"Larsen & Toubro Limited Q1 FY22 Earnings Conference Call"

July 26, 2021

MANAGEMENT: **MR. P. RAMAKRISHNAN - HEAD-INVESTOR RELATIONS, LARSEN & TOUBRO LIMITED**

Moderator: Ladies and gentlemen, good day and welcome to the Larsen & Toubro Limited Q1 FY22 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded.

I now hand the conference over to Mr. P. Ramakrishnan, Head-Investor Relations, Larsen & Toubro Limited. Thank you and over to you, sir.

P. Ramakrishnan: Thank you. Good day ladies and gentlemen. A very warm welcome to all of you into the L&T Q1 FY22 Earnings Call. The analyst presentation was uploaded on the stock exchange at our website today around 6:40pm. Hope you must have had a quick look at the numbers. Instead of taking you through the entire presentation, I will give you a brief overview of the performance of the company in the first 15-20 minutes, post which we will get into Q&A.

Before I begin with the overview, a brief disclaimer. The presentation which we have uploaded on the stock exchange, and our website today, including our call discussions that will happen now contains or may have certain forward-looking statements concerning our business prospects and profitability, which are subject to several risks and uncertainties and the actual results could materially differ from those in such forward-looking statements.

Coming to the overview, in the first quarter of the current financial year, India remained in the throes of a severe second COVID wave. The proliferation of infections was much faster than the first wave with significantly higher fatalities recorded. The fast pace of transmission put pressure on the healthcare systems across various states in the country. Unlike the national lockdown being announced last year, which resulted with sufficiently higher economic cost, this time around we have witnessed regional local lockdowns in order to curtail the rising infections.

Furthermore, several states imposed restrictions on discretionary services in order to limit the spread of the virus. Fortunately, India's second wave abated faster than initially feared, though concerns remain around the risk of future waves. Since vaccination programs have commenced in full swing, we hope the economic impact in the coming quarters will be insignificant. Coming to the company performance, Q1 FY22 was all about navigating against the COVID tide in difficult times. Our order inflows for Q1 FY22 at Rs. 266 billion, registered a growth of 13% over the corresponding quarter of the previous year.

The international orders constituted 34% of the total order inflow. Excluding of services and concessions, our order inflows in Q1 FY22 are Rs. 151 billion registering a growth of 10% over the quarter of the previous year. The order wins again excluding services and concessions are fairly well spread across Infrastructure, Hydrocarbon, Power, Heavy Engineering and Industrial Machinery businesses. Having said that, let me mention here that ordering momentum in Q1 was impacted by subdued tendering and award activity.

On a sequential basis, the project tenders and awards in Q1 FY22 were down 40% and 60% respectively. On a YoY basis, the same was 20% and 25% down with respect to tenders and awards. On a positive note, our prospects pipeline for the remaining nine months of the current financial year, is pegged at Rs. 8.96 trillion as against Rs. 9.06 trillion at the beginning of the current financial year.

The order book at Rs. 3.23 trillion is at near record high levels.A large and a diversified order book provides us multiyear revenue visibility currently having an average execution cycle of around 27 months. Currently, 80% of our order book is domestic and 20% is international. Within international, around 60% of the order book comes from Middle East and the remaining 40% from Africa and Southeast Asia. 89% of our total order book comprises of Infrastructure and Hydrocarbon, with Infrastructure having 76% and Hydrocarbon having 13% share. Within Infrastructure, our order book is well spread out across the various businesses like Heavy Civil, Water, Buildings & Factories, Power Transmission & Distribution, Transportation Infrastructure and Minerals & Material Handling. The composition of the domestic order book, which today is 80% of the overall order book comprises of central government share at 9%, state government at 31%, public sector corporations at 43% and private sector at 16%.

Coming to revenues, our revenues for Q1 FY22 at Rs. 293 billion registered a growth of 38% over a low base of Q1 FY21. International revenues constituted 38% of the revenues during the quarter. This was despite the project progress in Q1 FY22 being impacted by regional lockdowns, intermittent supply chain disruptions, a below optimum labor force and shortage of industrial oxygen. Some of these factors impacted manufacturing and site execution.

Our revenues excluding the services and concessions business at Rs. 179 billion for Q1 FY22 has registered a growth of 57% over the quarter of the previous year. Let me also mention here that in Q1 FY22, we have caught up to the revenues of Q1 FY20, thanks to the healthy portfolio mix of EPC projects, manufacturing and service businesses.

The group level EBITDA margins at 10.8% for Q1 FY22 is 320 bps higher than Q1 FY21, primarily due to improved overhead recovery. EBITDA margin excluding the services and concessions business has improved from 6.5% in Q1 FY21 to 8.9% in Q1 FY22, attributed to higher overhead recoveries despite input cost headwinds. The details on EBITDA margin are given in the annexures to the analyst presentation. As guided in our previous call that we had on 15th May, we will endeavor to maintain our core business margins at the same level that we printed for FY21. Our current composition of variable price contracts, jobs that are expected to cross margin recognition threshold in the current year, cost contingency releases for jobs that are near completion, overhead optimization initiatives, enhanced productivity through various digitization programs, value engineering and wastage control initiatives, negotiation with some of our key vendors and discussions with clients on use of alternate varieties of inputs should hopefully see us through in terms of managing costs headwinds during the current year.

Coming to PAT, our overall PAT for Q1 FY22 is at Rs. 12 billion as compared to Rs. 3 billion in Q1 FY21. This is largely due to the stabilization of operations in the current year as compared

to the corresponding quarter of the previous year. Anyway, Q1 FY21 would not be a right reference point for comparison because a major part of the Q1 of the previous year was affected due to the national lockdown. However, if we compare our PAT with Q1 FY20, that is the year prior to FY21, you will notice that our overall PAT in Q1 FY20 was Rs. 15 billion vis-à-vis Rs. 12 billion in the current quarter. Both Metro operations and the Financial Services business have been disproportionately impacted by COVID. Had this not happened for these one offs, our Q1 FY22 PAT should have been higher.

