"Zensar Technologies Limited Q2FY14 Earnings Conference Call"

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Moderator: Ladies and gentlemen good day and welcome to the Q2FY14 Earnings Conference Call of Zensar Technologies Limited. As a reminder for the duration of this conference, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. If you should need any assistance during this conference call, please signal an operator by pressing '*' followed by '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Dr. Ganesh Natarajan – Vice Chairman & CEO of Zensar Technologies. Thank you and over to you sir.

Dr. Ganesh Natarajan: Thank you very much and good afternoon to all of you and thank you for joining this Earnings Call. I have with me Nitin Parab who is our Chief Executive for Enterprise Services based in San Jose, California; Bala who is our CFO and Ajay Bhandari who is the Head of the Strategy & M&A for Zensar.

What I will do is I will make some brief comments just to explain some facets of the business which are not in the note sent to all of you. So you get a sense of how we are doing and then request Bala to add some other numerical factors which you will be interested in and then ask Nitin to comment on why we are today very confident about the health of our business today and going forward.

First of all I would like to say that we are delighted that for the first time in the history of Zensar, our PBT for the quarter has crossed 100 crores, 106.54 crores to be exact and I think if you look at the two sides of the business, clearly our star performer this quarter has been the Enterprise Services business which is headed by Nitin and particularly in the lead markets which as you know for us are primarily US, UK plus Europe and Africa. In fact the sequential quarter growth of the Enterprise Services business in the US will be 3.6%, Europe 7.5% and Africa 9.2% and overall if you look at the Enterprise Services business, I think there has been a sequential growth of 5.4% overall and 5.8% in the leader territories which is US, Europe and Africa. So very healthy and I think given the order book and the signs which of course Nitin will talk about, they are pretty confident about that business.

In the IM business, Infrastructure Management, though the numbers may look bad, I think we are seeing some very healthy signs. As I mentioned many times before, what we have been out to do ever since we started with an acquisition in the IM business has been to get slowly rid of the non-profitable and the slow moving data center onsite business and replace that with larger deals where we can add new services like moving Infrastructure to the Cloud, also looking at dual shore opportunities for IM and that has started happening. Although the services is more or less flat on a Quarter-on-Quarter basis, there is a quality of the revenues inside that which has definitely gone up and I think what you will see, which is what we have mentioned also, is there will be both growth in the services business and better quality of business going forward. The products has been low this quarter, one of the reasons for the revenue decline and we would expect that there is a goal that products will stabilize between 8 to 10 million per quarter and which will be good because we want to do more of services and less of products.

So overall if you look at the quarter itself, I think IM has been weak, but this will certainly improve by the fourth quarter which will be a good exit quarter for the next year. The Enterprise Business continues to be robust and as I said earlier, it looks good. We have some weak markets, some in Japan had been a weak market, Singapore had been a weak market and even Middle East, but we are seeing good signs of revival in the Middle East in terms of the market opportunity and we will also see that happening as we go forward in the other territory. So overall a good quarter for us and also the signs for the future are very positive.

I will now hand over to Bala to give you some financial numbers and then Nitin.

S Balasubramaniam: Thank you Ganesh. Good afternoon. I have residual data which analysts would be interested in. I want to cover it early so that follow up questions can be avoided. In terms of our forward cover, we have cover approximately 71% of our closing debtors as of end September which is about $37 million at an average rate of 60.94. In terms of our days cover, our DSO, it is 61 days. The loan in the books is $37 million as of end September which at current rate translated comes to about 234 crores. In terms of cash on hand, we have 263 crores represented by 173 crores as cash and 90 crores as in liquid investments. In terms of the capital expenditure for the first half, we have incurred 19 crores as the CAPEX. So these are generally the quick and ready key performance data and in case you have any other further questions, we are here to take it. Over to you Nitin.

Nitin Parab: Thanks Bala. Good afternoon. As you heard Ganesh say that in the ETS business, in the mature markets we have done very well with 5.8% Quarter-on-Quarter growth. I just thought I will give you some more details about what is really driving this growth and how does it look going forward even in the second half of the year.

There are few factors which have really been driving this growth which is a result of the investments and the efforts which have been put over the last 12 months. The first thing is in the large deal space, we spoke about this last quarter also. Instead of doing large number of smaller deals, we have been really focusing on doing fewer, but larger deals and I think those are now starting to come in and that is one of the reasons why we are seeing growth not just only in Q2, but also going forward.

