



“KPIT Technologies Limited Q1 FY2016 Post Earnings Conference”

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MODERATORS: **MR. APURVA PRASAD – RELIANCE SECURITIES LIMITED**

Moderator: Ladies and gentlemen good day and welcome to the KPIT Technologies Q1 FY2016 Post Earnings Conference Call hosted by Reliance Securities Limited. 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. Apurva Prasad from Reliance Securities. Thank you and over to you, sir.

Apurva Prasad: On behalf of Reliance Securities I welcome all the participants to KPIT Technologies' Q1 FY16 Results Conference call. Joining us on the call we have Mr Ravi Pandit – Co-Founder, Chairman and Group CEO; Mr. Kishor Patil – Co-Founder, MD and CEO; Mr. Sachin Tikekar – Board Member, President - Strategic Relationships and Business Transformation; Mr. Anil Patwardhan – Senior VP and Head-Corporate Finance and Governance; Mr. Sunil Phansalkar – Head-Investor Relations and AVP, M&A. I would now handover the call to Mr. Sunil. Over to you, sir.

Sunil Phansalkar: A warm welcome to everybody for the Q1 Earnings call of KPIT. I hope all of you have received our investor update where we have detailed in the quarter's performance and have talked about the various SBUs and the industry verticals that we operate in. As always we will have the initial comments by Mr. Ravi Pandit where he will talk about the quarter's performance and how we look at the year ahead and then we will throw open the floor for questions. Thanks for joining the call and once again a warm welcome and I will now transfer this to Mr. Pandit.

Ravi Pandit: Good afternoon everyone. So in my initial remarks I would like to talk about this quarter's revenue and its composition, EBITDA and what have been the factors which has impacted the EBITDA. I would also like to talk about the actions that we have taken pursuant to the discussion that we had on the Q4 of last year call we have said we will do certain set of things so I would like to update you on that. I would like to address some specific issues for which many of you have raised questions and then I would wrap it by looking at how do we

see the year's performance and after that I am sure we will be open to any questions that you might have.

So we closed the first quarter at \$118.3 million of topline and about Rs. 44 crores of the bottomline. As you would know that the aggregate income the revenue has gone down by about 3.3%. It is important to look at the composition of this and so broadly the work that we do falls in to two buckets one is the services both for engineering as well as business IT and the second bucket is the products and platforms that we sell. So if you look at the services the services revenue has increased by about 3.4% on a quarter-on-quarter basis and in this increase covers the work that we do in SAP it covers increase that we do in enterprise solutions and all other areas.

During the quarter there was growth in the major IT services; engineering grew business IT especially SAP. Our revenues from digital also grew. The SAP growth was on account of our normal increase and we believe that it is a sustainable increase.

As far as the digital revenues are concerned in our update we have given the composition of digital revenues in each of our lines of income business IT, engineering services products and platforms etcetera. On an aggregate basis our income from digital revenue is about 10% to 11% since we are a vertically focused company we believe that our ability to come out with digital revenues which typically include the work on sensors, mobility, Telematics, analytics etcetera. Our ability to deliver solutions in these areas is much better and we are seeing some traction in that account. We are certain that we will see some growth in the years to come in this regard.

The second component of our revenue is products revenue which has taken a hit during this quarter. A large part of that is on account of the revenues that we have from intelligent transport systems, which is a system that goes on buses and typically the bus revenues vary on a quarter-to-quarter basis and that has impacted our revenues during this quarter. If you notice last year also

significant part of the revenues came in Q3-Q4 we expect that during this year it would be on a similar lines.

On a year-to-year basis we expect that our revenues from this source should go up. So the revenue composition of last quarter shows a growth in services and cyclical or seasonal de-growth in products.

Now turning to EBITDA our EBITDA during the quarter has been 9.6%. If you recollect we had some tough decisions in the last quarter and our EBITDA was about 4.5%. On a sustainable basis that EBITDA in the last quarter was about 8%. From 8% we have moved to about 9.6%. Now this growth is contributed by various internal actions that we have taken and it is also contributed by the change in the Forex rates. So as we had mentioned in the last quarter we have done some work on the pyramid that we operate in. We have also done some work on how much should be the composition of the revenues delivered from subcontractors. We have worked on utilization we have got some credit on account of VPI payment because our VPI was less than 100%. So these have been some of the factors which are affected the growth in our EBITDA.

The decrease in the valuation of the rupee has contributed to about 65 basis points in the EBITDA improvement. So if you were to look at about 160 basis points total improvement in EBITDA 100 is caused by our internal actions and 65% is caused the external thing. Now as we had mentioned in the last call we are taking a lot of actions on three or four major areas. I had said in the last call that our actions will continue in Q1 and Q2 and a major parts of the result of those actions will express themselves actually in Q3. So the actions that we have taken and this is something that we have detailed in our update. The actions that we have taken fall broadly under the four areas of profit improvement, people development, predictability and on growth.

