



“KPIT Technologies Limited Q3 FY 2018
Results Conference Call”

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MANAGEMENT:

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MR. SUNIL PHANSALKAR - HEAD INVESTOR RELATIONS AND AVP M&A - KPIT TECHNOLOGIES LIMITED

- Moderator:** Ladies and gentlemen good day and welcome to the Q3 FY2018 results conference call of KPIT Technologies, hosted by Emkay Global Financial Services. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “*” then “0” on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Rahul Jain from Emkay Global. Thank you and over to you Sir!
- Rahul Jain:** Thanks Vikram. Good evening everyone. On behalf of Emkay Global, I welcome the senior management of KPIT represented by Mr. Ravi Pandit – Chairman and Group CEO, Mr. Kishor Patil, Co-Founder CEO and MD, Mr. Sachin Tikekar, Member Board, Mr. Anil Patwardhan, Senior VP Head, Corporate Finance and Governance and Mr. Sunil Phansalkar, Head IR and AVP, M&A. I would like the management to take us through Q3 FY2018 results. I now request Mr. Sunil to take it over from here. Sir over to you now!
- Sunil Phansalkar:** Thanks Rahul. A very warm welcome to everybody on the Q3 FY2018 earnings call. As you all would be aware we also had an important announcement yesterday so will cover the Q3 performance and that announcement in today’s call. One small change, Mr. Anil Patwardhan due to family emergency he is not able to attend the call so he is not on the call today. All the other management members mentioned are present on the call. As always, we will start the call with introductory remarks from Mr. Ravi Pandit and then we will open the floor for your questions. So once again a very warm welcome and now I will hand it over to Mr. Pandit.
- Ravi Pandit:** Good evening and welcome everyone. What I intend to do is that we will first spend some time going through the Q3 results and it would be nice if we can have the question answer on them after my comment so that we keep that aside and then we move to the announcement that we made last night.

On that announcement as well, we have some initial remarks to make so that should address some of the questions that you might possibly have in your mind and then we can have a question answer session on the second part.

Turning to the Q3 results, as you would have seen from our investor release, our Q3 revenue was kind of flattish although we had a year-on-year growth of almost 15% in dollar terms and 10% in rupee terms. Although the revenue was kind of flat as compared to the earlier quarters, the growth in the absolute EBITDA was about 9.5%. The growth in the profit on a quarter-on-quarter basis was 3.5% but as you would notice, it was largely on account of forex changes and if you were to look at the profits, PAT on a year-on-year basis there is a decline of 16% but if you take out the unusual items then there is actually a healthy growth.

Turning to the question that I am sure must be in your mind. How is it that the revenue is flat? There is an increase in the EBITDA. There are two factors which are behind it, one is the change in the composition of our revenues and the second thing is the change in the cost structure. Let me first turn to the change in the composition of revenue. As you would notice in this quarter as compared to the last quarter, our engineering sales went up by 2.8%, our overall digital sales went up by about 4%, whereas our product sales went down by about 2%, so the drop in the product sales was made up by the increase in the services, sales of engineering as well as in DT. The profitability of the engineering services and DT is good whereas the profitability of products was not good and therefore even with flat revenues our profits have gone up.

The second thing is the change in the cost structure. As you would have noticed that although the revenues from services have gone up reasonably well, the FTE number is practically the same and we have spoken to you earlier when we have said that our whole focus over the last three four quarters has been to bring our FTE numbers in line with our revenues, we have done reasonably well on that count in the earlier two quarters and we have continued to do well on that account. Therefore, there has been change in the cost structure. So, it is a combination of

the change in the revenues composition and the change in the cost structure that has given us the increase in the profitability.

There is also some increase in the SG&A, which has also been a feature of this quarter. So, this is as far as the profitability is concerned, and the last point that I would like to make about Q3 is the DSOs. Our DSO has crossed 73 days in the last quarter to 71 days in the current quarter and as you would have noticed from our release our net cash accrual continues. This is about the result of the Q3.

Generally, at the end of Q3, we give an indication about the Q4. Now the indication is that Q4 should see a moderate growth in the revenues as well as in EBITDA. We believe that in line with the trend of the three quarters, our annual rate of revenue growth should be anywhere between 13% and 14%.

So, these are the preliminary comments that we had on the Q3 and we shall be happy to take any questions if you have on this. And once we are done with that and we can turn to the other aspects about the announcement that we made recently. We would look forward to your questions.

Moderator: Thank you very much Sir. Ladies and gentlemen, we will now begin the question and answer session. We have our first question from the line of Nirav Dalal from May Bank. Please go ahead.

