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Transcript

Earnings Conference Call of CMC Limited – Q4 (FY 10)

Participants: Mr. R. Ramanan, MD & CEO
Mr. J. K. Gupta, CFO
Mr. Prashant Shukla, COO

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Presentation Session

Moderator: Good morning ladies and gentlemen. I am Edwin, moderator for this conference. Welcome to the conference call of CMC Limited. We have with us today, Mr. R. Ramanan, MD and CEO, Mr. J.K. Gupta, CFO and Mr. Prashant Shukla, COO. At this moment all participants are in listen only mode. Later, we will conduct a question and answer session, at that time if you have a question, please press * and 1 on your telephone key pad. Please note this conference is recorded. I would now like to hand over the conference to Mr. Ashish Aggarwal, from Tata Securities. Please go ahead sir.

Ashish Aggarwal: Yeah. Thanks Edwin. Good morning everyone. On behalf of Tata Securities, I welcome you all to CMC Limited Q4 FY 10 results conference call. I would like to offer my sincere thanks to the management and the participants for sparing their valuable time for the call. Without much further ado I would like to handover the call to the management to discuss the results. Over to you, sir.

J.K. Gupta: Thank you Ashish and a very warm welcome to all the participants in this call, on behalf of the full management team of CMC. I've with me, Mr. R. Ramanan, Managing Director and CEO of the company and Prashant Shukla, the Chief Operating Officer. And I, along with my two other colleagues in the management will endeavor to answer all the questions that people may have. And before that I would like to just give you a brief about the financial performance of the company that was approved by the board yesterday. The results were released yesterday and I am sure that most of the participants had time to go through the results; still I will give you a brief outline of the

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summary of our performance. The results of operations in the company for Q4 of FY 10 reflect continued all around improvement for the fourth successive quarter in this year in line with the clear strategic of the company to improve business mix, improve margins and cash flows. Consolidated operating revenue in Q4 was Rs.230.11 crores, an increase of 9% Q-on-Q, but a decline of 2% YOY, which is primarily due to decline in the equipment revenue by 64% YOY to 17.38 crores, very much in line with the company strategy that we have been sharing with all the stakeholders over last four quarters. Our services revenue grew 10% Q-on-Q and 12% YOY. And services revenue share in total revenue from sales and services was 92.4% compared to 91.5% in the last quarter. It means our equipment share came down to almost 7.6% in this quarter. International revenue grew 13% Q-on-Q and 22% YOY. And share of international business and total revenue from sales and services Improved further to 54.2% from 52.5% in the last quarter. American subsidiary, CMC Americas contributed significantly to the growth in the international and services revenue. CMC Americas grew 16% quarter on quarter in Dollar Terms. This is the fourth successive quarter of sequential growth in America. It delivered 50% YOY growth in dollar terms in Q4. This improvement in business mix towards more share of services business and international business helped improving the operating margins. Our consolidated operating margin i.e. EBITDA, in Q4 was Rs.48.26 crores, which grew 12% Q-on-Q and 22% YOY. And it gave us the highest ever EBITDA margins of 21% compared to 20.5% in the last quarter, an expansion of 50 basis points quarter on quarter. Company earned consolidated profit after tax of 44.30 crores, an increase of 22% Q-on-Q and 15% YOY. And PAT margin in this quarter was 18.7% versus 16.9% last quarter, an expansion of 180 basis points on a Q-on-Q basis. Our average effective tax rate during this quarter was 13.6%. As we shared in the previous quarter also the company got covered under the provision of minimum alternative tax this year. And accordingly we have taken Rs.5.08 crore as MAT credit entitlement for this financial year. In this quarter, we added nine new clients, that brings the total client addition during the year to 47. In this quarter, we added two clients in America in the areas of embedded systems and software services. In addition, we deepened our relationship with the key clients in America, with new orders from our existing clients. Two clients were added in UK and in Europe in the embedded systems. And five clients were added in India in e-Governance, education and

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infrastructure space. Our other income in this quarter was Rs. 6.26 crores, which includes income from mutual fund investment at Rs.1.56 crores, a recovery of old bad debts amounting to Rs.4.14 crores. Our annualized manpower attrition was reasonable at 13.0%. We further improved our manpower productivity in this quarter, measured as a Net Value Added per person month, which improved by 6% over Q3. The company had the total manpower strength of 5551 at the end of this quarter. Company had total Cash and Cash equivalent of Rs. 263 crores. This is an increase of 2 crores over last quarter. But during this quarter we repaid our complete loan of Rs.35 crores which we had earlier taken for capital expenditure. And further CAPEX of Rs.12 crores was incurred in this quarter. We had an investment of 195 crores in debt based mutual funds. We were able to further reduce our receivable days to 86 days from 89 days at the beginning of the quarter and 100 days at the beginning of the year. When we look at cumulative performance for full financial year, we are very pleased with the key performance parameters of this year. Company achieved significant improvement in the revenue mix, helping in the improvement in margins and profit after tax on a full year basis. Our services revenue increased by 8% and share of services revenue was 88.2% for the year compared to 75.3% last year. Equipment business decline by 56% to Rs. 103 crores. International revenue increased by 15% and share of international revenue was 50% compared to 40.4% last year. EBITDA increased to 161.72 crores, which is an increase of 28% over last year and EBITDA margin expanded by 510 basis points to 18.6%. PAT increased to 143.23 crores, which is an increase of 23% over last year. And PAT margin expanded by 410 basis points to 16.1%. PBT margin expansion of 390 basis points for the year as a whole expanded to 18.8%. And we had an effective tax rate for the year as a whole at 14.5%. So, from my side this was a brief snapshot of the financial performance and key financial performance indices. With this, I hand you over to Mr. Ramanan to take you through some of the key strategic initiatives and key focus areas of the company, which helped us in delivering this kind of improvement in financial numbers. Mr. Ramanan.

