TATA CONSULTANCY SERVICES

Tata Consultancy Services Limited

FY06-Q1 Analysts/Investors Conference Call

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Pratibha	Good morning ladies and gentlemen. I am Pratibha, the moderator for this conference. Welcome to the TCS Earnings Conference Call. For the duration of the presentation, all participants' lines will be in the listen-only mode. After the presentation, the question and answer session will be conducted for participants connected to the SingTel Bridge followed by question and answer session for participants connected to the India Bridge. I would now like to hand over to Mr. Arjun Marphatia, Head of Investor Relations at TCS. Thank you and over to Mr. Marphatia.
Arjun Marphatia	Thank you Pratibha. Good morning friends and thank you for joining us on this analysts call on a Saturday morning. As usual, we are all seated in our executive conference room at our Corporate Office in Mumbai, and I am sure that over the past one-year you all have had the privilege of meeting our leadership team, but nonetheless, I would like to introduce them to you. Mr. S. Ramadorai, our Chief Executive Officer and Managing Director.
S. Ramadorai	Good morning everyone, this is Ram here.
Arjun Marphatia	Mr. S. Mahalingam, our Chief Financial Officer.
S. Mahalingam	Good morning.
Arjun Marphatia	Our two Executive Vice Presidents, Mr. N. Chandrasekaran, Head of Global Operations.
N. Chandrasekaran	Good morning everybody.
Arjun Marphatia	Mr. S. Padmanabhan, Head of Global Human Resources.
S. Padmanabhan	Good morning.
Arjun Marphatia	And we are also joined today by Mr. Girija Pandey, our Regional Director for the Asia Pacific region. I am sure all of you have analyzed our results for the first quarter, which were declared last evening, and a copy of the presentation, the press release, and the financial statements are available on the website. Initially, Mr. Ramadorai will present an overview of the company's performance in the first quarter, after which we will proceed for discussions. A simultaneous live audio webcast of this call is

available on our website and will be available for the rest of the quarter. As you are aware, TCS does not give any guidance, and this call is being recorded. As usual, before proceeding further, I would like to remind you that anything said on this call and which reflects our outlook for the future or which can be construed as a forward-looking statement must be read in conjunction with the risks that the company faces. The full statement of this is available on the second slide in the presentation which has been uploaded on the tcs.com website. I now request Ram to present the overview. Thank you.

Ramadorai

Thank you, Arjun. Again, a very-very good morning to all of you. Getting into a call on Saturday, we sincerely and really appreciate the same.

Let me start by saying that we have had an excellent quarter, thanks to the entire team TCS and our subsidiaries, associates, who have made this happen.

The highlights essentially are, strong international revenues have driven our growth, and by US GAAP accounting, the international revenues grew at 5.47%, Indian revenues grew at about 0.25%, and the total revenues by 4.83%. The operating income grew at about 8.95% and the net income before one-off items was 32.84%.

More importantly, we added almost 68 clients during this quarter. That shows the traction and the growth momentum we would like keep as we go into the future, and these are potentially clients who are going to be helping us a lot in the future based on our service and our execution competencies.

One of the things I wanted to highlight was the leading financial services firm in the US, which has contracted us with a $100 million contract. We have already begun on this engagement and it is not in the process or anything, we have started working on this.

We added significant number of employees – 2690 – and we focused a lot on productivity and operational improvements like we always do. More importantly, the retention in the company was exceptionally high, best in class with regard to retaining at about 8.2%. I think the key message is the growth not just on one dimension but across all the identified service segments, namely the IT services, BPO, the infrastructure, consulting, and package-enabled services, all of them saw traction during this quarter and the cross-selling initiatives with any of these is going to be a way as we move forward.

I think the platform based BPO and the committed number of seats which we are building to enhance capacity shows the momentum that is likely to happen and very clearly Process, IT Strategy and Domain-based Consulting with a consulting organization, and the leader in the consulting organization we announced is a very-very important one. The win in China with regard to again establishing a presence and building a long-term future, a sustainable industry, TCS which does always as it started in 1968 in India, is going to be very critical for the well-being of not only TCS but the industry as a whole as we look at global delivery competencies. Last but not the least, we announced a very-very important merger, namely Tata Infotech with Tata Consultancy Services, which again is absolutely important not only to the shareholders to create value, the synergies that are possible between TCS and Tata Infotech in a number of areas including manufacturing where engineering and industrial services, which we have been saying that would be the next wave of growth for the industry as a whole, and we presented to the press conference during NASSCOM on 20th of June, and also gave some industry growth projections.

Overall, I think we are very pleased with the quarter and I would now turn it to my CFO, Maha, so that we can quickly go through a few things and then address all the questions and answers. Again, thank you so much, but essentially the key message is there is a growth momentum, we have merged Tata Infotech across all the geographies and across our global delivery model which we believe in, and China as overall strategy for the future, just like our global design delivery and marketing capabilities. Thank you.

S. Mahalingam: Thanks Ram. As Ram said, there has been an increase in revenue during the quarter, and the second factor that will have to be account is the improvement in cost management that has taken place, which has resulted in both the gross margins and the operating income showing improvement more than the improvement in the revenues. So these are the two factors that have really come in and helped us in posting a good result as far as this quarter is concerned. Now, over to Arjun.

Arjun Marphatia: Pratibha, I think we can now commence with the question and answers.

Pratibha: Yes sir. At this moment, I would like to hand over the floor to Salbiah to conduct the Q&A session for participants at the SingTel bridge. After that we will move over to the question and answer session at the India bridge. Thank you and over to Salbiah.

