

“HCL Infosystems’ Q2 FY18 Results Audio Conference Call”

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SPEAKERS: **Premkumar Seshadri, Executive VC and MD**
Mr. Kapil Kapur, Deputy CFO, HCL Infosystems
Mr. Sutikshan Naithani, Joint President, Consumer Distribution
Bimal Das, Joint President, Enterprise Product Distribution

Moderator: Good day, ladies and gentlemen. I’m Harpreet Kapur, the moderator of this call. Welcome to HCL Infosystems’ Q2 FY18 Results Audio Conference Call. We will start with the presentation and then follow up with a Q&A session. For the duration of presentation, all participants’ lines will be in listen-only mode. This presentation is available in the investor relations section of the company’s website.

We would like to begin with a mandatory disclaimer. This call may contain forward-looking information including statements concerning our outlook for the future as well as some of our other statements of beliefs, future plans and strategies. These forward-looking statements and information are subject to risk and uncertainties that they entail.

We have on the call with us Mr. Premkumar Seshadri, Executive Vice Chairman and Managing Director, HCL Infosystems; Mr. Kapil Kapur, Deputy Chief Financial Officer, HCL Infosystems; Mr. Bimal Das, Joint President, Enterprise Distribution Business; Mr. Sutikshan Naithani, Joint President, Consumer Distribution Business.

I would like to now hand over the proceedings to Mr. Premkumar.

Premkumar Seshadri: A very good afternoon to everyone of you and thank you for being here. Let me start by essentially talking about the

business highlights of the quarter that went by. Our Q2 revenue for 2018 was Rs. 881 crore, up from Rs. 685 crore in the previous quarter registering an increase of 29% quarter-on-quarter (q-on-q). As to what contributed to it and where it came from, we will be talking about as we progress. Primarily, this growth happened out of a significant momentum in the consumer distribution business, which went up to Rs. 299 crore in the last quarter from a low of Rs. 69 crore in Q1

We have been working on the consumer business. We were challenged by a portfolio issue which technically began almost 13–14 quarters ago. We had experienced a continuous Q-o-Q decline in a particular product; hence, we realigned our strategy to make it more appropriate to the market momentum. The multi-brand strategy of looking at the new avatar of Nokia through their Android product range, as well as the addition of Apple in our portfolio has given a boost to the momentum here. So after almost 14 quarters, but for a few exceptions here and there, we are, for the first time, seeing a robust Q-o-Q growth in this business.

On the Enterprise Business, if we refer to the last 13–14 quarters, that is, from fiscal 15 when this business was fundamentally incubated, it will be evident that we have reached the first phase of the threshold, maintaining approximately Rs. 300 crore in the last few quarters. The investments that we had made in the earlier quarters towards stabilizing this business from a market creation point of view are yielding profits now. Though on a Q-o-Q basis the Enterprise Business has undergone slight changes, but they were more in the context of specific deals. In this period we also had to deal with some of the changes in the regulatory space.

As far as the SI business is concerned, we are continuously seeing a reduction in the overall order book over the last 8–10 quarters, pertaining to some of the large contracts. However, we are glad that the total value of the build phase of the business is sub-Rs.100 crore. The total order book is down to Rs. 816 crore, it is worth mentioning that 12–13 quarters ago this amount was about Rs. 2500–2600 crore. So there has been a continuous reduction.

As regards the operational result of the company, in Q2 we have suffered a loss of Rs. 24.3 crore vis-à-vis Rs. 24.9 crore in the last quarter.

There has been an exceptional item for the quarter—impairment of goodwill—which has affected services business to the extent of Rs.390 crore. The impairment was the result of a strategy undertaken to review, streamline and wind down some components of services offerings, segments and geographies. We adopted a portfolio rationalization in our services business particularly with respect to service offerings, the customers that we were focusing on, both in public as well as private sectors, and the margin ratios. This has been an ongoing process. Once we started with rationalization and value discovery of the same, we realized that it is important to exit from some markets of the portfolio.

