Q1 FY20 Earnings Conference Call
July 18, 2019, 15:00 hrs IST

Moderator: Good day, ladies and gentlemen, and a very warm welcome to the Tata Elxsi Q1 FY'20 Earnings Conference Call. As a reminder, all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. I now hand the conference over to Mr. Vaidyanathan. Thank you and over to, you sir.

Vaidyanathan: Thank you. This is Vaidyanathan welcoming you all to the Q1 results investors' conference call.

We have with us Mr. Madhukar Dev – Managing Director and CEO; Mr. Manoj Raghavan – EVP, EPD, and Mr. Nitin Pai – SVP, Marketing.

Please restrict to one question to give opportunities to others. I will now hand over to Mr. Madhukar Dev to take it over.

Madhukar Dev: Thanks very much and welcome to this call. First of all, I will take a couple of minutes introducing Manoj Raghavan who all of you have known to be the Head of our EPD Division. Manoj is going to take over from me in early October as the CEO and MD of Tata Elxsi. He has been with us for 20+ years and has held a number of different roles. His first assignment was to build our business in Japan, and under his watch, our Japanese business grew to be in excess of 35% of our overall revenue. He then came back and handled all of East Asia, and that is when we started doing business in Asia outside of Japan. The

US market has been a challenge for us for a long time, and Manoj moved to the US and spent about three years and grew the business there very significantly. Now he is all set to take over the company, and he is very familiar with our strengths, challenges in the markets and our people. So, just like Manoj to say 'Hello' to all of you and then I will come back.

Manoj Raghavan: Hello, everybody. This is Manoj here. Thanks, Madhukar for the warm words.

Madhukar Dev: Thank you. Now, let us move to the quarter that ended on June 30th. It was indeed a tough quarter, but at the same time the numbers would probably exaggerate negatives a bit, there were a number of positives in the quarter and number of things went according to plan, of course, quite a few did not and I will first mention some of the significant positives for us in the quarter. In terms of new order booking, Q1 number was significantly higher than the previous quarter, and that really points in a positive direction for the time to come. Two of our business units that is the Broadcast and Communications as well as the Medical business unit both clocked a very high growth as compared to the previous quarter, higher than they have ever grown in two consecutive quarters. So, these were certainly some of the key positives for us. Yes, there were a lot of challenges and trying to compensate for the loss of business which was somewhat abrupt from Jaguar Land Rover. Though we did know that there would be ramp-downs, but the extent of ramp-down was a bit surprising, and the pace at which it happened was such that there was not too much that one could do. As an organization, they went through a period of great uncertainty and therefore, one has to hang in there and see how best to make our presence continue there. And happily having got on to the preferred supplier list of Jaguar Land Rover, we think that as soon as they start giving out work in a significant way, we should be able to make up for the setback that we have suffered. If you look at even the numbers that we have reported, there was a substantial amount of IP and one-off revenues in the previous quarter, which we were not able to repeat in the current quarter. And part of the reason why we were not able to replicate is the general slowdown in the pace of decision-making. While we have several active cases both for the IPs and other new engagements, which we were hoping to close and revenue in the quarter, some of them are still pending. We did have a number of significant new wins, including getting into a new country in Europe and the funnel that we have overall looks quite healthy. The alarming thing has been the pace at which the funnel is converting to revenue, and we hope that this trend will change and we will soon be back to our normal business growth.

With this, I would open it to questions which between, Manoj, Nitin and I be able to answer.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Vimal Gohil from Union Mutual Fund. Please go ahead.

Vimal Gohil: My first question would be if you could give me what was the proportion of revenues that came from JLR, total automotive business and from comms this particular quarter and what was the last quarter and the quarter last year?

Madhukar Dev: I will give you the figures that I have. The JLR business was about 21% last quarter, which is now down to about 14.5% to 15%. The entire transport business was about 60%, is now down to 50%, 51%. Communication and broadcast, we had merged a few quarters ago.

Vimal Gohil: Sir, if I'm not wrong, JLR was at about 18% in Q4 if you could reconfirm that number?

Madhukar Dev: No, for EPD, it was 18%, but totally for the company was 21-22%.

Vimal Gohil: Sir, how much was the one-off revenue in the last quarter that you spoke about?

Madhukar Dev: It would be close to about Rs.25-30 crores.

Vimal Gohil: Which was not there at all in this quarter?

Madhukar Dev: It came down to hardly Rs.2 crores.

Vimal Gohil: Have we gone ahead with our usual salary hike cycles in this quarter?

