

*Earnings call Transcript- FY15 (Q2)*

**Transcript**

**Earnings Conference Call of CMC Limited – Q2 (FY 15)**

**Participants: Mr. R. Ramanan, MD & CEO  
Mr. J. K. Gupta, CFO**

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**Moderator:** Ladies and gentlemen good day and welcome to the CMC Limited Q2 FY'15 results Conference Call hosted by Tata Securities Limited. As a remainder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference, please signal an operator by pressing "\*" and then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ashish Aggarwal from Tata Securities Limited. Thank you and over to you!

**Ashish Aggarwal:** Thanks Mosin. On behalf of Tata Securities, I welcome you all to CMC Limited Q2 FY'15 results call. From the management we have Mr. R. Ramanan, M.D. and CEO of the Company, and Mr. Gupta, CFO of Company. Before handing over the call to the management, I would like to thank them for giving us an opportunity to host this call. Now, over to you Sir!

**J.K. Gupta:** Thank you Ashish and a very good evening to all the participants in this call to discuss CMC Q2 Financial Results which were approved by the board earlier today. Before I give you a commentary on the financial performance of the quarter, I just want to share one important piece of the information that happened today. The board of directors of both CMC and TCS has approved amalgamation of CMC into TCS, which is subject to all the regulatory approvals so this was a decision of the board today which has been communicated to the stock exchanges also.

The swap ratio under the scheme has been fixed at for every 100 shares of CMC the shareholders of CMC will get 79 shares of TCS as on the record date which will depend on how fast we are able to complete the process. Since TCS is registered in Mumbai and CMC registered in Hyderabad CMC will follow its own process of obtaining the approval of Hyderabad High Court and the shareholders as per the AGM to be convened as per the court order. So that was an important piece of information that I want to be share before we start talking about the financial numbers.

In this quarter CMC earned consolidated operating revenue of Rs.616.69 Crores which is an increase of 4% QoQ and 10% on YoY basis. The company earned consolidated EBITDA of Rs.104 Crores in this quarter which is an increase of 14% QoQ and 18% on a YoY basis giving us an EBITDA margin expansion of 149 basis points.

In this quarter we have absorbed Rs.5.46 Crores as an impact of annual salary revision which normally is granted from July 1, every year. On basis point terms it had an impact of 89 basis points in EBITDA. This quarter we had a benefit of improvement in exchange rate. Average exchange rate improved from Rs.59.85 to Rs.60.62 as compared to quarter one which had a positive impact on revenue of Rs.503 Crores and positive impact on EBITDA was Rs.1.60 Crores that is 26 basis points.

This quarter we had a broad-based growth in revenue were both domestic market and international market grew almost in equal proportion our domestic growth is 9% on a YoY basis and international growth is 10% on YoY basis. Services revenue in this quarter was 570.38 Crores which gives 9% YoY and 7% on a QoQ basis.

As a result service revenue share in the overall revenue is 92.5% in this quarter compared to 90.3% in the previous quarter and 93.2% in the same quarter last year. International revenue grew to 428.4 Crores in Q2 which is a 7% growth on a QoQ basis the share of international revenue in this quarter is 69.5% compared to 67.8% in the previous quarter.

America which continues to be the larger geography for us which contributed about 61% of our total revenue in this quarter it grew 6% quarter-on-quarter and 14% YoY in dollar terms. Company earned consolidated profit after tax of 76 Crores which is up 30% quarter-on-quarter and 13% on a YoY basis.

We continue to have robust client addition in this quarter also and in this quarter we added 17 new clients taking the total client addition during the year to 29 in the first half year of this 17 clients we added 4 clients in America out of which two are in the embedded system area one in infra and one is in software services area.

One plant we added in European software solutions. We added two clients in MEA in insurance and e-governance areas, 11 clients were added in India in energy, ports, transportation, infrastructure, banking and education areas.

Other income during the quarter is Rs.2.52 Crores which includes 1.70 Crores income from mutual fund investments. We had net addition of 193 people during this quarter taking our total manpower account to 11585 at the end of quarter two. We ended the quarter with cash and cash equivalent of Rs.248 Crores and in this quarter we spent Rs.16 Crores in capital expenditure out of 248 Crores 178 Crores invested in debt based mutual funds.

