Transcript

Earnings Conference Call of CMC Limited – Q4 (FY 11)

Participants:
Mr. R. Ramanan, Managing Director & CEO
Mr. JK Gupta, CFO

Event Hosted by	**:**	**Tata Securities**
Event Date / Time	**:**	**19th April, 11.30 AM IST**
Moderator	**:**	**Mr. Ashish Aggarwal, Analyst, Tata Securities**

Presentation Session

Moderator Ladies and gentlemen good day and welcome to the Q4 FY11 results conference call of CMC Limited hosted by Tata Securities. As a reminder for the duration of the conference all participants' lines are in the listen only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call please signal an operator by pressing "*" and then "0" on your touchtone phone. Please note that this conference is being recorded. At this time I would like to hand the conference over to Mr. Ashish Aggarwal, thank you and over to you sir.

Ashish Aggarwal Good morning everyone. On behalf of Tata Securities, I welcome you all to CMC Limited Q4 FY11 results conference call. We have with us today Mr. R. Ramanan, MD and CEO and Mr. J.K. Gupta, CFO of CMC Limited. Without further ado I would now like to hand over the call to the management to discuss their Q4 FY11 results. Over to you sir.

JK Gupta Thanks Ashish and a very warm welcome to all the participants for sparing time to come on this call. First of all I will take you through some of the highlights of financial performance of the company which were approved by the board yesterday and I am sure that you had time to go through that.

Just a few highlights for the full year financials first before I come to the quarterly numbers. The company delivered a robust growth in revenue during the year as it completed phase of business transformation in the last year and the company continued to focus on improvement in revenue mix and improved cash flow management in 2010-2011. Total operating revenue this year grew almost 24% to Rs. 1,081 crore. Services revenue increased by 27% and the share of services revenue in overall operating revenue increased to 90.5% compared to 88.2% in the last year. Equipment business during this year remained flat at Rs. 103 crore. International revenue increased by 37% and the share of international revenue in overall revenue increased to 55% compared to 50% in the last year. CMC America business grew 47% in dollar terms to $102.6 million and the share of America geography in overall operating revenue increased to 43% from 38% last year.

Company had EBITDA increased to Rs. 206.84 crore which is an increase of 28% over last year. Profit after Tax increased to Rs. 179.41 crore which is an increase of 25% over last year. EBITDA margin expansion was 57 basis points to 19.14%, PBT margin expanded by 50 basis points to 19.3% and PAT margin expanded by 30 basis points to 16.4%. The company had an effective tax rate of 15.3% during the year as a whole.

Now coming to Q4 performance, the Company had operating revenue of Rs. 292.69 crore which is an increase of 7% Q-on-Q 27% Y-O-Y. Services revenue grew 7% Q-on-Q and 21% Y-O-Y. The share of services revenue and overall operating revenue was 88.8% compared to 89.5% in the previous quarter. International revenue grew 5% Q-on-Q and 26% Y-O-Y and the share of international revenue in total revenue from sales and services was 53.6% compared to 54.7% in the previous quarter.

American subsidiary continues to contribute significantly to growth in the international and services revenue. CMC America grew 7% Q-on-Q and 32% Y-O-Y in dollar terms. Consolidated operating profit in Q4 was Rs. 50.72 crore which is 1% up Q-on-Q and 5% up Y-O-Y giving an EBITDA margin of 17.3%. Company had the consolidated profit after tax of Rs. 43.97 crore during the quarter. The PAT margin in this quarter was 14.8% compared to 15.2% Y-O-Y. This quarter we had certain additional expenditure on manpower and increased expenditure on building up sales force. SG&A expenditure increased by almost 20 basis points this quarter compared to last quarter. Company had the effective average tax rate of 15.2%. As we have been sharing with all the investors, the company got covered under the provisions of MAT and during this quarter we have taken Rs. 3.7 crore as MAT credit entitlement.

We continue to add clients. In this quarter also we added 20 clients. For the year as a whole we have added 80 clients. Out of the 20 clients in this quarter, we have added eight clients in Americas in the areas from embedded systems and 12 clients were added in India in e-governance, education, retail and consumer goods space. Other income during this quarter was Rs. 4.2 crore which includes income from mutual fund at Rs. 2.15 crore and recovery of old bad debts amounting to Rs. 1.41 crore. The company had net addition of 702 in manpower during this quarter. Total manpower at the end of this quarter is 7396 people. We improved our manpower productivity by 5% during the quarter as measured in terms of NVA per person month. During full year we had manpower addition of 1845.

Company had a very good year and a very good quarter in terms of cash flow. Company ended the year with Rs. 283 crore of cash and cash equivalent after incurring a capital expenditure of around Rs. 100 crore during the year and about Rs. 31 crore during the quarter. Out of this Rs. 283 crore, Rs. 226 crore has been invested in debt based mutual funds. We have been able to reduce our receivable days from 89 days to 85 days during the quarter.

So this was a brief snapshot of financial performance from my side and now I will request Mr. Ramanan to take you through some of the business initiatives that we have taken during the quarter and during the year and what are we planning for the company. Mr. Ramanan?