Madhukar Dev: It will happen now in the current quarter.

Vimal Gohil: This is not reflected as yet?

Madhukar Dev: No.

Vimal Gohil: Okay. And then what would you then attribute the steep decline in margins to apart from the revenue decline?

Madhukar Dev: It is just the revenue decline. If you see our expenses, none of them is out of control, and they are all the way we expected them to be: the revenue that dropped and that straight gone from the bottom line.

Vimal Gohil: So, the salary hike is expected in the next quarter?

Madhukar Dev: In the current quarter, yes.

Vimal Gohil: There is a severe slowdown in the non-JLR business on the automotive side. When do you expect this to turn around because when we had last spoken in the call, we had alluded a significant optimism on the non-JLR business on the automotive piece, so what went wrong here in this particular quarter?

Madhukar Dev: It is not as if the business has been lost or programs have been called off. It is just the speed at which they were deciding earlier. It was very, very different from the speed at which these cases are processing now. And it is understandable when their sales are affected, the pressure on spending money and doing something new becomes much less. As soon as their business picks up, I expect the pressure on engineering will pick up too.

Moderator: Thank you. The next question is from the line of Rohan Advant from Multi-Act. Please go ahead.

Rohan Advant: Sir, just a clarification on the JLR numbers. You said Q4 FY '19, they were 21% and Q1 FY '20 which is this quarter, it is 14% or 14.5%, is that right?

Madhukar Dev: Yes.

Rohan Advant: Can you tell me what JLR was in Q1 of FY '19?

Madhukar Dev: I do not have the number readily, but from my memory, I would say it was about 24%, 25% somewhere there.

Rohan Advant: Sir, all these numbers are as a percentage of total revenues?

Madhukar Dev: That is right.

Rohan Advant: In one of your earlier calls, you had mentioned that JLR is also offshoring or shifting its work from onshore to offshore which has a negative impact on revenues, of course, because billing rates are lower. So, is that what happened and is continuing to happen, or is it more than the business has more stopped than just being offshore?

Madhukar Dev: More stopped than conversion from onsite to offshore.

Rohan Advant: Sir, just on the global auto landscape, everyone is facing a slowdown, and R&D budgets are being curtailed. One of the implications of this could also be that they would outsource more, and companies like us could benefit from that trend. Is that even what you are seeing or is a possibility, or it is just that the business pie is getting smaller and smaller?

Madhukar Dev: You are right, logically, it makes sense to outsource more and save money, but what is affecting us adversely right now is the speed at which decisions are being taken. So, it is not as if the budgets are being cut very drastically outside of Jaguar Land Rover; it is more the speed at which - to give you an example, there was an engagement that we were hoping to start in April. We were selected in March. We were told that you would start within 30-days with a reasonably significant growth trajectory to follow. We are sitting in the middle of July. We have been selected. The paperwork is in place. We are yet to start work. So, it is these things that are affecting our revenue more than cuts in budgets or anything which would be much more bothersome and worrisome for the long-term future. These I think, are temporary blips and will get set right.

Rohan Advant: But the larger story of the R&D spends though the whole number is being reduced, the kind of things that are being spent on and Elxsi being a beneficiary of those spends, is that continuing or you are seeing even those spends which benefit us are reducing to?

Madhukar Dev: No, we are not seeing those spends getting cut.

Rohan Advant: Sir, on Broadcast, Communications, you said that the growth rates have been very high. Can you give us a number on growth rate?

Madhukar Dev: It was about 10% on a sequential quarter.

Rohan Advant: On the hiring side, we had about 6,000 employees end of March '19. So, what are your hiring plans for the year?

Madhukar Dev: At the moment, we have a plan to bring in fresh graduates over the next six months; they have been selected and are being put through some pre-joining orientation and training. They will be joining in phases - about 500 of them.

Rohan Advant: Lastly, on constant currency revenue growth rate if you could help me?

Madhukar Dev: Constant currency the number I have is excluding the one-offs which are almost flat between Q4 and the current one.

Rohan Advant: Which one-off are you referring to -- the IP revenue of Q4?

Madhukar Dev: Yes.

Rohan Advant: Sir, I have not understood because it is a 10% sequential drop, right, INR terms?

Madhukar Dev: Yes, we were doing IP revenues of between 3.5% to 5.5% every quarter last year, in the current quarter, it is just 1%, so that is IP. And associated with engagement, there are some one-offs bits of revenue, which are not spread throughout the engagement, which every time you get a new engagement, you have those one-off revenues. If there were not too many new starts, that revenue does not accrue in that quarter, and this is one peculiar quarter where we did not have too many new starts in the auto business.

