



“Mastek Limited Q2 FY20 Earnings Conference Call”
October 17, 2019



MANAGEMENT: MR. JOHN OWEN – GROUP CEO, MASTEK
MR. ABHISHEK SINGH – GROUP CFO, MASTEK
LIMITED

MODERATOR: MS. ASHA GUPTA, CHRISTENSEN IR

Moderator: Good day, ladies and gentlemen. And a very warm welcome to the Q2 FY20 Earnings Conference Call of Mastek Limited. As a remainder, all participant lines will be in a 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 Ms. Asha Gupta from Christensen IR. Thank you and over to you, ma'am.

Asha Gupta: Thank you, Ali. Good afternoon to all of you and thanks for joining Q2 FY20 Results of Mastek. The results and presentation have already been mailed to you and you can view that in our website - www.mastek.com.

To take us through the results today and to answer your questions, we have the Top Management of Mastek, represented by Mr. John Owen – Group CEO and Mr. Abhishek Singh – Group CFO. Mr. John will start the call with brief overview of the quarter gone past and which will be followed by Mr. Abhishek who will be going into detailed financials. We will then take the Q&A session.

I would like to remind you that everything that is said on this call that reflects any outlook for the future or which can be construed as forward-looking statements must be viewed in conjunction with the risks and uncertainties that we face. This risk and uncertainties are included but not limited to what we have mentioned in the prospectus filed with SEBI and subsequent annual report that you can find it in our website.

With that said, I would now like to hand over the call to Mr. John. Over to you, sir.

John Owen: Thank you, Asha. Thank you and welcome to Mastek's earnings calls for Q2 fiscal 2020. Once again, it's a real pleasure to review our results for the quarter and share how our business continues to evolve in our third year of Vision 2020.

I think the digital world is different. And given the last 20 minutes, I think we can all see and appreciate the sensitivity Mastek's had to the UK economy and Brexit in particular. So, the fact that a deal has now been established between the UK and Europe is encouraging. And I think everything there's confidence now returning to the market.

So, what I am about to say was basically prepared about an hour ago, and we will have to change some of the context. I think a good way to summarize the quarter is being that we have worked incredibly hard and done all the good work to essentially standstill. And it's rare that I am pleased with flat growth, but I think it's important to put some short-term and medium-term context behind our results. The results don't truly reflect the real strategic progress we have made addressing our structural cost base and building the target operating model for our next phase of growth. And I was going to say, once we move beyond the market challenges of Brexit, which

I am now more encouraged, we will start to see over the next few quarters an improving market and confidence coming back. And I think there's a tailwind, where we have been operating in a headwind of Brexit and a massive exposure to the U.K., with 70% of our revenue, I would like to think quickly that could move to a tailwind with foreign exchange improvements, confidence in the market and those projects that we have talked about, particularly in the public sector, instead of moving to the right, will now start to be executed as the body of work moves forward.

What I would say, though, irrespective of the deal or no deal, our results reflect the new stability we have built in the business at Mastek over the last few years. And it's worth noting that our earnings quality also factored in the annual pay hike in July and also has further scope to improve as we layer accretive revenue on top over the next two to three quarters.

Back in our fiscal 2019 Q3 earnings call in January, I said that a sign of a great team is the honesty in which it deals with disappointment and setbacks, and to be very candid, Q3 fiscal 2019 didn't measure up to the high standards and expectations we now have as Mastekers. At that time, I was talking about the context of our U.S. business performing. So, today I am really pleased to report an encouraging sign of our recovery under the leadership of Raman Sapra with a revenue growth of 1.4% in constant currency. I think bringing that consistency in honesty and transparency in today's quarter, I am encouraged by the Mastek team's performance. We have delivered a solid performance at a group level, despite the significant headwinds we did face in our core market, primarily driven by Brexit. While I acknowledge we have a geographic dependency, and those impacted our short term, once we have clarity, we have a deal, and we move forward, I am confident the fundamentals for our UK business remain extremely solid. And that's evidenced by our stability in our revenue stream and this revenue stream is primarily anchored by strong public sector accounts, which provide a stable platform to expand once the political certainty is resolved. And hopefully, with the announcement over the last 30 minutes, we move into a more positive territory.

Brexit has unfortunately evolved from a political crisis to a fully-fledged constitutional and economic crisis. And therefore, I have always accepted that the true value of Mastek's business has been discounted due to external factors, and it will only truly be reflected and rewarded once we have stability in the external market. That being said, I still maintain that our U.K. public sector business is the jewel in the Mastek crown and differentiates Mastek against any other Indian services competitor. This vertical provides revenue resilience, good profitability and an excellent platform to expand once we are through this current uncertainty.

As I said earlier, our U.S. business continues its recovery, which is intended to deliver accretive growth in 2020. Under the leadership of Raman and his team, we have expanded our market coverage through a new partnership agreement we signed last month with Commercetools. This partnership builds on our proven industry knowledge and credibility around digital commerce established in the U.S. retail space.

Our India domestic business is now starting to contribute with a notable win with a large domestic securities firm. The first for many years, so we are starting to perform in all our geographies and markets.

In our Q4 earnings call, I announced the appointment of Dennis Badman, who joined us as Chief Business Officer, with a mandate to redesign our operating model to make it more scalable, more agile and more responsive to demands of the digital market. We have made excellent progress in Q2, and now have a much better alignment between our cost structure and the more modest revenue platform that we were planning for fiscal 2020.

