



**“Cyient Q4 FY2019
Earnings Conference Call”**

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MANAGEMENT:

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Moderator: Ladies and gentlemen, good day and welcome to the Cyient Q4 FY2019 Earnings Conference Call hosted by Edelweiss 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. Ajay Aggarwal, President and CFO of Cyient. Thank you, and over to you Sir!

Ajay Aggarwal: Thank you Aman. Good evening ladies and gentlemen and greetings for the day for people from other geographies. Welcome to Cyient Limited’s earning call for Q4 and also for the full year of FY2019 ending March 31, 2019. I am Ajay Aggarwal, CFO. Present with me on this call are our Executive Chairman Mr. B. V. R. Mohan Reddy and also Managing Director & Chief Executive Officer, Krishna Bodanapu. Before we begin, I would like to mention that some of the statements made in today’s discussion may be forward looking in nature and may involve risks and uncertainties. A detailed statement in this regard is available in our investor update, which has been e-mailed to you and is also posted on our corporate website. This call will be accompanied with the earnings call presentation. Details of the same have already been shared with all of you. May I now request Mr. Mohan Reddy to provide a brief overview of the company’s performance for the quarter and the year ended March 31, 2019.

B. V. R. Mohan Reddy: Thank you Ajay. A very good evening to all of you ladies and gentlemen. I welcome you all to this conference call, which is our Q4 earnings call as also for the whole financial year. Let me first take you through some of the highlights for the quarter.

We posted quarterly revenue of Rs. 11,629 million or it is Rs.1162.9 Crores. This signifies a very strong growth of 9.5% on a year-on-year basis in US Dollar terms. We posted revenue of \$165.2 million, which is a growth of 0.3% year-on-year basis. Services revenue is at \$146.9 million, which signifies a growth of 1.7% on a quarter-to-quarter basis and 1.4% on constant currency. Group operating margins stood at 15.1% for the quarter, which is the highest in the last 20 quarters expanding 33 basis points on a quarter-to-quarter basis and 101 basis points on year-on-year basis.

Services operating margins stood at 16.4% from the quarter, which also is the highest in the last 20 quarters signifying 126 basis points expansion on a year-on-year basis. DLM operating margin stood at 4.1% for the quarter. Operating profit growth stood at 17.4% on a year-on-year basis. Normalized net profit for the quarter stood at Rs.1881 million or Rs.188.1 Crores, which is the highest ever recorded by the company. This resulted in a quarter-on-quarter growth of 104.2% and year-on-year growth of 54.7%.

Now let me take you through the highlights of the full year. We saw yearly revenue of Rs.46,175 million or it is Rs.4,617.5 Crores signifying a strong growth of 17.9% on a full year basis. In US Dollar terms, the revenues are at \$660 million, which is a growth of 8.7% in Dollar terms and 10.1% in constant currency terms. Services revenue for the year stood at US\$580.2 million

signifying a growth of 6.3% in US Dollars and 7.6% in constant currency terms. The DLM revenues for the year stood at \$79.7 million, which is a growth of 29.2%. Group operating margins remain flat at 14% for the year. Services margin stood at 15.3% for the year and the DLM margin stood at 4% for the year. The operating profit stood at Rs.6,449 million or Rs.644.3 Crores, which is a robust growth of 17.3%. Please note that this growth is post our NBA or New Business Accelerator investments in business. Normalized profit for the year stands at Rs.4,898 million or Rs.489.8 Crores signifying a growth of 14% on a full year basis. Continued focus on cash flow has yielded good results with cash conservation at 48.4% for the full year and highest ever free cash flow at Rs.3,770 million or Rs.337 Crores. I am happy to announce the company has declared a final dividend of Rs.9 per share, which takes the total dividend to Rs.15 per share for the full year, which is the highest ever. Please note that this is over and above the buyback of Rs.200 Crores that the company announced in February 2019 and which was completed in the recent past.

Now we would come to a few business highlights for the quarter. I will just be very brief on them. I will just pick up four of them. The first is that Cyient successfully rolled out a portfolio of services and solutions for 5G deployment. We think there is a tremendous amount of opportunity, huge market availability for this particular service offering of ours. The company signed a tripartite MOU with the Government of Telangana, the Telangana State Aviation Academy for drone pilot training and certification programme and lastly just to touch upon a couple of points on CSR, I am extremely delighted to report that Cyient received the CSR leadership award from ET Now in community development category as a part of the initiative for Cyient's urban micro skilling centers for urban poor, we provide the training to a batch of 300 unemployed women in various vocational courses.

Finally on the awards and recognition front, Cyient is positioned as an established and expansive players in the Zinnov Zones' ER&D services report 2018. Cyient is recognized as a major contender in the Everest Group's Peak Matrix Medical Device Engineering Services Assessment 2019, Cyient and India 2022 coalition launched with MedTechConnect platform to address India's last mile challenges in health care. With this I would like to handover the call to Ajay who will take you through the detailed financial performance for the quarter and the year. Thank you very much.