Rohan Advant: So, there has been a significant currency impact also this quarter. Is that right?

Madhukar Dev: Yes, it is about 2% overall.

Moderator: Thank you. The next question is from the line of Soumitra Chatterjee from Spark Capital. Please go ahead.

Soumitra Chatterjee: My first question is the entire drop in JLR completely volume-led, or the incremental work that we are doing has come at lower pricing?

Madhukar Dev: No, there is no change in pricing.

Soumitra Chatterjee: It is entirely volume-led?

Madhukar Dev: Yes.

Soumitra Chatterjee: It is predominantly led by cut by JLR. Have you not lost wallet share within that account? I mean has the work shifted from Tata Elxsi to any other vendors, maybe Herman or KPIT, for that matter?

Madhukar Dev: No, none of our work has shifted anywhere, not to a supplier, nor a competitor, no.

Soumitra Chatterjee: My second question is, what happens to your guidance? Were you earlier expecting about 15% kind of growth in INR terms?

Madhukar Dev: I would like to correct you there. It is not guidance. We have always maintained that it is our internal aspiration. At the moment, we would like to stick to that aspiration.

Soumitra Chatterjee: So, your aspiration is still of 22-25% kind of margin. Are you still sticking with that for this particular fiscal?

Madhukar Dev: Yes.

Soumitra Chatterjee: Sir, one thing that you have mentioned about Rs. 30 crores kind of one-off revenue. So, your last quarter revenues were about Rs. 405 crores. Now if I were to calculate 21% of that, it becomes roughly JLR is contributing to Rs. 85 crores. If I were to look at this quarter revenue, which is just Rs. 362 crores and I do 15% on that, and it gives me about Rs.55 crores. So which means the entire one-off or SI work that was there last quarter, it was the JLR only to indicate Rs. 30 crores kind of a QoQ drop from JLR?

Madhukar Dev: No, it was not entirely from JLR, there was a lot of other declines that have happened, not the one-off declines, which have got compensated by new engagements from other customers. They are two different things -- the one-off revenues and decline in JLR partly offset by others. So, you do not see that entire decline in the overall number.

Soumitra Chatterjee: I agree that the ramp down has been steeper than you would have expected, but we have already come down to about Rs. 50 crores quarter revenue from JLR. From the next 12-months perspective, in your conversations with JLR, can it go below Rs. 50 crores of quarterly revenue run rate from JLR?

Madhukar Dev: In my conversations with JLR, I did not think it would come down to this current level either, and the discussions continue to be very encouraging and positive. We have to see how it plays out. I personally do not expect it to drop anymore.

Moderator: Thank you. The next question is from the line of Ritesh Rathod from Alchemy Capital. Please go ahead.

Ritesh Rathod: Sir, what is your view on the margins? You said JLR cut was more on volume-led and since you have not cut the employee cost and you have new employees, so going forward how should we see the margin trajectory?

Madhukar Dev: It will follow the revenue trajectory; it is as simple as that. If we are growing revenue at 10% QoQ, we will see margins also going up proportionately. The margins have declined not because of anything else. It is just that the cost base has remained the same, and the revenue has come down. So, we have to fix the revenue, and we will be back where we were.

Ritesh Rathod: So, we will have a wage hike, we will have fresher additions in coming quarters, so the cost base would keep moving upwards. So, as a percentage to revenue, margins will stay at 19% EBITDA margin, or it will improve on that percentage?

Madhukar Dev: We aspire to work towards improving it.

Ritesh Rathod: What would be that number for aspiration, 23%, 25%?

Madhukar Dev: Upwards of 20%.

Ritesh Rathod: Would we ever get back to 26% kind of margins because the mix has changed, within JLR the kind of work would get changed, a new business could come in, so would it be possible to get back to 26% margin in two, three-year scenario?

Madhukar Dev: I had mentioned this earlier in previous calls that 26% and 28% were really aberrations and we would be delighted if we maintain between 22% and 24% and I think that is the realistic number to expect. You may have an odd quarter where we will exceed 26%, but steady-state it has to be between 22% and 24%.

Ritesh Rathod: Just on this IP and hardware which were one-offs which we are seeing from last quarter base to this quarter, would we see IP and hardware revenue coming back in coming quarters?

