

Transcript

Earnings Conference Call of CMC Limited – Q3 (FY 13)

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

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Moderator

Ladies and gentlemen, good day and welcome to the CMC Limited Q3FY13 earnings conference call hosted by Tata Securities Limited. As a reminder for the duration of this 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 this 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 now like to hand over the conference to Mr. Ashish Aggarwal, thank you and over to you sir.

Ashish Aggarwal

I on behalf of Tata Securities, I welcome you all to CMC Limited Q3FY13 results conference call. From the management, we have Mr. Ramanan, MD and CEO, and Mr. J. K. Gupta, CFO. Before handing over the call to the management, I would like to thank the management for giving us an opportunity to host the call. Now I would like to hand over the call to Mr. Gupta.

J. K. Gupta

Thanks a lot Ashish and a very warm welcome to all the participants in this call to discuss Q3 results of CMC that were approved by the board today afternoon. These results have been available on the company website and I am sure all the participants had an opportunity to go through the results. Q3 results of the company continue to reflect the company's focus on growth with profitability. Company earned consolidated operating revenue of Rs. 492.69 crore in Quarter 3, which is an increase of 8% Q on Q and 24% YOY.

Services revenue grew 7% Q on Q and 32% YOY to Rs. 464.59 crore and the share of services revenue in total revenue from sales of services was 94.3% this quarter compared to 94.8% in the last quarter and 88.9% in Q3 of last year. International revenue grew 11% Q on Q and 38% YOY to Rs. 336.62 crore. International revenue share in total revenue from sales and services improved further to 68.3% from 66.4% in the last quarter and 61.5% in Q3 of the last year. America continues to drive growth in the international business. American subsidiary of the company i.e. CMC America Inc. grew 14% Q on Q and 36% YOY in dollar terms and the share of America geography in overall operating revenue increased to 60% during this quarter. Company earned consolidated operating profit i.e. EBITDA of Rs. 82.88 crore in Q3, which is an increase of 9% Q on Q and 38% YOY giving us improved margin of 16.8% compared to 16.6% in the last quarter and 15.2% in Q3 of last year. We had very good performance on Tax front. Company earned consolidated profit after tax of Rs. 61.06 crore, which is an increase of 24% Q on Q and 48% YOY. PAT margin also improved to 12.3% from 10.7% in the last quarter and 10.3% in Q3 of last year. We were able to bring down our average effective tax rate to 23.7% compared to 25.3% last quarter excluding the tax from dividend distribution by CMC America. Income from other sources was Rs. 2.56 crore compared to Rs. 1.53 crore in Q2, which includes Rs. Rs. 1.94 crore as earning from investment in mutual funds. Company continued to see good traction in the market place. It added 26 clients during the quarter, which includes 4 clients in Americas, 2 clients in MEA and APAC region and 20 clients in India. Company has net manpower addition of 473 in this quarter taking the total manpower count to 11224 at the end of the quarter. We had very good performance in cash flow front also. We ended the quarter with cash and cash surplus of Rs. 218 crore after incurring capital expenditure of Rs. 22 crore during the quarter. Our investment in mutual funds at the end of the quarter was Rs. 113 crore. Company was able to improve our receivable days further from 83 days to 81 days during this quarter. So if you look, this is the third successive quarter of excellent performance from the Company. If you look at our cumulative performance for first 9 month in this year, our operating revenue grew 33% to Rs. 1403 crore. Service revenue growth was 39% to Rs. 1310 crore. International business growth is 48% to Rs. 935 crore. EBITDA growth is 44% to Rs. 234

crore giving us an EBITDA margin expansion of 131 basis points to 16.7% in first 9 months. Profit after tax grew 55% to Rs. 168.89 crore giving us a PAT margin expansion of 178 basis points to 11.95% at the end of first 9 months. We were able to reduce our effective tax rates to around 26% from 32% that we had last year very much in line with our plans of scaling up business operations from SEZ giving us very critical tax advantage. So this was the snapshot of financial performance that we had during this quarter and with this I am handing over to Mr. Ramanan to take you through some of our business initiative and the market outlook that we have got.