With our ability to now flex up quickly, we can pivot the company to accelerate our growth once we get the clarity on Brexit. And I think there will be a lot of people who will be enthusiastic about Brexit, but I still think it's going to go through the U.K. Parliament, it's going to go through the European Parliament. But I do think it's when you are getting to that stage where we as an organization can start to pivot and look back to those sorts of double-digit growth that we enjoyed for the first two years of our journey.

Strategically, this cost agility will become increasingly more important because where traditional IT and service companies compete on traditional economies of scale, I would suggest, we in the digital industry and Mastek in particular with 84% of our revenue coming from digitally, we compete on an economy of speed to the business outcome for our customers. And I think that makes us a lot more valuable of creating value for our customers and the economy as we move forward. The experience we have built upon our end-user experience and customer experience driven out of our retail business in the U.S. isn't just for the retail customers but is now fundamental for all customer engagements. This power shift from the back office to the user experience isn't just a passing trend, but it's now a fundamental success factor in all digital projects.

Historically, Mastek has sometimes been criticized for operational surprises impacting investor confidence. But I hope you now recognize that despite some operational challenges in the U.S. and some economic challenges in our core U.K. market, we now have robust controls, we have the business agility, we have a strong operating model, we have the financial capacity and the management talent to successfully navigate Mastek through these factors and many that will come, I am sure, in the future.

But I think we have been probably through the hardest one in our core market with Brexit. As we progress through the year, we will continue to course-correct as we navigate prevailing market conditions. However, our strategic goal remains constant, which is, and I reiterate to be a recognized leader in enterprise digital transformation. To that end, we did repurpose our SG&A investment from the U.K. private sector to the public sector where we were getting more traction, and we see that in a stronger pipeline, and we have seen some new wins in places like U.K. hydrographics. But we are also developing an encouraging pipeline of public sector accounts

that are actively exploring the benefits of offshoring with Mastek. These programs will come to market in 2020, and I think Mastek is uniquely positioned to develop that niche.

We also have a successful model of growing point projects into major accounts as evidenced over the past few years of Vision 2020 with a demonstrable track record with the National Health Service, the Home Office, and we have now added the MOD to this growing list, and we must secure more. Growth also necessitates the need to expand all our market coverage through strategic partnerships, such as the new deals we have signed with UI Path in the RPA automation area and Denodo in virtualization. And there are more partnerships in the pipeline. Although this sales motion is relatively nascent to Mastek, it is getting encouraging traction, and we have some early wins.

Again, further evidence that we are positioned for growth once the uncertainty is resolved is the appointment of Laura Cameron-Peck to the newly created role of Chief Growth Officer for the U.K. with a clear mandate to build on the foundations we have established. Laura joins us with a track record of delivering a step change in growth in the service industry for the likes of HP, CSC and EDS.

So, although the numbers remained flat, we have stability, we have retained our ability to protect our quality of earnings, and we are balancing our attention to invest in targeted growth with an operating platform that once we start to see growth, we will grow faster than the market in fiscal 2021, that is our plan. This optimism is also evidenced by another strong order booking performance in Q2, where our 12 month order backlog now stands at GBP 71.8 million in constant currency, which represents a 3.5% quarter-on-quarter growth.

I have always believed that building a high-performing Mastek is only achievable by attracting, retaining and developing a passionate, professional and dedicated team of Mastekeers. This is the team that delivers for our customers every day around the world. I personally want to thank them for dealing with the last few quarters and another solid performance. They have shown character, resilience and good humor and their energy and their belief system remains strong.

So, although Q1 and Q2 has rightly been dominated by correcting the short-term organic growth out of the U.K. and internally focusing our cost structure, please also don't forget that we entered the final phase of our Vision 2020 strategy, and this is our growth phase where we intend to accelerate our growth through a combination of strong organic contribution and complementary inorganic routes once we digested the changes we have made. On this initiative, we have also made good progress in preparation to monetize our Majesco shareholding, which remains on plan.

As investors, thank you for your continued support and enthusiasm for our business. You continue to challenge our thinking, and we do appreciate the interactions. I have always said, digital is different while legacy IT continues its race to the bottom to compete, we cannot and will not play that game. But at Mastek, we continue to quietly and successfully carve out our

own niche as a trusted digital delivery partner, a partner who delivers business impact to some of the world's most demanding customers and institutions.

What I would like now to do is hand over to Abhishek, who will take us through the financial breakdown, and then we can take some questions. Abhishek, over to you.

Abhishek Singh:

Thank you, John. Wishes to everyone joining on this call. Continuing with the practice of last quarter, I am going to share the highlights of our performance for the quarter and then focus on the Q&A section. There has been a deck that has been circulated ahead of this call, and that contains all the details of the performance for this quarter vis-à-vis last quarter and last year, as well as the H1 view.

So, getting back on to the financial highlights. The revenues, both in terms of total income as well as operating income remained flat quarter-on-quarter in constant currency terms. Though in rupee terms it was lower, and also in year-on-year terms it was down by 2.5% in constant currency terms and 5.2% in INR terms. However, if you were to break down this revenue, the revenue in U.S. has grown by 1.4% quarter-on-quarter in constant currency terms. We added four new logos in the geography. The revenue in U.K. got impacted by the timing of some of the deal closures as well as the revenue recognition that we had. So, it's down by 0.8% in constant currency terms quarter-on-quarter. We added four new logos in the U.K geography during the quarter. India revenue on a very, very small base grew significantly by almost 16% quarter-on-quarter and we added three new logos. It has started to come to party with some of the interesting customers, large customers entrusting us with reasonable-size deals as we build on this and in this geography.

In terms of revenue composition, Application Development and Digital Commerce service line grew significantly. This correlates with the growth in Financial services vertical that we have experienced during the quarter.

