



REPORT JUNCTION

Sona THE PASSION TO BE WORLD CLASS
SONA KOYO STEERING SYSTEMS LTD

2003 • 04

Report  Junction.com

CONTENTS

2	Chairman's Letter
5	Board of Directors
7	Management Discussion & Analysis
17	Corporate Governance
25	Additional Shareholder Information
29	Directors' Report
33	Auditors' Report
36	Financials



THE DEMING PRIZE

The Deming Prize, awarded by the Union of Japanese Scientists and Engineers (JUSE) is one of the highest awards on TQM (Total Quality Management) in the world. It was established in 1951 in commemoration of the late Dr. William Edwards Deming, who contributed greatly to the proliferation of quality control in Japan after World War II.

Applicant companies and divisions of companies eligible for the Awards are those seeking new approaches to quality management that meets the needs of their business environment. These organisations develop effective quality management methods and establish the structures for implementation of these methods.

The Deming prize examination does not require companies to conform to any pre-existing model. Rather, the companies are expected to establish their own themes and objectives as per their current situation, and deploy them company-wide.

Commonly, those who have won the Prize share the feeling that they have had a valuable experience, and that the management principle of achieving business success through quality improvement has transformed their organisations. Thus, quality management has spread to many organisations, and its methods have evolved over the years.

There is no easy success at this time of constant change. No organisation can expect to build excellent quality and management systems by merely solving problems set by others. They need to set lofty goals and drive themselves towards achieving those goals. The Deming Application Prize is a tool for companies that introduce and implement TQM in this manner to transform their business management.



Dr. Surinder Kapur delivers his acceptance speech at the Deming Awards function





Chairman's Letter

Dear Shareholders,

India is back on a high growth path. For 2003-04, India's GDP growth will be 8.1 per cent. It will be the highest since economic reforms began in 1991, and second highest growth rate among the large economies of the world in 2003-04 — second only to China.

Thanks to this growth impetus leading to an increase in disposable income and easy access to financing schemes, the automobile sector witnessed a substantial spurt in demand though with some lag. According to the international benchmark, an automobile market is considered global sized when it sells over a million cars and utility vehicles. As I write this letter to you, India has nearly become a million car and utility vehicle market.

Your Company, which primarily manufactures steering systems, columns and driveline components for cars and utility vehicles, has begun to reap the scale advantages of a dominant share in the million vehicle Indian market. Moreover, it has crystallized its plans to and got the processes in place to become a significant exporter of auto components.

Driven by volume growth in India, your Company has achieved the excellent results. Given opposite are some indicators.

- Sales grew by over 30 per cent to Rs.2,869 million in 2003-04.
- Profit before depreciation, interest and tax (PBDIT) increased by nearly 60 per cent to Rs.283.5 million in 2003-04. The PBDIT margin increased from 10 per cent of net sales in 2002-03 to 12.1 per cent in 2003-04.
- Post-tax profit (PAT) grew by almost 100 per cent to Rs.121 million.
- RONW grew from 11.4 per cent in 2002-03 to 19.8 per cent in 2003-04. And earnings per share (EPS) increased from Rs.5.6 to Rs.13.8.

From my point of view, however, the high point of the year has been your Company winning the coveted **Deming Prize** in November 2003.

Instituted in 1950, the Deming Prize is considered by manufacturers as the most coveted award for quality. After stringent procedures and auditing by the Union of Japanese Scientists and Engineers (JUSE), the Prize is awarded to companies that have achieved distinctive performance improvement through the application of total quality management (TQM) in a designated year. It has been won by only a handful of non-Japanese companies. Sona Koyo Steering is proud to be one of them.

The benefits of the Deming Prize are manifold. The use of TQM principles throughout your Company has created a new mind-set in all of Sona's employees. Today, in Sona, there is a new corporate culture, which actively encourages employees to take ownership, voluntarily resolve problems and issues, focus wholly on quality, delivery and the needs of the customer, and exhibit a high level of corporate ownership. Your Company's employees are delighted, and even more motivated, to belong to an internationally recognised club of manufacturing and managerial excellence.

TQM tools have re-engineered production to eliminate waste, reduce costs, improve throughput and reduce inventories. In addition, our TPM (total productive maintenance) programme is improving operational efficiencies with its emphasis on zero accidents, zero breakdowns and zero rejections. These benefits have been critical to the success of Sona in the last couple of years and my belief is that they will continue to play a vital role in the progress of Sona.

