

Operator

Ladies and gentlemen, good day and welcome to the Blue Star Q2 FY14 Earnings Conference Call. We have with us today from Blue Star, Mr. Vir Advani, President, Electro Mechanical Projects Group and Executive Director; and Mr. B. Thiagarajan, President, Airconditioning & Refrigeration Products Group and Executive Director. As a reminder, for the duration of this conference, 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. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Vir Advani. Thank you, and over to you, sir.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thank you. Good afternoon ladies and gentlemen. This is Vir Advani, I have with me Mr. B. Thiagarajan, and we will be giving you an overview of the results for Blue Star Limited for the quarter and half year ended September 30th, 2013. The following are the financial highlights of the company for the quarter Q2 FY14.

The company reported total operating income of INR584.98 crores for the quarter ended September 30th, 2013, as compared to INR578.60 crores in Q2 FY13. The operating profit, which is PBIDT, excluding other non-operating income for the quarter increased 12% to INR 22.60 crores from INR20.15 crores in the same period last year. The financial expenses for the quarter increased by 14% to INR12.80 crores from INR11.20 crores in Q2 FY13. Consequently, net profit grew marginally by 3% from INR7.27 crores to INR7.52 crores during the quarter. The earnings per share for the quarter on a face value of INR2 stood at INR0.84 vis-a-vis INR0.81 in the corresponding The carry forward order book as on September 30th, 2013 increased marginally by 4% to INR1,744 crores compared to INR1,676 crores as at September 30th, 2012. The financial performance for the half year ended September 30th, 2013, that's for H1 FY14.

For the half year ended September 30th, 2013, the company reported total operating income of INR1,355.80 crores as compared to INR1,310.02 crores for the same period in the previous year, a marginal growth of 3%. The operating profit, that's PBIDT excluding other non-operating income increased by 14% from INR53.68 crores to INR61.02 crores. Net profit grew 9% from INR27.81 crores to INR30.29 crores in H1 FY14.

I will now go through the general outlook of each segments that we are operating in, for Q2 FY14 followed by specifics of our performance in each of these segments. General outlook for the segments, Segment 1, the external investment environment continues to be weak, added to it is the pre-election impasse, high inflation, high interest rate and volatile forex. The market has been sluggish in terms of new inquiry generation and order finalization. However, there have been some improvement in demand from the hotel, hospital, industrial and retail segments. At an aggregate level, the central plan market continues to be flat, the ducted AC market has de-grown by 5%. The only segment that has shown some growth this quarter is VRF, which has grown by 12%.

In Segment 2, the second quarter is usually a lean quarter for the room air conditioner industry and Q2 FY14 was no different. It in fact witnessed a de-growth of 5% over the same period last year. This de-growth after strong Q1 FY14 was due to an early monsoon in certain regions as well as sudden spurt in dollar vis-a-vis rupee, which forced companies, including ours to increase prices. Going forward, however, with the festival season coming up and also the energy table changes getting effective from January 1, 2014, the outlook for Q3 looks a little bit positive for volume growth. The demand in the commercial refrigeration business is stable, while the freezer market has grown around 15%, the water cooler market was flat in Q2 FY14.

The major segments contributing to business were ice-cream, dairy and frozen food. The trends looked to be similar in H2 FY14 as well. In cold storage products, the traditional segments of pharma, fast food and restaurants, ice-cream, banana ripening continue to fetch good business opportunities. In addition, we have also seen good demand in the marine, fruit and vegetable, and food processing segments.

Outlook for Segment 3, the demand for high technology imported equipment has been impacted by the appreciation of the dollar. The automobile and defense sector is showing some positive enquiry generation. In industrial projects, we are seeing demand in revamp & retrofit rather than ground field or greenfield expansions.

We hope to see some positive movement in demand in the coming quarters.

Now I'll move on to our performance for Q2 FY14, again, this will be segment wise. Segment 1, the electromechanical projects and packaged airconditioning systems business accounting for 64% of the total revenues in the quarter declined marginally by 1%, while segment results registered a decline of 24% to INR20.0 crores.

This drop was mainly due to lower billing volume, higher input cost and changes in planned revenue against planned cost in Q2 FY14 as compared to Q2 FY13. The margin of 5.4% in Segment 1 for Q2 FY14 is marginally lower than the operating margin in Q1 of FY14. However, it still continues to be higher than what we expect for the full year of FY14 on account of unexpected delays in closing some older low margin projects in the quarter. The capital employed in the business stood at INR487 crores as on September 2013, rising from INR423 crores as at September 30th, 2012.

The increase over last year is primarily on account of an increase in inventory levels in our equipment business and a drop in collections in the projects business as liquidity is getting tighter. After several quarters of anemic order inflow Q2 FY14 was a strong quarter for order booking. While order finalization in general continues to be muted, we booked two large orders in the quarter that have been delayed for over six months. The first is a Delhi metro Phase III Electrical and Mechanical project, and the second is, a mixed-use development for Oberoi Reality at Worli in Mumbai.

Together these account for close to INR300 crores of order inflow in the quarter. While positive movement in order inflow bodes well, the burden of a few large legacy jobs are still weighing heavy on us. The closure and settlement of Needless to say here, our strategy of being selective in booking orders while adhering to more stringent margins and commercial term guidelines continues. For the central AC products business, despite the overall sluggishness, we have witnessed some demand from the industrial, hospital, hotel, retail and IT, ITS sectors in this quarter. Our packaged airconditioning business continues to be stable, we are growing by 5% in our ducted business, and significantly higher percentage in the VRF segment owing to a smaller base.