R. Ramanan

I think JK has very comprehensively covered the numbers. The key thing has been for us that our growth momentum has continued through this quarter and has in a way increased in this quarter because it is reflected in the numbers in terms of an 8% growth quarter on quarter and 24% growth YOY. We have been focusing on the international market as all of you know did very well with 11% growth quarter on quarter and CMC America did 14% and overall our international grew by 11% quarter on quarter. We continued to see good traction in the key areas of system integration solution embedded in real time systems, digitization services. We added 26 clients during this quarter totally both in the domestic and international market out of which we saw growth and new client acquisitions in all the SBUs that we have. Customer services in India, Embedded & Real time systems in the America and SI solutions in the Middle East Africa and also in India. We continue to focus on emerging areas now which are emerging trends related to big data and analytics, mobility management and integration and cloud related services, so these have been finding expression in some of the new wins that we have done in the US. Also our products solution base continues to get enhanced through addition to the technology in all of these segments. We continue to see some improvement in productivity and operational efficiency through various initiatives that we have launched in the company and those initiatives have also enabled us to win several recognitions in the market place. In particular, I would like to draw attention to the fact that we won HR excellence award, Women leadership awards, innovation awards and other awards for solutions that we have deployed in the market place like the intelligent transport system that we implemented in Karnataka, which is the

first of its kind with more than 500 buses using state-of-the-art, GPS based command and control system. For a large mine in the state of Goa we had implemented and integrated mining management and control system, which again is the first of its kind in the country. So these innovations are replicable in nature and would help us drive to further opportunities and growth during the coming quarters. So with that I will be very happy to respond to any questions that you have or any clarifications that you may seek.

Moderator

We will now begin with the question and answer session. Our first question is from the line Priya Rohira from Axis Capital, please go ahead.

Priya Rohira

I have a couple of questions. One will be first on the overall revenue visibility which we see from the ITES and systems integration business, the second thing is if you could just walk in through the subcontracting expenses increase on the overseas employees, how do we see this going down with off shoring coming in over the next few quarters?

J. K. Gupta

First thing on segmentation, if you look at our systems integration revenue grew 12% quarter on quarter and ITES grew 4% quarter on quarter in this quarter, and if you look at 9 months period, these are the two business segments where bulk of the growth has come. SI has grown 43% on a 9-month basis and ITES has grown 49% on a 9-month basis. It is very much in line with whatever we have discussed over the previous investor calls also. These are the two business segments which are more profitable in terms of our business portfolio and put together they account for almost 80% of our business. If you look at margins also in this quarter, all the margin improvement also has come out of these two business segments where SI margin improved from 19% to 21% and IT enabled services improved from 27% to 31%. So, I think in terms of business portfolio, it is very much in line with our company strategy to increase our business share of more profitable businesses. When you talk of subcontracting cost, we had told that the shift from on site to off shore may take place only from first quarter of next financial year. So far as current quarter, last quarter that is quarter 3 have gone by, we have not seen that shift taking place, so we have continued the way we were doing in the previous quarter. This is the reason you are not

able to see any significant change in the pattern of subcontracting, but if you look at subcontracting and employee cost put together, it continues to form a pattern and we still have been able to improve our margins by 20 basis points. I think given the current environment, I think protecting and improving margin while maintaining the growth, I think is very important.

Priya Rohira

This is what means that we are yet at 24 to 25% of off shore share in our international business?

J. K. Gupta

Absolutely, in fact in this quarter it is about 23%.

Priya Rohira

Just one more thing on the visibility, when you say in ITES and the system integration business, and the new client wins, I am sure that would have been a material contribution, so can you just explain some quantitative

J. K. Gupta

Actually most of the new client win it is reflected in SI business segment. In ITES we have got wins, but some of the contract would have ended also and this is why they reflected in 4% growth in IT enabled services. Large portion of ITES, the existing work that we are executing in America, which is still substantial and the passport project which have gone through a ramp up phase over the last three or four quarters, which contribute significantly to IT enabled services business.

Priya Rohira

And where are we in terms of passport project right now, I mean in terms of FY 14?

J. K. Gupta

Passport project is now fully rolled out, it is in the stable phase, so we are not seeing an immediate further ramp up in passport because currently it is stabilized at all the 77 passport offices that have rolled out. Now the ramp up will happen based on volume growth. Means, if more number of passports are received to be issued in the offices, may be, we have to deploy more people or maybe we have to expand. Unless that happens, I think for sometime we are not banking on passport project to deliver growth in this business.

Priya Rohira

Last time you had shared that around 6.6 crore passport are the potential to be issued and we were at around 1.6, if I could have an update over that?