R. Ramanan Thanks J.K. and good afternoon to everybody. Thank you for joining this call. As J.K. has already shared with you the financial numbers, I will not repeat that, that it has been very satisfying for us to be able to register a growth both in revenue and profitability during this year by 24% and 28%. This is actually in line with what we have been working towards in the last 4-5 years. As we had a vision about 5 years ago; we entered into a phase of transformation, where we wanted to focus on the quality of business next. We wanted to focus on the private sector and we wanted to focus on the international market and we wanted to move away from low value adding equipment business and at that time we consciously took a hit on top line so that we are able to achieve a proper operational model within the organization focusing on the bottom line. Last year, as you are all are aware we actually grew revenues by about 24% but still we were focusing quality of business to ensure that our revenue and EBITDA and our margins as well as our PAT was growing. We also said that most of the correction phase was over and we would now be focusing on growth and it is quite heartening to share with you that we have been able to grow in the revenue and PAT in the current year. Also what is heartening to note is that all our SBUs have grown during this quarter, quarter-on-quarter and year-on-year. In America, a few years ago we were about $19 million and they were also coming very low in margins as the business there was not really pushing with the offshore capabilities in any major way. We have for the first time crossed $100 million at a time when international markets were passing through recession. We could manage global recession well, with CMC growing by 27% in the international markets and that has been very encouraging for us. We have also been able to improve our operational margins with very strong focus on operational efficiency, as well as our cash position.

We have grown in the Indian market as well in the American market. We also have expanded our focus to newer countries particularly Bangladesh, Sri Lanka and Africa which is basically attractive markets for us considering that we are a solutions company that increases our ability to penetrate into these markets in our existing solutions.

So with all of this we are reasonably happy with the performance of CMC. We achieved the growth that we have expected during this quarter. We would like to ensure that we continue to grow revenue but do not compromise on bottom line at the same time. We want to grow in line with the industry or better than the opportunities in the market. I am also happy to share we have significant initiative for tier 2 and tier 3 cities in India in the form of e-Pragati. So as I was saying all our SBUs grew and we are now expanding our focus in the SAARC countries as well as the Middle East Africa geographies. So overall it has been a very good year for the

company and in line with our strategies and achieving the growth in each of the SBUs that we have wanted to. So with that I am open to any questions.

Moderator Thank you, we can begin with the question and answer session. The first question is from the line of Sangam Iyer from Alpha Accurate Advisors. Please go ahead.

Sangam Iyer I want to get some more clarity on what is the kind of growth that you are looking at in the high margins segment system especially integration and ITES business? If you see in Q4 the growth kind of stranded as compared to nine months What is your outlook on that going forward considering that this year we saw very strong growth coming-in in both the segments. At least in the first nine months they were very strong and last quarter it was sort of slower as compared to the first nine months growth. So could you give us some outlook on that?

JK Gupta I wouldn't say that last quarter has been slower. If you look at our growth pattern that we have seen, we have almost similar kind of a growth pattern for Q4 as we have seen for the full year. When we see 24% growth on a full year basis for the company as a whole, most of this growth is coming from high margin businesses like Systems Integration has grown 23%, ITES has grown 54% and E&T has grown 28%. Both systems integration and ITES are operating at above 30% margin. E&T SBU is operating at about 21% margin. CS is predominately a domestic business and has also got a significant component of equipment business because of which their profitability is lower but our low profitable business is growing at a slower pace. So I think this whole focus on higher value added business and delivering better growth in higher value added business is uniformly reflected in full year and quarter. Now let me take through the quarter. CS SBU has grown 3%, SI and ITES have grown 9% on a Q-on-Q basis and E&T has grown 12%. So I think when you talk of the management focus and management perspective, we are clear that we want to grow more profitable business faster. And that is how we have been able to deliver improvement in profitability over the last four years and that focus is continuing to be there and we will continue in future also. Did I clarify or you have some more questions on that?

Moderator The next question is from the line of Vinay Kulkarni from HDFC Mutual Funds. Please go ahead.

Vinay Kulkarni One observation on my side is that in the past when you have shown very high growth in the higher margin businesses like systems integration and IT Enabled Services, we have seen a huge jump in margins especially at the gross level, for instance, Q4 FY10 and Q2 FY09 you had a huge jump in gross margin level. This time you had fairly good growth in Q4. I think 9% in systems integration and 8.9% in IT Enabled but it has not been accompanied by that sort of increase in margins. So could you throw some light on this?

JK Gupta I think, I shared in my initial remarks on the financial performance, that during this quarter we made some additional investments on sales and marketing. Our SG&A expenses in percentage points itself has gone up by about 20 basis points. In absolute terms these have gone up by almost Rs. 3 crore. In addition, we have added about 705 people during the quarter and you will see that in the last two quarters we have been aggressive in adding people. When we add people for some time they are not productive. Those kinds of reflections you had seen between Quarter 2 and Quarter 3 also. So that kind of a pattern is seen in Quarter 3 and Quarter 4 also. So there is always some kind of a lead and lag in terms of when you incur the cost and when you get the benefits. So I think one single quarter performance has to be seen in conjunction with a trend that we have seen over a period to read it better.

Vinay Kulkarni Right sir. So in terms of this manpower addition what sort of visibility do you see in the high margins services for FY 12?

JK Gupta Mr. Ramanan would you like to take this question?

