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Q3 FY2023 Earnings Call Transcript

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Chirag Jain

Good afternoon, everyone, and welcome to the Tata Communications Earnings Conference Call for Q3 FY23. We are joined today by our MD and CEO, Mr. Amur Lakshminarayanan and our CFO, Mr. Kabir Ahmed Shakir, and our head for Investor Relations Mr. Rajiv Sharma. The results for the quarter ended 31st, December 2022 have been announced yesterday and the quarterly fact sheet is available on our website.
I trust you would have had the chance to look through the key highlights. We will commence today's call with comments from Lakshmi, who will share his thoughts on the business and long-term outlook, followed by Kabir, who will share his views on the financial progress achieved. At the end of the management's remarks, you will have an opportunity to get your queries addressed. Before we get started, I would like to remind everyone that some of the statements made or discussed on the conference call today may be forward-looking in nature and must be viewed in conjunction with the risk and uncertainties we face. A detailed statement and explanation of these risks are included in our annual filings, which you can locate on our website www.tatacommunications.com. The company does not undertake to update these forward-looking statements publicly.

With that, I would like to invite Lakshmi to share his views. Over to you, Lakshmi.

AS Lakshminarayanan

Thanks Chirag and Good Afternoon everyone.

I welcome you all to Q3 FY23 Earnings Call, wishing you all a very Happy New Year. Coming to the results of Q3 FY23, we witnessed another healthy quarter reflecting strong growth momentum in our data revenues, and our profitability continues to be robust. Our YTD PAT is up 31.6% and ROCE is at 28.4%. Our results reflect the disciplined execution of our "Reimagined Strategy", focus on "Deeper with Fewer" and our abilities to impact both the cost and revenue side outcomes for our customers with our new portfolio of products. Our Products to Platforms shift, increased investments in front-end sales, particularly in the international markets, and building new capabilities across the portfolio has helped Data Revenues grow by 11.1% YoY again this quarter. To add more color to our data growth; we have added INR 948 Crores of incremental data revenues in FY23 till date, against an incremental revenue addition of INR 903 crores in FY21 and FY22 combined.

Our continuous investments in our core infrastructure and digital capabilities give us the confidence to efficiently cater to our customers' evolving digital transformation needs. We continue to be a leading player in India's Large Enterprise B2B segment and are continually investing in our undersea cable assets, which form the backbone of our suite of offerings, almost 30% to 40% higher versus our closest competitor over the last few years. Growth in international markets continues to show encouraging trends and is steadily progressing towards our long-term ambition of improving the international revenue pie. Large deals order book in the enterprise segment has exceeded full year FY22 performance and funnel additions in the enterprise segment have improved significantly both from an India and an International market perspective.

With our Media Business making strong strides, we announced our intent to acquire The Switch Enterprises LLC for a consideration of USD 58.8 Mn (INR 486.3 Cr.). With this transaction, we will gain a strong foothold into the Americas media and entertainment market. We have an established leadership in Global Sporting Events catering to a global audience. This acquisition will help us strengthen our region to region as well as the region to global play in the live sports industry, bringing these sports closer to the global audience. Not only this, upon completion of the acquisition, it will also open gates for us into the live production business, which will complement, and further strengthen our offerings in the Media portfolio. These synergies will help uniquely position us as an end-to-end media ecosystem player in the entire content development value chain globally and deepen our moats.

Moving to our performance for the third quarter of FY23. Our data business remains instrumental to our overall revenue growth momentum. It improved sequentially by 2.9%, coming in at INR 3,593 Crores. Our Digital Platforms and Services revenues stood at 1,056 Crores, registering a healthy growth of 17.2% YoY and 5.8% QoQ. Our Q3

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consolidated revenue was INR 4,528 Crores, improving by 8.2% YoY and 2.2% QoQ. EBITDA for the quarter stood at INR 1,077 Crores, while the EBITDA Margin stood at 23.8%. The profit for the quarter was INR 394 Crores, flat on a YoY basis.

Let me talk about our margins and the aspects shaping EBITDA trajectory. We are making planned investments in platform portfolios and also sales and marketing, particularly in international markets. Our investments in enhancing our talent and tools are in line with our strategy and we will continue to stay invested. These investments, coupled with our product mix plays a part on our margin profile, given growth in DPS is higher than core connectivity segment. We had some headwinds of inflation as well which has resulted in some near-term volatility in our margins. That said, we intend to stay the course as we continue to sharply focus on executing our strategy.

We are seeing good traction across the DPS portfolio and have a good pipeline in our sales funnel. We have a good pipeline of product feature releases and new products in coming months. From a medium to longer term perspective, we will see benefits accruing from our razor-sharp focus and investments on our product to platforms shift. More importantly each part of our data portfolio is driving stickiness, deepening our moats and will help us to improve our yields in the medium term.

Let me give you some more details about our Data portfolio. One key essence which is heartening is the huge transformation that is happening with the way our GTM is being approached. Most of our customer discussions have moved beyond connectivity to those factors that affect them, which are cost efficiencies and helping revenues to grow through our secure and intelligent digital fabric.