So we have done a fair amount of work on profit improvement. So as I mentioned earlier we have worked as far as the employee pyramid is concerned employee utilization is concerned also the composition of freshers as well as lateral recruits. We have also done a fair amount of work in proper client

selection as well as contract selection and profitability on individual contracts. We have taken some actions on this. Not all the actions are yet complete and not on the results of those actions are impeded in the results of Q1 nor will they be impeded in the results of Q2 completely because they will as I said they will become evident in the Q3 part.

The second area where we have done quite a few actions is in the area of people development. We are investing significant amount of money in training across the whole company. We have increased our budgets by almost 100% and our budgets have increased because we are doing more training of both our existing staff as well as the training of laterals we are investing additional amounts of money in training for our account managers; training for our project managers and program managers as well as training for our freshers who joined the company. And we expect that this will put us in good stead as times goes by.

The third area on which we have been doing some work is on the area of predictability. We have improved our ability to predict to a certain extent but I am sure we have some way to go and we have some work to do. And our work in this area will continue over the next two quarters. Here again I believe that we should be seeing better impact of this towards the end of the year.

The last area is our efforts on growth. Now there are some areas in which we are focusing for our future growth. So we have done significant investments in digital technologies and we are also invested in our products and platforms where we believe we will see a good growth in the quarters to come or the years to come. We have also done significant investments, as I said earlier, in improving our frontline presence. We have added people at senior levels we have recruited more people to be in the market for us both as the specialist as well as the account managers. So investment in growth in terms of people in the market is also grown up.

We believe that result of this should again display itself over the quarters in the rest of the year. So this is really like a broad picture of how we see the performance of this quarter and actions that we have taken during this quarter.

Based from the interactions that we have had with multiple analysts and investors we understand that there are certain set of questions that are in the minds of the community. So I would like to address as many of them as possible and should there be any areas which we do not cover in these you are of course welcome to ask any questions. So this quarter saw some growth in SAP and people have been asking whether this is sustainable. We believe it is sustainable. In the area of SAP as a matter of fact we have done a lot of work in the area of digital we are doing a fair amount of work in HANA, hybris, cloud solutions and as a matter of fact we are also SAP's preferred partner in this area so we see some traction. We are also seeing some traction in the area of utilities and so that has been the cause of the growth and we believe that we will continue to do well in this area.

Our investor update also shows that there has been a decline in the revenue from our top customers. The contract for our top customer for the whole year was decided towards the beginning of the year and it has been negotiated for the year. Every couple of years this customer reallocates various buckets and so there is some drop of revenue during this quarter on account of such a reallocation that has already happened. We have more or less reached the bottom as far as the revenues from the downward trend is concerned. We have have a slight de-growth in the last quarter but simultaneously we have also started winning quite a bit of new businesses in this customer and we believe that it will more or less bottom out in Q2 and thereafter we will start seeing an upswing.

The realization rate during this quarter has been a little over 64 and this presumably is a little higher than what the rest of the industry has seen but in our opinion if you take you need to look at two components what is one is the realization rate and the second one is the foreign exchange gain or loss booked

as a part of other income. And I believe that if you add the two together our results will be comparable with the rest of the industry.

There are also questions regarding the reduction in the depreciation amount from a Q4 to Q1 basis and that is on account of the fact that we have completed amortization of some of our expenses and going forward the depreciation will be more or less similar on a quarterly basis. There have been questions about the interest expense which shows a drop from Q4 to Q1. Now as we had mentioned in the last call we had to do restatement of interest expenses in accordance with AS16 now this restatement when we did in Q4 it included the effect spreading over more than one or two quarters and so the impacts of all of that came in over a single quarter namely quarter 4. And that was really not a normal sustainable figure. The figure that you see during this quarter is the normal sustainable figure which we expect to continue to see in the rest of the year. We have also provided you with our cash flow. Now there is some cash flow coming on account of the cash profit. During this period we have incurred some expenses on CAPEX in our Bangalore facility where we are seeing good growth in our engineering services. During this period we have also done some repayment of loan including the loan on long term basis as well as the working capital loan. This quarter also we had included an outflow on account of VPI provisions for which were made in the earlier two quarters.

Apart from that there has been an increase in our debtors in our DSO by three days which has impacted the cash flow during this quarter and on top of that there has been an increase in debtors on account of rupee devaluation and I think that increase is almost Rs. 20 crores. So all of that has had an impact on our cash flow. So this is where we stand as far as Q1 is concerned. As regards to the rest of the year as we had mentioned in our earlier call we would like to focus on improvement of our efficiency of our productivity in the first two quarters and we believe that the benefits of that will happen in quarter 3. We are unable to talk about specific guidance for the rest of the year because it is a little uncertain situation however we believe that as far as the revenues are concerned we should be seeing a slight upswing in the remaining part of the

year. So that is as far as our basic comments are concerned. We will be very happy to take any questions that you might have. Thank you.

Moderator: Thank you. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Harit Shah from HDFC Securities. Please go ahead.