In addition, we have been able to make inroads into some new national account customers. The top performing segments for the quarter were industrial, educational institutions and banks. Some of the major orders won by Blue Star during the quarter in Segment 1 are, for electromechanical projects, it is Oberoi Mixed Use Project in Worli, Delhi Metro in Delhi, Danfoss in Chennai, RMZ Ecoworld in Bengaluru, Apollo Hospital in Vizag, Tex Valley, Erode, Centenary Mall in Jamshedpur, Adlabs in Kolhapur and Noida One in Noida.

In the packaged airconditioning systems business, Kudankulam atomic power plant in Chennai, Dalmia Cements, et cetera. Central airconditioning products, we have a few, Kalyani Tech Park in Bengaluru, Park Hotel, Metro Mall in Faridabad, Nightingale Hospital in Guwahati.

Moving on to Segment 2, in the Cooling Products segment, revenue was flat in the quarter, while segment results grew by 3% to INR8.15 crores during the same period last year. The segment contributed to 29% of the overall share of revenues in the quarter. You may be aware that Q2 is usually a lean period for the room air conditioner and refrigeration business, while we had lean inventory level, the advertising expenses were higher. Coupled with that, was the impact of the rupee depreciation resulting in higher input cost, and thereby, a lower contribution for both the businesses.

Our room air conditioner business posted a growth of 6% in number terms in Q2 FY14 and we retained our market share gains as per GSK ORG [ph] survey for the period April to August 2013. For our refrigeration product and systems business, the demand was typically -- has typically come from ice cream, dairy and frozen food segments. The margin for this business continue to be under pressure owing to the increasing competition, price challenges and the company's re-entry into national accounts business where margins are comparatively lower.

Going forward, the company will continue its efforts to increase market share in both the room AC and the commercial refrigeration business. We will also keep our focus on initiatives like channel expansion, increasing share in the light commercial segment. We are confident that operating margins at the year-end will hold at last year's level of around 8% to 8.5%. The capital employed in Segment 2 decreased from INR237 crores in September '12 to INR173 crores in September '13. This is primarily due to an increase in inventory level and a decrease in receivables.

Moving on to Segment 3, in the Professional Electronics and Industrial Systems business, revenues increased by 25%, while segment results registered a significant growth of 216% to INR8.32 crores. As you are aware, Segment 3 consists mainly of three components, namely, an agency business, a system integration business and an industrial projects business. The agency business continues to be under pressure due to the appreciation of the rupee, our clients need to reset their budgets at these dollar levels. And so the purchase cycle is likely delayed by up to six months.

The system integration business is showing some signs of recovery with order inflow improving in the light industrial segment. This is however limited to very few specific projects and so competition is expected to be fierce. On a positive note, after having struggle for the last six quarters, the industrial projects business has bottomed out and is recovering albeit slowly.

We expect H2 to be stronger for the business as legacy projects have been cleaned up and order inflow has resumed as we have redirected our efforts to revamp & retrofit projects targeting energy efficiency improvement in the metallurgical sector. As always,

we recommend that Segment 3 should not be analyzed on a quarterly basis. Our Q2 FY14 results are encouraging compared to the previous year and we are on a path of recovery in this business.

While the Electro Mechanical Projects business will continue to be under pressure in H2 FY14 due to the challenging and uncertain business environment, cooling products business is likely to face challenging times owing to the appreciation of the dollar. However, the company intends to continue its focus on channel expansion and other initiatives related to cost control and prudent financial management in order to sustain this performance for the rest of the year.

With that, ladies and gentlemen, I'm done with my opening remarks. I would now like to pass it back to the moderator, who will open up the floor to questions between me and Thiag. We will try and answer as many questions as we can, to the extent we are unable to, we will come back to you via e-mail. With that, we are open for questions. Thank you.

Questions And Answers

Operator

Thank you, sir. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Anantha Narayanan from Kotak. Please go ahead.

Anantha Narayanan, Analyst

Good afternoon, sir. Just a couple of questions, in this order book of 17 crore, 44 crores, could you give us a break up of segments?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Break up of segments. I don't have that right now, but usually, what it is, is that segment 1 is about any 75%, 77% of the carry forward and the rest is in shared between 2 and 3.

Anantha Narayanan, Analyst

No, I meant between sectors.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Oh, between sectors, I am sorry. Again, we released that once a year. I think we did that at the beginning of this year, but broadly again, about 70% of this carry forward is in the commercial market, which is a primarily office buildings followed by hospitals and IT, about 15% to 18% would be in infrastructure and the rest would be -- and some in residential.

Anantha Narayanan, Analyst Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

I think at the end of the year, we had motioned that we had about 350 crores of --

Anantha Narayanan, Analyst

Legacy orders?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

All the low margin, no margin business, unfortunately, that number continues to be roughly there, it's come down marginally. The intention was to bring it down to zero by, during this year.

Anantha Narayanan, Analyst

Correct, correct.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

So that's what I mentioned in our -- in my opening remarks that we are finding it difficult to close many of these projects on time. And so we are still hopeful of closing them in H2, some of them may spill in to the next year, but the aim is to clean it all up in this current year and have a clean order book going forward.

Like I'd mentioned before, it's -- these projects are now depended on the client taking over, handing over and settling claims et cetera, so that's why it's taking longer than expected.