Salbiah: Thank you Pratibha. We will now begin the Q&A session for participants connected to the SingTel Bridge. Please press 01 to ask a question. The first question is from Mr. Pratik Gupta of Singapore. Over to you sir.

Pratik Gupta: Firstly congratulations on the quarter. I was just wondering if you can elaborate a bit more on a couple of things. Firstly the overall business environment, how you see it in terms of the deal pipeline and also in terms of the competitive landscape given that we keep hearing that the MNCs are ramping up a bit more aggressively in the offshore space, that's number one. Secondly, coming to the specifics for the quarter, if you could just elaborate a bit more on the onsite-offshore mix, is this just a Q-on-Q fluctuation wherein the offshore has come off, and what's the outlook for the full year as a whole in terms of how much we should expect this to improve, and the last is this move towards the global compensation structure, could you just elaborate a bit more on that and also the fact that you have given just an 11% offshore hike versus some of your peers who have given bigger hikes, could you just touch upon these things please?

N. Chandrasekaran: Thank you. There are a number of questions there. First, I will try and address the question on the deal pipeline and the business outlook. As part of the quarterly results announcement, we also shared a number of engagements where we have successfully delivered as well as engagements we have closed. As you can see, we closed the $100 million deal plus a number of other deals across verticals and across geographies. The deal pipeline is looking healthy, not only in our established geographies but also in the new geographies like the Middle East and continental Europe and Asia Pacific. So the deal pipeline is pretty strong. We are also looking at deal sizes which are larger.

Second point, the growth is also coming from existing accounts. If you see the presentation that we have made on some of the growth engines, the number of customers in each of these growth engines is increasing. When we say the number of customers in the growth engine, some of them are new customers for us, and many of them are existing customers who are adopting these services from TCS for the first time. So the business outlook is pretty positive and the volume growth is quite healthy.

Then on the value side, you can see the presentation on consulting. We are really stepping up. We have consolidated all our consulting efforts from the process, domain, technology, assurance activities. So we expect to do a large number of consulting engagements again on the existing customer base and also use it as a tool to get engaged with new customers.

Then coming to your second question in terms of the onsite-offshore mix. The onsite-offshore mix has shifted approximately about 3%, I think it is 3.1%, towards onsite during the quarter. There are two or three factors contributing to this. The first one is there is one of the existing large customers with whom we had a blended rate contract. During contract renewal, we have negotiated a specific onsite and offshore rate structure. So there is no increase in manpower with this customer but it is only more shift of revenue in line with the new contract structure. That is distorting the figure to some extent. The second one is, we have closed some fixed price projects, which the analysis work is on now. So in all the fixed price projects what happens is, the first phase is heavily onsite intensive, practically there is no offshore until the requirement is closed, and then it is predominantly offshore and very little onsite. So we expect the shift towards offshore in all these engagements will happen in the next quarter and the subsequent quarters, second and third quarter. So definitely the shift towards offshore will happen in the case of new fixed price projects. Even in the case of the existing customers where we change the contract, there is a heavy drive to shift all the work towards offshore. So there also the onsite revenues will come down and the offshore revenues would pick up. So the essence of the message is, you will see shift towards offshore definitely in the coming quarters. Then on the question of compensation, I am requesting Paddy to step in.

S. Padmanabhan: Thanks Chandra. Let me first address the global compensation. As of the 1st of July 2005, in the US, we will give a consolidated US salary. In the past, we were giving an Indian salary and an allowance structure in the US, so that is the first change that has happened. We have also implemented it in Australia and China. This is in line with our globalization process. We are also hiring outside India. This year we plan to add 2000 more people in our overseas geographies.

The other question, Pratik, which you asked is related to the competitive landscape and the presence of multinational companies in India. Yes, during the last one year, there has been a significant ramp up in terms of people by these companies. If you look at our hiring pattern, there are two basic processes. One is hiring in the campuses, and as of now we have completed close to 80% of the campus hiring this year and we have not seen any change in our hiring method or mix or any pressure in the type of institutions that we have been going. The second component is market hiring where we do have pressure in the 3 to 5 year category, so the company is putting a lot of effort in building competencies of people with special skill and ensuring better retention at that level.

Pratik Gupta: Okay, thanks. I just wanted to clarify this: consolidated US salary, will this imply the overall cost to the company being the same as what it was earlier, or will this imply an increase from the 1st of July onwards?

S. Padmanabhan: We have factored the increase as a result of this consolidation for the year.

Pratik Gupta: Sorry, I didn't follow. You mean to say, there will be an increase or…?

S. Padmanabhan: Yes, there will be an increase, starting 1st of July, but in the overall planning for the year, that has been factored in.

Pratik Gupta: Could you help quantify by roughly how much the increase might be, is it like similar to the 4% onsite you have given in the June quarter?

S. Padmanabhan: That is right.

Pratik Gupta: So effectively this will be another 3-4% hike in the September quarter?

S. Padmanabhan: No, the 4% hike in the overseas geographies includes this increase which is already planned.

Pratik Gupta Okay, thank you very much.

S. Padmanabhan Thank you.

Salbiah Thank you sir. Next on line, Mr. Bhuvnesh Singh of Singapore.

Bhuvnesh Singh Hi sir, congratulations for good results. Can you give me some idea of how exactly did our volume and pricing move this quarter.