In a year of softening component prices and an unprecedented 35 per cent hike in the price of steel, your Company has succeeded in raising operating profit margin from 10 per cent of net sales to above 12 per cent. This has much to do with our practice of TQM and TPM at all levels.

TQM and TPM are creating excellence in manufacturing. These will further help to consolidate your Company's position as a world class manufacturer of auto components — which ought to result in more substantial opening of global markets. Our vision is "To Make Sona Koyo A 'Supplier Of Choice' to Global Customers". For this, we have set the first milestone for 2006-07: to achieve net sales of Rs.5 billion, of which exports should be Rs.1 billion.

Although the export target might seem ambitious, I strongly feel that we will achieve it by 2006-07. There is an order book of almost Rs.750 million for 2006-07. Therefore, given your Company's partnership with Koyo Seiko and becoming an integral part of Koyo's global sourcing strategy, the Rs.1 billion export target for 2006-07 is achievable.

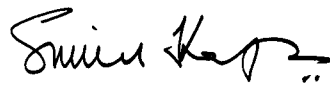
To become a "supplier of choice" for global automobile majors, we not only require further improvements in productivity but also need to develop partnerships with customers. Going forward, therefore, Sona has to transform itself from being just a manufacturing company to one that has high class research, design and development capabilities. Today, your Company has a 18-member R&D department comprising professionals specialising in electronics and mechanical engineering. It has also started a special R&D project in collaboration with the Indian Institute of Technology (IIT) Delhi, and has developed some innovative technologies that reduce costs while improving product performance. Such R&D work will intensify significantly in the future, with a focus on virtual development, prototyping and *real time simulation*.

While your Company has had a cordial relationship with its workers, to be a globally competitive player in the tough world of auto components, we need greater flexibility in the deployment of labour. More flexible labour laws alone can impart an extra 2-4 percentage point improvement in manufacturing costs — which can make all the difference to a company's competitiveness. I hope that the new government will address this issue.

I am optimistic about your Company's future. We can maintain double-digit growth. I can clearly see greater exports' visibility. In fact, given the need to build global scales, your Company intends to continue making investments in new capacities. In 2004-05, Sona has planned for investments worth Rs.540 million.

Your Company expects the growth momentum to continue. If we can leverage this, use the enthusiasm within Sona on winning the **Deming Prize** to further improve productivity and efficiency, and focus on R&D, design and development, you should see a healthy growth in your Company's top- and bottom-line.

Our mission is "To Create A Company that India is proud of". With your support and that of our customers, vendors and employees, I think we will achieve this goal in the years ahead.



Dr. Surinder Kapur
Chairman & Managing Director



Sona

SONA KOYO STEERING SYSTEMS LTD.

BOARD OF DIRECTORS

Dr. Surinder Kapur
Chairman & Managing Director

Mr. Kiyoshi Takeda
Nominee of Koyo Seiko Co., Ltd.

Mr. J. Sugimori
Nominee of Maruti Udyog Ltd.

Mr. Jug Mohan Kapur
Mr. B.L. Passi
Mr. Lalit Suri
Mr. Chander Uday Singh
Mr. Ravi Bhoothalingam
Mr. P.K. Chadha
Mr. Sunjay J. Kapur

EXECUTIVE MANAGEMENT

Dr. Surinder Kapur
Mr. K.M. Deshmukh
Mr. P.V. Prabhu Parriker
Mr. Yoshitaka Akiyama

COMPANY SECRETARY

Sudhir Chopra

COLLABORATORS

Koyo Seiko Co., Ltd., Japan
Mando Machinery Corporation, Korea

AUDITORS

M/s S P Puri & Co.
Chartered Accountants
4/18 Asaf Ali Road
New Delhi 110 002

BANKERS

State Bank of India
Standard Chartered Bank
State Bank of Hyderabad
Citibank N.A.
The Hongkong and Shanghai Banking Corp. Ltd.

