Hinduja Global Solutions
Q1 FY2016
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 Q1 FY2016 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 the conference call, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Bijay Sharma. Thank you and over to you, sir.

Bijay Sharma: Thank you Zaid. Good afternoon and welcome everyone to Hinduja Global Solutions Q1 FY2016 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 such 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 Good afternoon everyone. Thanks for joining us on the call today. We hope that you had a chance to review our presentations and financials which are also available under the investor sections on our website.

I would like to start with an overview of the financials for the quarter, this will be followed by operational highlights, 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 up for a Q&A session.

In the first quarter, we continued our momentum in top-line expansion. The revenue increased by 10.9% year-on-year to Rs. 7,388 million primarily driven by growth in the healthcare vertical. Of this growth of 10.9% in rupee terms, 2.3% growth is in account of exchange rate variation, 5.7% is on account of volume growth and 2.9% is on account of the Colibrium acquisition that we did in end March 2015.

As you know, first quarter is traditionally a slow quarter for HGS. However, Q1 FY2016 was slower than expected**,** this was mainly due to lower volumes in some geographies such as Canada, the US and Philippines which impacted utilization levels and profitability. The EBITDA for the quarter was Rs. 541 million with a margin of 7.3%. EBITDA for the quarter declined by 29.3% year-on-year. The PAT for the quarter was Rs.162 million with a margin of 2.2%. PAT for the quarter declined by 50.3% compared to the same period last year. The Board has approved an interim dividend of Rs.5 per share.

A big dent in our profitability has largely been driven by our performance in Canada. It has been a perfect storm in this particular geography and let me explain to you what is happening in Canada. You may be aware that the Canadian economy is going through a slowdown, the crashing oil prices has resulted in a semi-recession situation in Canada. The Exchange rate over the last four years has dipped by about 40%. We were operating with a low cost model out of rural Canada, and we are finding it very difficult to attract labor force in rural Canada and fill up our centers. So we have to shift from rural centers which were low cost to urban centers thereby increasing the cost of our operations. This has resulted in a need to close some of our smaller rural sites and this labor shortage has also caused an increase in their minimum wage. The Government of Canada used to earlier give us apprentice tax credit as grants, those have also been withdrawn. These two factors have seen an increase in cost of operations, which have severely impacted our margins. The impact of all of this has been rather severe and the operation for this quarter has run into losses.

We are working on renegotiating pricing and other contractual terms with our largest client in Canada to fix this. We are their largest vendor and so it is in our mutual interest to find a solution at the earliest. We expect to finalize our contract by the end of Q2, hopefully in favorable terms…we are banking on repricing some of these contracts to reflect the higher cost of operation.

Taking cognizance of this prevailing environment, we have also undertaken some cost containing measures on our side by giving people voluntary time-off, wage freeze for exempt employees and other expense rationalization measures like cut in travel and entertainment.

The silver lining in the situation is that, while overall the Canadian situation may look gloomy we have won a new client in Canada in the public sector. This project is expected to go live in Q3 and would ramp up to about 140 FTEs with a potential to increase to a multi-million dollar worth of annual revenues. Our estimate as of this point of time would be about $6 million in annual revenue from this particular contract. This year we will only see probably half of that coming in, the full year impact will be visible next fiscal.

Let me share some of the positive highlights from the quarter.

We continue to make progress on a number of fronts. With a solid growth of 43% in rupee terms the healthcare vertical continued to be the primary growth driver for us in the quarter. The revenue contribution of our healthcare vertical has increased from 32% in Q1 FY2015 to 41% in Q1 FY2016. Of this 43% growth, 9% is on account of the Colibrium acquisition while the balance is from volume growth.

We continue to experience strong traction from clients in this vertical across all the geographies. The EBOS business has added two new clients including a durable medical equipment company which would be serviced from both India and Philippines. This is a large start-up. A new SEZ in Hyderabad will go live in September to service this client. In Philippines we have received significant additional businesses form two existing healthcare clients, we expect to start support for one of them for Q2 FY2016 with 60 FTEs while the second engagement has the potential to ramp up to 200 FTEs. Our delivery center in Jamaica is expected to service its second healthcare client during the second half of FY2016. In the US we are getting ready for open enrolment season for healthcare which is typically a very busy season for us and brings in additional volumes within Q3 and Q4. This is particularly important for Colibrium, the business that we acquired last year. We are in the middle of this integration and the progress has been smooth.

During this quarter, HGS was recognized by various outsourcing research and analyst firms for its expertise in healthcare. This is a testament to Company's leadership position in this vertical.

