Blue Star Limited
Band Box House, 4th Floor,
254 D, Dr Annie Besant Road,
Worli, Mumbai 400 030, India.
T : +91 22 6654 4000
F : +91 22 6654 4001
www.bluestarindia.com

November 11, 2020

BSE Limited Phiroze Jeejeebhoy Towers, Dalal Street, Mumbai - 400 001 **BSE Scrip Code: 500067**	**National Stock Exchange of India Limited** Exchange Plaza, C-1, Block G, Bandra Kurla Complex, Bandra (East), Mumbai - 400 051 **NSE Symbol: BLUESTARCO**

Dear Sir/Ma'am,

Sub: Earnings Call Transcript – Q2&H1 of FY21

With reference to our letter dated October 19, 2020, and pursuant to Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, we are enclosing herewith the Earnings Call Transcript pertaining to Q2&H1 of FY21 Financial Results of the Company.

The aforesaid information is also being made available on the website of the Company at: www.bluestarindia.com

Thanking you,
Yours faithfully,
For **Blue Star Limited**

BLUE STAR LIMITED

Vijay Devadiga
Company Secretary

Encl: a/a

\\172.16.31.16\Legal and Secretarial Documents\(01) Blue Star Limited\2020-21\Stock Exchange Compliances\Regulation 30 - Information and Updates\Earnings Transcript\Q2FY21

Blue Star Limited

Q2 & H1 FY'21 Earnings Conference Call

October 29, 2020

MANAGEMENT: MR. NEERAJ BASUR – GROUP CHIEF FINANCIAL OFFICER

Moderator: Ladies and gentlemen, good day and welcome to Blue Star Limited Q2 & H1FY'21 Earnings Conference Call. We have with us today from the management Mr. Neeraj Basur -- Group Chief Financial Officer of Blue Star Limited. 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 phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Neeraj Basur. Thank you. And over to you, sir.

Neeraj Basur: Good morning ladies and gentlemen, this is Neeraj Basur. I will be providing you an overview of the results for Blue Star Limited for the quarter ended September 2020.

I. Financial Highlights for Q2FY21

After a challenging first quarter, Q2FY21 witnessed a revival in business activities with unlocks, easing of restrictions and consequent improvement in the consumer sentiment. We continued to focus on providing uninterrupted services to our customers. In addition, we launched a new range of products embedded with 'Virus Deactivation Technology' as part of our endeavor to fight the Pandemic through a contemporary range of product options for our customers. The business recovery trajectory continued to be encouraging in Q2 across most categories. However, on a year-to-date basis, the business scale continued to remain below pre-Covid levels and thus the financial results for H1FY21 are not comparable with H1FY20.

Financial highlights for the quarter ended September 30, 2020 on a consolidated basis, are summarized below:

-Revenue from operations for Q2FY21 was Rs 902.12 cr as compared to Rs 1249.47 cr in Q2FY20, a recovery of 72.2%.

-EBIDTA (excluding other income and finance income) for Q2FY21 was Rs 55.08 cr as compared to Rs 73.58 cr in Q2FY20. The robust recovery of 74.9% in our EBITDA in Q2FY21 is reflective of the business recovery along with prudent and swift cost containment measures undertaken by us.

-PBT before exceptional items was Rs 22.46 cr in Q2FY21 as compared to Rs 55.75 cr in Q2FY20, a recovery of 40.3%

-Tax expense for Q2FY21 was Rs 7.42 cr as compared to Rs 16.88 cr in Q2FY20.

-Net profit for Q2FY21 was Rs 15.32 cr as compared to Rs 37.94 cr in Q2FY20, a recovery of 40.4%.

-Carried-forward order book increased marginally to Rs 3019.57 cr as on September 30, 2020 as compared to Rs 2934.52 cr as on September 30, 2019.

-Capital Employed increased marginally by 6% to Rs 1124.27 cr as on September 30, 2020 from Rs 1063.49 cr as on September 30, 2019 as an outcome of robust working capital optimization measures implemented by us in the last six months.

-Net borrowings increased to Rs 344.06 cr as on September 30, 2020 (Debt Equity ratio of 0.44) as compared to a net borrowing of Rs 188.97 cr as on September 30, 2019 (debt-equity ratio of 0.22). Net borrowings have reduced by Rs 84.47 cr in Q2FY21 as compared to June 30, 2020 levels.