Let me spend some time talking about our strongly growing Incubation portfolio. The Incubation Portfolio progressed multi-fold growing by 125.3% YoY and 1.1% QoQ. Our Connected Solutions, our MOVE™ platform is a sophisticated platform, delivering connectivity management and data enablement with APIs across the globe. Our MOVE business continues to grow strongly and expanded by more than 2.1x compared to last year. Our ON CAMPUS connected solutions opportunity is driven by our IoT Offerings where we cater to both enterprises and smart cities. This quarter we completed our first international order of smart street lighting solutions, which has opened up opportunities in the international markets.

Our Core Connectivity Services grew by 6% YoY and 1.7% QoQ. We will continue to invest in the core capabilities, thus transforming our networks to be smarter and more agile to cater to the new market needs.

Now, coming to our Digital Platforms & Services portfolio, it has grown at 17.2% YoY and 5.8% QoQ. Our multitude of offerings in the Digital Platforms portfolio are intended to consistently deliver more holistic solutions, stitching multiple products together for our customers' ecosystems. Our digital fabric helps create a robust moat around increasing customer stickiness and insulates us from structural pricing decline seen in the legacy businesses. The portfolio grew broad based across all offerings. Our Collaboration Portfolio grew by 8.8% YoY and 6.2% QoQ. We continue to benefit from an increasing customer interest in our newer offerings namely Tata Communications GlobalRapide™, InstaCC and Tata Communications DIGO. DIGO continues to grow in capability as a Customer Interaction Suite, where it focuses to unify all customer interactions. In our augmentation strategy, we now integrate seamlessly with other CX ecosystem players like INSTACC® Platform, Salesforce, and more to enable contextual omnichannel interaction capabilities for businesses. Further we have partnered with META as Business Solution provider & with Google As Google Communication Partner, which enables us to add more channels to our Omnichannel offers globally – WhatsApp, Google Business Messaging, RCS and more. Besides a rich set of connectors that we would launch this quarter, Engage 2.0 Beta Version, that can enable marketing campaigns.

Moving to Cloud, Hosting and Security. This portfolio registered a growth of 23.7% YoY and 8.8% QoQ. In Q3FY23, we have focused on increasing customer experience with digital onboarding, automated provisioning & transparent billing through our TCX portal. We have also created a single pane of glass for multi-cloud management. Using our cross-product integration (Cloud, Security & Network), we have created several upsell opportunities in our premium customer base, contributing to high gross revenue growth. The global cybersecurity threat landscape continues to be grim, and as a result we are seeing good traction for our security offerings and solutions especially among enterprise customers looking to strengthen their estate with our threat management solutions. We have been continuously expanding our Threat Management Platform with new use cases and playbooks to ensure that we can help our

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customers faster detect threats as well as respond to them.

Coming to our Next-Gen Connectivity offerings, this increased by 26.8% YoY and by 5.5% QoQ. The increasing adoption of the Internet and the shift to the cloud is helping us drive growth in this segment and expand our market share. Our offerings such as IZO WAN and IZO SDWAN are gaining traction with our enterprise customers as we enable them with our simplified and cloud-like solutions to aid them in their network transformation journey. Our Media Services revenue grew by 17.1% YoY and declined marginally by 0.9% QoQ. We are witnessing a sustained push towards digital services with more focus on cloud & edge-based workflows for better performance and user experience in our media business. To sum up, as a digital ecosystem enabler, we remain committed to building innovative and scalable platforms to empower enterprises. With that, I would like to invite Kabir to give an overview of our financial performance. Kabir.

Kabir Ahmed Shakir

Thank you, Lakshmi. Good afternoon, everyone. I will take this opportunity to take you all through the highlights of our financial performance for the quarter.

Q3 of FY23 continued to witness a healthy growth momentum. Our Consolidated Revenue for the quarter stood at INR 4,528 Crores, improving by 8.2% YoY and 2.2% on a sequential basis. Data revenue for the quarter stood at INR 3,593 Crores, improving by 11.1% YoY and by 2.9% on a quarterly basis. The reported revenue numbers this quarter, like the previous quarter continues to have certain forex benefits accruing from a strengthening dollar. Our EBITDA for the quarter stood at INR 1,077 Crores, reporting a margin of 23.8%. Our YTD PAT is up by 31.6% and our PAT margins for this quarter stood at 8.7% and YTD is at 11.1%. Last quarter we revisited our deferred tax asset recognition policy. With our international operations becoming profitable, it is allowing us to utilize our NOLs, helping us drive a healthy balance sheet and maximize returns. Our ROCE is at 28.4% are up 3.6% YoY and within our ROCE guidance of 25%-30%. Net debt for the quarter stood at INR 6,270 Crores. Net debt to EBITDA is now at 1.4x compared to 1.5x last quarter. The most notable part is that our debt has been consistently coming down. Our cash flow generation continues to be healthy, reporting an FCF of INR 335 Crores this quarter. To sum up, I am quite delighted that our Fit to Grow strategy is coming to life as balance sheet and financial prudence have allowed us to fund inorganic growth opportunities and the acquisition of Switch is an outcome of our broader finance strategy.

