



KIRLOSKAR OIL ENGINES LIMITED | ANNUAL REPORT 2003-2004

Enriching Lives

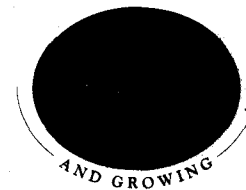
GLOBAL EMISSION NORMS

WIDEST RANGE OF ENGINES - 3 TO 11,000 HP

WORLD'S LARGEST GENSET BUSINESS IN 15 TO 250 kVA



TURNOVER OF 1000 CRORES



Yet another milestone achieved, as the journey continues.



Kirloskar Oil Engines Limited is now a 1000 crore company. A milestone

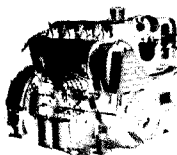
which we have crossed, thanks to your continuous support and trust



in us and our products. You'd be pleased to know that our world class engineering

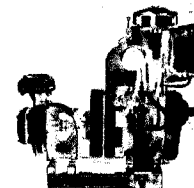
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solutions are making forays into untapped markets and the future looks promising



and buoyant. Which means, in the journey ahead, we are that

much more confident of crossing many more milestones.



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**Other public listed companies in Kirloskar Group:**

Kirloskar Brothers Ltd. - Kirloskar Pneumatic Co. Ltd. - Kirloskar Ferrous Industries Ltd.

Kirloskar is an acknowledged leader in Air-conditioning & Refrigeration equipments, Alternators, Engines, Engine Bearings, Engine & Transmission Castings, Air & Gas Compressors, Gensets, Engine Valves and Pumpsets.

## Annual report for the financial year ended on 31st March 2004

### Board of Directors

Mr. Atul C. Kirloskar	Chairman and Managing Director
Mr. Sanjay C. Kirloskar	Vice Chairman
Mr. Gautam A. Kulkarni	Joint Managing Director
Mr. Rahul C. Kirloskar	Director Exports
Mr. A.N. Alawani	Director (Finance)
Mr. D.R. Swar	Director (Engines, Auto Components, P, IR & HR)
Mr. Vikram S. Kirloskar	With effect from 19.05.2004
Mr. V.K. Bajhal	
Dr. N.A. Kalyani	
Mr. H.M. Kothari	
Air Marshal Y.V. Malse (Retd.)	
Mr. P.G. Pawar	
Mr. U.V. Rao	

**Assistant Company Secretary**  
Ms. Aditi Chirmule

### Auditors

M/s Dalal & Shah, Chartered Accountants

### Bankers

State Bank of India  
Bank of Baroda  
Bank of Maharashtra  
HDFC Bank Ltd  
The Cosmos Co-Operative Bank Ltd

### Registrar and Transfer Agent

Intime Spectrum Registry Ltd.

#### Mumbai Office:

C-13, Pannalal Silk Mills Compound,  
Lal Bahadur Shastri Road,  
Bhandup, Mumbai 400078

#### Pune Office:

102, Vidyanand, Dr. Ketkar Path,  
Erandwane, Near Old Karnataka High School  
Pune 411 004

### Registered office

Laxmanrao Kirloskar Road, Khadki, Pune 411 003

### Location of factories

Pune, Ahmednagar, Nasik, Solapur

## A DECADE AT A GLANCE

(Rupees in Millions)

Particulars	31 <sup>st</sup> March									
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Gross fixed assets	1499.72	2112.42	2366.66	2556.98	3291.16	3503.44	3609.95	3715.83	3902.39	3863.98
Net fixed assets	1170.08	1469.01	1583.59	1518.80	1731.41	1654.92	1537.63	1391.69	1414.25	1295.07
Net current assets	897.43	1304.72	2635.31	3614.32	1995.19	2022.57	1236.49	1280.68	914.38	1194.87
Total capital employed	2498.21	3714.05	5147.94	6558.38	5458.11	5315.51	4661.83	4795.31	4063.32	4504.26
Shareholders' funds	862.49	1566.89	2000.63	3475.73	2919.46	3665.01	3508.06	3637.05	3670.65	4157.57
Sales	4073.09	6138.96	6158.42	6313.52	7133.76	7447.95	7941.59	7444.60	8812.60	10412.82
Profit before tax	124.25	213.38	576.93	1716.87	159.19	890.93	417.03	274.00	383.01	1056.01
Retained earnings	87.00	157.20	429.67	1421.30	72.41	745.22	210.97	118.76	301.20	486.92
Dividend :										
Equity & preference	30.13	41.80	42.71	60.65	66.55	67.07	67.07	67.07	97.09	194.16
Equity dividend %	25	25	25	35	35	35	35	35	50	100*
Fob value of exports	220.99	193.56	150.80	169.14	293.43	306.99	443.31	353.07	378.39	610.10

\* Includes SLK Birth Centenary Special Interim Dividend of 50% (Rs. 5 per share) paid in December 2003.

