"Tata Motors Conference Call"

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Moderator: Ladies and gentlemen, Good day and welcome to the Tata Motors Conference Call. As a reminder, all participant lines will be in the listen-only mode. During the course of the call, if any participant intends to ask questions, they can use the chat box option appearing at the bottom of the screen to submit the question to the speakers. All questions will be taken up at the end of the session. Please note that this conference is being recorded. I now hand the conference over to Ms. Sneha Gavankar from Tata Motors. Thank you and over to you, ma'am.

Sneha Gavankar: Thank you and good day to everyone on the call. On behalf of Tata Motors, I would like to thank you for joining the call on short notice. This call is a Follow-Up of the Press Release Yesterday on the JLR Q1 FY'22 Sales Volume and Semiconductor Supply Situation and the subsequent queries we have received since.

Today, we have with us Mr. Adrian Mardell -- CFO, Jaguar Land Rover; Mr. Bennet Birgbauer -- Treasurer, Jaguar Land Rover; Mr. Dhiman Gupta and Mr. Vijay Somaiya – Treasury and Investor Relations, Tata Motors.

We shall start with an update from Adrian to set the context around yesterday's release on the Q1 sales numbers and the commentary around the Semiconductor Supply situation. This will be followed by a Q&A session led by Mr. Mardell. I now hand the conference over to Mr. Adrian Mardell from Jaguar Land Rover. Thank you and over to you, sir.

Adrian Mardell: Many thanks, and good afternoon, everybody. This is Adrian Mardell, and as you know, I am the CFO of Jaguar Land Rover. Thank you for joining the call today so we can update you further on our latest sales results and also, of course, update on Semiconductor Shortages, which we issued in the notes yesterday.

As indicated Jaguar Land Rover retail sales for the three month period to the 30th of June were 68% higher than the same quarter last year, reflecting the continued recovery from COVID from a demand perspective. You will also note that quarterly number was slightly higher than our Q4 retail levels. However, wholesales in particular were down about 30,000 units from a level we would have anticipated given the demand. It's about 27% lower than demand would have permitted. It's due to the semiconductor supply issues affecting the global auto industry.

Planned volumes for Q2 were originally close to Q1. And so now a 50% reduction in Q2 is of course greater than Q1. Let me be clear what that 50% means. I don't mean 50% lower than Q1; I mean 50% lower than we would have anticipated the demand to have required in Q2. Let me be even clearer; wholesales in Q2 will be lower than Q1 probably in the range of 60,000 to 65,000 units' wholesales in Q2. Now when I say 50% lower than we were expecting, we would have expected a wholesale number of about 120,000 units. So my 50% is at the lower end of the range of our expectations in Q2.

Let me go on to Production Data. Production back to Q1 was 75,000 units and finished vehicle inventory as a result, of course, was down to about 31,000 units at the end of June. We also have built WIP about 7,000 units. Now if you want to moderate what normal WIP is, it's about 3,000.

So we built an additional 4,000 cars ready for sale as soon as chips arrive. This situation of course has been very dynamic. However, this level of supply impact has been largely expected and was broadly expected to continue in Q2. That's the 27% level. In our Q4, full year results, we indicated we expected shortage to continue to impact half one and improvements only to start in the second half of this year. What has changed since then, is unfortunately, as suppliers only gave us visibility in the last week of June, Q2 supply could be constrained as much as the 50% level, I've now clearly referenced. We still expect the situation to start to improving in half two. That's a key point here. As certain specific capacity reductions come back online, for example, related to the fire in Japan, but we also expect continued, for a period of 12 months maybe up to 18 months, the situation not to fully normalize. What do I mean by fully normalize? I mean, being able to supply levels to what we now see is underlying demand.