Nirav Dalal: Thank you for the opportunity. Just wanted to know why the weak outlook for Q4 and second thing was wanted the subcontractor number for this quarter?

Kishor Patil: I think what we had said is we will have a moderate growth in Q4, so it is not a weak outlook. We will have a growth in Q4 and we will also have improvement in the margins during Q4 as we have also shown in Q3 and that improvement will continue. So, we believe that it is not a weak outlook it will be a growth quarter with improvement in margins.

- Nirav Dalal:** Okay and Sir comments in terms of the products, do you see that the energy and utilities has increased and there is an increase in the product so is the two related?
- Kishor Patil:** No, the two parts are not related, we have services revenues coming from energies and utilities as the market energy turns around as we are seeing some growth coming from energy and utilities. As far as the products are concerned, there is substantial growth year-on-year. It is just that there was tremendous amount of growth that we reported in Q1 over the last year so right now it is normalizing a little bit but year-on-year there is healthy amount of growth in products.
- Nirav Dalal:** No if I were to just exclude the SI bit from the products and platforms you have done about 4.2 million this quarter, which was like 2.9 in the last quarter and I saw an increase in the yield so that is the reason I was just matching the two?
- Kishor Patil:** Both are not related.
- Nirav Dalal:** Okay. So, the uptick in the products and platforms outside of SI if you could comment on that what is the outlook going ahead?
- Kishor Patil:** See we do not comment on individual products and etc., but this is largely in the area of diagnostics and that is more to do with our automotive and industrials customers.
- Nirav Dalal:** Okay and if you could give the services number for the quarter the cost?
- Sunil Phansalkar:** Just give a minute we will pull out, we can move out to a question and I will come back, I just give you the exact number.
- Nirav Dalal:** Sure. I am done.
- Moderator:** Thank you very much. We have the next question from the line of Apoorva Prasad from HDFC Securities. Please go ahead.

- Apoorva Prasad:** Thanks for taking my question. Could you split out margin profile across the segments, PES India and the other pieces please? And if you could talk about how it has moved in the past years?
- Kishor Patil:** Generally as we have been saying over the last year if you see the margins have been steadily improving quarter-on-quarter, if you look at a broad breakup then margins in PES are slightly higher than the overall IT business but obviously we have made a majority of the R&D investments fresh investments have happened in the PES business where we should see a good improvement in margins going ahead because we will utilize these freshers and we will see the benefits of those investments. So as of now the engineering margins are a tad better as compared to IT as of now but obviously the growth in the engineering margins could be more than the growth in the IT margins going ahead.
- Apoorva Prasad:** So this would be at about mid teens now?
- Kishor Patil:** Should be around early teens right now.
- Apoorva Prasad:** Okay, got it. Thanks.
- Moderator:** Thank you Sir. We have the next question from the line of Sangam Iyer from Subhkam Ventures. Please go ahead.
- Sangam Iyer:** Just a follow up on the earlier question asked. Sir I wanted to understand going forward when we talk about the levers for our margin expansion where from are we looking at, should we see the gross margins expanding significantly from hereon which would lead to our overall margin expansion?
- Kishor Patil:** Yes, so we have two major levers. One is we do look forward to improving the gross margins both on account of change in the mix of the revenues, better quality of revenues as well as some operational efficiencies and the second is we see a significant lever next going forward on the SG&A also where we believe that the

growth which we have can be leverage without any addition, if not little less cost, so I think these are the primary leverage we see.

Sangam Iyer: So, from a SG&A leverage perspective do you see another say may be 100 basis points or so or more leverage that you see there at the SG&A front which can act as a margin lever for us?

Kishor Patil: So at least a percent or a two that is possible depending upon the growth because there is no additional cost, which would incur so that is what we would see next year.

Sangam Iyer: Okay, so that should be visible throughout the year or towards the end of the year when the growth comes back?

Kishor Patil: I think we have been reporting growth quarter-on-quarter stronger growth, so as the growth comes in I think that leverage you will see.

Sangam Iyer: Got it. Sir so this quarter I was just going back to your explanation on the margin expansion that happened, when we looked at it, it was predominantly from the SG&A and this in where we got the margin lever because at the gross margin level in spite of product mix changing towards more engineering services our gross margin did not expand to that extent, it was more on the other expenses where we have actually seen the leverage coming through so just wanted to understand since you said that product business have better margins and that is what flowed down in the margin expansion in spite of the revenues not seeing that kind of growth?

Kishor Patil: We said our engineering margins are a tad better and this quarter the mix changed in favour of engineering. If you look at engineering there was a growth in engineering so that was one reason. I think the expansion in margins happened at the gross margins level because if you see the utilization has also marginally gone up and there has been a little increase in SG&A expenses during the quarter. So, the expansion was at a gross margin level mainly because of change in business mix and because of better utilization.