REGISTRAR AND SHARE TRANSFER AGENT

MCS Limited
Sri Venkatesh Bhawan
W-40, Okhla Industrial Area, Phase II
New Delhi 110 020

REGISTERED OFFICE

UGF-6, Indraprakash
21, Barakhamba Road
New Delhi 110 001

CORPORATE OFFICE

8th Floor, DLF Square, Jacaranda Marg
M Block, DLF City Phase II
Gurgaon 122 002 (Haryana)

LIAISON OFFICE

2nd Floor Piramal Mansion
235, D. N. Road, Fort
Mumbai 400 001

WORKS

1. 38/6 NH-8
Delhi-Jaipur Road
Gurgaon 122 002 (Haryana)
2. P.O. Box 14
Chennai-Bangalore Highway
Sriperumbudur
Distt Chinglepet
Tamil Nadu 602 105

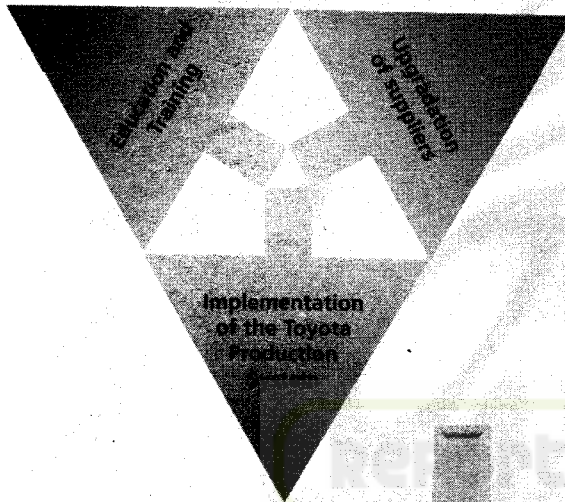


SONA'S DEMING PRIZE JOURNEY

For Sona, embarking on the TQM program has been a journey and not a project with deadlines, and winning the Deming Prize is the first major milestone. The journey has been an opportunity to learn, develop skills and continuously improve through practise of TQM techniques.

Preparing for the Deming examination resulted in benefits that were both business and cultural. While we saw improved quality, reduced cost, enhanced productivity and shorter period of new product development, we also saw the breaking down of intradepartmental barriers, an eagerness to build standardization, the enforcement of values, a better understanding of business plans and deepened commitment to management policies.

A 3-PRONGED STRATEGY



Drawing up this strategy was the starting point of the journey. The immediate result was a surge in productivity and a drop in customer rejections.

THE DEFINING MOMENT

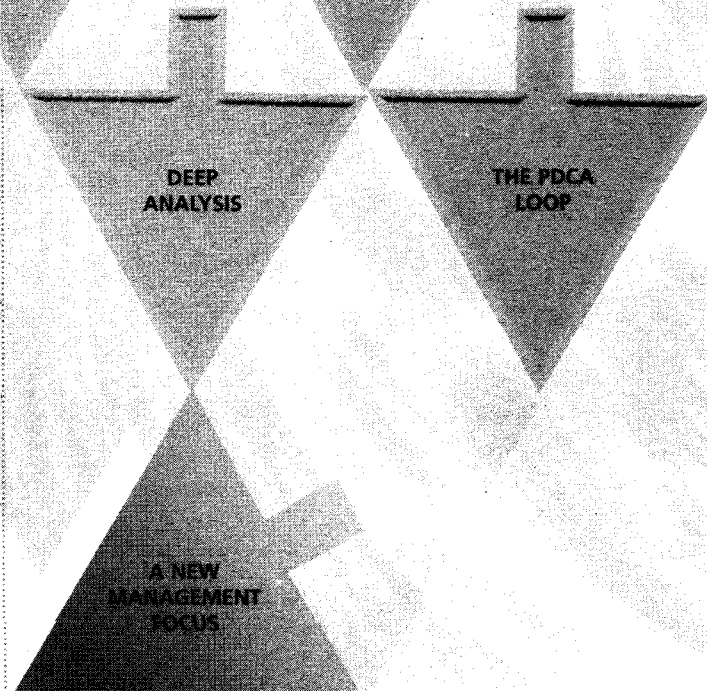
The inflexion point of our journey came with the creation of the Group Kaizen Activities with 100% participation of all employees.

TECHNIQUES FOR IMPROVEMENT

The TQM style of management teaches techniques for analyzing and improving the capabilities of given processes & systems.