Coming to working capital, our Net Working Capital to Sales ratio has improved from 26.8% in Q1 FY21 to 22.9% in Q1 FY22. One of the reasons for improvement in NWC to Sales is due to the denominator, that is the revenues moving higher. Having said that, let me mention here that our customer collections have improved in the current quarter over the comparable quarter of the previous year. Our group level collections in Q1 FY22 were at approximately Rs. 276 billion vis-à-vis Rs. 252 billion of Q1 FY21. Let me also mention here, that on a sequential basis, our NWC to Sales ratio has marginally worsened from 22.3% in Mar'21 to the current level of 22.9% in Jun'21. This is primarily due to release of supply chain payments that fell due in the current quarter. If you could glance through our Cash Flow Statement, given as part of the annexures to the analyst presentation, our net cash from operations is a minor negative at Rs. 7.9 billion. In summary, we have been able to preserve our cash levels in a predicted and a seasonally weaker quarter. As mentioned in the previous earnings call, we will again endeavor to maintain our NWC to sales ratio for the full year at around the Mar'21 levels, which was around 22.3%.

Pursuant to the repayment of liabilities in our financial services business, power development business and to some limited extent at the L&T parent entity during the current quarter, our group level gross debt to equity and net debt to equity levels have improved in the current quarter as compared to the quarter of the previous year. The details are mentioned in the balance sheet page that is attached as part of the annexures to the analyst presentation. Finally, our trailing 12-month ROE is at 17.2% in Q1 FY22 vis-a-vis 12.7% in Q1 FY21. The trailing 12-month ROE for Q1 FY22 also includes gain on the divestment of the E&A business that happened in Aug' 2020. Suffice to say the return ratios internally are being pursued very rigorously. Going forward, a robust business portfolio, focus on cash generation and distribution and the progressive divestments of some parts of our business portfolio should hopefully get us there.

The group performance P&L stack is available in the analyst presentation and the major variations have been explained. You may kindly go through the same. Very briefly I will comment on the performance of each of the segments before we conclude on the environment and outlook.

Coming to infrastructure, order inflows at Rs. 110 billion in Q1 FY22 is well spread out across the various sub segments.Let me mention here that during Q1, we did witness pandemic induced delay in tendering and award activities. Our order prospects pipeline for the remaining nine months of the year for the infrastructure segment remains very healthy at Rs. 6.4 trillion, up by 33% as compared to Jun' 20. Order book in the segment at Rs. 2.45 trillion as on 30-Jun-21 is quite healthy. Revenues for the current quarter at Rs. 104.1 billion registered a strong growth

over the corresponding quarter of the previous year despite the COVID second wave challenges. Consequent to a better job mix and as I said earlier, a higher recovery of overheads, our EBITDA margins in this segment improved from 6.3% in Q1 FY21 to 7.1% in the current quarter, despite commodity price inflation affecting input costs.

Going to Power, the receipt of a flue gas desulfurization order in Q1 FY22, boosted the existing large order book in this segment. Revenues for Q1 FY22 at Rs. 7.6 billion is up more than 100% with various projects in the order book gaining execution momentum. Better execution progress drives the margin recovery in the current quarter. As you may be aware, the profits of the manufacturing part of the EPC power business, i.e. the Boiler and Turbine business and the other Power JV companies are consolidated at PAT level under the equity method of accounting.

After that, I come to Heavy Engineering. Again, in this quarter, this segment had multiple order wins in the refinery, oil and gas verticals. Revenues for the quarter at Rs. 5.5 billion registered a growth of 45% over Q1 of the previous financial year. On account of improved execution across multiple jobs, their margins also consequently improved in the current quarter.

Coming to Defence, we believe the policy pronouncements and the recent indigenization drive of the government will drive order inflows in the segment in the medium to long term. Revenues for Q1 FY22 at Rs. 6.9 billion is up 46% on better job progress. Q1 FY22 margins for this segment was contributed by cost savings and contingency releases in certain jobs. At this stage, I would like to reiterate that this defense engineering business does not manufacture any explosives nor ammunition of any kind, including cluster munitions or anti-personnel landmines or nuclear weapons or components for such munitions. This business also does not customize any delivery systems for such munitions.

We come to Hydrocarbon segment. This segment had subdued order inflows in Q1 FY22 as we did face elevated levels of competitive intensity. Having said that, I wish to mention here that due to lower levels of ordering witnessed in the business since the second half of FY20, the prospects pipeline has significantly improved largely due to the recent pickup in oil prices. Our prospects pipeline in this segment for the balance 9 months of the current year is at Rs. 1.82 trillion which is significantly higher than Rs. 668 billion at the end of Q1 of last year. Revenues for the current quarter at Rs. 41.9 billion is up by 37% over Q1 of FY21. The strong execution activity drive revenues in the current quarter. Secondly, Q1 EBITDA margin improvement is aided by cost savings and a one-time claim.

Moving to development project. This segment includes the Power Development business portfolio of two operating assets, a 1,400-megawatt coal-based power plant in the state of Punjab, and a 99-megawatt hydel based plant operating in Uttaranchal. Besides these two assets, we also operate and report under this segment the Hyderabad Metro. The roads and the transmission line concession part of L&T Infrastructure Development Projects (L&T IDPL) is consolidated at PAT level under the equity method of accounting.