Coming on to the operating EBITDA parameter, it stood at 11.8% for the quarter, it's a degrowth of 150 basis points quarter-on-quarter and 40 basis point year-on-year. This degrowth has to be looked upon in the context of the wage hike and some of the exceptional activities that we had to drive during the quarter. So, wage hike as well as the headcount optimization and digital workforce buildup costed us possibly around 1.8% during the quarter. This was partly offset by the continued effort that we have made in terms of making an agile cost structure and a more variable cost structure, as well as efficiency gains that we have been driving in the core operational space.

PAT stood at Rs. 24.6 crores for the quarter as against Rs. 24.2 crores for last quarter, that's a modest gain of 1.7% quarter-on-quarter. However, it was down 1.9% on a year-on-year basis. Going by the lead indicators, our order backlog grew robustly, now it stands at Rs. 626.5 crores or GBP 71.8 million, which is a 4% growth in rupee terms quarter-on-quarter.

We acquired 11 new logos during the quarter and our trailing 12-month clientele now stands at 144. Cash balance continues to be a good story, it now stands at Rs. 265.5 crores and net of debt stands at Rs. 200 crores. This is in the context that we paid Rs. 12 crores in dividend and Rs. 1.2 crores in earn-outs for the U.S. acquisition of TAISTech.

Moving on from the financial parameters, just a couple of comments on the salient features for the quarter. It's very evident that the headwinds in our core geography, U.K., has had an impact on our quarterly growth momentum. However, we stand strong and steering the business to stability and building slowly but surely and all of these are reflected in our order backlog. In the geography, U.S. business has shown signs of stability. Now it's the second quarter in succession where it's not only grown, but it has kept its chin above the \$9 million a quarter that we have looked at. And all of this coupled with the buildup of the inorganic initiatives that we are working on, gives us the confidence that we will be able to add up the capability and the capacity to accelerate it as some of these headwinds stabilize.

EBITDA profile, as I mentioned, has had the impact of wage hike, but it also should be looked at in the context of the continued investment we have made in the leadership team. Starting with Dennis, as the Chief Business Officer, who came in on board in April, all the way to a Chief Revenue Officer for U.K. business, Laura Cameron-Peck, who came on board in September. So, our continued visibility and confidence in the business gives us the ability to invest in the business and some of these numbers have to be looked upon in that context. And the monetization process of Majesco as well as our real estate in Pune is following its course. So, we remain confident that coming quarters would reflect in the business performance.

With that, I will hand it over to the floor for question-and-answer session.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the questions-and-answer session. The first question is from the line of Romil Jain from Systematix Portfolio Management.

Romil Jain: Just had two questions. One is, this Brexit uncertainty has been there for quite some time, so we just wanted to get your sense that is there any pent-up demand which you expect over next few quarters because a lot of decision-making was held up because of the uncertainty? And secondly, if you can throw some light on the attrition? The attrition is actually above 24% this quarter. These are the two questions. Thanks.

John Owen: So, let me talk about Brexit, because you are right. Lots of deals have moved to the right, and there was a level of indecision. I think the way, and I am not too sure what the deal is, but a lot of the short-term impact of that, the government in particular, who were looking to reallocate resource to that scenario, that is their strategy. And so I think there will be some pent-up demand, but I think that will flow into probably the first quarter of 2020, but it will not be a bounce back of lots of projects being signed off. That being said, the U.K. government signed off that budget for what they call spending review 2019, that only got signed off in, I think it was the 6th of September. So, let's see how the deal flows through the European Parliament, how it flows

through the U.K. Parliament. But it will unlock that hesitancy that's been there. Will it unlock it this side of Christmas or beyond, I think it's probably more beyond given the ratification process. But if I look at the pipeline that we have got, it is looking encouraging. And as I say, it's also looking encouraging in a niche that I think lot of our competitors don't address and serve, which is offshoring. And they will only offshore with trusted partners, they have got an established relationship with. So, I do expect, I wouldn't say it will give you a bounce, but I do expect a more robust market over calendar 2020.

Going on to your point, your second point about attrition, I think if you look at our business, we have driven productivity gains consistently over the last few years. And I think a lot of that attrition now has come through one involuntary attrition. So, we are actually delaying the organization, we are getting more productive, and we are rightsizing certain elements to line up with the business. So, you are right, 24% in isolation is not a healthy position to be at, but I think we have been able to deliver better revenue with fewer people, which means a productivity gain. And we have reskilled our organization from legacy skills to digital skills, but I would expect that, particularly with a more robust pipeline and performance and that to come back down traditionally to our low attrition, which we have enjoyed at Mastek. So, hopefully that answers your two questions.

Romil Jain: So, where do you think we would normalize on attrition maybe next three, four quarters?

John Owen: I would say, over the three to four quarters. Yes.

Abhishek Singh: And my bet is around 15% to 18% annualized.

Moderator: Thank you. The next question is from the line of Princy Bhansali from Anand Rathi. Please go ahead.

Princy Bhansali: The first question is if the deal happens, so you highlighted like we can go back to the double-digit growth trajectory. So, when do you see that coming?

John Owen: I think we are talking next fiscal. As I said, it's not a bounce back, it's a climb back. But I think we have those anchor accounts and things like the NHS, in the Home Office, in the MOD. And we have got other projects in train that we have obviously got to go through the sales process with the customer. And we have a pipeline of offshoring projects that we are also putting through a process. I think it's fair to say governments tend to be a little bit slower in their reaction, but we have got to digest the news. I think it would be a little bit, I think with respect, we overcorrected on Brexit is going to kill everything. And I think we may overcorrect if we think it's going to suddenly bounce back. We are planning and we are budgeting, and we are operating on the principal that quarter-on-quarter we will climb back to that position.

