Hinduja Global Solutions
Q3 FY2015 Earnings Conference Call

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Management: Mr. Partha DeSarkar – CEO, Hinduja Global Solutions

Mr. Srinivas Palakodeti – CFO, Hinduja Global Solutions

Moderator Ladies and gentlemen good day and welcome to the Q3 FY2015 Earnings Conference Call of Hinduja Global Solutions Limited. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this 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. Bijay Sharma. Thank you and over to you, Mr. Sharma.

Bijay Sharma Thank you Malika. Good afternoon and welcome everyone to Hinduja Global Solutions' Q3 FY2015 Earnings Conference Call. Joining us today on this call are Mr. Partha DeSarkar, CEO and Mr. Srinivas Palakodeti, CFO. Before we begin, I would like to mention that some of the statements made in today's conference call may be forward-looking in nature and may involve risks and uncertainties. For a list of the considerations, please refer to our *Earnings Presentation*. Now, I would like to invite Mr. Partha DeSarkar to provide his perspective on the performance for this quarter. Over to you, sir.

Partha DeSarkar Thank you Bijay and welcome everyone to Hinduja Global Solutions' Earnings Conference Call for Q3 FY2015. We hope that you had a chance to review our presentation and financials, which are also available under the investors' section of our new website. I would like to start with an overview of the quarter's financials, followed by the operational highlights across key verticals and geographies and after that, I will hand over the call to our CFO – Mr. Srinivas Palakodeti to discuss the financial performance in detail. We will then open up the call for an interactive Q&A session.

In Q3 FY2015, we reported a strong revenue growth of 11.5% at Rs. 7,325 million. Growth was driven by increased contribution from the healthcare vertical which accounted for 36% of total revenues compared to 27% in the same period last year. In terms of geography, the revenue growth was broad based, even as we saw significant growth in Philippines. We achieved this performance despite some revenue loss on account of exit from non-profitable clients, which is in line with our portfolio rationalization strategy.

Coming to our margin front on a q-o-q basis, the margins at the EBITDA level improved from 11.5% to 12.3%. PBT was up from 7.4% to 8.0% and margins at PAT level were up from 5.5% to 7.2%. If you compare the margin performance across EBITDA and PAT for the previous year, you will find that the performance has been largely flat with some marginal decline and over the period of this call we are going to explain to you what had caused this marginal decline if you were to compare this performance on a year-on-year basis.

Moving to the operational performance, what I would like to say is that on an overall basis the Q3 has been on expected lines. India, Philippines, US and UK turned in strong performances. Canada has seen some pickup in demand but that will show impact from Q1 onward for the next fiscal. India domestic has been slower than usual in Q3. The healthcare vertical has been the shining star and one of the major growth drivers for our business and the trend continues in Q3. We saw growth in volumes across all healthcare clients and also added 3 new clients. The healthcare client for whom we started onshore delivery from the US in August 2014 has now become the largest client for us in the US domestic delivery operations. Margin from this vertical during the quarter was impacted a bit by the higher cost on account of ramp-up for the open enrolment session. We believe that the benefits from this investment will improve our profitability starting Q4 FY2015.

In the telecom sector, we continued to witness growth but it has remained a mixed bag. Volume from the telecom clients in Philippines remained robust, volumes in Canada improved marginally in the second half of Q3 FY2015, while India volumes have remained soft. Both geographies are expected to improve performance in the next two quarters with addition of new line business from existing clients.

In the consumer products vertical, we received additional business from a client in the fitness sector, which will be serviced from the Philippines. In the consumer electronics segment all clients who we added recently continued to perform as per our expectations. We have also added a new US based client in this vertical for onshore delivery, the engagement is expected to start from quarter Q4 FY2015. The encouraging news for this segment is that one of our UK clients has awarded us a small amount of business from India, serving the India market and we are going to set up a center for them in Mumbai.

I would now share some highlights for sales and marketing efforts and the industry recognition that we received. We are making significant investment in sales and account management to strengthen our client relationship that has given a very robust sales pipeline. We have also been making investments on brand building. As a result of these efforts, we have been recognized as one of the leading players in the contact center outsourcing space by the analyst and investor community. During Q3 FY2015, HGS has featured in a number of high profile reports that showcase our ability, our vertical expertise and our extensive capabilities to potential clients. NelsonHall recognized HGS as a leader in the customer management services for the telecommunication, cable and satellite space. You will be pleased to know that we were rated Numero-Uno in that particular vertical by NelsonHall. Gartner has included HGS in the Magic Quadrant for Customer Management Contact Center BPO. Our Preston Center in the UK also won a Silver Award for the Best Large Contact Center at a recently concluded Global Final of the Contact Center World Awards.