II. Business highlights for Q2 FY21

Segment I: Electro-Mechanical Projects & Commercial Air Conditioning Systems

Segment I revenue recovered 69.0% to Rs 540.83 cr in Q2FY21 as compared to Rs 783.54 cr in Q2FY20. Segment result was Rs 34.41 cr (6.4%) in Q2FY21 as against of Rs 44.56 cr (5.7%) in Q2FY20.

Order inflow during the quarter was Rs 684.91 cr as compared to Rs 794.35 cr in Q2FY20, a recovery of 86.2%.

1. Electro-Mechanical Projects business

Order inflow in Q2FY21 witnessed a gradual recovery. We won a prestigious Electrical & Mechanical works (E&M) order valued at Rs 149 cr for 'Mumbai Metro Line III, Package UGC-03' for five underground stations from Mumbai Central to Worli, from Dogus-Soma JV. However, the slow-down continues in Commercial buildings and Factories segments, which are expected to take longer to recover.

As of September end, more than two-third of the job sites are available for execution. However, we are prioritizing the mobilization based on cash flow.

We would continue to focus on Infrastructure segments such as metro railways and substation project tenders which are expected to get concluded in the upcoming quarters, offering immediate growth opportunities.

Carried-forward order book of the Electro-Mechanical Projects business increased marginally to Rs 2070 cr as on September 30, 2020 as compared to Rs 2063 cr as on September 30, 2019.

2. Commercial Air Conditioning Systems

While the order inflow and revenue from commercial spaces like malls, auditoriums, and movie halls were impacted, healthcare, pharma and government sectors helped the commercial air conditioning business to partially recover in Q2FY21.

Major orders bagged in Q2FY21 were from Greenfield Electronic Manufacturing Clusters (Hyderabad), Vijayanagar Institute of Medical Science (Bellary), Grand Hyatt Hotel (Bharuch), INTAS Pharmaceuticals (Ahmedabad) and National Mineral Development Corporation (Chandigarh).

In addition, the demand for retrofit and revamp solutions with Virus Deactivation Technology is robust. Major orders for products and solutions such as duct cleaning, UVC emitters, filters and fresh air augmentation have been received from ICICI Bank, Mercedes Benz India and Airport Authority of India.

3. International Business

The international markets in which we operate, witnessed gradual revival with encouraging order inflows during the quarter. The pace of the projects business in some of the key markets was promising.

Market for our joint venture in Qatar recovered, with a pick-up in government projects. Relaxations in pandemic restrictions & regulations are expected to aid pick-up in the forthcoming quarters.

We continue to focus on the expansion of Blue Star product range and building brand awareness and brand visibility in different markets that we are present in. Our campaigns across digital media platforms have been well received by our target customers.

Segment II: Unitary Products

Segment II revenue recovered 84.5% to Rs 318.65 cr in Q2FY21 as compared to Rs 377.21 cr in Q2FY20. Segment result was Rs 11.73 cr (3.7%) in Q2FY21 as compared to Rs 11.96 cr (3.2%) in Q2FY20.

1. Room Air Conditioner business

With the opening of retail outlets across the country and the growth of e-commerce channel, the demand recovery exceeded the expectations. However the demand is for affordable premium products. We have launched a wide range of Virus Deactivation Technology products. We have maintained our market share at 12.75%. The inventory pressure has been largely eased.

We expect the recovery momentum of Q2 FY21 to continue in the upcoming festive season and by December, the market is expected to reach 100% of last year's level.

2. Commercial Refrigeration business

Our commercial refrigeration business witnessed good recovery in Q2FY21 with excellent traction in the pharma and healthcare segments for our Modular Cold Rooms and Medical Refrigeration Products. We also gained momentum in the Supermarket Refrigeration business with order inflows from local and national retail chains. With the opening of restaurants and other unlock measures, the demand recovery is expected to accelerate in Q3.

We continue to maintain our market leadership position across the product categories.

We launched Touchless Storage Water Coolers and Bottled Water Dispensers during the quarter and these are expected to gain traction in the forthcoming quarters.

Major orders were bagged in Q2FY21 from UP Medical Supplies Corporation, Dr Reddy's Labs and Thyrocare.