Some of the recognitions are:

We were named as a leader in every market segment in the NelsonHall Healthcare Customer Management Services' NEAT Report. This report includes Payer and Provider CMS and back office and evaluated a total of 10 vendors. We were seen as the foremost leader in having the ability to meet future requirements for healthcare payer back office. We were also included in the HfS Population Health and Care Management Blueprint Report and are amongst the top three out of the eight vendors evaluated on ability to execute.

Our public sector has shown very encouraging growth signs. We are betting big on the public sector vertical and the expertise gained from having worked with major clients in this sector is paying dividend. As mentioned earlier, we have made inroads in the public sector segment in Canada with a significant win this quarter. Our UK business has won two new big contracts, each with annual revenues to the tune of $10 million from the UK public sector. As of this moment, we are not able to share further details, but these two wins will transform our UK business which has been subscale for some time. These engagements further boost the execution of our UK growth strategy taking our delivery center network to near capacity with new strategic centers in the offering.

New wins:

Our focus on proactive solutioning and customer experience, BPM and digital enablement is resonating in the market. We continue to win contracts with both existing clients and new logos. The developments in this quarter include:

- We have signed contracts for providing services to a UK high-street retailer to support its telecom product and for supporting the launch of a telecom company in Ireland.
- We have encouraging business flowing from a fitness company that has become our client since last year. This business is ramping up quickly in Philippines.
- Several clients are ramping up their business in Philippines; all the new centers we added last year have gone on stream and are filling up quickly even as we commissioned additional capacity in Manila and Iloilo**.** This year is going to be a strong year for Philippines.

Update on acquisitions:

We already talked about Colibrium earlier. In end June HGS signed definitive agreements to acquire a significant part of Mphasis group's BPM business in India. HGS has recently received approval for the acquisition from the Competition Commission of India and that transaction is expected to be closed in quarter ending 30th September 2015. This acquisition is opportunistic for us as we see an environment of bullishness in India where companies are getting back into investment mode and looking for ways to enable higher growth. The transaction will add significant scale for HGS in India with over 7,000 customer experienced professional and a wider footprint by adding seven delivery centers across six cities. HGS will also gain delivery presence in Hindi speaking areas like Noida, Raipur and Indore, something that we lacked in our network today. The business includes five marquee clients in the telecom and banking & financial sectors and the acquisition is expected to have annual revenues of Rs. 160 crores.

Looking ahead in today's dynamic environment, the right innovation at the right time can be a game changer. This means that the organizations need to be closely aligned with changing trends to make inroads in a competitive market. HGS is making significant investments and taking initiatives that are making or can create an impact in the customer experience industry. With a digital world becoming the new normal, we are focusing on building digital capabilities by leveraging the nexus of forces which is social, mobile, big data, cloud and the internet of things to enable digital value for clients. The solutions are geared towards customer experience, knowledge and insights, agility and efficiency. HGS is also looking to bring in more non-linearity into its organization. I believe that a platform and automation solution's portfolio can help us expand into new areas of services and emerging markets.

To summarize, our performance over the past couple of quarters has been a bit below expectation primarily due to volatility in volume changes and the Canadian environment. We believe that the requisite steps have been taken to ensure long-term and sustainable growth of the Company. Our sales pipeline continues to be strong across key verticals and geographies. We are confident that the healthy conversion of this pipeline will result in better performance in the coming quarters.

I would now like to hand it over to Pala who will walk us through the financials in detail. Thank you all once again for being with us on the call today. Over to you, Pala.

Srinivas Palakodeti: Thank you, Partha. Good afternoon everyone and thank you for joining on our Q1 FY2016 Earnings Call. As mentioned by Partha earlier, the financials for Q1 declared are without the impact of the proposed Mphasis BPM acquisition. The transaction documents were signed on June 30th, 2015 and the transaction is expected to close towards the end of this month, so the impact of the Mphasis BPM acquisition would be reported for the quarter ending September.

Our revenue for the quarter increased by 10.9% to Rs. 7,388 million compared to the same period last year. Excluding the impact of foreign exchange rate our growth rate was 8.6%. Of the total revenues around 40% of the revenues have offshore delivery and are exposed to cross currency movements. Compared to the quarter ended June 2014, rupee has depreciated 6.3% against the USD while the Pilipino Peso has depreciated 1.6% against the USD. On the other hand rupee has appreciated 6.8% against the Canadian dollar and 2.9% against the British Pound. Based on the mix of the currencies of our business the rupee revenue growth had an uplift of 2.3% on account of exchange rate variation.

