

# Management Discussion and Analysis

## INDUSTRY STRUCTURE AND DEVELOPMENTS:

### Economic Environment:

The financial year 2017-2018 has been quite an interesting period. While the first quarter saw the impact of demonetization settle down, the next quarter experienced the effect of the Goods and Services Tax (“GST”) which brought in some complexities as businesses aligned itself to the new system. This year also witnessed substantial steps being undertaken towards problems associated with non-performing assets of the banks, further liberalization of Foreign Direct Investment (FDI), etc., thus strengthening the momentum of reforms. There has been improvement in the economic scenario as there have been various investments in many sectors and industries.

GDP growth has averaged 7.3 per cent for the period from 2014-2015 to 2017-2018, which is the highest among the major economies in the world. Moody's has upgraded India's sovereign rating after 14 years to Baa2 with a stable economic outlook.

The Government this year focuses its budget on uplifting the rural economy, strengthening of agriculture sector, healthcare for the economically less privileged, infrastructure creation and improvement in the quality of education of the country. Budgetary allocation for infrastructure is set at ₹ 5.97 lakh crore (US\$ 93.85 billion) for 2018-2019. An all-time high allocation has been made to the rail and road sectors.

With world growth likely to witness moderate improvement in 2018, expectation of greater stability in GST, recovery in investment levels, and ongoing structural reforms, among others, should be supporting higher growth. Country's economic performance should witness an improvement in 2018-2019 as global economic activity continues to strengthen. Global growth is forecast to grow by 3.9 per cent during 2018 as per International Monetary Funds (IMF). The IMF expects India to grow at 7.4 per cent in 2018 which could increase further to 7.8 per cent during 2019 as against 6.7 per cent during 2017. However this is still below the 13 years average.

Steel consumption is expected to grow 5.7 per cent year-on-year to 92.1 million tonnes in 2018. India's steel production is expected to increase from 97.42 million tonnes in FY 2017 to 128.6 million tonnes by 2021. The Government of India has allowed 100 per cent Foreign Direct Investment (FDI) in the steel sector under the automatic route. Nearly 300 MoUs have been signed with various states for planned capacity of about 486.7 million tonnes.

India has also regained its tag as the fastest growing major economy and was the third largest steel producer

in 2017. The strengthening of the investments has largely improved trade and India holds a fair advantage in cost of production and conversion costs in steel and aluminum.

Resolution to the steel sector's problems either through write-offs, reclaiming of bad debt from insolvent companies or potential for loan payoffs as the sector comes back to health, can be a crucial step forward in getting the economic engine back on track.

Additionally the Government of India is focusing on infrastructure and restarting road projects which is a welcome development for the steel sector as this will aid in boosting the demand for steel.

2018 is likely to exhibit a sustainable scenario with no major shock. India is expected to become the world's second largest steel producer soon and aims to achieve 300 million tonnes of annual steel production by 2025-2030.

2018 has begun on an optimistic note which was not the case a year ago when excess capacity in global steel market was identified as a major constraint plaguing the industry in the backdrop of a subdued business scenario.

### Steel Scenario and Outlook:

Steel is the backbone of the economic activity of any country. India's economic growth is contingent upon the growth of core sectors which include the Indian steel industry. Consumption of steel is taken to be an indicator for economic development. While steel continues to have a strong hold in traditional sectors such as construction, transportation; special steels are increasingly used in engineering industries such as power generation, petro chemicals and fertilizers.

Hot-rolled, cold-rolled and galvanized steel products together play a vital role in the country's industrial development and economic growth. Rise in infrastructure development, automotive production are major factors for increasing growth. Power and cement industries are also aiding growth of this sector. Demand for iron and steel is set to continue, given the strong growth expectations in infrastructure, namely, residential and commercial building industry, rail and road development.

India produced 53.5 million tonnes crude steel in 2007 and 101.4 million tonnes in 2017, an 89.5 per cent increase. If current trends continue, India is likely to become the 2<sup>nd</sup> largest steel producing country in the near future. The demand-supply mismatch is significantly reduced and capacity utilization has improved and prices have rebounded. The prices of finished steel in the last 10 months have on an

average gone up by 18 to 21 per cent and have made a positive impact on the profitability position of steel industry. Steel industry is on the threshold of a boom but it has come after a long hiatus.

The liberalization of industrial policy and other initiatives taken by the Government have given a definite impetus for entry, participation and growth of the private sector in the steel industry. While the existing units are being modernized / expanded, a large number of new steel plants have also come up in different parts of the country based on modern, cost effective, state-of-the-art technologies. In the last few years, the rapid and stable growth of the demand side has also prompted domestic entrepreneurs to set up fresh green-field projects in different states of the country.