R. Ramanan: Yeah, thanks J.K. and good morning everybody and a Happy New Year to all of those who have been celebrating Vishu and the New Year. I don't think I have much to add to what J.K. has already covered, except that we are happy to share that some of the strategies we have been outlining to you over the last couple of years and that is

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focus on increased value adding solutions in services business. Focus in the domestic market in private sector and in key deals in the Government which are in synergies with TCS as well as direct revenues. And focus on the international business in key segments of CMC which are SI solutions, ITES, digitization and work flow management services and embedded systems technology. All of these have been yielding us good results. With the results that last quarter we had, one of our best performances ever in the history of CMC, both in terms of profitability, in margins as well as growth. We will continue to maintain this focus during the coming years. Of course, whatever we did in terms of decrease in equipment business or low margin business, we have been able to achieve as much as we could during the current year. So the focus going forward is seeing how we can increase now, consistently quarter on quarter and during the year, our solutions and services business in each of the segments. Now what was also heartening for us during the last quarter was all the four SBU's showed growth, including our education and training business which did quite well. And the thrust on all the four SBU's including the embedded systems which is part of our system integration SBU is going to have renewed focus and attention during the current year. We also added a couple of clients in each of the markets that we are in. And overall, we have added about 47 clients during the course of the year. And we hope that and these clients are good clients who have the potential to grow further for us. And therefore we look forward to the coming year with the same degree of optimism that we had during the last year. One of the things that we have also done is ensure that our cash flows has improved through very strong focus on operational excellence as well as the strong focus on operational excellence as well as the strong focus on the financial management. And as a result of that we have a much healthier balance sheet. And, as J.K. has shared, we have been able to even return back some of the loans that we have taken and still improved our overall position from a cash balance point of view. The other important thing that we are launching on during this year is a very sound focus on business excellence models that we are practicing within the company in line with the Tata business excellence model, the TBEM model as it is called. And that is supposed to help companies raise to the next level of growth which is what we would be aspiring for. And the initiatives are already in progress. There are some other initiatives that are in the company relating to Corporate Sustainability as well as Green Data Centre and technologies related to Green Data Centre. That's again

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within the core competency of the company. Infrastructure management has always been a strong core capability within the company. And with the increasing emphasis on climate change as well as Green IT and IT for Green, CMC will be also focusing in those areas. And in particular because CMC has always been strong on building management, intelligent management, building management systems and CMC house has been one of the first to be constructed in this country as an intelligent building. We are planning to launch this capability in the CMC on a much wider footprint, in the country and potentially also outside the country. So that's were we are. And we would be very happy to take questions from all of you on our performance during the quarter or any other clarifications that you may need.

Question and Answer Session

Moderator: Thank you sir. Ladies and gentlemen, we will now begin the question and answer session. If you have a question, please press * and 1 on your telephone key pad and wait for your turn to ask the question. If your question has been answered before your turn, and you wish to withdraw your request, you may do so by pressing # key. Ladies and gentlemen, please press * and 1 for your questions.

Our first question comes from Mr. Vinay Kulkarni from HDFC Mutual Fund. Please go ahead, sir.

Vinay Kulkarni: Good morning gentlemen. Congratulations on the great set of numbers.

J.K. Gupta: Thank you Vinay.

Vinay Kulkarni: Sir, if you could, Mr. Gupta, if you give me a break up of this system integration revenues of almost 471 crores for the quarter in whatever horizontals or verticals that you internally classified.

J.K. Gupta: Actually we have not got ready numbers of vertical-wise revenues. Out of Rs. 471 Crore, our domestic revenue is Rs. 128 Crore and remaining is international. So this is the break down that I can give you right away.

Vinay Kulkarni: Okay. And sir, I think it's been a great year, great quarter. I think great improvement in margins. Could you tell us some initiatives you are taking to take this company to the next level of growth, especially in terms of the high profit margin services revenues?

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R. Ramanan: Yeah. We are having, there are two additional focus that we are bringing into the organization now. We have had consistent focus on our product innovation over the last several years. But in this year, we are going to ensure that our product focus and our solution focus, is going to get strengthened. We have seen some good repeated, consistent growth in some of the products that we have namely the insurance product, the ports and cargo product, the identity management solutions product and the transportation, GPS, GIS based products as well as our securities product with respect to DP secure and trading systems and depository systems. So, we are going to ensure that these products are considerably strengthened and become competitive in the global market place. And therefore the R&D investment and the product innovation initiatives within the company will strengthen and we will continue to do that. We will also be strengthening our focus on embedded systems, IP creation. Because, in embedded systems, as we move up the value chain the ability to create prototype and to create intellectual property becomes key to the growth of this particular SBU. Couple of our clients in embedded systems have moved up the value chain in terms of leveraging the services of CMC. And two of these, I wouldn't want to name them, in the automotive sector for example, one of them has set up an engineering design center along with us. And in the transportation sector particularly in railways, embedded electronics, another customer has moved, has started working with us in higher design platforms with our core through the company itself. So, these are the sort of initiatives from a R&D and an innovation perspective that we will be strengthening to not only move up the value chain but also to be able to replicate our solutions in multiple geographies. The second area of focus that we are bringing in order to achieve growth is to bring a vertical focus in the key verticals in which we have been pretty consistent and strong. And what it means is, while we have been a SBU oriented organization to date, we are adding a layer of IP focus, industry practice focus in the key verticals particularly Government, defense and space, BFSI and transportation. Because, we see that we have a credible history of projects, system engineering and integration projects in these verticals. And we want to ensure that we are now able to address that vertical in a holistic manner in all the four SBU's that we practice in. So, this product focus as well as the industry sector focus will definitely be a key driver in the growth of the organization. On the