So this is the summary of financial performance during the quarter now I will ask Mr. Ramanan to give his perspective about the business.

**R. Ramanan:**

Thank you JK and thank you everybody for attending this call and as JK mentioned it is a momentous day for CMC today as we have announced the plans to amalgamate CMC into TCS. I am very proud of the fact that CMC is now becoming an integral member of the TCS family from a 51% ownership that was earlier held.

The performance of CMC in this quarter has been very good and JK has shared the numbers. We have had good growth in Q2 both in the revenue front as well as in the EBITDA front as he has mentioned we have grown about 30% quarter-on-quarter in the profit after tax and we have maintained a healthy quality of business mix.

We are 69.5% international revenue and it was 67.8% in the previous quarter so we have increase our share of the international revenue. We have also been able to add 17 clients as we mentioned and this has been a good all-round growth for the company both in the domestic market as well as in the international market.

We continue to add key clients in the energy, ports, transportation, infrastructure and banking and education areas and our core solutions in insurance have found new clients in the Middle East and African regions and we have also been able to add a client in software solutions in Europe during this quarter.

We have added four clients in America's all of which are in the key areas of embedded real time systems, software solutions and in infrastructure management. The quarter has been with these 17 new clients that we have added it has enabled us to get some new opportunities for further addition of revenues during the coming quarters.

On the operational front, we have continued our focus on ensuring that we will move up in terms of our EBITDA revenues and our EBITDA margins and we have been able to expand our EBITDA margin by 149 basis points this is after announcing the annual salary hikes which gets, which are effective from July 1<sup>st</sup> of this year.

So all and all it has been a very good year and in the half yearly basis he has already shared the numbers with you we have grown 16% YoY from the half year revenue point of view and about 18% YoY on the EBITDA point of view.

So with this I will be happy to answer any questions that you have on CMC.

**Moderator:** Thank you very much Sir. We will now begin the question and answer session. We have the first question from the line of Urmil Shah from May Bank. Please go ahead.

**Urmil Shah:** Congrats on a very strong quarter and thanks for taking my question. Sir just wanted to understand the quality of deals which you have announced while it is broad based as regards geographies and even the services, wanted to understand the tenures for the same and kind of domain expertise involved?

**R. Ramanan:** Most of our contracts are long-term contracts at least it is not multiple years both in the domestic market as well as in the international market. So from a tenure point of view typically CMC goes after long-term contracts and where we develop our solutions and implement our solutions there is an annual maintenance contract that will kick in after the implementation of the solution. So in general when we add when we talk about 17 new clients being added they are mostly in the solutions and services base. The only time where we have transition client is where we have a third party product sale because that is a quarterly sale and the sale ends with the supply of the equipment, but again as JK has shared 92.5% of our revenues during this quarter have come from service revenues and that is actually gone up as compared to the last quarter, last quarter it was 90.3% so all these clients are long-term clients or most of the clients that we have added a long-term clients during this quarter and we do expect that they will yield us revenues over multiple years.

**Urmil Shah:** Sir, an outlook on the India business you see the growth coming back especially on the government side?

**R. Ramanan:** Yes, we have actually added 11 clients in India this time and that is out of the 17 clients we have had slightly more number of clients added in India even though our revenue share from the international market has grown higher than the domestic but most of the domestic clients that we add the revenues kicks in during the later quarters because once you win a new client you have typically a cycle of about 12 months for implementation of any software solution. Now what we have done in India is we have won projects in ports, in energy, in transportation, and in the infrastructure and banking and education areas. The energy, ports, transportation are all solution driven

the one that we one in banking and infrastructure are service related projects but these are again long-term service related projects.

**Urmil Shah:** Thank you so much and all the best.

**Moderator:** Thank you. We have the next question is from the line of Omkar Hadkar from Edelweiss. Please go ahead.

**Sandeep:** Sandeep here from Edelweiss. Thanks Sir and congratulation for a decent set of numbers. Couple of questions Sir, what are the advantages I know the advantage of obviously the large amalgamating with TCS will be obviously there and being a small company we have always reap the benefit, what special additional benefit we will get through this merger point one, point two how will it help TCS and CMC both?