Although there is a rationale for India to scale-up its steelmaking capacity, the major obstacles faced by the country that will make this journey challenging are bureaucratic roadblocks to project implementation, credibility of government mandates and incentives and supply chain management of key raw materials are some of the major challenges. The Indian Steel industry also suffers as it is not able to support itself in a down turn due to wafer-thin margins. Research and Development is another issue as the sector is very slow in modernizing itself.

While current developments in the sector inspire confidence in India's growth story and convert India's image in terms of 'ease of doing businesses', the government, must have on an on-going basis a time-bound process, more transparent project planning and strong vigilance.

The overall outlook for Indian steel producers appears positive; what may be worrying is the risk of margins coming under pressure if prices do not increase enough to absorb higher costs. There is also another apprehension as large steel producers intend to bid for steel companies that have defaulted on loans and overpaying for them is a balance-sheet risk that bears watching.

#### **Review of Operations:**

CMI FPE has always strived for continuous modernization and upgradation of its workshops and better efficiency levels.

Our Company continues to support and enhance the performance management process. In moving forward CMI FPE this year too won the most anticipated 'Public Award' for its innovative product 'Compact Color Coating Line' in the innovation category, judged by the CMI global jury.

No 'Lost Time Accident' was reported in the course of

the year at any of the entity's locations. The Near miss reporting system was made more robust by assigning targets for reporting departmentwise and strengthening the monitoring system for the same.

Safety Return of Experience was taken up in Safety trainings, Tool Box meetings, and Monthly Safety meetings. Safety trainings were carried out at all entity locations in accordance with the Training Calendar set. As stated earlier, a detailed HIRA Study was completed for 17 CNC Machines and an action plan for implementation of the recommendations would be taken up in the ensuing year for implementation.

Our Company has shown a positive EBIT of ₹ 1416.20 lakhs in the year under review. The earnings per share of ₹ 10 were ₹ 13.61 (as against ₹ 11.73 in the previous year).

#### **Opportunities and Threats:**

The biggest opportunity before the Indian steel sector is that there is enormous scope for increasing consumption of steel in almost all sectors in India. The key opportunities include an unexplored rural market to boost consumption of steel, growing domestic demand for steel products including automobiles, construction, rapid urbanization and increasing interest of foreign steel producers in India.

The short range outlook by World Steel Association has projected India's finished steel consumption at 92.1 million tonnes in 2018 which is a 5.7 per cent growth. Industry forecasts create an ideal condition for product innovation, technology and supply chain efficiencies.

Based on the increased capacity addition in anticipation of upcoming demand and the new steel policy that has been approved by the Union Cabinet in May 2017 India's steel production is expected to receive a boost.

The 'Ministry of Steel' along with 'Metal Scrap Trade Corporation' has jointly launched an e-platform called 'MSTC Metal Mandi' under the 'Digital India' initiative, which will facilitate sale of finished and semi-finished steel products. The 'Ministry of Steel' is facilitating setting up of an Industry driven 'Steel Research and Technology Mission of India (SRTMI)' in association with the public and private sector steel companies to spearhead 'Research & Development' activities in the iron & steel industry at an initial corpus of ₹ 200 crore (app. US\$ 30 million).

But there are several threats; the Indian steel industry has witnessed spurts of price wars and heavy trade discounts, which has impacted the growth progress. Furthermore the easy-going progression in infrastructure developments, market fluctuations and dubious global economic trends, China's export possibilities and

increased protectionism in the west is a hindrance to the growth of exports in India. Another huge roadblock is in setting up of plants in India due to land acquisitions and mining license issues.

It is imperative that the Indian steel companies become significantly more competitive by improving productivity further and moving towards rapid technological upgradation. The fortunes of CMI FPE are closely linked to the turnaround and growth story of Indian steel companies.

Our Company is conceived as the Indian hub integral to the vision of CMI group's strategy and sees significant business opportunities in its key markets. The Company is a project management company and the average gestation period for each project is 12 to 18 months and is exposed to inherent risks like adverse developments at customer end leading to delays which could impact the overall project schedule.

Our Company focuses on 'value engineering and innovation' and the '2018 Public award' for 'Compact Color Coating Line' by global 'CMI jury' emphasis on the trust that CMI group places on CMI FPE.

CMI FPE is pursuing significant business opportunities in its key market and the Management is closely monitoring these activities to leverage the Company into leadership position in the Cold Rolling Complex market.