- J. K. Gupta** What we said is that the government say that there are 6.5 crore passport and 1.6 crore passports are issued year or renewed every year. Now what we were expecting is that as people start getting user experience and they find that getting passport is far more pleasant experience now, we expect more and more people to come in to the passport Kendra's and get passport issued. And this is where the volume growth we expect will take place. I think it is too early to really call what kind of growth will happen, but all of us are sure that the growth will reflect.
- Priya Rohira** The second question was no contribution as yet from UID, right?
- J. K. Gupta** No contribution from UID and we don't have any clear visibility on when and how this contribution is going to arise.
- Priya Rohira** What would be the share of TCS in the current quarter?
- J. K. Gupta** This quarter is 58%.
- Priya Rohira** If you could also share on CAPEX front because is we a little pushed back in terms of moving more towards FY14?
- J. K. Gupta** You are right. If we look at our CAPEX this quarter has been Rs. 22 crore. So on a cumulative basis it is about Rs. 67 crore. So it is slightly behind schedule, so some of the CAPEX will get postponed to the next financial year.
- Priya Rohira** FY13 and FY14 would it be possible for you to share?
- J. K. Gupta** We are still into the planning stage, so all the projects are going to be reviewed. You know that SEZ project, which is a major project; you can say that project is under a kind of time limit. We have to complete the project between June to September 2014, so I think there could be some bunching of CAPEX taking place later on. Overall timeframe to complete the project has not been extended. Still if we say next 18 months the total CAPEX will take place.
- Priya Rohira** For the tax assumption, what would be the tax for FY14?

- J. K. Gupta** If we look at our first 9 months tax, it is 25.8%, but this quarter has been 23.7%, so this is launching us to a very comfortable tax position for the next financial year. So if you talk of fiscal 14, I think we are very much on track to reduce it to around 22% and as by fiscal 15 we should it coming below 20% also.
- Priya Rohira** Just a last question, maybe I will then come for repeat. In that 11000 odd people, 11224, how much subcontractor?
- J. K. Gupta** Our contract employees are 6481 and regular are 4743.
- Moderator** We are going to take our next question from the line of Vinay Kulkarni from HDFC mutual fund, please go ahead.
- Vinay Kulkarni** I have a question regarding SEZ quarterly revenue seem to have dipped slightly, can you please explain this?
- J. K. Gupta** Basically you know that there is an accounting standard now on lease equalization accounting. So what happens, when some additional facility get commissioned, certain equalization amount is computed from the original period, so it is bunching of that equalization amount getting booked. In the next period, you book only for that period, so it is basically regarded as accounting issue.
- Vinay Kulkarni** And margins also seem to have gone down?
- J. K. Gupta** Basically depreciation that goes in. Margins went down because in last quarter we had bunching of revenue taking place there. This quarter it was not there, but there is no other element of cost.
- Vinay Kulkarni** I have more general questions on these three focus areas big data analytics, cloud, could you just elaborate more on what sort of internal work we are doing, what sort of projects we are working on and what percentage of revenues come from these three or four focus areas?
- R. Ramanan** In the area of cloud mobility, big data and analytics and intelligent enterprise systems, we are very focused on two segments of the market place, one is the

products and solutions that we have as a part of our SI solutions and so whatever are the cloud related extensions or the mobility related extensions, app related, software related to our products like insurance and so on, or the surveillance security system that need to be get integrated or the big data analytics this is forming one part of our innovation strategy and the second part is offering services on OEM related tools and technologies which are being used for cloud migration or mobility integration or big data analytics. For example, the vendors like EMP and Oracle and others have come up with their own extensions for integration into core platform, which are built using their products, so we are providing services, SI services on these getting the expertise on the particular platform and making sure that we can integrate it into the solution and services that are required. The third part is creating new solutions for the SME market. The small and medium enterprises which could be cloud related solutions, for example in Genesys we are creating a version of Genesys for Genesys Cloud and Genesys mobile and Genesys Analytics, which will be for the SME market. So this is our three prone strategy that we are having. We have put it all in the CMC 3.0 initiative which is forming the core framework under which we will be dealing with the emerging technologies and emerging trends. In terms of success, we have had early successes in big data analytics in the US, but it is still most of the implementations are still very new, so the market place is yet to absorb though you have smart phones and you have apps, which are consumer related apps and games related apps, there are still not many apps which have got integrated into the corporate space so those are areas which we are working on and we are sure that during the coming year, we are going to see a lot more of that.

Moderator Our next question from the line Sanjeev Hota from Sharekhan, please go ahead.

Sanjeev Hota My first question is on the segmental state if you can provide for CS, SI and ITES?

J. K. Gupta Yes, you can note down. Total CS revenue is Rs. 78 crore out of which Rs. 66 crore is domestic and Rs. 12 crore is international. In SI, we have got Rs.

316 crore, domestic is Rs. 42 out of that and the remaining is all international. IT enabled services total revenue is Rs. 75 crore of which domestic is Rs. 33 crore and remaining is international and E&T is all Domestic.