Let me now talk a little more about our consolidated EBITDA margins which have declined 170 bps this quarter to 23.8%. Our YTD EBITDA margins stand at 24.7%. Both the current quarter and YTD are in line with our EBITDA margin guidance of 23%-25%. This fiscal, we have laid strong foundations for achieving our growth ambitions, through deepening customer engagements and investing in expanding our global sales and product organizations to address emerging market opportunities. With pandemic receding, COVID benefits we had are no longer there. Today, our revenue mix is driven by a higher growth in DPS where margins are lower versus core connectivity. Though these factors may build in some volatility in our quarterly margins, we will continue to operate within our margin guidance of 23-25% for the full year. We have always maintained there will be times when we will operate at the lower end and there will be times when we operate at the higher end. We have been operating at the higher end of the range for past several quarters. That said, if we have the right proposals from the business to fund customer success we will stay the course and fund those opportunities. At the same time, we are focused on levers which will sharpen our moats and help us improve our trajectory in the medium term.

Cash Capex for the quarter stood at INR 440 Crores, though our approved capex is close to INR 500 Crores, due to delayed deliveries and better payment terms.

Moving to subsidiaries, we see a steady improvement in TCTS. TCTS revenue improved by 6.6% YoY and 3.7% sequentially, coming at INR 333 Crores. EBITDA for TCTS stood at INR 15 Crores for Q3. Our Payment business continues to make positive shifts as we expand our portfolio under the Franchise model. Revenue for the quarter came in at INR 50 Crores and an EBITDA of INR 2 Crores. As on date, we have added close to ~2800 Franchise ATMs to our portfolio and are working steadily on increasing this further.

Our continued focus on delivering best-in-class bespoke solutions is enabling us to drive both the cost side and revenue

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side outcomes of our customers and this will help us a long way in being a strategic partner to digital and network transformation journey of our customers. Our new positioning with our digital fabric combined with our strong balance sheet and healthy operating performance gives us the headroom to invest, innovate and grow and aligning with the evolving needs of enterprises.

This brings us to the end of our management commentary. I will now ask Chirag to open the forum for Q&A. Thank you for your attention.

Chirag Jain

The first question is from the line from Sanjesh Jain from ICICI Securities, you may now ask your question.

Sanjesh Jain

I have questions on the revenue side. Can you help us understand how the order book and sales funnel trajectory has been in this quarter? And how is this new sales effort helping us to drive that faster? That is number one. Secondly, on the enterprise side. I think this is the fastest ever growth in the last many years that I have seen where we are seen enterprise revenue growing by 20% YoY and 6% quarter on quarter while the wholesale business, which is a service provider, is seeing a decline. It's a conscious effort where we want to change the revenue mix or it's just a coincidence to see and what is driving the strong enterprise revenue that's the second. And the 3rd, on the collaboration side of the business. This is probably the 1st quarter on a YoY basis, we have seen growth after many quarters. Can you help us understand within the collaboration ? The 3 new products which touched upon, which is GlobalRapide™, InstaCC and Tata Communications DIGO, how is it growing and where are we in terms of drag from the SIP trunk. Is the SIP drag over, are we growing there or it still remains a decline for us.

A S Lakshminarayanan

Let me take each of those three Questions. The first, relating to order book and sales funnel. I think I've been maintaining that our order book is getting better every quarter and our sales funnel is improving. I think it's interesting to see the mix in our funnel is quite healthy, in terms of digital platforms is much higher in our sales funnel compared to core connectivity, which is in line with what you would expect in line with our strategy to grow the DPS and the Incubation portfolios. In terms of what is driving that, I sort of alluded to that. Two things I would want to point out: one is, we are able to have a more engaging conversation with enterprise customers at senior level beyond connectivity. We are able to go and talk. We are able to meet with not just the head of network, but meet with a CIO, COO, CMO for example. And sometimes we even held half day workshops with CEOs, because the positioning that we have as a digital fabric, when we tell them that, hey, car is nothing but another node in the network; and all the way to what happens in the factories with industrial connectivity as a service, which is part of our connected solutions; and then say how we can help them to connect various personas, branches to the network and transforming the network with the Internet and software defined WAN, but also software defined LANs and branches, taking them all the way to the cloud and between the clouds how we connect. And address some of their customer experience problems through our customer interaction platforms and so on, we are able to have more holistic conversations with customers. So that is one. I would say where we feel that, there is something that I call internally as a relevance quotient, is increasing with our customers. The 2nd is a reflection of that, we are able to have better pipeline. And as we improve our footprint, in terms of our coverage in the markets, the funnel is growing. we are also seeing that our win rates are inching slowly forward, not as rapidly as I would want, but it's definitely improving and inching better, which is helping us to convert the deals. So that is the sort of the color and flavor I would like to give on the order book and the sales funnel.