Madhukar Dev: Certainly, we are quite confident that we will be able to bring it back to at least 2-3% of our revenue every quarter, and the other one-offs all depend on the number of new starts that we do in the quarter. So, as soon as that picks up, we should be back to the same number.

Ritesh Rathod: So, 2-3% is the IP revenue?

Madhukar Dev: Yes.

Ritesh Rathod: Other one-offs are the hardware revenue which you are thinking to...

Madhukar Dev: It is a starting cost, various elements.

Ritesh Rathod: Within automotive, the non-JLR portion, which is 35% of revenue, that client base, how indirectly they are dependent on JLR R&D spend?

Madhukar Dev: No, they have virtually no connection with the JLR R&D spend. These are either independent car makers or system and component suppliers to the car companies.

Ritesh Rathod: Sir, your take on the overall global R&D spends in the auto vertical since they are getting deferred, where do you see things getting stabilized and recovering on the total spend?

Madhukar Dev: My view and I welcome views from Manoj and Nitin also is that what we are seeing is a temporary blip. I have always believed that if you look at the car industry over the last 75-years, there has never been a 15-year period without some slowdowns, some setback, but overall, the industry has grown continuously. So, it is a temporary blip as far as I am concerned.

Moderator: Thank you. The next question is from the line of Harish Kavalkar, who is an individual investor. Please go ahead.

Harish Kavalkar: I have two questions: First of all, you are working with driverless cars in the automobile. But you have any plan for two-wheelers, which are coming in electric two-wheelers right now?

Madhukar Dev: Right now, we do not have any plans to get into the two-wheeler market.

Harish Kavalkar: Have you faced any competition from any competitor? If yes, in which business segment?

Madhukar Dev: We have competitors in every segment that we operate in. We win business because of the value that we deliver to our customers and very often customers who tried us before, trust us more than they believe anybody else that is why more than 92-93% of our revenues in any period come from our existing customers. So, we compete, we win, and we retain our customers.

Harish Kavalkar: I just asked this question because a lot of people talk about the business mode and competitive advantage. I want your take on that competitive advantage and mode?

Madhukar Dev: Yes, our competitive advantage is two-fold -- One is the brand that we carry, the Tata brand today all over the world stands for a number of values that most customers covet, not the least of them being that we are trustworthy and we will not do anything that we should not be doing. The other crucial strength comes from our technical competence. We believe we have some of the best technical workforces in the world working with us in the areas that we operate in. So, given these two, we end up winning business in a competitive situation.

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 on this Communications and the Medical Devices that we are looking at, you said at the beginning of your commentary that those two segments had seen good growth. So, if you can put a growth number to it? Secondly, in light of 60% of our business, which is automobile slowing down, are these two segments having sufficient pipeline or can they drag the automobile segment enough to have a 15% kind of growth this year or they are too small at present?

Madhukar Dev: I will answer the second part first. You are right, they are relatively small, and if the auto business does not pick up, it would be tough for these two businesses to compensate for the lack of growth in the auto. While overall, we have seen a slowdown in the auto business, it is still very significant, and we are fairly confident that we will be able to clock in reasonable growth there. In terms of growth in these individual businesses, the Broadcast and Communications combined had about 10% growth QoQ and the Medical business, about 35%, 40% growth.

Nirmal Bari: And what would be Medical business as a percentage of revenue at present?

Madhukar R Dev: Under 10%.

Nirmal Bari: On the automobile excluding JLR, what kind of conversations are we having over there? You mentioned that the decision-making process is slow?

Madhukar Dev: Yes, we are having very good encouraging conversations. Nobody is saying that we are in trouble, we are not going to do anything for a while, no negatives that we are seeing. It is just that the conversations are not translating into revenues as quickly as they were.

Nirmal Bari: And then are we looking at a bigger pipeline?

Madhukar Dev: Yes, exactly, you are right, we are looking at having a much bigger pipeline given the fact that the conversion is a bit slow.

Nirmal Bari: It has been about 2.5-3-years if I am not wrong since we got into the Medical Devices segment, and now it has started showing growth. So, are we looking at some other verticals that we would like to enter to further reduce our dependence on automobiles?

Madhukar Dev: Yes, Nitin Pai has been continually evaluating other verticals to get into and some of them we do on a trial basis to see the characteristics of that market, and we will certainly be entering into other verticals too in the next three, four quarters. It's a bit premature to talk about them. Once we have a little more clarity, we will certainly be happy to share with you.

Moderator: Thank you. The next question is from the line of Vivek Ganguli from Nine Rivers Capital. Please go ahead.