## NOTE:

Preference shares were redeemed during the Financial Year 1996-97.

## Information for shareholders

Annual General Meeting Date:

Monday, 19 July 2004

Time : 11.00 A.M.

Venue : Registered Office of the Company

Proposed Dividend :

50 % (Rs. 5.00 per share of Rs. 10/- each)

[This is in addition to 50% (Rs. 5 per share of Rs. 10/- each) paid as SLK Birth Centenary Special Interim Dividend]

Dates of Book Closure :

9 July 2004 to 19 July 2004  
(both days inclusive)

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## DIRECTORS' REPORT

To the Members,

The Directors have pleasure in presenting this Report with audited annual accounts of the Company for the year ending March 31, 2004.

### Financial Performance:

	(Rupees in 000's)	
	2003-2004	2002-2003
Total Income	10,651,252	9,036,236
Total Expenditure	9,595,239	8,653,225
Profit before tax	1,056,013	383,011
Provision for tax (including Deferred Tax)	348,354	(32,354)
Net Profit	707,659	415,365
Surplus (After other adjustments)	857,498	536,053

### Appropriations

Your Directors propose to appropriate the available surplus as follows:

	(Rupees in 000's)
Proposed Dividend	97,087
Interim Dividend	97,086
Corporate Tax on dividend	24,878
Transfer to Contingency Reserve	NIL
Transfer to General Reserve	250,000
Balance carried to Balance Sheet	388,447

### Dividend:

In addition to the SLK Birth Centenary Special Year Interim Dividend of 50% (Rs.5/- per share) in December 2003, the Directors recommend a final dividend of 50% (Rs.5/- per share) for the year (previous year dividend was 50%) totalling to yearly dividend of 100% (Rs.10/- per share).

### Management Discussion and Analysis:

The operations of your Company comprise of Engine and Engine Bearings and Valves. This business segmentation forms the basis for review of operational performance.

#### A. Industry Overview:

During the year under review, the Indian economy and particularly the manufacturing sector has grown robustly. The automobile sector has also registered strong growth over previous year. The tractor market started showing signs of recovery, and tractor exports are increasing year by year. The resultant growth is also seen in capital goods sector. The services sector of the economy also continues to grow robustly.

We are happy to note that the newly installed Government at the centre has said that agriculture, road construction, housing will continue to be their priorities.

This vibrant economic scenario generated good demand for power generating sets, construction and material handling machinery and automobile components. However, in the irrigation pumpset sector, the demand for pumping units dropped by 12% and the input cost increases that could not be fully passed on to the consumer resulting in pressure on margins in this sector.

As regards competition within the sectors of economy in which the Company operates, it is our view that competition will continue to increase. Thus, marginal players who are not competitive will feel increasing pressures to survive.

## **B. Company Performance:**

During the year under review your Company achieved sales of Rs. 10,025 million (previous year Rs.8,639 million) in spite of sluggish tractor and farm machinery market resulting in increase in sales by 16% over previous year. The significant milestone of crossing Rs.10 billion sales was achieved in this year.

The profit before tax is at Rs.1,056 million (previous year Rs.383 million) after providing for depreciation of Rs. 260 million (previous year Rs.343 million).

**Analysis for both segments – Engines and Engine Bearings and Valves is presented below.**

## **C. Segment-wise Operational Performance:**

### **Engines:**

The sales of engines registered 22% increase at Rs. 7,807 million (previous year Rs. 6,413 million) in the year under review. The engines up to 20 hp are used in the farm machinery, generating sets and construction machinery. In this range, your Company faces competition from several domestic players, and your Company's strategy is to expand market share by in-depth effective marketing activities in the potential villages and offer products for each use while improving distribution network in depth, quality and service. However, the irrigation pumpset market dropped by 12% in the year under review. In spite of such drop in this market and significant drop in sales against world bank tenders as compared to previous year, Company's sales grew marginally in the year under review.