The revenues for this segment at Rs. 11.3 billion this quarter registered a growth of more than 100% of the quarter of the previous year, largely due to the Power Development business and it is because of the strong power demand, the Nabha power plant, the coal-based power plant in Punjab was operating at a PLF of 90% in the current quarter. Coming to Hyderabad Metro, unlike in the previous year when the metro services were completely shut, in the current quarter, the services did remain partially operational with restrictive timings due to the localized lockdown. This in turn affected the ridership. The Q1 FY21 ridership was averaging around 55,000 passengers per day. However, having said that, as we see now in the month of July, it is now improved to almost 120,000 to 130,000 passengers per day. The segment margin in this segment is affected by Opex under recovery in Metro and the non-recognition of Nabha margin. Since we have impaired the carrying value of Nabha in our books in Q2 FY21 and are looking out for prospective buyers, we do not consolidate Nabha at the margin level. Coming to Metro at a PAT level, the consolidated loss was around Rs. 4.72bn during Q1 FY22. Operating and amortization cost of Rs. 0.75 billion each and the interest cost of Rs. 3.7 billion were incurred for the quarter with respect to Hyderabad Metro.

At this juncture, let me give you a quick status update on divestments of our concessions portfolio. For our Power Development assets, comprising of Nabha and Uttaranchal, we are looking to divest our entire stake in both these projects. Coming to IDPL, we are exploring to divest our remaining 51% stake in favor of other third-party investors. Discussions are on currently with prospective buyers, however premature to comment on the timelines at this stage. As far as Hyderabad Metro is concerned, we are looking for new investors to putting new liquidity into the project. Discussions are on with the state government for assistance and we are also exploring the possibility of refinancing the current debt with a new debt having an extended tenure.

Now I come to the IT and Technology Services segment. The revenues for Q1 FY22 at Rs. 72.2 billion is up 7% q-o-q basis and 20% y-o-y basis, reflecting a surge in demand for technology led offerings in the sector. The export billings constituted 93% of the total customer revenues. The EBITDA margin improvement in the quarter is led by improved utilization, a more favorable onshore offshore ratio and operational efficiency. All the three companies in this segment are listed entities and the detailed results are already available in the public domain.

Coming to Others segment that comprises of Realty, Construction Mining Equipment, Rubber Processing Machinery, Industry Valves and Smart World & Communications. In Q1 FY22, there was a broad-based revenue and margin growth across all the businesses as compared to the quarter of the previous year.

Lastly, financial services. This segment was one of the segments besides Hyderabad Metro which was also affected due to COVID. L&T Finance Holdings is again a listed entity and the detailed results are available in the public domain. Q1 revolved around pickup in rural and infra disbursements, robust collections, improved net interest margins & fees and maintenance of adequate liquidity on the balance sheet. The business continues to pursue the strategy of higher retaili-sation of its loan book, diversification of liabilities, maintaining a more prudent ALM,

and targeting sustainable net interest margins. Sufficient growth capital is available post the rights issue that happened in Jan'21.

Now I come to the final portion of my overview, which is the environment and outlook. We believe that the road ahead is looking a little more optimistic and constructive. With the waning of the second wave and lockdown restrictions being progressively eased, there are definitely good signs of pickup in economic activity. The government with its fiscal stimulus and RBI with its accommodative monetary policy remain committed to support this growth revival. It is a matter of time before the business and consumer confidence comes back. No doubt the household balance sheets have undergone through immense stress in the recent past, however, with the envisaged increased investment spends the employment indicators also should look up in the near future.

Despite the weakness in the first quarter, we do believe that the Indian economy in the current year should be growing between 9% to 10% in nominal GDP terms. However, the first half will be led by low base effect, and the second half will see a sharper recovery. The vaccination efforts have been stepped up and hopefully the third wave will not disproportionately impact the economy. Having said this, I would say that the risk of the third wave and its consequent fallout can be a potentially adverse risk factor. Some of the key determinants for us at the group level revolve around an enabling environmental for better execution going ahead, sustained Capex ordering from the government and better private investment spends, if not in the current year, hopefully in the following financial year. And last but not the least, liquidity conditions continue to remain favorable. Internationally the order prospects also looking far better than what we witnessed in Jun'20.

We remain committed to our guidance of up to a low to mid-teens growth in the order inflow and revenues for the current financial year. As we said earlier, the ex-services and concessions business, comprising of the main EPC and the manufacturing businesses, as we mentioned earlier, we will endeavor to maintain the business margins around the same levels that we printed for FY21 and NWC/Revenues at a group level, we will continue to maintain the guidance of in and around the Mar'21 levels of 22.3%.

As a group, we believe we are positioned well with a healthy order book, strong balance sheet, proven ability to execute large projects and a growing IT and TS portfolio. In the medium term, our focus areas will revolve around cash generation, improved return ratios, exploring newer business areas and sustainability. We remain committed to sustainable business growth in the foreseeable future.

Our integrated report for FY21 should be released latest by mid-Aug 2021. Before I close, our five-year strategic plan is under preparation and should be completed latest by the end of this calendar year 2021. We will articulate our goals around the business portfolio, newer businesses and our sustainability roadmap in detail once we are ready. Thank you for the very patient listening. We will now get into Q&A.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Mohit Kumar from DAM Capital. Please go ahead.

Mohit Kumar: Sir, my question is that are we staying with the order inflow and revenue outlook of 12% to 15% growth and a stable core EBITDA margin as a guidance?

P. Ramakrishnan: Mohit, are you done or should I answer to this?

Mohit Kumar: No, that is the first question.

P. Ramakrishnan: So, as I said, Mohit, when we communicated this, around 14th May, we also knew about the status of affairs of the first quarter because of the COVID situation. We have factored this, while we gave the guidance. We do not want to put a number to it, but what we have stated is that we expect considering the current economic environment, stabilizing of the COVID crisis by the end of June and normalcy returning from the start of July, the government now focusing to bring back the economy by way of higher investment spend and improved international prospects given the rise in oil prices, gives us reasonable confidence that we should be in a position to maintain the guidance of up to a low to mid-teens in both, order inflows and revenues.

Given the fact that we have upwards of Rs. 3 trillion of order book and assuming that we come back to near normalcy from the start of Q2 onwards, gives us the confidence that we should be in a position to maintain around the same levels in the revenue side as well.