Princy Bhansali: Okay. And in terms of your margins, you highlighted there have been some exceptional items like what all those can be?

- Abhishek Singh:** So, if you triangulate this one with the headcount that we have between the quarters, we have gone down by almost around 100 FTEs, and this is essentially to have the digital workforce for the pipeline that we have and the work that we are doing, the legacy skill sets that we are not necessarily in the play. So, as expenses around employee separation, expenses around moving stuff from within the geography into the shared services model, we have done few things within the quarter and this is an exceptional item which is not likely to repeat in coming quarters.
- Princy Bhansali:** Okay. So, this impact of 1.8% will not recur, and we can expect the margins to inch up by that quantum?
- Abhishek Singh:** It's only a part of that Princy. Another part of that is wage hike, which will be here, but that will get offset as the revenue grows.
- Princy Bhansali:** Okay. Is your headcount reduction exercise done with?
- John Owen:** It's ongoing. And I think a lot of that has been focused in the U.K. where, obviously, the cost of change is significantly higher because you've got longer contracts by tradition. So, I think it's ongoing, but it's within that affordability envelope that Abhishek discussed.
- Princy Bhansali:** Okay. And any outlook in terms of your next year growth and margins in light of the Brexit deal?
- John Owen:** I think it's too early to factor that in, given it was only announced about 35 minutes ago. But what I have always said is, I think we look it through the lens of, we are really confident in our business model, our customers, our delivery and those customers will grow. So, I do expect us to grow. I think at the moment to calibrate it and to give you or quantify, I think is probably would be misleading, not intentionally, but I think we could overreact to the enthusiasm. I think it's just going to settle down. But I am confident we have got a fundamentally strong business.
- Abhishek Singh:** Yes. I would like to add to that, everything that John said. If you look at it even amidst the gloom and doom of Brexit, our order backlog continues to be robust. And that tells you that something fundamentally is right about it. A lot of it is existing business or existing customers, reaffirming their fate in the business that they have given to us or expanding the business that they have given to us. So, even with that gloom and doom, everything at a fundamental level was solid. And as this gives way to post-Brexit scenario and acceleration is an obvious result of it, what would be the quantum of that, I think we are at least 90 days before we get a clear view of it or some idea of it for that matter.
- Princy Bhansali:** Okay. And two more small questions. Firstly, there is a decline in your active clients, any reason on that? And secondly, any light on the U.S. part of your business, what all efforts are you seeing there being done and what all positive things are happening over there?

John Owen: Okay. So, let me just deal with the customer base. We have always had a strong customer base, I think we said with the IndigoBlue acquisition, we took lots of small tactical engagements, consulting engagements, particularly around the third sector in the U.K. And they have been GBP 20,000, GBP 30,000, and they were more a consultative engagement. What we have been able to do is grow our base by basically focusing. So, yes, the land-and-expand strategy is right, but I think you look at our core customers that are generating repeat business, digital business, they are the people that are spending with us. But I think there will still be some churn as we focus more on that and less on these, what I will call tactical transactions. I will let Abhishek talk about the U.S. if that's okay?

Abhishek Singh: Yes. I think U.S. has been what we called as, our first call on that one was, is it stable? And after a couple of quarters of being where it is, gives us the level of confidence. The management team is in place and has made some structural changes and continues to carve out the market. We have invested and repurposed some of our S&M spend to get more market coverage to ensure that we are reaching out to the customers and help accelerate it. So, over next two quarters, the true test of the business will come across, but the fundamentals are in place.

John Owen: I still think the fundamentals are, we want to balance out our geography. Let's not get carried away with the enthusiasm of Brexit, because I think as an organization, we always said we wanted to balance out our revenue geographically. That strategic objective still remains. And I think the U.S. is one of those areas that we could and should be growing better and faster. So, I am optimistic, but before you grow, you've got to have a stable operating model. You've got to know your focus. I think extending our partnership model with people like Commercetools is exciting, but I think it's too early to take that to the bank.

Moderator: Thank you. The next question is from the line of Madhu Babu from Centrum Broking. Please go ahead

Madhu Babu: Sir, first half has been a bit muted. So, second half, do we see any acceleration on the group? And second, you talked about offshoring in some U.K. government contracts, where you will start getting that work next year. So, could you tell us more in detail about that?

John Owen: Thanks, Madhu. I think the second half, it's too early to give you the visibility of how it's going to respond. As I say, we were very quick to cut our cost structure to align our costs with our revenue, which was more modest than it had been in fiscal 2019. And I think that's been well modeled. As Abhishek said, over the next 90 days, let's see how the market responds, let's see where we are. So, it's too easy to react to some good news and overcorrect. I think at the moment, the planning assumptions, everyone's got, I think is solid. But I do expect that the market to basically go from a headwind to a tailwind.

Regarding some of the offshoring, I think we have closed two of the, what I will call, pilot projects. And so we will start to deliver some services for the U.K. public sector in Q3. I don't think it will be material in its revenue contribution. But if I look at, it's more like a campaign

over the next 12 months. But I think we see something like GBP 20 million worth of annualized opportunity being offshore. We would expect to take the majority of that. It will be competitive, but the first two or three pilots are being done with Mastek because we are seen as a proven and trusted delivery partner. What the government don't want to do is launch it in and then find that they get a bad experience and then they cut themselves off on the competency roads from doing offshoring into India because they get a bad delivery outcome. So, at the moment, I think they trust Mastek to do it. We have got to pilot it. We have got to prove it. We have got to demonstrate the value. But I think though the intent on both sides is to scale this significantly over the next 12 to 18, 24 months.