There are few other areas where we are seeing sharp increase in investments from our own customers. One is the Digital Enterprise space which is really the social, mobile, Analytics and Cloud. We are seeing lot of our customers with increased demand in that area and this is again an investment that Zensar had made that we are now seeing converting into business. The second area is as you all know that we have a very strong story in Oracle and for the last year, year and a half, lot of customers who are on Release 11 and wanting to move to what Oracle released about 2 years back which is Release 12. We have been wanting to move to that area and they have been setting on the fence, but it is only in the last 3 months that we have seen there has been a surge of lot of customers now wanting to upgrade or re-implement and move to Release 12 which has fallen exactly in what our sweet spot is. So both with new customers as well as with existing customers, we are seeing increased amount of business in this Release 12 upgrade and last but not the least, whilst there was always a desire for us to start increasing IM business in the existing Zensar customer base it is now that we have seen lot of that getting converted into business for us. So if one has to look at the mix of business, Digital Enterprise, Oracle and IM from Zensar accounts which has traditionally been application accounts is really what has been driving the growth.

Now going forward, as I mentioned that some of these large accounts, large TCVs and ACVs is what we see as sticky business. The Digital Enterprise Business which is again where the company wants to transform to the digital space, It is an ongoing part of the business. So we see this growth trend continue over the next 6 months. Thanks.

Dr. Ganesh Natarajan: This is one last addition. There are two businesses that we are particularly bullish about, one is of course Africa. As many of you may have noticed, we have entered into a venture with local firm which is Kapela and the purpose of that is obviously today we will have much stronger base both to protect our business with existing clients. In the heightened move towards the affirmative action program, we will also be in a position to look for new businesses across Africa as well as with government. The second thing that we have actually launched recently is what we call an insourcing services division because there are a number of our customers in US and Europe who are saying that look in addition to doing a lot of work with you or any other third party providers, can you also help us to see what it takes to really set up a center for ourselves either in their own country or in India. So we have actually appointed a fairly senior person who is looking at that. So these are two new initiatives that we have taken, but broadly as far as Nitin had said, I think the booking has been good, the pipeline looks robust and we are looking forward to good growth in the next 2 quarters as well as in the year to come. So I will stop here and happy to answer any questions at all on anything to do with industry or company or our performance and outlook.

Moderator: Thank you very much sir. We have the first question from the line of Karan Taurani from IFCI Financial Services. Please go ahead.

Karan Taurani: Just wanted to ask you, is Enterprise Business which we mentioned last quarter that it had done really well and above the company average business, this quarter also has done 5.8% sequential growth. The contribution of this business to your revenues would be how much sir?

Ajay Bhandari: Karan this quarter the contribution is around 74%.

Karan Taurani: That is the Application Management Services business, the entire thing, the Enterprise Business?

Ajay Bhandari: By Enterprise Business, you mean all the Application Business, you are right.

Dr. Ganesh Natarajan: You look at non-IM because it is application as in both the traditional Application Management, ERP, Digital Enterprise, all the areas of enterprise.

Karan Taurani: Okay, so you are saying that pie has grown by 5.8% in constant currency?

Dr. Ganesh Natarajan: 5.4% and 5.8% in the leader market which is the US, Europe and Africa.

Karan Taurani: And sir coming to the way your dollar term growth basically this kind of a business which contributes 74% and in spite of growing 5.8%, your dollar term revenue is still dipped by 1% Q-o-Q, it is still gone down by 1%. So what is the reason for that? I know the IMS has also been on the negative growth trajectory because of the product business, but such a strong growth in this 74% pie of a business and the balance 26% no matter how much have it degrown, but still how can you showing a degrowth in the dollar revenue?

Dr. Ganesh Natarajan: You are right, it is Year-on-Year quarter 2 last year versus quarter 2 this year. I think we had an exceptional quarter 2 last year. So I think that is what you are seeing here and also as I mentioned earlier, one of our concerns has been we have consciously completely slowed down the Japan market because it was not profitable. Similarly even some of the smaller account we had in Singapore, we have slowed down. So I think what you are probably seeing, we are quite happy to give you the details, but the main revenue degrowth has been in the emerging markets. Today what we have done is we have chosen three markets and not including Africa. Africa for us is a fairly mature market, but we now chosen Middle East, China, and Australia where we are actually investing in growth and you will see that number really reflecting in the end of this year which is why if you look at, I mean, it is very difficult to comment on third quarter for all the reasons that you know in terms of customer furloughs that we can never really comment on what could be third quarter, but if you look at fourth quarter, I would expect to see in the enterprise services, continuing growth in the leader market, definite revival of growth on Quarter-on-Quarter basis for even the emerging markets and good growth in IM services and product. So I think that is really were it is. You are absolutely right that in spite of good sequential Quarter-on-Quarter growth in enterprise services, it has not been favorable compared to same period last year, but that is an aberration which you will see corrected very definitely in the fourth quarter.