Anantha Narayanan, Analyst

Right. And the balance will be sir about 5% to 7% EBITDA margins?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah. So, the rest of that business like site margins at between 10% and 12% and operating margin at that 5% level.

Anantha Narayanan, Analyst

And last question is sir on the borrowings, they seem to have gone up to around 420 crores?
Yes.

Anantha Narayanan, Analyst

Any reasons? And where do we see it at the year-end?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah. So, we have in Q1, 355, that's up to 417. This has gone up, again, it's funding the capital employed in segment 1 primarily. Two issues there, one is our inventory levels in our equipment business has gone up and the other is that we have receivables on our projects business side under -- it become very tight liquidity wise, so in fact, you will notice that is linked actually to our revenue. Our revenue is actually slowing in Segment 1.

We are holding back billing and material delivery because of the rising capital employees. So, we continue to follow that process. So, one of the -- so, obviously, the focus is to bring down this capital employed, which is essentially project wise you have to go out and close projects, and only then, we'll be funding other projects.

So, it's become, I think, the last three months have been very bad because the dollar moving the way, they had many corporate customers completely shut down payments until they sorted out their own issues in Forex. We're starting to see some easing off of that in the last few weeks after dollar stabilize at the 62 level of wherever it is right now. So, we should see improvement in Q3.

Anantha Narayanan, Analyst

So, we will meet the target of around 300 crores at the year-end borrowings?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

We should be about 350.

Anantha Narayanan, Analyst

350. Thank you. That's all from my side, sir. All the best.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thank you.

Operator Pritesh Chheda, Analyst

Yeah, hi, hello, Mr. Thiagarajan. One question, I couldn't actually understand what you said on the margins in segment 1 that -- they are going to be -- not be higher than the company level margin? If you could just read that statement?

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah. And what I said was, we've been indicating that operating margins in segment 1. I expect it to be in that 4% range for the year because we are still cleaning up our backlog, but in the first half, Q1 margins are 5.9%, Q2 margins are 5.4%, so just employing that H2 margins for segment 1 will be lower than H1.

Pritesh Chheda, Analyst

Okay. Now this is despite the fact that you have 300 crore backlog on legacy and you have a good order win since the last four quarters now, which will remain, which will be in execution, which will be in execution in H2 and the site level margin there are 11%, so if you could just reconcile that?

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah, what is happening is that our order book is now refilling, unfortunately, the execution of the newer orders is much slower than we would want, that's one issue. The bigger issue, however, is that this 300 crores of old low margin, no margin business, we have not managed to bill much of that in each one, most of it will -- we are hoping will be billed in H2 because the intention is to clean it out, so the more of that we bill, obviously, the lower the aggregate margin gets right for the segment.

So the intent is to bill as much of that as we can, which will pull down the aggregate margin in each group [ph] but we'll clean out the order books so that we have a much better FY15.

So, this was originally -- this 350 was originally intended to be spread through the year as we closed out, but we have been struggling to close in the first half, so a lot of it is going to be backlog into the second half.

Pritesh Chheda, Analyst

How old are these orders? So, they are in excess of couple of years now in the system?

B Thiagarajan, Executive Director and President, AC&R Products Business

Yes. Yes, way more than two years.

Pritesh Chheda, Analyst

Right. So, there is always an upside risk that if these don't come into closure in second half, then the margin is not 4%?

B Thiagarajan, Executive Director and President, AC&R Products Business Pritesh Chheda, Analyst

Upside risk.

B Thiagarajan, Executive Director and President, AC&R Products Business

What do you mean by an upside risk?

Pritesh Chheda, Analyst

So if they don't come in the second half for closure the way you planned it to come in 1H and it didn't come. So, there is a chance that the margin is not 4% in second half, but higher?

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah, so that's not risk, right. But actually that doesn't help us because that problem doesn't go away. So, we have to address it in H2, because others were carrying it forward into FY15, which you want to avoid.

Pritesh Chheda, Analyst

Okay. My second question is with respect to inflows, so back-to-back, some two, three quarters where we have a fairly decent inflow. The systemic activity and some data that we are tracking tend to show a fairly good amount of tenders in the system. Do you think that the H2 inflow should most likely be as strong as what it is in H1 or the momentum might continue for throughout the year in terms of the tenders which -- in terms of the orders that you have received?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

So, we are very clearly seeing H2 will be lower H1 in terms of order inflow. The reason is simply that, these orders that come in H1 are actually last year's orders that got pushed into this year. So -- and such large tenders are, we are not seeing many of them being finalized in the current FY. So, H2 is going to be smaller value regular business that comes in, and there, I am not seeing that deal flow and deal closure being on track, in fact, I am worried that moving into Q4 as we get closer to the election whether they will just completely postpone those decisions till the election decisions are taken.

So, for now, at least we are happy with the H1 order inflow, we are happy with the order book we have right now, leaving aside the old jobs. So we have to, we are now focused on executing it because part of the problem frankly is that some of the best projects that we had booked in the last one year are frankly not moving at even half the pace they should be. So, the concern right now is moved to execution, billing and completion of jobs.

Pritesh Chheda, Analyst

Should I assume that the base order inflow for your company is about 500 crores, that's what I see if I just scroll back few quarters?

I haven't done that mathematics. What do you mean by that question?