Okay, I am back online. I'm going to backtrack, just two or three sentences for those who drifted away. Some of you may hear this for a second time. In our Q4, full year results presentation, we indicated we expected shortages to continue to impact half one, and improvements to only start from half two. What has changed since then, is that unfortunately, some suppliers towards the end of June gave us clear visibility that supply in Q2 could be constrained as much as 50% in that quarter. With the data I've clearly actually listed. If some of you drifted off that while I said at that point, wholesales look like they will be in the range of 60,000 to 65,000 units. And the 50% number is supportive of a demand level we see, which would have meant wholesales would have been 120,000. And therefore, our 50% reduction is actually at the lower end of the range of what we expect to happen in Q2. We still expect the situation to start improving in half two, in part a certain capacity reductions come back online, for example, related to the fire event in Japan. But we also expect it to take 12 to 18 months for the situation to fully normalize, i.e. for us to support the levels of production and wholesale that retail demand is currently showing. As well of course, as the general industry capacity starts to be added which will happen as we know at the end of that period. In this scenario, we expect free cash outflow of about £1 billion with negative EBIT margin both in Q1, that's a validated number for Q1, but also in Q2. The cash restructuring charges related to Reimagine were expected to be minimal in those quarters. Working capital, of course, was significantly unfavorable in Q1, reflecting lower payables partially offset by lower inventory. And working capital will continue to be negative in Q2, but much less negative. The bigger driver behind the Q2 cash is the lower absolute wholesale value. 84,000 wholesales in Q1, a range of 60 to 65 as we currently see it in Q2. We expect free cash flow to significantly improve in half two as chip supply improves and the working capital items will either flat line out or eventually of course reverse. Let me point you towards last year when we had a 1.1 billion working capital negative in Q1 that was pretty much fully reversed across the balance of the year when production came back on line. It will be so this year when production comes back on line. We, of course, have been managing the chip supply issue and we've been managing the chips to the highest percentage margins and most valuable units.

As mentioned, the visibility given by suppliers on the supply situation came in only a few days before the end of June Now, there were visibility before that which we were managing away with allocations and shortages to vehicles. This latest visibility in Q2 was not possible to manage away further than the levels I have announced.

However, the really big point here is we are seeing strong demand across our markets; we now have record order banks of 110,000 vehicles. And if you understand our order bank process, it really only happens in three regions; UK, Europe and overseas. Order banks in China and North America, because they take cars from stock, don't really happen. So that level of vehicle [orders] is mostly just from three of our five regions. That shows you the confidence we have in the retail levels and the speed it will kick back once those chip supply positions improve. So this is a temporary supply phenomenon. And in the meantime, demand and customer orders are growing. Our obligation is to support those orders as soon as we possibly can do of course.

We are right now not expecting any significant launches to be delayed. The New Range Rover, we do not expect to be delayed as a result of these challenges. Although initial production volumes, of course, will depend on this chip supply at that time.

In the meantime, of course, we will be doing everything possible to mitigate the impact including prioritization of production of higher margin vehicles, for the chip supply available, as well as making chip and product specification changes where possible. So, we are looking to change features on vehicles which enable ongoing supply of chips and therefore vehicles to be produced. We are taking strong steps to ensure the security of our supply chain in the longer term also. We have actually been working to that, of course, for several months. We are working with our suppliers and our chip manufacturers, that is a change. Previously, everything went through our first tier suppliers. And we're working with the source to directly increase the visibility and control over chip supply for our vehicles. Ultimately, the 50% impact in Q2 is a function of overall capacity in Q2, combined with some specific supplier issues, such as the fire in Japan. We honestly don't know yet about what other OEMs are seeing in our Q2. Of course, we're aware of what they've communicated mostly in their Q2, which was the quarter to June. But we don't know what they are thinking or communicating for our Q2 through 30th of September '21. We do know of course that at least one other OEM communicated a 50% impact in the quarter through to the end of June. We were less impacted in that quarter with the 27% we actually experienced.

With this recap of the situation, I will run through some specific questions. I'll pass it back to the moderator for any specific questions. Many thanks for listening.

Sneha Gavankar: Thank you, Mr. Mardell. We can now begin the question-and-answer session. The first question is from Mr. Ruchit Mehta from SBI Mutual Fund. What is the system inventory at the end of the first quarter that's dealer plus factory plus transit? This inventory plus the planned production can support what level of retails, and on which product line is the inventory the leanest?

Adrian Mardell: Okay, so I'll give you a total inventory number… I've already given you unwholesaled inventory number. The total inventory number at the end of June is about 74,000 units. Now, the production levels for Q2 are going to be somewhere between 55,000 and 60,000 units. That's the latest intelligence we have. And from that, given the inventory position, our determination is the wholesale levels are in that 60,000 to 65,000 unit range in Q2 previously mentioned.

Sneha Gavankar: The next question is from Mr. Pramod Amte from InCred Capital. Considering the current production challenge, will you be delaying your new launches and CAPEX for FY' 22?