Karan Taurani: Sir my question was that the degrowth in the Y-o-Y 3.3% dollar term revenue is fine which you are saying last year, but even the sequential growth like last quarter your base was low because you were going through concerns and kind of not good growth. Even if the last quarter is based with this quarter, the base has degrown by 1% sequentially Q-on-Q basis, so?

Management: Karan that is 0.5%, it is not 1%.

Karan Taurani: It is 0.9%, 0.5% also, but then 0.5% degrowth Q-on-Q versus Q-on-Q growth in 75% of your business which is growing by 5.8%. So just wanted to touch base on that point, the reason for that basically?

Management: IM business. The infrastructure business is gone down by 12%.

Karan Taurani: Now coming to the IMS business, basically since the time Akibia was integrated in your company in FY12, post that the performance has been extremely volatile and could you give us some trend as to any seasonality effect which you see in this kind of business because there has not been any stability in the revenues from Akibia, one quarter it has been down by 12-8% and one quarter it has been up by 4-5%. So what is that going?

Dr. Ganesh Natarajan: Just to clarify again, all of you are aware the IM business today is a combination of three businesses. One is of course the traditional maintenance businesses and support which is both onsite and remote. The second is what we call multivendor support which is where we will go in with a large technology partner and while they will take over the support of their own technology, they will give the other technology to us, so which is business that has been there for the last one year or so. The third of course is all the new areas which is helping people to move to the Cloud where we have a very strong partner company called NaviSite where we are working with and the fourth is the product mix and as I have explained earlier, product is something you can only predict probably in the last two weeks of the quarter because most of the products, orders are placed in the last 2 weeks and that is really based on people's requirement, what they see, so it could vary literally between 5 million per quarter to what it has been as high as 12 million per quarter. So to answer your question Karan, which you are absolutely right, I think the real variability has been happening because of the product business and as a board of that company also, we have decided that over a period of time, the dependence on products should be as low as 15%. It has been high in the past. So there you will find the variability will come down and as I mentioned earlier what we have also done is the one to two people data center support business we have slowly kind of got rid of, it is still there to a certain extent, but replaced with larger businesses. So for instance if you look at the 5 or 6 multimillion dollar deals we have signed in the last 6 months, 4 of them are in the IM space and many of them are in areas which will be much more sustainable which is why I am saying it is a business in transition. As I have explained last time, we are probably 2 or 3 quarters later than we would have liked to be, but having said that and obviously we have been confident enough to say it that in the fourth quarter, you will see that all these businesses stabilizing and over the next year or so, I think we will continually reduce the dependence on products. So then to take your point, the variability will come down. It is nothing to do with seasonality, it is more of variability of products and the nature of which kind of technology are being supported where the customers, there are some old technologies which we were supporting in the past which have been completely de-supported. So we have to replace that with new ones. Again if any of you are interested, we can send you a very detailed analysis of this business, the way it was, the way it is today and the way we expect to see it over the next 5 to 6 quarters.

Karan Taurani: Okay sir and just one last question. The client addition you said, you won some large deals in this year, you won some 5 deals basically over $5 million, but if you see in terms of the client numbers of the client size, you have $5 million plus, that number has come down from 7 to 6 YoY. So it is not getting reflected in the client size engagement because even the $10 million clients which were two last year had now come down to one, I am talking about the YoY comparison. So the reason for that sir?

Dr. Ganesh Natarajan: The reason, lot of the deals we have signed in the last 6 to 9 months, obviously will not reflect as $5 million client or even a $1 million client immediately, but I think you will start seeing the impact in FY14 and thereafter. So that is where the addition will happen. Some of the changes in $1 million client is because of as Nitin explained, we do a fair amount of large Oracle projects and when the Oracle project which could be as high as 3 million in a year come down, then it goes into support which is probably about half a million a year. So that are the changes you are seeing, but you are right. I think the consistent growth in larger clients, I would expect to see definitely in FY15 because a lot of these are ramping up and IM deals typically takes about 4-5 months of ramp up time and if the full year impact of that has growing into multimillion dollar, you will probably see FY15 onwards.