**R. Ramanan:** I think as we have been sharing over several quarters we have been looking at some ambitious growth for CMC and what we there has been quite some deliberation on this and in order to unlock the full value of CMC and CMC having grown to a point where it makes a considerable amount of sense to now tap the global presence of TCS for the growth of CMC in the crucial areas that we are in and the solutions area that we are in, so this merger has now is able to unlock that value that we would otherwise not have been able to unlock where we on our own. So this is the reason that we have, the boards have been deliberating and we have agreed up on this merger. What did enables is a tremendous growth for each one of the service lines that CMC has in synergies with TCS. For example our embedded in real time systems, SBU, our SI solution for various verticals, our IT enabled services and digitization services for the various clients that we are servicing, the solutions that we have developed in ports and insurance and transportation and so on so all of these will find full expression within TCS and therefore there would be tremendous value to TCS also. It will enable them to penetrate newer clients. The second thing is the clients that we already have existing clients that CMC has we will be able TCS will be able to add further value through their full value service to these clients and CMC on the other hand will be able to harness TCS existing client based for pushing CMC solutions and services into TCS clients so it is going to be beneficial to the employees of CMC the solution sets and the service capability that CMC has and it will be able to enable it to find a place in the larger context and grow rapidly.

**Sandeep:** Thank you Sir. That is all from my side.

**Moderator:** Thank you. We have the next question from the line of Sanjiv Hota from Sharekhan. Please go ahead.

**Sanjiv Hota:** Thanks for the opportunity and congratulations to the management for noting amalgamated with TCS. My question pertains to the broader picture. There is some commentary from the management and the media there with regarding the digital India it is going to take place in the next two, three years. Now CMC and TCS how this opportunity is going to payout in next two, three years and what kind of growth opportunity can we see from the Digital India?

**R. Ramanan:** Yes, Digital India provides a great opportunity for the synergies of TCS and CMC to express themselves in across the country. Digital India is of course the roadmap and the plan for that is still being rolled out by the government and by various units responsible for it, but very clearly Digital India means three, or four things. Number one you will need solutions which are e-governance related, which are national or at a state level and which will need to be supported at a national level or at a state level. CMC brings one is the solution base that it already has and coupled with the TCS solutions that are already present between TCS and CMC we have I would say a lion's share of the

government solution service market already and this will find even better expression now with both the companies integrated and with them addressing the opportunities whether it be related to infrastructure services or digitization services or the solutioning and the software development services.

**Sanjiv Hota:** What kind of revenue size, your market size does Digital India's concept is going to offer in next two, three years?

**R. Ramanan:** From whatever the governments have been saying that is going to be some huge emphasis on that until the clear roadmap and the plan is rolled out, I would assume that these will be sizable projects some of them would be it could go anywhere between 50 and 100 Crores to more than that so it depends upon the conception of the project whether it is being conceived as smaller unit or whether it is one large project integrating many functional units of the Digital India. So those things will become clear as and when the RFP start getting rolled out but I would presume that they are significant opportunities for the company.

**Sanjiv Hota:** What would be our approach regarding the margin in this are we going to bid for each and every project and are we going to be choosy regarding the margins?

**R. Ramanan:** Obviously we will do projects which play to our strengths and which are meaningful from the point of view of both size as well as revenue and profitability so it will of course, we will not be bidding for each and every projects if we would bid for project that have value additions from TCS, CMC and which are having long-term potential as well as long-term sustainable profitability.

**Sanjiv Hota:** That is all from my side. Thank you very much.

**Moderator:** Thank you. We have the next question from the line of Priya Rohira from Axis Capital. Please go ahead.

**Priya Rohira:** I have Mr. Puranik and myself on the call, I will ask first Mr. Puranik to check.

**Puranik:** Hi Ramanan and JK. It has always been a great pleasure interacting with you. I must first thank you and congratulate you both for taking CMC what it was when we look at from the government and you people have put in tremendous effort in transforming the legacy company into what it is today. My congratulations and best wishes you. I have a couple of questions not many of them. One is about will CMC be focused on India business only and would the international business be managed separately as part of the TCS business groups and how will this happen?