Now moving to the key geographies where we operate, our US operations had a very good third quarter and that was driven by the fact that we were finally able to exit from one of our large clients as a part of our portfolio rationalization strategy. For these clients we were losing some money and we decided to exit and thankfully, at the same time we were also able to ramp up our first US onshore healthcare client. The overall profitability of the company benefitted from the change in this overall business mix and the new client additions coupled with incremental business from our existing clients will help us with our growth momentum in the next fiscal year.

Our Canadian operations have been slow in the first half of the year and the slowness continues even in the second half. Some of the volume has come back but we have faced a situation of labor pull shortages in some of our centers because of which we are not able to service these volumes. To address this issue we are opening a new center in Windsor, Ontario. We currently have been able to secure demand of about 120 FTEs initially and training is expected to commence in Q4 FY2015. Based on the current pipeline, we expect this facility to reach 400 FTEs by first half of FY2016.

Our UK and Europe operations have had strong traction as well in this quarter. During this quarter, we have consolidated two of our London sites into one to service multi-lingual clients primarily for the Government and the consumer goods sector. We are also expanding our Preston site to cater to increased client demand from telecom domain. We expect the growth profile to be steady for the last quarter of the fiscal year as well with significant improvement in profitability. We are also trying to build up some healthcare business in the UK. There have been some encouraging developments with some private health insurers in the UK who are trying to leverage on our expertise for the US markets and we are very excited to see that opportunity open up.

Philippines operations have had a continued focus on ramp-ups and customer service excellence. The 5th site in Alabang, which was started in November 2014, is operating at optimum levels. The strong preference of clients for Alabang as a delivery center has led us to plan to start a 6th facility of around 420 FTEs. The new site is expected to start operations by the end of this fiscal year. HGS Philippines also received additional business from an existing client in the fitness vertical. Also a US based durable medical equipment provider has awarded us with new business to cater to their mix of back office, outbound and inbound voice transactions for its four lines of businesses. We expect this operation to maintain a steady growth trajectory in Q4 FY2015. The benefits of the new contracts will be visible from the next fiscal year due to higher cost for ongoing ramp up activity.

Coming to India, our India International operations continued its stellar performance. It experienced strong growth momentum in the healthcare vertical. The EBOS business also continues to perform well and add new clients. Our India Domestic operations performed in line with our expectations. All non-telecom clients demonstrated strong performance and were broadly profitable. However, there was some volume dip that we saw in the telecom vertical and we are expecting the vertical to remain sluggish even in Q4 FY2015.

In nutshell, we are pleased with our performance and are confident of continuing the growth momentum going forward. Our ongoing focus on sales and marketing initiatives have started yielding results, which has enabled us to consistently add new clients and grow our existing clients. Though, the profitability remained soft during the quarter, we anticipate the investments in building a strong sales pipeline and capacity addition will drive future growth with improved margins.

I would now like to hand the call over to Pala who will walk us through the financials in detail. Over to you Pala and thank you all for being with us on the call today.

Srinivas Palakodeti Thank you, Partha. Good afternoon everyone and thank you for joining on our Q3 FY2015 Earnings Call. As Partha said, traditionally our third quarter is better than the first and second quarters and the trend has continued during the current year as well. We recorded a revenue growth of 11.5% year-on-year to reach Rs.7, 325 million. In constant currency terms our growth rate for the quarter was 13.1%.

In terms of exchange rates, the average rate for the US Dollar to the Rupee was Rs. 62.30 compared to Rs. 61.97 for the quarter ended December 31. Average exchange rate for the Philippine Pesos to the US Dollar changed from Rs. 43.80 for the quarter ended December to Rs. 44.89 for the quarter ended December 2014.

On a year-to-year basis the Rupee has depreciated 0.5% against the US Dollar while the Peso has depreciated 2.5% versus the US Dollar. More significantly the Rupee has appreciated 7.1% against the Canadian Dollar leading to an overall impact of 1.6% on the reported revenue earnings in Indian Rupees which explains the gap between the constant currency growth rate of 13.1% and the reported revenue rupee growth of 11.5%. Offshore business accounted for 39.4% of the total revenues during the quarter.