Sunil Phansalkar: Just to come back to the earlier question, Nirav the subcontracting cost during the quarter was about Rs.940 million.

Sangam Iyer: Great Sir. I will come back in the queue.

Moderator: Thank you very much Sir. Ladies and gentlemen as there are no questions in the queue I would hand the conference over to the management for the comments on the event. Over to you Sir!

Ravi Pandit: Thank you very much. Let me turn to the announcement that we made last night about the restructuring of the company. What I would like to do is to take you through the logic of the transaction. I would also like to take you through the actual transaction steps and the timeline. Then I would like to talk about the reason for this mechanism. I would talk about why we have chosen the partner that we have chosen. I would like to talk about at the end of this what would be the IT company like, what would be the engineering company like and then we will talk about some of the other details on which we have received some questions.

Coming to the basic rationale of the transaction, so if you look at the revenue profile of KPIT, we have two streams of income. One is the business IT income, which includes our ERP consulting, which includes PLM, which includes the maintenance work that we do, the IMS works that we do the digital work that we do. That is one stream. The second stream is the engineering, which is predominantly automotive, electronics, embedded software development and with a little bit of mechanical and some digital. So these are the two streams of revenue that we have. In the first case, we are more of an IT services company, whereas in the second place we are more of an ER&D company. The number of customers who receive both these services from us is probably 2% to 3% of our total number of customers and even within those customers the buyers are necessarily different and what we have found is that this mix sometimes confuses our identity and it does not give any significant benefit in these customers.

On our IT side, we have hardly any automotive customers and on the engineering side we have hardly any non-automotive customers. This confusion in the mix of the services also as you can imagine effects our valuation. So, this has been one of the reasons why we thought it is important for us to segregate the two. We also believe that if we segregate the two we can give adequate management attention to each of the two streams and then we can have two separate entities each of which can grow substantially and be known well in their respective domains. So that has been the basic thought process.

The steps that we are looking at are therefore get in association or get into a merger with the company, which is focused on IT services, put the two companies together then demerge the company so that one can be a business IT company and the second one can be an engineering company and with a view to do that transaction the law requires that before that we have an open offer so that those investors who prefer to go through this would continue and see value in this will continue and those who do not will have an option of selling their shares, which the promoters can buy.

Therefore, we are essentially talking about three steps. First is the open offer. So, this is open offer for the shares of the entire KPIT Technology as we stand today. That is the first step. The second step is the merger between KPIT and Birlasoft. The third step is the demerger where the engineering business is taken out but it is done by giving almost like a bonus share for every shareholder of KPIT Technology and that share will be the share in the engineering business. There is no swap it is an extra share issue and the shareholding of the IT Company will be reflected into the engineering company. So, this is the mechanism that we are using. This is a mechanism, which will be spread over a period of time. We made the announcement yesterday. We have submitted our papers to SEBI and the whole initial process of their clearance etc., would take two three months, after that the open offer will open and it will stay open for a few weeks as required by the law, post that the open offer will conclude after that we will go for the NCLT approval,

after the NCLT approval we will go for the necessary internal mechanism of AGM or the sanction from the shareholders and then the actual effect will happen.

After the demerger happens, a new company will be formed for engineering that engineering company will be listed and the shareholders of KPIT Technologies will be given the shares of the listed company. The current name of the KPIT Technology's business IT area will change to Birlasoft and the ER&D Company's name will become KPIT Technology. So, this whole process we expect to take anywhere between 12 and 18 months so we are looking at the next three to four quarters minimum, as a continuation of our current way of doing business. So, you would see KPIT Technology as it is operating for the next 12 months. The change will happen sometime towards the end of the next year and the change will be fully effective in the year thereafter so I just thought it would be important for us to put the steps in the place and mechanism of the steps.

We have been advised that this is the more tax efficient and time efficient mechanism, which is why we have gone in for this. Now I want to turn to the question as to why did we choose and how did we choose Birlasoft? Now there are a couple of issues that we need to talk about. We believe that from the perspective of customers as well as from the perspective of our employees a certain type of company is important for us to merge with. We were not very keen to merge with a very large company because our customers are used to getting the attention that a mid-sized company gives to them. And we thought that we would rather look for a mid-sized company than a large company. We have found many merits in working with Birlasoft. First this is the part of the Birla group and we believe that it would have long-term interest in the company, which will take care of our customers.