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operational side, I would like my COO to additionally talk about operational excellence parameters that we are focusing on, both in terms of delivery management as well as in terms of process excellence.

Prashant Shukla: Yeah, good morning everybody. To what J.K. and Mr. Ramanan have pointed out, there are few other areas that we are really tightly focusing on. One is the business excellence and business execution efficiency. You will notice the improvement in our margins. And one of the reasons why it has been achieved well is, because we have been able to do more with less. More work with better efficiency of our existing people. That has been made possible because of the several things that we have done in parallel. One of them is the creation of solutions around our asset. So, we have built, over the years we have developed expertise and domain knowledge in specific areas as well as in those areas that allows us to do the job that we were doing earlier more efficiently. And this will continue to manifest as we progress through the next year in terms of our business execution efficiency. The second thing is that as we engaged deeper with our customers, our ability to service them becomes better. In other words, we are able to offer more and more and more and more solutions to them. Because we have began to understand them better and better and better. And as a result of it, we are looking not only to grow vertically with our exiting customers as a strategy for growth, but also look at those particular verticals where we have identified those solutions and we have referenceable customers and we have domain experience to dwell into other customers. We do this for two reasons. One, it is a very good growth strategy from our perspective to say, we know this domain, we understand this customer and therefore we can replicate this solution with other customers. And to that extent, our answers are more credible. Two, because of the fact that we have been doing this with other customers; it allows us economies of scale as well as business execution, excellence and efficiency. In this way, we will continue to expand and grow and that is a key focus area for this year.

Vinay Kulkarni: Right sir. Thank you very much. I will come back for later.

Moderator: Thank you sir. Next question comes from Mr. Anup Upadhyay from SBI Mutual Fund.

Anup Upadhyay: Good morning sir. Congratulations for a great quarter. Sir, could you just throw some light on which verticals and

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service lines could have driven growth in system integration and particular trends within the target markets that you are addressing.

J.K. Gupta: Can you repeat the question? We lost you in between.

Anup Upadhyay: I wanted to understand which verticals, which industries or any particular kinds of projects are driving the growth in system integration. In this last quarter, we have grown by around 11% sequentially. So, I wanted to understand the source of growth.

R. Ramanan: Okay. In the system integration business, most of our growth comes through the solutions that we have developed in the banking, financial service, insurance sector. Particularly, insurance has grown remarkably well during the last year. And also, we have had growth in the banking, financial services area. We have two products and then we have solutions revolving around those products. One is our Trading system BOLT products which itself is a very important customer; Bombay Stock Exchange is a very important customer as all of you know. And our depository product, which has several derivative products associated with it, one of them also being the DP secure products which are there with most of the depository participants. The other area of growth has been in the transportation sector where our ports and cargo product has been implemented at multiple locations. And we have also won a couple of new clients during this year, which will have implementations during the next year. We have also grown in our GPS based Nirdeshak product for vehicle tracking systems as well as GPS based tracking systems both in the manufacturing segment as well as in mining and other energy segments. The third area in which we see potential for growth is biometric and identity management solutions during the coming year. Especially as the UID project is in the offing and there is going to be multiple need for identity management in various phase and various agencies which will integrate with the UID projects. And the fourth area that we see of course is the Government sector where 3 or 4 of our solutions have had multiple implementations. Our treasury management solution, our ERP solutions for the municipal corporation as well as our solutions for HR management have replicable potential in the Indian Government space. And we are definitely going to see multiple implementations during this year and the next year in various States in each of these areas. In terms of the international market, we have also focused on this, but we have also focused on

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working, establishing ODC's in India in the particular verticals where we have domain knowledge because of the product development capability that we have had. And our SI business has grown in the international market, particularly in BFSI and transportation sectors.

Anup Upadhyay: Great sir. And what percentage of our system integration revenues would be coming from products, license sale and implementation?

R. Ramanan: See most of our SI revenues actually come through license revenues and customization around our product. So, when we look at SI, it is difficult just to attribute a particular revenue size just to the license. Of course, there is a license part of it is there, but sometimes our business model is such that it is an integrated turnkey solution, where the software licenses get incorporated into a fixed price total project for the customer. So in the business that CMC has been in, traditionally in SI, it is always asset oriented. And even if there is no direct asset being used, some framework of the asset or some replication of a portion of the asset becomes an important differentiator in us winning that project. As an example, we have created a solution for digitization and workflow management. And around that comes also related knowledge processing and IT enabled services, services which would not have been possible if we did not have that asset and it would not have provided us the differentiator to be able to compete with some of the best in the market. So, it has been and it will continue to be asset driven, revolving around the asset, because that is where we differentiate ourselves from the rest of the people who provide pure services. And while we may be in the pure services play, it would be as a derivative and as a result of an asset that we have created.