Revenue origination from various geographies was broadly in line with our expectation. For the quarter ended June 2015 US accounted for 66% of the total revenues compared to the 62% in the same period last year. This growth was primarily been driven by the healthcare vertical revenues. With softness in volumes in Canada and appreciation of the rupee against the Canadian dollar share of Canada originated revenues has dropped from 19% to 16%. Share of UK and Europe originated business increased from 10% in quarter ended June 2014 to 11% in the quarter ended June 2015. In terms of India originated business, 6% of the total revenues came from the CRM business and the balance 2% came from our HRO business.

As compared to the quarter ended June 2014 share of Healthcare has increased from 32% to 41%, softness in volumes in Canada and other geographies has lead to the share of telecom revenues dropping from 29% to 25%. Share of the consumer vertical has dropped from 15% to 13%. While volumes from the old consumer electronic clients continue to remain soft, volumes from new logos added from consumer packaged goods and other consumer brands are performing well. The share of BFS vertical was 7%, media was 5%, chemicals, and biotech was 2%.

Our consolidated EBITDA for the quarter declined by 29% to Rs. 541 million and the margin was 7.3%. Employee benefit expenses for the year increased by around 14% compared to the same period to Rs. 5,175 million. This increase is primarily due to increase in headcount across geographies as well as salary increases as a result of increase in wage rate in geographies such as Canada. Our interest expense for the quarter was Rs. 96 million compared to Rs. 108 million in the same period last year. Other income for the quarter ended June 2015 increased to Rs. 102 million compared to Rs. 79 million in Q1 of last year primarily due to exchange rate variations. As a result of the drop in the EBITDA margin our profit before tax for the quarter was Rs. 251 million as compared to Rs. 458 million for the same period last year and profit after tax for the quarter came in Rs. 162 million, a decline of about 50% over the same quarter last year.

In terms of capital structure, our total debt as on 30th June was Rs. 7,276 million, our cash and treasury surplus at the end of the year was Rs. 5,081 million. This includes around $37 million of funds of our subsidiary HGS international Mauritius in the form of fixed deposits with the Bank of Baroda. Taking into account the cash and treasury surplus, net debt as of 30th June stood at Rs. 2,195 million. Our net worth as of 30th June 2015 is Rs. 11,177 million. Based on the current debt levels we have a debt to equity ratio of 0.65x and net debt to trailing 12 months EBITDA of 0.74x. The return on capital employed excluding treasury and surplus cash was 8.5%.

As on 30th June we had a total headcount of 29,531, of this 57% are based in India, 22% in Philippines, 8% in US, 9% in Canada and the remaining 4% are in UK and in Europe. Of the total 16,895 employees in India, around 7,500 are for the India CRM business, around 1,600 are for the HRO business and the balance are for India International and shared corporate function. The total number of seats as of June 30th, 2015 was 30,390, an increase of 844 seats compared to March 2015.

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

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the question-and-answer session. Our first question is from the line of Ravi Menon from Elara Securities. Please go ahead.

Ravi Menon: Do you have a target debt equity band that you would like to operate in?

Srinivas Palakodeti: No, we do not have any target debt equity ratio. We have currently as I said cash and treasury surplus of about Rs. 508 crores, so our focus would be to utilize that. At the same time we also try to take advantage of tax shields on interest in different geographies, while we decide whether to borrow or not. But we do not have any target debt equity number.

Ravi Menon: I was wondering if this limits your ability to make any attractive investments in say new acquisitions or even expansion in any geographies in terms of CAPEX, you do not see that as being any concern?

Srinivas Palakodeti: No, as I said we have cash and treasury surplus available for investments and we have a fairly strong balance sheet and when you are talking of debt equity that is what you are talking off gross debt, obviously on a net debt level if we have a net debt of about Rs. 220 crores and net worth of about over Rs. 1,100 crores, if you look at from that perspective it is even much lower.

Ravi Menon: And what is your target CAPEX for the year sir?

Srinivas Palakodeti: So this quarter we have spent about close to Rs. 46 - 47 crores, and this is primarily on the account of the expansions which were initiated for opening centers in Canada and in Philippines in the latter half of the previous financial year. So that is what you are seeing in the current year. Last year we had a CAPEX spend of about Rs. 162 crores, our sense is that it would be lower than that but the final numbers are a outcome of how new business or orders are coming in.