Karan Taurani: Just one question, small question just to end this. Your growth in the first two quarters order terms has not been up to the mark, for whatever reasons IM business is not doing well or whatever the reasons, but you see yourself achieving at least the lower end of NASSCOM guidance for FY14 in dollar terms?

Dr. Ganesh Natarajan: FY14, I really do not want to make any prediction because as you know we have been transitioning. What we are all excited about which I mentioned earlier is the exit quarter because if you look at all the businesses, things look very good for the January to March quarter and the reason we are focused on making that happen and depending on how good that quarter is, then FY14 will accordingly shape up, but I think that will determine the trend for FY15 and that is really our opportunity and the focus of the entire management team.

Moderator: Thank you. We have the next question from the line of Sudhakar Prabhu from Span Capital. Please go ahead.

Sudhakar Prabhu: My question is again regarding the IM business. This quarter we saw a 12% fall, so when do you think the revenue should stabilize and we should see growth forward?

Dr. Ganesh Natarajan: We have actually said that from 29 million in IM this quarter, we will be seeing minimum of 33 million in Q4. So clearly Q4 will be the beginning of growth. There will still be as I mentioned earlier to Karan's question, some variability because of products even as we reduce our dependence on products as a percentage of total IM revenue. We will however definitely see the services business given the order book we have today start growing in this quarter and you will definitely see the results in the fourth quarter because that is pretty much on the cards.

Sudhakar Prabhu: So from FY15 onwards, 30-33 million should be a stable run rate from this business?

Dr. Ganesh Natarajan: We would definitely look at 33 million per quarter as a stable run rate and growing from there absolutely.

Sudhakar Prabhu: And secondly Ganesh how do you see the margin improving from the current level?

Dr. Ganesh Natarajan: Margins are already pretty good. I am talking about the overall business. If you look at the IM business, at a 17 million services revenue, the margins are really dependent on how much of products we can book, the product is low margin, but still as to the margin which is why you see a much lower margin this quarter, but as the revenue of the services business goes up to the 19-20 million range, then obviously the margins will again move up to the 8.5-9% in this business and our goal is to bring this to double digits. Now whether the double digit margin for the IM business in PBT terms will happen in FY15 or not is difficult to say, but that is clearly the trend line that we have seen happening as the services business goes up and it becomes more profitable.

Ajay Bhandari: Just to add to what Ganesh said, the services business which is the more profitable business that has seen a continuous growth over the last 5 quarters and the product business which is low margin business is right now even though it is 10 million, we are anticipating that will be between 7 and 10. So I think you will find that margins at least on the IBU side are on the upward curve. If you look at the applications business, this quarter despite the salary hike that we give normally in the July quarter; it has almost seen no decrease in margins. So there is pretty good operations management and excellence on the application side anyway.

Sudhakar Prabhu: And my third question is regarding your healthcare and utility vertical, this vertical has been really a drag, so any thoughts on that?

Dr. Ganesh Natarajan: What we have really done is utility is now part of Manufacturing. So it actually gets reflected in the Manufacturing vertical, but we have showed it here to show this. So I think both in terms of existing utilities projects in the US, in Europe as well as MSEDCL which is Maharashtra State Electricity Distribution, I think we are seeing good traction in utilities. So I would not worry about that. Healthcare, yes has been slow. As all of you know, the Obama Healthcare plan has been very slow to take off. What we have done is instead of having an independent team marketing in the healthcare business, we have integrated that with us Insurance business. So the Insurance sales teams in the US are now looking at the healthcare business. So it is slow, you are absolutely right. You have two good clients who are slowly ramping up in healthcare which will take us there, but we are not seeing this as a big growth vertical, at least not for the next 3-4 quarters.

Sudhakar Prabhu: And my third question is again regarding your South African venture, what is your plan over next 2-3 years and how much do you plan to invest and I believe you already have a development center there. Would that center also be part of that venture?

Dr. Ganesh Natarajan: Very much true. In fact as again some of you would know, we have what is called a Learnership center in Johannesburg and that center has already trained 140 young black South Africans, partly trained for 3 months in Johannesburg and normally they come for one month to India. The good news is that out of those 140, 86 of them are already members of our team in South Africa which kind of shows both the quality of talent and the kind of training we have been in a way to provide which is one of the reasons why the partner we have in South Africa who are actually seen as one of the best black empowered partners in South Africa which advice got from most of the investment banks we spoke to. They are very keen because they see us a genuinely investor in that market. We have also started doing good work in Kenya. In fact one of the largest Retailers in Kenya is now a client of ours and that is likely to scale further. To answer your question, yes. The investment territories, we are looking at over the next 2-3 years. One is Middle East, the second is specific areas of India, we still see good opportunities in India in specific government areas and of course the area of Digital Enterprise and the third will be Africa. South Africa, I think we have already fairly significant scale, but like Kenya to look at may be 2 or 3 other African markets and invest in that, we will continue to that, but yes absolutely the Learnership center is very much part of this new venture and will be one of the drivers of growth both in the private sector and hopefully the government sector in Africa.