Ajay Aggarwal:

Thank you Mohan. In terms of the performance I would like to give a colour both on the quarter and the full year. If you look at the revenue for Q4, this has been flat quarter for us on overall basis. We saw in services, we had a growth in most of the businesses except in case of communication and that led to overall growth of about 1.7% in Dollar terms and 1.4% in constant currency. As far as design led manufacturing is concerned, I think we had already made a release in terms of some of the challenges we faced in terms of deferment of about \$5.5 million of revenue into future and that led to a number of \$18.5 million of revenue for DLM, which is a degrowth of quarter-on-quarter of about 11%, so overall if you see we are flat for the quarter and now let me move to the full year.

In terms of full year, we have done overall if you see in real terms the growth is 10.1% while in Dollar it is 8.7%, in constant currency the growth is 10.1%. Overall growth is led by 18.2% in aerospace and defence, 5% is there in services and if you add the manufacturing belonging to aerospace and defence it is 18.2%. Communication if you see in real terms you have to look at the remarks on the right side have grown by about 10% if you take the currency out and when you are looking at the negative number I would say that we have let go of the communication order in DLM that is what it reflects, but overall DLM has really grown very nicely in the full year at about 29% over the last year. Even on standalone basis if you exclude the US portion we have grown at 13% in DLM.

Then you come to U&G when you are looking at, I would say U&G also we are almost flat. Actually it is -1% in constant currency. Transport if you see services 13.7, this is more like 17% to 18% in constant currency SIA had good growth, IENR has growth nicely and in case of MT&H the growth of 16% was more in the manufacturing and it was muted in services at 1.5% so that is how we have grown 10%. If you make a quick comment here if you see our CAGR of last five years in Dollar terms we have grown at about 12.7% or 13%. In real terms we have grown at about 14%, so I would say that from that perspective this year has been lower than our historical performance, but still we are growing at about 14% and there have been fluctuations year-on-year and we will talk about how the New Year looks like that is FY2020 and Krishna will give more colour on that.

We have provided you a walkthrough of the reported and normalized. Piyush will help you if you have any questions on this separately. I just thought that we will give you a good reflection of other income. If you see our profit has been very good in this particular quarter there have been a number of drivers, our operating margin in services business has been one of the highest in the last 20 quarters and that is about 16.4% and that gives us a very nice base for the coming years to further improve on the margin. Also if you see from the profit perspective, the other income has been very strong. If you look at finally for the full year we are very close to the other income of last year and also I think I will talk about some of the drivers for next year that is also poised for a good growth in the coming years. What has happened on other income, I think if you would see between the foreign exchange related items, we have got 412 million on this as a combination of unrealized and realized. We also have got another claim on the export of services of 280 million for the services business and that is appearing in the other income. Also we have some one-offs. When we have consolidated if you remember last time we disclosed that we are buying the 26% stake in DLM. We also completed the transaction and our negotiated value versus the value in the books has given us 135 million benefit on that. For one of our acquisitions in US that is CERTON we had earn-out, which is not payable of 69 million then in line with the accounting standard that has been reversed. If you see based on this there is a swing of about 976 million between the quarters. Some of them are one offs, which you can see, but I think both in terms of foreign exchange as well as some of the benefits they are sustainable.

Overall if you see from the perspective of earnings per share I think overall we have ended the year. Let us go to the full year please. We have ended the year with EPS of 43.4 and this is on normalized basis. On the reported basis it was 42.4. I already called out some of the items

between this. Our tax has also been good. I think overall our tax rate for the full year is 23%. There are some one offs in the quarter, but what you should look at is the effective tax rate of 23%. As we have been talking our special economic zone focus continues to help us and I still feel there is a scope for us to further improve it in the coming year. I would like you read about the operating margin bridge. Basically there was a headwind from the foreign exchange, but we had good capacity this quarter and we had the headwind of more paid days versus less paid days in this particular quarter that gives us 83 BPS. There has been good this thing on SG&A spend, so overall I think this is the bridge and we can talk about it in some of the calls to explain this.

Very quickly in terms of hedge book all of us are curious whether we are changing the policy or not. There is no change in policy. As on date we have total contracts of about \$123 million comprising of all the currencies that you can see that are mentioned and the gap on our currency for example for Dollar our rates for the next 12 months forward is 72.8 as against the spot of 69.2 as on March 31, 2019. If you look at the spot waves versus now then we have a potential forex gain of \$9.8 million in the next year based on these positions, but again I caveat these are current spot rates and depending on the final exchange rate this will fructify in the next year. As Chairman said cash generation has been positive. We have done the highest free cash flow. We have also done a positive free cash flow overall in DLM of about Rs.111 million. Overall our conversion rate has been nice. While you would have seen some of the challenges marginal increase in the days sales outstanding, I want to assure you that while there were some milestone projects where our unbilled revenue has marginally gone up by about four or five days, but in general there is no concern and our performance on free cash flow will continue. With this, I would hand over to Krishna to share the business updates.