#### **Risk Management:**

From an entity perspective, and given the uncertain business and economic environment in which our Company operates, it is extremely important that it has in place a robust mechanism for risk appraisal, mitigation and management.

In the year under review, the Board, the Audit Committee and the Risk Management Committee carried out extensive reviews of the risk management framework, the risk mapping exercise and the various steps being taken to mitigate the key risks, particularly operational risks. These reviews were carried out in November 2017.

CMI FPE continues to follow the Internal Control Approach developed by COSO (Committee of Sponsoring Organizations of the Treadway Commission) 'COSO Internal Control – Integrated Framework, 2013' and has also adopted the 'COSO Enterprise Risk Management – Aligning Risk with Strategy and Performance 2017 framework' along with ISO 31000:2009 as the framework for risk management at the Company. The preference is to rely more on and institute, wherever possible, automated controls or semi-automated controls through the Company's state-of-the-art ERP Application.

In order to optimize the effectiveness of the risk mapping exercise, the Board, Audit Committee and Risk Management Committee reviewed various aspects such as the clarity in the rating scale descriptions, the basis on which the risk taxonomy had been arrived at, the degree of dispersion in the risk and controls scores for various risk IDs across the respondents (as measured by the coefficient of variance for each Risk ID) and the feasibility and implementation status of the action plans pursuant to the risk mapping exercise.

It was also ensured, through a special orientation session, that the participants in the risk mapping exercise, (viz., heads of functions), gained adequate awareness on the clauses of ISO 31000:2009, the concepts of inherent risk, target residual risk and actual residual risk as enunciated in the COSO ERM 2017 framework.

The risk mapping participants were also sensitized to the latest concepts in risk management such as 'Black Swan events' and 'Risk Velocity'.

The Audit Committee and Risk Management Committee also reviewed the various measures taken to comply with the provisions of Section 134(5) of the Companies Act, 2013 relating to 'internal financial controls', notably the templates adopted for internal financial controls, the quality of the information contained in these templates, the various risks identified at a process level, the manner in which 'test of design' and 'test of operating effectiveness' had been carried out for the various process controls by the management team and were quite satisfied with the extensive work done in this area.

Also, from an entity governance perspective, our Company continues to follow the Commitment Committee procedure, whereby all customer bids beyond a pre – determined value are reviewed by the 'Commitment Committee'. This Committee examines in great detail the various sources of risks and the risk mitigation strategies to be adopted preparatory to finalization of contracts with prospective customers. Business risk, financial risk, liquidity risk and market risks are the key risks reviewed by the Commitment Committee prior to their approving the various contracts. The various risks identified as well as risk mitigation strategies are reviewed on a periodic basis by the Company and emergent actions are taken on the basis of these reviews. The learnings from the actual risks and the effectiveness of the mitigation strategies are analyzed for further learning, and for refining the approach for future contracts.

#### **Finance:**

Our Company adopted a strategy of 'Cash and Carry' in respect of certain customers, where the outstanding

was more than 180 days. The project supplies to these customers were released only on receipt of advances for the current supplies after partial adjustment of their outstanding. Our Company finalised the time schedule for project closure and payments to be received by getting post-dated cheques from customers. The strategy of 'Cash and Carry' helped the Company to reduce the working capital cycle; regular payments from the customers helped the Company negotiate better resulting in reduction of bank charges and interest rates.

Our Company is a debt free company (no long term debt) as on March 31, 2018 and has not accepted any deposits from the public during the year under review.

CARE has reaffirmed Long Term Rating of CARE BBB+ and Short Term Rating of CARE A2+.

### **Human Resource Management and Industrial Relations:**

Human Resources play an instrumental role in securing the future of our Company. One of the key aspects is enabling employees to develop the skills necessary to take up new roles within the Company through cross functional mobility by identifying opportunities and offering training and development.

The permanent employee strength of the Company was 490 as on March 31, 2018. The Company devotes substantial man-hours towards training and development of its employees.

The Financial year 2017-2018 ended with 'PULSE 2018 – A CMI people survey' which received 100 per cent response. This response not only demonstrates the 'employee connect' with its Management but also emphasizes on the fact that CMI creates opportunities for employees to anonymously express their views.

'PULSE' survey is conducted every 2 years and based on the response received in 2016, CMI FPE 'formulated plans and ways of working' spread out over a period of 2 years to ensure 'maximum employee satisfaction', some of which resulted into:

- Project Management Training
- Optimised processes through continuous improvement plans
- Good Housekeeping Award to Services team by TATA Tinplate for 3 consecutive years
- Flexible work timings for better 'work-life balance'
- Support towards 'Work integrated education'
- Awareness on 'Near Miss' Reporting and recognition given to pro-active employees
- Low attrition rate of employees as compared to competitors

- Encouraged Internal transfers for better employee development and recognised employees for special achievements.