Anup Upadhyay: Sure sir. Thanks a lot for your answers.

Moderator: Thank you sir. Next question comes from Mr. Sujit Parab of Enam Securities.

Priya: Hi. This is Priya here. Congratulations to the team on delivering one set of great numbers once again. My first question relates to the top line traction one should expect in the next year, in FY 011. We have seen great performance and project wins from CMC, at the same time system integration just continues to surprise. Could you give us some visibility, what we could see from at least the two key domains, our two business segments which is system integration and ITES? The second thing is, this

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quarter we had peak EBITDA margins, how sustainable are these? And what are the additional levers, one should look at? And the third thing is, if you could comment more on your insurance product in terms of the traction which we have seen? And also just give us the guidance on what tax rate one should assume and what is the CAPEX plan for FY 011?

R. Ramanan: Okay. I'll answer the first two questions and I'll have J.K. answer on the CAPEX part of it. I forgot the question.

Priya: The first one was with respect to the top line traction across business segments and what top line visibility one should look at for FY 011 or maybe next two year to start off.

R. Ramanan: Yeah. During this year, we wanted to clean up our business in a way and make sure that we are into profitable segments and that was the focus. And that's why we didn't bother too much about the top line as would have been evident in our results. But we did focus very strongly on the bottom line and that also got manifested in the results. We have reached the stage where now it is important to focus on top line growth while maintaining our current margins and that's going to be our focus. And I think, this quarter was, there was some evidence of it. We grew 9% quarter on quarter in terms of revenue and at the same time we were also able to grow on margins to 21%. While in this quarter we had some real good margins, we do want to maintain our 17 to 20% margins during our subsequent initiatives, even as we grow our revenues. So the focus on growth in revenue will be very strong during the year and at the same time, trying to maintain the margins between 17 to 20% will remain. Because, we had originally targeted, even earlier, that we should be crossing 15% margin. And we have done better than what we had planned and we would like to maintain it at that and grow further. In terms of the pipeline that we see, what has been heartening for us is that we have been able to build sustainable service streams. And because of that and that will continue to be our focus where we enter into an engagement. Typically we try to enter into a long term engagement where in addition to project revenue that will kick in at the beginning of the project. We look for sustainable services revenues at the end of the project, so that we don't have lumps in our revenue stream. And that's what we have been trying to do, so that we are able to show consistent quarter on quarter growth. While this has been the intent, in a particular quarter you may see

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some lumps in it. But that has to be expected, because we are in a turnkey projects type of business. And overall, during the course of the year, we will be focusing on sustained growth. Did I answer both your questions?

Priya: Yeah. I just wanted a breakup more on the systems integration and ITES business. And also the follow on, what percentage of revenues are typically maintenance or recurring in nature, because embedded now is a strong practice for you.

R. Ramanan: Yeah, if I look at SI, if I look at embedded part, it is sustainable and it is repetitive. Because, typically there we enter into a relationship where it is not just one project or one product, but it is a relationship, a long term relationship for R&D outsourcing or high tech outsourcing. If you look at our solutions business, then it is one time. But typically there our experience has been, most of our solutions are solutions which people invest in for five years or ten years. So, there is a revenue stream which gets associated in terms of customization, enhancement and maintenance. So, it's not just maintenance. Typically, maintenance is 15 to 20% of whatever is our project value that is routine maintenance. But what really kicks in at the end of an implementation of a solution is customization and enhancement, because the customers keep wanting to enhance that. And that is a significant revenue stream. In general, we have seen that during the course of a project 60 to 70% of our revenues are service related revenues and 30 to 40% would be the license related first time revenues.

Priya: Okay. And also on the insurance side, we have seen good traction and the product is quite strong, if you could share some of your experience which the clients would have implemented and that's rolling across other insurance players as well?

R. Ramanan: Yes, our insurance business has done well. And in fact we have been able to penetrate the bracketing civil sector much better than our competition, I guess, because most of the large players, whether it is ICICI Lombard or HDFC and so on, they are all our customers today. And we see that we are seeing a pipeline of few other prospects which we are working on. The privatization of insurance in India is still taking place, so it's a story which is continuing, which is going to continue during the coming years. We are also trying to enter into related areas of business in life insurance as well as looking at the insurance vertical a little

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more holistically for digitization, document and work flow management services. These are the existing customers, because they see that they are leveraging us right now for our SI product but they could potentially leverage us for other areas of service, including education and training. So, we see growth in that area with our existing insurance clients. We are looking at the international markets in Middle East, Africa and even in APAC, Asia-Pacific region. So, that will be a plus during the coming year. And hopefully we will be able to make some penetration there which augers well for the future if we are able to replicate it in those geographies.

Priya: Sure. And what is the revenue breakup for embedded in pure absolute terms? J.K., if you could just help us over here. And also the tax rate for FY 011 and our CAPEX plans for FY 011.

J.K. Gupta: Our embedded system revenue has been around 100 crores this year. And our effective tax rates, for the current financial year has been 14.5% which came down from around 19.2% last year. We expect this kind of tax rate to be there for the next financial year also.

Priya: Sure. And in the CAPEX side?

J.K. Gupta: CAPEX in the current financial year, that is fiscal 2010, Rs. 27 crore was on the CAPEX. Our plan for the next financial year is Rs. 186 crore, because, we plan to complete the phase two of SEZ in Hyderabad in the current financial year. That is going to consume about Rs.132 crores of CAPEX.