3. Water Purifier business

The impact of the pandemic on our Water Purifier business has remained relatively moderate. E–commerce channel continued to contribute to a major share of revenue for water purifiers. We have reached market share of 3% in this category.

The Alkaline water purifier for immunity boosting campaign was well accepted by the targeted customers and the flow of enquiries to our network stores was encouraging.

We continue to stay focused on establishing our brand as a trusted one in the category, with well-engineered and the reliable products, backed by superior service.

Given the growing concerns on health and immunity, the demand for water purifiers is set to grow and the business is poised to break even this year.

Segment III: Professional Electronics and Industrial Systems

Segment III revenue was Rs 42.64 cr in Q2FY21 as compared to Rs 88.72 cr in Q2FY20. Segment result was Rs 8.15 cr (19.1%) in Q2FY21 as compared to Rs 24.43 cr (27.5%) in Q2FY20. The dip in revenue and profits in Q2FY21 is on account of a large, one time order in our data security business, executed by us in Q2FY20.

The Data Security Systems business continued to do well on the back of digitization initiatives in the BFSI sector. The demand for Healthcare products also increased during the quarter. With a revival in general economic activities, we also saw order inflows from the industrial segment with the Material Testing business regaining momentum during the quarter.

While the corporate capex spending is likely to be selective, we expect the Indian digital payment sector and healthcare sector to grow further in the current scenario and continue to offer opportunities.

With the wide portfolio of products and solutions forming part of our offerings, the prospects for this business segment are positive.

III. Business Outlook

Q2FY21 witnessed a much needed revival in business activities with easing of government restrictions. In the Electro-Mechanical projects business, we continue to prioritize our projects execution based on availability of work front and cash flows. We expect the markets for Room Air conditioners and Commercial Refrigeration businesses to get back to pre-Covid levels by Q4FY21. Digitization and Healthcare initiatives offer good prospects for the Professional Electronics and Industrial Systems segment.

While the revenue recovery will accelerate in the coming quarters, we will continue to focus on working capital and operating costs. We are optimistic about improving financial performance further in Q3 and Q4FY21.

With that ladies and gentlemen, I am done with the opening remarks. I would like to now pass it back to moderator, who will open up floor to questions. I will try and answer as many questions as I can. To the extent I am unable to, we will get back to you via e-mail.

With that, we are open for questions.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Lavina Quadros from Jefferies. Please go ahead.

Lavina Quadros: As far as your order book analysis exercise is concerned, are you all seeing any potential for cancellations of slow-moving orders in your existing book? Any comments over there? Secondly, as far as the residential AC is concerned, how has pricing moved like in the first quarter, you all had indicated pricing had weakened and what are the current inventory levels like?

Neeraj Basur: As far as our order book in the projects business is concerned, there are a few slow-moving projects in the building and commercial real estate sectors since our focus is to get the jobs restarted where we have visibility of cash flows. We have not really witnessed any major cancellations per se, but we can expect some slowdown because of this reason. On the infrastructure front, we have recently bagged an order of almost Rs 150 cr from Mumbai Metro. Our focus remains sharply on projects where our execution can be balanced with the operating cash flows.

As far as the pricing of residential ACs is concerned, there is not much change in Quarter 2. There was pricing pressure in Quarter 1 due to high inventory levels, then. Inventory levels started to improve in July and August and our understanding is that as of September and October, the inventory pressures have eased across most players. As far as Blue Star is concerned, we are fine in terms of our inventory level which is also reflected in our working capital numbers.

Lavina Quadros: Any color on the number of days like inventory days, channel inventory like is it 30-45 days or lower?

Neeraj Basur: As far as the channel is concerned, our understanding is it should be around 45 to 60 days. In the context of the scale of disruption, we feel that is an encouraging level and it continues to improve.

Moderator: Thank you. The next question is from the line of Naval Seth from Emkay Global.

Naval Seth: Two questions. First, why did working capital increase? If you look at in terms of payable days have kind of reduced or payables have reduced? That is my first question and in terms of your project business, as a percentage of the total order book, which you have not commenced over the last 6 months, what would be that percentage right now?