Coming to margins, the margins what we have given as a guidance is for businesses which comprises of our traditional business of EPC projects and manufacturing. It is what we had reported for FY21, around 10.3%, excluding the services part and excluding the concessions. We do expect the revenue momentum will continue for the balance nine months and we are reasonably confident that we will be able to achieve the number after factoring into account the recent increases in the commodity prices.

Mohit Kumar: The second questions is on the Middle East; you did speak that the OPEC plus agreement and imminent recovery gives you confidence that the Hydrocarbon segment will see traction. But do you also see any larger improvement in the Power T&D and other segments from Middle East and Africa which gives you a confidence that somewhere around 20%-30% of your order inflows will comprise from Middle East and Africa.

P. Ramakrishnan: So Mohit, out of the order prospects that I just now talked about aggregating to Rs. 8.96 trillion rupees as we see in June, the share of Hydrocarbon business is almost around Rs. 1.8 trillion. And against that, roughly around 70% of that prospects are coming out of international, which is largely Middle East. Similarly, coming to Power Transmission and Distribution, the prospects are roughly around Rs. 1.07 trillion to Rs. 1.08 trillion as at June. And out of that, again, almost 60% of those prospects are outside of India, having a combination largely of Middle East and some part of Africa as well.

Moderator: Thank you. The next question is from the line of Parikshit Kandpal from HDFC Securities. Please go ahead.

Parikshit Kandpal: Sir, my first question is on the asset monetization. So, first one is on Hyderabad Metro. We have been engaging with the government to get some relief. Every quarter, we have been going to them and asking for some relief. So, do you think any tangible momentum has happened from the government side and is likely to materialize in the near future.

Secondly, if that does not happen, you did list out that you are trying to get some investors and also looking at refinancing. So, whether refinancing will happen first and then investor will come in or the investor comes in, and then maybe refinancing may not happen at all? That is my first question.

P. Ramakrishnan: So Parikshit, you have asked a very right question and whatever questions you have asked on various measures, all are at parallel, it is not sequential. So, whereas our discussions with the Telangana Government is going on quite favorable, but as you are aware, it will take some time for the government to take a final decision on that. But I would like to reiterate here that the discussions have been quite positive. And we have been asking. It is very easy for us to get extended concessions period, anyway it is for 60 years.

Citing the COVID situation as force majeure, that anyway could be possible but that doesn't really help us out. So, we are talking to them for financial assistance and they have heard us positively. We do believe that we will see some amount of conclusion on this. Yes, the talks are on also with investors to bring in equity, because at this juncture, the priority is for us is to reduce the overall level of debt. Now the debt reduction can happen in any of the scenarios like, a new investor coming in with equity or the government giving some sort of funds and last and not the least, we are also looking at monetizing the TOD rights, the transit-oriented development rights that we have almost of 18 million square feet. So, there are discussions happening. Now really, it is difficult for me to stage the sequence part of it. Parallelly we are also looking at trying to refinance the existing loan, because the loan that Hyderabad Metro currently has was a loan that was taken at the time of construction. Now that the project is done, we are looking forward to refinance the loan with a slightly extended tenure so that we are able to at least bring down the cash support requirements in the near term.

So, all of this is, again, work in progress. Very difficult to put a timelines on all of these, but we do believe that by Mar'22, we should be in a far more better position from what we are today. As it stands now, like during the last call, we did talk that we have set aside around Rs. 2,000 crores for the next four quarters, out of which we have given cash support of almost Rs. 500 crores in the current Q1. And hopefully a balance of Rs. 1,500 crores should suffice and before that we should be able to get through with whatever things I just know spoke about.

Parikshit Kandpal: So, you preempted my second question. So, you think Rs. 2,000 crores should be sufficient enough before some resolution on the funding side and you may not require further funding support to the projects?

P. Ramakrishnan: So, that is the plan Parikshit, we have today. And we do believe that with the easing of COVID situation, (as I said during my overview that today, the traffic has inched up to 120-140L average ridership per day), as the economy opens up and as all the restrictions go away, we should be in a position to see higher ridership. And also, some of the points that I spoke about, we should get near our visibility of closure by the end of this financial year.

Parikshit Kandpal: So, this financial assistance is basically a concessional loan kind of assistance, which you are seeking from the government?

P. Ramakrishnan: There are many parts to it, Parikshit. It would not be inappropriate for us to really comment on it, but we are talking about financial assistance in many forms. Now, how the government finally gives it or how much they give is a question of time, but we will keep you posted.

Parikshit Kandpal: Last question. On third quarter of FY21 call you highlighted that you had a net exposure of Rs. 1,800 crores of AP receivables and had done Rs. 100 crores of ECL provisioning against that. So, any improvement in that status now? Have they paid you something the last two quarters? What is the status?

P. Ramakrishnan: Sorry, can you repeat that question please?

Parikshit Kandpal: During the third quarter of FY21, you had mentioned that about Rs. 1,800 crores of net exposure to the stuck 80 projects which got cancelled and there was a Rs.100 crore ECL provisioning done against those projects. So, any update on what will be the status now, has that reduced and what will be the ECL provisioning done against those receivables?

P. Ramakrishnan: Okay, roughly speaking, we do have an exposure of almost Rs. 1,200 crores on the AP projects. But I wish to tell you that discussions are on with the various state agencies who have awarded these contracts. Our first objective is to get some of these amounts realized and possibly I do not know whether we will be able to kick start the projects, however some part of the AP projects also is actually funded by multilaterals. To that extent, we should expect a revival. But as it stands now, our exposure to these projects stands at a net Rs. 1,200 crores level.

Parikshit Kandpal: So Rs. 600 crores is the recovery which has happened in last two quarters?

P. Ramakrishnan: Partially recovery and partially attributed to higher provisions.

Moderator: Thank you. The next question is from the line of Sumit Kishore from Axis Capital. Please go ahead.