Sudhakar Prabhu: And my last question is to Bala. Bala, if you look at the goodwill on consolidation, the goodwill amount seems to have gone up from 290 plus to 330 odd crores.

Balasubramaniam: It is purely a currency translation impact. The goodwill remains the same. It is a currency translation.

Sudhakar Prabhu: Any plans on amortizing the same?

Balasubramaniam: Not at the moment.

Moderator: Thank you. We have the next question from the line of Dipen Shah from Kotak Securities. Please go ahead.

Dipen Shah: Ganesh just a couple of questions. First of all on the Application Management Services, we have reported a good growth. Can you just give us more insights into the macro as to what is actually leading to this growth? I understand it is the SMAC business, the digital initiatives which are large part, but just some more color on how our clients see the discretionary spends and some other things which you might want to tell?

Nitin Parab: So Dipen, I mentioned four points which I am seeing as the key reasons for this growth. The first is as against a lot of project business from the last one year, we have been signing annuity business and therefore it shows as consistent part of the business. So project to annuity ratio that has changed over the last 12 months. Second is even in terms of the annuity business as against going up for a large number of customers who were giving us smaller amount of annuity business, we have signed fewer number of customers with whom we have got larger business. I think that is also there for contributing to the growth on a Quarter-on-Quarter basis and the two other areas where we have seen a lot of our existing customers begin initiatives and therefore starting to spend, one is in the Release 12 Oracle area because a large customer base of ours use Oracle as their ERP and for several other technologies within the footprint. So we are seeing a growth in that business and the second is the Digital Enterprise because a lot of our customers who are in across all the three verticals – Insurance, Manufacturing as well as Retail are seeing increasing need of adopting the Digital Enterprise which is all around Mobility, Social, Analytics and Cloud and that is a play which is resulting in additional business from them. So these are the four reasons why I will see Quarter-on-Quarter growth in revenues.

Dipen Shah: In terms of the order booking, how would you put the order booking currently as compared to what it was in the last quarter and also in the same quarter of the last year?

Dr. Ganesh Natarajan: Dipen, the order booking has been steady. So I do not see any complaints and we are well-covered to do what I mentioned, we can do it in fourth quarter. So that is not a problem. Going forward our current pipeline is over 200 million if you look at both the IM and the Application Services Business. So again given what we expect to close in terms of what this quarter which is all about what we call the 70% probability of closure, it looks pretty good and as Nitin was saying with the credibility we today have with being able to not only talk about supporting legacy, also managing their infrastructure in some cases managing like in some of our retail clients managing their merchandise through business process management and then leading them to new technologies and the whole area of Digital Enterprise. I think we are able to not only hold all our existing accounts, but gets new orders from existing accounts as well as new orders from new accounts. So I think it is a pretty robust environment. Unless something goes wrong with the whole overseas economies which we do not see happening, we should be pretty well placed to get. In fact Cisco itself, we were recently rated the highest award in quality, we got the award couple of weeks back in terms of the quality of work we provide. So I think we have a very mature delivery operation profitable and being able to deliver this. So we are pretty confident Dipen to answer your question.

Dipen Shah: That was the next question. How is the Cisco account growing and what are the prospects of that?

Dr. Ganesh Natarajan: I think it is fine. In fact we continued to have an excellent relationship. Our reputation for quality continues to be excellent and obviously it is a large account. So we do not expect that to grow at any astronomical pace, but I think it will continue to grow. The trends are all good and our own positioning within that account is excellent.

Dipen Shah: Once again coming to the IMS Business in order to stretch it further, but first of all on the products front, we have seen that while the revenues have gone down by about 12 crores on a sequential basis. We are seeing the profits from that segment go down by 15 crores. So just wanted to understand as to what exactly led to this?