**R. Ramanan:** Puranik, this is a scheme of amalgamation that has been approved by the board today both the respective boards so till the time all the regulatory approvals are achieved these companies will continue to operate like independent companies as these are operating. Once the amalgamation is approved CMC will no more be there. It will get absorbed in TCS so at that time respective businesses will be handled in the manner TCS handle the businesses. So there is not going to be a separate approach for domestic or international but till the time we are operating our approach to business is going to remain the same as which has been here today.

**Puranik:** So it will get integrated into TCS business groups?

**R. Ramanan:** Yes, basically this company been actually as we to say this company without getting wound up this company get dissolved this is the technical term, this company dissolves without winding or proceedings.

- Puranik:** The business groups will get merged with various business groups of TCS that is what you are saying?
- R. Ramanan:** Yes basically CMC becomes a part of TCS there is no CMC separate so you cannot identify CMC after merger.
- Puranik:** Then my only question was will it be focused India business which will be part of this still improve?
- R. Ramanan:** Those things will have to be now discuss over the time.
- Puranik:** Too early time to discuss about that.
- J. K. Gupta:** Thanks Puranik. You always been a person who has encouraged use all the way and I want to personally thank you for that.
- Puranik:** I think you people are wonderful. Both of you have done enormous jobs. I wish you all the very best to both of you. Thank you.
- Moderator:** Thank you. We have the next question from the line of Nirav Dalal from SBI Cap Securities. Please go ahead.
- Nirav Dalal:** Thank you for the opportunity. I had few questions, one is, is there any update in terms of in what has been done for CRIS towards the Indian railways any update on that?
- R. Ramanan:** Yes we are currently executing their Passenger management system. So the last deal that came out of CRIS was bagged by us and after that these people are still working on the transaction. Railway continues to be one of the key focus areas of CMC and we believe that not only that we have got required domain strengths we have got excellent understanding of their requirements and their working so that gives us lot of headstart in terms of how we are able to execute projects efficiently with them so the new projects come out we will evaluate that decide about it.
- Nirav Dalal:** So when was this project won Passenger management?
- R. Ramanan:** Last quarter.
- Nirav Dalal:** And what will have been the size?
- J.K. Gupta:** I think this Passenger management is a significant size actually.
- Nirav Dalal:** Sir and I had some book keeping questions, if you could give the split of the employees into contract and on roads?
- J.K. Gupta:** We had regular employee strength of 4578 and contract employee strength of 7011 and the split of the various segments into exports and domestic. You can take down domestic number then on aggregate you can use that so our domestic number in customer services is 89.13 Crores systems integration is 44 Crores IT enabled services 42 Crores education and training is all domestic.
- Nirav Dalal:** Thank you.

- Moderator:** Thank you. We have the next question from the line of Priya Rohira from Axis Capital. Please go ahead.
- Priya Rohira:** Hi JK, Ji, hi Ramanan. I just want your insight more on the SI outlook which you see for your business especially in the TCS and the second thing is if you could just share on the onsite offshore mix which we had in the current quarter?
- J.K. Gupta:** Yes, onsite offshore mix is almost stable as we had last quarter. It is around 21.5% that is offshore and so far SI is concerned we have seen that in SI we have consistently delivered growth in this quarter also our SI growth has been 12% on a quarter-on-quarter basis and sorry 6% on a quarter-on-quarter basis and 12% on a YoY basis. So average increase in SI is higher than the average increase in the overall revenue, so that is what we believe that we continue to have traction. Second thing is our strategy is also to grow this business as we enter into additional geographies whether it is in Middle East and Africa or whether it is Europe or APAC in most of these geographies the differentiated offering that you bring to the market are mostly coming out of SI business segment so SI business segment will have a tendency to grow faster compared to the average growth of the company.
- Priya Rohira:** But it can accelerate even from these levels under the...
- J.K. Gupta:** No basically what we believe Priya is that whatever effort that we have invested in these new geographies over last 18 months have started yielding results and as you know that as the time passes by the momentum picks up so we do believe that there is new geographies are going to deliver better growth for us in SI business segment.
- Priya Rohira:** That is helpful. Thank you very much and wish you all the best.
- Moderator:** Thank you. We have the next question from the line of Bharat Seth from Quest Investment. Please go ahead.
- Bharat Seth:** Hi Ramanan and JK. Good evening and congratulations on an excellent set and again now I do not know next quarter whether we will be able to talk separately for CMC or not. Well really you people have created a tremendous value for the investors. Now on the port side we were looking a bigger picture on Europe side so just part of this transportation so how do you see that?
- R. Ramanan:** In fact we have been aggressively positioning ourselves in ports in Europe and we have had some successes already but we think that we will have quite a few more successes in the coming months. Now with this amalgamation in plan and in action we will probably have even more traction in many of the ports that TCS geographies can enable us to attack. For example you have a number of ports in the Netherlands and the Scandinavian countries in the Eastern Europe and so on and so we feel that the access to that will become even greater for us and so I think we have a great solution in ports will can capture a lion's share of the market as many of the ports are trying to modernize right now and we seem to be in a very good position to capture a real value for CMC and for TCS in the process.
- Bharat Seth:** There is a recent slowdown in the Europe so how do you see European market for our sales?
- R. Ramanan:** The slowdown is at a macro level, which is happening but most of these ports are direly in need of modernization and modernization is actually going to help them become more efficient so if they want to address the slowdown