Ravi Menon: And one more thing, last year around the first quarter we said that there has been some impact of seasonality in the Canadian revenues and this year it seems despite that low base we still seem to have come off a little more. So is there any specific client issue as well, is the client having problem with their own end demand and therefore is there an impact on your volumes?

Partha DeSarkar: I tried to explain the Canadian situation in fairly great detail at the beginning of the call, quite a few issues. Some are mostly macroeconomic which is slowdown of Canadian economy, the drop in the exchange rate which actually reduces the reported income and the top-line that comes from Canada when you look at translation, the move from rural to urban markets, the labor shortage, the increase in minimum wages all of that has increased the cost of operations. We have gone back to our clients and asked for revision of prices to reflect adequate margins to service them. We are the largest vendor for our clients and therefore it is in the client interest to make sure that we do business profitably. We do believe that we will have a positive outcome out of those negotiations, we expect to close these negotiations by the end of Q2.

Ravi Menon: So what you have explained in a lot of detail was supply side of the issue that you were finding it difficult to staff up in the rural and therefore you just had to move to urban centers. So my question is more on the demand side, is there also a demand issue as well that was my question?

Partha DeSarkar: We had volume softness in the Q1 but that is seasonal, I mean it is not something very different from what we have seen in previous year. The volumes start picking up towards the end of Q2, and Q3 and Q4 is when the volumes are actually there in full flow. We do not expect to see any change to that but as I said we will be able to give you a better update of that by the end of Q2.

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

Rahul Jain: Just a couple of questions, firstly if you could tell in terms of the growth pipeline we have done some couple of inorganic efforts in the recent past, so going forward how do you see the business shaping up in terms of the growth potential organically and any inorganic strategy in the mind?

Partha DeSarkar: If you look at our CAGR for the last four, five years that has been in excess of about 20%. If you were to look at growth on a pure organic basis last year our growth in a pure organic basis was I would say somewhere in the 11% to 12% range, so that explains how we have grown. We have completed two acquisitions this year, one was closed in March, this was a healthcare company called Colibrium, and we have talked about that in the previous call. This year we have had a very opportunistic acquisition that we were able to do with Mphasis when we were able to buy off their domestic BPM business for Rs. 17 crores. This transaction has just received regulatory approvals last week, we are expecting to close that very soon and revenues and the bottom-line from that business would show in our books from Q3 and Q4 onwards.

Rahul Jain: And so from a going forward perspective what is the strategy in mind in terms of what we should focus on and what should be the accepted level of growth one can expect in those lines?

Partha DeSarkar: I mentioned that our CAGR for the last four five years has been in excess of 20%.

Rahul Jain: So the similar growth one can expect going forward?

Partha DeSarkar: I cannot give you a forward guidance, but when I give you a CAGR for the last four five years, I am not talking about one year, I am talking about a track record of about four, five years, our growth has been very healthy.

Rahul Jain: Secondly in terms of this Mphasis acquisition what is the total amount we have paid for this?

Partha DeSarkar: Rs. 17 crores is the purchase consideration.

Rahul Jain: And we said around Rs. 160 odd crores of revenue we would expect from this?

Partha DeSarkar: That is correct.

Rahul Jain: So any reason why we have got this transaction at this cost and what is the expected EBITDA margin over a long-term on this kind of a deal?

Partha DeSarkar: You would have read in the media and I do not know whether you track Mphasis, their rationale was to exit from India domestic business because that was not part of their strategy, they wanted to exit from this business and they were looking for a right home for their employees and that is why they did this transaction to strategically focus on IT.

Rahul Jain: And what are our thoughts on it, what is the long-term margin achievable?

Partha DeSarkar: We have been able to reprice all our contracts when we took over this business, most of our contracts, not all, most of the major contracts we have been able to reprice and therefore there is an uplift that we are expecting because of that repricing. We expect this transaction to be EPS accretive to us. By the time the integration is over which we are expecting to be over by Q4 this is going to generate healthy margins for us which is typical of Indian domestic business.

Rahul Jain: So EPS attractive obviously because we have not paid anything for it but will it be margin accretive as well?

Partha DeSarkar: Yes, it will be. But you understand that India domestic margins are lower margins than international businesses, right.

Rahul Jain: Right. And secondly in this the kind of employees which we have taken as part of this acquisition in terms of their salary structure how it is different from a similar set of people within the HGS brand?

Partha DeSarkar: Not dramatically different, it will be more or less in the same ballpark.

Moderator: Thank you. Our next question is from the line of Sahil Jain from Money Curve Investments. Please go ahead.