Harit Shah: I just had a one question regarding your SAP business so you have achieved 17% sequential revenue growth in this particular quarter and you had mentioned at the start that this is sustainable so you need to clarify is it are you trying to therefore imply that 17% sequential growth is a possibility or is it that SAP revenues would probably remain at similar levels or may be slightly higher in the coming quarters? I am not necessarily asking for a guidance but just a kind of what trend that we can possibly expect going forward?

Ravi Pandit: What I meant was the level of revenue is sustainable I did not mean that 17% quarter-on-quarter growth is sustainable. I am sorry if I was a little unclear.

Harit Shah: Sir, my second question so would you give the EBITDA margin for your SAP business because that has not been given out so if you could give some idea about that level and whether it is sustainable going forward or not because this has obviously been one very big pain area for your in the last two, three years now. So that is why I think in that context I am asking this question?

Ravi Pandit: It is true that we have had problems in EBITDA margin in the SAP business. We do not give the margin information on a quarter-to-quarter basis because it varies with the revenues of that period and we will give it on an annual basis as we have done earlier. Quite a few of the actions that I outlined regarding efficiency of our productivity improvement also relate to SAP business and we are beginning to see an improvement in our EBITDA margins in the SAP business.

Harit Shah: My third question is as far as your IES business is concerned so I know obviously your overall services revenue grew by 3.4% but within that the largest component has obviously declined and I understand this because of the

Cummins' account so you had obviously mentioned that Cummins is more or less hit the bottom so therefore again the reason I am asking is that this is the second successive quarter or USD revenue growth decline in IES so they being your largest vertical or SBU the other kind of growth that we are expecting is that we can expect going forward that is something which I would like to get a sense about?

Ravi Pandit:

Yes, so as I mentioned our largest client did have a de-growth and I said that there might be a slight de-growth in this quarter but that has kind of bottomed out. And we are seeing some traction outside of the largest customer and we will see how the growth plans out. But as I mentioned earlier we would not want to give a definitive indication about the growth numbers at least in this quarter. We would like to work on our current initiatives for one more quarter and may be hopefully at the Q2 call we might in a position to talk a little bit more about the how does the growth in every segment pan out over the rest of the year. I would request you to bear with us for some time before we talk about the growth.

Harit Shah:

And one final question from my side. This is regarding your cash flow so I noticed that I mean I am not heard over the CAPEX but if you see your operating cash flow it is just about less than 10% of your EBITDA so is it possible then that as we see improved profitability going forward that this should improve because if I were to compare with your peers it is much, much lower when you compare it as percentage of EBITDA. So what is the kind of we can expect on this front going forward?

Sunil Phansalkar:

As we said this quarter it has been lower because of the reason that Mr. Pandit talked about the beginning that DSO's have gone up. I think that is the basic reason for reduction in the cash flow from operation. Obviously as we move ahead this will improve and definitely it will improve as a percentage to EBITDA. If you look at the last year as a whole I think that percentage was much, much higher and as we move ahead we should be able to improve that number.

Moderator: Thank you. The next question is from the line of Rahul Jain from Systematix Shares. Please go ahead.

Rahul Jain: Firstly, I think you said that product and platform revenue should grow for the full year basis as compared to the Q1 which is a seasonal factor so if you could help us with first what is the total revenue you booked last year in the Fiscal 15 in this and secondly is it backed by some order which you have already won or is it just an anticipation of a growth which we have seen?

Kishor Patil: In products and platform mainly we were talking about ITS where we did about 19 million last year roughly and overall we serviced about 3,000 to 4,000 buses and basically we have significant part of that orders but the delivery schedule depend upon the final uptake from the state transport units. So you have orders on hand but delivery schedules can vary a bit. So knowing about their plans and the government funding as well as every year a certain number of buses needs to be replenished we believe that is what we will do certainly. But more importantly we are also now exploring other markets outside India and looking at what we have in hand we feel that we will be in a position to certainly meet if not exceed that number.

Rahul Jain: So you said from a revenue we booked 19 million under this side last year?

Kishor Patil: Yeah.

Rahul Jain: That 19 million is just the ITS part not the entire products and platforms?

Kishor Patil: No, I talked about only ITS.

Rahul Jain: So from this 19 million for full year we did some 1.8 million in this quarter?

Kishor Patil: Yes.

Rahul Jain: So technically if everything goes well another 17 million to 18 million should come on this front?

Kishor Patil: Yeah, that is true.