Sanjeev Hota

My second question is on the off shore shift that is you are saying that it is going to happen in the first quarter of FY14, so last several quarter, this is the lowest off shore revenue we have seen in this quarter, so what are the reason for that and what kind of upside we can see in the rest of the other quarters in the off shore shift?

J. K. Gupta

In fact I would not like to call it lowest off shore. You have seen in our international business in this quarter have grown significantly, so it grew 11% and the significant portion of that growth came in the onsite portion, thereby on a percentage basis you may see some decline in off shore component. We have told that we are expecting to see this current trend of ramp up on onsite for at least 1 or 2 more quarters, US election is just out and we are yet to see its impact on Visa regime. We also have shared with you that because of the current visa regime this onsite has gone up. It was not a part of our original plan. This is what we were expected to see in the end of this financial year and we expect to have a different trend from next financial year. This is what our expectation is. We still have to play by the time to see how the things unfold.

Sanjeev Hota

If you could comment and give some colour on the IT budget and what you are client was getting some colours from your client?

J. K. Gupta

Simply speaking we have not seen any major challenge in terms of IT spends of our plan base. If you look at businesses, we are into two kinds of businesses. One is that we have got long standing relationship with the client as said earlier like TRW in America and all that, so with those clients typically we engage with them that their initial R&D budgeting stage itself so we get fair amount of clarity about what kind of expenditures are planned and since we are into the niche area which is core R&D for them, we have not seen any problem with any of those clients. The other business segment that we have got is on the project by project basis. We get lot of projects in India. We keep hearing a lot about slow down and delayed decision making and all

that. But that has not significantly impacted us because contribution of these businesses in our overall businesses have come down over a period of time, like last quarter we got only 32% business from India geography, so we have got sufficient business opportunities available here to insulate us from this talks of slow down. So as of now I do not see any major worry on account of clients reducing their budgets or slowing down their businesses, their IT spends.

Sanjeev Hota My last question was on product and solution, have you seen any big jump in the revenue contribution coming from product and solution this quarter?

R. Ramanan Yes this quarter we saw because we were able to close a few insurance transactions because of which we saw some jump in the product and solution this quarter.

Sanjeev Hota So now it contributes more than 30% of

R. Ramanan No we are still about 18 or 19%.

Sanjeev Hota But for SI perspective, it contributes more than 30%, right?

R. Ramanan That is right.

Moderator We are going to take our next question from the line of Pankaj Murarka from Axis Mutual Fund, please go ahead.

Pankaj Murarka If you could share some more light in terms of on some of key dealings we have had in the quarter and also on the traction we have seen on the infrastructure management side?

R. Ramanan We have, as you are aware added 26 clients during the quarter and client addition has been in almost all the segments of our business embedded in real time systems, we added 4 clients in the international market. We have added infrastructure services customers in the Indian market and we have added SI solutions in all the markets, both India as well as international and the emerging geographies. We have been also able to grow our ITES business in the domestic and international markets. So overall the growth has been

uniform. Education and training has been a little bit of plateau during this quarter, but we have initiated some new initiatives on vocational training which we expect will gain momentum during this quarter and the next quarter. We have also been able to establish formal relationship with some expert partners in vocational training particularly Unitech from New Zealand and we expect that this will have a good impact on our education and training service revenues.

Moderator We are going to take our next question from the line of HR Gala from Quest Investment, please go ahead.

HR Gala Just one book keeping question, can you guide us through how much has been FOREX gain/loss effect in this Q3 vis-à-vis Q1?

J. K. Gupta In Q3 we had an exchange gain of Rs. 3.4 crore. Last quarter we had exchange loss Rs. 1.66 crore.

HR Gala So in 9 months what is the position?

J. K. Gupta In 9 months cumulative we have got gain of about Rs. 1.3 crore.

HR Gala This will include the translational as well as the transactional, both put together?

J. K. Gupta That is right.

HR Gala So 1.3 crore was the gain in 9 months, visa-vise how much was gain or loss in the corresponding 9 months?

J. K. Gupta Last year we had about 4 crore loss.

HR Gala There is a good positive swing has taken place in this year. Another question is you said that the cash and cash equivalence we had is something around 218 crore that I hope includes 113 crore of mutual funds?