Vivek Ganguli: Sir, there are two broad trends that we are noticing. One is the general slowdown in the auto industry and the second is a consolidation of platforms or different companies starting to collaborate on various platforms and consolidation happening there like in the case, we have heard of JLR, BMW merging their EV platforms. So, the slowdown in the budgetary support or the decision-making process, is it coming because of the slowdown in the industry generally or because of these development consolidations that are happening and then they need to figure out who leads the process?

Nitin Pai: It is a fact that, yes, OEMs are looking at how they cannot necessarily burn cash all by themselves and lead to sub-optimal results but rather join hands with appropriate partners across the industry, and therefore pool R&D resources and talent as well as budgets, right, so this is a fact. But you have to look at it in the context of car production and what goes in as electronics. A large part of that is still supplied to them by suppliers, right? So, the whole platform game is being driven towards what the future would be, which is as we go electric, what components do OEMs need to own vis-à-vis what will come from suppliers. And to that extent, what part of that development should be done all by one-self versus being done jointly with other partners to increase chances of success. Equally, it allows you to share IPR, patents, and so on and so forth. So, in my view, at this time, yes, if you look at a little more longer-term future, one trend is OEMs will do more, they will take more control of software. So, that should not affect us anyway, because either you will get business from tier-1s, or you get business from OEMs. The consolidation of programs directly does not impact you because this is for the future. So, there would be a part of it, which also has to be outsourced ultimately, right?

Vivek Ganguli: But when we are talking of consolidation of programs, let us say JLR had one EV program and then BMW had another. So, each of them has one or two of these products. Now they suddenly decide that they merge and instead of six programs cumulatively have three programs, from which they have to decide which are the ones they want to pick and which will become the base on which both of them will manufacture or design their futuristic cars. Now the decision might shift that it has to be taken by BMW instead of JLR or one program you all might have been working on is no longer relevant going forward. So, is the cut that we are seeing coming from there? Of course, there is a budgetary constraint right now, but that also because we know this consolidation between many different companies. So, what it means is going forward, the budget itself will shrink or the R&D pie.

Nitin Pai: Let me put it simply; did any of our revenues that did not come through this quarter happen because of such consolidation and the impact of that consolidation? No. Having said that, you have to remember the context of these collaborations is for very advanced R&D; they are not for production programs going on today, it is for production programs that will come up three years, five years, ten years, hence. So, the understanding is that the collaboration that they are doing now may not be massive, but it should lead to much larger budgets and much larger work to be done. I am sorry, I am not able to illustrate it well enough, but the way I see there is an opportunity that is yet to unfold and develop. It is not a negative impact because we are all for advanced R&D programs. So, if you look at BMW and Mercedes collaborating for shared mobility that is for the future, it is not for today. If you look at JLR and BMW, it is for developing a joint EDU or Electronic Drive Unit. That is again for the future because they are not meant for cars that are going in right now.

Vivek Ganguli: So, your budget would mainly be from the cars which are already under production, and those being remodified, developed and so on. These are very little of the work that you will be doing would be from very futuristic programs?

Nitin Pai: That is correct. So, work that we do in design and so on, is very futuristic, for example, we would explore what would be the human-machine interface or UI or the UX 10-years down. There would be a particular portion of work that we do even today in terms of pure R&D from the electronic space, which is also for five, ten years. For example, everything that we are doing in autonomous is five plus years. It is not going to be anything before 2023, 2025 that you see driverless cars. So, some part of what we do is very-very forward-looking, but a large part of what we do is typically towards productizing into programs today.

Vivek Ganguli: So, the budgetary constraint that you will have seen in the case of JLR would mostly be for projects which are already online, and what is the further incremental improvement or incremental feature additions that are happening on existing product lines?

Nitin Pai: That is correct.

Moderator: Thank you. Next question is from the line of Srikanth Krishnan from Acacia Partners. Please go ahead.

Shrinath Krishnan: You shared an anecdote to where you mentioned that one of your programs got extended. So, are these discretionary programs, what quality of work is this, we do not want to know the OEM, but can you throw some light on the quality of work that you are supposed to do? Secondly, generally in the auto industry, we are seeing that there is 2-3 year visibility for the suppliers when they are going to get into newer models. Likewise, would you also have similar visibility, do you have the same order book with you?

Madhukar Dev: The thing that happened was a delay; it was not an extension of an existing project; it was a delay in commencement and the nature of work is contemporary technology. It is not a discretionary R&D which can be put off indefinitely. Thus, we are prepared for delays in, but whatever is part of contemporary programs, we usually expect that to move at a faster pace, and it was moving earlier. In terms of the visibility of two years, it is a bit hard to say. I hope what visible today is not for two years, but just for three months and everything changes in three months from now.

