



Q3 FY14

Earnings Conference Call

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Members of Nucleus Management

Mr. Vishnu R. Dusad	Managing Director and CEO
Mr. Pramod. K. Sanghi	President Finance and CFO
Mr. R. P. Singh	President & Head, Global Product Management
Mr. V. Murali Krishna	Executive Vice President and Head, Sales and Marketing
Mr. Pankaj Bhatt	Executive Vice President, Global Delivery
Mr. Manu Arora	Vice President and Head, Human Resources

[Note: This transcript has been edited for improved readability]



Meenakshi Sharma:

Thank you, Sourodip. With New Year greetings, I would like to welcome you all to this Nucleus Software earnings conference call for the third quarter and nine months ended 31st December 2013. For discussions here, we have from the management team Mr. Vishnu R. Dusad, our Managing Director and CEO; Mr. Pramod K. Sanghi, President Finance and CFO; Mr. R. P. Singh, President and Head, Product Management; Mr. V. Murli Krishna, Executive Vice President and Head, Sales and Marketing; Mr. Pankaj Bhatt, Executive Vice President, Global Delivery; and Mr. Manu Arora, Vice President and Head, Human Resources.

Nucleus Software does not provide any specific revenue earnings guidance. Anything which is said during the call which will reflect our outlook for the future or which may be construed as a forward-looking statement must be reviewed in conjunction with the risk that the company faces. An audio and transcript of this call would be shortly available on the investors' section of our website www.nucleussoftware.com. With this, we are now ready to begin with the opening comments on the performance of the company for the quarter straight from the CEO, and post that we would be available for the Q&A session. With this, I may now pass it over to Vishnu.

Vishnu R. Dusad:

Thank you Meenakshi, good afternoon ladies and gentlemen. I am pleased to once again get in touch with you at this earnings call for the Third Quarter & Nine Months Ended December 31, 2013.

We are continuing to register a healthy growth in the current financial year. We are happy to share that our increasing penetration in new markets has given us a positive momentum. Additionally, with the objective of building capabilities for the future, we have been investing in new talent and nurturing the existing talent pool. Our focus on our people has been to ensure quality and achieving perfection while delivering world class products to our customers.

Let me take you through the numbers.

- **Our Consolidated revenue** for the quarter is at Rs. 89.96 crore up by 21% against Rs. 74.63 crore in the corresponding quarter previous year.
- **Revenue from product business** for the quarter is at Rs. 61.41 crore, 68% of the total revenue against Rs. 49.67 crore, 67% of the total revenue in the corresponding quarter previous year.



- **Product revenue from own business**, for the quarter is at Rs. 58.77 crore, 65% of the total revenue against Rs. 48.28 crore, 65% of the total revenue in the corresponding quarter previous year.
- **Projects and services business revenue** for the quarter is at Rs. 28.55 crore, 32% of total revenue against Rs. 24.96 crore, 33% of total revenue in the corresponding quarter previous year.
- **EBITDA** for the quarter is at Rs. 19.45 crore, 22% of total revenue against Rs. 12.51 crore, 17% of total revenue in the corresponding quarter previous year.
- **Taxes including withholding taxes** are at Rs. 1.78 crore against Rs. 3.61 crore, in the corresponding quarter previous year.
- **Net profit** for the quarter is at Rs. 23.39 crore, 26% of total revenue, up by 90% against Rs. 12.33 crore, 17% of total revenue in the corresponding quarter previous year.
- **EPS** for the quarter is at Rs. 7.22 against Rs. 3.81 in the corresponding quarter previous year.

For the Nine Months period ended December 31, 2013, our consolidated revenue from software products and services is at Rs.258.54 crore against Rs. 220.32 crore, 17% higher, year on year.

- **Revenue from product business** for the Nine Months period is at Rs.178.84 crore, 69% of the total revenue against Rs. 148.07 crore, 67% of the total revenue year on year
- **Product revenue from own business**, for the Nine Months period is at Rs.164.60 crore, 64% of the total revenue against Rs.142.94 crore, 65% of the total revenue year on year
- **Projects and services business revenue** for the Nine Months period is at Rs.79.70 crore, 31% of total revenue against Rs. 72.25 crore, 33% of total revenue year on year
- **EBITDA** for the Nine Months period is at Rs. 46.49 crore, (18% of revenue), an increase of 38% against Rs. 33.63 crore, (15% of revenue) year on year.