J. K. Gupta Yes that includes, because investment is all liquid in this.

- HR Gala** How much will be the total CAPEX for FY13, you did not give the number, you said 67 crore has been spent so far?
- J. K. Gupta** Actually our original plan for the year was Rs. 228 crore, but there are a few projects which are a bit slow in terms of pushback and that is what Priya was asking initially. Overall we do not see the project getting delayed, but some of the expenses would have got pushed from this year to next financial year. So I guess like Rs. 67 have been spent for first 9 months so even if we take say about 50 to 60 crore, I think the full year CAPEX could be anywhere about 130 crore or so.
- HR Gala** And the balance will be in the next year or something more will come in FY14?
- J. K. Gupta** Actually most of the shortfall of CAPEX this year will get to next year, so as of now we are not planning to push it beyond next financial year.
- HR Gala** So next year will be roughly how much?
- J. K. Gupta** Next year our plan initially thought was about 150 crore, you can say that in this case, next year will become something like Rs. 225-230-240 crore. We are working on that but ballpark is this.
- HR Gala** That is fine that I understand, and the tax rate, this year will be how much? You said that next year we are looking forward to 22% in FY 13 how much do we look forward to?
- J. K. Gupta** First 9 months tax rate is 25.8%, I guess by the time we close the year it should be around 24.5 to 25%. Next year, I say that we are well get to go around 22%.
- HR Gala** Now one question for Mr. Ramanan, any company that we study in this technology field everybody is talking about the same big data mobility, applications, analytics, cloud and all that, now you explained three areas in which CMC is going to concentrate, but basically I just wanted to understand how do we differentiate from the other companies in terms of our offerings so that we try to gain more business out of these new initiatives?

R. Ramanan

The differentiation comes in really the focus area, because the underlying technology is still the same, so our approach is the following. Number 1, all our existing products and solutions that have been developed as a result of that we are making sure that the cloud mobility and big data analytics becomes an integral part of an extended solution. The second part that is proactively our products, we are doing the necessary innovation to ensure that they will keep ahead of the technology or keep ahead of the learning curve otherwise our products will become obsolete, one is from the customer point of view and one is from our own products sustenance point of view. The other two areas in fact are today you have SI becoming an important element in the cloud, mobility, and big data analytics implementation. You see all the OEM vendors, whether it is IBM or whether it is Oracle or SAP, they are all coming up with their own offerings, but those offerings have to integrate with the core platform which has been developed, so these are all coming as additions and add on, so that is SI opportunity for us in addressing wherever these implementations are there, so that is the second part. The third part is coming up with solutions for the SME sector, which again we are focused on our products as a possible offering for the SME sector using cloud or mobility or analytics. As an example, we have Genesys which is for the larger enterprise, but now that we have lot of small insurance company and broker companies which are also coming for the insurance segment, so we are looking at offering a cloud based service for them, so this is a three-prong strategy that we are doing.

Moderator

We are going to take our next question from the line of NGM Puranik from Enam Securities, please go ahead.

NGM Puranik

Interesting couple of things, couple of your businesses have been doing very good. I was looking at the long term approach to developing customer services business, what are your thoughts in terms of bringing the services element, like you talked about big data analytics and all that, is there any other infrastructure IMS you have been talking about or any other way you can get more services into the hardware system integration and get that business more sensible because the margin here is pretty volatile.

- R. Ramanan** Yes, I think on the infrastructure side, we are seeing actually a very good opportunity in integrating a hardware related, it is not hardware, it is hardware-software combination related offering by OEMs in the infrastructure space. For example, today you have EMC which is offering cloud based virtual storage and virtual storage is going to be a big thing in the future because a) it helps in virtualization of your hardware and in optimizing it and b) making it also very affordable, so they have come up with offerings and products and we have already formed a partnership with them to see how to get address that.
- NGM Puranik** What exactly you will be doing, what value add solution you build up, is an IP that you have on that or your connector that you will connect this to?
- R. Ramanan** That will be an IP which we are looking at taking from a configuration management, cloud management so this will sit on top of that particular solution.
- NGM Puranik** How will you make money, what will be the typical deal size and how will you make money in this?
- R. Ramanan** One is migration itself could be a fixed price project and so on, but the other is if you offer a solution on top of it, then you can have pay-per-use and that is the transformative model that we want to go into. Instead of going into manpower based services because cloud or mobile-based service offers you the ability to have pay-per-use.
- NGM Puranik** This is per storage solution you get paid like that or how does it happen?
- Management** No, it could be the transaction that you are conducting on it. That normally the vendor himself will provide that. What we have to do is provide a solution on top of it, so if I have for example let us say we have a depository product, DP Secure, if I am able to implement this DP Secure over a virtualized network, then I can have people paying per use, per transaction for their depository participate. We are already doing some IP development in that.
- NGM Puranik** So is it a platform approach or is it just a solution approach or a combination?