- Rahul Jain:** And for total product and platform per se also we are expecting our full year growth should happen?
- Kishor Patil:** Yeah, I mean because of the ITS itself we should in a position to grow in this segment.
- Rahul Jain:** So this 3,000 to 4,000 buses which we deployed last year is there any is it tender driven or how we see this any predictability on this business?
- Kishor Patil:** No, actually last year we got a 100% of the market share we expect about 80% to 85% of the market share this year.
- Rahul Jain:** And this year it is for much bigger fleet?
- Kishor Patil:** No, I think around similar styles for this specific market but as I said we are also exploring market beyond this specific area.
- Rahul Jain:** So beyond JNNURM?
- Kishor Patil:** Yeah.
- Rahul Jain:** And secondly, OPM recovery path if I have to call so, so from a nine months perspective what we delivered in Q4 was a far lower a number and obviously it had lot of components involved for that substantial fall. Now since we are on a track of coming back. So if you could just sort of give a thought how and how much I am not asking the tenure but how much of it is recoverable or full of it is recoverable and what could be the major attributes for that?
- Sunil Phansalkar:** So Rahul, as we have said we have been working on three, four areas to look at profitability improvement. These areas are income plus employee pyramid because we will be looking at hiring majority of our people say about 70% odd plus people would be post graduates and the investments required for getting these graduates in to projects we have done so I think that engine will get rolling. So our employee pyramid will look much better we are also working on looking at how we improve the productivity. We are also working on areas like employee utilization, improvement in those because both of our metrics were

at a pretty low level in Q4. So most of the operational efficiencies would be driven through these mechanisms which would help us improve our operating profit margins.

Rahul Jain: That I can gauge it but what I am trying to see is that we did first month of Fiscal 15 we did an average of 13% EBITDA margin and right now we have come back to 9.6% I guess. So this 13% which is still good 340 bps away so you are trying to say whatever efforts we are taking we should reach to this kind of a number probably over the next four to six quarters?

Sunil Phansalkar: I think it is we do not want to commit any or state any number. What we are saying is that yes, this is an improvement and we will continue on the improvement. Whether it would be at what number I think at the end of Q2 is a better time to talk about it.

Rahul Jain: I think you have talked about a product that can be monetized post Q2 if you could give more clarity on that?

Sunil Phansalkar: So we have said that a couple of areas in Smart Meter is where some of our products might come out. So these are in the areas of Smart Metering.

Rahul Jain: And if you could tell the kind of potential which we may be chasing?

Sunil Phansalkar: No, it is difficult to talk about that right now. I think let us get in to it and then we can speak about it.

Moderator: Thank you. The next question is from the line of Ramnath Venkatesh from LIC. Please go ahead.

Ramnath Venkatesh: Sir, my question is on the SAP practice. We had this skew which was there towards the implementation projects and we were talking about making it more stable through AMC revenues. So how far are we in that journey having a more stable base of SAP revenues going forward for us?

Ravi Pandit: So we are working in that area we are beginning to see some AMS contracts coming in. So the change in the composition of SAP is actually moving from

the traditional ERP in to the new world digital and moving from one time implementations more AMS. We do see some movement in that area. During this quarter we have also invested in building an IMS practice and we believe that a combination of AMS and IMS can give us a good edge in this business. But there is a conscious efforts in moving towards more annuity based or a long term business that we are doing.

Ramnath Venkatesh: So can you share with us in terms of how much is the proportion now of annuity based revenues that we have currently in our?

Ravi Pandit: I do not have a proportion of that data with me just now but we will kind of compile that and may be in the call we can talk about it.

Ramnath Venkatesh: And sir, the other question is on the winning new clients like one is you are talking about looking at project level profitability or client level profitability to kind of clean up some of your client base. But with the existing clients in terms of building relationships with ones with great potential and in terms of building the team of account management capabilities at the front end. Have you taken any measures in this regard in this quarter or in the last few quarters too?

Ravi Pandit: So you know as I mentioned earlier there are four initiatives we are working on and growth is definitely one of them. And the initiatives on growth are both in terms of new offering development as well as the new market muscle development. We have significantly increased our presence in the markets both in the area of account management as well as in the area of business specialist and we will continue to invest in that area. We have over the years worked with quite a few customers and now we are actually segregating those where we want to put far more efforts through additional investment in account managers.

So we are looking at customer composition in I should say two or three buckets. So those customers who belong to our verticals those who have a potential to grow and who are a profitable relationship these are the areas where we are actually investing in our customer connect. We have also added quite a few

senior people from the rest of the industry at senior levels as the heads of our SBUs or IBUs these are the people typically in the market. And yes, there is an investment in the growth as far as the sales end is concerned.

Moderator: Thank you. The next question is from the line of Ashish Chopra from Motilal Oswal Securities. Please go ahead.

Ashish Chopra: Just a couple of questions from my end. Firstly, if you could just give some color around the reminder of your top accounts? Earlier you did mentioned about the top most account but the other nine accounts within the top 10 have been in this band of \$30 million to \$35 million for the past 8 to 9 quarters. So just wanted to understand how does this really stack up as to whether there are a few growing ones while the others are coming down or whether these are more or less saturated at the level at which they are so any color around that would be helpful?

Sunil Phansalkar: So Ashish, if you look at the other nine accounts then there has been some movement if you look at the last four to five quarters I think a couple of customers they have gone out of the top 10 but two, three new accounts have got added there. So it is a mix that some of the accounts are growing and one or two of them have not grown. Last year we had a specific customer where we are said there would be a decline. So because of the top 5. So there are accounts which are growing it is not that they have reached saturation it is just that the mix of those accounts has been changing in the last four to five quarters. We are seeing some good auto accounts also coming in the top 10 in the last four quarters.