Srikanth Krishnan: Apart from JLR, who is your next biggest client? Secondly, my limited understanding was in the segment that you were participating, you are still a small fish, and the opportunity is pretty significant for you. So, in such a case, would it be fair to blame the industry because you have the capabilities? Also, the market is growing fast in terms of ADAS, or the end-market spend in the market is growing, so would it be fair to blame the end-market growth or the total auto industry decline that is happening at this point in time?

Madhukar R Dev: One is not trying to blame the external environment. It is a reality - the way the external environment prevailed 2-3 quarters ago was very different from what prevails today. It is for us to adapt to the change and make the most of it, and that is purely an internal thing, which is what we are all working to do, and that is what gives us the confidence that we can bounce back to our old-growth rates pretty quick.

Shrinath Krishnan: And the next biggest client apart from JLR in the automotive segment?

Manoj Raghavan: Tier-1 supplier from the US.

Moderator: Thank you. The question is from the line of Adit Shah from Reliance Securities. Please go ahead.

Adit Shah: There was a question earlier regarding you are entering some new verticals. So, I think in the last quarter you had also alluded to something in markets which are adjacent to that of automotive, like railways or aerospace, commercial vehicles, off-road vehicles. So, were these verticals you were referring to earlier in this call?

Madhukar Dev: No, we were talking about entirely new markets. The adjacencies are something that we have started work on already. We have some engagements, and they need to be nurtured and grown. When I was mentioning new verticals earlier in the call, they are entirely new areas which we are evaluating.

Adit Shah: Can you name any of those?

Madhukar Dev: Not yet, no.

Adit Shah: Can you give out what was the utilization and the onsite/offshore break-up?

Madhukar Dev: The utilization dropped to about 65%, and the offshore/onsite is about 56%/44%.

Moderator: Thank you. The next question is from the line of Amar Morya from AIFAccurate Advisors. Please go ahead.

Amar Morya: Sir, when you say that 15% growth is possible even after the first quarter of weaker performance. So, what gives you the confidence and if you can bifurcate that into how do you see that? This kind of growth would be driven by because still today, the bulk of the business is the auto business.

Madhukar Dev: Yes, we expect things to pick up, just need to have a larger funnel in auto and a lot more ongoing cases to have new starts in every quarter. So, it is not as if auto is likely to shut down or anything.

Amar Morya: No, I am not saying the shutdown, but like…?

Madhukar Dev: I expect the growth to come from auto.

Amar Morya: Sir, when you have this kind of visibility, usually this kind of weakness was also expected by you?

Madhukar Dev: Weakness was certainly expected, in fact, in a number of our previous interactions, we did mention, but the extent of weakness was not anticipated to be as much as we saw and as quickly as it happened.

Amar Morya: Sir, what gives you the confidence that these things will reverse and we will be able to reach to the number which we are talking about? We already got some confidence from the client-side.

Madhukar Dev: I have mentioned earlier in the call that the funnel that we have is fairly healthy and it is significantly better than what we had a few quarters ago. We are working towards expanding that even further given the fact that decision-making is slow. So, that is what provides us with the confidence that we will be able to get back to the growth rates that we have.

Amar Morya: You expect the turnaround to happen in Q2 itself?

Madhukar Dev: It is little difficult to say whether it will happen this month, next month or the next quarter, but the trend is being reversed already.

Moderator: Thank you. The next question is from the line of Mayank Babla from Dalal and Broacha. Please go ahead.

Mayank Babla: In the automotive space, how many customers do we have in the non-JLR space for the last three years? if you could give us in the automotive space.

Nitin Pai: Close to 50 now.

Mayank Babla: Over the last three years, what is the trend?

Nitin Pai: About three years back, we had about 60, right, and then we consciously trimmed the portfolio of customers that we had, because the idea was to grow around the set of customers and improve wallet share rather than try and service too many customers. So, we dropped that to about 45-46, if I am not mistaken and then subsequently, we have added about three or four customers in this quarter.

Moderator: Thank you. The question is from the line of Sanjeev C from Tamohara Investments. Please go ahead.

Sanjeev C: Sir, in the initial commentary, you said about the funnel and order book looks better than last quarter. So, in that, could you please help us to understand how much would we like auto and how much would be on the non-auto side on the order book position that you said?