The results of this survey which is conducted by 'Willis Towers Watson' will be declared in June 2018 and the resulting action plans will be aligned with the KPIs of the Company. The KPIs of our Company are set during an 'employee-offsite meeting' for 'inclusive ownership' in deciding Company targets.

Our Company also demonstrated their operational efficiency by winning the 'Total Productive Maintenance (TPM) Award' by TCIL for innovative approach. A team of 8 employees were successful in yielding results by implementing '47 Kaizens' and '50 One Point Lessons (OPL)'. 2017 was indeed a year of celebration as CMI FPE was chosen as the 'Best Company of the Year' by 'International Brand Consulting Corporation'. This year our Company focuses on initiating projects under 'Industry 4.0'.

Efforts will continue in creating an optimistic workplace for its employees through resilience and positive leadership. The Management continues to maintain cordial and transparent relations with all its stakeholders.

### **Health and Safety:**

CMI FPE adopts a proactive approach to occupational health and safety through a 'hierarchy of controls' which are deployed in a seamless manner i.e. elimination / substitution of unsafe conditions, deployment of engineering controls and administrative controls and using appropriate PPE for carrying out hazardous tasks.

Our Company has implemented various engineering controls, pursuant to hazard identification and risk assessment for its major work centres such as EOT crane proximity sensors, flash back arrestors, colour coding, testing of lifting tools and tackles, pneumatic hose reels, interlocks, machine guards, sensors for transfer trolley, etc.

The Company takes very seriously its obligations to provide a safe working environment to its employees and has carried out 'hazard impact and risk assessment study' for its CNC work centres. It has also adopted 'LOTO (Lock Out Tag Out) approach' towards maintenance of machining work centres for its maintenance team.

The principal administrative controls deployed include safety meetings, safety trainings and tool box talks. Our Taloja workshop completed 1712 days and Hedavali workshop completed 1391 days without any 'lost time accident' as of March 31, 2018.

Focused initiatives have been pursued to bring about greater awareness on 'near misses'. Individual departments have taken targets relating to reporting on 'near miss' incidents in standard templates. This will ensure that the organisation learns from the analysis of 'near miss' events on an ongoing basis.

Various safety-related programs were organized during the 47<sup>th</sup> National Safety Week from March 4 to 10, 2018 – the primary purpose of having a week – long event being of course to renew the commitment of employees to 'work safely throughout the year'. In addition to practical training programs such as Fire Fighting for Emergency Response team members, our Company also had departmental presentations on Safety Improvements, Safety Drawing Poster Competition and Safety Quizzes.

Machine Shop at Taloja Plant won the 'Housekeeping Contest' and also the award for 'best presentation' relating to Safety improvements actually implemented at departmental shop level. Prizes were also given out for 'Near-Miss Reporting,' for which departmental targets had been set earlier in the year.

As per the Factories Act, 1948, a yearly medical examination was also conducted for all employees exposed to shop floor activities. No significant issues were found.

A revised version of the entity's Safety manual, aligned with OHSAS 18001:2007, was issued in February 2018 and will now be revised in accordance with ISO 45001: 2018 in FY 2018 -19.

The International Labour Organization (ILO) celebrates the World Day for Safety and Health at Work on the 28<sup>th</sup> of April to promote the prevention of occupational accidents and diseases globally. It is an awareness-raising campaign intended to focus international attention on emerging trends in the field of occupational safety and health and on the magnitude of work-related injuries, diseases and fatalities worldwide.

As the traditional date, April 28<sup>th</sup>, falls on a Saturday this year (2018), the Group decided to fix Friday 27<sup>th</sup> April as its own day for this. As per Groups guidelines, we at CMI FPE organised different events on 27<sup>th</sup> April, at different locations, to promote the importance of this day. All employees actively participated in the celebration of "World Day for Safety and Health at Work".

#### **Optimization of Key Business Processes:**

Considering that the Company operates in an extremely competitive market, both in the domestic and international arena, it was felt that specific initiatives need to be taken to strengthen the Company's "process

orientation" on an ongoing basis.

Optimization of machining time is periodically carried out with the help of new generation toolings. Also, standardization of routing times for internal processing is carried out periodically with restriction placed on changing master routings and production routings.

Focus on operational excellence is continuing for strengthening design / engineering, project execution and controls, optimizing cost structure and assets utilization, optimization of throughput at the Company's workshops.