Sumit Kishore: I have two questions. My first question is that you seem to have added order prospects to your March 2021 tally, because your order prospects seem to have reduced by about Rs. 100 billion while you have got core inflows of over Rs. 150 billion in the first quarter. So, where have these additional prospects come from, can you please elaborate?

P. Ramakrishnan: So, I think Sumit, while I covered that, as of March, our order prospects were aggregating at Rs 9.06 trillion. And today as we report and as we look at it, it is around Rs 8.96 trillion. Just a marginal drop. The drop obviously includes the orders that we have already bagged during the current quarter. But I would like to mention two parts to it, that the hydrocarbon prospects, which was Rs 1.44 trillion as at March end, has jumped to Rs 1.81 trillion as of June. So, that is one of the very important thing which we are looking at, which has attributed to, I would say almost the same levels of order prospects as at June end.

Sumit Kishore: And these incremental prospects are mainly overseas prospects?

P. Ramakrishnan: Yes, in the hydrocarbon against Rs 1.81 trillion, almost 71% seems to be coming outside of India. And coming to the other part of order prospects, where we have seen a reduction because of the passage of time and orders having got awarded is in Infrastructure segment, where we report at Rs 6.97 trillion as an overall subset of Rs 9.08 trillion. That has partially dropped to Rs 6.40 trillion as of June for Infrastructure.

Sumit Kishore: And my second question is, you commented that impact of COVID in coming quarters will be insignificant. You partly covered that, but what gives you that confidence, you know, how much below normal levels was the average workforce availability during Q1 FY22? And where are we right now? And, is there any execution issue overseas as mobility from India may have been impacted because of COVID?

P. Ramakrishnan: Okay so, Sumit, it is like this. During the first quarter, I remember clearly that the call we said that, in the month of April and May, we were averaging at around 170,000 workforce, partially because anyway during the first two months, summer months, we do see a drop, but partially attributed to COVID, that drop was almost 30,000 to 40,000. Normally it should have dropped down to 210,000. But we actually witnessed 170,000 in April and May.

But by the end of June, we were almost at 235,000 to 240,000 of labor force. And for peak execution as per the requirements in Q2, which is again, not the best of a quarter in terms of seasonality because of monsoon, what we need is typically 250,000 to meet our planned targets. So, we are today at almost 235,000. So maybe running at shortfall of about 10,000. But that is not much of a challenge. When I spoke on Covid, I did communicate that our assumptions for the revenue momentum or operations momentum to become normalized is on one assumption that we would not witness lockdowns that will impact the economy from a business perspective. That is either manufacturing or site execution. And despite a more severe second wave, I do not think manufacturing or site execution got impacted as much as what we witnessed in the Q1 of the previous year. So that is one of the reasons that we have been able to demonstrate growth in our businesses outside of services and concessions.

And we do believe with near normalcy, as we are witnessing now, this should hopefully become normal. But again, there is an assumption that the third wave, even if it were to happen, should not impact the economic activity on the business side.

Sumit Kishore: I had also asked that, you know, have there been any execution issues overseas?

P. Ramakrishnan: No. Our international execution, I would say has been near normal at pre COVID level I would believe. We do not have evidence to say about lack of workforce availability. The only one thing which keeps lingering once in a while, is intermittent supply side constraints, especially when it comes to importing into Middle East from outside of other continents. So, there are some delays that are being witnessed, but nothing material.

Sumit Kishore: Okay, but given that travel is a bit difficult right now to Middle East, does mobility of workforce from India to Middle East impact execution?

P. Ramakrishnan: Actually speaking, no. Middle East actually came back to normalcy even before the onset of what we witnessed as second wave. So, Middle East execution went into normalcy from August September onwards itself. So, we have not had a situation like India where we had labor moving back to their native places or hometowns and we had a challenge of bringing them back. In the Middle East, it was not that kind of situation. So, they moved back to the site well before the end of the last calendar year itself.

Moderator: Thank you. The next question is from the line of Ashish Shah from Centrum Broking. Please go ahead.

Ashish Shah: First question is on the HSR projects. So, where are we in terms of the on-ground mobilization, on-ground execution of these projects? And by when do you think, some significant amount of revenue start hitting the P&L for us from the HSR packages.

P. Ramakrishnan: So, Ashish, let me tell you that the work has commenced sometime in Feb'21. Actually, the deadline for us, that is the four years deadline starts from Jan'21 and ends exactly 48 months later. The work is progressing as per the schedule of activities that are done. But I would believe that, a meaningful increase into top line, that is a substantial increase where we will have to articulate that the increase in revenue in the segment is attributed to sufficient progress or major progress will happen or will be witnessed in the next financial year and not in the current financial year.

But I would like to state here that, some of the important things as a contractor that we need to do, because along the parcel right from the entire Gujarat stretch, we are supposed to have places where we can do the concreting and all, the batch mix plants and all that for which we need to take land. I think around 15 or 16 land parcels had to be taken to facilitate the construction and that is all in the scope of L&T. All those enablements have been done, and the progress of work has started in full capacity. But in terms of major accretion to revenue, possibly we could witness maybe in Q4 of current financial year, but a large part would get into FY23.

Ashish Shah: Secondly, when I look at the debt breakup in the presentation, the developmental projects has gone down from about 20,600 to 18,700. So, this reduction of about Rs. 1,900 crores, is that in in the metro or in the power plant?

P. Ramakrishnan: So, in the power plant, we reduced the debt levels by around Rs. 1,250 odd crores because of a favorable settlement that happened of a case that was under dispute. That enabled us to recover a lot of money that was stuck up from the client. That money got released and it enabled us to reduce the overall debt level. And the balance Rs. 600 odd crores was a reduction in the debt level at Hyderabad Metro. So, but actually speaking, that debt level came down because that was third party debt. Obviously, it went into part of our L&T cash support that I just now referred to 10 minutes back.