Adrian Mardell: So, we have no plans to delay our current launches as a result of any issues we see today. Key point here, right. So there are no delays in our launch readiness as a result of any of the issues that we have in current production today. However, launch readiness and delivering full production units is still several months away. Of course, I said 12 months away on the call last May. So let me say, its nine months away. So it'll be early next year and supply of chips next year which will finally determine the levels of production we may have on the New Range Rover, but we have no plans to delay the launch of the new car. In terms of CAPEX, our guidance was £2.5 billion for the year. You'll see when we finally declare Q1, the numbers going to be around £600 million. My expectation is Q2 will be a similar number. So the first half capital investment will be consistent with the full year guidance. I have no intention to delay capital expenditure on new product, none at all. From what I see today, there is no need to do so.

Sneha Gavankar: The next question is from Mr. Sonal Gupta from L&T Mutual Fund. Can you please explain if we were getting enough chip supplies for production in Q3 and Q4? And why has it deteriorated so much -- is it due to supply of plants shutting down or has JLR allocation reduced?

Adrian Mardell: So let me talk about different causes of semiconductors. There are disaster events in Japan and in Texas. Those will eradicate with time, they'll be the first ones to eradicate. Obviously, the scale of reproduction for those plants which were devastated will take time, but supply will progressively come on board from the chip supplier in Japan and the chip supplier in North America over the course of the second half. Exactly the speed of that, I would be misleading you to say I knew, but it will increase progressively as we go into half two. The overall capacity issues in the industry, of course, is not just an automotive phenomenon. It's a consumer phenomenon. So the ability for chip suppliers to add increased production becomes the final inhibitor. And that's where the reference in the announcement talks to the 12-months to 18-months. So it's reasonable to assume we will progressively increase production over the next 12-months period from the level we've given you as our best estimate in Q2.

Sneha Gavankar: The next question is from Mr. Pramod Kumar from Goldman Sachs. Will the exceptional charge further increase the cash outflow beyond the 2 GBP billion number guided for H1 FY'22? And what led to this drastic change in production guidance between the Q4 call and now? Can you please guide on your H2 FY'22 production schedule?

Adrian Mardell: So what can I tell you? I can tell you production will be higher in the second half than the first half for the reasons that I've already said the Japanese issue is getting resolved, albeit slower than everybody would wish. And the issues in Texas are getting resolved, albeit slower than everybody would wish to do so. When we actually announced in May, those Q2 shortages from those sources were not known to us. We were working to the planned schedule that we originally had. And the reality is bringing production back onboard has been more difficult. Not only will we suffer from that, others will suffer from that as well. So as I've mentioned, we don't know what others will communicate and say, but there will be some impact from some others, depending on where they source their semiconductors from. The Q2 cash position is much worse than we were expecting in Q2. Why? Because the whole sales are up to 50% lower than we're expecting. How much that impacts the full year, will totally depend on the speed of build in the second half of the year. There will be a dramatic rebound once we start building towards normal levels. Let me take you back to last year; last year, we lost £1.6 billion cash in the first three months. And we generated £1.8 billion in the following nine months to give us the best cash performance for five years. Clearly, if you measure on a fiscal year basis, the full impact of this may not have actually transpired, i.e. the full reversal of Q2. But that reversal will happen, we can actually build back and it may be we end up with one of the best quarter ones we've had for seven, eight years. I don't know yet. It really depends speed of reproduction. But once we're able to build cars, the reversal of these issues will happen very quickly.

Sneha Gavankar: The next question is from Avi Hoddes from Sandbar Asset Management. Historically, JLR would wholesale 10% to 15% more cars in fiscal Q2 versus fiscal Q1. Would that have been your prior expectation this time around?

Adrian Mardell: Look, rather than use percentages, let me be really clear on what my expectations were. My expectations were 115,000 wholesales in Q1, 120,000 in Q2, 235,000 in first half. Hopefully, that really does explain rather than use percentages here. I think the obligation is for me to be very, very clear what I would have expected before the semiconductor issue. What we actually did in Q1 was what I would have expected when we actually talked in May time for Q1. I expected in Q2 to be a bit better than that actually, but just a few thousand units. The news here, as a result of the latest schedule we receive from some key suppliers at the end of June, when I knew my expectations for Q2 needed to be moderated down below to the level I've just said down to 60,000 to 65,000 units. Final point on quarter two, we haven't given up, right? I can assure you every day, every day, we're talking to sources here. And we're talking to the engineers to actually make simple reconfiguration so we can use other chips. And obviously we'll test those chips. And if it does work, we will introduce them. So nobody's just sitting back and allowing this position to happen. Teams are working tirelessly to speed up the normal return and to improve the short term position, but it'd be wrong of me to commit that we can do that without having that specific knowledge today which I do not have. In terms of the last question, if the reference behind the question was about the Reimagine claims, then my expectation is Reimagine claims will be as we said in May, up to 500 million this fiscal year, most of which will be in the second half of the year. Just a clarification point if that was behind the question, I didn't answer the question fully.