Sahil Jain: I have understood the Canada impact. Our revenues have gone up which is good to see, should that not have partly offset due to economies of scale the challenges on the Canadian side? The drop in margin is quite alarming. So how do I perceive that? We got increase in sales and the economies of scale still could not offset, and how should the margin picture be going forward? Is there some one-offs from the Canadian side, have we set it right, could we expect uptick in margins going forward?

Partha DeSarkar: Sir if you have been following our performance you would find that our year begins slow, there is a seasonality in our business and therefore Q3 and Q4 is when our capacity utilization is at its peak and therefore margins are lower in Q1 and generally improve over the rest of the year. We expect this year also to follow similar norms. We expect that we will be able to replicate the margin improvement performance that we have done year-on-year. About the Canadian situation, as I explained to you the Canadian situation is a bit complex because it is not a one-off transaction that is causing us the headwinds in Canada. It is a mix of the state of the economy, the state of the exchange rate, the fact that labor costs have gone up, the fact that there is a migration of labor from rural markets to urban markets and therefore an increase in cost of operation. So we have been talking to our client who is also coincidently our second largest client globally to get a proportionate increase in our prices. The negotiations are underway and we believe that we will be able to conclude those negotiations favorably by the end of Q2. So the answer to your question, the Canadian situation is a little more difficult but it is not likely to impact the other businesses that we have which are doing very well and therefore those businesses will continue to result in increased margins going forward the way we see the business today and the Canadian situation also we believe by Q2 we will have a satisfactory resolution with our clients.

Moderator: Thank you. The next question is from the line of Shubhankar Ojha from SKS Capital & Research. Please go ahead.

Shubhankar Ojha: Sir it is exactly on the similar line on the Canadian operations, you said Q2 end you will in the position to renegotiate with your clients in Canada, so your Q2 margins will also get impacted because of this?

Partha DeSarkar: The Canadian performance in Q2 will be soft but the rest of the geograpies should be able to pull our margins up.

Shubhankar Ojha: So June is obviously seasonally a poor quarter in terms of margin, but what was disappointing for the quarter was year-on-year sharp drop in the margin. So are we in a position to get back to a double-digit margin for FY2016?

Srinivas Palakodeti: Being traditionally weak quarter, the problems in Canada have aggravated the overall profitability resulting in substantial drop in the margin. But as Partha said, while Canada will have a soft performance continuing into Q2, we expect the other parts of the business to pull up and this increase in margin we expect to continue through Q3 and Q4.

Shubhankar Ojha: Secondly you mentioned the Mphasis acquisition you paid how much, Rs. 17 crores right?

Srinivas Palakodeti: We have not paid, what we have agreed to pay is Rs.17 crores, the transaction is not yet closed.

Shubhankar Ojha: And the financials of that will come only in next financial year because you will close that deal by year end, right?

Srinivas Palakodeti: No, no we expect to close by end of the month so we will have one month impact in Q2 and then the full three months through Q3 and Q4. So we expect to get about seven months of revenues into FY2016.

Moderator: Thank you. Our next question is from the line of Sarthak Sayyal from CRISIL. Please go ahead.

Sarthak Sayyal: Sir basically two questions, instead of seeing it geography wise if we see it vertical wise also, the telecom vertical has seen a decline in the revenue, so is this because of the vertical being served out of Canada?

Partha DeSarkar: That is correct.

Sarthak Sayyal: And sir on the health insurance side as we are seeing good pick up and traction in the segment, so how much growth potential is there in this segment, I mean while I know that a number would not be a good reflection of the growth but I mean how do you see this shaping up and till what extent you see the growth?

Partha DeSarkar: Look, the healthcare vertical is a massive vertical and because of the reforms in the healthcare sector driven by President Obama himself, the growth has been very-very good for us. On top of that if you look at the ratings that the analyst firms have done for us, you can go to our website and find those ratings, they have rated us very highly in terms of current capability and future capabilities both, we are rated leaders in all three segments that they have rated us. So a combination of having solid clients for the last 15 years demonstrated domain expertise and ability to execute for current clients and future needs of the industry, we are placed very strongly in this domain. We are very bullish about this, this is our strongest domain, this is the only domain that we are verticalized, the rest of the domains we are not. So we are very bullish about how healthcare is going to be panning out for us.

Sarthak Sayyal: So sir do we expect some mid-teens kind of a growth year-on-year still in the coming quarters or let's say for the coming year or the next year or so?