Priya: It's 132 and not 180. Out of 186, 132.

J.K. Gupta: Total Rs. 186 crore, total CAPEX plan. Rs. 132 crore is going to be on the Hyderabad SEZ.

Priya: Sure. And out of the 5551 people, what are the number of subcontractors here?

J.K. Gupta: 1900.

Priya: Okay, great. Thanks sir. Thanks and wish you all the best.

J.K. Gupta: Thank you.

R. Ramanan: Thank you.

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Moderator: Thank you sir. Next question comes from Mr. Shekar Singh of Goldman Sachs.

Shekar Singh: Hello sir. Just wanted to understand sort of the opportunities which exist for the biometric products, you mentioned about the UID project and you might be associated with it. What is the sort of opportunity, what can be the revenue stream?

R. Ramanan: The UID project has different sources of revenue. First is related to the centralized UID project itself where you are actually creating the database and you are creating the de-duplication software for the biometrics and so on for the identity management. So, that is one. That is a large project where we would synergize with partners including TCS and so on to address those projects. The second part is the services part which will happen in several States across the country, because you have to collect this data. And it is very similar to the type of projects that we did for census in India and so on. So, that's a very service related intensive exercise. And there would be multiple projects that could get spawned in different States. The third this, there would be agencies which are going to interface with the UID systems. Because the whole process is that once the UID has been created then different agencies can use the UID for their own purposes, whether it be banks or financial service organizations or insurance companies or telecom companies and so on. So, again there would be a multiple opportunities in identity management or applications using identity management which should be opened up. So, overall the UID project would spawn several opportunities. And therefore having been in the business of census and identity management, CMC is looking very proactively at all these opportunities. And I am not able to put a number or a value to what we will win or how much we will win, but the opportunity exists and we have to see which one are the ones that we will go after and which will maximize both the revenue as well as profitability.

Prashant Shukla: To that if I may add, this entire identity space is just coming to fore. If you look at the overall kind of things that are happening in the identity space, that is pretty big. I definitely see UID has a very large part of it. But, if you look at identity management as in even private companies, access control and so on and so forth, all that will be centered around, a large part of that will be centered around biometrics. And here I want to point out that CMC

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is in fact the only companies in India with a track record in biometrics and finger printing for I would say for 2-2½ decades. So, we are well positioned in terms of our domain experience to take advantage of this, not only for UID, but for the larger identity management space.

Shekar Singh: Thanks a lot for this. Secondly, just wanted to know like, you mentioned the sustainable long term services revenues which you have. So, of FY 10 revenues, what percentage of that will be in this category?

J.K. Gupta: Most of our revenues, IT enabled services and SI is falling in this category.

Shekar Singh: I thought some portion of system integration will be lumpy project based business.

J.K. Gupta: Very less. We have reduced that portion very low now. Out of Rs. 471 crore that we have in SI, these kinds of lumpy business will not be more than 20%.

Shekar Singh: Okay, great. Thanks a lot sir.

Moderator: Thank you sir. Next question comes from Ms. Subhashini Gurumuthy of Ambit Capital.

Subhashini Gurumuthy: Hi. Congrats to the management on the good set of numbers. My question was primarily retained to the SI business. Apart from the BFSI and transportation, space which you mentioned are your focus areas, how will basically power and e-Governance areas coming up for you?

R. Ramanan: Like I said, the four areas in which CMC would be focusing on are BFSI, manufacturing energy resources, because there we have SCADA systems and power systems and electricity and billing systems which we have been doing projects in those areas. And in addition to the transportation, space, we will also be focusing on e-Governance. I had mentioned about the applicable solutions of treasury management or HR management systems or Government or citizen services, which are products which have been well established in the Government and which have good references. Of course, the UID project is another large e-Governance project. And the Passport Seva Project which is also underway is going to have significant implementation happening during the course of the year. One other area that we are working, but we hope to see some good growth and

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typically the cycles are longer in this are the defense and space related activities. CMC has had good track record in these areas and we are hoping that some of the large projects that are being undertaken by defense and space will at least see closure in terms of the orders during the year. Some of it may kick in during this year, the revenues and some of it would kick in during the next year.

Prashant Shukla: Of course, I want to add to this. The solutions that we are providing for the Government on police and that also we consider as a part of the Government business.

Subhashini Gurumuthy: Sure. And how does the order pipeline for, basically the order book for SI business look for FY 11 now?

R. Ramanan: We normally don't give guidance on the order book or on the numbers. But these are areas which I mentioned where we have been actively working and proactively engaging with our customers. And there are some orders which we have won already during the current year which will see some fruition of revenue. And I would just say that the opportunity base that is there in the market is pretty decent.

Subhashini Gurumuthy: Sure. Also, I wanted to understand any new initiatives which we are taking basically in the education and training space?

R. Ramanan: We are. We are going to be very strongly relooking at the educational and training space during this current year. As I had mentioned in the last telecon or the analysts call, we are revamping our education and training portfolio to include somewhere elements of corporate training, somewhere elements of vocational training and also seeing what we can do in the international markets. The amount that's spent that is there and which has been identified by the Government for education, training is quite high. We need to see how and what agencies in the Government will be leveraging these funds and in what manner. And we are still studying because things are still not clear there. But, with the type of fund that is expected we are looking at education and training more from a knowledge systems integrations perspective than pure education and training. What I mean by that is that this is going to result in several schools getting computerized, several colleges getting computerized, rural educational establishment being set and so on. And so there is an element of systems integration business, coupled with education and training that is going to be enabled through

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these initiatives. So, we are going to be looking at it in a slightly different manner, not just conducting education and training but looking at the educational sector itself and see how we can leverage that using our education and training core capability.