R. Ramanan Like I had mentioned we have seen opportunities for growth both in India as well as in the international market. In India we are seeing an increased opportunity for spend infrastructure sector, in the e-governance area, in banking financial services and insurance where there are opportunities related to core insurance, modernization of many of the financial services institutions as well as in the rural and cooperate banking. We are also seeing opportunities in mobile technology and cloud computing-based services in India. We have been successful in penetrating the retail market in India particularly with fast growth of retail that is happening so there is an opportunity for us for roll out services as well as nationwide infrastructure management services. In the international market we see continued growth embedded in real-time systems and digitization and work flow management services, both of which are value adding, high-margin solutions and services and we have been looking at penetrating the SAARC countries and Middle East and Africa on high end solutions particularly replicating our core banking, core insurance, financial services, trading systems, depository solutions. Recently we won a large order from Nepal stock exchange for the depository in Nepal. We are already involved in depository solutions in Bangladesh and we see similar opportunities coming up in other markets.

Vinay Kulkarni Right sir. Could you throw some light on the Passport Sewa Project which was supposed to take off in FY12?

R. Ramanan The Passport Sewa Project is front ended by TCS and during this year there will be a rollout of the Passport Sewa Kendras so there will be an opportunity for CMC to participate in that in a much bigger way because the initial pilots activities for the last years have already been concluded and there will be a rollout during the remaining part of the year. So CMC is

involved in infrastructure management, infrastructure roll out as well as associated digitization services in the Passport Sewa. So we will continue our focus on that and work along with TCS. And further expansion of that is based on the government's intent how to expand that in the rest of the country.

Vinay Kulkarni There are some media reports on some delay, is it substantiated at the ground level?

R. Ramanan There have been some delays during the last year but I think it would be more appropriate to address this question of any knowledge of any further delay with TCS who are front-ending the deal. I think during this year the plan is to roll out in a very systematic manner so I do not see any major delays in the plan for the year.

Vinay Kulkarni Thank you very much and all the best.

Moderator Thank you. The next question is from the line of Nishit Shah from IDFC. Please go ahead.

Nishit Shah My first question is, why have you reduced the dividend payout ratio?

JK Gupta Nishit, you know that we have been maintaining the dividend payout between 20-25% and there is no particular ratio that we had in mind. You know that we have been planning significant amount of capital expenditure to complete SEZ facility. This year we spent about Rs. 100 crore on CAPEX. Next financial year we are planning a CAPEX of Rs. 246 crore. Fiscal 2013 also will have a CAPEX of more than Rs. 100 crore though we are yet to finalize the plan. So we have got significant requirement of funds for completing all these ongoing projects. What I feel is that this is going to lead this company to significant advantage in terms of future scale up of the business and the return on investment that we are getting on all these investments in SEZ are pretty high. So considering the requirement of CAPEX and all that we thought of doing a balancing between how much to distribute and how much to retain. There is no other objective behind this. I think we will continue to be fair in terms of distributing dividend.

Nishit Shah The next question is if you look at your last four quarter numbers to have been more or less in the range of about Rs. 28 to Rs. 30 earnings per share starting from Q1 FY11 till Q4 of FY11 and since sequentially you aren't seeing significant improvement as you move into Q1 of next year either there has to be a big jump up how you will start seeing a year-on-year- things flattening out. I also understand that there is a good jump in your IT Enabled Services last quarter but that has still not resulted in bottom line moving up because of investments that you have made in people as well as in marketing. What I want to know is the color on how you see the business ramping up and how you see the growth panning out over the next 12 to 18 months?

JK Gupta Nishit, I'll just make a quick comment on this before Mr. Ramanan talk about color on how things are going to work out. I just want to reiterate that what we said at the end of last financial year, is that we had all this margin expansions coming out of business transformation where we were changing rapidly the business mix and all that and we also commented that our phase of this transformation is over and all future growth in EPS or PAT will come from business growth. And this was a very well thought out step-by-step phasing out of how do we want to see this business building up and we are pretty happy to see that this year since we did not have any significant scope for further margin expansion we deliver growth in net profit through business growth. We achieved some slight increase in our margins also but I think more important is that we are back to growth and Nishit; this is the single largest increase in a top-line in absolute terms in any year that we have seen in the last 10 years. So I think we have bounced back very strongly after seeing declining top-line for four continuous years. And in future also we will continue to focus on growth. Of course, we want to deliver improvement in earnings per share. And ultimately in terms of how we are going to do that possibly Mr. Ramanan can throw some more light on that.

R. Ramanan Yeah J.K., I think you have answered the question pretty well. Our focus continues to remain on ensuring growth, at the same time maintaining our margins and we did tell last year that we would like to operate between the 16% to 18% margin as we embark on further growth and that is what we have tried to ensure even as we grew in revenues during this year we have ensured that our margins have not suffered. And also along with revenue growth comes associated anticipatory expenses that we have to keep now in context. When we were in the initial phases of expanding on our margins we were controlling costs, we were managing costs better, we were ensuring that we will not increase our expenses but get the maximum out of the existing base. Now we have started investing in the existing base because we have already reached a stage where we are 90% in solutions and services and we need to ensure that we invest in anticipation of some of the other growth that is coming. So this has I think been reflected in the Q4 numbers and I would not read too much into the specific number or the profitability being flat considering that we have had a 7% growth in revenue and in the business that we are in. You have always seen a slight lag in the solutions and services revenue versus the growth in top-line.