Sneha Gavankar: The next question is from Jay Kale from Elara Capital. Have there been incremental cost pressures too to secure the supplies? Can there be another revision in the supplies of semiconductors at the end of Q2?"Do we have enough visibility for H2?

Adrian Mardell: So on the first part of that question, look, we've been looking for all sources of chips like everybody, right, so we have been able to source a small number of chips from other sources, all tested, all good, all use, I'm talking of a few thousand units, they'll be more expensive. Given the impact here are the paid for 10s of 1000s of units more expensive if we could have sourced them. But there is no noticeable increase in the cost of our material base because of sourcing chips in the first half. And I think, unless I misunderstood moderator, the second half of the question, if it was getting towards expectations for production in the second half, I really don't have anything to add apart from, and it will get better. I don't have precise numbers for the second half at this point.

Sneha Gavankar: The next question is from the line of Chirag Shah from Edelweiss. What is driving sharp shortage suddenly in the last 15 days? Most Europe and US companies have given similar. Is the sourcing of fab from Taiwan a challenge due to lower production given the recent surge in COVID? What kind of chips are an area of issues, new age less than 28 mm chips or traditional chips? Is the diversion of supply to other industries by the fab manufacturers? Can the chip consumption be reduced by increased memory or some other technical changes. And what gives us the confidence that the issue will not get dragged to Q3 and Q4?

Adrian Mardell: There's a lot of questions there. In terms of the supply issues, if I take out Japan, and if I take out the snow storm in Texas, you know behind this, in the tiered base, there are some issues in terms of COVID impacting a number of companies, right, along the whole tier chain. When I talk about the tier chain for supply, there can be five, six companies within a single supply chain here, right, from the source, semiconductor. So, some of the issues are as a result of supply along that chain, if not all sorts of semiconductors, it's just about the ability to build a complete feature through the end chain. So there is some of that. And in this sad world today, some of that will continue into the second half of the year, we know that, we know COVID is hitting different countries at different points in time. And we all want the same thing. We all want for the vaccines to actually start to work to break the link between this horrible disease and significant illness, even death. That's what we all want. But it's happening at different paces along the globe. And we have a global supply network. So we will for a period of time, maybe that 12 to 18 months period, have different disturbances from different suppliers in different parts of the world. That's just the new reality we're in until this disease is neutralized, by the vaccine it looks. So that's going to continue. The new news, which I've mentioned towards the end of June, that's as a result of a discrete number of suppliers - two actually – when they've reassessed their supply from semiconductors, their ability to build, and the exhaustion of the pipeline which they've now done through Q1, they're basically shorting all OEMs. So it's an allocation process from there which is why I've said earlier, other OEMs will be impacted here even if they actually haven't communicated that as yet. Now how they're impacted, whether they take out vehicle lines, plants, shifts, lower margin units that would be down to them. But there is a universal impact here on an allocation from first tiers to all OEMs. And, of course, the first tier supplier has an obligation to uniformly allocate that supply across all of their customer bases. That's a legal obligation they have. So others will be impacted. Now, they may manage it slightly differently, they may have more excess stock in the system, who knows? But we've all seen pictures of finished vehicles parked up in car parks across North America, for example. So a lot are doing exactly the same thing, building cars, waiting for chips, and ultimately there'll be a huge, huge inventory build. We've chosen mostly not to do that. Why have we chosen not to that? Because we have huge margins in our vehicles as you know. And we've also recognized that one of those vehicles are will be on a change cycle in the next nine months. So we don't want high buildup of stocks of vehicles that will be running out. So our approach is correct for us, but it might be bespoke for us. Our approach will maximize our position over time. But our approach does hurt us in Q2.

Sneha Gavankar: The next is from Kapil Singh from Nomura. Why is the impact so much higher for JLR compared to other large OEMs? Are you confident at this time that Q3 of FY'22 will not have a large impact? And if your competitors have much better supplies, is there a risk that they will gain retail market share as they would have inventory for the next six months and your customers may cancel orders, now that they are aware of this issue and go to competition?