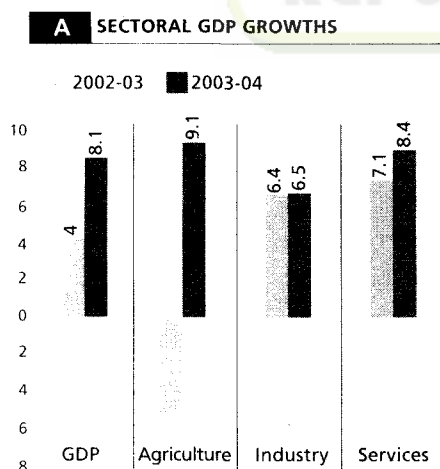


THEN	NOW
Management focus on Controlling Quality	Management focus on Improving Quality
PDS (Plan, Do, See)	PDCA (Plan, Do, Check, Act) Always looking for gaps & finding counter measures
Problem Change the system	Problem Eliminate weakness for existing system rather than changing the system



Management Discussion and Analysis

India's economy is on the move. After a low GDP growth in FY2003 of 4%, GDP growth momentum commenced with a 5.7 per cent growth in the first quarter of 2003-04 followed by a 8.4 per cent growth in the second quarter and 10.4 per cent growth in the third quarter. **Real GDP growth for 2003-04 is estimated at 8.1 per cent.** This will be the second highest growth rate in the world after China. Chart A compares overall and sector-wise GDP growth rates between 2002-03 and 2003-04.



Note: CSO estimates, (Press Release : 9th February, 2004)

Sona manufactures steering systems and driveline components for passenger cars and utility vehicles, therefore, the Company's performance is closely linked to the performance of these automotive industry segments. The impressive macro-economic environment coupled with easier access to and lower cost credit has resulted in high growth in the automobile industry during 2003-04. India is approaching the million car and UV market size and will figure among the top 10 automotive markets in the world.

The Indian market can be broadly classified into four segments — economy, medium, lower premium and upper premium. Initially, there were two classes of customers: a middle-income category which preferred economical cars and a higher income category which are relatively price insensitive and preferred technologically advanced cars with high brand value. The industry has since matured. Today, in India, there are several OEMs with offerings in each segment. Thus, the market is being increased by approaching not only the first time buyers with cars in the economy segment, but also inducing middle-income buyers to purchase higher segment cars.

In this phase of rapid market expansion, while brands and technology are important, the key differentiator between competing products is price. Manufacturers like Maruti Suzuki have been constantly reducing prices of their economy models to induce two-wheeler buyers, and to make their mid/premium cars more affordable. Therefore, it is very likely that the value growth of the industry in 2003-04 has not kept pace with the impressive volume growth of 28%.

As a result of price wars among OEMs, they have pressurised their component vendors to cut prices as well. Consequently, auto-component manufacturers in India are increasingly operating in a soft price regime. In 2003-04, the margin pressure increased significantly on account of an unprecedented 35 per cent hike in steel prices.

Sona has been able to withstand these pressures. It has succeeded in posting its highest sales as well as profit in the last five years. We are satisfied with this performance and believe that it is a testament to our efforts at creating long term shareholder value. The highlights of Sona's financial performance in 2003-04 follow overleaf.

• **Total sales** grew by over 30 per cent from Rs.2,192 million in 2002-03 to Rs. 2,869 million in 2003-04.

• **Profit before depreciation, interest and tax (PBDIT)** as a ratio to net sales increased from 10 per cent in 2002-03 to 12 per cent in 2003-04

• **PBDIT grew** by over 58 per cent from Rs.179 million in 2002-03 to Rs. 284 million in 2003-04.

• **Post tax profit (PAT)** grew by almost 100 per cent from Rs. 61 million in 2002-03 to Rs.121 million in 2003-04.

As a result,

• **Return on capital employed (ROCE)** increased from 10.2 per cent in 2002-03 to 16.5 per cent in 2003-04.

• **Return on net worth (RONW)** increased from 11.4 per cent in 2002-03 to 19.8 per cent in 2003-04.

• **Earnings per share (EPS)** also has increased from Rs.5.61 in 2002-03 to Rs.13.76 in 2003-04.

Apart from these financial achievements, Sona adherence to TQM practices were recognised in 2003-04 when it became the world's first steering company to bag the prestigious **Deming Prize**.

