the last 2-3 years. Equipment, sand and brick have not doubled. But when we take projects, we expect them to last for two years and we build in a 5-7% escalation on these things vis-à-vis the risk we carry. So we expect them to escalate at a 7% average over a year but these have now escalated at almost 15-20%.

Nitin Bhasin: Per annum?

Santosh Sundararajan: Per annum, yes.

Moderator: We have the next question, which is a follow-up question from the line of K C Suri from Span Capital. Please go ahead.

K C Suri: Sir, in terms of the Talegaon launch, what we spoke about in FY14 was classified under your real estate portfolio. What is it classified under?

Santosh Sundararajan: It is real estate.

K C Suri: No, but is it completely owned land?

Santosh Sundararajan: No, it is a JDA.

K C Suri: So that is part of the 6.6 million square feet of your share developer built?

Santosh Sundararajan: Yes.

K C Suri: It is entirely one project or this 6.6 million square feet is one parcel?

Santosh Sundararajan: 6.6 million is the total land.

M. Krishnamurthi: 6.6 is the total portion, and so this is one of that.

K C Suri: What is your share in the JV in Thane land?

M. Krishnamurthi: This is about 45%.

K C Suri: Where exactly is this land located? What area of Thane are we talking about?

M. Krishnamurthi: It is diagonally opposite to Rustomjee and Lodha after the toll naka on the right side along the pipeline.

K C Suri: You are referring to the Lodha Casa Rio project, right?

M. Krishnamurthi: Yes.

K C Suri: In terms of what we just discussed earlier regarding your real estate realisation that you would actually have—about Rs140 crores being realised this year and the Rs50 crores of your balance recognised in FY15. Do you think any more of your projects would be significantly recognisable in '15 and '16?

M. Krishnamurthi: No, actually if you look at our sales, out of 2.72 million square foot, we have sold 1.63 million square foot. Once the unsold area is sold because of the percentage completion they have almost different stages of completion and so that amount also will get recognised.

Moderator: Participants, this was the last question. I would now like to hand the floor back to Mr. Nitin Bhasin for closing comments. Over to you, sir.

Nitin Bhasin: Thank you to Dr. Sundararajan and Mr. Krishnamurthi for taking time to share your views on the performance as well as the industry. I would also like to thank you for giving us the opportunity to host this call.

Moderator: Thank you, sir. Ladies and gentlemen on behalf of Ambit Capital that concludes this conference call. Thank you for joining us and you may now disconnect your lines. Thank you.