- **Taxes** are at Rs. 12.78 crore against Rs. 10.44 crore.
- **Net profit** for the Nine Months period is at Rs. 45.50 crore, 18% of total revenue, up by 31% against Rs. 34.72 crore, 16% of total revenue year on year.
- **EPS** for the Nine Months period at Rs. 14.05 as against Rs. 10.72 in the corresponding previous year.
- **Our total Current investments and bank position** is at Rs. 299.45 crore as on 31st Dec, 2013 against Rs. 290.01 crore as on Sep 30, 2013.
- In terms of **manpower**, we are at 1,532 as on Dec 31, 2013 against 1,562 as on Dec 31, 2012.

With this I would hand it over to Pramod for details on the financials.

Pramod K. Sanghi:

Good afternoon everybody. This is Pramod and I welcome you all to this conference call.

- **On a sequential basis, revenue** for the quarter is at Rs. 89.96 crore, 9% higher than Rs. 82.25 crore previous quarter.
 - **Product revenue for the quarter** is at Rs. 61.41 crore, 68.3% of the total revenue against Rs. 54.95 crore, 66.8% of revenue previous quarter
 - **Revenue from own Products** for the quarter is at Rs. 58.77 crore, 65.3% of revenue, against Rs. 52.36 crore, 63.7% of revenue, previous quarter.
 - **Traded revenue from products** included in this product revenue is at Rs. 2.64 crore, 3% of revenue for the quarter, against Rs. 2.59 crore,
- **Revenue from projects and services** for the quarter is at Rs. 28.55 crore, 31.7% of revenue, against Rs. 27.30 crore, 33.2% of revenue, previous quarter.
- **Overall Revenue in constant dollar term including India Rupee revenue** is US\$ 14.89 million for the quarter against US\$ 13.49 million in the previous qtr. **Excluding India Rupee Revenue**, the foreign currency revenue is US \$ 12.49 million for the quarter against US \$ 10.89 million in the previous qtr. India rupee revenue is Rs. 14.87 crore this quarter against Rs. 16.55 crore in the previous qtr.



- Overall **Revenue in foreign currency including India rupee revenue** for the nine month period is US\$ 43.62 million against US\$ 40.74 million in the corresponding nine month period. Excluding India Rupee Revenue, the foreign currency revenue for the nine month period is US \$ 34.77 million against US \$ 33.47 million. India rupee revenue for the nine month period is Rs. 53.26 crore against Rs. 39.71 crore in the for the corresponding nine month period.
- **Cost of delivery including cost of product development** is 59.6% of revenue, 63.4% of revenue in the previous quarter. In absolute terms this is Rs. 53.62 crore against Rs. 52.15 crore previous quarter.
 - For the nine month period, it is Rs. 160.23 crore (62% of revenue) against Rs.140.95 crore (64% of revenue) in the corresponding nine month period.
- **Marketing & sales expenses** are at 9.78% of revenue this quarter, against 10.25% of revenue previous quarter. In absolute terms, they are at Rs. 8.79 crore against Rs. 8.43 crore previous quarter.
 - For the nine month period, they are Rs. 26.00 crore (10.1% of revenue) against Rs. 25.77 crore (11.7% of revenue) in the corresponding nine month period.
- **G&A expenses** are at 9.01% of revenue this quarter, against 10.8% of revenue previous quarter. In absolute terms, they are at Rs. 8.10 crore against Rs. 8.84 crore previous quarter.
 - For the nine month period, they are at Rs. 25.81 crore (10.0% of revenue) against Rs. 19.97 crore (9.1% of revenue) in the corresponding nine month period.
- **EBITDA** is at Rs. 19.45 crore, 21.6% of total revenue this quarter, against Rs. 12.82 crore, 15.6% of revenue previous quarter.
 - For the nine month period, **EBITDA** is at Rs. 46.49 crore, 18.0% of revenue, an increase of 38.2% against Rs. 33.63 crore, 15.3% of revenue in the corresponding nine month period.
- **Depreciation** is at Rs.1.93 crore against Rs.1.78 crore previous quarter. For the nine month period, it is Rs.5.28 crore against Rs.4.58 crore in the corresponding nine month period.