Moderator: Thank you. The next question is from the line of Renu Baid from IIFL Securities. Please go ahead.

Renu Baid: Two, three questions from my end. First question is on coastal road project, which was significantly delayed. Can you give a broad heads up in terms of where are we in terms of execution phase? And are we through with the margin recognition or that should be expected from sometime in 2Q?

P. Ramakrishnan: So coastal road project, Renu, is almost covered one-third now. We are 32% covered at this juncture. And usually we recognize margins upwards of 25%. So, it has come into margin recognition stage. We do believe that it is going on in a normal way. So, 32% is the completion what we have witnessed today.

Renu Baid: Secondly, in the Hydrocarbon segment while we have seen a strong jump sequentially in terms of prospect list. Clearly, after 18 to 24 months since the orders have come, global players are also very aggressive in terms of pricing. We have lost two orders in the last two quarters. So, what is our perspective in terms of the strike rate in this segment, and what is the expected perspective on the competitive scenario in the international Hydrocarbon orders which are coming?

P. Ramakrishnan: So Renu, you are right in terms of having said that, off late we have been witnessing a lot of competitive intensity. But let me tell you that, we are as much very clearly focused to ensure that we do not want to be seen to win orders by compromising big time on margins. Whereas competitive intensity is there, and obviously, we will be a little more careful while bidding for projects but that does not mean we compromise on profitability. So there has been some slip ups, but we are fairly bullish on a combination of whatever domestic opportunities and international opportunities are there and we stand a good chance to secure some of them in the balance nine months.

Renu Baid: And would it be possible for you to quantify approximately what was the onetime impact in Hydrocarbon margin?

P. Ramakrishnan: The impact of a onetime claim was in the range of Rs. 90 odd crores. But, you know, at the end of the day, with all these things running in a project space, you will have settlements and claims and everything happening. So, I just wanted to say that, yes, margins have gone up because of

onetime claim but does not mean one time claim is one time. You can have claims across each of the segments in every quarter.

Renu Baid: Yes sir, it is a recurring activity, and it is not a very alarming number that one should be worried about.

P. Ramakrishnan: Correct.

Renu Baid: And broadly if you observe the core ROCE on a TTM basis have actually now inched up to almost 21%. This is after two years that is now back to FY19 levels.

P. Ramakrishnan: Can you repeat that question? I did not get your first part, sorry?

Renu Baid: The core ROCE for the L&T ex-services business is now back to 21% levels after two years. It was hovering around 19. Last year it was depressed but even in FY20, it was around 20%. So in the 1Q numbers if we look on a trailing 12-month basis, ROCEs are at 21% plus, which is similar to FY19 levels. So, with this as an improvement in the capital employed or return that we are seeing through should we expect that in subsequent quarters if payment collection remains through the gross debt on book should taper off relatively faster than what we had expected?

P. Ramakrishnan: So Renu, I think you must have heard me, I have stopped using the word core.

Renu Baid: L&T and services.

P. Ramakrishnan: So, we are talking about excluding services and concessions. If I have to talk about what we used to call traditionally the core, which is nothing but EPC projects and manufacturing, whereas I do not want to comment on the numbers that you spoke, but I wish to tell you that for the current year, we are endeavoring to maintain the margin of this part of the business at around 10.3%. The same things that we printed for FY21.

And as far as working capital is concerned, of course the overall working capital is what we spoke about 22.3. But at core level, it could have slipped slightly higher. If we can manage that, I am sure our ROCE should improve. But that is the target. In fact, all the projects which are going under bids, and the way we are executing projects, some of the projects are sometimes kept on a slower pace because collections are not coming in the same way.

We restrict ourselves and we do believe that we will focus on margins stability and also controlling working capital to the best of our capability.

Renu Baid: Sir, broadly the gross debt which has been almost flattish on a sequential basis at Rs. 25,000 crores, one can expect a substantial reduction in that towards the end of the year. So, debt de-leveraging or I would say debt reduction should be one of the objectives of improvement in cash flows?

P. Ramakrishnan: Yes, 100%. Of course, in the first quarter of last year, as a pre-emptive COVID measure to preserve liquidity because we did not expect the collections momentum that actually happened, we went ahead and did almost Rs. 12,000 crore borrowing. Also, at that same time, the fact of the EA IC divestment was not very clear. But definitely at the parent L&T level, the objective is to reduce the debt level sequentially. And that has been happening.

So, we will ensure that liquidity will be maintained to the extent of what is required based on the overall investment requirements and managing the overall working capital situation. The rest of that will be used to retire all the debts that is falling due.

Renu Baid: And if I can ask one more question. In Nabha Power, you mentioned that since the project is up for sale, we are not consolidating the profits at the margin level. So, do we have any internal timelines or targets that we are targeting this in the next six months, nine months or within the current financial year or it is still open ended?

P. Ramakrishnan: So, I do not want to comment on the timelines, Renu. But I wish to tell you that talks are on with prospective investors. At least it is now known to the market that both these two assets are for sale and hopefully, we should see some developments happening. But very difficult to comment on timelines unless and until we get into a sort of what we call as a typical binding agreement or settlement.

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

Renjith Sivaram: Sir, the infra margins have been healthy. So, is there any kind of a provision right back or what is the sense you are getting on the infra margins?

P. Ramakrishnan: So, for Infra margin, I think I did communicate that current quarter was 7.1% as against 6.3% for the Q1 of the previous year and that has been largely on the back of an improved execution despite the COVID second wave. It has also factored some amount of steel price increase that has come because of impact on the input cost materials. But Renjith, we are working on multiple things to mitigate the steel price or the cement price increase in this part of the business.