Madhu Babu:

And second, we have done a couple of senior hires over the last six months, I think most recently of the Chief Revenue Officer. So, would there be targeting incremental new departments in the U.K. government? And if at all, I mean what is the pipeline? Could you give us some view on which are the departments, which have been targeted?

John Owen:

Okay. No, I think you are right. One of the areas, that reflect our confidence is we are investing in a talented team who run large organizations, Laura's been revenue responsibility for GBP 0.5 billion in the U.K., Raman's been responsible for \$400 million, \$500 million in the U.S. Dennis Badman from a Chief Operating Officer, has been responsible for GBP 2 billion and 10,000 people. I will tell you, these people are not here to maintain the status quo of Mastek. They're here to lift Mastek to its true potential, which is a leader in digital transformation. That being said, we have got to earn the right of our customers and build that pipeline. So, at the moment, we do have two targets in train a bit like the NHS, the Home Office, we have secured the MOD. We have got two other departments that we are developing, but I think it's too early to bake that into the business plan at the moment. But I think when you have that level of talent, not only is it an investment, and we are putting our money where our merit is, but I think we can now attract the talent to lift the organization to where it should be. So, yes, we are confident internally, but it's too early to bake it into the numbers. if that's okay..

Moderator:

Thank you. The next question is from the line of Sarvesh Gupta from Maximal Capital. Please go ahead.

Sarvesh Gupta:

Congratulations, Sir, first of all, for a satisfactory performance irrespective of the headwinds. Now my first question is that one obvious case is the Brexit getting done, where you said that probably in a quarter or two, you will be able to give us the guidance for the things moving forward. But let's say, the deal doesn't go through and the status quo is maintained. In that case, is there some idea that you can give about the performance for the coming year?

John Owen:

I think that's a really good question because I think, to be candid, we had a deal before under Prime Minister May. So, I don't think we should all rush off and bank this, as I have said. What I will say is we have been fairly pragmatic in reducing our cost structure and bringing our costs in line with our revenue and our market. I think as Abhishek quite rightly said, the revenue we delivered in Q2, which was probably in the face of this headwinds because we did have not only

a political crisis, but we had a constitutional crisis, and we had an economic crisis. And if you look at it, up until about a week ago, technically, the U.K. was in recession. So, I fully respect why a lot of analysts have looked and said, U.K. in recession, Mastek has problems. I understand why you have made the connection.

We were probably more confident because we know, even in a recession, those customers and those projects, we do have revenue stickiness and resilience because we are creating value, which is driving cost out of the U.K. government, it's driving BI and analytics for our retail customers. We have got banking customers who rely on us because we have got some customer experience and user experience, and that's what they are competing that's why they are buying from Mastek. So, I think at the moment, we have probably got the modest plan that you've baked in, and we have talked about. It's probably our, what I say, inconclusive scenario of Brexit. I would expect Brexit clarity to give us an upside on that.

Notwithstanding, I think now we have got a team of Dennis, Raman and Laura, I also expect us to outperform the market because I do think we have a talented team and I think there are projects that can defy the macroeconomics, and I think this team is credible to deliver that. But at the moment, from a planning hypothesis, I would say, flat is where we are at, with continued indecision as we get stability and that decision translates into an executable decision. My expectation and our working hypothesis is the investments we have made, we will accelerate.

Sarvesh Gupta:

Understood. And second thing that I noticed was there is some reduction in the interim dividend, which has been paid in spite of having a lot of cash on the books. So, is there anything on the pipeline in terms of the inorganic acquisitions, anything which has moved forward in this quarter, which you want to talk about because that would explain why we want to have so much of cash in the balance sheet?

John Owen:

Well, I think we have always been transparent that we do want to both have organic and inorganic growth, and we have been very busy positioning ourselves for that. So, I think we have been building up the war chest of cash. And so there's a lot of work in progress. But when we pull the trigger on why, I think it's easy to look at that and say, why don't we do what we do with the cash now. Again, let's get Brexit because if we have got stability in our core market, it would make sense to accelerate because you've got a solid base. But yes, we have got about three or four scenarios that we are looking at the moment. But I think we are just trying to be prudent, as we would always be in our overall planning.

Sarvesh Gupta:

Understood. And this potential acquisition, would it be accretive to our EPS and return on capital numbers or how do you look at it?

Abhishek Singh:

So, depending upon which option we select. Yes, it will be accretive to the existing operating EBITDA threshold or for that matter, even for the last quarter, yes, it will be accretive.

John Owen: Can I just say, on M&A, we have got a very strict criteria of why. So, some we may buy for capacity, and it's good value for money. Others we may buy because it can accelerate our core business growth. And there are those two extremes and there's obviously things in between. But it's our ability to digest the acquisition. It's the ability for that acquisition to line up with our operating model. It's got to be good value for money. But at the end, inorganic and organic, it's got to drive the engine faster, quicker and more profitably.

Sarvesh Gupta: Understood. And my final question is that, are commentary on Majesco sale has remained the same since last quarter, so any update on that as to how quickly that can be done?

Abhishek Singh: Sure. So, you have to understand that we are in a highly regulated U.S. market where you have to go through a process, a 10% plus holding is not small for us, we just go and sell in retail where the volumes are not there. Long story short, it has to go through a book-building process. It has to go through a public process and that has its limitations. We came into the earnings season and the feedback from the market or the book runners was that you are better off picking up after the results are announced. So, we had to pause on that process. But two things I want to clarify, to you and to all of our participants who are very keenly following this event is, it will be monetized, and we are following the process and the process is a little bit onerous, but it is in motion.