To your second observation, that enterprise is seeing the fastest growth is it a conscious effort? I mean, exactly. That is all our narratives on our strategy, it is all geared towards enterprises. Service provider is an important segment. But we buy from them, they buy from us. It's more of a trading relationship that we have, it is still a significant segment, and we continue to address that segment, but the core of the growth and core of whatever we have

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articulated in our strategy, the new platforms are all addressed towards the enterprise segment. So, it is a conscious effort and that is what is bearing fruit.

Kabir Ahmed Shakir

If I may include, the reclassification we've done, especially primarily in the MECCA region, where we don't have a license that we will have to go through some of the service providers, either we were classifying that as a service provider. Now, looking at the kind of revenue, if it is pure play connectivity, which is resold by them, that continues to be service provider. But if the end customer is actually an enterprise, and that's what we are doing, and we are using the service provider to reach them, then we are reclassifying that. That impact is about 2.9%. So, it still does not take away the point that Lakshmi is making, our strategies on enterprises. That is where we do our coverage, that's where is our feet on street investment is also going and that is bearing fruit. But, I will be a miss it if I don't mention that there's been a reclassification in this quarter also.

A S Lakshminarayanan

And the third part of the question, on the collaboration. Yes, I think collaboration, we've talked a lot about this in the last few quarters. Particularly GSIP was a large part of our, digital platforms and solutions. And as it started going down, we had an impact, even though there were other parts of digital platforms that are growing and glad to see that. Overall collaboration is back on the growth trajectory. There has been a significant effort, in terms of pivoting the segment away from purely depending on the usage-based SIP, to a more fixed PUPM plus the usage kind of model that we are going with the GlobalRapide™, InstaCC, not just our own InstaCC platform, but also partnering with Genesys and AWS to deliver holistic solutions in the area of contact center as a service. All of that helps to put us back in the growth track. So, with respect to your question, yeah, we are betting less than less on that. So, while we would want to keep it steady, slowly our dependence on that is going away, but we would like to see that stabilizing. It is stabilizing. But the dependence on that is not as much as we were a few quarters ago.

Sanjesh Jain

Thank you. Thanks for all those answers. The second is on acquisition. What is the synergy? I know we have given the potential revenue, which they do. But I want to understand more how much it will contribute to the profitability. And what is the synergy from Tata Comm to Switch and Switch to Tata Comm. Can a merged entity deliver, a much better profitability, if at all there is a probability for that. And once it picks up, will it be EBITDA accretive or once it smoothens, we will pick it up from there?

A S Lakshminarayanan

So, let me talk about synergies. I mean all these acquisitions that we do, as we had said that we will do that for capability or regional and customer reach, and they have to make financial sense. So, that having said, Switch particularly is very interesting, because they are one of the leaders in the U. S. market, taking a lot of regional sports and taking to regional U. S. audiences'. If you look at our media business, which I briefly commented in my statement, our media play has been largely what I would call as a global to global play. We take global events and take it to the global audience, that is our strength to us and we are one of the strongest players in that space. The other 2 segments, if I were to call is a region to global play, and the region to region play. And in those places, it's like a regional sport taking to a like, maybe cricket would be a good example where it's a regional one, but it's got some global appeal. It's not as global appeal as in terms of number of countries, the audience reach out.

So those are the three places that we see the global, region to global and region to region. We are strong in the global to global. We have some play in the region to global. What Switch does is, helps us to strengthen the region to region in the U. S. which is the large market. It also helps to take the region to region, to region to global through our global footprint. That is one synergy. The second synergy that we see is they have a product for production which we do not

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have at the moment. And that production capability enhances and will enhance our product offering once we merge and we can take that offering to our other global customers. So, these are broadly the synergies from markets and product perspective and how we see the segment in our minds. The third question regarding the margin accretion.

Kabir Ahmed Shakir

With the first year being integration, it will be dilutive, but with all the synergies that we see in the business case, and the rational overall, we do see that the overall margin portfolio for media business will definitely be held by Switch and be able to sell more, we're able to give more value to our customers, and in the medium term, EBITDA will pick up. But in the first year, it's all about integration and about the thing that will be a bit margin dilutive.

I think if you take the PMI costs out, then it should be okay, but as a business, we are very clear, nothing structurally to worry about the profitability.

Sanjesh Jain

My last question on the cost inflation. are we behind, in terms of peak of the cost inflation. We have seen almost 150 Crores getting added. to the total operating cost. Are we behind in terms of the majority of the cost investment, which we intend to do ?

Kabir Ahmed Shakir

For example, on hiring, I think now we are seeing the full impact of the hiring come through. In fact, we did not see that full impact in Q1 and Q2 as we still had attrition along with the hiring. Now that attrition is stabilized and its behind us. Assuming things will probably reverse with all the layoffs that we see.