Krishna Bodanapu:

Thank you Ajay. To give you a quick update on where things stand vis-à-vis the business let me start with some significant developments for Q4. One is we have completed the equity share buyback as most of you recall at the end of last board meeting we had approval from the board that we would buy back up to Rs.200 Crores worth of Cyient shares. The buyback is completed as of April 15, 2019 or so, but as of April 31, 2019 we bought 2.6 million shares, which was Rs.167 Crores of cash. We also acquired the balance 26% in Cyient DLM, which is our manufacturing subsidiary and which is where we do the electronic manufacturing related work. We originally had budgeted for a higher consideration of about Rs.56 Crores, but we ended up paying them Rs.42.5 Crores, so we ended up paying Rs.42.5 Crores for the 26% based on various things based on how the business has evolved and so on and so forth, so that is one of the things that Ajay just talked back is that we wrote back the difference of Rs.12.5 Crores. The new business accelerative, which is our technology accelerator and which has been consuming a fair amount of money because we are developing new solutions and technologies that are deployed well into the future is going to plan. We have 16 projects under development. The total approved is 19 and we are seeing traction in a few areas especially around internet of things, augmented reality and smart city. The current NBA initiatives will give a kick on revenue and ultimately profits by 2021 and we are happy to note that two of the initiatives are starting to generate revenue though the starting point is quite small, they are starting to generate revenue and we will see some revenue from both our vegetation management solution and also from our augmented reality solution during the course of this year.

If you look at the investment pipeline it remains the same. I would say FY2019 was not a great year from an acquisition and inorganic perspective because while there are a number of deals that were mostly true-ups that is the acquisition of the balance in Cyient DLM, the acquisition of the balance in Cyient insights, which is our analytics subsidiary. Obviously AnSem was a big part of it, so that was the only new deal that was in there, but we continue to focus on that and we continue to look at ways to accelerate this performance. The areas that we will focus on remain the same and they have been listed out there for your consideration.

If you look at the business by business update, let me start in the order of some of services revenue and the sites. The aerospace and defence industry is still looking good. There is a strong demand for commercial aircraft with a strong production pipeline for commercial aircraft. There is a ramp up that is growing and defence spending is also growing because of spend in countries like China and India. Obviously there is a short term problem, which some of you are also aware of based on the communication of what happened in Q4. There is a short term problem. There is going to be a fair amount of push out because Boeing is going to push out a fair amount of their spend because of the 737 issues, but having said that we also see some very significant longer term opportunities so we need to make sure that there is a good balance. What you will see is A&D was a reason for why Q4 was a little bit tepid because there were two challenges primarily because of capacity issues in the U.S., we were not able to ramp up as much as we thought we would and also the Boeing issue of push outs. We are seeing some upside there, but it would not happen in Q1. We will start to see upside starting from, some of it will happen in Q1, so I will say the real upside will hit in Q2 because some of these orders were really pushed out rather than lost, but the challenge currently is that it will really happen towards the end of Q1, so the impact will really be seen in Q2.

In terms of the Communications business, I mean the industry continues to be decent. Obviously, there is a significant amount of data that is being consumed. Devices are now throwing out data that has never been seen or heard before that data has to be transmitted, so the fundamental industry continues to be strong. 5G is another big area that the Chairman also talked about on our focus. We are starting to bring some beams, which are also quite interesting because they are on the technology rather than just on the network. The network piece will happen in due course, but the technologies where we are doing things like software-defined networks, network virtualization and so on and so forth.

As you recall, this is another deal that contributed to the challenge in Q4. One of our large customers has gone through renegotiation. The good news is not only did we win most of the business we also have a much wider scope, but what we are seeing is the workflow is just starting. So the impact will really be Q2 onwards and I want to assure you that it is going to be significant impact. It is just that it will start in Q2.

Also what we have done is we have combined 2 older businesses together, which is the energy business, which focuses on the mining customers and then the generation customers and also the utility business, which focuses on transmission and distribution. We brought both these businesses together into a BU just to make sure that we have an offering continuing from raw

materials extraction all the way through generation, transmission, distribution. We are calling it energy and utility. With the recovery in the oil and gas sector, we will see some capital projects coming back. So we are seeing that there will be some good investments into new capex and we are well positioned there. In the transport business, which is rail business, the industry looks fine. Again, it is not a great growth industry overall, but I think it will grow 2% to 3%, and we are well positioned there.

The next business and we are calling it the industrial and geospatial view because it is two separate businesses. On the industrial segment, there has just been a lot of softness. This is the work that we do for industrial type of applications such as off-highway equipment, mining equipment and so on and so forth. The business itself is tepid. Our value proposition is also something that is not necessarily at the same level of strength with some of the other industries. So we will continue to look out and see what we can do. The geospatial market is growing. As you know, the focus on geographic data is higher than it has ever been. So everything has a geographic tag and a geographic connotation to it and we are very well positioned there. That is the reason why we pulled it out as a separate horizontal business unit. Because we want to focus on that, we want to see how we can leverage our 27-year geospatial heritage and capabilities into some of the other industries.