Neeraj Basur: Increase in working capital is largely related to the Quarter 1 impact of the business disruption a. As far as the payables are concerned, partly the reduction is reflective of the business de-growth that happened in Q1, and also in the last few months, we have substantially caught up with the payables obligations, specifically to our MSME suppliers. We have been consciously ensuring that the entire supply chain is kept sufficiently supported by us as far as our payment obligations are concerned. On your second question, the proportion of the buildings and the commercial real estate projects included in the carried forward order book is available in our update of Q4FY20. Those numbers did not substantially change as we have not added or substantially completed any of those jobs. We provide that breakup once a year.

Naval Seth: Can you give market share in categories like HVAC and within HVAC- chillers, VRF and commercial refrigeration if possible?

Neeraj Basur: We have about 19% to 20% market share in the VRF segment and are the joint number 2 player in that category now. Our market share in the Chiller space ranges from 35-40%. In the deep freezer market, we enjoy almost 30% market share.

Moderator: Thank you. The next question is from the line of Nitin Arora from Axis Mutual Fund.

Nitin Arora: Is it possible to break up in your UCP segment, how AC and Commercial Refrigeration declined as such? Given you are saying that inventory is getting normalized, your commentary looks quite encouraging with respect to Q3 and Q4 where despite 45 days or let us say 50 days of inventory, you are talking about market coming at 100%, looks like the channels will again start restocking. Is it specific to you because you are changing some channel or getting more aggressive in North markets where you believe that you can get more to the national chains or to the regional chains? Just want clarity on that? Also, if you can guide us for the whole year EBIT margins for the UCP and the EPC segment.

Neeraj Basur: The year-to-date decline in the Room AC and the Commercial Refrigeration product categories within segment-II are pretty much even because both these product categories are summer season dependent and in Q1, both the categories got impacted. The demand revival for the Commercial Refrigeration segment starts in Q4 and that is similar for both these categories. As far as your question on the optimism and the inventory levels getting liquidated, we are quite comfortable as far as our own inventory levels are concerned since we had taken action in early Q1 in the month of April on rationalizing additional procurement. While we ended Q1 with higher than normal inventories, it was not disproportionately high. We were able to mitigate that risk quite sufficiently in Q1 and as the business recovers, inventory levels will keep getting better.

Market inventory levels may be a little higher than what is expected to be at this time of the year, but the festival season and a number of other factors such as the demand boosting measures announced by the government may positively impact the consumer durables sales including that for Room ACs. The only caveat is that there should not be any further disruptions caused by the pandemic.

. For the full year, we expect Segment I margin to remain in the region of 4-4.5%, and the segment-II margin between 7-7.5%. This is after absorbing the adverse impact of Q1.

Moderator: Thank you. The next question is from the line of Sandeep Tulsiyan from JM Financial.

Sandeep Tulsiyan: I have two questions. Firstly on the Room Air Conditioner part, there were two factors which were primarily impacting our sales is what we understand. First is regional mix. As Blue Star is more dominant in South, that region relatively has underperformed the other regions in terms of growth which probably led us our market share sustaining at correct levels and we were not able to increase further and second was due to downtrading of products to this affordable category. So what are the steps that we have taken to counter these moves, have we made any notable shift in our regional mix or any other steps in terms of pricing or product catalog correction towards addressing this downtrading part, if you could highlight please?

Neeraj Basur: The market is gravitating towards mass premium range of products. Typically the sweet spot will be the middle of the belly of this market. While retaining a range of differentiators around quality and brand image, we are also making sure that we remain competitive in line with the market requirements and that may not exactly be downtrading..

As far as the regional mix goes, we are consciously enhancing our position in the Northern market. Therefore, the relative impact will be visible in the mix change between North, West and South markets. Share of the North and South markets within our sales is almost evenly split at around 30-35% followed by West and East. That has been a very conscious choice exercised over the last couple of years because North is a big market which we would like to focus on without giving up on leadership position in the Southern market. We would like to make sure that there is a good balance between growth and the margin profile.

Within that context, the new channel that has emerged in the context of the current environment is e-commerce and we have taken few steps to make sure that our overall market share from e-commerce gets calibrated with the market.. Epcommerce which has now grown up to around 16-17% as far as the market is concerned. We are currently at around 12-12.5% in terms of our e-commerce sales and that is where we are now focusing including the own e-store on our website. The product portfolio is being consciously made competitive while retaining the mass premium appea.