In the Middle East, where vast changes are taking place, Qatar is a core component of our portfolio. We wanted to rationalize so as to make investments at the right places. But as we are consciously attempting at reducing our geography as well we also realized that this would impair our earlier goodwill to some extent.

Similarly, on the consumer care business which largely had focused on the services in the consumer segment, we have been thinking of certain strategic options leading us to value discovery. So these are the core elements that contributed to the impairment of goodwill. However, what is significant is that the profit and loss for the quarter that went by is negative at Rs. 454.4 crore against Rs. 66.5 with Rs. 390 crore contribution obtained from goodwill.

Now, you will receive a detailed picture, through the Q2 P&L snapshot and know about the specific numbers.

Kapil Kapur:

Good afternoon to all of you. I am on slide 5 which gives the snapshot of the P&L. The overall revenue for the quarter was Rs. 881 crore which is a 29% sequential increase from the previous quarter reported at Rs. 685 crore. As explained, it was largely due to the multi-brand strategy kicking off in our consumer distribution business. As a result, the loss before provision and write-offs came down from Rs. 18.2 crore in Q1 to Rs. 11.7 crore in Q2. As the consumer business column of the P&L snapshot shows,

in Q1 the only quarter where there was a loss in consumer distribution was in the PBIT amounting to a loss of Rs. 3.1 crore which made a comeback in Q2 with a profit of Rs. 3.2 crore in Q2. This has been reflected in the improvement of the overall loss of the company at a consolidated level.

Our provisions increased marginally from Rs.11 crore to Rs.15 crore and the loss before tax and exceptional items decreased from Rs. 66.5 crore in Q1 to Rs. 64.4 crore. As explained earlier, this quarter we took an exceptional item of a goodwill write-off, post which the PBT is Rs.454 crore of loss.

Slide 6 is similar to the previous slide except that it shows a bifurcation between enterprise distribution and enterprise services. Enterprise Distribution revenue was Rs. 316 crore. The margins improved from a Rs. 40 lakh profit to Rs. 1.7 crore. However, in services, due to rationalization the loss went up from Rs. 10.6 to Rs. 14 crore.

The next slide presents a detailed view of the consumer distribution business which has been discussed earlier. We embarked upon a multi-brand strategy a couple of quarters back which is now showing some good initial results. Of course, the full impact of this transition will take a couple of quarters more because if we take the example of Apple, we did it only for a week in end September. So, the revenue for consumer distribution business which was at Rs. 69 crore has increased up to Rs. 299 crore in Q2.

The next slide shows the numbers. So revenue amounted to Rs. 299 crore and the PBIT saw an upswing of about Rs. 6 crore, having Rs. 2.3 crore positive from a negative of Rs. 3.1 in the previous quarter.

The next slide gives details on the enterprise business. Our revenue in this quarter was Rs. 316 crore, a little lower than Q1 due to certain temporary factors such as delay in receipt of material and certain GST-related complications post the rolling out of GST in the previous quarter. However, some of the orders which were supposed to be executed in the previous quarter are now getting executed in the current quarter.

With regard to enterprise services, revenue amounted to Rs. 235 crore, sequentially better than the previous quarter, but

there was a one-off order in this quarter which caused the revenue to go up. In Singapore we continue to be stable and do well. We executed a major command centre comprising remote infra platform for a major government project, so this geography is doing well for us.

The next slide shows that the overall revenue of enterprise business, including enterprise products and enterprise services is Rs.551 crore and the PBIT is Rs. 12.3 crore, a little lower than the earlier quarter owing to a drop in revenue.

The next slide is on system integration and solutions. As mentioned earlier, we have a order book of about Rs. 816 crore and the build phase is coming to its end with orders of sub-Rs. 100 crore level left to be executed. The rest of the order book relates to managed services amounting to about Rs. 270 crore and supports services, a kind of an annuity support service which is about Rs. 455 crore. We are largely on track as far as our execution goes. However, as SI business is milestone-based and has varying project mix quarter by quarter, the number varies from quarter to quarter.

Slide number 12 talks about the numbers of system integration and solutions. While revenue amounted to Rs. 43 crore, PBIT loss was Rs. 13.4 crore which has been in line with the revenue.