Moderator: Thank you. The next question is from the line of Nirmal Bari from Sameeksha Capital. Please go ahead.

Nirmal Bari: My first question is, so in the last quarter we had some one-off in the government revenue came down from Rs. 110 crores in Q4 to Rs. 99 crores in the previous quarter because there was some project, which was delayed. And our understanding was that now that the project was there, the revenue should return to their normal levels. But now this quarter, again, there is a minor drop in revenue from the U.K. government sector. So, what was responsible for this drop? And going forward, for the next two quarters because Brexit is going to take some time to resolve, should we expect a similar run rate for the U.K. government sector? And I also want a clarification on what was the impact of employee separation in absolute terms? What was the amount that we paid for employee separation, which was onetime, which won't be repeated in next quarter?

Abhishek Singh: Right. So, Nirmal, the last question is the first I would answer. And the impact is roughly around 50 bps that we don't expect to continue unless we may do something of similar nature, which is not in the pipeline. So, that's on that.

As far as the government revenues quarter-on-quarter or for that matter, the overall trajectory is concerned. There are always puts and takes, as John mentioned in his opening comment, the Ministry of Defense, the whole strategy of landing and expanding the government contracts or government departments. The plus or the highlight of the quarter and for this financial year would be the expansion that we are experiencing in Ministry of Defense as a customer. And this is on the backdrop of Home Office and two of the decision-makers that we serve under in Home

Office department. And the other pivot is NHS, which is going through a significant focus on serving its population. If I can just give you some stats, they are busy hoarding the medicines and the essential supplies to service the U.K. population. So, long story short, NHS has had a slower ramp up, which is what has reflected in the numbers. But overall, the trajectory is solid, but the Q3 with its softness and holiday season would do something to it. And Q4, we bounce back stronger. That trajectory is going to be solid.

Nirmal Bari:

Okay. And in our 12-month order backlog of Rs. 626 crores, are there some orders which were slow moving primarily because of Brexit or for some other reasons that are there in stuck orders?

John Owen:

Yes. I mean, think again, we would be probably giving you the commentary based on what we have experienced in Q2, which is indecision, things being stalled, things being moved to the right and a lot of resource being focused, particularly on what-if scenarios. Now hopefully, we are all optimistic and those what-if scenarios go into right. We are going into firm planning and execution around scenario A or B or whatever the case may be. So, I think as I said, this isn't a bounce back. This is a climb back. But I think once we have got stability and clarity, we are incredibly well positioned to grow all our accounts until our new ones because in simple terms, the digital opportunities within government is going to grow. I think now we have removed the uncertainty. And I caveat that, and we can plan with some optimism. And the customer can plan with some optimism because quite firmly, there is a skill shortage of delivering digital outcomes for the U.K. government. Let's not forget the U.K. private sector, where the confidence in discretionary spending should come back now there's clarity. I don't know what the deal looks like. Mr. Johnson didn't actually declare it when I phoned him up about 20 minutes ago. But obviously, we have now got some optimism. And hopefully, we can follow that through to clarity.

Moderator:

Thank you. The next question is from the line of Parag Bharamda, an individual investor. Please go ahead.

Parag Bharamda:

Can you elaborate on your capital allocation strategy as what is your long term goal, not necessarily long term, medium to long term. Around how much you want to retain and how much you want to pass, although you agree with that? And also, you have so much cash on the balance sheet, monetization is coming up, you have real estate coming up for sale. In spite of that, why you thought a need of reducing the dividend by Rs. 0.5?

Abhishek Singh:

Thanks for your question. I think we will put it in perspective and then the perspective here being that while for the size of the company, it looks to be a large amount of cash. We have always said that this cash and all the noncore assets have to be bought back into the business because growth is essentially what drives the organization and builds it for the overall shareholders' return perspective. So, this cash and the noncore assets are clearly allocated for us to bring it back into the business to grow the size of the business, which is right around Rs. 1,000 crores as a pivot right now. And the ambition is to double it over next 2.5 to 3 years. So, that's where we will need the capital to drive both organic as well as inorganic initiatives.

- Parag Bharamda:** Okay. Yes, and the second one is Majesco, are you trying to sell this through a secondary route or are you planning to place it through by buyers whenever it happens?
- Abhishek Singh:** So, in U.S., the process is called secondary offering when a publicly listed company, this big of a block comes up, it's got a secondary offering process, and it has to follow certain route. One of it is you could go retail and look for interested parties. We are a broker and do an off-market deal, or the other one is to run a book-building process, or the third one is that you find a strategic investor and offload this kind of block. So, all options are on the table as we have evaluated, even realized that getting into the market and going through what is called as secondary offering process could be more feasible and more viable to get it done.
- Moderator:** Thank you. The next question is from the line of Keshav Garg from Counter Cyclical Investments. Please go ahead.
- Keshav Garg:** Sir, according today's closing price, the company's market cap is Rs. 792 crores. And company has around Rs. 500 crores of cash and cash equivalents. So, our Enterprise value is less than Rs. 300 crores. And on that, we are doing around Rs. 130 crores of EBITDA. So, which means that company is barely trading at 2.2x EV to EBITDA. And then you are saying that you are expecting organic growth also. So, in that case in a growing business, if it is trading at 2.2x EV EBITDA and yet you don't see value in purchasing back your own shares through a share buyback and you want to go and acquire some other company. And I am sure it's unlikely that you will find an acquisition target at 2.2x EV/EBITDA. If you are going to find, then great, go ahead. But otherwise, I mean share buyback is a logical thing, what you have to say on this?
- Abhishek Singh:** Share buyback is a logical thing when you have no avenues to deploy your capital and building the business, running the business and growing the business has got a little bit more to do with just the financial metrics and analytics that you shared. And I completely respect that we are aware of it. We do debate this one internally as well. And the current EV/EBITDA, it has never been phenomenally high for the organization. But that said, there is an expectation, and there is a clear path for us to grow the organization. And on share prices, while you look at it, 10 minutes before the close was different. And at the time of the close was completely different when the Brexit announcement or the news flash came through. So, these phenomena's do not determine or fundamentally change the direction of business or the strategy that you pursue. And the strategy is very clear that we operate in twin markets of U.K. and U.S., where we have tremendous headroom for growth. Our capability is well respected and established. And if we were to accelerate that, then that would generate a far better shareholders' return on a sustainable basis for a period of time than just returning the capital back to the shareholders in the form of share buybacks.
- Keshav Garg:** Okay. And also, sir for the remaining second half of this financial year, are we going to maintain the same trend around and for this FY20, around Rs. 1,000 crores. Basically, year-on-year flat top line and bottom line, by and large?