Subhashini Gurumuthy: Sure. Are we also looking at the private school space here?

R. Ramanan: Yes. We would be looking at both private schools as well as public schools, Government schools because there is a major dearth of good school management system or educational management systems, student university management systems, many of these. Even some of the private schools and advanced or well established schools do not have good educational management systems, content management systems and learning management systems. And I think the emphasis on business learning and some of this is also increasing with some of the schools spreading across multiple locations. So, there is an opportunity there which we want to tap.

Subhashini Gurumuthy: Sure. Just one last question, basically on the ITES margins, while for the full year we have done pretty well, this quarter I see some slippage. Could you just throw some light on it?

J.K. Gupta: Yeah. We had some amount of setup cost for a new project that we have, so which cost got expensed in one quarter. I think you should look at our annual numbers. Well, last quarter when we had 40% margin, at that time also we told that we are not seeing 40% margin sustainable for a longer period. We have been always telling that a margin of around 33% or 34% is something which is more sustainable over longer period. We are happy for the full year margin at 36%; I think that's a right kind of an indicator.

Subhashini Gurumuthy: Sure. Thanks. That's all from my side. That was very helpful.

J.K. Gupta: Thank you.

Moderator: Thank you sir. Next question comes from Mr. Bharat Sheth of Quest Investment.

Bharat Sheth: Congratulations sir, on a good set of numbers to management.

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J.K. Gupta: Thank you Bharat.

Bharat Sheth: Sir, you said international business is 50%, so that is our total business or say service business only?

J.K. Gupta: No, total business. We had a total revenue of Rs. 871 crores, out of which about 435 is international and 435 is services.

Bharat Sheth: Okay sir. Does it mean that in domestic service business, we have not been able to grow this year? Only growth has come from international services?

J.K. Gupta: Not service, because if you look at our equipment business, that is fallen almost 56%, so most of the decline in the domestic has been on the front of equipment business.

Bharat Sheth: Okay. Now what I gather from whatever talks, that next year we are looking top line, service growth substantially. So, in last concall also you mentioned that around 25% kind of service growth, we can look for, the kind of traction we have. This year we averaged to only 8% growth service business. So, what kind of a service growth that we are looking for? In last concall, you said around 25%.

J.K. Gupta: Bharat let me just clarify. What we said that this year we have been focusing primarily on readjusting our business mix towards more profitable businesses. And another clarification we did is not an issue of equipment and services; it's a question of where we are getting lower margins. If there is an equipment transaction which is justified based on margins, we will go for that also. So, the test of selecting the business is whether the business is profitable and generating cash or not. That's one aspect. Second aspect is that when we talked about this domestic and international focus, there also primarily we got more deals into international because of the profit margins. Any deal which is in the domestic market which offers a good margin, we'll go for that also. So, in last year, what we have been differentiating in the opportunities on the basis of profitability. This 8% growth is an outcome of that focus, not that we were targeting certain specific number. When we talked about going forward we can grow 20%, 25% or whatever, our message at that time was that in the current year we would focus on the adjustment of business, next year we would like to grow in line with what the market growth rate is. So, we said at that time that we do expect the industry to grow at say around 20%, because we

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started seeing some signs of turnaround in the industry. So, again we want to repeat this message, we don't want to put precise number, whether we would grow 20% or we are likely to grow 20 or 25% or whatever. But, what we are trying to say is that our phase of adjustment of the business mix is over and now we would like to deliver growth in line with the industry growth.

Bharat Sheth: Okay. And sir, second question is that how do you see, again in service sector side, in business revenue mix between domestic and international, is it going in more or less the same?

J.K. Gupta: Again as I said, we don't have a particular target in mind in terms of domestic and international business. We are seeing some very good opportunities base emerging in the domestic market also. And we traditionally have got some strength in the domestic market opportunities. So, we are not going to ignore any of these large domestic market opportunities. We will continue to select the business opportunities, both in domestic and international market based on its profit potential. Other thing is that we do see on horizon some of the large e-Governance projects and all that which we would like to address in collaboration with TCS. For example, last year we got Passport Seva Project. We would be seeing, some larger revenues streams to start materializing in the financial year FY 11. So, that may have a positive impact on overall domestic businesses. So, we are again not giving a particular kind of a target number. If you remember three years ago, we told that, at that time we would like to see our domestic, international business mix to go to 50-50. And we are very happy that this year, whatever we promised three years ago, that in 2 to 3 years time we would be reaching there, we have reached here. The idea at that time, that we were operating at a single digit of operating margins and we wanted to break out of it. We promised that once we do 50-50 of domestic, international mix, we will be able to cross 15% of EBITDA margins. At that time, we were operating at around 8-8½% of margins. And this is where our belief is that what is required to be done to achieve, that belief has been proved right. We delivered the EBITDA margin of 18.6% at 50-50. So, going forward we are not fixing a particular target mix of a business. But, definitely we would continue to keep our eyes in the margins and we would like to continue this trajectory of improvement in margins. And if it comes to business mix improvement, that would be one of the index that we will be tracking.