Dr. Ganesh Natarajan: I think the problem has been that as I mentioned to the earlier question Dipen that we do have a cost structure which has been set up which should support a larger operation. Even in Zensar itself when we first started building the business in 2001, we have set up a cost structure for operation which was 20% higher than that. So it took some time to reach that level and I think the answer to your question is really what I would say that once we reach that level of 30-33 million as IM Business and with this current cost structure for managing the business both in terms of marketing onsite execution as well as consulting and offshore, I think then you will see the real movement towards double digit profitability I talked about. You are absolutely right in this quarter if you look at the numbers both the product and the services business have been slow, but that is because we have built a structure where revised structure of product of services, we need a larger revenue and the revenue is not coming has affected the profits which will definitely change in the fourth quarter of this year.

Dipen Shah: That I would understand, but just trying to stretch it a bit further. Even in the Services business in the Infra Management part, we are seeing margins go down from 10% to 5% despite the rupee having depreciated by 11%. So just trying to understand like what exactly has led to that? Profits have actually halved from 12.5 crores to about 6.8 crores on the services business of IMS. So that was slightly surprising as to how come the profits actually half from 12 crores to 6 crores?

Dr. Ganesh Natarajan: Dipen, it is a little bit of accounting there because end of the day our OPEX in a ways is constant. Product revenue goes down, the margins on a product goes down which means the allocation on OPEX is almost completely goes on the services business, but from a gross margin side, if you see the gross margins are still pretty good, but it is just the way we allocate and we have been allocating like that for the last 3 years. So there is no point in changing the method of allocation right now. It is more an accounting allocation thing than any serious quality of business. The quality of business at least on the Services side continues to be good and the margins continue to be good.

S Balasubramaniam: Yes obviously. If the revenue coming down, the allocation base will completely get skewed and that is what Ganesh had explained. The fundamental issue dependence once the revenue goes down, then obviously the allocations and profitability with which we are quite confident of saying the thing all leveling up in Q4.

Dipen Shah: Basically on a steady state like how do we see the margins in the Infra Management Services business like we leave aside products because that is volatile and may be that will settle at somewhere between 8-10 million as Ganesh was saying, but on the Infra Management Services business, what should we look at the steady state margins in the next year?

Dr. Ganesh Natarajan: If you look at the steady state being the right mix of as I said Cloud Services which is most profitable, Multivendor Support which is profitable and then of course the Maintenance Services. So I think if you look at all these three together, I would not say steady state yet, but I would think the real steady state would probably be FY16, but FY15 for the services part of the business we should definitely be seeing 12-12.5% PBT and then you couple that with may be a 6% or 5% product, we will still have touching the 10% PBT mark, but that is really what we are looking at. I think the potential is to grow even further as you get more of the Cloud based solutions because that is obviously much better to serve. So definitely that is the trajectory we see going forward.

Moderator: Thank you. We will take the next question from the line of Kavitha Vempalli from Nirmal Bang Securities. Please go ahead.

Kavitha Vempalli: Sir to begin with, are you anticipating any kind of furloughs in the coming quarter, any kind of shutdowns?

Dr. Ganesh Natarajan: I think we always anticipate furloughs in the last quarter. Sometimes the furloughs are less severe than we expect, but the answer is yes because most of the Fortune 500, Fortune 1000 companies the reason why you cannot anticipate is they look at their own numbers end of November and then decide whether they want to do a furlough, whether they want to do a five day which is really a one week or two week shutdown end of December. So it is almost impossible for us to predict, but we do anticipate like most of the companies there will be some furloughs which is why the third quarter tends to be relatively weak quarter and which is why I mentioned. We are training all our guns on doing a very good fourth quarter which is the exit quarter for this year. Third quarter is difficult to predict because of these quarters.

Kavitha Vempalli: Sir secondly on the margin front, can you give us a breakup of 370 bps expansion in the current quarter, what is the currency benefit and I think you all gave an offshore hike. So could you give us a detailed explanation on that?

S Balasubramaniam: We will send it to you because the various constituents of margin in terms of product mix, revenue mix, territories it is too complex kind to explain on a call. We will send it to you.

Kavitha Vempalli: Sir lastly your outlook on the tax rate, what is your like expectation for FY14 and FY15 on tax rate?

S Balasubramaniam: As I had explained in last quarter also, we are exploring the movement into the SEZ in a very consistent basis. So we have been able to kind of bring the tax rate marginally this quarter, obviously it will kind of keep on improving every quarter. I think this quarter was about 33.7 as against 34 in Q1. What we are doing also is that we are improving the offshore percentage that has also come down by 1% and so a combination of SEZ movements, we also expanding our SEZ in Pune. We have expanded our SEZ in Hyderabad and in the coming quarters all of them gradually will kind of fill up in production and we therefore see a transition to anything between 32-30% as we move along, but as I told you this has to be calibrated quarter-to-quarter rather than just flat for a particular accounting period because as it gets occupied, the taxation rate keeps coming down.