Abhishek Singh: While we do not guide on those lines, I do want to say that the lead indicators of order backlog as well as the pipeline that we see gives us the confidence that we will be able to build on that.

Moderator: Thank you. The next question is from the line of Amit Doshi from Care Portfolio Management. Please go ahead.

Amit Doshi: With respect to this current order book, what portion of it you mentioned in your opening remarks that some part of it is maybe because stuck up or is not been accelerated owing to this Brexit things, what portion of that would be in that segment? And apart from that, on the government, apart from that, on the U.K. private side, what is the position? And how do we see that because government, as you said, might take some more time in order pipeline etc. will take more time. But on the private side, if you can put some comment on that?

John Owen: Okay. I think in Q1, where we have the uncertainty, we move very quickly to protect our earnings. So, that was our number one objective. And I think the team has done a fantastic job protecting earnings in Q1, Q2 and that's got to be our sort of direction of travel for the full year. Regarding our growth in our order book, we moved, we repurposed our SG&A away from the private sector because that was the one that was hit immediately on the pipeline. It just eroded, and we moved it into the public to drive that pipeline.

To answer your question, once we get clarity on the market, the exit, we do expect to grow in the public sector and the private sector. I think they will both recover. What we are saying is I think we can make quicker returns in the public sector because we put the sales investment in upfront. We have also made the appointment of Laura, and we are building a team and the alliances. So, we are extending our market reach through that. But I do expect our loyal customers in the private sector to return with some discretionary investment once their confidence about what the deal looks like for their business returns. So, yes, there's many variables, I think it goes back to Abhishek's direction and the direction we have always had it at Mastek is we are cautious, we are prudent, and it goes back to where do we allocate the cash. The key message from Mastek is it's stable, it's got loyal customers, it generates revenue, it can protect the quality of earnings, but we are here to grow in the digital economy, not standstill.

Amit Doshi: Okay. And on the U.S. side, now that it's been few quarters that we have already stabilized operations. When do you think that growth is likely to kick in the U.S. part of it?

Abhishek Singh: So, I think that the real meaningful growth or the first signs of the growth came in Q1 on the backdrop of the prior couple of quarters or possibly a much lower revenue base. Q1 was the first one and it got tested and validated in the Q2 revenues. So, we believe this should be the norm on which we will build our sales team further and increase our outreach, which can help accelerate over the coming years. But the demand as well as the requirement for such services in the market is huge. As you know, the retailers continue to be under continuous pressure. Till four quarters or three quarters back, we used to be one-trick pony just working on the Oracle Cloud Commerce or Oracle stack of digital commerce platforms. Today, we have diversified,

and we have got Commercetools as one of the partnerships. We developed capability on Salesforce platforms. So, we are extending our reach to basically address the requirements of the customer and the requirement for which is phenomenal, given the retail way in which U.S. exists.

John Owen: So, I think to build on that, we are extending our addressable market, both with Commercetools, with Salesforce, with UI path, with Denodo, we are basically selling work. We are also looking at how do we extend our capacity in that region because, obviously, I think we have always said, you work with a direct model, and then you basically offshore and it's that mixed delivery model, which gets the real benefit and the engineering benefit of working with Mastek. So, we are looking at all those scenarios, but the U.S. now we have got stability, we can plan with optimism, both in organic and an inorganic play.

Amit Doshi: So, any senior management that has been currently, in past or a couple of quarters been recruited, anything on the U.S. side or all on the U.K. side only?

John Owen: I think it was in June. So, that would have been in our earnings call in Q1, we announced the appointment of Raman Sapra and Raman comes from Wipro and Dell Services. This is a gentleman and an executive that's very comfortable doing \$500 million, \$600 million, \$700 million business. So, yes, we have the management talent, capacity and motivation in the region, and he's based in Dallas, which is our headquarters. All the other appointments have been global appointments. So, Dennis Badman coming in also has a global mandate to help deliver a consistent, high quality, robust delivery model, and that's what we are taking to the U.S. So, yes, the U.S. has the talent to execute the plans as does the U.K. as we do in India at a group level.

Amit Doshi: Okay. And with this sign of relief of Brexit, I am sure you have lot of more work to do in the coming quarters. All the very best. Thank you.

Moderator: Thank you. The next question is from the line of Akshay Ramnani from HDFC Securities. Please go ahead.

Akshay Ramnani: So, in your opening remarks, you mentioned that the spending review has gone past, I believe even this was acting as an overhang on a government business.

John Owen: Yes.

Akshay Ramnani: Can you just throw some light on what impact this event would have on our government business?