In the market upto 20 hp, the input cost increases experienced from second half of the year could not be fully passed on to the consumer as these products use Iron and Steel in much larger proportion as compared to higher output engines.

The Farm Tractor market started showing signs of revival from second half of the year and market share of our principal customer in this market – Punjab Tractors – has started growing. The growth in sales to tractor manufacturers is also due to Company developing engines to meet specific needs of domestic and international markets and offering these at competitive prices. Tractor manufacturers believe that exports of their tractors with our Company's emission compliant engines will increase in coming years.

The engines developed by your Company in 50 to 105 hp range not only surpass Indian emission norms, but also meet Tier II norms for off road use in United States and are capable of Tier III up-gradation as it becomes necessary. It is significant to note that as last published, your Company's fourteen engines were approved by Emission Protection Agency (EPA) of United States. This is the highest number of approvals given as on date to any engine manufacturer in India. Besides opening doors for Indian equipment manufacturers to explore worldwide markets, this technology development is also enabling your Company to offer engines meeting emission norms to foreign customers. Company has started seeing initial successes in securing OEM customers in overseas markets. Parallely, the essential and time-consuming activity of creating after sales service network in chosen overseas markets continues.





Government of India has set very challenging emission and noise standards for diesel generating sets. We had reported last year that your Company's gensets are the first in the world to be certified to meet world's toughest emission norms for generating sets set by Government of India. Now, the Noise Emission Norms set by Government of India are scheduled for implementation from July 01, 2004. You will be happy to know that your Company's silent canopies have been approved by the authorities months ahead of implementation date. Here again, your Company is the first one to obtain such approvals and be ready to meet the regulatory and market requirements.

The Power Generation market experienced a double-digit growth in the year under review mainly due to demand from manufacturing, telecommunication and services sector. The sales of factory assembled generating sets launched in the previous year continued to grow in the year under review.

Your Company concentrated on effective marketing of the gensets under the brand "Kirloskar Green Power Ideas".

The Company has introduced generating sets in 250 to 600 kVA range in the previous year. These products now command a share of about 10% in Indian market.

In the previous years, your Company decided to improve the quality and specifications of generating sets. Thus, "Kirloskar Green Power Ideas" were conceptualized and implemented. Over time, the brand "Kirloskar Green Power Ideas" has become the largest selling brand of diesel generating sets in the country. In the year under review, your company expanded on the list of aggregates used in the "Kirloskar Green Power Ideas" gensets by providing silent canopies and increasing sales of AG generators. This has not only resulted in improved quality of gensets offered to end users but has also improved the distribution of aggregates of the gensets as your Company controls the manufacture, quality and distribution of all aggregates. Moreover, customers benefit by obtaining single window service for complete generating set.

As a result, your Company registered an increase of 25% by units and 20% by value over previous year in the range 15 to 600 kVA. With a business of over 40,000 diesel gensets in the range of 15 to 600 kVA, we believe this is amongst world's leading businesses in its class. We are leveraging this position to increase exports.

In the year under review, Company delivered seven engines and four generating sets in range 1600 to 11000 hp. The sales of generating sets in 2.5 MW class and strong order board for these affirms the customers confidence in the Company to deliver quality products at competitive prices.

Your Company assesses that Construction and Material Handling Equipment has good prospects in the country. In the year under review, couple of foreign manufacturers have set up manufacturing facilities in India and you will be happy to know that these new entrants have chosen your Company's engines for OE fitment on machines for domestic and foreign markets. In the year under review, your Company's sales to this sector grew by 17% by value and 14% by units.

Engines for stationary fire fighting pumps is another thrust area for your Company. In the previous year seven engine models were introduced to this market after required development and certification. Now, we see signs of these engines being accepted by foreign markets.

Your Company is an established supplier to the Indian Armed Forces for decades of engines and engine based systems. In the year under review, your Company has expanded range of its supplies to the Armed Forces and sales have increased in units and value.

