“Subex Analysts’ Result Conference Call”

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SPEAKER: **Subash Menon, Founder-Chairman, MD and CEO**
Sudeesh Yezhuvath, COO and Wholetime Director
Ramanathan J., Vice President, Finance and Company Secretary

Moderator: Thank you for standing by and welcome to the Subex Analysts' Result Conference Call presented by Subash Menon, Founder-Chairman, MD and CEO, Subex; Sudeesh Yezhuvath, COO and Wholetime Director, Subex; and Ramanathan J., Vice President, Finance and Company Secretary, Finance, Subex. At this time, all participants are in a listen-only mode. There will be presentation followed by a question-and-answer session. Please be advised this conference call is being recorded today. I would like to now hand over the conference to Sudeesh. Over to you, sir.

Subash Menon: Actually this is Subash Menon here. I will start off and then I will hand over to Sudeesh. Thanks a lot for joining this call. As is our practice, we will take you through the presentation which has already been e-mailed to you all and also has been put up on the website. Sudeesh will cover the business aspects of this quarter. Then Ram will cover the financial parts, and I will come in for summary. And all of us will be available for questions and answers. So, I will hand over to Sudeesh at this point in time.

Sudeesh Yezhuvath: Good afternoon, everybody. This is Sudeesh. After the forward looking statements have been read, I will move on to the next slide which is on qualitative points for the quarter that we just finished. As we had been promising, we have been looking to sell off the non-core business of activation, and we sold it off to a company called NetCracker in the last quarter and that deal has been signed. So, the activation product stream which was part of what we had got from Syndesis has been sold off to NetCracker now with this transaction.

Another aspect I would like to update you on is that customer satisfaction survey was conducted and results have come in. And we have performed better than what we have done last year, which is still an improvement over the years before. So, the customer satisfaction results have been increasing year-on-year and that is a very important part of our business because when we look at our numbers, significant portion of our revenue order intake comes from existing customers. So, in this business it is very important that you keep your customers quite happy and that is an aspect on which the management puts a lot of focus; and the fact that we are improving and our position is fairly good, our consolidated score was in the range of around 4.2 or 4.3 out of a score of 1 to 5 and so that is a very good performance. We have also signed a deal with one of the large groups in South America. These days the Telecom business has a lot of Tel groups in different parts of the world. In South America, America Movil represents a very large group and they have operations in many different countries. They're headquartered in Mexico. They of course belong to the famous Carlos Slim who is the entrepreneur behind the group. So, we have signed a deal with them for implementing our fraud management and revenue assurance solutions across their group and this would by and by involve some replacement of a competition who were already installed at some of the properties. This is going to be something which will be rolled out over a period of time; it is a group-wide contract that we have signed. We consider this as a very important win because they are one of the two largest groups in South America and very important to have a position with them.

And the last point, managed services has been an area of continuous focus for us and it has continued to yield results and it contributed as we expected for the order intake in the quarter. So, the managed services business is also going very well.

If we move on now to the next slide which is order intake, here we are only talking about the continuing product business, after the disinvestment of the non-core business which is the activation business which of course is the continuing business, and if you look at that in the quarter just ended we did a total revenue of $23.5 million which is a good performance as we consider. And if you look at the last four quarters, you will see there is a significant uptick in the business and improvement moving forward. We expect this to continue and we expect our performance to be in this line as we move forward which represents a significant turnaround for the business. So, with that I complete the business set of slide. And I will now hand over to Ramanathan to take you through from slide number 5 onwards.

Ramanathan J.: Thank you, Sudeesh. Good evening to everyone. As you can see the continuing business revenue has grown 15% sequentially and also 26% year-on-year. We want you to look at on a constant currency basis, it is 11% and 32% because the currency has moved significantly during the quarter. And also if you are to look at the continuing business EBITDA, it reads at 41.7%. Again if you are to look at our inner constant currency because it makes sense to compare it with the last quarter. That is at 40% as compared to 39.2% in Q1 of this year. As you can see in our results, a significant amount of Apex is raised upon FCCB.

That is a non-cash item. So, if we are to exclude that we have an operational PAT for the company which reads as 240.67 million rupees for this quarter. If you compare that with the first quarter of this year, it is comparing to 141.6 million rupees. And if you are to look at the similar quarter of last year, that number reads as 196.03 million rupees. One can clearly see that the continuing business is really growing and also the EBITDAs are quite strong.