So the pressure on that side of the talent market should come down and we see the full impact of that staffing cost increase, come through this quarter. There are other elements of inflation that will continue to be there, which energy for example. If you actually see there are a lot of energy costs that impact our power at PoP locations across the world, both Europe and U. S. That I don't think I can put a finger on it and say, when that will come down. I don't think anyone can say in both in Europe and in the USA, the energy crisis that we actually see today. In some places where we have the ability to pass on the price, we will do that, but there are a lot of longer contracts which we have, where we don't have the ability to pass on the price. We will have to take that hit and manage in our overall PnL. So that's how I would put both of these together. Plus, one of the reasons, as I mentioned, the COVID benefits. We've always called out, we used to have about 50 Crores of COVID benefit every quarter. That benefit is no longer there. This quarter as we are resumed to 100% normalcy, we are back in office, travel started, spending on marketing, we are going to events and that's all coming back to normalcy.

Sanjesh Jain

Just on that power cost, I think peak inflation is behind. I don't think anybody is anticipating the cost to go up from here. I know a decline is something we cannot expect. I am calling from the inflation perspective. We are done, right?

Kabir Ahmed Shakir

I hope so, but the impact of it will trickle in, because not all of that has also come in for us because we also had contracts and stuff like that.

A S Lakshminarayanan

Also the staff cost and I think we had called out as early as last year, we said we were going to start investing in the

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front end of the sales and marketing. We also said that we would add to our products and platforms and develop new capabilities. I think the 150 crores cost that you are talking about here, a fairly large part of it is also staff cost. In specific digital skills and so on, there was a wage inflation and retention scheme that had to be put in place. So, there were many factors that went into it, this is why YoY the staff cost is a significant part of the of the increase.

Chirag Jain

Next question is from Shubham Shukla from Voyager Capital. Please go ahead and ask your question.

Shubham Shukla

On the debt level of our company, it has reduced from 6,400, goes to 6,270 Crores which is good, but finance cost has gone up, like, 25%, quarter on quarter. 98 to 125 Crores. Just want to understand what the reasons are like? Is it only due to the increase in cost of borrowings or there is something missing.

Kabir Ahmed Shakir

Well, I'm, sure you're seeing the news as much as I do. You see the Fed hikes, that has been happening since March onwards. Even in this last quarter, three hikes that have happened - in September, in November, and in December, 75 basis points, 75 basis points and 50 basis points respectively. So I would say, it's great that we've been able to do the cash generation that we have been doing for the last 2 years and it reduced our debt significantly in the last 2 years. Otherwise, our interest cost would have been a lot higher than what you currently see in the PnL. So it is completely because of the FED taking the interest rates up, which we see, all the economies also reporting. But for us, a lot of, most of our debt is dollar denominated and it is just as a result of the base rates going up.

Shubham Shukla

My second question is around the other income. Like, if you could give some colors or like, what it includes and it is at its lowest in last 4 to 5 quarters what also affected our margin for this quarter.

Kabir Ahmed Shakir

Well, other income is having its own vagaries in it. When we have income tax refunds and then the interest competent on the income tax refunds that come through. I cannot give you an idea on the projection, because these are related to old cases. And again, I would say, I would really like to thank the cross functional teams, in tax, regulatory, in treasury, who actually are putting their mind behind and clearing up all these old deals. So, we've collected quite an amount of all those refunds of the past. And this is not predictable show up. I wouldn't know as to when the order is going to get passed and when the case will come up for hearing and when do we actually get. So the other income gets impacted, largely because of the interest Income that we received for the refunds that are due from the authorities.

Chirag Jain

Thank you. So, the next question is from the line from Abhishek Singhal. Please go ahead and ask your question.

Abhishek Singhal

So, my question, what is EBITDA margin of Switch enterprises LLC and second question – The company has grown at 6.5% YoY 9 month. So, what is the program of the company that the growth would come in double digit?

Kabir Ahmed Shakir

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Well, we have not spoken about EBITDA Margin of Switch and that's one of the parts of our portfolios within DPS, within data. So we are restricting to that portfolio as a whole and focusing on how we would like to imagine progression of our data portfolio. I wouldn't want to go into talking about the profitability of that. We looked at the whole acquisition and it makes strategic sense for Tata Comm, and for the media services portfolio and that's the reason why we are quite optimistic of the opportunity and we are glad to have Switch as part of our portfolio.

Chirag Jain

Thank you. So, the next question is from the line from Pratap Maliwal from Mount Infra Finance. Please go ahead and ask your question.

Pratap Maliwal

I just wanted to ask the share of a EBITDA by segments, the breakup of the data segment into core connectivity, DPS and incubation. It was given last quarter, but I don't think it's present in the current fact sheet. Can we have those numbers please.

Kabir Ahmed Shakir

We have taken a call that, and I've said it about that in last 3 quarters when these questions have been asking that we would like you to look at our data business as a whole because there are vagaries that happen. These are all at various stages of evolution. We are investing in platforms, we are investing in capabilities, and some of them need upfront investment. Some of them are design wins where we invest, and we learn from it and then we scrap it. And then we reinvest again. So, there are multiple elements that go in and sometimes quarter on quarter, these tend to give a wrong picture, without context. And that is the reason why we've taken a call to take this off. And I would encourage you to look at the overall data portfolio, which probably gives a little bit more stability and a little bit more clarity from a future growth perspective as well. So that is one of the reasons. And we do not intend to give those breakdowns anymore.