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Bharat Sheth: Okay. And sir, second thing so Mr. Ramanan said that in Q4 we achieved 21% kind of margin, so that is sustainable or full year kind of a margin is sustainable?

J.K. Gupta: Again I would like to clarify; we don't want to give a particular number. This quarter we had international business share of 54%. So, definitely it has got a correlation with international business share. But, I would think in our kind of business, a bit of longer period should be taken for a comparison or a review, so better will be to start building up on a full year margin of 18.6%.

Bharat Sheth: Okay. And sir, just on tax side, for FY 11 what tax rate that you said will be?

J.K. Gupta: This year we had about 14.5%, next year should be almost similar.

Bharat Sheth: Similar?

J.K. Gupta: Yeah.

Bharat Sheth: Okay. And sir, can you elaborate more on this e-Passport, how much revenue we got in FY 10? And what was the mix whether equipment and all?

J.K. Gupta: We didn't too much equipment in Passport Seva project. We have been focusing only on the services part. In current financial year, there is not substantial amount of Passport Seva revenue that we got. It has been less than Rs. 10 crores. So, I think fiscal 2011 is going to be the year when the passport project is going to be rolled out in all locations. So, I think by the end of the financial year, when the rollout is complete, the numbers will start reflecting and fiscal 2012 will be the year of full blown revenue stream coming into this project.

Bharat Sheth: In FY 12?

J.K. Gupta: Yeah, because, in the current financial year we have rolled out only the pilot sites. And in phases it will be rolled out all other sites which are over 80. So, in phases this revenue will start building up. And as all the sites are rolled out and the business starts flowing, current year also will not reflect full year of operation. The first full year operation is going to be next financial year that is fiscal 2012.

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Bharat Sheth: Okay. And sir, how much rental income we got from TCS last year and how much we are expecting this year?

J.K. Gupta: In fiscal 2010, we got about 12 crores. Fiscal 2011, we are not expecting any significant addition to this, because phase one is complete and the phase two will become occupiable only by the fourth quarter. So, there is a potential of some small additional revenue coming in fourth quarter. Otherwise, our next financial year again will be a kind of full blown additional revenue coming out of it.

Bharat Sheth: But I understand that in second phase we are also going to occupy CMC for our sales…

J.K. Gupta: Yeah, you are absolutely right. Second phase is going to be jointly used by TCS and CMC. As you are fully aware that STP is going to be phased out, STP is going to be phased out by fiscal 2011. So, we would like to do all new businesses in SEZ. So, this is the reason why we are building up our own SEZ delivery capabilities.

Bharat Sheth: How much seats capability that we are building for CMC in that?

J.K. Gupta: In this second phase we will be taking about 2000 seats. Total in second phase is going to be 6300, so remaining will go to TCS.

Bharat Sheth: Okay. Thank you sir. Thank you very much.

J.K. Gupta: Thank you Bharat.

Moderator: Thank you sir. Next question comes from Mr. Niral Dalal of Almondz Securities.

Niral Dalal: Yeah, hello sir. Congrats on a good set of numbers.

J.K. Gupta: Thank you Niral.

Niral Dalal: Yeah. Can you explain to me as to why the subcontracting costs have been increasing?

J.K. Gupta: Niral, we are not able to hear you, can you speak a bit louder?

Niral Dalal: Yeah. I was interested in knowing about the subcontracting costs which have been increasing over the past few quarters. And is it related to the increase in the system integration business? And if that is so, since the

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margins have been increasing, so does subcontracting, increase in subcontracting relate to increase in margins or should it be related to decrease in margins?

J.K. Gupta: No, subcontracting is more in the IT enabled services business. It's not too much in SI business. And why we use subcontracting model, because it converts lot of our fixed cost into variable cost. And it really helps us in achieving our desired margins or controlling the margins.

J.K. Gupta: Niral, we are still not able to hear you properly, can you speak a bit louder?

Niral Dalal: Yeah. So, that is why the margins in the ITES business have gone down?

J.K. Gupta: No, Niral. In fact, ITES business margins for the full year have gone up from 21% to 36%. Of course, in this quarter as compared to the last quarter that is Q3, it has come down. Two reasons. We told last quarter also that 40% margin should not build in for future. Second thing is as I told a bit earlier in this call itself, that there was certain initial setup cost for one of the project which we got in this quarter that was factored in Q4. And I think over a longer period you must look at our full year margin that is something which is inherent in this business.

Niral Dalal: Okay fine. Yeah, thanks a lot.

J.K. Gupta: Thank you.

Moderator: Thank you sir. Next question comes from Mr. Neerav Dalal of Capital Market.

Neerav Dalal: Sir, good morning sir. All my questions have been answered. Thanks a lot.

Moderator: Thank you sir. Next question comes from Mr. Prashant Kumar Jha of Wealth Management.

Prashant Kumar Jha: Good afternoon.

J.K. Gupta: Good afternoon.

Prashant Kumar Jha: Sir, can you briefly say about what kind of revenue you are getting from Government projects from India?

J.K. Gupta: Our Government business share is about 28-29% of the total business.

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Prashant Kumar Jha: Of total revenues?

J.K. Gupta: Yeah.

Prashant Kumar Jha: The breakup in terms of SI business?

J.K. Gupta: I don't have a ready break down. I think if you give me a call later, I can give you the break down.

Prashant Kumar Jha: Okay. And what kind of revenue can we expect going forward from the Government business in India?