Pritesh Chheda, Analyst

Sir, you said that my inflows in H2 will be weaker than H1 and it should only around the base inflows, the regular jobs. So, I'm just putting a number here. Can it be quantified up to 500 vis-a-vis the 800 crore and the 900 crore figures which you saw in quarter-one and quarter-two?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah, yeah, yeah. I suppose you're right, I suppose you're right. Correct.

Pritesh Chheda, Analyst

Right. And, last question I just want to reconcile, what you told in segment 2 was the air conditioners market declined 5%.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Okay.

Pritesh Chheda, Analyst

And, the room air conditioners business for you grew up to 5%?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Correct.

Pritesh Chheda, Analyst

Okay. The segment revenue there is flat. And your commentary on the other businesses of commercial cold storage et cetera didn't point out that anomaly that those business have actually declined in the quarter. So, if could just reconcile this, I didn't understand?

**Vir S Advani, Executive Director and President, Electro Mechanical Projects Business B
Thiagarajan, Executive Director and President, AC&R Products Business**

Yeah. See, first let us deal with the room air conditioners. For the period April to September, the growth in, we normally don't break up any one of this. It will become a limited disclosure, but still I am taking the largest one and which is room air conditioners. It grew by around 11% in Room Air Conditioner Segment and Blue Star's growth is in region of around 22%.

Pritesh Chheda, Analyst

That's H1.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

That is right, April to September.

Pritesh Chheda, Analyst

Okay.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Okay. I am now moving to the refrigeration products business, which has also grown. Now, your question is with regard to why it is looking flat in the quarter two?

Pritesh Chheda, Analyst

In quarter-two, yeah.

B Thiagarajan, Executive Director and President, AC&R Products Business

So, the thing is that quarter-two is lesser growth than quarter-one, even in room air conditioner or refrigeration products, the first reason. Second reason is, you know last year, we reported there, in this particular segment, one another, actually there are two products, which are constituting that. one is to do with the part of the service business, which is related to that, the second is insulation accessories business, which we had told last year, we will be exiting that part of the business.

So strictly speaking, this quarter two revenue in not really comparable because the last year that insulation accessories business continued, which are actually copper pipes and other stuff, insulation material et cetera, which we exited because that business was losing money.

Pritesh Chheda, Analyst B Thiagarajan, Executive Director and President, AC&R Products

Business

Cold storage did not, cold storage is really not, it has not grown, it is somewhere around some 5% or something like that. But the --

Pritesh Chheda, Analyst

Commercial refrigeration.

B Thiagarajan, Executive Director and President, AC&R Products Business

The deep freezer, deep freezer has grown and the --

Pritesh Chheda, Analyst

ACs.

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah, and one of the other products, in fact, degrew, which is bottled water dispensers.

Pritesh Chheda, Analyst

Okay, okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah, but the bottle water dispenser, I think, we have degrown of the market.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yes, so I'll answer your question. Thiagu is actually travelling. So he might find it difficult to talk. FY14 CapEx were 25 to 30 crores and FY'15 should be marginally higher than that.

Pritesh Chheda, Analyst

Okay. I think this was useful. Sir, if you could just tell us, lastly, what is the CapEx that you're looking for fiscal '14 and '15?

B Thiagarajan, Executive Director and President, AC&R Products Business Pritesh Chheda, Analyst

Capital expenditure.

Operator

Sorry to interrupt. Mr. Thiagarajan. There is disturbance from your line, sir.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thiag, I think we will move out. Yes. I'll answer that question. Thiag is actually travelling, so he might find it difficult to talk. FY14 CapEx is about 25 crores to 30 crores and FY15 should be marginally higher than that.

Pritesh Chheda, Analyst

Okay. Many thanks to you and Happy Diwali to you, sir.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thank you.

Operator

Thank you. The next question is from the line of Sonal Minhas from SAIF Partners. Please go ahead.

Sonal Minhas, Analyst

Hi, Mr. Thiagarajan. Hi, Vir. I just had two questions, the first one was on the Delhi project, the Delhi metro project that you have taken, wanted to understand that there is another Delhi project that you actually decided not to get for three to six months back, being the fact that you wanted to allocate capital for your cooling product business because you thought the returns there are much higher. The electrical and the pumping being the non-core of the business, would you believe that this -- the margins here would be much better than what you saw in the other business, which you left out three to six months back?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah, sure. So, what we had said was the project was 2.5 times the size and that decision made sense at that time subsequently, so we chose -- this is Delhi Metro Phase III, there are four sections of the metro that are getting built, so we withdrew from the HBSC offer that we had made because as per the larger section, like I said, 2.5 times this project

Sonal Minhas, Analyst

Get that. Next thing I wanted to understand was on the debtors. So what is the collection cycle that you have for the old orders of 350 crores that -- obviously, these are two-year old, so it's 720 days if you may summarize that? But what is the data cycle that you have for the new projects that you are executing? Could you just explain that?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

It's a tough question, I'll -- how will I answer that? Our running projects, typically the debtors cycle will be about 90 to 100 days and creditor's cycle will be about 50 to 60 days, that's roughly what we are running the current projects at.

That's pure debtor, from a cash flow point of view, the cash flow would be far better here because our terms on the new projects are better than the old one. And so, from a cash flow point of view, our objective is actually to be cash neutral in our projects that we executive now. It does tend to be a bit of a challenge given the liquidity in the market, so we kind of have a limit where we say that we would not want the cash flow to exceed a certain percentage of the overall value of the project, that's how we are controlling the cash flow and projects right now.