Pratap Maliwal

Okay, sure now you just said about the Switch TV acquisition. I think our previous participant had asked, not the margin, but the potential revenue, can we please have that number? The revenue base.

Kabir Ahmed Shakir

Yeah, we have already mentioned the revenue, it's about 80 million dollars of revenue last fiscal of this business.

Pratap Maliwal

There were some forex benefits that we got for our margins. So, can we quantify that? Because of the stronger dollar? Can we quantify the forex benefits?

Kabir Ahmed Shakir

On margins, it's a small portion, on revenue, it was still material, but on margins, it's a very minor portion benefit that we got from forex.

Pratap Maliwal

Okay, sure and just one last observation I had. I think you've addressed this in the previous quarters from other participants as well, but regarding the DPS segment growth that we've had 6% increase in growth, but there's been a

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decline in the net revenue. So, what was it about the product mix? Because I think we had good growth in a lot of DPS products. So, what is actually driving that?

Kabir Ahmed Shakir

Yes, it is. As you rightly said, it's largely mix, which is contributing to it. Plus, there are some upfront costs and certain deal specific vagaries that probably explain DPS. I'm less worried about it because these are the right things for us to do, so I wouldn't worry about quarter on quarter vagaries about net revenue. I think our focus is on improving the mix of our business more towards DPS, versus core connectivity. So, while we do that, there will be headwinds on margin that will come through overall at a company level because of this shift between DPS and core connectivity. And that will also has in the short to medium term, headwind between products within DPS as well but I think that's the right thing to do until we gain scale in each of these products and therefore that is the right business call to take.

Chirag Jain

Thank you. So, the next question is from the line from Aliasgar Shakir from MOSL. Please go ahead and ask your question.

Aliasgar Shakir

So quite a detailed explanation on the revenue and funnel trajectory. I just wanted to look at it in the context of your cost increases. So, I mean you have mentioned in the past that we are investing in growth, both on the capex and on the opex side. So, in that context, as we've seen some increase in cost in this quarter, could you share some visibility in terms of this increase in cost, is it related to any specific projects that we are foreseeing, given in terms of the funnel looking strong. So, how should we see this cost, should we expect growth to inch up and are there any projects that we are seeing that should come by in the near term.

Kabir Ahmed Shakir

I kind of said it in bits and pieces, but let me summarize for everyone. It's at various levels that we actually see the margin explanation, at the net revenue level, as I explained it is largely mix, which has resulted in the net revenue fall. If I go below net revenue to EBITDA, these are cost increases that we actually see, majority of the cost increases is a staffing cost increase that we have this quarter compared to last and compared to last year as well and that is something which we had called out earlier. You can see in our factsheet, the number of employees increase that we actually have this year roughly about 1000. We also eluded earlier the wage increase that we had to give and retention bonus we have to retain our people. Plus also, the war on talent that we saw 2 quarters ago, the great attrition, which was occupying all our vocabulary. So, we had to kind of retain and attract the right talent in our organization. So that was one. Also, not only I would say on the product and engineering side, but also investment on feet on street, and largely shifting towards the international geographies where the cost is higher as you can imagine of an FTE out there. But these are the places where we are also seeing the benefit already come through. When you are investing in those geographies when we are getting sales, coming in international geographies, and they become profitable. And I'm sitting with NOLs in those geographies. They utilize faster and our PAT is up. EBITDA may still be lower, because they may not be, getting full there, but as they become profitable, I'm even adding a little bit of revenue to what I have, I'm seeing at a PAT level that is being activated. So, staffing cost is one big element. The return to office, and the CVOID savings going away is the other element and there are minor things like energy costs that I talked about. In relation to these two that is minor. But on its own, it's still a material amount. So, I would say these are the three broad elements on cost, that they sit there and combined with mix explains the margin profile. None of which is something which we did not know. None of this is, which is something we did not plan for. And this is the reason why 2 quarters ago when I talked about, I did say that look, we will operate at the low to mid part of our guidance range in the year. And in the first 2 quarters, we had the benefit on the market shift that came in the voice business, which again I talked about last quarter as well. So, to that extent, our consolidated EBITDA actually had a benefit and a bump up and the erosion got delayed a little bit in the first 2 quarters. So we benefited from that, which was also transparently shared with all of you in the last quarter call as well. So, that's how I would sum up.

A S Lakshminarayanan

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Let me just expand on one element of it. We talked about and I, in my opening remarks, said that all these are planned investments. And I emphasize that a lot of sales and marketing investments are going in international geographies. And we had said that, as part of our strategy because while we are a market leader in the segments that we choose to operate in the B2B segment in India, in international markets, it's a huge market. And our market share, that is still not what it can be potentially. So, I've been saying that the network is a 1.5 Billion market in India, whereas it's 145 Billion market in the international market. So, there is much more upside to be had, with the right products the right solutions, which we are investing and I think we have to invest in the right sales and marketing capabilities in those regions, which is what we have begun to do, and which is also why we are beginning to see some of the results come through. So, those investments, in our opinion, have to be made, and we will stay invested in both those aspects of sales and marketing as well as in for the enhancing the platform capabilities.