The performance of the company in terms of origination of business from various geographies was in line with our expectations. For the quarter ended December 2014, US accounted for 62% of the total revenues as compared to 59% in the same period last year. Share of Canada was 19% for the quarter ended December as compared to 23% for the quarter ended December 2013. Share of UK revenues went up from 9% to 11% for the quarter ended December 2014 and the balance was contributed from India. Of the total 8% from India originated business around 5.5% came from the India CRM business and around 2.5% of the total revenues came from HGS Business Services, our HRO business.

Strong traction from clients in the vertical as well as new client additions has led to significant growth in the healthcare vertical. For the quarter ended December 2014, the healthcare vertical accounted for 36% of the revenues as compared to 27% for the quarter ended December 2013, which means an increase of about 900 basis points. Share of telecom and technology vertical declined from 32% for the quarter ended December 2013 to 28% for the quarter ended December 2014. This decline was due to ongoing portfolio rationalization initiatives, exit of a client which was unprofitable and softness in volumes in India. Contribution from the consumer segment declined from 16% for the quarter ended December 2013 to 13% for the quarter ended December 2014. The performance of recently added clients in the consumer sector was as per expectations. The share of other key verticals such as banking and financial services, media, chemicals, and biotechnology were 8%, 5% and 2% of the total revenues, respectively.

Our consolidated EBITDA for the quarter was Rs. 904 million and EBITDA margin was 12.3% as compared to 14.0% for the quarter ended 31st December 2013. The drop in EBITDA margin was primarily on account of impact of ramp-up cost in Philippines. We expect margins to improve as these investments and the cost which we have incurred in the first three quarters starts yielding results.

Employee expenses for the quarter increased by around 14% compared to the same period last year to Rs. 4,950 million. This increase was primary due to increase in total headcount across geographies driven by facilities expansion. As a percentage of sales, employee related expenses remained at 68% which was same as last year.

Our interest expense for the quarter was Rs. 95 million as compared to Rs. 108 million in the same period last year. This decline was driven by scheduled repayment of term loans and better working capital management. Our other income for the quarter ended December 2014 remained flat compared to the same period at Rs. 39 million.

Our PBT for the quarter was Rs. 589 million compared to Rs. 618 million for the same period last year. PBT for the quarter is not comparable on a year-on-year basis and it also includes the impact of higher depreciation due to the new provisions of the Companies Act. PAT margin for the quarter was 7.2% after factoring a tax reversal of Rs. 10.3 crores in an overseas subsidiary.

Based on the results, you would have noted, that the Board has approved a third interim dividend of Rs. 5 per share bringing the total dividends for the year to Rs. 15 per share.

In terms of cash flows, our cash flow from operations after working capital changes for the nine months ended 31st December 2014 were Rs. 1,417 million. We are comfortable with our current capital structure, our total debt as of 31st December 2014 was Rs. 6,297 million. Our cash and treasury surplus stood at Rs. 5,647 million, this includes around US$ 48.5 million of our Mauritius subsidiary HGS International, which have been placed as fixed deposits with Bank of Baroda London. Net debt for the quarter stood at Rs. 651 million and a net worth at the end of December 2014 stood at Rs. 15,562 million. Based on our current debt, we have a conservative leverage position of debt equity ratio 0.4x and net debt to EBITDA of 0.2x. The Business Return on Capital Employed, which is return on capital excluding the treasury surplus stood at 15.2% for the quarter. If we exclude the impact of additional depreciation due to change in the Companies Act, the Business Return on Capital Employed will be 15.7%.

Our total headcount as of 31st December was 28,630, an increase of 510 employees compared to the quarter ended September 2014. There was a significant increase in the headcount of Philippines, Canada and the US operations compared to September 2014, this was primarily due to support the additional demand from clients. Of the total headcount, 57% are based in India, 21% in Philippines, 9% in US, 10% in Canada and the remaining 3% were in UK and Europe. Of the total 16,302 employees based in India, approximately 7, 600 are for the India CRM business, 1, 600 for the HRO business and around 6,600 for the India International operations. The total number of seats as of 31st December 2014 was 28,801; an increase of 798 compared to September 2014.

With this I would like to conclude my section and would like to open the conference call for the Q&A session. Thank you very much.

Moderator Thank you very much sir. Ladies and Gentlemen, we will now begin the question-and-answer session. The first question is from the line of Govindlal Gilada who is an individual investor. Please go ahead.

Govindlal Gilada In Philippines, we have made significant CAPEX and increasing capacities in Philippines, so I want to know how it will benefit us, what is the current capacity is, how much of fresh capacities will it add and next year, how will it contribute in increasing revenue from Philippines?