J.K. Gupta: I think as we mentioned in the call earlier, we do expect lot of spends to take place in Government. And we do expect some of the large projects to come out of the Government, which we plan to address in collaboration with TCS. If you look at the domestic market, that is widely believed that the Government spending could be a driver for the growth in IT business. If that is true then we can expect an uptick in the share of the Government business in domestic market. But, we can't put a number right now.

Prashant Kumar Jha: Will the margins be similar to the company margins?

J.K. Gupta: No. Government margins, our profiling is slightly different. You know all these larger projects are fiercely competitive, lot of large companies are competing on that. But, one aspect of the Government business, I would like to just put on the table is that on a project profitability basis, sometimes the Government project may not really reflect good margins comparable to the other businesses that the company does. But the experience that we gain in executing large Government projects are something which is so invaluable, which you can showcase and leverage in gaining some of the more profitable businesses in other geographies and other clients. So, we strongly believe that most of the projects that is coming about from the Indian Government and the Governments in India, because of the sheer size and the sheer complexities that the experience that you gain are much more valuable than the margins that you may be getting on those projects. Another thing I would like to clarify that every project will still have to be justified on its own commercials. And we definitely don't do projects on a loss and we would like to get reasonable margins.

Prashant Kumar Jha: Okay, thank you sir.

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Moderator: Thank you sir. Ladies and gentlemen, please press * and 1 for your questions. Next question comes from Mr. Anshul Doshi of Amansa Capital.

Anshul Doshi: Hello, hello.

J.K. Gupta: Yeah Anshul.

Anshul Doshi: Yes sir, under what head do you receive your rental income from TCS in whatever you receive?

J.K. Gupta: That is under services.

Anshul Doshi: Services?

J.K. Gupta: Yeah, if you look at the last year printed balance sheet you will see the clarification.

Anshul Doshi: Okay. And what is the head count for this quarter?

J.K. Gupta: Our total head count at the end is 5551. We had a net addition of 285 people in this quarter.

Anshul Doshi: 285?

J.K. Gupta: 285.

Anshul Doshi: And you expect any more increase in next quarter?

J.K. Gupta: Yeah. As we continue to focus more on services business, which is going to be people intensive, there could be expectation of more additions.

Anshul Doshi: And what would be the FOREX gain or loss during the quarter?

J.K. Gupta: In this quarter, we lost about Rs. 1.4 crore. Last quarter, we had lost about Rs. 1.2 crores.

Anshul Doshi: And for the full year?

J.K. Gupta: 6 crore rupees loss, which was a gain of Rs. 9.4 crore last year.

Anshul Doshi: Okay. And the other thing, what would be our hedge position?

J.K. Gupta: We have got about a million dollar of forward cover, sorry 1.5 million dollars of forward cover as of now.

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Anshul Doshi: 1.5 million dollars of forward. At what rate?

J.K. Gupta: I think average rate is about 44.85.

Anshul Doshi: 40?

J.K. Gupta: 44.85.

Anshul Doshi: Okay. Okay sir. Thank you sir.

Moderator: Next question comes from Ms. Sohini Andani of SBI Mutual Fund.

Sohini Andani: Just wanted to understand in case of your international revenues, in terms of geographies how it would be split between US, Europe and other geographies?

J.K. Gupta: The bulk of the international business is coming out of US. For the year, we had about 50% international, of this 50%, 38% came from US. So, that's where the largest geography.

Sohini Andani: And that is largely reflected in the revenues of CMC Americas?

J.K. Gupta: That's right.

Sohini Andani: Okay. Right sir. Thank you. Thank you sir.

Moderator: Next follow up question comes from Mr. Bharat Sheth of Quest Investment.

Bharat Sheth: Hello.

J.K. Gupta: Hello Bharat.

Bharat Sheth: Yes. Can you just elaborate, what will be the impact of rupees strengthening on our profitability? And second is this wage increase in salary, how is it going to affect us?

J.K. Gupta: Dollar, rupee parity change, in fact I just told, in this quarter we lost about Rs. 1.4 crores.

Bharat Sheth: No, no, going ahead, how do you see?

J.K. Gupta: Yeah, going ahead, because America itself is contributing about 40% of our overall business. So, definitely we are going to have impact on that base. But, if you see in this

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financial year itself, we had a significant change in dollar rupee parity. It came down from Rs. 50 to around Rs.45 or even less than Rs.45. For the year as a whole, we lost about Rs.6 crores on this account. So, if you just make an average assessment of that, a rupee change will affect us to the extent of about 1.2 crores.

Bharat Sheth: Okay. And sir, last year there was no much of salary hike, whereas this year the whole industry is increasing, so how is going to affect us?

J.K. Gupta: This year we are making an assessment and see what kind of salary hikes are going to be granted. In our case, salary hikes are granted from 1st of July. So, we have still got some time to do our detailing on this.

Bharat Sheth: Okay. Thank you.

Moderator: Thank you sir. There are no further questions. Now I hand over the floor to Mr. Ashish Aggarwal for closing comments.

Ashish Aggarwal: I would like to thank all the participants who participated in this call. I would also like to thank the management for giving us an opportunity to host this call. Thanks, thanks, thank all of you.

Moderator: Thank you sir. Ladies and gentlemen, this concludes your conference for today. Thank you for your participation and for using Door Sabha's conference call service. You may disconnect your lines now. Thank you and have a pleasant day.

Note: 1.This document has been edited to improve readability.
2. Blanks in this transcript represent inaudible or incomprehensible words.