Secondly if we were to look at the offerings that these companies had Birlasoft is a focused IT services company. Within IT services their offerings are very complimentary to us. In our case the ERP revenues are almost 60% of our total revenues whereas in their case the non-ERP revenues is especially the digital and application development revenues are 85% of their revenues, so the two companies

put together in the business IT area will be giving complete end-to-end solutions on the IT services area. We believe that the knowledge and the depth that they have in digital revenues will add more value to the digital technology revenues that we are having and therefore we can be very well known in that segment also. As we have mentioned in our calls earlier as far as the ERP is concerned we are already recognized as very good partners, platinum partner for some of the major ERP providers and therefore we are strong on that wicket but with this we will be stronger on the non-ERP as well.

Secondly the verticals of the two companies are also complimentary. We work largely in the manufacturing and energy domain, Birlasoft also works on manufacturing but they also work on BFSI. Now the new digital technologies are very relevant to BFSI and we have not been able to take these services to the BFSI customers. We believe we will be able to do that going forward.

So, this is as far as the complementarity of the offerings or the verticals are concerned, but as important as what you offer is the person that we work with and I would like to here talk about the leadership that is currently there in the Birlasoft. Now many of us know that Birlasoft has been operational for many years. Many of us know that GE was one of their major customers and what I would like to bring out the changes that have happened in the last two years. And I would like to talk about the new leadership team led by Mr. Anjan Lahiri and then we spend a few minutes on Anjan.

Anjan started his career with Wipro then he worked with Cambridge Technology Partner, which as you would recollect has been known as the high-end IT, strategic consulting company and he spent three years with that and he has an extremely good consulting aptitude and consulting ability. We believe that the kind of technologies that we have built over the years will get substantial boost if we can give a technology edge to it and we believe that with Anjan and his team we should be able to do that.

Secondly Anjan after CTP was one of the Founder members of Mindtree and we had been always very happy about the culture that Mindtree has and which is what Anjan reflects it is a culture of openness, culture of vibrancy, a culture of ambition and also a culture of taking care of the customers and the people and we are very happy with that and we feel comfortable in working with such a leader from the perspective of our customers as well as our employees.

So Anjan led the Mindtree operations in the US. He then led their operations in the Europe subsequently he was the head of all their business IT services and he handled a large chunk of Mindtree business and in each of the areas, he did very well. So, we feel comfortable about the leadership, we feel comfortable about their ability to bring results, to work in a consultative manner with customers and to take care of our customers and employees and that has been one of the major reasons why we think that together the companies can do well growing forward.

As a company Birlasoft has done good revenue growth better than ours especially in the business IT area over the last two three years. Their margins are better than ours at around 14%. They have significant cash on their balance sheet more than 300 Crores. So, all these things put together, I think give us every reason to be very happy about this partnership and that is a reason after looking at multiple companies after evaluating multiple companies, we have chosen to go with Birlasoft.

Now let me just turn to the question as to what kind of an IT company we will have going forward and what kind of an engineering company we will have going forward? I believe that the IT company which will be called after the year Birlasoft will become amongst the largest midcap IT company with core focus on digital. I believe that it will have a proper mix of ERP and digital revenues. We believe that we will be able to service customers both in BFSI as well as the manufacturing, it would have a balanced portfolio and a starting revenue of \$500 million, which puts in the possibility of bidding for decent sized contract in the IT domain.

Our engineering company will be sharply focused on the automotive engineering and as you know we have been speaking about the automotive world is up for a major change, almost all those changes in that world are driven by software. We are very well known in that domain. We work with at least 15 out of the top 20 global OEMs. We also work in practically every cutting-edge area on automotive electronics. We have good potential of growth and as Sunil mentioned in his earlier comments better profitability. We also believe that we will be able to do very good brand creation to attract talent globally. We are also attracting talent in the area at board level and we believe that this provides with a very sharply defined, highly focused entity in the times to come. We are also beginning to see some revenues coming out of licensing as well as product sale.

This is what we think our IT Company will be and our engineering company will be. We believe that with these two entities, we should be able to provide room for growth to both and we feel that in both of them there would be a significant value creation. Now there have been questions asked to us about why is it that when the current market price is in excess of 200 the open offer price is little over at 180? Now the open offer price is determined on the basis of SEBI guidelines and that is on the basis of last 60 days average of the highest on each of those days and we have gone by that. Admittedly that price is lower than the current market price but we have to recognize the fact that the actual open offer will take some time before it opens. It might take three to four months. We do not know what the prices at that time could be and therefore we have gone by what is legally required. That is as far as the open offer price is concerned.