Srinivas Palakodeti So, if you see between September 2014 and December 2014, we have added about 750 seats roughly and as a broad thumb rule every 50 seats will add to about $1 million of revenues if all of them are utilized. That is the broad thumb rule I can give you.

Govindlas Gilada. Sir, what is the total capacity right now including this 750? What we have done addition?

Srinivas Palakodeti In this quarter, we have added about 800. During the full year we have added 1,000+ seats.

Govindlal Gilada. 800 in third quarter?

Srinivas Palakodeti Yes.

Govindlal Gilada. And how many in the full year?

Srinivas Palakodeti Over 1,000 seats.

Govindlal Gilada. Also, mostly, have we added in the third quarter only?

Srinivas Palakodeti Yes.

Govindlal Gilada. So, what is the total capacity in Philippines now?

Srinivas Palakodeti About 7,000.

Govindlal Gilada. So for every 50 seats, we increase $1 million revenue?

Srinivas Palakodeti Yes, as a broad thumb rule.

Govindlal Gilada. Okay. So, are we making any more additions in the fourth quarter for Philippines?

Srinivas Palakodeti Yes, looking at the demand situation, we are looking at add additional seats.

Moderator Thank you. Next question is from the line of Ankit Pande from Quant Capital. Please go ahead.

Ankit Pande I actually missed the first part of the earnings call. So, can you just run me through your strategy in Canada and how that is coming through? I see through the metrics that over nine months, the revenues are down 6%, but the Canadian currency is also around 5% so it is nearly flat. Where do you see things going from here?

Partha DeSarkar The Canadian operations have had a problem with volumes in the first half of the year, but in the second half of the year the volumes have actually picked up. I did mention that fact that even though the volumes are up, we are not able to leverage on the higher volumes because we have some labor market shortages in some of the centers that we have in rural Canada. So given that situation, owing to the fact that there is demand, we are opening a new site in a place called Windsor in Canada where we will add 400 to 500 seats to take care of the increased volumes. So the volume growth is there and the reason for the flat depiction in revenue is because the Canadian currency has taken a dip. We do believe this softness may continue even in Q4 but once the center goes live, which will be in Q1 FY2016, I think somewhere around May, we will see the volumes in Canada pick up again.

Ankit Pande Is there anything to note in consumer electronics also? Because it is up by just 3% Q-o-Q, in what is seasonally a pretty strong quarter for our consumer electronics?

Partha DeSarkar If you have been hearing our conference calls, we have been talking about the fact that some of our Japanese consumer electronic clients are actually having some trouble in the marketplace. Because of that, some of the consumer electronics volumes that generally pick up around this time of the year have not picked up so much. But the good news is that while we have lost some traction with our Japanese clients, some of our Chinese clients have started to pick up and these are new clients.

Ankit Pande Have we been delivering for the Chinese brands?

Partha DeSarkar Both Philippines and the US, some of the Chinese brands have started to do very well in the US market and so you will see a shift of demand from Japanese players to Chinese players and so far as our clients are concerned.

Ankit Pande Can you also talk about the growth in BFSI this quarter? Was that along expected lines or was that a little bit higher than expected?

Partha DeSarkar In India, we are making good traction in the financial services space. Our strategy is to strive to develop other verticals in India because we do have a fairly high telecom concentration in India, that has started to do well and we believe that if that sector opens up because of easing up some regulations towards outsourcing, then that vertical could be of interest to us for the India market. As far as the US is concerned, we have had some good movement in our new center that we opened in the last week of January in El Paso, Texas, where we serve one of the biggest global insurers in the general insurance field. And also, this year, our credit card issuance client who has been with us for a very long time, has started giving us volumes from Canada that is going into Philippines, which is also doing well. These are the some financial service clients that we are doing well with. We are also adding volume in Jamaica from a local Jamaican bank, which is doing well. In addition to Jamaican clients in Jamaica, we have also been able to get some business from one of our US health insurance clients. They have just started a pilot of about 100 odd people, but we are very bullish that Jamaica will start doing very well and then we will see a lot of growth coming out of Jamaica.

Moderator Thank you. The next question is from the line of Shubhankar Ojha from SKS Capital and research. Thank you.

Shubhankar Ojha What was the volume growth for quarter three and nine months?

Srinivas Palakodeti Year-on-year basis, the volume growth is about 13% at constant exchange rates, but because of the appreciation of the rupee against the Canadian dollar, it is showing up as 11.5% in rupee terms, in revenue growth.

Shubhankar Ojha Alright. And regarding the Canadian labor issue, is it temporary? Will this get sorted in the next quarter?