But it tends to be a challenge where you can see from the billing, from the revenue that we are choking revenue in Segment 1 quite substantially. There is a fine line between choking it too much because obviously, there is also a need to execute coupled with the capital employed. So capital employed has risen to a level in Q2 that we are not comfortable. We need to pull it down, you will see substantial improvement in Q3.

Sonal Minhas, Analyst

Get that. So, at the company level, if the debtors are around -- debtors to the other current assets are around 122 odd days, which basically means that the orders with the bad margins are essentially weighing down the number on the debtors as a whole and that's why the number is looking that much higher.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Correct.

Sonal Minhas, Analyst

But the new ones, it's that.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Correct, correct.

Last question, just a hypothetical question, just a hypothetical question, so if the 350 crores of orders were to be written off, let's say today from the balance sheet, I would presume that they would not have any P&L impact because that has already been effected in the P&L, just that you would bring down your balance sheet by amount of 350 crores, hypothetically, if that is what it was to be?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

No, that's not true because, obviously, we have, as you saw, yes, one is, we have the balance sheet side of it obviously stuck. The second is, there are obligations in terms of bank guarantees, liquidated damages, settlement with customers because these are old projects and we have dues and not debtors necessarily, but escalation claims et cetera pending with them.

So, there will be a P&L impact where we are to, like you're saying, short close these. So, in fact, that is the reason why they continue, we are struggling to close them because if there was no financial implication to them, either we would close them or the customer would close them.

So, actually getting through this last 300 crores is quiet critical for us. Obviously, as you would imagine, these are also tending to be the harder and more difficult jobs to close, right, because two years into it, the easier ones we have dealt with.

So, we're well placed to minimize the damage out of this. But, there is always a possibility that settlements don't go in our favor et cetera. So, actually walking away from these projects is not an option.

Sonal Minhas, Analyst

I understand that. Vir, just a last question, you mentioned that the working capital is a little stretched, but if I was to look at the company's balance sheet as such, the inventories compared to 31st March, the inventory is down, so is receivables and so is there other current assets. There is a head of short-term loans and advances, which is the only one which has gone up and so just wanted to understand what is this head actually?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

What is what, I'm sorry. What is the question?

Sonal Minhas, Analyst

The question is that, there is this head short-term loans and advances, which is the only item which has gone up, if we compare your numbers for September, the balance sheet from September to March. So, the other heads, which are inventory trade receivables and other current assets are pretty much down from the numbers in March?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah.

Sonal Minhas, Analyst

Just wanted to understand that, what is this head?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

What is this head? Okay, I see. This will be payables to suppliers, advances essentially and our revenue in excess or billing. So, its

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Sonal Minhas, Analyst

This is -- this won't be revenue in excess of billing, that would be in other current assets?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Other current assets. It's there in other current assets? Hey, we are asking our CFO to check. Yeah, give me five minutes, I will make sure I answer this question on the call.

Sonal Minhas, Analyst

Sure. Okay, all right. And I am done with my question. Thanks a ton.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thank you.

Sonal Minhas, Analyst

Thank you. The next question is from the line of Sourabh Arya from Bajaj Allianz Life Insurance Company Limited. Please go ahead.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah.

Sourabh Arya, Analyst

Yeah, hi, sir. Sir, my question pertains to unitary cooling segment. Sir, what I want to ask you in last couple of months, we have seen that in news a lot of MNCs are planning their manufacturing plant in India. So I want to get the sense do we have any idea that what kind of plants are those? Are those assembly plants or they are manufacturing complete ACs India? And in line with now, the rupee depreciating and you know, we have seen pricing, price of ACs increase and subsequently in January also, there are energy norms which are expected to change, which will increase the pricing further. So, how does it keep us and other players who are importing from China or other location in this particular segment?

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah, your question has got actually some seven, eight questions within. Number one is that manufacturing in India versus importing, yes, the answer is evident, and when the exchange rates are like this, it makes sense to manufacture here more or add value more here. Okay.

Sourabh Arya, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

That is point number one. Point number two, we have been much larger manufacturer in India than many other companies, because Blue Star always believed in manufacturing.

Sourabh Arya, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

No, but having said this, the room air conditioners per se, you know, there are lot of items, which are imported, like for example, the compressor is not manufactured till now in India. The plastics by and large are imported, the indoor units, which you are seeing and copper is imported. In some cases, the refrigerating gas, in some cases, invertors, many imports are there. The average import content in the room air conditioner, even if you want to make it here will be roughly around 60%. Okay?

Sourabh Arya, Analyst

Import content would be 60?

B Thiagarajan, Executive Director and President, AC&R Products Business

60%. Now, more and more companies, what you are seeing in the news items is, first of all, in the press conference, the people get excited about two things. One is, they plant a question as when you will invest and if they say, we are thinking, they will write us they are already investing. Then they will say, if you are going to invest, how much it will be and then they will write 200 crores or so. The second thing is about headcount reduction or sacking out the people, these two are again and again return.

Now, almost all manufacturers who are here at MNCs are in the process of or already have set up their manufacturing unit, and as I mentioned in air conditioning manufacturing, it is more of an assembly rather than an integrated

Sourabh Arya, Analyst

In those articles, there were comments like those guys would be manufacturing even compressors here?

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah. I'm coming to that, I'm coming to that. There is a plant of Hitachi first time in India manufacturing rotary compressors and this compressor company is a different company from whom all we'll be buying. Okay?