Nishit Shah On the tax rate Ramanan, you had an average tax rate of 15.1%. Do you expect the tax rate around this next year or do you expect to move over the MAT as you move forward?

R. Ramanan J.K. I think you should answer that.

JK Gupta Nishit, next year tax rate is going to have an implication of phasing out STP benefits because we have been executing all of our export business out of STP and this is how we have been able to reduce our average tax rate to 15% which is one of the best in the industry. But as STP

goes out and as we start executing all our new export businesses into SEZ, there is going to be a transition period because we cannot move any of our existing business from STP to SEZ. So during this period there is going to be an increase in average tax rates. So I think fiscal 2012 is the year when we will see maximum impact of this transition and by fiscal 2013 we will start coming back to our most effective tax planning or in the tax rates as we have got in fiscal 2011.

Nishit Shah But would you want to put a figure to average tax rate for FY12?

JK Gupta Average tax rate in FY12 could be in the range of around say, 25%.

Nishit Shah That will eat away lot of your PBT growth that you will see, isn't it?

JK Gupta No, this will not impact the PBT growth because PBT growth ……

Nishit Shah No, what I am saying is what translates into a PBT growth will be eaten away by the tax…

JK Gupta I think, Nishit that is common to the industry. We are not alone in this industry. Everybody is going to face a similar kind of a situation and we knew that this one year is going to be difficult in terms of tax management. But I think it's a pure transitionary phase because most of our contracts that are currently being executed in STP, none of those contracts have got a life of more than 12 months. So as those contracts phase out we will see returning back to the tax benefit situation. So I think we have to allow some time for this transition.

Nishit Shah And your Hyderabad facility, how much of it is being used by CMC and how much is leased out to TCS and how much is lease rentals?

JK Gupta Our current lease rentals are about Rs. 3.1 crore per quarter and that is basically for Phase 1. Phase 2 is going to become operational from this month. I think next week we are going to commission our Phase 2. There are two ODCs in Phase 2, one ODC is going to be used by CMC and a part is going to be used by TCS and another ODC is going be used by TCS. So there is definitely going to be an increase in rentals from TCS in the next financial year. We are expecting this rental to go up from current about say Rs. 12 crore per year to around Rs. 25 crore per year, or so. We will have phase 3 for which the construction is going to start sometime in June-July. Then this tax benefit will continue because the SEZ developer tax benefit that we have availed this year also, next year this should increase. So this is not getting phased out.

Nishit Shah Okay. So would you say that FY13 you should be back to 15% to 16% tax rate which you had?

JK Gupta Yeah actually my feeling is, if not the 1st Quarter, by the middle of FY13 we should be back to our current tax structures or current tax implications. By that time everything would have been transitioned.

Nishit Shah Okay. Thank you very much. This is useful. And I think your board is echoing the confidence by announcing the 1 to 1.

JK Gupta Yeah thanks a lot Nishit. Thanks for your feedback and comments.

Moderator Thank you. The next question is from the line of Shikha Jalan from Smith Securities. Please go ahead.

Shikha Jalan My question is regarding the growth we see in terms of top-line for FY12?

JK Gupta Shikha, we really do not give any guidance on the numbers but I think in terms of direction as Mr. Ramanan explained a little while ago that what kind of focus we have got and the only comment we can make is that we are seeing good traction in the market. I think the market conditions are pretty good.

Shikha Jalan Okay. Sir in terms of pricing growth or volume growth how will the growth be? Are we seeing any pricing growth going forward or it will purely be a volume growth?

JK Gupta It will be mostly based on volume growth. There could be some implication of pricing growth also but largely we are depending on volume growth.

Shikha Jalan And going forward, the outsourcing contracts are expiring in US and all, around $20 billion contracts are expiring. So are we eyeing those contracts?

JK Gupta Shikha, one thing that we can see through is that as CMC America has grown in size from about $19 million five years ago, to $102 million in fiscal 2011, and with that kind of a visibility being created in America with a stronger balance sheet in America, I feel that we have got a stronger stake or stronger claim in trying to get bigger deals in America. So that is the only comment I can make. So definitely we are better positioned now as compared to where we were four years ago in America. We will be eyeing some of those deals which are expiring and are available in the marketplace to take.

Shikha Jalan Okay. Sir your take on general discretionary spend which is in U.S. or Europe let us say, what is your take on that?

JK Gupta Mr. Ramanan would you like to answer this about discretionary spending in the U.S.?

R. Ramanan In terms of our opportunities in Americas we continue to see increased opportunities in embedded and real time systems which have grown very well over the last several years and continue to grow during the last year. We are seeing increased opportunities for digitization and work flow management services. We have been able to enhance our presence in the SI SBU in the Americas. We have also set up ODCs for some of our customers where we had initially entered into digitization and IPS set of work but subsequently we have graduated to software development and even products enhancement sort of work. So we continue to proceed along these lines. We have also set up the first on-sight delivery centre in the United States. It's a 100 seater now located at Austin and that is enabling us to provide near shore delivery capabilities which when combined with offshore delivery capabilities enhances the value proposition for our customers. In Europe we see opportunities in embedded and real time systems and also in the U.K. we see opportunities in the market because U.K. government has been pretty favorably disposed towards outsourcing. And CMC is with a strong presence in the Government in India and many solutions that we have developed had an opportunity in those areas. In the Middle East and Africa and in the SAARC countries we are looking at replicating CMC's solutions as we have done in India in these markets.