Moving on to the next slide, we have revenue of product [Unclear] [0:06:45]. As we can see, license continues to top our list. This quarter license revenue is 58% of the total revenue followed by our support which is AMC at 22%. Customization stands at 8% and managed services for the quarter is at about 12%. On the geography spread, we have been fairly consistent as in line with the previous quarter. For the quarter 2, AMEA tops the chart at 56% followed by Americas at 29% and Air Pack at about 15%. If you are to look at the qualified pipelines that stands at 428 million dollars and is growing and if you are to look at the share of product business in the total revenue, that is about 90%. It is remaining the same as what we had in the previous quarter. As you can see that product business is contributing more to the revenue and that has been the trend for the last three quarters and also the last couple of years. That brings to the end of the financial summary. I hand over to Subash for the closing summary.

Subash Menon: Thanks, JR. Coming to the summary slide, the fundamental or the key aspect that we all need to be aware of at this point in time is the fact that the company had sold pretty much non-performing or poorly performing asset which is the activation product line. As on 30th September we sold that business for the current quarter which is a new product quarter 3 and going forward we would not have a negative impact of that business on our continuing business. So, the continuing product business is only business optimization. This is what we have always had traditionally. And that has all the different products like Fraud and Revenue Assurance and Cost Management, Data Integrity Management and so on and so forth. So, until now in the three to four years when we look at the numbers what was happening was that while the core business which is this continuing product business which is business optimization was doing quite well. That was being dragged down by the poor performance of the activation business. It was significantly loss making initially. Then it kind of reached a breakeven situation and in one second split into loss over the past couple of quarters.

So, with that one could never really show the real performance of our core products business which has grown quite nicely over the past three, four years and has also clocked some significant contracts over the past, clocked some significant growth on the order intake side by entering into some large contracts with several big Telcos. So, what we can look forward to going forward is this good performance to become obvious to everybody without negative impact of the discontinued business. So, we expect our business optimization, product business to grow at about 15% to 20% while maintaining the EBITDA at 40%, the kind of number that we have had in the past, though that was not obvious because of the dampening effect of the Activation Business. Managed Services and ROC will help the company to achieve the kind of profitable growth that we are looking at. We are continuing to see traction on both fronts. And on the whole this means that the company can now, not that we have not focused on our business optimization space in the past, we have always been focused on that. But now, we can focus even more because the distraction that Activation Business was is no more there. So, in the absence of the distraction, naturally the focus can be even more sharp which would then naturally get us better returns in the quarters and the years to come. So, that is why the most significant act or event of the last quarter was the sale of Activation Business which will now start showing in our financials as we move forward. With that, we are done with our presentation and we are open to questions at this point of time. Thank you.

Moderator: Thanks, sir. At this time, if you wish to ask a question, please press, "0" "1" on your telephone keypad and wait for your name to be announced. And if you wish to cancel your request, please press "0" "2". I repeat, to ask a question, press, "0" "1" and to cancel press "0" "2". The first question is from Deepen Shah. Deepen, please go ahead and ask your question.

Deepen Shah: Subash, if you can get some more details on the financials of the Activation Business which was sold off and if you can just throw some light if this is the same business which we acquired from Syndesis?

Subash Menon: This is what we acquired from Syndesis. Most of what we acquired from Syndesis has been sold off. Financials, well, it was loss making in first quarter, it was loss making in the second quarter as well.

Deepen Shah: And what were the revenues and profits in the last year and in the first quarter?

Subash Menon: Okay, the last year's revenue from that space was about $15 million. The first half was about $3 million, this year first half.

Deepen Shah: Okay. And how about the loss or profit last year?

Subash Menon: Cost wise, the cost kind of remained at that $15 million number run rate for the year. So, for the first half about $7.5 million. So, roughly we have lost about $4.5 million in that process there.

Deepen Shah: Okay, so, $4.5 million is the loss in the first half, is it?

Subash Menon: Yeah.

Deepen Shah: Okay. And this has been transferred for what amount for consideration?

Subash Menon: I beg your pardon. What is that?

Deepen Shah: The Activation Business has been sold off for what consideration?

Subash Menon: That we have not made public debentures. I'm sorry, I cannot share that with you.

Deepen Shah: Okay, but the cost of this acquisition was about $140 million when we acquired Syndesis?

Subash Menon: $165 million.

Deepen Shah: $165 million. Okay. And at that time, what was the revenue of Syndesis?

Subash Menon: When we acquired $40 million.

Deepen Shah: $40 million, okay. Fair enough. And on the FCCB side like how is the status right now and how do you intend to repay debt?

Subash Menon: Well, the status is the same with regard to what we owe them and what we have [Unclear]. We have told in the past that we are working on raising adequate fund through whatever means to pay debt or equity or a combination of all that to pay back. So, that is where we are at.