Sourabh Arya, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

Now, LG doesn't manufacture compressors here, they get it from there, same is Samsung. So, the question is more and more are manufacturing, you will begin to see as the volumes go up and that is the direction in which it is moving.

Now coming to your other part of the question, energy, labor, norms are changing, and therefore, will the prices go up? It is not -- it is -- optically, it will go up right, because what is five-star today will become a four-star in January 2014, so the rating of that has become four-star. What you are going to buy as a five-star in January is equivalent to six-star today. So therefore, indeed, you will pay higher price. You got the point?

Sourabh Arya, Analyst

Right.

B Thiagarajan, Executive Director and President, AC&R Products Business

So, it will optically, like you are paying a higher price, but in real life it is not. Where you are paying for this -- what is that?

Sourabh Arya, Analyst

The bare minimum rating is going out of the market?

B Thiagarajan, Executive Director and President, AC&R Products Business

What will go out is a one-star, okay? The three-star of today will become a two-star, so therefore, what will happen is, the ratios of the machines that are bought will dramatically change, that is why you keep seeing this five-star as a volume is remaining at a 25% for many, many years.

Sourabh Arya, Analyst B Thiagarajan, Executive Director and President, AC&R Products Business

Three-star continuous to sell maximum, more than 50% is three star.

Sourabh Arya, Analyst

Sure. If I were to sum up, right now, all the players are at nearly equal footage and as all are doing assembly only, and till now, there is no real threat and even if we --?

B Thiagarajan, Executive Director and President, AC&R Products Business

Some people do more value addition. Like LG, Samsung, with their volumes, they will do much more value addition than Blue Star. Domestic value addition.

Sourabh Arya, Analyst

Sure, sir. Thank you very much. That was helpful. Thanks a lot, sir.

Operator

Thank you. The next question is from the line of Renjith Sivaram from B&K Securities. Please go ahead.

Renjith Sivaram, Analyst

Hello? Sir, pertaining to these projects like in our 4Q con call, we had mentioned that around 50 crores of zero margin and around 300 crores of 5% hike margin jobs are pending. Are these the same jobs, which are currently also pending with us?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Could you repeat that? I'm sorry.

Renjith Sivaram, Analyst

As per our fourth quarter con call, we had mentioned that around 550 crores of zero margin and 300 crores of 5% hike margin jobs are pending and these are expected to be executed in 1H FY14?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

No, I'll just clarify. I pulled out my Q4 discussion, we had said 350 crores of zero and low margin business, I'm not sure where you got 550 from?

Renjith Sivaram, Analyst

Okay.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

But in any case, it was 350, that 350 has come down marginally, I mentioned, may be it's down to about 300 or something, it hasn't been -- hasn't seen much movement in H1. And, that was the point I was making earlier, I'd like to push a lot of this through in H2, which will probably impact the H2 margins for Segment 1.

Renjith Sivaram, Analyst

And, these are having roughly around 5% hike margin?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah, yeah. This is a combination of zero margin and that sub-5%.

Renjith Sivaram, Analyst

Okay. And sir, you generally -- in a half yearly basis, you generally give out in your current order book how much is lower margin, how much is mid margin and high margin. So, can you help us with that at least an approximate break up?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

No, I think we'll do it at the end of the year because this -- every quarter this number doesn't make much sense. Like I said it's very simple, we wanted, that 350 number is important, that 350 has barely come down to some 300. And that's what we need to push in H2, so if that 300 is zero and sub-5, the rest is that healthy 10%, 12%.

Renjith Sivaram, Analyst

Okay. So, mostly the new orders, which we have booked are in the range of that?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yes, correct.

So, probably if we see through this then our margins can come back to around 6% to 7%?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

In the next year is our plan. In the current year, it will be difficult because H2 will be worst than H1.

Renjith Sivaram, Analyst

Okay. And sir, in our interest cost, is there any forex because our borrowings haven't grown that much?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Okay.

Renjith Sivaram, Analyst

Is there any forex element in our interest cost?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah, foreign exchange cost for Q2 was 4.6 crores, which is up from 3.1 crores in Q2 of FY13.

Renjith Sivaram, Analyst

Okay. So this 4.6 crores is an addition to the interest cost?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah, as is our finance cost, if I'm not mistaken.

Renjith Sivaram, Analyst

Okay. And generally in the Segment 2, there has been a reduction in margin, how do you see the full-year margins in Segment 2?

B Thiagarajan, Executive Director and President, AC&R Products Business

You are talking about how it will pan out in the year-end?

Renjith Sivaram, Analyst

Yeah, yeah, yeah.

B Thiagarajan, Executive Director and President, AC&R Products Business

He mentioned somewhere around 8.5%, it should be.

Renjith Sivaram, Analyst

8.5% and --

B Thiagarajan, Executive Director and President, AC&R Products Business

Normally, Q2 is lower.

Renjith Sivaram, Analyst

Okay. And in Segment 3 for the full-year?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

What about it?

Renjith Sivaram, Analyst

Margins of Segment 3?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Margins for Segment 3, I -- frankly, we haven't projected that. So, they will be slightly better than last year.

Renjith Sivaram, Analyst

Okay. And, sir, just one small thing, when we look at our capital employed, as a whole, it hasn't grown much. So, and, it generally reconciles with our net worth?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yes.

Renjith Sivaram, Analyst

So, is there something missing because generally when we look at the capital employed, the debt also get added to it. In our segment wise, the capital employed, so that hasn't grown much?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

No, it has -- if you see, it's grown from 667 crores to 738 crores, right. Now you want for Q2?