Ashish Chopra: So as a result of that would you expect this to pick up in terms of a run rate from here or the decline in a select few accounts is still continuing which will keep it probably range bound?

Ravi Pandit: So as a matter of fact if you were to look at our top 10 accounts; year-on-year basis in this quarter they grew by about 3%, on a quarter-on-quarter basis they grew by about 1% and this is after taking into account the reduction that has

happened in the top customers. So in reality the growth is quite healthy and we expect that growth to continue.

Ashish Chopra:

If I move to the other end of the spectrum where you mentioned that you are taking a very close look at some of these large tail accounts so just wanted to know if you would have an assessment handy whereby you would be able to quantify the impact of the contribution from those customers today which you think is not really very strategic to you in the long run and hence you may want to do away with them so just some color around how much could that impact the top line by in the current year.

Ravi Pandit:

We are quite sure that it will not impact negatively our top line because when we are clearing the bandwidth from some of our long tail customers, we are doing it at a time where the same people can be absorbed in our preferred customers. So we would see a reallocation of our resources and an improvement in our margins as a result of this.

Ashish Chopra:

And just lastly the utilization levels at both off-shore as well as on-site remained pretty low and now with the focus being on hiring a lot of freshers and also undertaking a lot more training programs versus before, just wanted to know where would the new normal targeted levels of utilization be at both locations and by when do you think you would be able to reach there.

Ravi Pandit:

You would notice that we have had a decrease in the total headcount while the number of freshers added has been quite significant about 170 or so. So there is a decline on a net basis that should help us in improving our utilization. On the other hand when you look at the freshers, see we work with some select colleges across the country. These colleges actually run our courses in the last year of their college and it has been successful so far. Our attempt has been that when these professionals join us within a period of 4 weeks or so, they become billable because they have been trained for more than a year by the time these few months on their joining is over. So we don't think that the recruitment of freshers would adversely affect our utilization. On the other hand the actions that we are taking on account of our pyramid and span of

control etc. would mean possibly improvement in the utilization. Utilization is one of the areas on which we are doing a lot of focused work and we believe that over time we will see better and better results in it.

Moderator: Thank you. The next question is from the line of Jagdish Bhanushali from Florin Tree Advisors. Please go ahead.

Jagdish Bhanushali: I wanted to understand how much has been the maintenance part in the SAP of the \$25 million of revenue.

Ravi Pandit: That was the question that was asked earlier on AMS and as I said we don't have an exact number. I would like to clarify here those companies who have been in this business for much longer rationally have a much larger proportion of their income from AMS. Our growth in SAP has been a little recent like in the last 3-4 years it has moved from like \$40 million of revenue to more than \$100 million of revenue. So naturally a larger part of our revenues come from new implementation. So I don't think our maintenance revenues will be on the same lines as others but we will do some working on that and at the end of the next quarter we will talk about the specific numbers and the trend in that over the last couple of quarters.

Jagdish Bhanushali: Just if you could not disclose the margin wanted to understand, was the SAP profitable at the EBITDA front in this quarter?

Ravi Pandit: No so as I said earlier I've answered this question is a matter of fact, the EBITDA margins for each line of business, we give on an annual basis so I wouldn't have a quarterly figure available for us to talk about. But as I mentioned again we are seeing a good improvement in that margin by virtue of all the actions that we have talked about earlier and quite a few of those actions have focused on SAP because that has been a problem area for us so that is really the center of our actions as of now.

Jagdish Bhanushali: And we have seen that digital part has been about 22% in the SAP business so wanted to understand where do we see at the end of the year this 22% moving up to?

Ravi Pandit: I can't give exact number as to where it will move but I would like to tell you that we are like preferred partners for SAP on all aspects of their digital business which includes success factors, which includes HANA, which includes Hybris. We have our own solutions anchored on this which are more industry-specific and that's the reason why we are seeing good traction. We have good number of case studies along with SAP in this area. So our attempt has been to increase this part of the business because this is like a new business so we are at the same level as any other large entrenched player.

Jagdish Bhanushali: Just the last question is that we have an employee count of about 10,840 so where do we see at the end of the year, any target on this?

Ravi Pandit: No I don't think I will be able to talk about that target because it's a composite safety and it will be a joint impact of the growth that we will have and the productivity measures that we take so I won't be able to talk about the numbers just now.

Moderator: Thank you. The next question is from the line of Nandish Jalan from IIFL. Please go ahead.

Nandish Jalan: I have two questions, one is you did mention in the pre-quarter brief that you expected revenues to decline marginally. However, it has come at 3.3%, has anything surprised you negatively after that release that's number one. In terms of your fixed asset addition you have mentioned that there is a capital expense for internal digitization, could you just help explain the nature of this and the amount related to this?