- R. Ramanan** It is a combination because it cannot be just a solution, it has to operate on multiple platforms, sometimes you have organizations which have combination of hardware platforms, so you will have to work on that.
- NGM Puranik** So you will have a joint go-to-market in this?
- R. Ramanan** Yeah, correct.
- NGM Puranik** Your separate team who are dedicated for this?
- R. Ramanan** Yes, we have an innovation team which we have separately set up and that is we call it business and technology innovation team.
- NGM Puranik** You are saying something about infrastructure.
- R. Ramanan** Yeah, one portion is just the infrastructure migration, infrastructure modernization, according to me that is going to happen, but you have let us say dedicated enterprise customers who would want to go for a cloud-based data center for instance. Today, they have their own centers, but they may say we want to move into a cloud-based data center because we do not want to maintain this and run it and all of that. There is a migration to cloud-based data center which would call for a whole lot of infrastructure management services associated with that.
- NGM Puranik** You do the cloud enabling you will build your own tools and methodologies?
- R. Ramanan** Correct.
- NGM Puranik** JK, if you do all this, how will the margin profile change for this CS business?
- J. K. Gupta** Actually, we are yet to do the completing modeling of this but honestly speaking margin should improve from here because this new models provided us great flexibility in terms of leveraging the infrastructure and also creating variability in the revenue. And once we provide kind of a platform-based offering, as we go in volume, the margins will improve disproportionately.

NGM Puranik No, what is your definition of improvement? Is it double the margin or what?

J. K. Gupta Look, typically what happens like in India the services margin are close to about 18-20%. So when we say improved margin we are talking of margin improvement over the current margin structure.

NGM Puranik You are saying at the gross level?

J. K. Gupta At the deal level.

R. Ramanan Let me answer that question a little more differently. What we are looking for in the CS Services today we have 95% of our business coming in the domestic market. We want to take it to 60/40 type of thing initially. 60% from domestic market, 40% from international market. Just like we had started off in the other areas.

NGM Puranik So that you do go-to-market with TCS?

R. Ramanan So we will do go-to-market with TCS, we will also do go-to-market with vendors because in this vendors are open to new players in this market. And in fact, they are looking forward to somebody who also has a solution, because the success of their sale is based upon a solution riding on it. If we improve our international business, clearly, there will be a huge upside in the margin.

NGM Puranik You already started the process there?

R. Ramanan Yeah.

NGM Puranik The other thing is about your system integration business. How much of that is embedded in others?

J. K. Gupta Our total systems integration is about 65%. Embedded is about 19% out of this.

NGM Puranik And the margin profile for both?

- J. K. Gupta** Embedded is slightly better as compared to our average margin is 21%. Embedded is slightly better than this because embedded has got significant offshore component because of that margins are better.
- NGM Puranik** There are a lot of IPs in that?
- R. Ramanan** Actually, we create IP for the clients. So, mostly IP is resting with the client.
- NGM Puranik** And this business are there, what, fixed price or time and material?
- R. Ramanan** Combination. Actually, it is basically budget-based you can say.
- NGM Puranik** And this IT-enabled services, what is the kind of work you do? Is it lot more digitizing kind of work or better value-added work, what exactly you do in IT-enabled?
- R. Ramanan** In IT-enabled services there are three or four segments that we work. One is digitization services, which calls for digitization of not only paper but also other feet that an organization receives in terms of information. The second part is work flow management. So we take this digitized data and then we do work flow management because it has to integrate into various systems. For example, if you have HR related data it should get rooted to the HR system. If it is SAP related, order related data it has to go there and so on and so forth. If it is customer complaints, it has to go to the CRM customer complaint management system and so on. The third part is analytics which is what we have already entered into, because you are collecting a lot of information. So what do you do with that and how do you use analytics or knowledge processing. To extract vital information or meaningful information from all that information that you are collecting and then pass it on to the decision support systems. So that is the higher end value adding service which has very good margins.
- NGM Puranik** What is the mix of revenue in this JK?
- J. K. Gupta** In IT-enabled services?
- NGM Puranik** Digitization, work flow and analytics?