Renjith Sivaram, Analyst

And, generally this matches with our net worth?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

You know -- why don't you send us an email, so we are not wasting everyone's time. We'll be happy to answer this specific question.

Renjith Sivaram, Analyst

Okay, okay. Sure, thanks.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah, thanks. I'll just answer one question before we go back to questions, so, someone had asked us about the increase in short-term loans and advances, 9 crores of it is on account of advances to suppliers going up and 11 crores of that increase is on account of MODVAT and VAT credit balances. So, that's an total addition of 20 crores. Hope that's clear. Thank you.

Operator

Thank you. The next question is from the line of Sharada Vikas from NTAsset. Please go ahead.

Vikas Sharda, Analyst

Hi, sir. Thank you. I have two questions. One is that in the Segment 1, what percentage of the products you sell with the manufactured versus brought out? And, secondly on those income from services which is around 8% to 10% of your revenues, which is much more is peaky, I guess, in nature. What kind of margins do you make on the services income?

Okay. So, in our Segment 1, we have two businesses, right. We have a projects businesses and we have an equipment business. In our equipment business, central air conditioning equipment products. That is 100% manufactured and sold by us.

So, there is no import or I mean, there is no purchase from outside, so that's all ours. As far as our projects business is concerned, it's much harder to answer because our projects business is now in NEP business, so the air conditioning, electrical power -- plumbing, fire fighting, BMS and we only manufacture air conditioning equipment, we do not manufacture any electrical plumbing, fire fighting or BMS equipment.

So, in the air conditioning projects that we execute in that business, maybe about 50% of the projects would have Blue Star equipment in it. And, the other 50% we'll be buying out competitors, equipment based on specification of the tenders.

Vikas Sharda, Analyst

Okay, thank you. And, the second question on the services?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Oh, I'm sorry, yeah, services, so we don't disclose service as a separate business. What we have indicated in the past is that, it is about 15% of our overall revenue of the company, its quiet substantial. It is obviously more profitable than our sales and manufacturing organization, but it's blended into these margins that you see across Segment 1 and Segment 2.

Vikas Sharda, Analyst

All right. Thank you.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thank you.

Operator

Thank you. The next question is from the line of Tanuj Mukhija from Ambit Capital. Please go ahead.

Tanuj Mukhija, Analyst

Hi, sir. Thank you for taking my question. My question pertains to Segment 1. Your margins have been quiet stable in the last two quarter above 5%. Will it be fair to say that the margins have been stable due to a change in revenue mix, wherein the share projects business has gone down?

Yeah. No, yes and no. Actually, one is, you are right, the project's business revenue is down for the reasons I mentioned, the capital employed has gone up, and therefore, we are choking billing and delivery in the projects business. So, that's one reason.

The other equally important reason I had mentioned is that because we are unable to close the old legacy projects at the rate we need to, to that extent where the revenue is being recognized in our projects business, in these or in the first two quarters is more, the newer business as compared to the older business. And, so as compared to the same period last year or whatever. So that is the process, the combination of the two, both have contributed, you're absolutely right.

Tanuj Mukhija, Analyst

Okay, okay. And the second thing, so look at your another kind of expenditure given that's increased steadily in the last two or three quarters along with improvement in the Segment 1 margins. Sir, can we break up the expenditure in to Segment 1, 2 or 3?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

No, if we could then we would have allocated it. So, no, I'm -- I would not, but they are materially different in -- we have not changed our method of allocation or anything year-on-year, so it's like to like, beyond that no, I don't think that it will be possible.

Tanuj Mukhija, Analyst

And, sir one last question, may be repeat of the earlier question, what was the volume growth and value growth of your room AC business in this quarter?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thiag, are you there?

B Thiagarajan, Executive Director and President, AC&R Products Business

Volume growth for the room air conditioners you are asking?

Tanuj Mukhija, Analyst

Volume and value growth, both, for room AC?

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah, I will just give it you. For the -- I have it for the period April to September readily.

Tanuj Mukhija, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

Which is the March.

Tanuj Mukhija, Analyst

11% volume and 21% value, if I am not mistaken?

B Thiagarajan, Executive Director and President, AC&R Products Business

22%, no, no, no, 11% is the market growth.

Tanuj Mukhija, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

Blue Star's growth is 22%.

Tanuj Mukhija, Analyst

In terms of volume?

B Thiagarajan, Executive Director and President, AC&R Products Business

In terms of volume. The value growth will be slightly higher at 27.5%. I repeat, I am talking about the period April to September.

Tanuj Mukhija, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

Yeah.

Tanuj Mukhija, Analyst

Okay. Thank you very much.

Operator

Thank you. The next question is from the line of (inaudible) from HDFC Mutual Fund. Please go ahead.

Unidentified Participant

Could you tell us what the expected tax rate for this year and next year might be?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

The expected tax rate. It will mat.

B Thiagarajan, Executive Director and President, AC&R Products Business

It will be mat.

Unidentified Participant

For this year and next year?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

For this year definitely, and --

B Thiagarajan, Executive Director and President, AC&R Products Business

Partly for next year.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Give me five minutes, we'll answer that more clearly, my CFO has just worked that out, but this year it is mat.

Unidentified Participant

Okay, great. Thank you.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business Operator

Thank you. The next question is from the line of Sandeep Tulsiyan from JM Financial. Please go ahead.