Premkumar Seshadri:

You may now open up the audience for question-and-answers (Q&A). Thank you.

Moderator:

Thank you. With this, we will open the floor for Q&A interactive session. Participants, if you wish to ask a question, you may please press “0” and then “1” on your telephone keypad and wait for your like to be un-muted. I’ll repeat. To ask a question, you may please press “0” and then “1”.

First question of the day we have from Mr. Ritesh Kularia. Your line is un-muted. Please go ahead and ask a question.

Ritesh Kularia:

Thanks for the opportunity. Sir, between June and September quarter, the stake has been reduced from 58% to 50% by the promoter and now there is a right issue announcement. Is there any disconnect? Also, assuming

that the rights issue gets undersubscribed from the non-promoter, would the promoter subscribe to the remaining part?

Kapil Kapur:

I think it is not correct. I think there has just been a reclassification of other members who are promoters. So the promoter group remains in terms of its holding; as for any unsubscribed portion to the extent of what the promoter can subscribe, there is a commitment from the promoter to subscribe.

Ritesh Kularia:

What are the objectives of the Rs. 499-crore rights issue?

Kapil Kapur:

Our aim is to use 80% of what we get out of rights issue towards repayment of debt and retain 20% for general internal needs, especially, for the growing business of consumer distribution.

Ritesh Kularia

Okay. Thank you.

Moderator:

Thanks for your question. Once again, participants, to ask a question, you may please press “0” and then “1”. I’ll repeat. If you have any question, you may please press “0” and then “1”.

Moderator:

Yes. We have a question from Mr. Parimal. Mr. Parimal, your line is un-muted.

Parimal:

Sir, what is the debt on the balance sheet as of 31 September?

Premkumar Seshadri:

Net debt is Rs. 1050 crore and gross is about Rs. 1300 crore.

Parimal:

What is the receivable from the SI business, as of now, for the last one year?

Kapil Kapur:

The total receivables in the SI is about Rs. 500 crore.

Parimal:

From last one year?

Kapil Kapur:

No, SI has a milestone-based billing process. So, one keeps billing as the milestone is achieved and gets paid. The receivable, as of now is about Rs. 500 crore.

- Parimal:** Okay. Of the Rs. 800 crore that you have in the order book, how much can be executed in a year?
- Premkumar Seshadri:** It's again milestone-based. The build phase amount is Rs. 89 crore. Parallely, there is a managed phase and an ongoing annuity support phase some of which will trigger off at the end of the build phase and some have already started.
- Parimal:** You have given a timeline in terms of receivables in SI business. Do you think it is possible to attain?
- Premkumar Seshadri:** Our expectations have been on track in terms of our internal plans and cash flow.
- Parimal:** What will be the net debt post the rights on the balance sheet?
- Kapil Kapur:** As we have stated, 80% of the proceeds will go towards repayment of debt. Hence, as per calculation, about Rs. 400 odd crore would go into repayment of debt which currently is at Rs. 1300 crore.
- Parimal:** Okay.
- Premkumar Seshadri:** We are talking about the rights perspective. There is an ongoing operation where cash requirement and cash inflow would happen simultaneously. This is what we highly expect.
- Parimal:** Any further write-off in the business as of now or are we going to have surprises down the line?
- Premkumar Seshadri:** I think the goodwill write-off that you see is a non-cash one. So I think we have done what we saw was relevant at this quarter.
- Parimal:** Okay, sir. Thank you.
- Premkumar Seshadri:** Thank you.
- Moderator:** Thanks for your question. At this time, there are no further questions from the participants. So, I would like to now hand over the floor back to Mr. Premkumar for the final remarks. Thank you, and over to you, Sir.

Premkumar Seshadri: Thank you very much, Harpreet. Thanks, everybody, for joining in. In case you have any questions, you could write to Sumeet.ahluwalia@hcl.com. Also, the details would be available on our website right away. Thank you very much.

Moderator: Thank you, Sir, for addressing the session. Thank you, participants, for joining in. That does conclude our conference call for today. You may all disconnect now. Thank you and have a pleasant day.