Semiconductors is looking a little bit weak at this point. There has been a drop in the industry, but we also have to look at it from the context of the previous year, saw in excess of 15% growth on a very large industry. So while there is a little bit of a drop, we believe our value proposition is resonating very well and one of the very good performances we had in Q4 was the capability we have in Belgium with the acquisition of AnSem, who design and manufacture end-to-end chips. We are quite bullish about that industry. There is some good pipeline that is built up. We have converted the orders and we will see growth.

Medical technology and healthcare is also in a good spot for us obviously it is a small deal, but we are trying to look at how we can grow that and how we can accelerate the growth in that business.

What I will quickly take you through is just the recap for the year in terms of how the outlook has panned out. If you look at it, at the beginning of the year we had an outlook for double-digit growth in services. We have moderated it down to 8.5% to 9.5% in constant currency. The actual number will be 7.6%, so that has been a little bit of miss. Similarly in the legacy DLM business, we said it will grow at least 20% and we had that forecast through the year or we had that outlook through the year. Unfortunately, the deferment only happened on March 29, 2019. If the deferment did not happen we would have hit that number. So that is also an unfortunate miss, but we will be at about 13% and therefore the overall DLM number was also a miss by about 5%.

But in terms of the operating profit and earnings in general, we did much better. We said double-digit growth in operating profit we did 17.3%. We started the year with OPM being flat we thought it would be marginally higher. We are essentially flat at 14%. I think the previous year was 14.1%, so essentially, we are flat on that.

We said DLM margin will improve and we actually did quite well there. We are at 4%, but more importantly we have a line of sight to do much better there next year and we are working through that.

Tax we started the year at between 22 and 23. We thought it would be about 24, 25, but we ended up with 23. We have had some good initiatives. We have also been given some sound advice in terms of how some of the other income can also be attributed to special economic zones and therefore we have been able to bring it down to 23 and I believe that we can hold at that range for the coming year, which I will comment in a second.

Net profit, we said single-digit growth we did slightly better. Though as you know there are some other onetime issues also that came in, but even if you take those out, in terms of net profit we have had a decent year in terms of because the other income and currency hedges did not necessarily play out to our benefit. So taking all that into account we have had a decent year.

So now looking at the outlook for FY2020, in terms of revenue, we will have a high single-digit growth in services in constant currency. DLM will grow by about 15% again in constant currency. EBIT will be at least in the double digit, which is earnings before interest and tax and also what we will do going forward is we will anchor the earnings number to EBIT rather than operating profit, which is what we were doing. Given that there are also some changes in accounting standards, etc., we will focus on EBIT rather than operating profit or operating profit going forward. So when we talk about margins also we will start talking about EBIT margins going forward.

The tax rate, like I said, will be between 22.5% and 23.5%, in line with the 22% EBIT. Other income is expected to be marginally higher based on the strong forex position as Ajay presented and also will have recurring export benefits.

This forecast also assumes that some of the deferment and challenges we face in services, especially in aerospace and comms that we talked about, will contribute to the first half of Q1 at least. So we will see some impact of that in Q1 and we can comment better at the end of the quarter in terms of how much that deferment has already been consumed or not, but what I can assure you is while Q1 we are just coming off these deferment issues, from Q2 onwards we are quite confident that we will have a strong second quarter and that is what gives us the confidence to comment on the high-single-digit revenue growth for services and the 15% plus for DLM.

With that, I will stop, and I believe we have some time for questions.

Moderator: Thank you very much. Ladies and gentlemen we will now begin the question and answer session. The first question is from the line of Urmil Shah from IDBI Capital. Please go ahead.

Urmil Shah: Hi Krishna, just it would be great if you can provide more colour on services growth outlook, which you have given for FY2020 across at least a large vertical?