- **Other income from investments and deposits** is at Rs. 7.77 crore against Rs. 3.61 crore in the previous quarter with significant FMP maturities in the quarter and full year income being booked. Other income includes foreign exchange loss of Rs.0.30 crore against a gain of Rs. 0.36 crore previous quarter. Dollar closed end of December at 61.84, against 62.89 at the end of September 2013. **Total other Income for the quarter** is Rs. 7.65 crore against Rs. 4.08 crore last qtr.
- For the nine month period, **Other income from investments and deposits** is at Rs.14.90 crore against Rs.11.24 crore in the corresponding nine month period. Foreign exchange gain for the nine month period is Rs. 2.00 crore against Rs. 3.83 crore in the corresponding nine month period. **Total other Income** for the nine month period is Rs. 17.07 crore against Rs. 16.10 crore in the corresponding nine month period.
- **Total taxes** are at Rs. 1.78 crore, 7.1 % of PBT against Rs. 4.18 crore, 27.6% of PBT previous quarter. For the nine month period, **total taxes are at** Rs. 12.78 crore, 21.9% of PBT against Rs. 10.44 crore, 23.1% of PBT in the corresponding nine month period. Taxes for the quarter are after effect of weighted deduction for R&D expenditure for calendar year 2013 subsequent to all approvals being in place.
- **PAT** is at Rs. 23.39 crore for the quarter, 26% of revenue against Rs. 10.94 crore for the quarter, 13.3% of revenue previous quarter. **For the nine month period** it is at Rs. 45.50 crore, 17.6% of total revenue, against Rs. 34.72 crore, 15.8% of total revenue in the corresponding nine month period.
- **EPS** for the quarter is at Rs. 7.22 against Rs. 3.38 previous quarter. **For the nine month period EPS** is at Rs. 14.05 against Rs. 10.72 in the corresponding nine month period.
- In terms of **foreign currency hedges**, on Dec 31 we had USD 8.75 million dollars of forward contracts at an average rate of 64.37. There is a mark-to-market gain of Rs. 92.10 lakhs which is taken to hedging reserve in the balance sheet. On Sep 2013 we had a total hedge of USD 9.15 million at an average rate of 60.60 and there was mark-to-market loss of Rs. 3.33 crore.
- **Revenue contribution from the top 5 clients for the quarter** is 40%. This is similar to 40% previous quarter.
- **The order book position** is Rs. 233 crore including Rs. 156.75 crore of products business and Rs. 76.50 crore of projects and services business. In Sep. 30, 2013,



the order book position was Rs. Rs. 220.41 crore including Rs. 129.56 crore of products business and Rs. 90.85 crore of projects and services business.

- **Total Cash and cash equivalents** as on 31st Dec, 2013 are Rs. 299.45 crore against Rs.290.01 crore as on 30th Sep, 2013. This includes balances in current accounts of Rs. 23.60 crore, liquid fund schemes of mutual funds Rs.111.88 crore, Rs.90.75 crore in fixed maturity plans, fixed deposits with banks of Rs. 54.16 crore and investments in tax free bonds of Rs. 19.06 crore.
- With regard to **receivables**, we are at Rs. 67.96 crore against Rs. 62.12 crore previous quarter. The DSR is 70 days against 69 days.
- During the quarter, **there is a gross addition of fixed assets** of Rs. 13.15 crore, consisting largely of Rs. 2.29 crore hardware and Rs. 10.86 crore software licenses purchased.

R. P. Singh:

Thank you Pramod and good afternoon everyone. Wishing you all a very happy new year, I am happy to announce that the new integrated transaction-banking product has gone live at one of our customers in this quarter. Two more are now expected to go live in this quarter. The new product covers the entire spectrum of transaction banking, i.e. Payments, Receivable Collections including EIPP which is Invoice Presentment and Payments, Liquidity Management and Financial Supply Chain Management. There is also good progress on the new FinnOneTM version that we have been working on. We have initiated three beta implementations which are part of the final test for the product. Hopefully, I will have more news next time when we connect.

V. Murli Krishna:

Thank you, RP. Wish you all a very happy and prosperous new year. Very good afternoon. This is V. Murli Krishna, VMK. I will take you through the sales marketing and alliances highlights for Q3. I am happy to share that we are continuing to register a healthy growth. Q3 has been a positive quarter for us and we have eight new product orders worldwide. This quarter, Nucleus Software completed a total of 31-product module implementation of our products across multiple geographies. Three new customers were added to the existing account of over 150 customers across the globe.