- J. K. Gupta** Actually, almost all the international business that we have got is on digitization and analytics. A lot of Indian business is on work flow management.
- NGM Puranik** Within that the analytics would be what, 50% or 70/30?
- J. K. Gupta** We do not have that breakdown as of now.
- R. Ramanan** I would say anything that we are doing at the international market today is a combination of digitization and analytics because pure digitization will not bring much value to us in the international market, whereas in India we do digitization of work flow management, for example, the MCA project is the passport seva project, there is a huge amount of work flow management in that.
- NGM Puranik** And your love for education business continues?
- R. Ramanan** Love for it continues, result hopefully will come during this year.
- NGM Puranik** It will continue to stay like that or the growth also will come?
- R. Ramanan** No, growth will come.
- NGM Puranik** This is on the SEZ investment, you have significant investment in SEZ. So the long-term strategy is going to stay like that because it does not give you returns on investment?
- J. K. Gupta** Puranik, SEZ is a project. It is not like that we are going to continue to make investments. This is one project that we have picked up which is going to consume about Rs. 445 crore and in terms of costing of the project we are still firm on this, no variation taking place. It is a long-term investment.
- NGM Puranik** What kind of capital returns it will generate?
- J. K. Gupta** It will generate huge amount of capital return. I will tell you this project cannot be solely analyzed on capital returns. It is like monetizing an asset which otherwise idle asset was not having any value, there was a risk associated with this. Second thing is for the company, for CMC itself as we

grow international business and in order to avail tax advantages we require to have SEZ and SEZ has to have a minimum size. So it is a great opportunity where TCS also says that we guarantee you utilization. So it cannot be measured only with regard to the current return that we are getting.

NGM Puranik But you will also be selling some assets?

J. K. Gupta We are not going to sell assets.

NGM Puranik But how will you get your greater returns then?

J. K. Gupta Actually, overall when the project is fully commissioned and everything is on. One is that we are going to have about 2500 of our own seats which is going to deliver us critical international revenue at high margin plus whatever we get from TCS. Overall return on this project is not going to be less than 25%.

Moderator Thank you. The next question is from the line of Urmil Shah from Kim Eng Securities. Please go ahead.

Urmil Shah Last question we discussed about embedded software solutions for electronics in the automotive segments and we are signing long-term deals with automotive companies abroad. Any update on the same?

R. Ramanan We continue to see that as a good growth market for CMC. We have increased our revenues in that space from existing customers and we have acquired a few new customers from whom offshore revenues will start flowing during the next quarter or maybe the quarter after.

Urmil Shah So of the four clients added in embedded software, how many would be from the Auto segment?

R. Ramanan We do not have a very clear breakup on that but I would say at least 30% of our embedded system revenues would come from Automotive segment.

J. K. Gupta Existing client if you see is the much larger portion because our largest client is from Automotive segment.

- Urmil Shah** Just a breakup of the 20 clients acquired in India across the sector?
- R. Ramanan** Actually, we have got a wide variety of clients which includes e-governance, we have transportation, we have got infrastructure, we have got financial services and insurance.
- Urmil Shah** So similar spread is in previous quarter?
- R. Ramanan** Yeah, that is true.
- Urmil Shah** And a last bit of book-keeping question, The SG&A cost has declined by about 9 crore this quarter...
- J. K. Gupta** No. If you look at segmentation from there you are driving is because of the change in other income.
- Urmil Shah** What is the changed?
- J. K. Gupta** SG&A cost has slightly gone up this quarter if you just have a look at it, about Rs. 1.5 crore increase is there.
- Moderator** Thank you. The next question is from the line of Bharat Seth from Quest Investments. Please go ahead.
- Bharat Seth** Taking ahead of this embedded side, which are the sectors that we are targeting that is one? And second, geographic expansion that we were looking for this MEA side, so just can you highlight it?
- R. Ramanan** The sector is within the embedded system that we are targeting is Automotive, Transportation, Office Automation, Communication Electronics and Industrial Systems. So these are the areas that we are targeting and we have customers in all of these segments.
- Bharat Seth** Are we looking for consumer electronics also?
- R. Ramanan** No, not so much. Consumer electronics, we do not see too much of an opportunity for CMC right now in that. In the hi-tech segment, we service embedded system customers who service consumer electronics because

typically today's consumer electronics you have a lot of parts which are manufactured by different hi-tech vendors and then they are all integrated.

Bharat Seth

Recently, in this telecom policy which was announced by where government is putting a lot of pressure on importing these chips manufacture in India so how that will translate for us?

R. Ramanan

We are not in that Manufacturing segment at all. So I do not think it will

Bharat Seth

Those people like CISCO and they have to put up a factory over here, telecommunication and all, so if they have one, how do I mean our embedded business can get benefit where we can leverage our embedded strength in those areas?

R. Ramanan

The one way of servicing those customers would be in India itself because they would have products which they would create which are meant for the Indian market and they would typically be low cost devices which they will come up to service the market and so any R&D and design services or even development services that we can do for them and we are already doing it for quite a few multinationals in India now. So, that is the opportunity for us. But if it is purely a manufacturing set up we would not have

Bharat Seth

Catering our services to those manufacturers?