Madhukar Dev: The marked improvement is in the auto segment as compared to the last quarter, and the other two are steady as they were, there is nothing dramatically different.

Sanjeev C: We also saw the non-JLR part of the business falling this time. So, the trend is likely to be or if I consider this order book improvement that you say in that consideration?

Madhukar Dev: I said a little while back that I think it is a temporary setback that we are seeing, it is not likely to be a long-term trend.

Sanjeev C: The JLR and the non-JLR if I look at in a ballpark basis, the JLR supposed to be a better margin business for us, am I right in...?

Madhukar Dev: No, all our customers are more or less the same margin.

Moderator: Thank you. The next question is from the line of Tushar Bohra from MK Ventures. Please go ahead.

Tushar Bohra: Few points, sir. You had I think about three or four quarters back in one of the con calls mentioned the ambition for the company. If I can state that again, that you wanted to move to a deeper engagement mode from a shorter duration project mode to longer duration projects. You had mentioned you wanted to get more revenue from IP. I think the stated ambition was to get to 10% revenue from IP. The third was to get to 10% QoQ kind of revenue growth for the company sustainably. I think about three or four quarters back is what you had mentioned. I wanted to understand where we are vis-à-vis that ambition? If this is a process like really how long do you think we would take to sort of getting there, or what steps need to be done to get there qualitatively also?

Madhukar Dev: On the IP, I mentioned earlier that in the current quarter, IP revenue was just about 1%. So, there is a lot of work that we have to do to get to the 10% mark that I had mentioned. If you look at sequential growth of 10%, we did clock over 5% sequentially for several quarters till the last one, which is an aberration. So, once we get back to 5%, then it will be much easier to give you a timeline by when we will be growing sequentially 10%.

Tushar Bohra: Sir from a project engagement perspective as in...?

Madhukar Dev: Longer and deeper engagements, yes, certainly our average deal size has improved considerably, so also the duration of an engagement. That is also possibly one reason why we see a slower pace in decision-making. If you were taking too many small orders, you would be able to do it better than you are doing. It is a bit of a trade-off. And I think in the long-term it will be to our benefit. So, we are pushing for larger, more sustainable engagements.

Tushar Bohra: So, are we voluntarily letting go of some shorter duration projects or smaller...?

Madhukar Dev: No, we are not letting go, but we are not chasing those.

Tushar Bohra: In terms of the opportunity spaces, medical devices being one area for us and automotive vehicle, self-driving cars, and EV as space. Apart from these, in terms of themes, when I say artificial intelligence or 3D printing and stuff like that, which are the other themes that you see traction in that and that you would want to focus on let us say, from a 3-5 year perspective?

Manoj Raghavan: So, yes, the broad themes are definitely around artificial intelligence, robotics, IoT is a big theme for us. We have software-defined networking as a key theme. So, these are some of the few key themes that we are already working on, and hopefully, in the coming quarters, we will see returns coming from these areas.

Tushar Bohra: When we say IP, we want to get to let us say 10%. How exactly are we booking IP revenue -- is there a sort of non-linearity in terms of letting us say any one of our platform products goes into production, we can scale up exponentially, is that how we read on the IP revenue front?

Madhukar Dev: We have a few engagements like that and one of them is probably nearing the end of life now. So, we would not see too many upsides. We did not see any in the current quarter. Another significant one, we should start seeing an upside in two quarters, where we will have a share of the revenue that our customer generates.

Nitin Pai: This is Nitin here. I just wanted to add, please note that in general the model is not tuned towards long annuities or royalties over a period when it goes into production. That is a state we would like to get into.

Tushar Bohra: But we do have products, so we do have conversations happening along those lines already?

Nitin Pai: Yes, in fact, the first proposal we make is always to do with the annuity.

Tushar Bohra: Sir, you mentioned on JLR that we did 18% as part of the automotive and 21%, 22% of the overall last quarter. So, is it fair to assume that there would be some element of IP revenue from JLR and that your IP revenue gets tagged separately and not to a particular domain?

Madhukar Dev: No, what I said was the overall company-wide, which includes industrial design and visualization.

Tushar Bohra: So, there would be some revenues that would be coming from non-engineering stuff from JLR?

Madhukar Dev: Yes, non-engineering would be design and visualization, and there would be some work in the area of connectivity and communications.

Tushar Bohra: And your IP gets tagged to the domain revenue as in automotive IP would come into the automotive share of revenue, or IP gets reported separately?

Madhukar Dev: Internally, we track it separately, but we club it under the industry vertical.