Kavitha Vempalli: And sir finally your hiring outlook and the component of trainees in that?

Dr. Ganesh Natarajan: Hiring outlook just to give you a sense, our goal for this year has been to hire close to 350 trainees. Out of which, about 200 will be engineer trainees and about 150 will be non-engineer trainees. In fact interestingly we are having more difficulty finding the non-engineer trainees because clearly the whole industry is looking at 1.6 lakh starting salary resource rather than 2.75 or 3 lakhs. So that is something we are doing directly as well as with partners and apart from that I think we are already seeing the hiring starting. So I would expect that cumulative for the year is probably higher between 525 and 600 people addition which is really the goal for the year and given the trends and the facts that orders have already come in, hiring is going on both of laterals and in freshers on a regular basis.

Moderator: Thank you. We have the next question from the line of Dhananjay Mishra from Sushil Finance. Please go ahead.

Dhananjay Mishra: Just wanted to ask about Mr. Natarajan was talking with us about million dollar plan. So going forward, do you see more growth coming from this IMS or Enterprise Application?

Dr. Ganesh Natarajan: It is a very good question and what we are now looking at is if you look at the 3 year, 4 year projection for Zensar, we would definitely like to see the growing double digit growth which is definitely going to happen on both sides of the business which is infrastructure management and the Application Services Business. As my colleague, Nitin, mentioned, we are very excited about the opportunities for digitalization as you may have read a lot of American companies are now actually appointing a chief digital officer which really looks at this whole impact of Cloud, Social media, Mobility, and Big Data very seriously. That is a play that we are clearly going to be very aggressive, we have already started making the movement in that area and in fact over the next 6 months, we will probably have multiple workshops going on in the US and Europe with the CEOs and their teams of our clients and they are all very interested in seeing how we can picked up. I think that is one growth driver. The third growth driver we are looking at this is the whole area of Product Engineering because we do very little today in Engineering Services and offshore product development. We have a couple of opportunities. In fact we are going to build that business both organically as well as probably look for an acquisition in FY15 in that area. So I think that is really what we are looking at. So I would expect that if we find the right companies, if you look at the next year, we would look at adding about $75 to 100 million through acquisition and the rest of that would be organic.

Dhananjay Mishra: So this FY17 target is still intact, right?

Dr. Ganesh Natarajan: FY17 at this point of time, it is difficult to say because it depends on the market. So we really have not even put a number in place, but I think the goal really is to ensure that the high-teen double digit growth is sustained over the next 3-4 years as I mentioned to a combination of good organic growth and some acquisition in the right strategic space as and when the opportunity presents itself.

Dhananjay Mishra: In this quarter, we have very good growth of 5.8% in the Enterprise Application space. So in near term, how do you see growth in next 3, 4 quarters in sequential years?

Dr. Ganesh Natarajan: It is difficult to predict, but if you look at FY15, definitely given the pipeline and the trends we are seeing unless something goes wrong in the US and Europe market, definitely sustaining double digit growth in the Enterprise Services Business is definitely possible and again if you look at FY15, by the time we have an exit quarter which we are already looking at 33 million plus for the IM business, there again sustaining a good growth will happen. So I think both the businesses will grow. Exact numbers I find it difficult to predict because that seasonality based on projects we sign and got complete, but if you look at trending over the next 4-6 quarters, definitely it looks positive for all markets as well as all businesses.

Dhananjay Mishra: And last one bookkeeping question to Bala about other income. In this quarter, we have about this 14 crores of exchange gain and last quarter also we had 28 crores, right. So we are hedging close to 60-70% of cash flow and we also have debt in US dollars, so how we are making such a huge gains on Quarter-on-Quarter basis?

S. Balasubramaniam: There are two elements to that exchange gain. One is the currency translation. Since we have a very large onsite operation and therefore the quantum of debtors which gets converted. So you will have a currency gain every quarter depending on how the currency moves or a currency loss on account of the translations. So to that extent, it is an accounting gain. The second answer to the question Dhananjay is that because we hedge on a consistent basis regardless of which way the currency moves, typically if you do that on a consistent basis, you tend to gain in the realized gains. So it is a bit complex to explain in the call, but I would only say so much that as long as you follow a hedging policy which is consistent over larger period of timeframe, you tend to gain and our hedging is just not only spread over short term quarter of just 30 days or 60 days, we typically hedge portion of it in 30 days, portion of it in 60 days, portion of it in 90 days, portion of it in 120 days so that the movement it gets over a period of time smoothened out and this has worked for us overall.