Ravi Pandit: Sure, in month or so ago we had talked about how would the revenues pan out during this period and we had made two statements. We had said that as far as our services revenues are concerned they will be like steady. I think we have done better than that. We had also stated that when it comes to product revenues we expected a decline because of the seasonality of the revenues and that is how the things have panned out. So I think that has been adequately covered in a statement that we made available to all of you.

As far as the digital part is concerned we are doing investment in digital, see if you were to look at the digital technologies the impact of them you will see broadly into three areas. One is creation of a better customer experience, the second is improvement in the internal processes and the third is in creation of a new set of products. Our work in digital technologies covers all these three areas. So the work that we are doing in our products and platforms actually incorporates generations of new products based on digital technologies. The one that we are doing internally is largely related to the change of the processes and this is the case where we are using substantially the mobility lever, we are using social network and we are also doing analytics. So we are doing a fair amount of work, it's an internal investment. We believe that the best way for us to go and talk to the customer about these technologies is to show how we have developed these technologies ourselves. Now the work that we are doing internally for ourselves are really in area of open source or roundup technologies. These are not the typical ISV technologies like the Oracle or the SAP technologies so that is where our investments are.

Nandish Jalan:

Just a quick follow up, could you just quantify that amount regarding this CAPEX and one thing on the earlier question, was the decline under Cummins account expected from the start of the quarter during the release you get the extent at which the decline has happened?

Ravi Pandit:

So as far as Cummins is concerned we don't talk about an individual customer and when we talked about very low growth or steady-state in the overall IT services area we had factored in Cummins. So the decline in Cummins is known from the beginning of the year because that is the time the contracts were renegotiated and there is no negative surprise at Cummins. As a matter of fact as I mentioned we are seeing greater traction in Cummins because we are winning additional business.

Moderator:

Thank you. The next question is from the line of Nirav Dalal from May Bank Securities. Please go ahead.

- Nirav Dalal:** I had a couple of questions; one is Q2 margins would be impacted by the wage hikes so what is the impact that you envisage in?
- Ravi Pandit:** It is true that our Q2 margins will be impacted by the wage hike. Our wage hike is around 2% for onsite people and around 7% or 8% for our offshore people. Both of that put together would hit us, our EBITDA by about 200 basis points. On the other hand we should see some improvement in EBITDA on account of all the actions that we have taken so far plus some growth that would normally come year after year. So we don't know what could be the net impact of both these things. I think we will see it as the quarter progresses.
- Nirav Dalal:** And what will be the fresher addition for the full year given for Q1 and Q2 what then would you follow up?
- Ravi Pandit:** We have talked about the 300 people in Q2 so let us wait till the end of the quarter for the balance number.
- Moderator:** Thank you. The next question is from the line of Shraddha Agarwal from B&K Securities. Please go ahead.
- Shraddha Agarwal:** Just one question, you mentioned at the beginning of the call that there was some renegotiation done with Cummins. So was it on both enterprise and engineering side of your business and I also see some pricing decline when I do some back of the envelope calculation. So I was just curious to know was volume discussion also led by some pricing renegotiation at Cummins.
- Ravi Pandit:** See I don't want to go into individual customer negotiation. The fact is that Cummins does this renegotiation every couple of years. This is a normal part of their operations and this is how it went.
- Shraddha Agarwal:** But what gives you this confidence that you would have bottomed out at Cummins and you do not see further decline in that account?
- Ravi Pandit:** Because we are seeing an additional business coming in. We are winning business.

- Shraddha Agarwal:** And that's on the business IT side?
- Ravi Pandit:** No I'm talking about business as a whole.
- Shraddha Agarwal:** And secondly you said you've made some improvement and you've made some changes on your employee pyramid so what pyramid are you currently operating at as in people with experience of less than three years what is that current ratio?
- Ravi Pandit:** That should be in the range of about 28%-29%.
- Shraddha Agarwal:** And how does it stack up against last quarter?
- Ravi Pandit:** I don't know the percentage but what I can say is this we have added about 170 freshers and of the 140 people that reduction is there in this quarter almost everything is lateral.
- Moderator:** Thank you. The next question is from the line of Amar Maurya from India Nivesh. Please go ahead.
- Amar Maurya:** Sir I have two questions, number one is about this time and material. Sir time and material contribution has gone up during this quarter and onsite contribution has also gone up. So is that this during this quarter subcontracting cost has gone up for us?
- Sunil Phansalkar:** Actually as we said subcontracting costs have gone down for us in the quarter as compared to last quarter. But if obviously then we classify the decline that we had in the top customers most of it was fixed price, decline in products and platforms other than ITS was also fixed price that's where the fixed price has gone down. The growth has happened in SAP where we have majority of the revenue still on-site so the on-site number has also gone up.
- Amar Maurya:** And you said the digital contribution this quarter was 22%, right?
- Sunil Phansalkar:** For the SAP SBU, at the organization level it's about 10%-11%.