N. Chandrasekaran Both on the volume side and on pricing, it has been an excellent quarter for us. On the volume side, I think I would like to make two or three points. First, the business has shifted more towards international business, volume growth. The India business, especially the CMC business has dropped from the last quarter onwards and as a consequence of that, the equipment related business which is a little bit low margin has gone down and this has been compensated by increase in growth in the international business, volume growth. The second point I want to make is, even in the domestic business our margins have gone up because of the quality of the engagements mix in the Indian business. By design, we have taken a conscious decision to move away from these businesses whether it is the CMC or the TCS domestic, and that has improved the domestic margins as well.

Then, in terms of pricing, overall there has been an increase in pricing or the billing realization as we call it because of two reasons. One, because of the efficiency in the execution of the fixed price projects. Second is because of the marginal rate improvements we have been able to achieve both in the case of some of the new contracts and also in the case of some contracts which we have re-negotiated, that have come into effect this quarter.

Bhuvnesh Singh In that, would it be possible for you to quantify, like last quarter you said that the volume growth was around 3%, can you give us similar quantifiable number this time?

N. Chandrasekaran I am hesitant to give a number because the mix, the volume growth has happened both in the case of the time and material contracts but also in the case of the fixed price contracts. But it is definitely upwards of 2.5 percentage points.

Bhuvnesh Singh Sorry, upwards of how much?

N. Chandrasekaran 2.5 percentage points.

Bhuvnesh Singh Okay, and going forward when we look at our forward business, I want to understand what sort of visibility do we have for may be next quarter revenues or next four quarter revenues, like can we say that 90% of revenues what we have planned is already in the bag or how is that do we look at it?

N. Chandrasekaran See, if you really look at it, the repeat business ratio is 98.5% during this quarter and the new customer revenue is about 1.5% in this quarter, and all the time and material contracts that we have and the fixed-price contracts that we have are completely known for the coming quarters, definitely the second and third quarters. Maha, is signaling to me that he wants to add something here.

S. Mahalingam — You know, I have been saying earlier that the visibility for the year would be approximately about 70% at the beginning of the year and each quarter you enter into it with about 80% to 90%, somewhere there, and that's the kind of percentages that still continue to guide our business.

Bhuvnesh Singh — Sir in that, I just have a request, when for the next quarter we have got 80-90% of visibility, shouldn't we give a sort of guidance of the revenues of next quarter, one number which we can look that this is what management visibility is for next quarter. This is just a request, you know, in whatever way you guys want to look at it, but overall I think the quarter was very good and thanks a lot, and congratulations on good quarter.

S. Mahalingam — We keep listening to the feedback from all of you, and yes, we will consider this. But as of now, we don't give any guidance, that's a policy.

Bhuvnesh Singh — Sure sir, thanks a lot.

Salbiah — Participants, who wish to ask questions, please press 01.

Arjun Marphatia — Could we move to India please?

Salbiah — At this moment, there are no further questions from participants at SingTel. I would like to hand over the proceedings back to WebEx moderator, Prathiba.

Pratibha — Thank you very much Salbiah. We will now begin the Q&A interactive session for participants connected to the India Bridge. Participants' who wish to ask questions, please press *1 on your touchtone-enabled telephone keypad. On pressing *1, participants will get a chance to present their questions on a first-in-line basis. Participants' are requested to kindly restrict to one question in the initial round. Follow-up questions will be taken later. Please use handsets to ask your question. To ask a question, please press *1 now. Our first question comes from Mr. Ashish Agarwal of IL&FS Investsmart.

Ashish Agarwal — Yeah, my question is regarding your utilization rates. Your utilization rates have fallen this quarter, any specific reason for that or…

N. Chandrasekaran — See the utilization rates keep fluctuating by two or three percentage points, and also if you see the number of people that we have added also plays a part. Net-net, there have been more number of people who have become billable during the quarter. Then, the utilization variation is also due to completion of certain fixed-price projects and commencement of certain new fixed-price projects. Our goal is to push up the utilization during the coming two or three quarters at least by another 3 to 4% percentage points from the current levels, and since we have a healthy pipeline we feel that we will be able to do it.

Ashish Agarwal: My next question is regarding the synergies, what synergies do you see between Tata Infotech and TCS?

S. Ramadorai: This is Ram, let me address this question. If you know, Tata Infotech is in the solutions and systems integration business, both in the international and the domestic market. They have a set of Fortune 500 customers, which would be a great synergy to cross-sell to those customer base as well as enhance our business within those customers through our Value Engines. Second one is, certain capabilities, certain verticals which they have along with the solution framing capabilities of TCS and the joint go-to-market, the capabilities when the merger happens will become very, very useful. So it is to address a larger market space and a larger customer base. Third is the manufacturing competencies and the manufacturing capabilities including the design engineering capabilities which this company has will give us a lot of end-to-end engineering and industrial solution space where contract manufacturing tied to design engineering services will become a value differentiator for this company. Last but not the least is the engineering and the education and training segment, and with CMC's presence in the education and training space, a combination of that will become a very powerful market to address, which we believe education and training is becoming very crucial for the future with the expansion that is likely to happen in this country, not just on the IT space but domain plus IT combinations thereof. Lastly, the 3600 professionals which come gives us an enormous strength with the offshore capabilities and the onsite presence in terms of market reach. So, we will be working through these synergies as the merger process happens through a court process, and that is what we will articulate as we go into the subsequent quarters. Finally, the investors are going to benefit where the ratios have been worked out in the ratio of 1 TCS share of one rupee for 2 Tata Infotech shares of 10 rupees each, and that is also done by an independent set of valuers, where both the boards approved this merger and that is what we announced.