Dhananjay Mishra: So this 28 crores is M-to-M provision we have made so far in terms of all asset and liability we have right?

S. Balasubramaniam: It is a combination of realized gain and currency translation.

Moderator: Thank you. We will take the next question from the line of Sonal Kohli from ENR Advisors. Please go ahead.

Sonal Kohli: Firstly sir on your other operating income, we have seen a 8 crores growth in Q-on-Q on the operating income, is this on because of some provision being written-back and if so, is it fair to assume that this will show a substantial fall going forward and it is not a sustainable number?

Ajay Bhandari: These are primarily some provisions write-back in this quarter which we had in books for certain employee related project bonus, which is based primarily on achievement of annual numbers. So this is normally adjusted in the month of July.

Sonal Kohli: So this is pertaining to last year, is that what you are saying sir?

Dr. Ganesh Natarajan: Yes, that also has to mitigate some of the immediate impact of the wage increases we have done this year and of course as we go along which we always do, even the wage increase impact is absorbed by better productivity and over the next few quarters, I think broadly you will find that this is definitely helped us to mitigate that impact. I think the profit itself is fairly sustainable going forward especially because the expected improvement in the overall business as well.

Sonal Kohli: So you would not expect the 130-120 basis points improvement on margins because of sector would lead to relatively at least this much reduction in margins going forward because of this being a one-off?

Dr. Ganesh Natarajan: I agree. See the problem is margins itself is a very fairly complex combination of event. So there is obviously some revenue benefit. There is the benefit of the growth of the Enterprise Business which is also a negative of this kind of decline in the IM business. So I think as the IM business grows, the Enterprise Business sustains. So some of these which are one-off including currency, I think that will have to be overcome by that. So very difficult for me to make a margin prediction going forward, but as I said the trend is positive in terms of the operating margins of the company.

Sonal Kohli: And sir is it fair to assume that you would have a sensitive for about 15 basis points to every change in currency to your margins?

Management: That again is very difficult to kind of predict.

Sonal Kohli: Assuming sector parameters no change in any of the other parameters.

S. Balasubramaniam: Very difficult because we have a basket of currencies and Ganesh said our three major markets are three different currencies. GBP has its own volatility and ZAR has the volatility which is sometimes worse than the Indian currency. It is very difficult to say.

Sonal Kohli: Sir let me rephrase my question, maybe I did not explain my question properly. What I meant was that let us say for all the currencies if you have would by a similar fashion by 1%, they appreciate by 1% all your international exposures, then in that scenario would typically your sensitive to currency is about 15 basis points or would it be like 10 or 20 basis points?

S Balasubramaniam Sonal honestly I have not done that kind of sensitivity, but what I can do is I can do it and we can have a chat later on offline.

Sonal Kohli: Sure sir and sir December is it fair to assume December is typically a weak quarter for IT industry and like in last year it will hold true this year as well?

Dr. Ganesh Natarajan: No absolutely. This is a weak quarter for IT industry. There is always weakness because of Thanksgiving and other holidays and now with this wonderful phenomenon called furloughs which many of the customers do, it makes a bit weaker. So certainly I think that is an industry trend and obviously I have seen it in the commentaries of everybody including Chandra of TCS. That is why most of us find it difficult to predict exactly where third quarter will be. The more important trending as I had said before in this call is what we can achieve in the fourth quarter and at this point that looks very positive.

Moderator: Thank you. Sir there are no further questions from the participants. So would you like to add any closing remarks before we conclude?

Dr. Ganesh Natarajan: Yes, sure I will do that and thank you very much for asking the questions and as I mentioned earlier, we are very confident about the state of the business today. As I said, we have had some delays in replacing the old IM business with the new IM business. So I think that transition has taken more time and we would have liked, but having said that I think it is clearly over the hump. We had detailed discussions with both our chief executives over here for the last 2 days, Vivek Gupta who runs IM and of course Nitin who is on the call as well and I think both of them are very confident in terms of going forward. So overall I think thanks to last year's organization excellence initiative we did. I think we just kept the cost structures fairly low. We are obviously getting the benefits of currency that is clearly there for everybody, but at the same time given the overall good trend in order book pipeline as well as the execution and quality capabilities of our teams, I think there is a full confidence that this is a very healthy business and going forward we will continue to do well, but thank you very much for joining this call.

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