- Krishna Bodanapu:** Sorry, Urmil. Can you say that again? I did not catch the last part.
- Urmil Shah:** Yes. Basically if you can provide more colour as to how do you expect at least a large vertical to grow in line with what guidance we have given for FY2020?
- Krishna Bodanapu:** Yes. So the aerospace business will grow at about that number. Aerospace will be high single-digits kind of a growth. Comms will be much better than that because if you look at the Communications business, when we had a rough year-end in the Communication business, overall it is still a pretty decent year. Growth in comms was 10% in constant currency, so even this year we are coming off of a decent year in terms of the Communication business not taking into account the challenge that we had towards the end of the year. So we believe comms will grow actually quite a bit higher than the single-digit growth whereas aerospace will be about that high single-digit growth.
- Urmil Shah:** Sure and also on U&G and transport, both of them saw good growth in this quarter, and transport did well on a full year basis also?
- Krishna Bodanapu:** Yes. So if you look at the transport business, transport grew well this year there were strong years, but also the challenge is the opportunity set there is limited. We work with every single transport customers. So we believe transport will be a little bit lower than high single digit. We are working on what we can do there, but transport will be a little bit lower. The U&G business will grow quite well and higher than this single-digit number. We believe that it will grow closer to double digit because what is happening is while the geospatial part of that, which we popped out as a horizontal, had some challenges and had some headwinds. The utilities is doing very well we have had a significant order intake. Also we had a good year. Again, if we break it down, we had a degrowth in geospatial, but utilities grew some 12% or 13%. So now that we also have synergies with energy we believe that we will see some good growth there also.
- Urmil Shah:** Sure. Ajay, two questions. It is about the subcon cost. Despite a lower DLM, in absolute number or as a percentage of revenue is higher as compared to other quarters, how should we look at that and secondly the export incentive was also higher than what we have had indicated in Q2, so what is a number we should build in for FY2020?
- Ajay Aggarwal:** Your voice is a little breaking. I got the second question. Let me answer the second question, and then I can come back for question #1. In terms of the other income on export incentives that we are doing, I think we, year-on-year, the number increases for two reasons. One is the volume that increases, of course, for the services that are qualified for that entitlement. So I think we have still some catching up that is being done and we keep filing for previous years, and we will be filing for the year 2018-2019 in the next year. There also there should be a volume increase and also the percentage of incentive has also been modified for that period. So it has to be higher than what is the number that has come in this quarter, but I would leave it there because you have to still wait for that final computation. Can you repeat your question #1?

- Urmil Shah:** Sure. Ajay, I was basically asking about the subcon cost. Given the decline in the DLM revenue, it is the highest in Q4 also as a percentage of revenue what has driven that and how should we look at it from FY2020 perspective?
- Ajay Aggarwal:** See, the driver of subcon cost is mainly in two areas, one is in utility and one is in communication and when we are doing the work there are some areas including for the field services where we have to use these subcontractors. It is purely based on the mix of the jobs that we are getting and I think it is quite volatile. I would say the way to look at it internally is we have gross margin for those jobs, which is in line, and subcontracting or whether we use internal resources, this is not the way we look at it. So I would say broadly, from your modeling, if we are looking at subcontracting separately, I think you can look at the current levels and then take it to the level of volume growth, but internally we really take it job by job. Even within the account it has to go job by job.
- Urmil Shah:** Thank you so much and all the best.
- Moderator:** Thank you. The next question is from the line of Pankaj Kapoor from JM Financial. Please go ahead.
- Pankaj Kapoor:** Krishna, during this year FY2019 we had at least a couple of quarters in which what we guided for versus what finally came in, there was a reasonable gap. So I am just trying to understand that how who have looked at this issue and have you made any changes to the way you try to forecast the business outlook and based on that what is giving us the confidence that even now for FY2020 when we are looking at a slightly weak start in Q1 what is the visibility we have in terms of achieving the numbers as the growth looks to be more of a back-ended one. So if you can help me just understand any learnings or any changes that you have made post the couple of misses that we had this year?
- Krishna Bodanapu:** That is a good question and I will say that obviously Q3 and Q4. Q3 was not that bad, but Q4 is when we had a quite a bit of a miss from what we originally anticipated and where the numbers have come up. So I mean I think we explained what happened both in terms of the aerospace business, the comms business and the DLM business. I would not hard too much further into that. But I think the key for us has been to understand the longer-term impact of some of the POs that are already in place. The certainty around the POs. They are not just to look at the POs, but also that is the demand, but also to look at the supplies. Because I think we are typically focused really on the demand side and if there was demand we thought that fine we will be able to achieve it, but I think the key challenge that we faced, which is what happened more or less in Q4 is the supply side did not really stood up. That is also the case of, say, the DLM. We had the demand we were not able to supply it because of various reasons. In the case of Aerospace & Defence, for the most part, the demand was there, and it was locked in. It was just the supply could not be made because of attrition challenges in some case, etc.
- So I said one is I mean obviously we have looked at the pipeline with a lot more intensity. We have looked at the pipeline with a lot more rigor all that is there, but we have also looked at the

supply equation with the same rigor as the demand equation because even if demand is there if we cannot service it then there is no point anticipating. That is one aspect of it.

And the second thing that we have also done is even in the budget we have done a fair amount of risk projections in terms of what could happen and what could not happen. So what we are guiding or what we are giving you as an outlook really is that is taking all that into account. So we are taking all the risks into account. So what we are talking about is therefore I mean it is a realistic/pessimistic scenario rather than an optimistic scenario. So that being the case, we are fairly confident that at least to start off with we have single digit is achievable because it is a while it is a little bit pessimistic, it is also realistic. So I think these are the two things. One is the supply side, and the outlook that we have has a lot of risks baked in, so we do not jump in front of the opportunities before they actually happen.

Pankaj Kapoor: So just one clarification on this. So basically you are saying it was more of a fulfillment challenge that you faced because of absence of the supply pool or the talent availability rather than anything on the client or demand side.

Krishna Bodanapu: I said 75% of it was on that, 25% was demand being pushed out.

Pankaj Kapoor: Got it. Thank you and all the best.