- Moderator:** Thank you. The next question is from the line of PriteshVora from Incedo. Please go ahead.
- Pritesh Vora:** My question is your IES revenue as you mentioned is gone down by 2.5%. Is it due to entirely due to Cummins or there is another account also?
- Ravi Pandit:** No it's almost more than 90% is because of Cummins.
- Pritesh Vora:** So sir what is the outlook in this because this is the largest segment of our business? What is the outlook here, what do you see this..
- Ravi Pandit:** You are talking about the outlook in the case of Oracle or in the case of Cummins?
- Pritesh Vora:** No Oracle.
- Ravi Pandit :** In the IES area we work not only on Oracle but we also work on JD Edwards, it's a combination of both. We have been extremely strong in the area of JD Edwards over the years and we are seeing growth in that area. As I said even in the Oracle area because we are winning back business at Cummins, it's largely on the Oracle side.
- Pritesh Vora:** So you don't see any worry in the IES area mainly.
- Ravi Pandit:** I would say so.
- Moderator:** Thank you. The next question is from the line of Harit Shah from HDFC Securities. Please go ahead.
- Harit Shah:** You mentioned that the digital proportion in IES is about 5% around or so. Would you consider that as a risk given the kind of growth the Oracle itself is seeing in the digital business and given that you're more than 20% coming from SAP so would you think that this is a bit of a negative for you going forward potential risk?

Ravi Pandit: No I wouldn't say so that actually reflects in the case of SAP and Oracle are how strong they are going in the area of digital. SAP has in our opinion moved fast and that is where we have been able to have more digital revenues. In the area of Oracle wherever they are now opening up new avenues in the field of digital we are doing that. But apart from Oracle or SAP there is also an area of digital where we are seeing growth which you will see in our enterprise solutions area as well as products and platform area.

Moderator: Thank you. The next question is from the line of Foram Parekh from Khambata Securities. Please go ahead.

Foram Parekh: I had two questions; one is on the rest of the world segment like we see 27% sequential fall in this area. So I just wanted to understand what went wrong in this quarter and secondly if you can just tell me what is the attrition rate for this quarter?

Ravi Pandit: On the first question if you look at the ITS business, it is all currently in India and the decline in that business is prime reason for the decline in ROW revenue. Attrition on an annualized basis was about 21%-22%. But when we look at attrition this is the overall number. We mainly look at attrition of our top block people and our senior-level people; there the attrition was in lower single-digit, about 4%.

Foram Parekh: Just a follow up question on the previous question like where do you see this digital technology at the end of the year. I mean you see it at 11% or you see it going down by FY16?

Ravi Pandit: It's a matter of fact if you notice from our update; a substantial part of our product revenues is on digital. So our product revenues stabilize or grow over the year we should see an increase in the digital revenues. If you see the trend in the rest of the areas also there is an uptick in that area. So I won't be able to comment as to exactly what proportion of our revenues will be digital. But we would imagine that we should see growth, if for no other reason just for the growth on product business.

Moderator: Thank you. The next question is from the line of Nirav Dalal from May Bank Securities. Please go ahead.

Nirav Dalal: Just had this question regarding the subcontracting cost that has declined this quarter. So what do you see the trend in that and why was the decline?

Sunil Phansalkar: See as an overall major we obviously want to reduce our dependence on subcontracting and wherever possible see how we can deploy our own people. I think that is an ongoing exercise so if you take medium-term view it has to go down. Obviously quarter-on-quarter there might be some variations but over a period it has to go down.

Nirav Dalal: Sir and finally other expenses last quarter included the 2.6 million provision but this time again the costs have gone up so any comment on that?

Sunil Phansalkar: I think if you look at the SG&A as a total growth that has declined in Q1 over Q4. So overall there has been a decline there. Some of the additions as we have said earlier have been done in the frontend people and that is where some of the cost would have gone up in the SG&A part.

Moderator: Thank you. The next question is from the line of Shekhar Singh from Excelsior Capital. Please go ahead.

Shekhar Singh: Just wanted to know like other than your top client in the top 10 list are there any services gaps in the sense like can't we grow those clients at a much faster pace with the current set of services and if not then are there certain gaps because of which we are unable to grow some of the other clients at a much faster pace because whatever said and done your size as compared to other companies is much smaller but in terms of your services bandwidth you almost look like any other large company. So sometimes we wonder why the growth in KPIT should not significantly exceed many of the large companies.

Ravi Pandit: First is we had stated that for these two quarters our focus will be on efficiency improvement and that has actually been our strong focus in Q1 it would be so in Q2. Secondly if you were to look at our growth picture you would see that

on a quarter-on-quarter basis on services we have grown by 3.4% after accounting for a significant reduction in our major clients. So in reality our services growth has been reasonably good.

We are focused on three types of customers, we are focused on automotive, we are focused on manufacturing of a certain type, and we are focused on energy and utility. These customers the kind of services that they need include the engineering services and the business IT services and some kind of an interconnecting service like the PLM. So we have done investments in the area of PLM in the last one 1.5 year. We have done investments in business IT over the last 4-5 years and we have been growing the engineering part. We believe that with our services spectrum our existing customers should give us much larger revenues than we are currently getting. We believe that our existing customers should give us that growth. I don't think there are any gaps in services. I believe that greater focus on account management and the utilization of our existing services can give us the traction. Currently our engineering services are focused largely on automotive and not on manufacturing or on energy. I think that is some area that should give us growth and lastly the products and platform that we have should also be kind of taking care of extra needs of our customers and that's what we are really targeting for.