Tushar Bohra: The engagement that we mentioned was supposed to start in April. It was a significant engagement in terms of the number of resources and billing, fair to assume?

Madhukar Dev: Yes.

Tushar Bohra: So, we would have had to do fresh hiring for that project?

Madhukar Dev: A combination of some limited amount of fresh hiring and by and large re-skilling and deployment of the existing workforce.

Tushar Bohra: Would there be a material impact on the margins that we have seen in Q1 because of this project not starting because the cost would have already been incurred which would not be your regular cost?

Madhukar Dev: Not so much, this one project, but there were about half a dozen such engagements which were to start during the quarter, which has not begun till June 30th. So, the combined effect would be significant.

Tushar Bohra: What would be our funnel right now in terms of either as a percentage to last year's revenue or as an absolute number?

Madhukar Dev: What we track is the funnel for the current quarter, and that number is significantly higher than what it was a quarter ago.

Moderator: Thank you. The next question is from the line of Kunal Shah from Carnelian Capital.

Kunal Shah: I have got one question as regards the consolidation that we see in the auto industry. Do we see consolidation also in terms of companies that are servicing them for R&D? What I mean is like companies like us?

Nitin Pai: In terms of consolidation in the industry around engineering, yes, but it is not so much consolidation. It is just the fact that with the larger IT stories slowing down even further, a lot of companies are looking at opportunities in the engineering space and therefore, you have, for example, Capgemini acquiring Altran and who has acquired Aricent, who has acquired so on and so forth, right? We have a chain of acquisitions, but if you look at it, it is to target alternatives to IT slowdown and the attractiveness of engineering in contrast. It is not so much consolidation within that industry itself.

Kunal Shah: Second question is also, are we looking at kind of any acquisition or something to double growth?

Nitin Pai: To that extent, yes, there is a reasonable cash balance, of course, nowhere close to what some of our big IT companies would have, but we have a decent cash on hand, and the idea is, of course, to use it either internally for growth-related aspects or to look at inorganic options. It is just that we have been a little careful about what we look at as strategic acquisitions. So, we are very clear that it is not the capacity; obviously, it has to be of a very differentiated capability or for the customer and market access. So, sometimes finding that right company and the right place at the right time and the right value is always a difficult thing.

Kunal Shah: When we say that we are looking at new verticals to be added in the next two, three quarters, we are building upon it right now or we are looking at it through acquisition mode?

Nitin Pai: We first look at the logic of getting into a vertical based on internal capability, capacity, and ability to scale. If the entry into the vertical itself has to happen purely through acquisition, possibly, there is no great upside in that sense. So, it has to be first of all, driven by a certain amount of capability and capacity internally and then complemented with market access or otherwise from outside.

Moderator: Due to time constraints, we will take the last question from the line of Apurva Prasad from HDFC Securities. Please go ahead.

Apurva Prasad: Sir, not still very clear on the JLR number? I believe last quarter, which is the March quarter, you spoke about 18% of the overall revenue and you have given a number of 14.5% of the overall revenue for the June quarter. Would that be correct?

Madhukar Dev: It was 21% in the March quarter overall, and it is 14.5% now. It was 18% of our EPD business in Q4.

Apurva Prasad: How do you see that trending sir, going forward you talked about...?

Madhukar Dev: I do not see it is coming down any further. I expect it to start moving upwards again.

Apurva Prasad: And also on the margins with the upcoming wage hikes, how comfortable are we from the current quarter margins, do you think that can go up despite the wage headwinds that we see for the second quarter?

Madhukar Dev: Yes, it ought to go up from where we are indeed, but how quickly we will get back to 20% is a bit difficult to say. It depends on how much more business we are able to bring in, what revenue growth we are able to clock in the rest of the current quarter and the subsequent one. But it should be possible by December end.

Apurva Prasad: Any initiatives that you can talk about in terms of building the funnel?

Manoj Raghavan: Yes, of course, funnel building is an ongoing activity, and as Madhukar said, both the actual size of the funnel and the quality of funnel is much better as compared to the last quarter

Moderator: Thank you very much. I now hand the conference over to Mr. Vaidyanathan for closing comments.

Vaidyanathan: Thank you, everyone. We hope to come back next quarter strongly.

Moderator: Thank you. Ladies and gentlemen, on behalf of Tata Elxsi, that concludes this conference call for today. Thank you for joining us, and you may now disconnect your lines.

Note: *This transcript has been edited for readability and does not purport to be a verbatim record of the proceedings.*