R. Ramanan

No, that will not be an opportunity for catering to the manufacturing plant, but if they have design services within India to enable in their manufacturing decisions then we can service them and which is what they will do, they will set up local design shops so that they can continuously innovate and come up with products. It is just like the most of the car manufacturers have come up with low cost cars or low cost vehicles in the Indian market because after Tata came up with the Nano car, it has really given room for a lot of companies to innovate in that area. Similarly, in the semiconductor space or in the electronics space you will have a lot of design houses being set up here.

Bharat Seth

Geographically, how are embedded? We are mainly in Europe or we are catering to Europe, Japan, US all?

- R. Ramanan** We are in US and in Europe. In Europe we are more concentrated in Germany where we have a bigger presence.
- Bharat Seth** And for our solution we were looking to expand geographically. So can you update a bit on that?
- R. Ramanan** We are looking at all our solutions for expansion in the Middle East, Africa and Asia Pacific region, particularly, insurance solutions, ports embargo solutions, eGovernance solutions, banking and financial services solutions and mining related solutions.
- Bharat Seth** How is the current traction in that and how do you see going ahead that will...?
- R. Ramanan** We see good opportunities for this and we have had initial successes which is going to enable us to replicate them in this marketplace.
- Bharat Seth** And Genesys as you said we are looking up for the SME segment. So do we have any other such cloud-based services where you look targeting SME sector other than this Genesys?
- R. Ramanan** We do have some other solutions. For example, vehicle management systems could be a SAP-based service and then we are also looking at core banking for small and medium sector and so on.
- Bharat Seth** And this vehicle tracking, do you think that our solution can be offered globally, like port solution we have internalized...
- R. Ramanan** We already have got international customers in vehicle tracking in Africa. So this is fairly significant development for us. So we see an opportunity in Middle East and Africa. About the American market and the more advanced markets we see SI opportunities there, not for our product to be positioned there.
- Moderator** Thank you. The next question is from the line of Pralay Das from Elara Capital. Please go ahead.

- Pralay Das** To start off with on CS there is obviously a quarter-on-quarter variability in margin which is I guess led by the component of equipment. But this particular quarter, the component of equipment seems to have gone down with the margins have done down as well. So, am I reading this wrong?
- J. K. Gupta** No, equipment has actually gone up this quarter, it has gone up by about 18% quarter-on-quarter.
- Pralay Das** I was actually comparing it versus the first quarter when we had 11% kind of a margin. So, we expect this kind of variability to continue but on a longer-term basis where do you think the margins on CS will settle?
- J. K. Gupta** The CS margin typically till the time we do not scale up international business significantly. With the current business mix our CS margins are like lower double-digit or higher single-digit. So, it has been in the range of around, you can say 9-10%. That is the kind of natural margin of this business.
- Pralay Das** And of the number of SEZ seats that are online, how many would be vacant as of now, as in not being used by you, as well as not leased out to TCS.
- J. K. Gupta** There is nothing vacant. So what has happened is that we were supposed to use 2500 seats, of which, we are currently using say 1200, the remaining seats for the time being we have given to TCS temporarily to use?
- Pralay Das** And what is the kind of notice that you require to give to TCS to...?
- J. K. Gupta** Whenever we sign a new contract we know that we need to have more seats and we are able to tell them and there maybe with the time of two to three months which normally takes for ramping up, they will be able to give. Another thing is that those seats have been temporarily given to them pending commissioning of Phase III, so ultimately they will move there.
- Pralay Das** What was the TCS GTM this particular quarter?
- J. K. Gupta** 58%.

- Pralay Das** It was 53% I guess last quarter.
- J. K. Gupta** Last quarter was 56%.
- Pralay Das** And the driver of margin expansion in both SI and ITES, had it been portfolio mix changes or more organic levers in.....?
- J. K. Gupta** Actually, there is no significant change in portfolio mix. It is basically because of volume and a bit of FOREX being favorable. These are the businesses which have got bulk of international business. So they get advantage of favorable FOREX conditions.
- Moderator** Thank you. Ladies and gentlemen, that was the last question. At this time I would like to hand over the conference to Mr. Ashish Aggarwal for closing comments. Thank you.
- Ashish Aggarwal** I would like thank all the participants for taking out the time for the call and as well as the management for taking out the valuable time to participate in the call.
- J. K. Gupta** Thank you, Ashish and thanks to all the participants to take time out to participate in this call.
- R. Ramanan** Thank you very much everybody.
- Moderator** Thank you. On behalf of Tata Securities Limited that concludes this conference call. Thank you for joining us, you may now disconnect your lines.