Shikha Jalan Okay. And sir your sense on currency movements, are we seeing any Rupee appreciation going forward, or what is our average rate going forward?

JK Gupta Shikha, we have factored-in an average rate of around 45 for the business plan for the next financial year. Currently after the end of this financial year, lately it came down to a level of around Rs. 44.13, luckily it is back to around 44.65 today because of certain weaknesses in Europe and all that. So we are very closely monitoring what is going to happen to Rupee-Dollar. As of now we are not seeing any significant volatile movement on that but we are very closely watching. We will try to achieve an average rate of 45 as we have done in the business plans. Just to give you a sense of its implication on us. A one rupee movement in dollar-rupee rates affects our bottom line by almost a crore. I am just giving you a very simple equation, how does it translate into. I think, it is not very significant in terms of our exposure to currency movement. Possibly we can neutralize some of that through volume growth and all that. So right now we are focusing more on growing the business.

Shikha Jalan Okay sir and we saw a very good increase in SG&A in Q4, almost 20% there and some expenses on wages and manpower as well. Do we see this trend going forward also for FY12 or this coming quarter?

JK Gupta Shikha, what happens that, when you are in the growth phase, some of these investments are always required for benefits that you are able to do because manpower is not something which is like inventing just-in-time, pick people and then you execute the projects. In any growth phase this kind of lead-lag relationship will be there and as Mr. Ramanan also explained, that

in last four years we had been focusing on more of business transformation which really did not require too much of investment. Now since we have returned back to the growth, we need to make investments into marketing. But when we look at our investments in SG&A it is not very much off or very much out of our business growth, though in absolute terms our SG&A expenses have gone up by almost Rs. 3 crore in this quarter but when we talk on a percentage terms, this has gone up only 20 basis points and I think we have to make all this kind of investments for future growth.

Shikha Jalan Actually sir, what I meant to ask was, when are we seeing the expenses leveraging out for us, the benefits coming in our book?

JK Gupta Normally this lead-lag is between one to two quarters, so whenever we make such investments, we start getting benefits in the next quarter and some of the benefits come in the quarter after next. We don't have significant gap between these costs and benefits being reaped.

Shikha Jalan Sir, our overall will be same as FY 11 or for that matter it will not dampen our margins going forward much?

JK Gupta That's what our efforts are going to be that we put at our margins and grow and deliver profit growth through volume growths. So our efforts are going to be in that direction.

Shikha Jalan Okay, thanks a lot sir, that is from my side and all the best for the future.

Moderator Thank you. The next question is from the line of HR Gala from Qwest Investment, please go ahead.

HR Gala Just a couple of observations, we did miss out a lot from Mr. R. Ramanan initial remarks, so Mr. Ramanan, you have given a broad macro picture for our company as to what is likely to happen but if you talk specifically about the type of assignments that we get, how do we differentiate our say TCS-CMC combine in accepting different kind of international business as compared to maybe some other software projects, which can give us a visibility for the longer duration than maybe next one or two years. Can you throw some light on that sir?

R. Ramanan Yeah, there is a clear differentiation that TCS-CMC together brings to the market place as compared to many of the others, because CMC brings three very complimentary capabilities to TCS. One is, on the infrastructure management from end-to-end prospective, as TCS is also involved in infrastructure services as a remote infrastructure management just like many other IT companies are. But when you go for significant large turnkey projects, as you are going in India which has a combination of software, Pan India support, infrastructure enablement,

maintenance rollout, CMC's proven experience in this is a great value add to TCS and provide the unique differentiation in the market.

The second is in the international market CMC brings value to TCS both in its existing customer base as well as new customers in the embedded and real time system. They have large engineering customer base, they have hi-tech as a very large unit. Both of these are natural recipients of CMC's services in embedded and real time system and therefore, this is a complimentary thing that we bring to the table.

Third area is digitalization and workflow management, because the TCS is in the full-service space and in the full-service space of course they have built a number of competencies but the digitalization of workflow management services so CMC still plays a very important role within the TCS full-service play. And many existing customers of TCS, they have been doing these operations internally among themselves but now they are looking at, can we leverage TCS and CMC for that matter in being able to tap this.

The fourth area that we bring synergy value is in the products that we have developed and some of these products and some of these solutions are applicable globally. For example our Ports and Cargo solution is very strong and it is among the top three in the world. The solution that we have developed in insurance again helped TCS in the emerging economies market, so that can be positioned there. The e-governance solution, some of the e-governance solution that we have developed including biometric and identity management are again strong assets that TCS can leverage.

So we together are able to synergize very effectively and leverage these capabilities both in India as well as in international markets. On a standalone basis, CMC addresses the same segment but for client base which is not being addressed by TCS and since the global opportunities are very large, even in a country like United States the number of companies which can be addressed. So we have a well-defined process within the company to see which are the opportunities that CMC will go directly and which are the ones that are best done by a combination of TCS-CMC.

HR Gala So sir, currently out of our total revenue of a thousand odd crore, how much would be to the joint efforts of TCS-CMC and how much would be on our own?

JK Gupta Yes, about 47-48% is such joint opportunities and remaining is our own.