Moderator: Thank you. The next question is from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria: Krishna, simple question on aerospace and comms. Your growth was dragged by client-specific challenges. So ex of the largest client in each of the vertical, what would have been the growth in fiscal 2019?

Krishna Bodanapu: See, in comms, it would have been 25% ex of the largest customer, maybe slightly lower than 25%, but give or take 25%. So in comms it was really an issue of the largest customer dragging growth down. We talked about it as the POs got pushed out and the work got pushed out. It was starting to happen and we are quite confident. So that is about 25% or between 20% and 25% in comms. In Aerospace just quickly doing the math it would also be about 15% to 20% in that range. I do not know the exact number, but it will be 15% to 20%, which is the largest client there, essentially it was a small degrowth. I think there was 3% or 4% degrowth, but if I look ahead the growth in aerospace and defence is also being driven by the largest customer going forward. That gives us a little bit more confidence and certainty in terms of where next year's growth is going to come from. So to your point you take out our top customer, we actually are doing quite okay.

Gaurav Rateria: Couple of questions for Ajay, fiscal 2019, your margin was stable. It was helped by FX to the extent of 120 basis points. There was NBA investment, which you anticipated to be 100 basis points, but that turned out to be lower at around 50 basis points. So for fiscal 2020 how do you

expect to manage margins given that FX tailwind may not be there and NBA investment may actually step up from current 50 basis points?

Ajay Aggarwal:

Very fair point. I would say that there are two or three things that we are doing. One is that we have embarked on exercise for cost optimization where we are working with an external agency with a very focused program, which has started in December and which gets concluded by Q4 of the year. So that program is explicitly focusing on improving the margins through the cost optimization and some other initiatives. The entire management team, the leadership from delivery, sales, functional areas all are spending a lot of time on that particular exercise and our guidance, if you see or the outlook that we have given for the year to be flat is only for the reason that exercise is going to complete by the exit quarter. Also in this particular year, there are going to be costs associated with the exercise so but at the end of the exercise we will get a nice run rate for the coming year.

Gaurav Rateria:

Fair enough and can you please explain what the change in lease accounting will lead to impact on EBITDA line item and what would be the corresponding impact on some other line item and lastly on the other income do you expect other income to be flat in absolute terms because the FY2019 other income included some one-offs and also you will have the cash of Rs.200 Crores going away for next year because of buybacks, so would not other income come off in absolute terms?

Ajay Aggarwal:

So I would say that from the perspective of other income, if you see the hedges position that we presented, we had in this year, overall, a loss and if you have seen in the last 5 years I think this was the only year we had a loss on the forward position. That is a very strong tailwind on other income in the coming year. We have given the impact of it in this presentation based on the current spot rate, but even if you take the rate as on today we have a very strong position on other income, so that is a tailwind. In terms of the export benefits I already explained. We expect that the annual number for this year is going to be significantly higher than what we have used for 2017-2018 and filed in Q4. I cannot quantify that, but that it is slightly to be higher. Some of the one-offs will not be there in the next year, but overall based on these drivers our estimate at the current exchange rate is that our other income should be marginally higher and on tax also, as Krishna said, we are looking at continued focus on Special Economic Zone and there also we will try to work there is still room of about 50, 100 basis points to further improve.

These will be the two things which will be there between the operating profit and the EBIT. Now let me explain to you about the leasing. In the case of leasing, as most of you are aware the accounting standard calls for any agreements, which are beyond 12 months including the rent for premises, rent for machines they all have to be capitalized and you have to provide for them below the operating margin. So the impact on us is the operating margin will go up by 1.5% purely on account of this. That is why as Krishna said, it will not be a like-to-like comparison by saying that our operating margin is going higher, it will reflect in the line items, in depreciation and finance cost and at EBIT level it will be neutral and you will report at the EBIT level.