Aliasgar Shakir

Got it, this is very detailed and only point that I wanted to just clarify. I understand these are planned investments but given that we are adding a lot of resources, we should expect the growth to inch up in the near term with whatever new funnel or any order book that we are seeing.

A S Lakshminarayanan

No, I think these resources did not materialize just this quarter, we've been talking about for the last 3 to 4 quarters, and gradually the people have come in and with that is what you see the results.

Kabir Ahmed Shakir

And it is already visible in the last 2 quarters, when we started touching double digit growth ambition, and it is what we will continue to push for. So, this investment has already started seeing benefits and fruits in the last 2 quarters and as we said we are committed to it and we should, we will stay on course.

Aliasgar Shakir

Second question on the 5G investments that other 2 telcos have made and they've been quite vocal in their offerings in the enterprise side. We have not spent on spectrum, but of course our offerings are well understood. So, you think the competition from these 2 telcos will increase or are you seeing anything on the ground? Do you think that capabilities can increase with this spectrum? I mean, your thoughts here.

AS Lakshminarayanan

No, our strategy with respect to 5G is very, very focused on the private network that they can enable for enterprises. We have built our capabilities quite strongly to be able to compete in that space. We announced the launch of a lab, and our stack of solutions on 5G a quarter ago. It is in Pune. We've had several customers use the lab as a service to trial the use cases, and we're also taking these capabilities to international market where we are addressing in this space. So, just not focused on 5G. We have a pedigree with our IoT fabric solution, and we want to offer this truly as an IoT fabric. Regardless of the technology, whether it's LORA, whether it's WiFi6, unlicensed LTE or 5G or in future its 6G. We will have an industrial connectivity as a service and fabric capabilities that we have built, and we are already selling that capability in multiple forms, with various customers. And with 5G, we are waiting for the DoT to announce, the are firming up what they've announced in terms of the opening up for the enterprises to set up this captive networks. And we are all set to grow when that happens. And, as I said, this capability is not just for India. But we are also talking to international customers to take and deploy this capability

Aliasgar Shakir

Are we seeing the competition also growing?

AS Lakshminarayanan

Yes, of course I mean, they have invested in spectrum, in every sphere there is varied competition. So, even in our DIGO as a product that we launched, yes, there are competitors. We talk about MOVE™ there are competitors. So, that is not the concern. I think we are very focused on our customers, understand what they seek and want, we want to be

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a lot more technology and OEM agnostic solution. Our MOVE™ solution is intended to make our customers more MNO agnostic. So, we are not a MNO player with mobility spectrum, even on the 3G or 2G for that matter, and MOVE™ still delivers the connectivity management solution for our customers. So, we come at it from a different angle, and I'm sure there will be competition in all the spaces. But, we are quite confident of what we are building and to be able to deliver.

Chirag Jain

The next question is from Mr. Vinit Manek from Karma Capital. You may now go ahead and ask the question.

Vinit Manek

We answered this question, but just wanted to check one thing with you that on the increased interest cost quarter on quarter there wasn't any element of forex that might be impacting us, because our payments would be presumably in the interest payments will be in terms of the U.S dollars. So, was there any impact of that available, during this quarter or maybe the last 2 quarters?

Kabir Ahmed Shakir

You are absolutely right, its dollar, so there is hardly anything in there. There is a very minor impact I would rather say there's hardly any impact from forex on interest cost

Vinit Manek

Okay, and any other line item has been impacted because of the change in the foreign exchange happening.

Kabir Ahmed

I did mention in my speech, that our revenue has been positively impacted. Like, it's been there for a couple of quarters due to the strengthening dollar. Revenues is more material, the profit is also positively impacted, but not that much material. Foreign currency translation reserve and then the net worth, all of those in the balance sheet does get impacted.

Chirag Jain

The next question from the line of Mr. Sanjesh Jain from ICICI Securities you may ask the question now.

Sanjesh Jain

Just one follow-up on the revenue side, which we spoke of earlier considering this sales funnel as well as the Order Book we see today, are we reasonably confident in terms of growing 20% easier for the next few years? It's not a guidance just wanted to understand. Is it possible for us to go at the 20% CAGR in the DPS portfolio? Or do you see any challenges for that?

AS Lakshminarayanan

It is possible. I think in order for our data revenues to grow consistently at double digit, we need to have our digital portfolio, and sometimes I mix up the portfolio and I include the incubation, this together has to grow at that level. So that is clearly our ambition. That is possible and that is what we would be aiming for and targeting to do.

Sanjesh Jain

No, but is our order book and sales funnel that is building gives that that confidence that it is quite achievable.

AS Lakshminarayanan

That gets close to the guidance then. All I would say is, that is what I have been saying since we are investing in all these places, these products and platforms, and they are getting stronger. Yes, there is good momentum in terms of

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the final build up. And I think I also mentioned that if you look at the color of the funnel that is more in DPS than in the core connectivity. So, the mix is already positive there. So, I think that is the best color I can give. I think we must execute on those and definitely we will aim to push the DPS growth to that trajectory.