Ashish Agarwal: My last question is regarding this 100 million dollar contract, what is the duration of this contract?

N. Chandrasekaran: Did you ask about the duration of the contract?

Ashish Agarwal: Yeah.

N. Chandrasekaran: See, we expect to realize this within a period of three years.

Ashish Agarwal: Okay, yeah thanks.

Pratibha: Thank you very much sir. Participants are requested to kindly restrict to one question in the initial round. Next question comes from Mr. Mahesh Vaze of Brics Securities.

Mahesh Vaze: Yeah, hi sir. We have seen margin expansion this quarter, there have been three things that happened, onsite as proportion of revenues went up by 3% sequentially, you gave an offshore salary hike of about 11%, and your utilization fell by about 2% or so, all these three factors, other things being equal, are negative to gross margins. If I just do some modeling, it comes to about 300 bps should be the falling gross margins because of these three things, yet your gross margins have expanded by 100 bps. Could you just give a bit more detail as to why this happened?

S. Mahalingam: I will do some broad explanation and then Chandra will also supplement that with details from an operational efficiency and so on. When you look at gross margins, of course Mahesh you have pointed out exactly the factors which have acted adversely in this period. But let's analyze each one of them. The first one is, you know, this onsite-offshore ratio that Chandra had earlier explained, where we essentially moved up by about 3% additional in terms of onsite. The quality of revenues - you will have to be looking at it because as was pointed out there are blended rates which have become different from onsite and offshore. At this moment in time, onsite rate is quite [word inaudible] and therefore that has had a positive effect from profitability sense or you know the cost of revenue in proportion to revenues have been more efficient. The second factor that has also come in is that the productivity improvement as far as the fixed-price contracts are concerned, the turnkey contracts, that has also helped in the process of shoring up the gross margin. The third factor that has also come in is in terms of the overall additions to the manpower that takes place and overall addition to billing that takes place as a result of utilization as a percentage, and that has to be applied to the total number of people that we have at this moment in time, we have had an increase. And there are additional people who have become billable. And the increase has also taken place at a salary point which is lower than the average of TCS because a fair amount of increase takes place at the trainee level. So that also has an effect on the cost pattern of the organization. So increase in billable resources and decrease in average cost – these are the two factors that really apply in terms of additional billable manpower and the associated costs with that. So these are broadly the kind of factors that have really taken place. Chandra, you want to add?

N. Chandrasekaran: I want to add here additional points. Definitely, the points that Maha covered in terms of the contract change from blended rate to onsite rate and offshore rate. There we have been able to get good onsite rates – that has definitely helped us in the gross margin improvement. Second one is, the productivity and the execution capability in the fixed price projects. Some of the fixed price projects we have been able to bring in additional productivity improvements significantly. The third one is the shift of revenue from the domestic revenue to international revenue. There are two different phenomena here, one is the decrease in revenue of CMC where some of the equipment related revenue has completely decreased in this quarter, and as a result that business itself, the domestic business itself is much more profitable this quarter than the previous quarter.

Then the second point is the decrease in the percentage of revenue from the domestic business has been compensated by increase in international revenues. That has again contributed to the improvement in margins.

Then the other point I want to definitely emphasize is the billing rates has shown improvement, both in the re-negotiation of some existing contracts and also in some of the new contracts that have come in this quarter. All of these together have contributed. But if you really see the overall numbers, we have gone back to our original levels in terms of the employee cost. Even in the equipment and software, which was 6.15% last quarter has come to 4.07% this quarter, and the employee cost though marginally up is at sustainable level we think. So it is a good story. I think we have been able to realize the benefits of the actions that we put in place, and our focus in the coming quarters will be two or three levers, which will continue to maintain the margins. Number one is to leverage the high onsite mix we have in terms of revenue and shift it towards offshore as we see growth. Again, since we have a high fixed price content, some of this movement from onsite to offshore we can still achieve without impacting the overall top line. The second one is to continue to engage in productivity improvements. And third one is to look at the billing rates improvements and high values services.

Mahesh Vaze: Okay. Sir I do take the operational efficiency part in the gross margins. If one focuses just on the salary cost, I do agree, I have seen that your cost of services or cost of equipment and software has come down significantly sequentially. If one just looks at the salary cost, it has gone up by 59 crores sequentially. Now there were three things which would have driven the salary cost up, there was a salary hike, there were additional number of people recruited during the quarter, and the third thing is onsite was higher, so some more people must have been onsite and they would have been paid onsite wages, which are higher than the offshore wages, okay. Now if one leaves out the salary hike as well as the fresh recruitment, just focus on the onsite part. Your onsite revenues have gone up by 148 crore rupees and your total salaries have gone up by 59 crore rupees, okay, so it shows a phenomenally high gross margins on onsite. I am just focusing on purely salary cost. All the other costs there can always be operational efficiencies. Why is it that despite salary hike, despite recruiting people, despite onsite increasing, your salary costs have gone up just by 59 crores?

N. Chandrasekaran: See this is what we have clearly mentioned. If you really see the answers that we gave before, a particular contract has…the contract structuring has changed. So the high onsite revenue not necessarily reflects the corresponding increase in manpower, that is a very important point and Maha wants to walk you through the numbers on this point.