- Moderator:** Thank you. The next question is from the line of Sandeep Shah from CGS-CIMB. Please go ahead.
- Sandeep Shah:** Just wanted to understand the order intake in this quarter. On a Y-o-Y basis, both services and DLM in this quarter has gone down. So are you witnessing any slowdown in terms of macro-related stuff in any of your client discussions on the deal wins?
- Krishna Bodanapu:** Not necessarily. I think one is just a marginal change, but also we have to look at it in the context of what happens within various businesses, so some of the major customers in A&D, the purchase orders for the full year happened in Q3, and therefore Q4 is automatically lower. Actually last year what happened is in one of our large A&D customers or our largest customer the Q3 order intake actually moved into Q4. So Q4 was a little bit more inflated last year. So I will say taking that into account it is not really a major issue. It is just a point in time thing and I would also look at the order backlog, which is quite strong. So I would not be too worried about it because it is a little bit lower, because for the year also if you look at it, the order intake is about 13% higher on services and 14% higher as a company. So it is just a point in time thing.
- Sandeep Shah:** Just further to what Pankaj has asked. In terms of the guidance, if we look at for the services business this year if we exclude the inorganic growth, the growth could have been as low as 5.5% to 5.6% in CC terms. While the NASSCOM has reported that the industry growth in engineering R&D is 11% to 12%. So in terms of, Krishna, you believe that there is a need to create a lot of order book maybe through large deal wins, which some of your competitors are doing, so any clue what we are doing in terms of large deal creation, in terms of efforts and creation of separate team, or what is the focus on that because it looks like in the industry of engineering R&D also there are a lot of larger deal wins?
- Krishna Bodanapu:** The NASSCOM numbers have a lot of software product development, which are embedded into them and actually the software product development, so this is the state of work that happened for Microsoft, for Oracle, and so on and so forth. That is where there is a significant amount of growth that is actually coming. So 60% of that, Mr. Mohan Reddy is here, so obviously, we are talking from the source. So the 60% of that growth is really because of that issue. So if you look at like-for-like in our case, which is really product engineering as it relates to hardware products not software products, the number is much smaller, and it really comes down to 7%, 8% kind of a growth, 6%, 7% kind of growth. So also if you look at the competitor's number and we have diced it and sliced it in many ways, there are also inorganic is involved in that, some of them have product buyout from their customers, some of them have IT buyouts from their customers. So we have to look at the overall number rather than slice it too much because once we start to slice the number too much we do not know who is including what and so on and so forth. So I will put it in that context, but having said that though I think your point is fair that if we look at this concept of large deal wins, more than large deal wins in our industry, at least where we play, it is more about once we have won the deal we have to effectively mind the account, and we have to start winning more business because typically most customers start small and grow big and therefore the mining pit becomes quite important. So what we have done is we put a lot of focus on the smaller customers where we believe that there is a lot of potential, and we are really

focused on mining those customers because that will give us the immediate growth, but we do not report a TCV because our contracts do not come with a TCV, I can assure you that there is a lot more that is going on in terms of mining the existing customers, especially those who have a large potential so we can grow their business more in the immediate term because longer term obviously there is a bigger strategic play and we continue to work towards that.

Sandeep Shah:

Just the last question, Ajay, on the margins. If we look at your exit rate in Q4 for the consolidated business is 15% as well as for the services business it is close to around 16.4% while the full year margin is almost 100 basis points lower in both the scenario. So what are we guiding in terms of the margins for FY2020, because your exit rate is so strong that there has to be some amount of upside in terms of the Y-o-Y margins and also if you can give us some colour in terms of the DLM margins for the FY2020 from low single digit where are we looking in terms of an outlook?

Ajay Aggarwal:

Sure. So if you see from the perspective of headwinds and tailwinds into the New Year, when you look at the exit margin of 16% plus for the services we are going to all sit down and look at what kind of wage hikes or the salary increases we provide for. Right now we are assuming that something like 200 basis points is what we will be providing for the salary increases. So that is the headwind, which hits on the exit rate and as I said some of these details have to be worked out. Then you get the benefits of the operational improvement, the project I talked about. It takes about 9 months to execute. If we can do it earlier, some of those actions, then possibly the average impact of that could be higher, but as you think see the things today, I would say flat is a very reasonable expectation. With very strong Q4 of next year the cost of implementation of that program, I think we should see a significant increase from the exit 16.4% to the Q4 of the next year, which should be 18% plus. Also if you see that, what you have to keep in mind that we are, this whole discussion about our growth I think we are really investing into creating the differentiation around solutions and there also we are investing quite aggressively and we are estimating higher investments compared to the last year in FY2020. So these are the points and I think every quarter we would be able to provide you better insights depending on how we deal with the salary increases, how we deal with this program and what is the progress on this program. So at this stage, I think the best visibility is to have a flat margin, a very strong margin by the end of the year for a buildup of strong margin for the coming years, at least next 2 years.

Moderator:

Thank you. The next question is from the line of Rishi Jhunjhunwala from IIFL. Please go ahead.

Rishi Jhunjhunwala:

A couple of things I just wanted to clarify. One, you had mentioned that there were some supply side issues for the slippages that happened last year. So just wanted to understand what is the situation in terms of currently because as far as we do not see too much improvement in your headcount over the past two, three quarters as well so where are we on that front and what are the risks that it could continue to play out in first half as well?

Krishna Bodanapu:

So I think we are starting to see the head count coming in at this quarter. In Q1 we started seeing some head count coming. Actually what you also mentioned is a good point because if you look at the growth in our revenue and let us just talk about constant currency for the moment, we had

7.3% growth in revenue and I will keep it like-to-like, but our head count only increased by about 150 people or 180 people for the year, which is about 1.5%. So if you look at it of course the revenue has the inorganic piece, but also you have to look at -- people also have this organic piece, so both are like-for-like. So on a 7.3%, 7.4% constant currency growth in revenue, head count only grew 1%, 1.5%. Also if you look at, it is not because more business front onsite. It is the onsite mix is essentially flat year-on-year. So that is because where we have been able to do more with, in terms of automation, in terms of productivity, etc., etc. So we believe that, that trend will continue. Now obviously, it is a good thing from a business perspective, from sort of a job and employment creation that is a different topic for a different time, but we believe that growth would not be linear and a very good example is what is happening in, what happened in last year, and that is a reflection of why we were still able to win some significant thresholds in terms of salary increases. We did the NBA. Obviously, currency also offset it, but net-net margins were held because otherwise we would have a significant degrowth in margins. So that trend will continue. So I would not read too much into the head count because there is a lot more going on in terms of nonlinear type of revenue.