Partha DeSarkar: See growth has never been a challenge for us, if you have been tracking us we have always shown good growth, the problem has been the inconsistency with our margins. In some years it has been something, in some years it has been something else. So that has been our constant endeavor to make sure that there is predictability in our margin performance. I have to concede the fact that we are onshore heavy and this has a certain dilution impact on our margins, if we were a pure offshore player then our margins probably would have been healthier, but if you had been pure offshore our growth would have also been much slower. The reason why we grow faster than our peer group is because we have a large onshore presence and that large onshore if you were to compare this as a funnel the large onshore gives us a bigger funnel which eventually improves the offshore performance as well. So that has been our strategy. Now what has hurt us is the Canadian performance because the Canadian performance is about $96 million book of business out of which offshoring over the last four years has only been about 300 seats. It will improve. I believe that we will get more offshore out of Canada and that is when the mix of businesses from Canada will actually improve because our onshore margin is not high, we go onshore so that we can push more offshore. As more and more businesses get sourced out of Canada into Philippines and India that is when a justification of having a high onshore presence will actually play out, so we will have to be a little patient with that. Our strategy has been to show high growth to our clients and that can only achieved if you have a good presence onshore. If we were to be a pure offshore player our margins will probably be much higher than what it is today, but then our growth will also slow down to low single-digits. So it is a balance between growth and margins.

Sarthak Sayyal: So sir now that we are well placed to see the growth numbers, we have the operations, we have done some acquisitions as well, do we see not a near term but a gradual shift in strategy towards more offshore mix to support the margins, not in the near term may be a five year or a seven year kind of a strategy on that part?

Partha DeSarkar: I will ask Pala to tell you the exact percentage of our offshore story over the period of time how it has moved. So before I give it up to Pala let me say one thing, there are two things that we have done, Pala will give you the numbers. Our offshore percentage as a percentage of revenue has actually gone up over the period of the last two three years, that Pala will share you those numbers. On top of that if you look at what we have done with Colibrium, which is actually a platform play which means that it is non-linear in nature, therefore we would be able to add revenues faster than seats. As Colibrium settles down, it is a start-up and we have just acquired the company and the integration is going on, next year Colibrium is going to be a game changer for us because it is a very important play in the healthcare sector and it is non-linear platform based. So those are the two things, non-linear platform play and increased offshoring from the onshore base that we have, these are our two trump cards that we hope to play out in the future. So Pala will you share with him how our offshore percentages have gone up?

Srinivas Palakodeti: Yes, so for this quarter about 40% of our revenues had an offshore delivery component, and if you go back about three years it would be in the 32- 33% range.

Sarthak Sayyal: And sir one more question I had, so do we have any plans to maybe get into digital or social media sector, are any plans materializing as of now or maybe in two years time do we see that opportunity being tapped?

Partha DeSarkar: We have a very strong presence in digital and social media space, but we only service the Indian market today. The capability is very strong and we are now taking that capability onshore as well. We have a team of about 160 people who work in this space of digital marketing, social media analytics and all of that. This capability as I said has been developed for the Indian market where we are finding increased acceptance of this capability. We are investing in this business to take this capability onshore as well because that is where we believe the price points are much-much better.

Moderator: Thank you. Our next question is from the line of Rukun Tarachandani from Kotak PMS. Please go ahead.

Rukun Tarachandani: Sir just wanted to understand, how does the management look at the profitability of the business, I mean on the reported return ratios the ROCs are pretty low, if you exclude the goodwill I think the return on tangible assets would be on a 20% plus kind of a basis, so how does the management look at it, do you think this as a business this is a 20% plus kind of an ROC business?

Srinivas Palakodeti: If you look at our balance sheet we have had a different point in time different levels of cash, but if you look at FY2014 which was a real good year for us, our business return on capital employed, which basically excludes the treasury surplus as well as the corresponding interest income, was about 16.6%. You can remove, if you wish, the goodwill on consolidation which is somewhere in the range of about Rs. 500 crores as of March 2014, then you know what the business is capable of delivering.

Rukun Tarachandani: Sir the next question is, on the face of it this appears to be a very commoditized business, so what is really your competitive advantage that helps you earn these kind of returns?

Partha DeSarkar: We are not into the commoditized space, so that is a very generic comment that you just made, there are various spaces in which people work. We work in healthcare which is highly domain specific, we work with thousands of nurses and medical coders and doctors in that particular space. We work in very high end of technical troubleshooting and all of that, we work with some of the best FMCG brands that you can talk about. So we are not really in the commoditized space, I will hesitate to call the business that we are in being very commoditized because I think you will have various spectrums of players who operate in that so we would probably not fall in that space.