Major part of the infrastructure segment orders, I would say a substantial part, are actually variable price contracts. So, to that extent, that will partly mitigate the cost increases. But more important is that this year, if we do as per our plan, we do have some decent number of jobs getting into margin recognition threshold and if there is a volume recovery i.e. site execution stabilizes with no kind of COVID restrictions or any lockdown protocols, then that itself will enable us to cover those thresholds and recover a major part of our overheads. And touchwood as it stands now, the job mix that we are witnessing in the infrastructure side are a mix of orders that are all as per schedule and not getting into major cost overruns. Whereas in some jobs you could have but those kinds of jobs also have the perspective of some claim releases and settlements. So overall, we do believe that we should be in a position to maintain the infrastructure segment margins at these levels as what it had printed for FY21.

Renjith Sivaram: Just wanted to reach out, is this coastal road getting into margin recognition? Was that a factor which led to this improvement?

P. Ramakrishnan: No Renjith, let me tell you I was responding to a particular project progress. In infrastructure segment we operate around 800 sites are there. So, which means roughly around 600-700 projects are there under execution. It is not necessary that one project went into margin recognition threshold enabled us to have this higher margin. It is a combination of various factors. And let me tell you, it is not that each and every project gets into a complete profitable execution, we do have negative surprises. But as I said earlier, our ability to execute in terms of volumes by which I can absorb a major part of overheads and also successfully complete the project on time, including some claims that we put on the client, adjust for claims of the client on us, with all these things into taken at a holistic level, we do believe that if the volume uptick happens we should be in a position to improve or sustain the margins that we reported last year after factoring the input cost increase, which will have an impact on the fixed price contracts.

Renjith Sivaram: Okay, and there was some news flow regarding the submarine order. Some of the technologies they are not likely to go with. How are we placed? There is expression of interest have been placed. So, do you see a light at the end of the tunnel this year or anything that like we should be happy about in that submarine contract which has been long overdue?

P. Ramakrishnan: So Renjith, I will put it like this, as this is a sort of classified to the extent it is available in the domain, I can definitely comment on that. Yes, the Defence Advisory Council has cleared the P75I which is India based indigenous supply of submarines. The RFP was issued last week, if I remember I think it was on 20th of July and we are supposed to submit our response within four months, unless the government extends it or the customer extends it.

At this juncture, I can say, that we have got RFP and we are supposed to submit the RFP response within four months, which is again maybe 20th of November, unless extended by the client.

Renjith Sivaram: Okay, so our technology is in line with what they want, there is no negative surprises for us?

P. Ramakrishnan: We are supposed to, as part of the requirement, also have a technology partner to it. But at this juncture Renjith, this is all I can say. We do believe that it should not be a problem for L&T per se. The only thing is we have to submit our response on or before the end of four months.

Moderator: Thank you. The next question is from the line of Sujit Jain ASK Investments. Please go ahead.

Sujit Jain: In NWC and correct me if I am wrong, it was at around Rs. 21,000 crores for E&C and manufacturing and Rs. 27,000 crores overall consol. What those numbers stood as on June?

P. Ramakrishnan: The core which was Rs 21,000 crore as of June has become Rs 22,000 crore, with almost an increase of Rs. 1,000 crore. And at a consolidated level, that Rs. 27,000 crores odd NWC has become around Rs. 29,500 crores. And I would say, this is primarily because of our current liabilities i.e. vendor payouts have actually gone up substantially, by almost Rs. 3,000 odd crore

that we have paid as per schedule. But at the same site because of higher activity levels, obviously the invoicing on the clients also happened big time in the current quarter and some of that we will get into collections mode in the next quarter or subsequent quarters depending on the terms of payment.

So, let me tell you, Sujit at this juncture, if you have observed the movement of what we call the projects business part of the working capital, normally the way it happens is that, because of the enhanced Q4, when the customers also ensure a faster pace of certifications and they also release a lot of money as part of their overall budgets that gets completed, you will find that the working capital situation improves maximum during the Q4 and then it worsens in Q1 and then slowly improves. So, today as we speak, the number which I talked about at a group level of 22.9 is as expected, it is not that it is not expected and in fact, it is slightly better than our own internal estimate.

This gives us that at a group level, when we close for FY22, obviously with the caveats of all the third wave and other things coming back to normalcy, we do believe that we should be in a position to maintain the working capital in and around the 22.4 levels of FY21.

Sujit Jain: Got that and for the core what this NWC number would have stood? The consol is 22.9, core would have stood at what level?

P. Ramakrishnan: That will be around 25%.

Sujit Jain: And the ROE ex of the onetime gain of E&A would have been what?

P. Ramakrishnan: Around 11%-11.2%.

Sujit Jain: Okay. And for Hyderabad Metro, what is the absolute debt and equity as on June?

P. Ramakrishnan: Our absolute debt is around Rs. 13,500 crores - Rs. 13,600 crores and equity what we have put is around Rs. 2,541 crores and cash support will be another Rs. 5,000 odd crores.

Sujit Jain: Right and lastly, if we include Rs. 1,000 crores and you are saying Rs. 2,000 crores?

P. Ramakrishnan: No, with cash support which includes equity, our total exposure in Hyderabad Metro would be in the range of Rs. 5,000 odd crores and Rs. 13,600 crores is the debt.

Sujit Jain: You have guided that this year we may have to support by around Rs. 2,000 crores. Rs. 500 crores you have already given as support in Q1 and I believe that last year we have infused about Rs. 1,000 crores, right?

P. Ramakrishnan: Yes, last year from Q2 onwards we infused up to Rs. 1,000 crores until March and we have set aside another Rs. 2,000 crores in the current financial year. Out of which Rs. 500 crores have gone in the first quarter.

Sujit Jain: Right. And one last question is that, how much is the actual number of contribution of PAT from realty and IT services business?

P. Ramakrishnan: I think I would request you to kindly go into the segment result which shows the PBIT of those businesses. It would not be right for us to calculate and report the PAT for those segments per se. As far as IT&TS segments are concerned, their respective PAT whatever they have reported, you just take with respect to LTTS and LTI at 75% and Mindtree would be 61%.