Deepen Shah: Okay. But what kind of assumptions can we make about the cash flows of the company because we do not know the sale price of activation of the Activation Business. So, maybe if you can get some more insight on how is the cash balance of the company right now or the net cash balance.

Subahash Menon: We have been paying down bank debts over the past couple of quarters as well. So, there is no cash at this point in time, but I'll let JR speak about the cash flow.

Ramanathan J.: For the quarter, we cashed additional amount $2.4 million. For the first six months we have about $4.3 million of cash.

Deepen Shah: And at the quarter end, what is the position of debt and cash, maybe cash you do not have but, say, what is the debt on the books of the value of the company?

Ramanathan J.: Ours and FCCB's at $25.5 million.

Deepen Shah: FCCB is at, sorry, I didn't get it.

Ramanathan J.: The FCCB debt is at about 98… hold on…

Deepen Shah: 98.3, if I'm not wrong.

Ramanathan J.: 93.8, that is right.

Deepen Shah: Okay, and apart from the FCCB, any other debt?

Ramanathan J.: No. [Unclear] [0:15:49]

Deepen Shah: Okay, fair enough. Right, okay. Thank you very much and all the best.

Moderator: Thanks, Deepen. The next question is from Manish Gupta. Manish, please go ahead and ask your question.

Manish Gupta: This is a question for Ram. Ram, what is the absolute EBITDA that the RMS business generated in Q1 and Q2 of this year?

Ramanathan J.: You mean to say absolute number?

Manish Gupta: Rupees crore or million dollars, whatever.

Ramanathan J.: 39.

Manish Gupta: Okay. Sorry, I missed you for a bit, can you repeat that please?

Ramanathan J.: 39 crores in FY12 Q1. 45 crores in Q2.

Manish Gupta: 45, did you say?

Ramanathan J.: 45.

Manish Gupta: Okay, and did I get that right that the free cash flow in this quarter was $2.5 million?

Ramanathan J.: Right.

Manish Gupta: Okay. And you also mentioned that you had no other debt other than FCCB, but don't we also have some local debt?

Ramanathan J.: That is what I said. I gave the number as $25.5 million.

Manish Gupta: Other than the FCCB?

Ramanathan J.: Yes.

Manish Gupta: $25.5. How much was this local debt at the end of Q1?

Ramanathan J.: Hold on, just one minute.

Manish Gupta: Because this seems to have increased compared to last quarter, I think.

Ramanathan J.: September was 25.5 in dollar terms, June it was $26.6 million.

Manish Gupta: Sorry Ram, your voice is breaking. I don't know whether it is the problem at my end or at your end.

Ramanathan J.: In September, in dollar terms, it is 25.5; in June, it is 26.6.

Manish Gupta: Okay. And can you also share the top line of the RMS business in Q1 and Q2?

Ramanathan J.: The income from this business in Q1 is about 100.6 crores in Q1 and in Q2, about 108.4.

Manish Gupta: Okay. Thanks.

Moderator: Thanks, Manish. The next question… I request you to please stay on the line. Sorry for the inconvenience caused. Hello, sir, can you hear me?

Male Speaker: Yes, we can hear you.

Moderator: I am so sorry for this inconvenience. Participants, if you wish to ask questions, you can please press "0" "1" on your telephone keypad. The question is coming from Amitabh**.** Amitabh, please go ahead and ask your question.

Amitabh: I joined the call late and there have been a lot of disturbances in the call. So, pardon me if my question has been asked earlier or has been answered by you. But, I wanted to get some indication of our FCCB debt and the measures or the results that the company has in place to be able to meet its commitment. What is the surety or the confidence that the company has in terms of meeting our liabilities as far as the FCCB principal as well as the promise to ITM? And what is the likelihood of the company not being able to meet its commitment and thereby having its implications on the market cap of the company in the future?

Subash Menon: The total principal or amount as the face value outstanding is about $94 million including the redemption premium that will be about $131 million. We are in discussion with a variety of investors and lenders to raise a combination of debt and equity and to pay this back and we expect including possible rollover of some part of this FCCB. And we expect that to be completed within the next 1- to 2-month period at the max. We are absolutely confident of doing it. We do not think that the company will default on its liabilities on these premiums.

Amitabh: And when are these FCCB due again?

Subash Menon: March 2012.

Amitabh: Okay. But you are hopeful of concluding the fund raising well ahead of that, you are saying? When you said rollovers, this [Unclear] [0:21:31]

Moderator: Sorry, again. The next question is from Dipesh Mehta. Dipesh, can you hear me? Dipesh, you can please go ahead and ask your question.