Then there have been questions about the valuation of Birlasoft. You know that Birlasoft is a Private Limited Company. I talked about their numbers. They are at about \$120 million to \$130 million revenue. Their growth rate as I said are better about 13%-14% on the IT side and totally of course, their EBITDA margins are around 14% and their cash on hand is better. So, the valuation of the two companies has been done on the basis of (a) KPIT valuation on the basis of the market price on the day on which we did it and the Birlasoft on the basis of the

valuation of the earnings after taking into account the variations that are there, the valuation has been done by a big four companies and that is how we have arrived at that numbers.

The reflection of the share exchange etc., is actually dependent on the number of shares that the two companies have but the basic enterprise value is based on this basic principle that I spoke to you about. After the demerger we will continue to have interest in each of this company, so one or more of us will continue to be on the board of directors of the IT company and some members from the IT group will continue to be on our board. We will continue to hold shares in the IT company for the period of time and we want to ensure that this whole transition happens smoothly an over a period of time. We would also like at the same time to ensure that our time spent of the management team that comes with the engineering area would get sharply focused on engineering whereas the team that goes on the IT side will focus on the IT area so that should help us achieve the objective of gaining focus on both these areas.

I would like to close the remark by talking about the timeframe. So, the transaction has been announced yesterday, so obviously nothing will happen during this current year, so you would see ourselves, KPIT Technologies in the way we are, in the year 2017-2018. As I mentioned to you even next year, the entire operation will continue more or less, the same way for another ten eleven months so any change that might happen will happen towards the end of year 2018-2019. So, when you look at KPIT Technologies operations in 2018-2019 you might want to say that for most of the year the operations will be on the same lines as they are now and the real merger and demerger will become effective almost at the end of the year 2018-2019 and thereafter in 2019-2020 we will be two separate companies running differently. Our working so far showed that in the year 2019-2020 everything that we have done so far would ensure that both the companies will have EPS accretive future. With that I would like to close my comments about the overall deal structure of the deal etc., and we will be happy to take questions from you. Thank you.

- Moderator:** Thank you very much Sir. Ladies and gentlemen, we will now begin the question and answer session. We have a first question from the line of Nirav Dalal from May Bank. Please go ahead.
- Nirav Dalal:** Thank you again for the opportunity. I just wanted to have some clarification in Birla numbers because if I were to see the FY2015 and 2016 numbers they are close to \$160-\$165 million in those two years and now you talking about \$150 million so just wanted why the difference in the numbers?
- Sunil Phansalkar:** So as Mr. Pandit mentioned Birla had GE as a major customer at a point of time and in last two years their revenues from GE were about 65%, last year they sold back that business to GE and basically that is why that significant business was actually sold and they replenished that with the new business so that is why it is there, so the growth which we are talking about has been consistent on the business excluding naturally the business which they have sold.
- Kishor Patil:** So, the decision regarding terminating GE business was on the basis of the profitability of that area, in two years' time they brought it down from 65% their revenues to single digit revenues and they were rapidly able to ramp up their non GE business and we were particularly actually impressed by that because you know there is another company who showed such courage to reduce the GE business in order to ensure that the right quality of the business is brought in.
- Nirav Dalal:** Okay so because their margins are that time around some 13% EBITDA margin which now has improved to 15% so that is the reason the margin improvement as well as the absolute revenue decline but improvement in other revenues?
- Kishor Patil:** Correct.
- Nirav Dalal:** Thank you.
- Moderator:** Thank you. We have next question from the line of Avro Raichoudhary from SKS Capital. Please go ahead.

Avro Raichoudhary: Thank you gentlemen for taking the time to explain in detail the structure of the deal and also your results and I really appreciate that. One question about the IT business or the Business IT as you referred to it, the combined entity of Birlasoft and KPIT's IT services business that will only cater to application development and maintenance and services and delivery if I understand and the products side that you focused right now will completely go with the engineering division, which would be renamed or relisted newly listed as KPIT Technologies if I correct?

Ravi Pandit: Yes, that is true.

Avro Raichoudhary: So what if somebody could approach the question this way that now you have more optimized diversified portfolio where you have a mix of more niche product facing division earning you higher margins and that was outweighing some of your standard or in lines with the industry fairly ordinary results on the IT services side, I am very cognizant of the pressures that IT industry whole is going through. So even you had a good mix of a product and services you are completely letting the product side grow how are you planning to meet the headwinds with this combined IT services business, going beyond the complementarity between your verticals as a whole how do you, what are your plans to improve your margins given rise in salaries in India and price pressures from clients abroad the fees are backlash and overall anti-outsourcing globalization backlash?