Shekhar Singh:

And just like just trying to understand, is it that you are in verticals like automotive, manufacturing, energy which are considered to be slightly in terms of billing they are slightly low as compared to other sectors. So is it that reason because of which your margins are slightly on the lower side as compared to the larger companies?

Ravi Pandit:

I wouldn't say that there is a problem in the verticals that we are working with. We have stated that our problems are more on the efficiency side of operation and that has been the focus of our attention. If you recollect we have always been a growth focused company and now excepting for the last two years we were growing at 25%-30% on an yearly basis and our focus has been on investments in tune with that. I think over the period we accumulated some

inefficiencies which is what we are currently trying to address. We believe that if we work on it for the next 2-3 quarters our margins should be in line and then we can focus seriously on organic growth.

Moderator: Thank you. We got the last question from the line of Dipen Seth from HDFC Securities. Please go ahead.

Dipen Seth: Sir just one question which is more of about promise in the business rather than the troubles that you are going through and I thought it might be interesting to raise it. This products and platforms slice within our SBU split, now there was a time when this used to be subsumed within the product engineering services, right? It's only recently that we have started kind of giving this as a separate split. So last quarter we were at close to \$13 million revenue, this quarter we are at \$5 million. The comparable quarter last year we were also at about \$5 million. Now what is the scope in this business to ramp up substantially and is there nonlinearity in this part of the business if you know what I mean? Can this bring in disproportionate profits when it grows faster because of the fact that its product-oriented? Is there that kind of characteristic in this part of the business?

Ravi Pandit: So as you rightly said we have just taken this house as a separate unit and we certainly believe that this is quite a potentially significant area relevant for our customers and potentially a growth area. But we are learning this again bit by bit and naturally this is a nonlinear revenue. This is also in the area of largely into IOT or digital so it's very important and relevant from the customer spend also. I think we have picked up some niche areas and we are taking our markets and getting a market share in a specific market right now. But as we learn and we are successful in this I think there is a much greater scope to take it beyond the current market segments as well as the geographical market. So absolutely this is certainly an exciting area.

Dipen Seth: So right now it looks too small if you know what I mean, it's just about \$5 million or \$10 million in the quarter but at some stage this holds the potential



of becoming of \$30 million or \$40 million business. Maybe you will take 2-3 years to do it, I don't know about that part but certainly...

Ravi Pandit: It is certainly scalable business. We don't know right now what the time frame is but it is certainly a scalable business.

Dipen Seth: And it would probably be IP driven and have nonlinearity?

Ravi Pandit: Absolutely.

Dipen Seth: So I can see close to about what 500 crores odd of goodwill on your balance sheet which is obviously the result of the premiums that you paid to make the acquisitions over book value of the acquired companies. Now at some stage I guess once your profit and loss and your operations allow it you will have to progressively take write-offs on this or what is the internal plan or what do the accounting policies allow you to do because for me it's essentially 500 crores of fictitious assets on your balance sheet?

Anil Patwardhan: Under the current accounting rule to write-off the goodwill in two conditions, one is when you merge these companies and at which point in time you set up the goodwill of is the reserves that you have. What we have done in the last couple of years and we have negated some goodwill.

Dipen Seth: Yeah from close to 700 crores odd to now we are a bit over 500 crores, yes.

Anil Patwardhan: Yes so it's about 200 crores lower that we have already negated. Now when there is no consolidation the call on the goodwill is taken on the basis of the impairment of a particular entity for whom the goodwill has been paid. That's impairment discussion happens on the basis of the profitability of that entity. We haven't had a reason or the auditors haven't had a reason to question that in the conversation so far. We would like the goodwill to be written off to be very honest with you but there are only conditions under which we can do it and we cannot do it arbitrarily. You would also noticed that in appropriate cases we targeting tax reduction for it and that is the case that we have made that's



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the case that we have won at an initial level. So in a sense it is intangible asset but it is also a tax asset.

Dipen Seth: Absolutely sir in fact I would be very happy if you could progressively write this off and use it to gain tax shields and therefore and the on cash outflow from the business so your reported profits might fall but for me you would become a much more valuable company.

Anil Patwardhan: But you know the tax write-off is unconnected with the book write-off. The tax write-off happens as it is. So even if you might see it here in the books the amortization of existing goodwill in accordance with the tax log keeps on happening.

Moderator: Thank you. That was the last question. Ladies and gentleman I would now like to hand the floor over to Mr. Apurva Prasad for closing comments.

Apurva Prasad: On behalf of Reliance Securities I would like to thank the management for giving us the opportunity to host the call and all participants for joining the call. Thank you very much.

Moderator: Thank you. Ladies and gentlemen on behalf of Reliance Securities that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.