Dipesh Mehta: I have two questions. One is that I need clarity about the activation revenue run rate. What is it for FY11 and first half? Second is about, I need accumulated losses of that business till date. And last is, whether we realize cap before quarter closing or thereafter?

Subash Menon: We have not been sharing inside information for that business until now. We just shared you some information for the first half as the business has been sold now. So, we will not be able to share anything more than that. This got closed 30th of September and cash came in as on that day.

Dipesh Mehta: So, I think in the conference call earlier you said some revenue number for Activation Business. Can you just reiterate those numbers?

Subash Menon: That's for H1. So, we said that is $1 million for quarter 1 and $2 million for quarter 2 adding up to $3 million.

Dipesh Mehta: Okay. You said some number for FY11 also?

Subash Menon: That is $15 million.

Dipesh Mehta: And you accumulated losses because 1H number you said around $4.5 million, so cumulative number can you tell that?

Subash Menon: [Unclear] [0:23:11] I have given you for Q1 and Q2, so, add the two and that's H1.

Dipesh Mehta: No, FY11, we made profit or we incurred loss in that business?

Subash Menon: Trend was [Unclear] [0:23:22].

Dipesh Mehta: Okay. Thank you.

Moderator: Thank you, Dipesh. The next question is from Nihar. Nihar, please go ahead.

Nihar: Good afternoon, sir. I just have a couple of questions. One was, I missed out the first few minutes of the call. Sir, I just wanted to know, could you give me the breakdown of your product revenues in terms of license and managed services and others?

Ramanathan J.: License is at 58%, AMC is at 22%, customization is 8% and managed services is 12%.

Nihar: Okay, thank you. And my second question was again sort of on the FCCB. I believe that you are looking at rolling over the FCCBs. Can you give us any sort of idea on the new terms at the FCCB and also in terms of there is an FCCB2 which was the unconverted or the un-exchanged portion last time which was the original bonds which are still convertible at the 650 rupees share price? Given that they did not roll over back then, what surety do we have that they will be interested in rolling over their FCCBs when they come due in March '12?

Ramanathan J.: Okay, the rollover what we are intending to talk is on FCCB2 which is the one which came for restructuring. So, the terms of restructuring, we are using the same coupon and we are looking at rolling it over till 2015.

Nihar: At the same conversion price?

Subash Menon: We are still working on all the details and we can only share this much.

Nihar: Okay, and what about the FCCB2, the original sort of which are convertible at 656? How do you plan to pay down that? That I believe $54 million is repayable, right?

Subash Menon: That is why we are looking at raising debt and equity to repay.

Nihar: Okay. That is fine. That is all from my side. Thank you.

Moderator: Thanks, Nihar. Participants, if you wish to ask any other question, please press "0" "1" on your telephone keypad. And the question is coming from Jayavardhan. Jayavardhan, you can please go ahead and ask your question.

Jayavardhan: Hi Subash, how are you? You had mentioned that you have paid some debts during the current year, but if I see the total status of the debt is exactly the same because if you are looking for 36.5 versus 25.5, FCCB being constant to the other debt, I mean if you just take the current impact from June to the current quarter end, the total net debt is exactly the same. Can you just tell me as to how much debt have you repaid actually during the quarter at the net level?

Ramanathan J.: What has been repaid is the rupee term loan of about 7.5 crores and the working capital has increased by about the corresponding amount because of the working capital consumption in the business.

Jayavardhan: Okay.

Ramanathan J.: On INR basis, you'll see an increase of about 5 crores in the debt going up from June to September. In dollar terms, obviously because of the exchange fluctuation you will see the other way around because a dollar moved up from 44 to close to about 49 at the end of September. So, in dollar terms the debt would have been lower.

Jayavardhan: In dollar term last year, you basically mentioned it was 36.5 in June and now it is 37.5. The other thing is that can you just highlight as to when you are given a provision of about 202 billion rupees or so – I think I'm right with that number – what exactly these provisions are for?

Ramanathan J.: This includes the redemption premium on FCCB that is shown under the provision line.

Jayavardhan: Oh, that is the item. And what else is there?

Ramanathan J.: Sorry?

Jayavardhan: What else?

Ramanathan J.: That is about it. That is the significant piece of that.

Jayavardhan: Okay. Fair enough. And other losses that you had, was just because of the Apex movement?

Ramanathan J.: Which one? Sorry.

Jayavardhan: The extraordinary loss which you had was only because of the Apex movement or was it something else? The 378…

Ramanathan J.: That is purely because of the exchange fluctuation. You are right.

Jayavardhan: Okay, fair enough. Thank you.

Moderator: Thanks, Jayavardhan. The next question is from Ashish Agarwal. Sir, you can please ask your question.