S. Mahalingam: You are right in terms of onsite offshore, but we will also have to take into account the efficiency and productivity improvements in there, whether it is onsite relating to fixed price projects or onsite relating to time and material. Just giving you a percentage in terms of people allocated to onsite and the cost associated with that on projects, we have made some improvement there from 20.41% to 19.46%, close to about 95 basis points improvement there. So, yes, the cost has increased, but this was the result of the efficiency factors that we have introduced in the organization.

Mahesh Vaze: Maha would you just explain this 20.41, what exactly is this?

S. Mahalingam: The expenses that we incur on people on onsite assignments. So the point that I want to make is that there has been efficiency factor that we have brought in even with regard to the onsite work.

Mahesh Vaze: Okay fine, thanks a lot and all the best.

Pratibha: Thank you very much sir. Participants are requested to kindly restrict to one question in the initial round. Next question comes from Mr. Pramod Gupta of HSBC Securities.

Pramod Gupta: Hello sir. I just wanted to have some data points, if you could give us. Was there any overflow of revenue from Q4, and what was the BPO and product contribution in this quarter and what are the account receivables and unbilled revenues in this quarter, if you just give these five data points it would be really helpful.

S. Mahalingam: Overflow, there is no overflow into this quarter, and there is no overflow from this quarter to next quarter. But having said this I just want to add this point that we have two types of contracts which are not the normal ones for most organizations, the first type of contract is – we have fairly sizable system integration contracts, and in those cases what we will do is that people recognize the revenue, and we will recognize the cost at the point at which the actual transfer of ownership or transfer of property takes place to the customer, so that is one. But this has an impact both on the revenue as well as the cost associated with that. The second one is we are also looking at revenue recognition as far as fixed price projects is concerned, and there we essentially follow the conservative approach of recognizing revenue based on the efforts put in, and if there is any loss that we think would arise on those contracts, we recognize it as soon as we realize that there could be a loss. So to that extent there could be some changes and modifications that gets done towards the end of the projects, but at this moment all that I want to assure you is that as far as Q1 is concerned, these two factors have not played any significant part in terms of revenue. I just want to give you the basic principle.

Pramod, can you just repeat the other question.

N Chandrasekaran — The second question was in terms of the contribution from BPO and products. BPO contribution is little more than 1% of the overall revenues.

Pramod Gupta — How was it last quarter sir?

N. Chandrasekaran — BPO revenues are consistently increasing. We pointed out that last year we did about 22 million dollars. This year the growth rate is much higher for BPO, last year it's very negligible. Last year first quarter it is very, very negligible. So the contribution of BPO revenue is significantly increasing from a BPO point of view, but in the overall size it is still very, very small.

Pramod Gupta — I wanted to know about the account receivable and unbilled revenue.

S. Mahalingam — Okay let me give you the unbilled revenues and account receivable figures. Unbilled revenues stand at 3.984 billion rupees or 398.4 crores of rupees. This is to be compared with 2.203 billion rupees on 31st March, which is 220.3 crores. And as far as the Accounts Receivable is concerned, it is standing at 21.924 billion rupees or 2192.4 crores of rupees against 20.498 billion rupees or 2049.8 crores of rupees.

Pramod Gupta — Thank you. Finally sir, if you are saying that you have had in this quarter productivity increases, you have had a kind of pricing increases, still not very clear that how can you have a volume growth of 2.5% because your onsite volume growth is probably about 10%, if I assume the billing rate to be fixed. But if I assume that to be increasing then 10, it's surely lesser than that. And your offshore has actually declined 2.7%. Now if I assume some rate – offshore rate which is one third of onsite, my calculation shows that even if the rates are flat your volume growth is just less than 2%. So can you please explain where is the dichotomy and, I mean, where I am missing the point.

N. Chandrasekaran — See as we said you know the contract mix is between 50% fixed price and 50% time and material, so it is quite difficult to clearly say that this is the exact percentage for volume growth, that is why it is in the range of 2.5%, predominantly coming from time and material contracts and then the rest from the fixed price contract.

Pramod Gupta — Thanks and all the best.

Pratibha — Thank you very much sir. Participants are requested to kindly use handsets while asking the question. Next question comes from Mr. Anantha Narayan of JM Morgan Stanley.

Anantha Narayan — Thanks and good morning everyone. I had a question for Paddy on the variable compensation. Two parts, firstly, this will be the first year where you are recognizing the expense in the period of accrual itself, so consequently do you expect any volatility across the four quarters this year? And secondly Paddy, can you give us the exact variable

	comp number for this quarter and the previous quarter?
S. Padmanabhan	Okay. Let me address the second one first Anantha. Till last year we were distributing the variable compensation based on the EVA which we achieved in the previous year. As a result we actually announced how much variable we were distributing. Starting this year the variable distribution is based on the EVA that we will make this year. So since as a policy we do not give any guidance, I would not be able to separately tell you what is the EVA projection for the year and variable distribution that we are doing quarter on quarter. The first question, which you asked is in terms of the spread of the variable distribution during the course of the year, yes, it will be evenly spread out in all the four quarters.
S. Mahalingam	I want to add one thing to what Paddy has said, and that is, Anantha if you look at the manner in which we would go about doing this in terms of relating it. The percentage to revenue and profitability will not show any great volatility because we announced this incentive payment is actually related to the performance, I just wanted to add that.
Anantha Narayan	Okay thank you. That's helpful.
Pratibha	Thank you very much sir. Next in line we have Mr. Manoj Singla from JP Morgan.
Manoj Singla	Yeah hi, thank you. Congratulations on a good result. My first question actually relates to the offshore side of revenues and as those referred some time back, revenues seem to have declined roughly 2.5% sequentially. Coming back to the fact that last quarter you also had decline in revenues, and given that pricing has gone up, volume decline will be more than then the revenues. Can you throw some light on what is happening here, and what do we expect especially on the volume side going forward, especially in offshore?
N. Chandrasekaran	One of the reasons the offshore revenues has gone down again – what impacted the onsite growth – is that general contract which has obstructed the onsite revenues positively has affected the offshore revenue negatively. So that is why you probably see that in the offshore revenue. But overall if you really see, the deal flow is pretty good. We have announced quite a few deals, some of which we shared in the results announcement, and also are working on quite a few healthy deals. So we think that there is going to be a volume led growth in the coming quarters.
S. Mahalingam	You know, Manoj, one of the points that Chandra had made earlier was also in relation to the fixed price projects, due to which the onsite portion has gone up slightly right now, and that will trigger volume growth as far as offshore is concerned as we go along. So we don't really expect too much of a problem.
Manoj Singla	Yes sir, and can you just tell us about the GE business in dollar