Rishi Jhunjunwala: Okay and on the tax incentive bit so. You made a comment that it will probably recur going forward as well and last year it actually ended up being more than 10% of your profit. So just wanted to understand, I mean, how does it work, how do we handle modeling if we have to and if it has to be recurring?

Ajay Aggarwal: So if you look at in the current year, we started taking these initiatives, and it was available to us from 2015-2016. So we did have the advantage of clearing the backlog in this year, but as I already explained that the last filing that we did in Q4 for 2017-2018 is the highest for any year and the filing, which will happen in the next year will be much higher than what we have filed in Q4, both in terms of the rates from the government and also the kind of volume of business that we are doing is higher, so how you should model it I would say that you can take it about 20% to 30% higher compared to where we are in Q4 for the next year and at least for the next two years in terms of the policy it is quite well stated policy and we do not expect any surprises on this. So I think on the EPS of FY2020 as well as FY2021 you can bake something 20% to 30% higher than what we have done in Q4.

Rishi Jhunjunwala: Q4 and not the full year, you were saying?

Ajay Aggarwal: That is right. So it should be somewhere between Rs.35 Crores to Rs.45 Crores or Rs.35 Crores to 50 Crores depending on the volume of those particular services. This is very specifically available for the kind of services. That is the reason we cannot anticipate it very precisely.

Rishi Jhunjunwala: Thank you.

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, Krishna. So as far your guidance goes, while I understand that it is a little bit more conservative this time around, but it is the second consecutive year of maybe a single-digit growth now in services and when I put that in the backdrop of your commentary may be regarding transportation where opportunity is slightly lesser and semiconductors, which is too small. Your commentary seems to be pretty fine as far as the opportunity set in these verticals is concerned. So I was just wondering what is that will take us to actually propel this services growth into double digits and maybe at a higher rate compared to where they are today.
- Krishna Bodanapu:** Sure. I think it is also a little bit of mathematics. Q1 is a little bit soft. So for the year, if you look at, if you just extrapolate it actually Q2, Q3, Q4, you will definitely see double-digit growth year-on-year, but it is just that we are coming off a weak quarter the issues have not been fully solved, with both demands, which is 25% and supply, which is 75%. Those issues have to be solved. So I think it is just we need to solve some of these issues in Q1, which means that hopefully, if we look three quarters over three quarters we will have a fairly robust double-digit growth. It is just that till we solve those problems I feel it is more prudent not to think very aggressively and also I would say when the demand is there the commentary was more about the demand of the industry, which is fine. So I am saying macro wise it is not really an issue. It is really how we address the opportunity is the issue.
- Ashish Chopra:** Right. But internally, you would feel that you are again well enough to actually growing double digits, but barring these slips that we witnessed in the last quarter is also impacting Q1 would that be a fair understanding?
- Krishna Bodanapu:** I do not think you would have ever come across a management team that was not optimistic about their business and that is correct I would say yes.
- Ashish Chopra:** Fair enough and just lastly from my side. So this year, including the buybacks, obviously, the payout is handsome 82%. Any thoughts around that going forward on a normalized basis do you plan to inch it up on an average?
- Krishna Bodanapu:** Yes. We agreed with the board that the dividend policy will be maintained consistently and every two years or so we will do a true-up of what our capital requirements are and what our capex, opex requirements are and whatever the additional cash we do not think we can deploy, we will pay out as a buyback. So we will continue to stick with that. I think this round went quite well. The dividend yield is 41%, 42%. The yield because of buyback will be Rs.200 Crores, so we will continue to do that. I mean even if you look at it from a yield perspective it is 2.5%, 3% on dividend, and it would also be another 2.5%, 3% on the buybacks. So those are the 5% yield this year. So anyways, the short effect is dividend, we will consistently follow and every two years, we will do a capital requirement analysis and whatever is excess we will pay back as a special buyback.
- Ashish Chopra:** That is very helpful. Thanks so much and all the best.

Moderator: Ladies and gentlemen, due to time constraints, that would be the last question. I now hand the conference over to our Chairman, Mr. B. V. R. Mohan Reddy for closing comments. Thank you and over to you Sir!

Mohan Reddy: Thank you very much to all of you for attending our Q4 and the annual earnings call. We appreciate your support. We appreciate your participation. To conclude I just want to announce that we have our Investor Day coming up on May 10, 2019. This is a personal invite to all of you. We would request all of you to come to Hyderabad and participate in our Investor Day. Thank you again.

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