Sujit Jain: That I can get but what realty would have contributed in June quarter? Because the margins have gone up?

P. Ramakrishnan: So, I will put it like this. In the other segment, of the total revenue that we have posted, realty would be in the range of Rs. 330 crores and PAT would be around Rs. 100 odd crores, but that would be a basis number.

Moderator: Thank you. The next question is from the line of Ankur Sharma from HDFC Life. Please go ahead.

Ankur Sharma: Just two questions from my side. One, you know, given that labor is largely kind of back to normal, is it fair to assume that, without a third wave coming in, we at least go back to the sales we saw in Q2 20, you know, for this quarter? If not more that is?

P. Ramakrishnan: See, let me put it like this that, I would only maintain what I said earlier, that when we gave the guidance on revenue, up to a low to mid-teens, we factored that Q1 would be a little subdued because we gave those guidance in the middle of the second COVID wave. So, we knew what actually Q1 was looking like. But we also communicated that we should be able to demonstrate this revenue growth on the back of no restrictions coming into effect from Q2 onwards.

If those things are normalized, hopefully you should see a better set of numbers that finally aggregate to what I spoke on our guidance of low to mid-teens in revenue.

Ankur Sharma: So, it is just the question of labor normalizing and things being okay and not about any significant headwind to execution on the order book side, right, in terms of right of way or environment, etcetera?

P. Ramakrishnan: Okay, that way, I will tell you that whatever our internal estimates are there, they are all on the basis of whatever active order book that we are having. Basis that and with the assumption that there is no COVID third wave and everything comes to normalcy gives us the confidence to see up to a low to mid-teen kind of a growth.

Hopefully, I think by the end of Q2, maybe we will be in a better position to finally put out a number because the issue is that, we can say the assumption, but we do not know how the whole thing pans out. Of course, this time around, let me tell you, at least not only at L&T, at an economy level, people now know how to face the third wave, and with all these improved

vaccination efforts, it gives us the confidence that we should be far more better positioned to manage the execution.

Ankur Sharma: Okay, and just one quick one. While you did mention about Rs. 90 crores kind of claim in Hydrocarbon, there also seems to be some kind of a contingency release in Defence business. Could you quantify that please?

P. Ramakrishnan: No, that is not material. I am saying it is, at the end of the day, the margins for the defence machine is at around 20% odd. So, it is a combination of various jobs that went into closure. Usually, the last bit of contingencies that get released. So, that is a mix out there. I will put it that way.

Moderator: Thank you. The next question is from the line of Aditya Bhartia from Investec. Please go ahead.

Aditya Bhartia: Sir, you spoke about non recognition of Nabha Power margin. I just want to understand where exactly is it getting recorded now?

P. Ramakrishnan: Okay, like, for example, what we did, in Q2 of FY21, the group decided that this asset will be put up for divestment. And consequently, we have capped the carrying value of that asset in our books at what we believe should be our realizable value. So, since then, we only take Nabha's revenues and costs. But we do not factor the margins.

That margins get impaired in one of the schedules in our financials so that we keep the carrying cost at the same level, unless and until we are able to seeing a higher realization, or maybe even a lower realization, either which way.

Aditya Bhartia: And secondly, you spoke about margin improvement happening on account of better overhead absorption. And this is really interesting. Because Q1 itself has been a bit of a disrupted quarter. So, does that mean that, had there been no second wave, we would have managed to cut our overhead costs to an extent our margins would have looked better than what we are seeing today? And also, is overhead reduction being that material, that we are able to offset complete RM cost increase and still able to show some improvement in margin?

P. Ramakrishnan: So, actually speaking, I will tell you that in absolute terms the overheads may have gone up, but the thing is that, when you are in the projects business, it is not necessary that your revenue is only a combination of whatever we report in manufacturing, construction and operating expenses. Part of the direct project related spend also gets factored into staff costs and in the other operating expenses schedule that we have on the advertisement.

So higher recovery, because some of these costs like staff costs and part of operating expenses could be largely fixed. So, the more amount of site productivity output that we manifest, obviously means that we are able to factor that in our billable costs and get into recovery mode. And consequently, as a share of revenues, if you see staff costs and also manufacturing construction operating expense that has come down, that is essentially the margin recovery that

is visible. And obviously, there can be other reasons, as I said, in the earlier part of the call, claims, counterclaims, ECL provisions, reversal of ECL provisions because of collections, all of that is part of the overall margin stack up.

Moderator: Thank you. The next question is on the line of Subhadip Mitra from JM Financial. Please go ahead.

Subhadip Mitra: You did mention that you know a significant portion of the infrastructure order book has variable price contracts. So, is it possible to quantify in terms of a percentage?

P. Ramakrishnan: I will tell you that at a global level, when we are talking of a Rs. 3.23 trillion order book that we have covering the entire project segment, roughly around 40% is fixed price contracts and 60% is variable price contracts.

Subhadip Mitra: So, from infra or hydrocarbon, it is not going to be possible to give those split ups?

P. Ramakrishnan: At this juncture for some reason, see we keep it at the overall segment level, Subhadip.

Subhadip Mitra: Also, I think, in the early part of your commentary you had given this breakup of the 80% domestic orderbook, between government, PSU etcetera. I missed those numbers. If it is possible to just repeat that?

P. Ramakrishnan: 9% is from Central Government, 31% is State, Public Sector Enterprise is 43% and the last 16% is private.

Moderator: Thank you. Ladies and gentlemen, due to time constraints, this was the last question for today. I would now like to handover the conference over to Mr. P. Ramakrishnan for his closing comments.

P. Ramakrishnan: So, thank you Rutuja and thanks to all of you for participating in this call at this late hour. I wish you all the good luck and all the best. In case if anyone of you have specific questions, please reach out to me or my colleague Harish. To the extent possible we will try to clarify that. And thanks for your time. Thank you.

Moderator: Thank you. On behalf of Larsen & Toubro Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.