terms, how much was it down quarter on quarter and how is it tracking now?

N. Chandrasekaran — GE business is about 13.1% of the international revenues now going from 13.9%. In terms of the absolute numbers the GE business is pretty steady. There is a marginal increase or pretty steady, quarter on quarter basis. It is not growing at the same pace at which the rest of the business is growing and that is what we would expect. So we expect that the GE concentration as a percentage of the overall revenue will continue to decline at least for the next few quarters.

Manoj Singla — Thank you. And sir very lastly, on the fringe benefit tax, how much was the impact this quarter and what do we see on the tax rates going forward? Thank you.

S. Mahalingam — The fringe benefit tax, we have provided 9 crores of rupees in this quarter. As can be expected, there is very little change that we can make other than in the superannuation area as far as fringe benefit tax is concerned. We will give some information if there is going to be any change as far as superannuation practice at TCS, which as you know covers almost everyone in the company.

Manoj — Sure Maha. Thank you.

Pratibha — Thank you very much sir. Participants are requested to kindly restrict to one question in the initial round. Next in line we have a question from Mr. Sameer Goyal of Anand Rathi Securities.

Sameer Goyal — Yeah Hi. Actually I just wanted to know, some of the industry practices are consistently showing some decline in numbers, could you elaborate a little bit more on that and strategy going forward? And b), again on the tax rate, we have you seen some increase in tax rate in the current quarter, would we be seeing this as a trend going forward, are we losing some of the tax benefits going forward?

N. Chandrasekaran — With regard to you first question in terms of the industry practices, by and large we are seeing a healthy pipeline in all the industry verticals in which we operate, but some of the industry practices are new and they are picking up, for example Life Sciences and Healthcare, or Utilities. Banking and Financial Services which is established is continuing to see more traction. So, since we are adding some additional industry practices, we are definitely going to see some volatility in terms of the percentage of revenue that is coming from each of the industry practices, but there is really no cause of concern, whether it is Banking Financial Services or Insurance or Retail and Distribution, or Life Sciences, these are all practices which are growing. Telecom, by and large if you take the service provider segment or the equipment segment, it is stable and there are not specific larger deals. The deals are more smaller sized deals at this point in time. So that is only comment I would make with respect to telecom. And regarding the other question…

S. Mahalingam — As you know, we are covered by 10A, and there are very small units which have moved out of 10A, two units moved out of 10A last year. Total impact on TCS from a number of people perspective is about 2000. Going forward there is nothing that is happening until 2009. So we are not expecting any change as far as this is concerned. Any new facility that is coming up, if it is any major one, it will obviously be covered by the SEZ and the provisions connected with that.

Sameer Goyal — So the tax as we have seen in this current quarter, 16-16.5% effective tax rate, would that be a trend going forward?

S. Mahalingam — I think that could be the trend that would be followed as far as the current year is concerned.

Sameer Goyal — Okay, thanks a lot and best of luck.

Pratibha — Thank you very much sir. Next question comes from Mr. Rishikesh Patel of ICICI Securities.

Shekhar Singh — Hi, this is Shekhar here. I just wanted to know, you have indicated some very strong recruitment in the coming nine months, almost 15,500 employees, of these how many will be in the BPO area?

S. Padmanabhan — Out of the 13,500 additions in India, 2000 people would be added in the BPO space.

Shekhar Singh — Okay. And this 4000 employee BPO center which you have indicated as a confirmed order, when is it expected to ramp up to the full stage, and what is the sort of profitability that you are expecting in the BPO business?

N. Chandrasekaran — See BPO currently has about 1900 people, and what we have done is we increased the capacity for about 4000 people between the three centers, which is, one in Mumbai, one in Chennai, and we also have facility in Bangalore. The facility itself is already coming up and the infrastructure is ready and some of the interior work is going on. The facility is getting ready as we speak, but the ramp up in terms of all the 4000 seats will take time, but we have started doing it with three specific customers, and we expect that it will take about 18 months at least.

Shekhar Singh — Okay.

N. Chandrasekaran — Maybe about 18 to 20 months. And as Paddy mentioned, we will definitely take in additional 2000 people, and in some cases we also use business associates selectively.

Shekhar Singh — Okay. Lastly just wanted to know like some of your peers have experienced ramp down by a few large clients, I just wanted to find out in case of TCS have you seen something of this sort happening in any of your large clients?