Rukun Tarachandani: And sir one last question, so just before you made the comment that the onshore to offshore has increased from 32% to 40% odd, and when I look at the margins on a consol level they have actually come down from your March 2010-11 kind of levels. So what were the other factors that lead to that margin decline?

Srinivas Palakodeti: So see if you are looking at the financial year ended March 2009 or 2010 that was a much smaller business and we had a completely different profile. So basically there were only two originating geographies either US or India and that was if I recall correctly in the year ended March 2010, we had a top-line of about Rs. 890 crores, so when you compare that, there is a Rs. 2,800 crores top-line for the year ended March 2015, so that is a growth but the mix has also changed. So obviously the businesses which we have acquired in UK and Canada are same shore. The payroll business which we have acquired is onshore, these are businesses which have a different margin profile and obviously when you change the mix of onshore offshore it changes substantially. But the reason is for doing these acquisitions and having a strong onshore presence is to basically build a funnel for growth for the offshore business. Some of our clients are really big clients and just becoming an approved vendor is a long process so if you are a vendor who offers only offshore delivery as opposed to somebody who wants onshore and offshore then obviously the vendor would offer the global delivery model would be chosen as opposed to somebody who offers only offshore. And the choice of how much to do onshore and how much to do offshore is driven by what the client wants and also sometimes there are regulatory issues with some kind of work. Let's say if it is originating from the government has to be done onshore and cannot be offshore.

Rukun Tarachandani: And sir what was cash flow from operations for last financial year?

Srinivas Palakodeti: So the cash flow from operations after working capital for the year ended March 2015 was Rs. 192 crores.

Moderator: Thank you. Our next question is from the line of Jagdish Bhanushali from Florintree Advisors. Please go ahead.

Jagdish Bhanushali: I think I may have missed, but wanted to know what was the average dollar rate for this quarter?

Srinivas Palakodeti: See reporting from currency perspective the average dollar rate was Rs. 63.65 as compared to Rs. 59.86 for the quarter ended June 2014.

Jagdish Bhanushali: And the earlier comment I just missed that the breakup of the revenue growth of about 10.9%, so what was attributable to volume and currency, could you please give it to me?

Srinivas Palakodeti: Yes, so based on our currency mix the impact of exchange rate on the revenue growth was 2.3%, so that is an uplift which we got. Then the balance 8.6% is on account of volume growth and the impact of the Colibrium acquisition which happened in end-March 2015.

Jagdish Bhanushali: And how much would be Colibrium in that?

Srinivas Palakodeti: That is about 2.9%, so pure volume growth despite whatever the challenges we have had in Canada is about 5.7%.

Jagdish Bhanushali: Just one more thing, we are winning contracts in UK so wanted to understand major of this everything is usually in onshore in UK?

Partha DeSarkar: Of the two contracts that we have won, one will be majorly onshore while the other has potential of moving offshore but that will not happen in the first year, it will happen in the second year.

Jagdish Bhanushali: Because is there any clause or anything that when you operate in Europe probably you cannot offshore or something?

Partha DeSarkar: No, nothing like that, it depends upon the nature of the business, so some businesses do have that constraint that you cannot operate from offshore but as I said, of the two contracts one has no such constraints but it will start offshoring only probably in the second year, the other one will be onshore.

Jagdish Bhanushali: So it would be a lower EBITDA margin business for us currently?

Partha DeSarkar: See on the onshore basis we do generate about 20% gross margin, but at an EBITDA level it comes to high single-digits.

Jagdish Bhanushali: Then another question comes is that, our other expenses have been moving up since about one year since we have been talking that, we have been investing but the revenues will come in subsequent quarters but when we compare it with other expenses to our revenue that I still constant in terms, so any comment on that?

Partha DeSarkar: Pala can comment more specifically, we have increased our expenditure on sales and marketing and if you look at our conversion in Q1 itself we are telling you that we will close about $26 million in annual business sales which I think is a fairly good number to talk about, it is pure organic growth and that is the return on investment in expenses in sales and marketing but apart from that if there are other expenses in operating expenses that we had talked about, Pala can elaborate on that.

Srinivas Palakodeti: Yes, so if you look at it this way, the expenses which are there other expenses as a percentage of revenue that is about 20% for the quarter ended June 2014 as compared to about 23% for the quarter ended June 2015. And there is about 2.3% is the mix is what you are seeing is after factoring account of mix of currencies, so there is about 2.3% is the impact of the exchange rate. And also as we said for the quarter ended June 2015 revenues have come much lower than expected because we were left with some stranded cost because there is no corresponding revenue. So all this percentages would need to be seen in that perspective.