In the past quarter in the area of marketing and alliances, we continue to focus our outreach to key audiences across geographies through customized mailers, events and



webinars and in-person meetings. We reached out to our Philippines customers through an exclusive Nucleus Software hosted event in Manila. Our engagement with various analyst groups has also stepped up with a mobility webinar organized showcasing our mobility offerings. Nucleus Software also features various analyst reports like Forrester etc. Apart from this, we increase our momentum with marketing programmes across various digital channels for greater brand visibility and presence. The response we have been getting has been very encouraging and we continue to invest in more such outreach programme.

Finally, we added a feather in our cap by winning IR Global Rankings 2013 award. We were adjudged the third best ranked company investors relations website for India region in this quarter.

Pankaj Bhatt:

Thank you, V. M. K. Good afternoon, ladies and gentlemen. As V. M. K. mentioned, for the quarter ending 31st December, we did 31 product modules implementation across the regions. So for the three quarters ending on 31st December, we have completed 43 product modules including our transaction banking product. I am happy to inform that our transaction banking product implementation team set up earlier last quarter has started leading an implementation engagement with our customers in a close alignment with our transaction banking product team.

Manu Arora:

Thank you, Pankaj. Good evening, ladies and gentlemen and wishing a very happy new year. At Nucleus, we continue to focus on strengthening our investment in building world-class workforce and development initiatives. We have strengthened our relationships with key academic institutes in this quarter for longer-term effectiveness including the top engineering and management schools in India. This quarter, we have put in a special focus on strengthening, retaining and development interventions, a young leaders' programme, employee development plans and e-learning methodologies.

Jatin Khemani from Aadhar Securities:

Jatin:

How much of the 20% growth which we have achieved in INR terms, would be due to currency movements, in constant currency terms? The second question is about cash.



Has Board come to a consensus in terms of threshold level for cash beyond which shareholders could be rewarded through high payout or buybacks?

Pramod:

I will answer the first part of the question which is that overall revenue in foreign currency including India rupee revenue is USD 14.89 million for the quarter against USD 13.49 million in the previous quarter. On the cash part, I will ask Vishnu to answer on behalf of the Board.

Vishnu:

We will come back to you on this in the next quarter.

Dhananjay Mishra from Sushil Finance

Dhananjay:

In product segment, what is your outlook and also what is the addressable market size in core banking segment because you mainly represent in this emerging market segment? Also, if you could answer that in context of competition.

VMK:

In terms of product that we offer, there are basically two lines of products that we offer. One is on the lending side which is our flagship product called FinnOne™ and the other one is on the transaction banking side, the Cash Management side. These are the two products that we offer on the product side. On the services side, we offer a multiple types of services, application development services and so on.

We take these products and services globally to all potential customers which are primarily the banks as well as the non-banking financial companies. In terms of the market size, out there for us, is the universe of banking and lending organizations who need to buy system software or application software to automate either their lending processes or their cash management and they are all potential customers for us.

Dhananjay:

How is the deal pipeline looking like in these emerging markets especially?

Pramod:

We do not talk too much about pipelines and details of future revenue, which would be next question coming up. We are generally positive about both emerging and partially in the developed markets where we are currently.



Sanjeev from Sharekhan

Sanjeev:

Some more detail on the services order book on the services like and how did it come to this state?

Pramod:

We are a product company and we provide services for our larger clients. We do look for services as a line of business for existing customers. The order book is going down, but most services which we execute are booked and executed within a short frame of time.

Sanjeev:

Are you saying that you might see the services as a total percentage of revenue going to come down drastically in the next two-three years?

Vishnu

We would want to keep it at 70:30 ratio. Having said that, services may come down depending upon how the requirements grow at our existing clients. Another factor behind the services business is that we developed our capability to offer services in new technologies and they help us in our product development as well and that is the reason we are going to keep this ratio in this range.

Sanjeev:

What is the margin in services and product business?

Pramod:

Overall including the cost of development for the last some years, the margins have not been significantly different as such, but we do hope to get better margins in the product business going ahead. Product business should give us better margins but, as of now, our R&D cost has been high and we do expect them to result in higher revenues.