Sanjesh Jain

A small request, it would be great if we could call out the order book. So that gives us confidence and visibility in terms of how is the revenue stacking up ? We did this in between, but again, I think we pulled it out, but this is a request from our side if you can.

AS Lakshminarayanan

We'll try and look at whatever indicators that are helpful to you. I think we pulled it out 3 years ago because the color of the business had a lot more of usage. And when we talked about order book, one assumes a certain degree of usage and says, that's the order book. But the usage is never sort of guaranteed, and either it comes off, or it doesn't come and there were a lot of fluctuations as a result. The last 2 to 3 years we've been trying internally to work out the algorithms that we can get right. So, the predictability on the usage Contracts we can get it right? I would say we still haven't got it absolutely right. So, anything that we give could be misleading as well. So, we hear you, I think we would give it out at the right time. We understand the reason why you're asking as well. So, we will start to give at the right time. We're beginning to give more and better color through words. But as figures we will start to do that whenever the time is right.

Chirag Jain

We will take one last question from Neel Nadkarni from Dalal & Broacha. You may ask the questions now.

Neel Nadkarni

My question is again on the margins. So sorry to bother you in that. But what I get from the call is, we have made material investments on improving our funnel, our sales mix, etc. and, is it fair to assume that this is the bottom end of the margins. While we have indicated that we want the margins to be between 23 and 25%, but is it fair to assume that from here on, all the margin should improve going forward primarily because the thinking goes that if the funnel is looking better, if the execution is going to be better and operating leverage should kick in and given the business model, it should take in a very big way. So, is it fair to assume that the margins from here on should start improving.

Kabir Ahmed Shakir

Well, I would say 23 to 25. And I've been saying that consistently for the last 2 and a half years now. And it'll be times when we will be at the lower end, there'll be times we will be at higher end. And, and because of COVID, because of lots of other tailwinds that we actually got, we've been operating at the higher end of the range. For us going outside of this higher end will be irresponsible because then we will be choking the right investments to make and setting high bars, especially in digital platforms and services areas where you need to allow for experimentation. You need to allow for POCs to come through and then identify the use cases. So, we do have a 1,3,30 approach for our innovation programs internally, and these needs that right level of support at every place. So, I cannot answer the question in yes or no, whether this is the bottom, whether this will go up. 23-25% is our range, our endeavor will be, in one quarter, it goes below 23%, I am not going to sweat myself because we have made the right investment decision for our products. And these markers are good markers for us to guide as to how to run the business. But if these markers go away for a quarter, for the right business reasons I think we are not worried as management and you, as investors, should not be worried either.

AS Lakshminarayanan

So, to your other point, a lot of while we are seeing the growth, in each of the portfolios whether it's the connected solutions, or in collaboration with DIGO or even GlobalRapide™, these are only getting started now. So, I think they are a mix of a platform as a services play, so I think, we have to continue to invest and we are upgrading these products and launching. So, we are launching GlobalRapide™ 2.0 with a new set of tools and services capability. So, each one of them have a different profile and trajectory. We are continuing to enhance these products and do that. So, I think for a while longer, I think we would be continuing to invest and it's not upto scale where, when you talked about the

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operating leverage kicking in. These are multiple products are varying degrees of investments, with a combination of product and the combination of services play attached to that as well.

Kabir Ahmed Shakir

And I would also encourage you to look at it holistically, business in totality. Look at the operating performance of the business, not just EBITDA, look PAT, look at free cash flow, look at ROCE, look at our reducing debt. Despite the increased interest cost that a couple of you asked for our PAT has actually gone up. So, with all of those levers, these are all giving us the elbow room, the head room to actually make the right investments in the business. So, after a point in time, one shouldn't get fixated about numbers in the middle and do what is the right economic value that actually drives. And frankly, it has been a guiding force in the last 2 years for this particular company to change the trajectory and get onto this particular path. And I fundamentally believe, Lakshmi, me and my other colleagues in the GMC are completely committed to this rational, and that's how we are actually driving the business and we believe drives bong term value to all stakeholders in the business.

Chirag Jain

This brings us to the end of the call. I would request Lakshmi to share his closing comments.

AS Lakshminarayanan

I think we are very, very delighted in the progress that we're making in the overall strategy execution. We are making good progress in the Platforms to Product shift, and many of these products are beginning to get good traction in the market. As I said, we will continue to stay invested in both, the talent and building the talent to help us shift to the digital play and also invest in the products and platforms. And the most encouraging thing is the kind of conversations that we are able to have with our customers, is really encouraging to see. So, thank you very much all for a patient hearing. Thank you very much.

Chirag Jain

Thank you, Lakshmi. For any follow up questions, kindly write to investor.relations@tatacommunications.com. This brings us to the end of the call. The recording will be available on our website in the next 24 hours. You may please disconnect now. Thank you.

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