MARKETS

Domestic

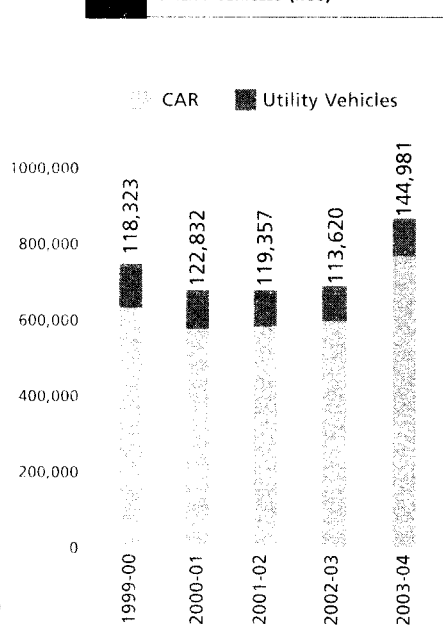
Your Company primarily manufactures steering systems (steering gears and columns), axle components and propeller shafts and caters mainly to cars and utility vehicles. As mentioned earlier, for all purposes, India has

become a market of a million cars and UVs. Driven by a buoyant economy, there was a sharp increase in sales of passenger cars (including MPVs) and utility vehicles in India. The former grew by 27 per cent from 593,578 units in 2002-03 to 755,771 units in 2003-04, while the latter rose by 28 per cent from 113,620 units in 2002-03 to 144,981 units in 2003-04. Both segments recorded their highest-ever sales volumes. Chart B plots volume sales in cars and UVs over the last five years.

In terms of volumes, with over 45 per cent market share, Sona is the leader for steering gears and steering columns for the passenger car and UV segments. In 2003-04 your Company recorded its highest ever sales. Chart C plots Sona's sales in the last five years.

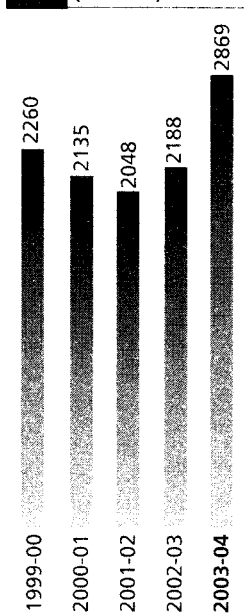
This top-line growth is due to volume driven growth. Prices have, however, continued to be under pressure. Segment A constituting the economy segment (Maruti 800, Omni) registered volume growths, however, their share in total revenue continued to decline. This is reflected in reduction in share of the economy segment in total car sales, as shown in Chart D. The focus of your Company now is to have greater customer diversity, and increase the sale of power steering systems which cater to the medium and lower premium segments.

B SALES GROWTH IN CARS AND UTILITY VEHICLES (NOS)

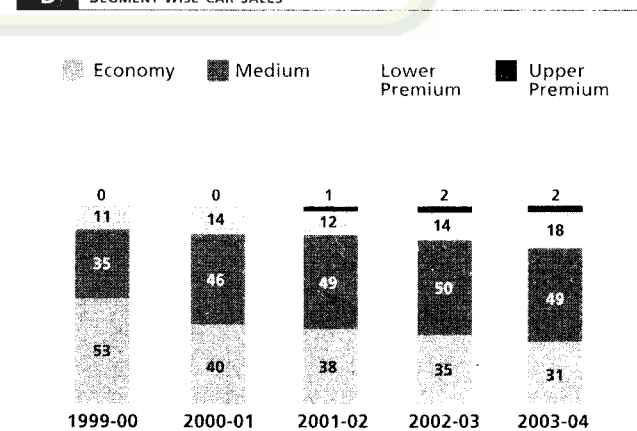


Source: SIAM flash reports (March each year)

C SONA'S SALES IN LAST FIVE YEARS (RS MILLION)



D SEGMENT-WISE CAR SALES



While Maruti remains our largest customer, Sona has targeted other OEMs to diversify the risk of overdependence on Maruti. The share of other OEMs like Hyundai and Mahindra in our customer portfolio has increased to 10 per cent and 17 per cent, while that of Maruti has reduced to 57 per cent.

Your Company believes that power steering — both electronic and hydraulic — will be the growth drivers in the steering systems industry. Your Company has laid emphasis on localising this product segment — power steering sales grew by 58 per cent in 2003-04 over 2002-03. The