Partha DeSarkar I think it can go up to quarter one. So that is when our new center will become productive, around May let's say. So that is when this will sort itself out.

Shubhankar Ojha In Philippines, out of the 7,000 capacity, what is the utilization? Are we done with the addition in Philippines?

Partha DeSarkar Are we done with addition…?

Shubhankar Ojha I mean, it is obviously a continuous process, so we have largely added a 1,000 plus for nine months. For the current financial year, are we going to add any more to the capacity there?

Partha DeSarkar Yes, we are going to. As Pala said, we are going to have another center there, because the demand for Philippines is high. We are going to see another center, it's probably required in one of our tier 2 towns in Philippines called Iloilo.

Shubhankar Ojha What would be this capacity?

Srinivas Palakodeti It would be about 400.

Shubhankar Ojha The current quarter margin is 12.3%. Are you going to see an exit rate of approximately 14%, which you have seen for the entire last year? Can we get back to that in the quarter ending in March?

Partha DeSarkar I think the full impact of all the ramp ups will probably show itself more in quarter one. If Canada goes on stream on quarter one, the work on the ramp up for the center that we are going to start in Iloilo is just going to start and it will also probably take us to quarter one to get it fully ramped up. But Pala will have a specific answer to your question.

Shubhankar Ojha I was looking for EBITDA margin, not guidance but indication and directional view on the EBITDA margin.

Srinivas Palakodeti Yes, as we have said, if you look at the first half, we have done about 11.5% in Q1 and Q2, so first half came in at 11.1% and this Q3 came in at 12.3%. On an YTD basis, it is around 11.8%. And we expect the cost of ramps in Philippines to abate as we go into Q4.

Shubhankar Ojha Okay. And lastly, how much CAPEX have we done for nine months?

Srinivas Palakodeti Yes, the total CAPEX is about Rs. 120 crores on an YTD basis.

Shubhankar Ojha What is the tax rate guidance for the current financial year since you got some credit for quarter three?

Srinivas Palakodeti Yes, there was a tax reversal of Rs. 10 crores. We expect the tax rate to be same for Q4. Obviously we won't see this kind of a tax reversal every quarter.

Moderator Thank you. Our next question is from the line of Mohit Jain from Anand Rathi. Please go ahead.

Mohit Jain Can you give the number of seats at the end of this quarter?

Srinivas Palakodeti It is about 28,800 seats.

Mohit Jain About the growth in the telecom and consumer vertical for next year, should we start looking at a double-digit growth or is it expected to be muted next year as well?

Srinivas Palakodeti We have added some new clients in the consumer sector and the numbers we have is not just consumer electronics but also consumer products and consumer services. It is a wider bag, so we do expect growth and also the fact that we are adding clients and their growth ramps ups have been as expected. But, they are still starting small so we have to see how they progress. These are new clients for us compared to the ones we had earlier, the Japanese ones.

Mohit Jain In the telecom vertical?

Srinivas Palakodeti For telecom, definitely in the US, Canada and UK we expect growth. In India, we have observed in the last two quarters, the volumes have been a little soft.

Mohit Jain Okay. What is the expected CAPEX for next year? Could you give some guidance for the fourth quarter also?

Srinivas Palakodeti It is about Rs. 120 crores for the first nine months. As we said, there may be some centers which we are looking to add. One in Canada some work would start, in Philippines we have talked about it and also the fact that even in India there is a demand for healthcare clients we are looking to add seats. But depending on how the schedules for ramp up get frozen, we may have to decide whether cost will come in before March 31or post March 31 which is still in progress and have to put a number right now.

Mohit Jain Should we look at CAPEX more like CAPEX-to-sales as a percentage when we project or do you see it as an absolute number which may sometimes exceed cash flow from operations as well?

Srinivas Palakodeti No, I think our cash flow from operations after working capital changes has been higher on an YTD basis or it is not significantly off. But sometimes for a client, we may look from a calendar year perspective but the client may want the CAPEX up and ready by March 31. So the number may get bloated for a particular quarter or a year but the advantage is, you will get revenues from that center through the rest of the quarter or the financial year. So client decisions have their own decision cycle and it is hard to dovetail to quarterly reporting numbers.

Mohit Jain Is there any change in demand environment or in terms of deal sizes in our pipeline which you would have noticed till this quarter versus last few quarters?