The Company has been certified to the ISO 9001 : 2008 Quality Management System for the last 16 years and has base lined its safety management system with OSHAS 18000:2007.

Pursuant to the Stage 1 audit in June 2017 and the Stage 2 audit executed in July 2017 by certifying body TUV Nord (Accreditation body DAkkS), CMI FPE was upgraded to ISO 9001:2015.

This significant achievement was made possible due to the active involvement of employees across all levels, under the leadership of the Operations Committee and handholding by the QMS team.

It bears mention that the ISO 9001 : 2015 certification was completed in July 2017 (entity readiness handled internally) with 4 Good Practices, 2 Potential for Improvement aspects and no non-conformities noted by certifying body TUV Nord.

Internal quality audits, internal safety audits and internal supplier process audits were carried out as per the Annual Calendar set.

In addition, QMS awareness training, EHS awareness training, as well as internal quality audit refresher training for the team of cross functional internal ISO auditors has been carried out.

The Company had earlier successfully deployed 'CAM software' and 'network infrastructure' to facilitate CAD/ CAM integration. This has given us a capability to simulate tool motions for various machining jobs in the software, thereby arriving at a realistic touch time for the various machining operations on our CNC machining centres.

#### **Information Technology:**

Our Company's business processes have been calibrated in a state-of-the-art ERP system, which provides a high degree of visibility and transparency. Incremental configuration was carried out during the year to improve the functional deployment in line with user needs.

Training programs, facilitated by internal faculty, were carried out for users of the Company's ERP system to optimize productivity in the use of this application. The Company has also deployed a reliable infrastructure for local onsite backups and cross site replicated backups, which are auto-scheduled.

The entity's internal Data Centre 'hardware refresh' for Servers, Storage was completed in October 2017 and for Network Active Devices in March 2018, with zero downtime. Care was taken to deploy suitable sizing tools on the old infrastructure to determine new infrastructure provisioning on a realistic basis. All Server workloads have been virtualized.

The WAN topology was further optimized by provisioning a separate Firewall at Talaja Plant and a redundant ILL (Internet Lease Line) link of 4MBPS for Email and business internet, independently out of Talaja Plant.

The Mailing application and Operating System were upgraded with zero downtime. Also, download interfaces from SAP to the APS application were built internally in SAP without external support, with significant saving accruing to the Company. Some critical APS application enhancements were completed in March 2018. This has significantly increased the efficacy of the APS application in project related complex planning scenarios. SAP enhancements for GST were carried out in a timely manner.

As part of its security posture, the entity has deployed Security Certificates on its website and Mail Server to enhance security. It has also deployed a 'Web Gateway' and 'Messaging Gateway' to protect against 'zero day attacks', 'Advanced Crypto malware', 'Cyber Threats'.

We have also provisioned a Disaster Recovery capability, on an outsourced model with a well-defined Service Level Agreement to a third party data centre. This Disaster Recovery capability was implemented based on a detailed 'project plan'. Periodic Disaster Recovery drills are carried out.

#### **Internal Control Systems:**

The Company engaged PricewaterhouseCoopers Private Limited as Internal Auditors for the year under review, for examining the adequacy and compliance with laid down policies, controls, statements of operating procedures and statutory requirements. The Audit Committee of the Board of Directors approves the Annual Internal Audit Plan at the beginning of the year, and reviews at every meeting the findings from the internal audit reports as well as action taken on the matters reported. The focus of the Internal Audit team is on identifying improvements in "business processes" and "design of controls", with "substantive testing" being carried out as needed.

The scope of the Internal Audit mandate covered traditional audit reviews for key processes, analytics to be run on a periodic basis on the entity's ERP system to track the health of key controls, special reviews, to be carried out on the directions of the Audit Committee along with IFC (Internal Financial Controls) reviews – 'test of design' and 'test of operating effectiveness' for 11 processes.

#### **Cautionary Statement:**

The Statements made in this report are forward-looking and are made on the basis of certain assumptions and expectations of future events. The Company cannot guarantee that these forward-looking statements will be realized, though they are set out based on anticipated results and management plans. The Company's actual results, performance or achievements are subject to risk, uncertainties and even inaccurate assumptions, which could thus differ materially from those projected in any such forward looking statements. The Board of Directors of the Company assumes no responsibility in respect of the forward-looking statements mentioned herein, which may differ in future on account of subsequent developments, events or otherwise and the Company is under no obligation to publicly update any forward-looking statements on the basis of subsequent developments, information, future events or otherwise.