Sanjeev:

Most of the quarters you have been mentioning that the R&D cost would be continuing year-after-year. So when do you see that these costs would contribute higher to the margins and the margins would be similar to the other product companies?



Pramod:

The product business has been running at about a Rs. 50 crore run rate. And now this quarter, we are looking at a Rs. 60 crore run rate. We can only tell you after each quarter how we have done and then we have to take a call on that.

Sanjeev:

Any qualitative commentary on FY15 given that most of your peers is talking on optimism for FY15?

Vishnu:

We continue to be optimistic about FY15. We have good traction for our products across geographies. We are speaking to prospective and existing customers for upgrade etc. We are optimistic.

Sanjeev:

What would be the margin trend? Is it going to be similar to what we have seen in the last nine months?

Pramod:

For the nine months period, the margins are running at about 18%. We have done better than that in the past. We have also done lower at times, but we would like to maintain and improve that definitely.

Sanjeev:

What would you say constructively, you are reaching a stage where there will be lesser volatility in the performance going forward?

Pramod:

Actually, we have not seen much volatility. We have been a little constant in turnover and EBITDA for some time now.

Sanjeev:

Going forward, can we see a better growth perspective in next two years?

Pramod:

We would always like to grow and it is up to us how we address the market and make sure we grow at industry rate or better.

Sanjeev:

What is the tax rate and what kind of tax rates are we expecting for FY15?



Pramod:

We pay full taxes now and get an R&D credit. So it depends on the total profit as well as, other income component because our number of other income components like FMPs and Liquid Fund Dividend Schemes and Tax Free Bonds which are of course free of tax. But 25% to 28% should be a reasonable rate to assume.

Sanjeev:

What is the order book added from the new products and how many clients have you added?

Vishnu:

We have three customers as of now and we are speaking to number of our existing customers for deploying our mobility suite for their benefits.

Sanjeev:

The market that mainly you are seeing is the African market?

Vishnu:

We are talking to customers' right from Japan to America for the mobility suite.

Sanjeev:

In which markets have you added these three clients?

Vishnu:

In Africa, India and Southeast Asia.

Sanjeev:

Is the Board taking any decision on the usage of the cash? Last quarter, in the concall you mentioned about some acquisition with this cash. So are we close to that acquisition?

Pramod:

Our focus is on to increase our current business. We have been rather busy with product development and seeing new markets and we believe the result have started showing now. Acquisitions, while we may consider, but at this moment, they are not a high priority item for us.

Sanjeev:

So you will be using the cash for reasons other than that acquisition?



Pramod:

At the moment, the cash is reserved for it. But it does not mean it will happen immediately.

Dhiraj Sachdev from HSBC Asset Management

Dhiraj:

If you can elaborate the tax at 7% of PBT for the quarter while it was 27% last quarter. When you mentioned effective tax rate of 25% to 28%, for the nine months so far it's 22% with a total tax expense of Rs. 12.8 crore. Hence, in the fourth quarter we may see higher tax as an absolute amount?

Pramod:

You have to look at the nine months' numbers. The numbers for this quarter are affected because we have taken a full calendar year effect of the R&D deduction.

Dhiraj:

That has already been accounted for in the third quarter. Fourth quarter you will see normalization?

Pramod:

We received approvals in the last quarter only.

Dhiraj:

12% sequential growth in own product revenues have led to 600-basis points margin extension this quarter on a sequential basis from 15.5% to about 21.5% at the EBITDA level over the income. So, obviously, there is an operating leverage and product business has largely been flowing through the PBT numbers as well. Is the implementation going live got to do with lumpiness or is it far even spread throughout the quarter as the implementation gains momentum?

Pramod:

There may not be lumpiness in terms of implementations, but there can be lumpiness in terms of our new strategy of having additional licenses being given to existing customers. We have changed the model partially to limited licenses and therefore there could be lumpiness at times.



Dhiraj:

So largely it is recurring in nature unlike other product companies where license creates lumpiness in a quarter?

Pramod:

Not at the moment, I do not see lumpiness really. We are still at reasonably low numbers.

Dhiraj:

Geography-wise, which are the new geographies, which are contributing now and seem fairly positive?