Ashish Agarwal: Sir, just one clarification on my side. I wanted to understand the money from selling of this Activation Business, has it come in at the end of 30th September?

Subash Menon: Yes, it has indeed come in. However, given all the cost related to that, that is pretty much of a wash. So, there is no cash coming into operations at all because of that.

Ashish Agarwal: Okay, thanks. Thanks a lot.

Moderator: Thanks, sir. Any other questions from any other participants, they can press "0" "1" on their telephone keypad. One question is coming from Amitabh again. Amitabh, you can go ahead please.

Amitabh: My question is the same pretty much some of it which you addressed but we got cut off. So, I did not get any part of your answer, honestly. So, to repeat myself, I was just concerned about the FCCB repayment issues which you said you are in the process of raising both debt and equity for some part of the repayment and rollovers. So, I just wanted a little more clarity on that as to what the reasonable options are for the company given the environment globally which is not very conducive for raising either rollovers or for debt for such type of fresh fund raising?

Subash Menon: Indeed the macro economic climate is not very conducive to grant it. Having said that, there is a specific situation here where we have cleaned up all the issues within the business that turned around completely and have a tremendous opportunity for both going forward. We are in discussion with certain potential investors who are looking at this as a growth opportunity.

Amitabh: Okay. If you can share a little bit in terms of the business, what makes us optimistic about the business in our future cash flows in terms of the growth opportunities as well as… do we have aspirations to sort of become debt-free at any point in time or at least have a debt-equity ratio which is quite low in line with most of the IT companies?

Subash Menon: We do harbor all those ambitions. Now, with regard to business itself, the last few quarters you will see that things have improved quite significantly, be it on the order intake front or revenue or profit or whatever. That is what giving us the confidence and the kind of pipeline that we are sitting on now and the kind of conversions that we are seeing from that to order intake. We expect things to be quite fine going forward.

Amitabh: Okay. And to the extent that you are looking at rollovers of the existing debt, the FCCBs, what are the possible…? I know it is probably under discussion stage and nothing is finalized yet. But what are the various options that are potentially there for the investors or for example for the company, what are you putting on the table and what possible outcome could be favorable for you? What would be your sort of wish list as to what would be the ideal terms as far the company is concerned for the restructuring of the FCCBs?

Subash Menon: Actually at this point in time, I cannot be sharing that publicly.

Amitabh: Sorry?

Subash Menon: The fact that we are in discussion with bondholders at this point in time, I quite naturally cannot be sharing that publicly.

Amitabh: Right. I was not looking at the details but broadly I guess the question was stemming from the concern that how dilutive can those provisions be in terms of let us say the conversion price is reset to the current levels or somewhere thereabout. I was just trying to get some idea about what could be the future implications of the dilution that our current ratio of debt to equity that we may see in the future and the resulting impact on the… again currently whatever the X value is of the enterprise. The moment that that equity swop happens, the debt just gets replaced by equity. So, the shareholders can potentially be… the value can bee impacted. So, that is where I was coming from as to ascertain what type of dilution is possible.

Subash Menon: Okay, in the absence of final terms, anything that we discuss here would be pure conjecture.

Amitabh: Yeah, I appreciate that.

Subash Menon: And depending upon what sort of assumptions we take, there could be wide swing in the final numbers. Honestly, I would not like to get into a discussion at this point in time. You kindly wait for another month or two and we should have better clarity.

Amitabh: Okay, fair enough. Thank you.

Moderator: Thanks, Amitabh. Participants are requested to press "0" "1" to ask questions please. I repeat, participants if you wish to ask questions, please press "0" "1" on your telephone keypad. At this time, there are no further questions from the participants. I would now like to hand over the floor back to Subash Menon. Over to you, sir.

Subash Menon: Okay, thank you. And let me summarize by stating that we have got rid of the piece of business which was creating all the problems which resulted in all the issues over the past three, four years. Now, with that gone, we can really go back to the core business and stay even more focused than the way we were in the past three, four years. We are looking at business growth going forward in line with our expectation and continuing to be quite profitable at that. So, we have been addressing our issues one step at a time. The first thing was to fix the P&L. That is all done. The business is back to good growth phase. Then we had to shed this asset which was a problematic asset. That is done. The last piece is the balance sheet. We have added and we should solve that in the next month or two. With that, we will be fully back on track and we will do business as usual. We all look forward to that and we would be back with you every quarter to give you the progress on that. Thank you very much for having joined the call today. Have a wonderful evening.

Moderator: Thank you so much. With this, we conclude the conference call for today. Thank you for your participation, and have a great day.