Partha DeSarkar It has been the usual. The second half has been as a long expected line. Typically, the second-half is stronger than the first-half because of the open enrollment session for the US healthcare clients. Demand environment is strong across all geographies. Canada has kind of caught up but we are stuck because we are getting some labor shortage in some of our centers in Canada. In India domestic, we are not sure yet as to what it will turn to, but overall India contributes a low amount to our total revenues. We are very optimistic about growth projections for the next year. It is going to be strong growth next year as well.

Mohit Jain Is the client rationalization exercise done with or not?

Partha DeSarkar Mostly, he big ones are all done. Whatever is left are the small ones.

Mohit Jain If we exclude that, can you share the growth number for the quarter?

Partha DeSarkar This growth has been achieved on top of the client rationalization.

Mohit Jain Excluding that, where would you be trending?

Partha DeSarkar So the big client that we lost was a $10 million account that we let go and we had about 300 people working in that. We moved the 300 people to another account that opened up at the same time so we did not have to incur any separation cost for people. So we have replaced $10 million of revenues almost overnight.

Moderator Thank you. Next question is from the line of Jagdish Bhanushali from Florintree. Please go ahead.

Jagdish Bhanushali I wanted to get a sense how has the healthcare vertical has performed in terms of enrollments which were supposed to pick up in November.

Partha DeSarkar We have done very well. A lot of the large ramp-ups that you are seeing in Philippines is because of that and we have also added new clients. We have added a big client in the EBOS space, which is in the durable medical equipment supplier space that will bring in new kinds of specializations in what we do. We are doing very high end work with registered nurses in Philippines. If you look at the percentage of revenues, it has gone up from 27% last year to 36% this year for the quarter. So we are really doing very well in the healthcare vertical.

Jagdish Bhanushali Because of the Canada depreciation and INR appreciation, how much would have been the headwinds on the EBITDA margins?

Srinivas Palakodeti The revenue growth which has got sort of muted because of appreciation. Some chunks of revenues go from Canada to Philippines, but even with the appreciation of the rupee versus dollar, the offshore portion from Canada is still small. But with the one which is pure Canada domestic, if I had made a $1 million of profit last year, the same million dollars will show up as 7% less in absolute rupee terms in the current quarter.

Jagdish Bhanushali Okay. And another question is that, usually for us or for the industry, healthcare is a very good margin business overall. So, even this time the healthcare business has performed very well and other verticals in rupee terms have been flattish. Should our margin have been in an upward trajectory? Is there any issue in some of the accounts in other verticals where the margins are going down?

Partha DeSarkar We had exited from a $10 million telecom client and replaced it with the healthcare client. So the fact is that on a quarter-on-quarter margin basis, our margins have actually improved. It could have been further improved if the ramp up cost pertaining to healthcare was covered, but there is a fair amount of ramp up cost of about 800 people that we had this quarter, which are not yet productive and they will become productive in Q4. There is no issue as far as profitability is concerned in any of our businesses anymore. It was there two years ago. Our India Domestic business was bleeding, but once we have downsized that business, we no longer have any parts of our portfolio which is causing any margin concern.

Jagdish Bhanushali Right. We ramped down one of the $10 million clients and we have got into one healthcare client so as far as the industry we know, healthcare margins are higher compared to other verticals as far as BPOs are concerned. Seeing the sort of service that we are providing to Healthcare margins compared to that particular client that we lost should have been a little high, there would be some transition cost. And the second thing is that the ramp up is an ongoing process of HGS which we also did in FY2014 as well. We added 1,000 employees in one of the quarters but our margins did not fall off. So wanted to understand was there a one-off in the transition cost because of change in the client or is there any vertical where the margins have come down?

Partha DeSarkar There is no vertical where the margins have come down. What you will have to bear with is the fact that there is something called a cost of growth that comes before the margins of growth come. That is exactly what you are seeing, if things could be timed exactly then cost and revenues can come in the same quarter. Sometimes, the costs come in one quarter the revenue starts accruing in the next quarter. In every quarter it is impossible to match revenues and cost at the same time. So what you would have seen last year would have been a situation where the revenues and the costs would have come in the same quarter. That is why the margins probably in percentage terms could have been better, but sometimes it is absolutely impossible to pull that off because clients give you business when it suits them right so you cannot predict it in a way that quarter-on-quarter there is something. But again I reiterate, whatever problems that we had with our portfolio is behind us with the downsizing of the India domestic business, what remains with us is a very healthy portfolio which is growing fast, our rate of growth is higher than our peer group and you have to be patient with the fact that if you see high growth it will come at a cost. Right now, if I stop growing if I do not hire anybody you will see our profitability will zoom, but that has a cost, we do not want to go down that line of stopping our growth to try to improve our profitability. We would like to balance both of them, sometimes it is impossible to time both of them at the same time.