HR Gala Sir, recently a newspaper carried an interesting article of Mr. Ramdorai wherein he said that CMC, Tata Elxsi, CRL, and Tata Technology are each a TCS in the making in their respective sectors. Can you just specify, what kind of agenda has been carved out for CMC within the

Tata Group technology companies and how do we go beyond, say certain areas and competencies that we have already developed?

R. Ramanan Yeah, I think the area that CMC occupies within the Tata Group is that of a system engineering and integration company. So that is the space that we want to be in and that is the space that we have excel that and we have a track record. Now what does this imply. It implies from our perspective four areas in which CMC continues to grow its efficiencies in and its capabilities in. One is infrastructure systems integration, because when you are putting together end-to-end solutions, how do you connect the various pieces, it may be cloud computing, it may be data servers, it may be virtualization, it may be setting up green data centers, it could be connecting the communication and the hardware capacity and planning for that and so on and so forth. This is all falling under infrastructure systems engineering and integration.

The second is how do we put together the solutions and here it is a combination of both applications solutions as well as products that we had developed. There are certain products which CMC has developed because it has R&D capabilities, does R&D investments and we will continue to grow those products and grow those specific solutions but at the same time how do we integrate it with other third party solutions because today if you take, let us say core insurance, core insurance is no longer just, we have Genesis which is a excellent product, which is having more than 80% of the market shares. But when you are going for core insurance, the insurance client is saying can you integrate it with the HRM solutions, with the financial management solutions, with a CRM solution and so on. So we need to bring that capability in addition to Genesis and that becomes a unique differentiator that we are able to provide a core product and surrounding it all the integrations.

The third part is the digitization and the workflow systems integration. Now here, you are looking at not just this classical BPO, classical BPO is what many companies are doing, what we are looking at what is the automation, what is the productivity improvement, and what are the tools? We have developed our own tools called CMC DOS which can reduce the efforts in the workflow systems integration substantially and thereby give major benefits to the customers, so it is an automation driven, asset driven service. So you have a service component but that service becomes meaningless or it becomes low-margins when we just provide it as a service. Where as if we integrate it with tools and automation that we have developed then it becomes a profitable high-margin service and improves the productivity and provides the differentiation.

The fourth area which we have been looking at is real-time and embedded system integration, which you already know. And today we have education and training as an SBU. We see training itself as a unique opportunity in India especially with the emphasis now for skill

development and all of that but the larger vision that we have is we want to become a knowledge systems integration company. So we are moving towards that direction, we are not there yet but what does knowledge system integration implies for us, it implies as we put together the end-to-end learning systems training and content management capability together. Now we have done all of this individually, for example the UID project is an example of creating training content for the UID project. But when we enhanced this capability to give training at the other end but in the front we are able to create the learning systems and the knowledge management systems ahead of it then it becomes a much more powerful service than just providing training as a separate service. So this is our growth path and this is a unique space which we are trying to expand and this has huge opportunities in India and internationally and so our aspirations are to become one of the top 20 organizations in the world and that.

HR Gala Sir, just a last question from my side. With all these initiatives which you have described, where do you see CMC five years down the line?

R. Ramanan The five years down the line, we hope we will see a CMC that is living up to our board and chairman's dreams.

HR Gala Okay. Could we grow more than two times, maybe three times?

R. Ramanan See, I do not want to give any forward guidance but we have gained a certain momentum. We are going at 24% today, last year we have grown. We would like to maintain that momentum, we would like to increase that momentum and at the minimum we want to make sure that we are growing at industry standards, better than the industry standards. Of course, we could accelerate that through some of the initiatives because the business that we are in provides us that opportunity to accelerate at a faster rate but we would be at a minimum want to meet the sort of industry growth.

Moderator Thank you. The next question is from the line of Apoorva Oza from Standard Chartered Securities. Please go ahead.

Apoorva Oza Sir, if I may just ask for a couple of data points, one was in terms of your staff people if I can just know what could be the break up between regular and contracts?

JK Gupta As of 31st of March, total manpower strength was 7396, out of which regular employees of 4103 and the contract employees were 3293.

Apoorva Oza In terms of the overseas living expenses, what would that number be?

JK Gupta Overseas living expenses during this quarter was Rs. 2.16 crore.

Apoorva Oza If I look at your EBIDTA margin, from a peak of 22.4% in fourth quarter of FY10, that number has come down to about 17.7%. Now you are mentioning a margin of16% to 18%, in line of the fact that our America's business is growing and we are becoming more susceptible to the currency fluctuation. How do you think you would be managing the margin at the current levels given the currency and the wages?

JK Gupta What we are expecting is that as we grow in volumes, it provides us certain amount of leverage on cost of operation though we have made certain investments in SG&A but in terms of percentage of overall revenue or SG&A has been very much moderated with a slight increase of only 20 basis points in this quarter. I think this margin potential and expansion, whatever you are talking about will come through the volume play.

Apoorva Oza Right sir, and 16% to 18% level that you spoke was that at the EBIDTA level or EBIT level?

R. Ramanan EBIDTA level.

Apoorva Oza Okay sir. The other thing was in terms of the revenue growths, especially for lines like ITES and Education and Training, do you still expect it to be lumpy or do you think the growth trajectory going forward will be more stable?

JK Gupta Actually we are getting into more contracts on a longer-term basis to reduce the lumpiness and this benefit we have seen over few quarters. I think more and more growth in both ITES and E&T is going to be normalized.