N. Chandrasekaran: If you take our large clients, the business is extremely robust, and the business is continuing to grow. Earlier there was a question from, I think it was Manoj, on GE. GE being the largest customer, the size pretty much is flat or marginally growing, but apart from that all the other customers are pretty healthy.

Shekhar Singh: And none of your customers plan to setup their own India dedicated centers, and therefore they will be ramping down from the other vendors?

N. Chandrasekaran: I think, you know, it is very difficult for me to comment on the strategy that any particular customer may choose, but all I would say is that our pipeline is healthy with all our customers, and it is quite robust.

Shekhar: And lastly, if you can just indicate – this China initiative of yours, and what is the sort of revenue expectation from this China initiative? Thanks a lot and all the best.

N. Chandrasekaran: Girija, are you there on the call?

Girija Pandey: Yes, Chandra. China initiative was signed on 30th of June. We have a three-way joint venture, Chinese government entities, Microsoft, and ourselves, with TCS as a dominant partner and the other two as strategic minority partners. The entity is expected to look at broad-based services in BPO, IT services solutions across China in the domestic market as well as in the global market. We are expecting, at the moment the numbers have not yet been firmed up, our business planning team is working on it. We are expecting the entity to start in the first quarter of calendar 2006.

Shekhar Singh: Okay sir. Congratulations on a very good set of numbers. Thanks.

Pratibha: Thank you very much sir. Participants are requested to kindly restrict to one question in the initial round. We have our next question from Ms. Mitali of DSP Merrill Lynch.

Mitali Ghosh: Good morning and congratulations on a good operational management this quarter. My question is really on the revenue growth where you know we have been discussing the outlook is quite robust in terms of the revenue flow. But if I look at the last quarter as well as this quarter, volumes have really not grown by more than 2-3% sequentially, and this compares with volume growth of definitely upwards of 6% in the previous quarters, and we have seen a similar performance in the some of the other majors as well. So what I am wondering is that if we could discuss some of the factors which are key to volume growth and how they are panning out, one is global vendor competition, two is in terms of the larger accounts that you have, you did touch upon it, but essentially are you seeing some plateauing there? And thirdly in the older services, the application development and maintenance and package implementation kind of services, are we seeing some sort of change in growth trends there?

N. Chandrasekaran There are multiple points, Mitali here. First one is, we talked about the large win that we announced in the results. We are also pursuing on a couple of more large wins. The closure of those wins, we expect to happen in this quarter definitely. And the closure of those wins kicking in of the transition so that we can start to ramp up this year, later part of the second quarter and in the third quarter is very critical. The size of the deals are also increasing, not only in the deals that I mentioned. Also in UK I mentioned a couple of cases, where the size of the opportunity is large, and as a result the sales cycle is also taking long. So the closure of these deals in a timely manner is one factor, that is critical, and we need to carefully watch it and ensure that we close it on time. The second thing is regarding your question on application services. I think these large deals mean a good amount of growth in the application management services, whether it is application maintenance, support, development, production support, those kind of activities, so all these large deals contribute significantly to that.

The second question on the enterprise solutions, actually that practice is picking up as we speak. What happens is that apart from the package implementation services, the maintenance and migration and integration of these packages is also becoming very important. The only thing is those deals are few million dollars or few 10s of millions of dollars, so you need to do more number of deals in those situations than one large application outsourcing deal, that is the factor. Then the growth engines we talked about, whether it is BPO, assurance services, then the infrastructure services, these are tools which we effectively use in order to penetrate the large existing accounts. If you see some of the statistics that we have given in the presentation, we have added a good number of clients for these practices. When we say we are adding good number of clients for these practices, it means we are selling these services into our existing customer base. So it is a new client for that practice. So the more we do that or the cross selling is good. We see our cross sell ability is picking up. So these are the factors which give us positive indications, but we need to carefully monitor and close these in a timely fashion.

Mitali Ghosh Why has it not really been translating into growth in the last couple of quarters in terms of volume?

N. Chandrasekaran We have closed some of these deals this quarter, so they will translate in the subsequent quarters Mitali.

Mitali Ghosh And follow-on on the large deals that couple of them that you have mentioned, if you could take us through how the economics of these deals work compared to the more typical smaller duration projects that we have been seeing so far?

N. Chandrasekaran The advantage of the large deals is that once you close the deals, and then you have got a good governance structure, we definitely have significant productivity benefits in those deals. You start at a particular level and you are able to operationally improve. And also it depends on the structure of the deals whether you have structured all the deals as time and material contracts or you have got the option to convert some of them into fixed price. The situations vary from contract to contract. In our case, I think there are two or three levers which help us to achieve higher productivity in these kind of deals and we continuously focus on those.

S. Ramadorai — Just to add to what Chandra is saying Mitali, some of these large deals are global deals and do not stand just one location or one geography, so it involves certain legal due diligence, legal implications to operate in multiple countries. It would also involve some of the employees of those organizations becoming a part of that. So the whole transition and our ability to understand and enable it, and give convincing comfort to the customers who are going to be dealing with us will necessarily involve time, and there is only a certain amount of push we can give to accelerate it, but at the end of the day both the parties have to be completely comfortable that the business is not at risk. And that's why these get delayed and we have got to anticipate that and factor into our business plan.

Mitali Ghosh — If I am understanding correct, for several months, maybe like the first year of the deal these could actually not really be profitable?

N. Chandrasekaran — I am not sure about the first year. Typically, what happens is that in very large deals, customers definitely want some relief during the transition time. The logic I think I am sure you are aware is during the first transition period we are already having a cost on the current set of people who are doing that work, so they don't want to incur double cost because it is against their budgeting that they have already done. So you need to work out an innovative structure, contractual structure, by which you are able to give some cash flow relief to them during the period of transition, and certainly it is not for a year.