Ravi Pandit: So if I understood correctly your question and I will just repeat it so that you are basically talking about the IT part of the business, which is combining of KPIT's IT business and Birlasoft business specifically in the line that our product engineering business and product and platform business will be in the new company. So, on the IT side we believe that the areas in which we are working, I think specifically led by the digital part will be a growth driver. Now currently we are largely focused in the digital area and mainly in the areas of IoT, specifically because our focus has been in the manufacturing area. We have very good skills in that area, which will remain with the IT Company. More so I think we have got many other digital competencies, which are more relevant to the verticals outside manufacturing. In

line with the current strategy of KPIT not to go after these customers that is what we do not have go to market strategy for those verticals. Now that is what will be added or will be complimentary from this merger, which will allow us to grow in that path. The second thing as we talked about the consulting capabilities, which will also allow and bring a very good business mix between the ERP and the non-ERP revenues. Currently we have very good quality of customers and I think our opportunity to cross sell into that specifically more digital capabilities is also high that we will be in a position to do it. Also, the fact that on the IT side, in KPIT, relatively our portfolio is limited in Europe where Birlasoft has some better presence on the Europe side also so I think there is a complimentary base because we have a better presence in terms of KPIT IT in terms of Asia while Birlasoft has better presence in terms of Europe for this and US is a big market for both of us. So, I think there are multiple ways in which this can be done, and from the IT margins also we have shown improvement and we believe there is a further room to improve specifically looking at the areas in which we are so I think in all it will be a better growth engine and a better margin portfolio going forward.

Avro Raichoudhary: Thank you. My last tail question is just a clarification; you mentioned that there is 2% to 3% overlap between customers if I did not hear it incorrectly?

Ravi Pandit: Yes, 2% of our customers where we have we provide both the IT services as well as the engineering services.

Avro Raichoudhary: So you feel that since its fairly minimal it makes sense to cut it down?

Ravi Pandit: Yes.

Avro Raichoudhary: Thank you very much Sir. Good luck to you.

Moderator: Thank you Sir. We have a next question from the line of Ashish Chopra from Motilal Oswal Securities. Please go ahead.

- Ashish Chopra:** Thanks for the opportunity. Sir could you just elaborate a little bit more on some of the financials of Birlasoft in terms of what could be the earnings number for them?
- Kishor Patil:** As we said the EBITDA numbers are about 14%, their growth has been in the 14%-15% range over the last three years if you look at the profit numbers this should be typically in the 8% to 9% bracket.
- Ashish Chopra:** I think the question really here was that if you look at the kind of dilution that is being brought about so would probably fetch valuation of Birlasoft north of I think \$225-\$230 million so just wanted to know what would be the basis for that because it looks like a slightly higher valuation versus our own IT business which is probably \$350 million and that could be a concern from the perspective of minority shareholders?
- Ravi Pandit:** As we said earlier the valuation has been done by a big four, now there are two three areas while doing the valuation of Birlasoft we are looked at the valuer has looked at the comparable companies of that size, what are their valuation and as we said earlier their growth rate in the range of 14%-15% is a high growth rate and on the IT side as compared to our growth rate and also their margins are also higher side, 14% consistent EBITDA margin they have been able to show so I think the multiples are similar but just because the margins are high, the growth rate is high and also the net cash positions they have no debt on the balance sheet. Cash is in excess of Rs. 300 Crores on their balance sheet so I think these are the three factors, higher growth rate, higher margins and better cash position with no debt where the valuations have been made.
- Ashish Chopra:** Okay, 300 Crores net cash is what you said right?
- Ravi Pandit:** That is correct.
- Ashish Chopra:** Okay that is helpful. And secondly just on the last bit following the demerger so the swap of shares between the promoter on engineering and IT services just your

thoughts on, do you expect it to be a one-time exercise or a sporadic one spread over a period of time how do we envisage that to take place?

Sunil Phansalkar: We will do it over a period of time, we will do something initially and we will do other over the period, over next two years and the purpose is basically we have common understanding, common management to some extent while operationally we may have a little more management bandwidth in the engineering and they would have more on the IT side basically this will ensure that both companies remain interested in both the parts of the business during the integration period and the integration is better and the value creation is persistent. And the second thing as Mr. Pandit mentioned every shareholder will have another share in the engineering side, so absolutely the value creation will be of the mirror of what will be in IT or engineering in terms of shareholding.

Ashish Chopra: I will come back in the queue. Thanks.

Moderator: Thank you Sir. We have a next question from the line of Mayank Babla from Dalal & Broacha Stock Broking Private Limited. Please go ahead.

Mayank Babla: Thank you for taking my question. Sir I just wanted one clarity on the I mean accounting clarity what will be the shareholding pattern like between KPIT and Birlasoft or as far as both companies are concerned after the deal is that?