Jagdish Bhanushali: So do we have any FOREX impact in those other expenses?

Srinivas Palakodeti: No, if at all there is an impact of the restatement receivables that would show up in other income.

Jagdish Bhanushali: And one more thing I wanted to understand, we have a top client which is about 16% or 17% of our revenues, so is that a telecom client or a healthcare one?

Srinivas Palakodeti: The top client is the healthcare client.

Jagdish Bhanushali: And wanted to understand who is the second best one, is it closer to 17% of total revenues or it has fallen below 15% or something like that? Your second top customer probably would be a telecom client, so is it close to 15%, 16% or it has fallen below that as well?

Partha DeSarkar: It will be below that.

Jagdish Bhanushali: And just one question that I have, we have been talking about 20% CAGR over five years that we have been able to achieve in revenue but our EBITDA growth has been much lower and our PAT growth has been much lower than that in terms of CAGR, at what point of time any quarter or any year that we feel that our EBITDA growth and PAT growth will exceed our revenue growth?

Partha DeSarkar: See it is a theoretical question, but let me try and answer this. The easiest way to improve EBITDA is to slowdown growth because there is a cost of growth. If we were to be in a non-liner business then yes that would have been very easy to achieve, that you are in a platform business and therefore once that platform comes in you can keep continuing to sell on that platform. So it is a balance between growth and profitability, if we slowdown growth our profitability will improve.

Jagdish Bhanushali: So the pace of revenue, maybe profitability won't come at that pace at least for some time…

Partha DeSarkar: Yes, I mean that is what we will have to do, we will have to balance that out. In the year that we will grow slower our profitability will improve and the next year if we grow faster again the profitability will show the impact of that growth.

Jagdish Bhanushali: Yes, but at some point of time our investments have to give us much bigger benefit in terms where probably our revenue growth slows down a little bit maybe, but your PAT growth is much higher and EBITDA growth is much higher.

Partha DeSarkar: Yes, that is why I said, as more and more of our business becomes non-linear that is when it will be possible to do that.

Jagdish Bhanushali: So do we talk about that these are the margins that should be currently?

Partha DeSarkar: Look, our attempt has always been to be able to push towards a middle teen margin at an EBITDA level, some years we have come close, this Canada thing was completely unprecedented, obviously nobody foresaw that world oil prices will crash so low and the impact that it will have on oil producing country like Canada, those are macro economic factors that are clearly beyond management control and we are trying to fix it by getting our clients to pay for some of the cost increase in cost of operations. If you leave those factors out I believe the rest of the business has been on predictable profitability, the Canada thing clearly came from nowhere and we could not predict it.

Jagdish Bhanushali: So just to confirm, Canada has hit us about for two quarters right now, so if we would assume that if Canada was normalized what could be our EBITDA margin or what is the EBITDA cost impact on that?

Srinivas Palakodeti: If we did not have Canada, for this quarter the EBITDA margin would be about upwards of 10%.

Moderator: Thank you. Our next question is a follow-up question from the line of Rukun Tarachandani from Kotak PMS. Please go ahead.

Rukun Tarachandani: Sir you mentioned that the CAPEX for this year would be less than the Rs. 160 crores last year, just wanted to understand how much of this is maintenance CAPEX?

Srinivas Palakodeti: I do not have specific number but if your question is for the number for Rs. 162 crores plus which we spent last year then it is primarily growth CAPEX because we have been adding centers in adding capacity in Philippines where we added about 4 centers last year and we have added a center, we have expanded capacity in India. So that is where the bulk of the CAPEX has gone and some may have gone into a little bit in Canada. I am sorry I do not have a specific number but a majority of that or a significant portion of that would be growth CAPEX.

Moderator: Thank you. Ladies and Gentlemen, that was our last question. I now hand the conference over to Mr. Partha DeSarkar for closing remarks. Over to you, sir.

Partha DeSarkar: Thank you once again for joining us on this earnings conference call. We will again talk to you sometime in October when we have our Q2 results. Once again, thanks for taking the time to hear us.

Moderator: Thank you very much Members of Management. Ladies and gentlemen, on behalf of Hinduja Global Solutions Limited, that concludes today's conference call. Thank you all for joining us and you may now disconnect your lines.

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Note: This transcript has been edited to improve readability