Pramod:

The geographies Africa, India and Middle East are up this quarter. Japan is more or less the same. We are actually now looking at both emerging and developed markets as such to make sure that we grow.

Dhiraj:

Anything you want to update on mobility side of the business because it is a new thing that you had taken up in terms of product development for customers. How big is the opportunity?

Vishnu:

Not so big in terms of revenue. But in terms of value delivered to our customers, it is a pretty sizeable opportunity. All the three customers where we have implemented, they have been able to derive immense value for their business and we do hope that our other customers would also be able to derive the similar value or so.

Dhiraj:

It is a long pending question of utilization of cash. I hope the Board comes back in the next quarter with some decisiveness regarding the right utilization of cash for the benefit of all shareholders.

Vishnu

Sure. We will certainly get the message across.

Grishma Shah from Malabar Investment



Grishma:

The India rupee revenue for nine month ended Dec. 31, 2013 is around Rs. 53 crore versus Rs.40 crore for the corresponding nine month period last year. Is it primarily because of the services revenue?

Pramod:

In India, we do not have any services revenue. It is all revenue which comes from existing clients and new clients, which contributes to the product business. You can interpret that there are clients that like us and are satisfied customers.

Grishma:

But the dollar revenue seems to vary around 4-5%. So how are we seeing an uptake in that going ahead?

Pramod:

After a long time, dollar revenues have started moving upwards. Our revenues have gone down earlier as such and in the last quarter, we said that we have understood the fall and now finally this is rising.

Grishma:

How this growth is compared with the market growth for the segment that we are functioning in?

Pramod:

There are not too many players in this segment and some of them are yet to announce their results. So we will see. But I expect wherever we are strong, we will continue to do well in those markets in terms of market share also. There are still a lot of markets where we have one or two implementations only. So we still need to do a lot of work there.

Grishma:

Is it that we have re-launched our product or done a lot of work on the mobility side that is work for us or is it just that the market growth is coming back?

Pramod:

At the moment, the results are coming from the existing products and mobility has added great value to the customer, but it is not resulting in high revenues for us. We do hope that the additional revenues in the future will come from the new product launches.



Grishma:

Does the higher percentage of revenue still come from FinnOne™ and are witnessing good traction with Cash@will™ also? Is it, like, now 80:20?

Pramod:

As of now, the larger contribution continues to come from FinnOne™. But we do hope that in the coming quarters, transaction banking percentage will go up.

Grishma:

Any particular reason for that, I mean, are you seeing any changes on regulatory side that is impacting it or is the new version of our product much better than the earlier version that is helping us?

Pramod:

We are seeing greater demand and interest in cash management across several regions as such and the product capabilities contribute to that confidence.

Akash Vohra from Raj Investments

Akash:

Would you like to elaborate something on margin improvement? What was the main driver for that?

Pramod:

Increase in revenue has contributed. The costs have largely remained where they were in the last quarter as such. So we have stated over a period of time that when we leverage our cost-based adequately to get more revenue, there would be a flip to the EBITDA.

Akash:

So it is likely to be sustainable in coming quarters, sir?

Pramod:

It is difficult to say, but let us hope for the best.

Akash:

Last quarter, you had mentioned that we are going to focus on Africa, Middle East, Australia. Has the Company planned any targets for the revenue contributions from



those regions? Like, Middle East has 12% revenue contribution right now, one year down the line; does the company have any targets like 15% or 20%?

Pramod:

We do have targets for different regions which will be part of our budgeting exercise for next year. But I do not think we share them in that greater detail really.

Akash:

Do you see the shift changing more towards the upcoming markets like Africa, Middle East, Australia from the Southeast Asia or the share will be maintained for them?

Pramod:

We do expect more growth for the markets you have mentioned.

Akash:

But the shift will be seeing or the Middle East and particular region will maintain their share?

Pramod:

Well, the absolute numbers may be maintained, but some regions – Southeast Asia does move a little slower than other markets at the moment.

Akash:

This growth would be coming from product segment only?

Pramod:

Yes.

Meenakshi Sharma:

We thank all of you for joining us in this conference call. And with this, I would hand it over back to Vishnu for these closing comments.

Vishnu R. Dusad:

I would like to once again take this opportunity for your continued interest in Nucleus Software and I would like to reiterate our commitment to deliver value to all our stakeholders. Thank you very much.