Apoorva Oza Right sir. Also in terms of our equipment sales, how do you see that going forward?

JK Gupta If you see this financial year, we have caped our equipment sales to the last year's level. Last year we had equipment sales of Rs.103 crore and this year also we have Rs.103 crore. As we have been mentioning, we get into equipment only when it is a part of an overall turnkey project where there is an associated services portion of the business also so. We have delivered all the growth of 24% that we have seen in this year is from services. We feel that going forward also we will continue to see the majority of the growth delivered by services. There could be some variation in equipment as may be necessary to execute some of those services transaction but not very significant and our focus is continued to be on services.

Apoorva Oza Thanks sir. That is it from my side.

Moderator Thank you. The next question is from the line of Nirav Dalal from Almond Global, please go ahead.

Nirav Dalal Thanks for taking my question. Sir, if I see the performance of the past few quarters, your margins have been declining despite international business taking a larger share of the overall revenues. I understand that you have done investments in SG&A but when can we see a reversal in margins with international business doing well?

JK Gupta No, if you see quarter-on-quarter there could be a certain variations in quarter, may be sometimes in future also, given the nature of our business. Let us take quarter 4, in quarter 4 our share of equipment business slightly gone up from 10.5% to 11.2%. Similarly share of international revenue is slightly down from 54.7% to 53.6%. These are very small variations, but do have some implications for the percentage margins but not very significant. So I think we have to see a bit longer-term to see whether we have got the right kind of trajectory and whether we are firm in terms of what business strategy we have got in place. So I think one or two quarters only, quarter-on-quarter basis may not tell the complete story.

Nirav Dalal Okay and what is our hiring plan for FY12 and are looking at hiring more contract staff because this quarter subcontracting cost has gone up, we have hired quite a few temporary staff. So what is the hiring plan?

JK Gupta Nirav, we have been sharing with all of you that we will continue to create a mix of regular, contract and vendor contract people depending on the nature of deals that we are getting. Whatever deals which are having with no certainty of a repeat nature, we do not want to increase our fixed cost and get into a long-term cost commitment. In terms of cost management our efforts have always been to create cost structure as variable as possible so that we can very effectively take care of quarter-on-quarter and year-on-year variations between various segments of businesses. So very difficult for that matter to put a number that how much of regular and how much of subcontract and how much of vendor contract people are going to be there in the system. That is definitely going to be dictated by the requirement of new deals that we are getting. But as we have been going mostly in the services side, the future growth of business will require more hiring to take place as you have seen in this financial year as well.

Nirav Dalal Okay, so that can be taken on the regular employee front?

JK Gupta I think we have to put everything into a pool. We have to look at the aggregate number, instead of seeing a breakdown between regular and contract.

Nirav Dalal Okay. Can you tell me the current number of clients that the company has?

JK Gupta Current active clients will be about 850.

Nirav Dalal And between domestic and international, what will be the mix?

JK Gupta I do not have a ready number right now. Our international clients would be about around 150, out of this.

Nirav Dalal Okay fine. And predominantly they will be in US?

JK Gupta Yes, US, since that gives us the largest chunk of revenue, they have got largest number of clients also.

Nirav Dalal Okay fine. Thanks a lot.

Moderator Thank you. The next question is from the line of Srinivas Sheshadri from RBS, please go ahead.

Srinivas Sheshadri My first question is relating to the salary hikes which typically get paid out in the first quarter. Just wanted to get some sense on what you are planning for this year and what kind of impact it will have on the financials?

JK Gupta Mr. Sheshadri, in our case we normally provide salary hike in the second quarter and we are still working it out how much of increase is going to be given.

Srinivas Sheshadri Okay, any preliminary sense in terms of how much it could be, because I think, generally the consensus is that it will be maybe around 10 to 12% for the industry.

JK Gupta We will not be outside the industry, I think like last year we granted increase of 9% which was also in line with what the industry gave. So this year by the time we take our decision, we will have lot more information available with us to take a final view.

Srinivas Sheshadri Right and the margins for the next year there has obviously been a bit of a slippage through the year in FY11. So when we are comparing from an expectation perspective, is the overall FY11 margins a good indicator of where it could end up next year or should we look at the exit margin which is a little lower than the average?

JK Gupta My feel is that a one single quarter number cannot be extrapolated. We have to see about longer-term average numbers and my feel is that full year number is something which is a better basis.

Srinivas Sheshadri And we hope to maintain the margins or do you see any kind of significant pressure which can get built on…..

JK Gupta Our focus is going to be delivering the growth and deliver the profit expansion through growth. So as we told that last four years we have been focusing on expanding margins, now we are focusing on expanding the absolute numbers. So that is what is going to be the focus.

Srinivas Sheshadri So it will be more top line led profitable growth rather than margins change here or there?

JK Gupta Yes.

Srinivas Sheshadri Finally wanted a small data point, in terms of the living expenses for overseas contractors in this point of time?

JK Gupta I think I just gave that. Living expense in this quarter is Rs. 2.16 crore; if you want to see it for the year as a whole we had Rs. 8.48 crore.

Srinivas Sheshadri Thank you. That is it all from my side.

Moderator The next question is from the line of Priya Rohira from Enam Securities. Please go ahead.

Sujit This is Sujit asking on behalf of Priya. Just a couple of questions, just in term of the average deal sizes overall can you give some color on the average deal sizes and specifically you closed a few deals in the e-governance space in the current quarter? It would be great if you could also give some color on the average deal sizes in the e-governance space?