Sunil Phansalkar: As we have said the swap ratio is about 22 shares of KPIT for every nine shares of Birlasoft that is how the merger consideration will happen.

Mayank Babla: Okay and in KPIT Tech after this, in the engineering company?

Sunil Phansalkar: So, this is what will happen in the combined entity and the merger and demerger are simultaneous mirror shareholding would be there present in the engineering company initially as on date of the demerger. Every shareholder in the combined entity will get one share in the engineering entity this will be an additional share like a bonus share.

Mayank Babla: Thank you.

Moderator: We have a next question from the line of Vaibhav Badjatya from HNI Investment. Please go ahead.

Vaibhav Badjatya: Thanks for providing this opportunity. Sir I have one question on the whole merger scheme, Sir instead of merging Birlasoft into the existing KPIT and then converting that company into two different listed companies would it not has been have been better to first demerge the IT services of KPIT and then merge Birlasoft into that would that have been simpler process, in your view what is a consideration that has driven the management decision regarding this way of doing than the other way of doing?

Ravi Pandit: We have been advised by people that the mechanism that we are going through now is more efficient in terms of time as well as in terms of processes apart from a tax perspective.

Kishor Pati: Also the other part is once we demerge we will have to find a home or a partner for our IT business so this basically takes down the uncertainty and we have a partner in place, while we are going through this process I think that makes this whole process more smoother.

Vaibhav Badjatya: Okay fair enough. That is it from my side. Thank you.

Moderator: Thank you. We have the next question from Shekhar Singh from Excelsior Capital. Please go ahead.

Shekhar Singh: Sir just wanted to know like the promoters of KPIT they have been reducing their stake over the last two – two and half years so now with will open up for increasing the stake so just wanted to know like did this Birlasoft merger was it there in the works or is it something which just took as surprises?

- Ravi Pandit:** See I do not know which data element you are looking at our main shareholder is Proficient, through which we are holding the shares, to the best of my memory we have never sold a share of KPIT so you might want to recheck your data point.
- Sunil Phansalkar:** There could be one thing where earlier if you look at the promoter holding the employee welfare trust was included as part of promoter shareholding, the reporting rules changed and the shares held by the employee shareholding trust are not now reported as a promoter group holding so they have been taken out, the trust owns around 4% plus shares in KPIT. Apart from that, actually last year in March the promoters increased their stake, they bought a stake of around 2.2% about a year and half before and they have been increasing stake, so there is no decrease in the stake. It is actually, just a reclassification of the employee welfare trust if you are looking at that number.
- Shekhar Singh:** Yes, right may be basically because of that employee welfare trust. Thank you.
- Moderator:** Thank you Sir. We have a next question from Rahul Jain from Emkay Global. Please go ahead.
- Rahul Jain:** Sir, just on the valuation part can you say that what would be the EBITDA multiple of the respective organization that would be part of the non-engineering business piece?
- Sunil Phansalkar:** I think currently as we have said the ratio, which we explained earlier that is the ratio in which the merger consideration will flow, the EV to EBITDA ratios would be about 9X for both the businesses.
- Rahul Jain:** Okay so you mean to say if we do the reverse maths it would look like 9X EV to EBITDA on both the deals?
- Sunil Phansalkar:** So it is based on sustainable EBITDA of FY2018 for both the entities.

- Rahul Jain:** Okay and secondly there is another comment in terms of how the gross holding would shape up and the sole ownership would be, how the stake would move so any color you could give on that front?
- Sunil Phansalkar:** As we said, I mean we can obviously can sit and do the maths as to, if we have this as a merger ratio what will be the shareholding look like at the time of merger and at the time of the demerger and as we have said over a period there would be change in the shareholdings as far as the KPIT promoters are concerned and Birlasoft promoters are concerned, where there will be majority of shareholding of KPIT promoters in engineering and majority shareholding of Birlasoft promoters in the IT company over the next two-two and half years.
- Rahul Jain:** That is it from my side. Thank you.
- Moderator:** Thank you Sir. We have a next question from the line of Deepesh Mehta from SBI Cap Securities. Please go ahead.
- Deepesh Mehta:** Sir just one question how many number of outstanding shares are there in Birlasoft and what would be the cumulative shares post the transaction of the combined entity?
- Sunil Phansalkar:** So they have about 31.4 million shares outstanding.
- Deepesh Mehta:** And then based on share swap one can find the shares about a combined KPIT?
- Sunil Phansalkar:** Yes.
- Deepesh Mehta:** And their face value are the same right?
- Sunil Phansalkar:** Rs.10 face value for Birlasoft and Rs.2 for KPIT.
- Deepesh Mehta:** Thank you.