Sandeep Tulsiyan: What you highlighted on e-commerce channel, Blue Star is around 12-12.5% versus 16-17% of the industry share of e-commerce. So how that has grown over the last 2-3 quarters, if you could help us with that trajectory? What are the measures we have taken? Second question is on the recent DGFT restrictions on completely built units, what portion of our portfolio gets impacted with that? I know there should be a market share gain because some of the other fringe players may get impacted more than Blue Star. How are you exactly reading this entire restriction to have an impact on Blue Star, if you could elaborate on that?.

Neeraj Basur: We have to watch for a couple of more quarters to check whether the e-commerce share of revenues for the market will stay at the 16%-17%-18% level or will taper down as the recent spurt in e-commerce sales is closely linked to the way consumers are preferring to buy in the current phase. Whether those preferences will remain for the next one year or 6 months or 2 years, remains to be seen. Till the last year, the e-commerce share for the industry used to be below 10% .We are taking necessary steps required to calibrate our own share from e-commerce sales in line with the industry .

As far as the prohibition on import of completely built air conditioning units with refrigerants, we are less impacted because we had a choice of fulfillment predominantly comprising of our own manufacturing facility supported by or supplemented by some SKUs that we buy from the ODM manufacturers in India. As we are predominantly self-dependent on our own manufacturing; it will be not too much of a challenge for us to reorient the fulfillment requirements between the other two choices that we have. The theme of this change is mainly to bring a level playing field from for imports of CBUs from FTA benefited countries. Different players will adopt different fulfillment strategies. Right now, there is inventory in the system to take care of everyone’s requirements for few more months. So the real effect of this play will probably be visible either in Q4 or in Q1 next year.

We see this as an opportunity. This in a way reiterates the self-manufactured strategy that we have always adopted. We have also been sharing with you the fact that almost 100% of the indoor units that were imported earlier are now getting manufactured by us inhouse and that proportion has increased over the last 2 years . That was a part of our long-term strategy to derisk our import dependence. That is also in line with the current thinking around being ‘Atmanirbhar’ as far as manufacturing of some of these categories go. We will continue to enhance our manufacturing capabilities while being judicious about buying from the ODM supplies as well.

Moderator: Thank you. The next question is from the line of Anupam Gupta from IIFL.

Anupam Gupta: First question is on the margin guidance which you gave for the product business where you said 7-7.5% for the full year which basically implies 10-10.5% at least for the second half and if I go back many years, second half 10.5% has not been there primarily because of water purifier also. What is underpinning this sort of a guidance for the product business especially when you also have Virat Kohli this year, you will have additional expenses towards that or right now saying that the market has 45 days sort of inventory. So is this margin doable or what is underpinning this sort of guidance?

Neeraj Basur: There is a significant impact of cost reduction measures that we have undertaken which are quite visible even in our H1 results. All the cost reduction measures may not be structural in nature, but definitely by design most of them are intended to give us benefit in FY21. Margins of FY20 were also impacted due to disruption in the month of March. This is a high level guidance at this point in time. If the situation changes in 3 months' time, we will come back and let you know.

Anupam Gupta: Sure and just one thing in continuation, water purifier as you had guided earlier will be breakeven this year, right?

Neeraj Basur: That is correct.

Anupam Gupta: Second question is given all the import restrictions and your focus on domestic manufacturing, are you relooking at the CAPEX plan and doing it faster given the deadlines of the tax as well, what is the CAPEX outlook, what is the commissioning outlook for the new plant which we are planning?

Neeraj Basur: We are yet to redo our long-term strategy. . We are yet to go back to the drawing board on the long-term strategy. The focus currently is on FY21 and in that context, we have also tapered down the expansion CAPEX in FY21. CAPEX in FY21 will be mainly for maintenance reasons and it should be in the range of Rs 90 to 100 cr for the full year in line with the usual CAPEX level. We are not planning to accelerate any expansion projects in FY21. We will take those views over the next few months and we will keep you guided.

Moderator: Thank you. We will take the next question from the line of Amber Singhania from AMSEC.

Amber Singhania: Does that mean that the Sri City CAPEX is on hold as of now?

Neeraj Basur: In Sri City, we had bought land and we have not finalized the exact project plan in terms of commencement dates and end date, commercial production date etc. It is very much on the radar with the added advantage of being able to utilize the benefit of reduce corporate tax rate.. As mentioned earlier, we have to go back to the drawing board and draw up longer-duration plans and then decide on the plan for the Sri City plant also.