#### **Engine Bearings and Valves:**

The buoyant automobile market, especially commercial vehicle and car markets grew robustly in the year under review. Moreover, increased goods movement resulted in growth in aftermarket. The resultant growth in your Company's sales was about 13% over previous year at Rs. 968 million (previous year Rs. 854 million).

The growth of industrial engine production in the country resulted in about 30% increase of sales to this class of customers.

It is noteworthy that three leading Automotive OEM customers have increased purchases from your Company significantly due to superior service, near zero defects and quicker product development. And, five new OEMs have been added to the list of customers in the year under review.

The sales of engine valves grew by about 20% in the year under review.

#### **Other Businesses:**

Your Company is also in the business of manufacturing gray iron castings and trading in oil and power generation and power sales. Additionally, during year under review, your Company has obtained licence to trade in power.

The casting business predominantly supplies to Company's engine business. However, external sales of castings increased during the year and new foreign customers were developed for specialized castings. The financial performance of castings business improved further during the year under review.

The oil trading business caters predominantly to Company's engine users who require fuel oil and also lubricants. This business registered double digit increase in the year under review while expanding its area of operations, customer base and product range.

The Power Business at Hospet in Karnataka was de-emphasised to some extent due to adverse power tariff and cost relationships. This resulted in drop of about 15% in sales of power.

#### **Cost Control:**

Your Company believes that costs have to be continuously brought down while improving product performance. Towards this objective, several initiatives started in previous years have delivered results in the year under review. Noteworthy results seen in the year under review are improved Employee Expenses to Sales and Value Added ratios.

In the second half of year under review, economy started experiencing unprecedented and volatile increase in Iron and Steel and Copper prices. The impact of increase was also felt by your Company and efforts were made to pass on the increase to the market. Due to inability of the markets to fully absorb price increase, the raw material consumption increased marginally as a percentage to sales during the year under review.

#### **D. Exports:**

Your Company traditionally exports engines, pumpsets and generating sets mainly to Africa, Middle East, and Asian Region. In order to increase exports, Company has upgraded products to meet international market expectations in the previous years. The results of specific efforts to increase exports are now showing as the Company's product, geographic and customer class portfolio is being expanded. By securing OEM business in Europe, USA and China we expect to grow exports significantly and also to remove year on year uncertainties. Though OEM business takes time to develop momentum, initial interest of customers is promising.

The efforts to increase exports of engine bearings, bushes and valves have resulted in a significant rise in sales. The focus for this product group is to develop new products targeted at precise needs of the foreign markets. Thus, this business is now leveraging Company's capability to design and develop bearings and valves on the strength of Company's engine design capability.

In the year under review, the exports of the Company grew by 67% to Rs. 632 million (previous year Rs.378 million).

With continued efforts, your Company's exports sales are poised to soon cross Rs.1,000 million mark.



**E. Concerns and Threats:**

We notice signs of competitive pressure from foreign manufacturers in the range up to 20 hp engines. The Company is addressing the threat by developing new cost effective products precisely targeted at meeting customers needs and also to attend to cost increase in Iron and Steel that could not be fully passed on to the market in the second half of the year under review.

**F. Prospects for Current Year:**

The domestic farm machinery market in engine range up to 20 hp is expected to remain weak due to inability of market to absorb price increase necessitated due to increase in Iron and Steel prices. The Company's efforts are to design products that meet customers expectations while lowering costs.

The tractor market is now growing. And, the market share of Punjab Tractors Ltd. is increasing. Moreover, tractor manufacturers have shown interest in increasing exports of tractors with our Company's emission compliant engines. We believe that these factors will result in healthy increase in sales in the current year.

In the current year, Company will enhance its customer centricity by implementing world class Customer Relationship Management (CRM) solution that will run on Internet in a similar way as presently deployed IT solutions.

The genset market is expected to continue its growth driven by demand from manufacturing and services sector in the vibrant economy. Barring unforeseen developments, the genset market and your Company's sales to this market will grow in the current year.

Having secured new customers who have introduced new equipments with Company's engines growth in sales to Construction and Material Handling market is expected in the current year.

As the growth of automobile sector continues, your Company expects to continue increase in sales of Engine Bearings and Valves.