- Moderator:** Thank you Sir. We have next question from the line of Ritesh Poladia from Girik Capital. Please go ahead.
- Ritesh Poladia:** Sir does Birlasoft has any engineering business?
- Sunil Phansalkar:** No.
- Ritesh Poladia:** So after the demerger in the KPIT there would not be any revenue flow from the Birlasoft?
- Sunil Phansalkar:** No there would not be.
- Ritesh Poladia:** Okay. The new share to be issued to Birlasoft for the merger the number of shares would be 7.66 Crores is my calculation right?
- Sunil Phansalkar:** It will be roughly in that range, assuming there is no tendering in the open offer so there is some tendering in the open offer that number will change.
- Ritesh Poladia:** Sir this entire complex arrangement can you say that KPIT is actually selling the IT business to the Birlasoft and this is more tax efficient way?
- Kishor Patil:** I think the whole thing is meant for two three reasons, No.1 is basically to make sure that as Mr. Pandit mentioned too do this in a more efficient in terms of time, tax and cost perspective. The second thing, which is very important, is when you do this there is proper clarity in terms of how the management will be there and there is no uncertainty. No.3 a better transition of customers and employees so this has been done in multiple ways and fourth naturally this was run as one business so whatever the synergies are they maximize on this in this year. So that is the main purpose of all this arrangement.
- Ritesh Poladia:** Sure Sir. Sir as per the demerger I believe KPIT promoter would buy the Birlasoft share in the new KPIT is that understanding right?
- Sunil Phansalkar:** It would happen over a period but yes.

- Ritesh Poladia:** So again at that time there would be open offer for the minority?
- Sunil Phansalkar:** So, it depends on the way in which we purchase. Of course, we do it as a larger stake at one time, it might trigger an open offer but it all depends on the how we purchase it over a period of time.
- Ritesh Poladia:** Is the same thing would happen in the new Birlasoft where Birlasoft promoter would buy out the KPIT promoter?
- Sunil Phansalkar:** Again the same answer it depends on how that sale purchase happens.
- Ritesh Poladia:** But the promoter would exchange their shares that is there?
- Sunil Phansalkar:** That will happen as we said but it is not an one-time event. It will happen over a period time.
- Ritesh Poladia:** Sure. That is all from my side. Thank you Sir.
- Moderator:** Thank you Sir. We have a next question from the line of Moiz Tambawala from Florintree Advisors. Please go ahead.
- Moiz Tambawala:** Good evening everyone. I have a question on the margin while you have mentioned Birlasoft is at about 14% on the KPIT business in several quarters back in one of your investor releases you had mentioned that the product engineering services were a 20% margin business and I think right now only you indicated that that is somewhere in the low teens 13%-14%-15-odd% so the overall margins of the company sort of remained same so what exactly has happened? Why has product range even sort of come down and which other margins have come back up so that the overall margins are sort of same can you walk us through that?
- Kishor Patil:** Absolutely. So if you really look at we have given this profile how we will improve the margins quarter-on-quarter and we are doing it over last four quarters exactly in line with what we have said. In spite of currency headwinds, we have been in a position to improve the margins and even during the last quarter even now if you

see we have improved our margin in spite the revenues being stagnant. Now in case of engineering side your question we have two parts of the engineering one is engineering services and the second is the products and platform. Engineering services do not have a 20% margin. What we would have said is that the possible that what is possible in the services margin to go beyond 20% margin but we are not there at this point of time but we are much higher than the overall company margin in the IT services but net off investments into product those margins are into the low teens that is how I would explain.

Sunil Phansalkar: I think 20% number which you might have read I mean as we said it is investment into product, investment into normal R&D for the engineering business, which is about 3%--4% so which is all charged to the P&L and we might have said that number excluding these R&D investments and product investments and the number, which we said today was including everything.

Moiz Tambawala: Okay got it. And the number of business IT would be around 10% margin that we expect?

Kishor Patil: We are looking to improve that and as we said every quarter we are showing that improvement.

Moiz Tambawala: Thank you so much.

Moderator: Thank you Sir. We have a next question from the line of Vaibhav Badjatya from HNI Investments. Please go ahead.

Vaibhav Badjatya: My question has been answered. Thank you.

Moderator: Thank you Sir. Ladies and gentlemen that was the last question. I now hand the conference over to the management for closing comments. Over to you Sir!

Sunil Phansalkar: We thank everybody for participating on the call. I hope we were able to answer your questions but if still you have any queries, please feel free to write to me. Thank you and have a good evening. Bye.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of Emkay Global Financial Services that concludes this conference. Thank you for joining us. You may now disconnect your lines.