Jagdish Bhanushali Okay, alright. And we are seeing some ramp-up in UK. In the UK, probably everything is onshore so margins will be on a lower side out over there.

Partha DeSarkar That is correct.

Jagdish Bhanushali So what sort of margins would we able to achieve by Q4 and Q1 coming because by Q1 seems all problems will be resolved as you say.

Partha DeSarkar Yes, Canadian new center will open up in Q1.

Jagdish Bhanushali And healthcare will be doing better in terms of the margins?

Partha DeSarkar That is right. We have not finished our budgeting process of next year yet. So I would ask you to hold on to that question. At some time in the near future, we will soon be able to answer that question.

Jagdish Bhanushali In the past, within four quarters we are achieving some 14% on the EBITDA margins. So wanted to understand that…

Partha DeSarkar I am sorry. I do not think that is correct.

Srinivas Palakodeti So Jagdish, for the quarter ended December 2013, it was 14%. There was a dip in the quarter ended March 2014 because there was a start-up cost for a project in UK, so that was roughly about £300K. So that is something which pulled down Q4 earnings of last year, but after that it has been basically 11.5% in the first two quarters and now at up to 12.3%.

Jagdish Bhanushali So that is what I wanted to understand. With all the problems behind us, would we be able to see ourselves at about 14% margins in coming quarters now?

Srinivas Palakodeti No, I think if you look at FY2014 overall we were at about close to 13%. So this year has a trend base that is lower because there were certain specifics both to Canada and the ramp cost in Philippines, where we will start benefiting from the investments made and the growth and the demand scenario in Canada as we move into FY2016.

Jagdish Bhanushali Okay, alright. And one more question was, what has been the CAPEX in this particular quarter, any idea?

Partha DeSarkar Yeah, it is roughly about Rs. 43 crores.

Moderator Thank you. Next question is from the line of Govindlal Gilada who is an Individual Investor. Please go ahead.

Govindlal Gilada In continuation of my last question regarding Philippines, what is present utilization on total capacities of 7,000 you told?

Srinivas Palakodeti Yeah, it is almost at full utilization.

Govindlal Gilada You have added 800 seats. You said that it will come in the fourth quarter?

Srinivas Palakodeti No, on an overall basis, there are about technically 9% empty seats but those are for people under training. Because we have reached a level we have said we are going to open an additional center.

Govindlal Gilada Okay. Correct me if I am wrong, what I understood is that this ramp-up cost has come for 800 capacities in third quarter in Philippines. Is it correct?

Srinivas Palakodeti No. Seat increase is one, the other is that we are taking people for training, so even while our center is being built-up we could still take temporary facilities and put people on training. So the impact on profitability is because of people who are under training and who are yet to go into production or started production are operating yet to reach the optimum level of efficiency.

Govindlal Gilada Yeah, that is what the cost is coming in third quarter so…

Srinivas Palakodeti No, it has been right through from Q1, Q2, Q3, it is there all through all the three quarters.

Govindlal Gilada Okay. If I can understand sir, that it will contribute in fourth quarter with what you have for ramp up and all that, fourth quarter and first quarter from Philippines. So, just as a layman, I want to understand whether now we can presume that fourth quarter margin will be little better than third quarter?

Srinivas Palakodeti Yeah, because the cost which have been incurred in Philippines in Q1, Q2, and Q3 will start tapering off and the impact which Philippines is making on the overall profitability will go away and the margins will improve because we won't have this cost.

Govindlal Gilada Yeah, so I can presume that it will little better than third quarter margin wise and sale wise?

Srinivas Palakodeti Yeah, we expect the growth to continue.

Govindlal Gilada Okay. Next year, you are projecting good growth. So can you quantify the exact growth we can see? What kind of margin can we see next year?

Partha DeSarkar It is a little too early right now. If you could bear with us for us some more time, we will be able to give you the figures. But we do not give you any guidance. We are not in a position of giving any guidance.

Moderator Thank you. Next question is from the line of Ankit Pandey from Quant Capital. Please go ahead.

Ankit Pandey Partha, could you just talk a little bit about Europe? I think I missed the commentary again but…

Partha DeSarkar We have very negligible business in Europe. Most of our Europe business is actually UK. So Europe does not really impact us as much.