Sandeep Tulsiyan, Analyst

Yeah. Good evening, sir.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Good evening.

Sandeep Tulsiyan, Analyst

Sir, I just wanted to know the split between window ACs and split ACs, what would be the share and post the increase in prices after implementation of new norms, how do you expect this share to behave?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Thiag, are you there?

B Thiagarajan, Executive Director and President, AC&R Products Business

In the room air conditioner business right?

Sandeep Tulsiyan, Analyst

Right.

B Thiagarajan, Executive Director and President, AC&R Products Business

The -- can you repeat the question? You are asking about the share.

Sandeep Tulsiyan, Analyst

Basically, what percentage of our total room air conditioner business is window ACs as of now and post price increases in January, what we are given to understand is, the price differential between a window AC and split AC would narrow down. So there will be cannibalization of sales as in people would want to upgrade from a window AC to a split AC?

B Thiagarajan, Executive Director and President, AC&R Products Business

Okay, this is point number one. Point number two is that in the forthcoming energy label change, the window air conditioner and split air conditioner energy levels are not getting changed in the same level.

Okay, the window air conditioner escaped the energy label change last year, last time. In other words, 2010 to 2012, split alone changed, the window air conditioner remained the same.

Sandeep Tulsiyan, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

Now, the split is changing, window is also changing, which means the EER or the Energy Efficiency Ratio of window air conditioner is kept at a much lower level than the split air conditioner.

Therefore, I do not see a dramatic change in the consumption of pattern of window air conditioner at all. Already, we are beginning to feel window air conditioners are procured in certain markets, which is specifically New Delhi and Punjab, Uttar Pradesh. These are the markets in which window air conditioner are consumed as a new product. In many other markets, it's serving as a replacement only.

Sandeep Tulsiyan, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

So, to answer your question, we do not see a window air conditioner, yeah, abnormal drop. It will be as it is happening every year, it will keep declining. So, the last -- yeah?

Sandeep Tulsiyan, Analyst

Sorry. Based on the long-term trend, how people are upgrading, that would continue, no significant change you are seeing in the market?

B Thiagarajan, Executive Director and President, AC&R Products Business

Because of this energy label I'm not seeing. And, in other words, I am foreseeing till around 2016 or so window air conditioner will exist. The next change when it happens, in 2016, split air conditioner, as of now, there is no label proposed, because it has reached its maximum at present. Window has got one more change. So, that time, it will for sure decline definitely in a much sharper manner.

Sandeep Tulsiyan, Analyst

Okay. And, sir, what would be the split between the two in our sales mix? What would be the mix for Blue Star? In our case, it is 75, 25, 75% is split, 25% is window.

Sandeep Tulsiyan, Analyst

Okay, sir. Thank you very much. That's it from my side.

B Thiagarajan, Executive Director and President, AC&R Products Business

Thank you.

Operator

Thank you. Ladies and gentlemen, the management would be taking one last question. The next question is from the line of Sanjeev Zarbade from Kotak Securities. Please go ahead.

Sanjeev Zarbade, Analyst

Yeah, sir, wanted to know, what is the order intake figure for this, for the second quarter?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Order inflow in Q2 was 890 crores.

Sanjeev Zarbade, Analyst

Okay, 890 crore. And in this quarter, definitely couple of large orders has helped us to built order backlog, do you see a similar kind of orders also occurring in the second half, I mean, is the possibility reasonable?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

No, actually there are no large projects that we are working on for finalization in H2 unfortunately. There are midsize projects, of course, as usual. But as I had mentioned earlier, I am finding that, as the months pass, pass and H2 is becoming more and more harder to finalize contracts, I think people are getting concerned about the election.

Sanjeev Zarbade, Analyst

Okay.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Sanjeev Zarbade, Analyst

Okay. Sir, just last question. This advertising expenses that we incurred in Q2, could it decline in the Q3, I mean, sequentially, or --?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah --

B Thiagarajan, Executive Director and President, AC&R Products Business

Normally, yes, in the sense that the -- out of our total advertising expenses in a year, 75% happens in H1.

Sanjeev Zarbade, Analyst

Okay.

B Thiagarajan, Executive Director and President, AC&R Products Business

And so the H2, it will be very negligible. That is one of the reasons you see the operating margin going up for the stand-alone quarters.

Sanjeev Zarbade, Analyst

Okay, okay. Okay, sir. Thanks and all the best for the team.

B Thiagarajan, Executive Director and President, AC&R Products Business

Thank you.

Sanjeev Zarbade, Analyst

Thank you, sir.

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah. There was one -- before we close, there was a question on the tax rate, I clarify that in the current year it will be at mat, for the next year, unfortunately, we have not worked out the details, but it will be partially mat and partially regular. It's the best I can do right now, we will try and get a better feel of the tax rate for FY15 by the time we have our next call. Yeah. Thank you very much.

Operator

Thank you, sir. Mr. Advani, would you like to have any closing comments?

Vir S Advani, Executive Director and President, Electro Mechanical Projects Business

Yeah. No, just thank you very much everyone for being on the call. We appreciate it. We will be talking again in a quarter. If there are any questions that we have been unable to answer, please do send us an email and we will make sure we get back to you. Otherwise, Happy Diwali to everyone and talk to you after the New year. Thank you.

Operator

Thank you. On behalf of Blue Star, that concludes the conference. Thank you for joining us. You may now disconnect your lines. Thank you.