they have to bring greater efficiency in the operations of their ports and so on so I see that as an opportunity for the CMC rather than as a negative situation.

**Bharat Seth:** Now can you give some flavor in this six international wins that we have in this quarter so is there anything out of which in solution side?

**R. Ramanan:** In Europe it has been on solutions and in the America's we have got two wins in embedded and real time systems one in software solutions and services and one in infrastructure management and in the Middle East and Africa again we have got solutions for insurance and e-governance and we have added two clients there.

**Bharat Seth:** What stage we have reached for rolling out our life insurance product?

**R. Ramanan:** Our life insurance product is already being implemented in Africa for one major client. We are currently in discussions with the few other customers and hopefully within the next two quarters we should be able to see some additional wins in that area.

**Bharat Seth:** Looking at the opportunity in this insurance now vis-à-vis in general insurance now in with life so which offer the larger opportunity?

**R. Ramanan:** The larger opportunity is still in general insurance for us because many of the life insurance solutions have longer life cycles of change and whereas in general insurance the need to introduce newer products and faster products and configuration of new products is high so we still see greater opportunities in general insurance than in life but the life insurance solutions would be long-term and significant if whenever we win that.

**Bharat Seth:** So the ticket size will be larger.

**R. Ramanan:** The ticket size will be larger.

**Bharat Seth:** Sir how our effort in this data analytics or now with TCS we says also larger presence in data analytics is going to help each other so what are our strength vis-à-vis with TCS strength?

**R. Ramanan:** Our strength we have develop some core platform we have developed a solution called Proteon and Proteon is solution based on big data analytics. It is generic big data analytic solution that can be applied to multiple verticals so I am sure we will have opportunities of leveraging that and integrating it with TCS solutions in big data analytics.

**Bharat Seth:** So both the companies have the solution?

**R. Ramanan:** Yes, we have a product and it is a generic product which can be used for multiple verticals.

**Bharat Seth:** Have you got any win on this generic product?

**R. Ramanan:** Yes we already had in fact this was used this product was developed as a result of the work that we were doing for university of Ervine in healthcare related big data and analytics. It has already a reference and we have now also implemented it for a few other customers in India.

- Bharat Seth:** Now and so far our presence was not there in Latin American side so do we see any opportunity on Latin American big opportunity?
- R. Ramanan:** Yes, I think in the transportation, e-governance and ports area I do see opportunity for CMC to leverage TCS presence in a significant manner in those areas.
- Bharat Seth:** Thanks and all the best both of you. Thank you very much.
- Moderator:** Thank you. As there are no further questions, I now hand the floor back to Mr. Ashish Aggarwal.
- Ashish Aggarwal:** Thanks Mosin. I would like to thank all the participants' for taking out their valuable time for this call as well as the management for taking out their time to participate in this call. Thanks Sir.
- J.K. Gupta:** Thank you Ashish and thanks to all the participants' to come on the call. Thank you very much and have a good night.
- Moderator:** Thank you. On behalf of Tata Securities Limited that concludes this conference. Thank you for joining us and you may disconnect your lines.