With the healthy growth in domestic sales and exports expected in coming years and also to meet product up-gradation needs, Company expects to invest adequately in plant and machinery in the current year. This capital expenditure will be targeted to expand capacity, develop new products, improve quality and reduce costs. We expect that the benefits of capacity expansion will start from later half of this year.

**Cautionary Statement:**

Statements in this Report, particularly those which relate to Management Discussion and Analysis, describing the Company's objectives, projections, estimates and expectations may constitute "forward looking statements" within the meaning of applicable laws and regulations. Actual results might differ materially from those either expressed or implied.

**G. Internal Controls Systems and their adequacy:**

Your Company's operations are IT enabled for the last few years by use of the world-renowned Enterprise Resource Planning (ERP) system. In the year 2000, the entire Supply Chain from dealers to factories, to suppliers was Internet enabled for on-line eCommerce transactions. In the year under review, your Company extended the use of these proven solutions to cover operations of sales offices and logistic service providers to Engine Bearings and Valves business and to large engine and castings. Additionally, your Company started use of enhanced IT interface and transactions with banks and also use of world class IT solutions in Cash Management and Treasury functions.

While the wide and in-depth deployment of IT solutions provides built-in controls, checks and audits, the purity and timeliness of data input has to be ensured for good final results. To ensure that the data captured is accurate and timely, many initiatives have been taken in last couple of years. Thus, stage is now reached wherein manual intervention and efforts are substantially cut down and ensure its quality and integrity.

The selected auditing firms continue to conduct Internal Audit of the Strategic Business Units, Corporate Services, and Area Offices of your Company. The system weaknesses noticed during the audits have been attended to the satisfaction of the Audit Committee of the Board of Directors.

#### **H. Personnel and Human Resource:**

Company continues to enjoy healthy and productive relationship with employees. One reflection of this can be seen in Company's ability to execute Wage Agreements with the Employee Union for the next period of three years prior to expiry of the previous three-year period. The latest such agreement valid for 3 years starting with the current year was executed on March 31, 2004. This is the fourth agreement that has been executed prior to expiry of the previous agreement and each subsequent Wage Agreement has enhanced productivity goals.

#### **I. Environment:**

Your Company has to deal with the environmental issues on two fronts. One, the Company's products (that is, engines) are inherently polluting. Thus, research and technology up-gradation is necessary to meet the stringent emission standards. The Company's products already meet the emission standards in target markets. With the investment in the emission center, and development of in-house capability, your Company is poised to keep developing products to meet future standards.

Two, the Company believes that operations have to exceed the regulatory norms concerning pollution. Towards this objective, your Company has in place TUV certified Environmental Management System to ISO-14001 since November 1999.

In the year under review, Company obtained noteworthy certification for its engines for emission compliance to government of India's norms and also to EPA, USA norms. Additionally, Company obtained certification of its silent canopies for generating sets to the norms set by Government of India.

#### **Buyback of Shares:**

You may recall that the Board of Directors of your Company approved buyback of 4,000,000 equity shares of Rs. 10 each, from its shareholders, in its meeting held on 23 April 2003, at a price of Rs. 75 per share. The Securities and Exchange Board of India (SEBI), vide its letter no. PMIMD / Buyback /AK/11023/03 dated June 5, 2003, advised your Company not to proceed with the buyback of equity shares till further communication from it in this regard. Thereafter your Company has not received any communication from SEBI.

#### **SEBI Regulations & Listing Fees:**

Since SEBI has stipulated electronic filing of Annual Report, Corporate Governance Report, Financial Results, Share Holding Pattern etc. on website [www.sebiedifarnic.in](http://www.sebiedifarnic.in), statements of your Company can be accessed at this website.

The annual listing fees for the year under review have been paid to Stock Exchange, Mumbai and National Stock Exchange of India Limited, where your Company's shares are listed.

Your Company's equity shares were delisted from Pune Stock Exchange with effect from 6 October 2003.

#### **Directors**

Mr. V. K. Bajhal, Mr. H. M. Kothari and Air Marshal Y. V. Malse (Retd.), retire by rotation and being eligible, offer themselves for re-appointment.

The brief resume and other details relating to the Directors, who are to be reappointed, form part of the Report on Corporate Governance.

Mr. Vikram S. Kirloskar was appointed on the Board as an Additional Director with effect from 19 May 2004. He holds office upto the date of the ensuing AGM. He is eligible for appointment.