Amber Singhania: To harp upon more on this points of margin guidance from UCP side of 7-7.5% which is more or less equal to the last year's number despite having a major part of the season which is Q1 already off in larger terms. Is there anything which we are building significant time improvement in Q4 per se or is there any major improvement we are building because of the water purifier getting breaking even? Just wanted to understand your thought process on this 7-7.5% kind of number despite having difficult Q1?

Neeraj Basur: I will again reiterate that the margin % is just a high level guidance. It is not a projection and if the situation changes in terms of market levels, we will continue to review and revisit this outlook. Till last year, we had the impact of investments in water purifier, a sub category in this segment. It is going to be a breakeven year for water purifier and that is also going to help. The quarter 4 of last year specifically the month of March was impacted due to the pandemic, and therefore, we do not see any reason why Quarter 4 in FY21 should not be better than Quarter 4 of last year. The reduction in the overall operating cost structure that is visible in H1 are likely to continue even in H2. A sum total of all will enable our margin profile for the full year to match last year's levels.

Moderator: Thank you. The next question is from the line of Nirav Vasa from Anand Rathi.

Nirav Vasa: My question pertains to the credit or I can say the business terms that we are going to have with our channel partners. As I understand last season, they were impacted by COVID and a season before that, they were impacted by unseasonal rainfalls. So they have seen two seasons of back-to-back peak summer season getting impacted. So are we going to have any kind of liberal trade terms with our channel partners for the forthcoming season?

Neeraj Basur: Not really, In fact, it has been quite encouraging and it has been a very positive experience even in Q1. In Q1 we were worried on the credit profile of the channel partners and their ability to liquidate stocks and continue to buy more. The credit period in this trade is hardly a few days and that has not changed even in last 6 months. Our own belief is the worst phase in terms of the inventory management for them has pretty much got over, we do not see any reason why this will deteriorate going forward specifically as we are getting into a festival season and then of course Q4 once summer season sets in. So, we are not expecting any change in the credit.

Nirav Vasa: My second question would be pertaining to the marketing expenditure. So we have a brand ambassador and I believe that these brand endorsement contracts are for a limited period and between which we had an impact of COVID. So has there been any change in the contractual terms with these brand ambassadors and what can be the marketing spend? This year we might be down, but over next year, how can we look at it?

Neeraj Basur: We are very sharply focused on managing FY21. We have not yet decided what we want to do from FY22 onwards. In the next 2 or 3 months, we will have all those answers as we take stock of the expected market recovery or market growth in FY22, our own aspiration for market positioning, our product portfolio choices and then distribution and marketing will also follow all these decisions. We will be clearer about some of these decisions that we want to take in FY22 in few months from now. As of now, it is very sharp focus on handling cash flows, managing working capital, reviving growth and coming back on a very strong and robust profitability trajectory track record.

Moderator: Thank you. The next question is from the line of Vineet Prasad from Investec.

Vineet Prasad: What has led to such a sharp improvement in our EMP margins despite almost a 30% drop in revenues? Whether they were any ECL reversals or some lower provisioning etc.?

Neeraj Basur: It all depends on which jobs are getting closed in a given quarter. If the mix of jobs having slightly better margin profile get clubbed in one particular quarter, there would be an improvement in the profitability profile. This needs to be looked at over a period of time, not at a point in time. In addition to that, the rationale and logic of the cost management also applies to segment-I. In segment-I also, there is a conscious attempt to manage our operating cost structure which had impact in Q1 and also Q2. It is however largely the impact of the embedded profitability in the jobs that get closed, we have not reversed any ECL in Quarter 2.

Vineet Prasad: My second question is again on the guidance, but on EMP side, so for us to make 4-4.5% margin this year after impacted in Q1, which implies roughly more than 5.5-6% sort of margin for next 2 quarters as well. So are these margins which we have recorded in Q2 more of a sustainable margin going forward?

Neeraj Basur: .In FY20, we had a 4.3% margin after taking into account the impact of disruption in the month of Marc. We are almost at around 3% for H1 and are confident of improving it to around 4-4.5% for the full year.

Moderator: Thank you. The next question is from the line of Rahul Soni from SMIFS Limited.