John Owen: I can't quantify it at the moment because I am reacting as you are to the news. And I hope it flows through. But I think what it will do, it will remove that uncertainty. People have budgets, they have got spend. And it's how they budget. I mean it's all about having the budget, but you still going to go through a procurement process. So, I would say there's going to be a sort of

from start to finish, this probably will flow through because they only have so much capacity to let contracts as well. But at least, we have removed the block. And how quickly the pipeline is opened up and what the capacity is, it's hard to judge. But I think that's what we will get when we talk to our customers over the next sort of 30 day. Day two, we will get a flow of how do they want to take this body of work to market.

Akshay Ramnani: And the second one was on the fixed price. So, fixed price has been falling for the past two quarters. Can you please explain what exactly is happening there?

Abhishek Singh: So, fixed price is a phenomenon, you have to understand is actually driven by the businesses from private sector, which had remained flattish to weak. In public sector, though government has an overall budget, but the default way of contracting is T&M. So, that's kind of causing the skew.

Akshay Ramnani: Okay. So, public sector revenues are predominantly T&M?

Abhishek Singh: That's the way government contracts, if they have a GBP2 million remit the billing or the contracting model will still come down. Fewer day rates for the roles, though the overall spend would be limited to a fixed price.

Moderator: Thank you. The next question is from the line of Bhavin Shah from Sameeksha Capital. Please go ahead.

Bhavin Shah: Actually, I go back to the question that was raised about the acquisition. I would like to claim that based on my observation that most of the acquisitions don't work, they don't generate value in net present value terms. And I think our experience so far with the acquisition in U.S., I guess the verdict is still out if we will be able to make it NPV positive, net present value positive. And today, as I see valuations in the tech world are all-time high. So, I mean I hope you don't end up buying something, which you will not be able to generate positive and net present value from. And I said certainly go by that, investors who have been patient with the company for some time now and are sitting on losses, you give them some benefit by doing a meaningful buyback. I mean I think I am happy to hear quantitative counterargument to my question. But it's very difficult to generate value from acquisition.

Abhishek Singh: So, Bhavin, thank you for your counsel, and we take that in the right spirit. The simple fact that, yes, if you don't do acquisitions just for the sake of it. You don't do acquisitions to grow out of your organic challenges. You do acquisition to complement your existing skill, skill gaps or to create some capacity that may be needed to accelerate the growth. We continue to evaluate it and if we do not find the right fit for the right price point, then we would not spend our investors' money and that's the only assurance we can make here.

John Owen: But I think your observation is correct. And I think it's well founded. Let me assure you, we acknowledge we can't buy our way to success. We have got to operate our way to success.

However, we can accelerate our way once our operating model is stable. Our market confidence is there, the pipeline is there. It would be a logical thing to use our cash to accelerate the capital growth of our company, and that is the lens that we will evaluate, and we do have a strict evaluation criteria, why we would acquire, how we would integrate, how we would extract value. And if it doesn't drive economic value, we won't be doing it.

Bhavin Shah: What is your definition of economic value, please?

Abhishek Singh: So, it has to be the right EBITDA multiple, it has to have the growth opportunity for that matter. I mean either you do it for capability or capacity. Capacity acquisitions where we can enhance the EBITDA from where we would have bought the asset over. Capability is where it should be able to accelerate our business i.e. bring in those skill sets that we know we can do a cross-sell and then build on.

Bhavin Shah: Those are definitely very good criteria, but I don't hear you measuring yourself up to some sort of a quantitative figure of net present value, generating a positive net present value. And I am sure you all understand what I am talking about.

Abhishek Singh: Absolutely, Bhavin, and if there is a need for us to connect offline, happy to do that for us to outline some of it. We are sensitive and aware of all the definitions that are needed before we do the capital allocation.

Moderator: Thank you. As there are no further questions, I now hand the conference over to the management for their closing comments.

John Owen: Okay. Thank you very much. I think as we started this in the last hour, you've seen the sensitivity of external factors do to confidence in Mastek because of our exposure to the U.K., and I would argue we were disproportionately damaged because we have such a U.K. exposure. I would say that, that headwind will suddenly become a tailwind. What I would say is there is an element of caution. We have got to go through this and make sure that we understand the market that we are now working in. But I will say over the last three years, what this team has done in this company is delivered consistency. It's delivered revenue and profitability. We are in a good market. Digital is growing. I know we have got some uncertainties. Our job is to navigate those and exploit the opportunities the market will deliver because the market does need a company like Mastek to come and deliver reliable, quality digital outcomes to drive their business. I think we have the top tier customers, both in the U.S. and the U.K., and these are solid customers, they are demanding customers, and that makes Mastek a better company.

We have the financial strength to execute and as Abhishek rightly said, how we allocate our capital between working capital and where we create our value is something that we look at every day. But I think most importantly, we have the talent, the ambition and the motivation to execute. And as I say, when you appoint Chief Growth Officer, let me assure you, they are not here to come in and maintain the status quo. So, it is about how we, as a team, we have a very



*Mastek Limited
October 17, 2019*

talented team, how we lift the organization and break through that glass ceiling that Mastek's had traditionally. I am confident the market needs Mastek, I am confident Mastek can execute. It's now about assessing which markets we are going after. So, I am going into Q3 with some optimism. It's not going to bounce back. But likewise, we are not going to fall off. So, thank you for your support. Hopefully, we do ratify the Brexit, and we will move forward with some clarity. But I think, hopefully, Mastek will enjoy the true valuation that you have all discussed, and it will be rewarded in our share price. But thank you. Appreciate it.

Moderator:

Thank you very much. Ladies and gentlemen, on behalf of Mastek Limited, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.