Ankit Pandey Because we did invest in leadership and we built some capabilities, so…

Partha DeSarkar Yeah, so that is how UK business was slower last year, it is kind of turn-around, it has grown back. If you look at last year, it was about GBP 25 million. With this year, I think we will close by about GBP 30 million. We have added GBP 5 million on top of 25, so it is about 25% growth in one year.

Ankit Pandey So if I just read the commentary that the overall sales pack that has strengthened primarily Telecom, so the pipeline is qualified by client and it is coming to use specifically?

Partha DeSarkar Yeah.

Ankit Pandey Okay, that is good. And if I could just take up a couple of technical parameters. Pala, can you just comment on the constant currency growth? Can you give me the numbers for this quarter and may be nine months?

Srinivas Palakodeti I can send you numbers for the nine months separately, but for the quarter it is about 13% in constant currency terms, 13.1% and 11.5% is the reported revenue growth, so 1.6% has been sort of erased or not visible because of appreciation.

Ankit Pandey I understand. And as far as depreciation or the new run-rate that is possible on the depreciation side. I think this run rate is what the visibility is, the last couple of quarters has been pretty much similar in terms of percentage of revenues by that time?

Srinivas Palakodeti Yeah, maybe a little bit because we are also adding capacity.

Ankit Pandey But that is business.

Srinivas Palakodeti Yes.

Ankit Pandey Okay. And in terms of utilization, I think you did not mention that we can expect 800 more people to come into the work force next quarter. So I do assume that there is some headroom for improvement in utilization and if you could quantify that?

Srinivas Palakodeti I cannot quantify directly. But yes, definitely we have people in Philippines around a 1,000. I guess who are under training and who will start be fully productive in Q4.

Ankit Pandey Okay. And Partha, any comments on the Middle East operations that that we have just commenced?

Partha DeSarkar That is just a start up, so right now we are still exploring the market and it seems to be encouraging.

Ankit Pandey Which sectors have we invested into over there?

Partha DeSarkar We are already serving one client from Hyderabad. It is a telecom client and we have some payroll clients which get serviced out of India. We think it is an interesting market but beyond that I do not have much to report yet. It is just a start-up.

Srinivas Palakodeti Right now what we have is primarily marketing and business development.

Ankit Pandey Would you like to make any comment on the dividend policy?

Srinivas Palakodeti Nothing. We have declared three dividends of Rs. 5 each and that comes on a payout ratio about 30-40%.

Moderator Thank you. We have next question from the line of Atul Mehra from Motilal Oswal. Please go ahead.

Atul Mehra Just more of a broader question over there in terms of how would you typically look at capital efficiency in the business assuming inorganic as a part of the strategy for us so from a more since from five to seven year angle, what is the kind of capital efficiently that we can expect on a incremental as well as on ongoing basis?

Partha DeSarkar And what has inorganic got to do with that? Could you clarify that? Since you made a point about inorganic, I wanted to understand that.

Atul Mehra No, I am saying in the sense that if that is a part of strategy, from a holistic prospective, what is the kind of return on capital that we could expect?

Srinivas Palakodeti Okay, we have a fair amount of cash sitting in the books. So the way we would like to do is to look at what have a measure called business return on capital employed, which is basically taking out the impact of cash and the treasury income. So I said for this quarter it comes in at about 15.7% if you exclude the impact of extra depreciation as per Company's Act otherwise it is about 15.2%. So in the last year, we did about 16.6% for full year.

Atul Mehra It will be pre-tax right?

Srinivas Palakodeti Yeah, EBIT on average capital employed..

Atul Mehra Yeah. So where can we possibly look at this number going to the medium-term?

Srinivas Palakodeti No, I have showed you what we have just one year ago and obviously our endeavor is to improve both margins and the return on capital employed.

Partha DeSarkar And the fact that the depreciation policy actually has changed this year have impacted the reported this thing.

Atul Mehra Right. But if you have to just look at maybe where we can potentially go to in terms of return on capital, is there a number that you would be targeting internally?

Partha DeSarkar Unfortunately, we do not give any guidance.

Moderator Thank you. As there are no further questions from the participants I would now like to hand over the floor back to Mr. Partha for his closing comments. Over to you sir.

Partha De Sarkar Thank you very much for being a part of this call and taking your time to listen to us. We expect our next quarter ending to happen sometime in May, the specific date will be announced by our Investor Relations team. Once again, thank you very much for taking your time to listen to us.

Moderator Thank you very much sir. Ladies and gentlemen, on behalf of Hinduja Global Solutions Limited, that concludes this conference call. Thank you for joining us. You may now disconnect your lines.

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Note: This transcript has been edited to improve readability