Rahul Soni: You said Blue Star has 100% self-sufficiency in indoor unit manufacturing. What about the outdoor unit self-sufficiency currently? Are you dependent on the other ODM manufacturers for that and at what extent?

Neeraj Basur: There are few SKUs which we consciously buy from our ODM partners. We work with multiple partners and we distribute our requirements amongst them. It depends on the economics of the product family to decide whether to manufacture inhouse or get it manufactured on a contract basis. To the extent we are buying the units from an Indian ODM manufacturer, the ODU and IDU is bundled. The context of 100% IDU is those for our own manufactured CBUs. It was 100% imported around 3 years back. We have moved from fully imported IDUs to 100% self-manufactured IDU which is expected to have a positive impact.

Moderator: Thank you. The next question is from the line of Anupam Gupta from IIFL.

Anupam Gupta: The cost reduction which you are talking about, obviously this year you will see benefit, but any of those can sustain even beyond FY'21?

Neeraj Basur: We have implemented cost optimization measures across all our expense lines. Now as the business normalizes, as the situation looks better, we will review the levels of cost that we need to incur to support business growth. Our endeavor is to use this crisis as an opportunity to embed to the extent we can structural cost improvement changes, that is why got on to the cost optimization curve right from the first week of April. At that point in time, we were not even aware whether this pandemic disruption will last for 21 days or 40 days, but we started this exercise in the first week of April itself and that helped us in Q1, helped us again in Q2, will also help in Q3 and Q4. On how it will play out in next year or next years, we will have to draw up our entire thinking and realign, recalibrate the cost lines. The endeavor is to ensure that cost benefits become structural in nature.

Anupam Gupta: On the working capital, the increase to some extent obviously is driven by your reduction in current liabilities, wherein your supported MSMEs and there is a government directive also that you need to clear their dues faster. Will this be a structural feature or will it revert as you move ahead?

Neeraj Basur: It will revert to more normalized levels. We had to resort to increased borrowings in the short duration because most of these liabilities were also committed in nature, backed by LCs in Q1, so they had to be paid off. That combined with the fact that our procurement has not been at the normal scale led to a reduction in payables. As we start procuring again, this will get normalized.

Anupam Gupta: On the projects, what should be the growth guidance, sort of revenue run rate in the current quarter per se, for the next 2 quarters where you will see an uptake?

Neeraj Basur: Our choice of resuming work wherever we have visibility of cash flow is the driver more than the ability or the market reopening potential. We are keen to start work in most of the job sites, but are consciously moderating the progress based on visibility of operating cash flows and quick turnaround of working capital. Reduction in borrowings during the quarter of around close to Rs 85-90 cr, is an outcome of some of these measures. In Q3, we want to achieve further reduction in borrowings and we are confident we will be able to do that as long as we stay focused on some of these measures.

Moderator: Thank you. The next question is from the line of Mayank Bhandari from B&K Securities.

Mayank Bhandari: Now you are completely manufacturing the indoor units by yourself. In last 2 years, I think you changed it completely from nearly 0% to now it is 100% inhouse indoor manufacturing. How has it impacted your margin? Have you got any cuts or got any gains in terms of margin because of which inhouse shifting of indoor unit manufacturing?

Neeraj Basur: This is a good question. The cost which you can expect to get from a Chinese supplier will always be quite competitive as compared to the cost at which we will manufacture that in India. That has been one of the constraints in not being able to migrate to this inhouse manufacturing in the last few years which we have overcome now.

In fact, at this point in time, at the current scale we are quite cost competitive even if we manufacture ourselves. In addition, governmental interventions around Atmanirbhar policies and imposition of higher customs duty structure will only make inhouse manufacturing of IDUs more attractive, but those benefits will get realized sometime in the future and as the scale grows up, those economic benefits will be more visible. There are many other cost optimization measures on the product cost side as well; however, the margin pressures in the market mean that one has to balance in terms of maintaining a certain price level and a cost level and margin profile.

Moderator: Thank you. Ladies and gentlemen, as there are no further questions from the participants, I would now like to hand the conference over to Mr. Neeraj Basur for closing comments.

Neeraj Basur: Thank you very much, Ladies and Gentlemen. With this, we conclude this quarter's earning call. Do feel free to revert to us in case any of your questions were not fully answered and we will be happy to provide you additional details by email or in person.