Adrian Mardell: Okay, let me take that one from source, I think it goes from source to supply through to end demand. From a source supply perspective, a lot of our - and not just our competitors by the way - but a lot of the automotive industry will be sourcing from the same supply base. As I say that supply base have an obligation to allocate appropriately from demand levels. So if I ask for 40,000 units a month, which is a good ask for me, and they take me down by 25%, then I'd lose 10,000 units, I'd expect BMWs ask of 150,000 units to be taken down by a proportional number, for example. So the allocation of units from the first tier suppliers, they have an obligation. From the first tier supplier perspective, of course, they're very nervous, because all of the OEMs will be asking for more supply. So not only do they have an obligation to fairly allocate, if they do not fairly allocate, there could be consequences on them afterwards. So don't think that apart from a first tier supplier, we are going to be doing much worse or much better than anybody else. In the early days of this actually, we did do better because our volumes are relatively less. But as this really did bite, and as the shortages came through that vanilla allocation, if you understand that term, would be appropriate for us in all OEMs. Now, the key point, again, is back to the last answer, different OEMs have different positions they can take. Look Volkswagen, right, they can build all their Porsches and not build any Volkswagen units. So when you then talk to about a competitor of ours, a competitor of ours will be Porsche and not Volkswagen. So you might actually see a fall out in Volkswagen big enough and not a fall out in Porsche. In which case, you might come back and say, but Porsche weren't affected? Well, that's because Volkswagen took the hit elsewhere. So they have those choices, because they cross a segment of different brands. And what they choose to do, and guess what I would do, right, I'd hit Volkswagen not Porsche. So you may see, it may look like Porsche isn't impacted. But that's only because the allocation has been impacted more severely elsewhere. From a demand perspective, we have 110,000 orders, that was grown by 1,000 to 2,000 a week. We slowed down the growth of that actually, because we may need to reposition the value transaction here if this continues for too long. We've had very, very few cancellations at this point, I mean, 10s of units, right, there is a risk, if this continues for three to six months. And if I take my last example, Porsche isn't impacted, there is a risk that could increase. But please don't think the big risk here is cancellation of orders. The big risk here is resupply of conductors. And we are in a super healthy place on orders and they continue to increase. It's the parts, the supply, the production, which is the riskier. And ultimately, if we end up with production being more than demand, I can see that potentially a long way down the road. That isn't going to be the challenge we have over the next weeks and months. And again, the second half of the year, what confidence do I have? Well, I have confidence that Japan issues are going to go away. I have confidence that the snow storms in Texas are going to go away and I have confidence in 12 to 18 months' time that recapacity will happen. And then over that period of time, we will get better for the two issues I know are going to get better, but I don't think we're going to be able to support normal demand for a 12 month period. Exactly where we land between those two points, I would be misleading you by guessing. So I'm not going to guess at this point. When we do get back towards those normal demand levels, we will have a huge rebound and a huge boost for the issues we're seeing today for the reasons I've said.

Sneha Gavankar: The last question is from Binay Singh, Morgan Stanley. Is there any change to FY'22 revenue, EBIT and FCF guidance?

Adrian Mardell: I'm not going to give you new guidance today, but let's just stand back and think about the first half of the year which we've told you, right? I've told you that the wholesale number we anticipated was 235,000 units. I've told you that the likely wholesale number we get will be closer to 145,000 or 150,000 units. If we get a very, very sharp quick return to normality in Q3 which I am not expecting, then the guidance we've given on revenue will be lower. But EBIT margin in cash will be close, right? Maybe 500 million worse on cash. But the 4% would land. But I don't expect that to happen, because I don't expect it to rebound immediately from September to October. So, I'm not going to give you new guidance for the second half year yet. Because if I did, you'll be probably thinking I had the detail in front of me and I don't. What I will say is once we get back the volume levels, even towards normality, there will be a sharp rebound in cash first, and the growing increase in EBIT. Don't forget our EBIT in the second half of last year was 6.7% in Q3 and 7.5% in Q4. You were surprised in May when I gave 4% guidance, but obviously underpinning that was semiconductor issues. So our underlying EBIT is 6%, not 4% today, but I knew we had constraints coming at us. So obviously we all wish this to continue and get back to normality as soon as we can. It probably will mean this year, we won't fully get to that guidance, but that's not new guidance, that's just a likelihood. But we will with free supply now be much better than the 4%. So it's only time.

Sneha Gavankar: That was the last question. Thank you everyone for joining us today. We look forward to speaking with you in our results call shortly. Till then stay safe.

Adrian Mardell: Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of Tata Motors Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.