R. Ramanan The deal sizes actually have quite a range, some of them are at least a couple of crore but there are others which are of the order of Rs.50-100 crore. So it depends upon the specific opportunity, if it is a large opportunity at a state level than the deal sizes typically in the 5 to 10 plus range. If it is for the private sector then we typically enter into relationship with the multi-crore type of deal but then significantly it expands because the stickiness there is much higher. So our entry points would be lower.

Sujit This is for the e-governance space?

R. Ramanan No not e-governance, I'm talking in general the deal sizes. In the e-governance space it is always typically Rs. 5-10 crore plus type of deal but some of the deals can be pretty large.

Sujit In the last quarter you mentioned the company has got a long-term target to increase the share of exports in the customer services business. What would be the share of exports in the customer service business for the current quarter?

R. Ramanan During the last year we were interested more in consolidating our customer service business in the domestic market. This year we will see an increased thrust and a special thrust in the international segment, so while we did have some international revenues for the quarter, I think the real thrust will come during the coming year.

JK Gupta Just to give the data point for this year, we had 15% of the CS revenues coming out of international.

Sujit If I am not wrong, the long-term target here is to bring it to around 50% over a long-term?

JK Gupta In the CS business? What we said is that we had set a target of 50% overall international revenues for the company. So we definitely found systems integration and ITES is a bigger driver of international business presence, possibly CS and E&T has a lesser ones. And we feel that given the momentum that we have built up and visibility which we have built up for SI and ITES that is going to be our key to drive our international business in the medium term.

Sujit I just wanting to confirm whether I have picked it right, you mentioned you are targeting an EBIDTA margin in the range of around 16 to 18%?

JK Gupta Yes.

Sujit Thanks. That is it from my side.

Moderator Thank you. The next question is from the line of Jigar Walia from OHM Group. Please go ahead.

Jayesh Hi this is Jayesh from the OHM Group. We recall that in the last conference call you talked about a tax rate of around 19%, you seem to be indicating 25%, is my understanding correct?

JK Gupta Yes, we are expecting next year to be around 25%. One of the reasons is that our SEZ facility is going to become operational this month. We have just worked out how we are going to ramp up our SEZ utilization. It is going to be around 25%.

Jayesh On a full-year basis in 2012, you still think you will be able to hold the margins?

JK Gupta At the operating level yes.

Jayesh Thanks.

Moderator Thank you. The next question is from the line of Sanjeeth Hota from ShareKhan. Please go ahead.

Sanjeeth Hota Sir I wanted a data point what is the government contribution as a revenues?

JK Gupta Almost 1/3.

Sanjeev If you could share the revenues you are getting from the solution business?

JK Gupta For this financial year we have got our total systems integration revenue of Rs. 577 crore. Out of this Rs. 577 crore, this consists of Rs. 160 cores of the embedded systems. My feel is that embedded systems is having solutions also, I do not have an exact breakdown, of what is the solutions business and services business in there, I think it is mostly solutions. And out of the remaining figure of Rs. 417 crore that we have, services in this will be about Rs. 180 crore and the remaining will be solutions.

Sanjeev Could you share the attrition numbers during the quarter or last 12 months?

JK Gupta Our attrition is about 25%.

Sanjeev And the last question is, little bit about some of the deal pipelines you have seen in the domestic as well as in the overseas markets?

JK Gupta Very difficult to put a number on deal, but what we can say is that we have consistently seen an improvement over the last four quarters and we're definitely better placed this year compared to the same point in time last year in terms of deal pipelines.

Sanjeev Have a great year ahead. Thank you.

Moderator The next question is from the line of Sandeep Agarwal from Antiques Stock Broking. Please go ahead.

Sandeep Agarwal Just a few questions, where do you see the utilization level excluding trainees going forward. Second is on attrition, where do you see the rate to come and what is your new recruitment guidance form the next year?

JK Gupta Our utilization level is about 79% and so far as attrition is concerned, I think again it is difficult to put a number because it is very complex pull and push of various factors, how the industry is growing and how the wages are working out in the industry and all that. So we'll see how the thing works out but definitely would like to bring down the attrition numbers from the current level. So that is the only thing that we will say that we are taking certain measures to bring down the attrition levels from the current levels.

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Sandeep Agarwal What is the current level?

JK Gupta 25%.

Sandeep Agarwal Last question was on addition guidance?

JK Gupta I think we did not put a number but we did give you a kind of a color on how we are going to work it out. Since most of the growth that is coming in the company is on the services side which requires deployment of people, like last year we grew 24% overall revenue, which all came out of the services and services grew almost 27%, so most of that required an addition of people. Going forward also when we see growth coming out of the services, this will require a similar kind of addition of people.

Sandeep Agarwal Thank you.

Moderator Thank you. I would now like to hand the floor over to Mr. Ashish Aggarwal for closing comments.

Ashish Aggarwal I would like to thank the management for spending their valuable time for the call as well as giving us an opportunity to host the call. I would also like to thank the participants for attending the call. Thanks a lot.

R. Ramanan Thank you very much.

JK Gupta Thank you.

Moderator Thank you. On behalf of Tata Securities that concludes this conference. Thank you for joining us, you may now disconnect your lines.

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