S. Mahalingam — And also we will monitor the cost fairly effectively.

S. Ramadorai — And it will always be a multi-year, it's not one year, and it will ramp up also differently, and I think we have to manage both the costs and the revenue flow and what does the client at the end of the day buy-in.

Mitali Ghosh — Sure, I think that is very helpful. Last quick question to Paddy, if I may, is on the onsite compensation essentially being restructured, you had mentioned yesterday in the press meet that some 1.5 to 1.8 percentage points impact on gross margin, I just want to be sure that, is this something that we are going to see impacting margins in the next three quarters or is this, hereon the margins should not change on account of that?

S. Padmanabhan — This is year-on-year impact. If everything else is stationary, this is the contribution to the margin that will happen. And (of) this 1.5 to 1.8, 70% will go to the gross margin and the 30% will go to the operating margin...

Mitali Ghosh	Okay, maybe I will discuss this with you offline.
Arjun Marphatia	I think we have the last 10 minutes only, so participants are requested to ask only one question each please.
Pratibha	Thank you very much madam. Participants are requested to kindly restrict to one question each. Next in line, we have Mr. Trideep from UBS.
Trideep Bhattacharya	Good morning and congratulations on the results. My question is regarding, if you could update us regarding the NHS contract and this $100 million deal, when do you expect the revenues to start kicking in please?
N. Chandrasekaran	Okay, on the NHS contract, we mentioned during the last call that the contract is going slow. As a result, the revenue flow to us is slowing down, and consequently we have taken a very, very conservative projection on account of the NHS contract for all the quarters of this year. And whatever is our expectation from NHS that we have been able to make in the current quarter. With regards to the $100 million contract, it has already commenced and revenues have started kicking in, including in Q1.
Trideep Bhattacharya	I see. Any significant timelines, like you know, contracts which close during this quarter which might not be there in the next quarter that one should be aware of, which could cause significant volatility in the revenues. I know you don't give guidance, but any out of ordinary completions which might cause volatility?
N. Chandrasekaran	The only contract which Ram mentioned yesterday in the press conference is that, which I would like to mention again. We are in discussion with a European customer on a very large contract. We expect to get that contract closed within the next 30 days, and so we expect the transition to start in this quarter definitely and some revenues kicking in the next quarter. So if there is a delay in that, we will keep you updated, during the next call, but apart from that there is nothing specific.
S. Mahalingam	As regards closing of large projects which we talked about, there is nothing that has had an effect here, which will not be repeated in the next quarter.
Trideep Bhattacharya	Okay fantastic. Again best of luck for large contracts as well as next quarter.
N. Chandrasekaran	Thank you.
Pratibha	Thank you very much sir. Next in line, we have a question from Mr. Hitesh Zaveri of Edelweiss.
Hitesh Zaveri	Hi. My question was on the client addition in the current quarter, you reported 68 numbers. Could you give some color on the quality of the

clients that you added, in terms of size, and geography, and verticals, and what kind of ramp up would you expect. If you could throw some light on this? Thank you.

N. Chandrasekaran The clients have been distributed across geographies, and the clients are also spread across verticals: banking, financial services, insurance, retail customers, pharma customers, also in some of the other verticals like transportation. Thus in terms of the quality of customers, our focus is about two or three basic criteria. One is customers who are in the Fortune 500, Fortune 1000 space, Global 500 space, and essentially customers who can give million dollars plus revenue, that is the focus. And also we look at the current set of customers who are sub-million customers and who can migrate to $3 million, $5 million category. So this is the criteria that we use and the client additions have been pretty much in line with that.

Hitesh Zaveri Just a point here that was about…can you share numbers, how many Fortune 500 clients that you have and how is the growth you are seeing from that segment?

N. Chandrasekaran Overall in the active customers?

Hitesh Zaveri Yes.

N. Chandrasekaran We don’t specifically say the number of Fortune 500, that we should be able to give data to your through IR.

Arjun Marphatia Hitesh I will give it to you on Monday.

Hitesh Zaveri Sure, thank you.

Pratibha Thank you very much sir. Next in line, we have Mr. Pankaj from ABN Amro.

Pankaj Kapoor Hi, congratulations on a good set of numbers. Just wanted to understand one thing, we are talking about a fairly large wins in this quarter which are typically going to have high onsite component in the initial phase, also seeing a healthy pipeline of such deals in the coming quarter, and since you are moving to a global compensation structure, onsite salaries are going to go up, so given all these things, do you see a pressure on margins going forward, essentially because offshore is not going to increase the way we are planning and the salaries are going to go up?

N. Chandrasekaran There are two bullets for this. Number one is the increase in the onsite salary cost has been very carefully planned and that has been budgeted for this year, for immediate quarters. Certainly on long term, there are multiple levers that we continue to focus on. One is definitely the offshore mix will increase from the current levels, definitely. There are two factors that will contribute, one is the fixed price projects, which have started, we definitely move those projects offshore. Second one is, some of the large accounts have still scope for good movement towards offshore. So that is definitely an area. Second one is, our value based offerings and, like consulting and other areas like RFID, etc., are coming in at premium pricing, and we will be cross selling those services and also across new customers at higher billing rates.

Pankaj Kapoor: On the consulting service, can you give some sense of how many people are there and what typically are the billing rates that we are able to get for such services?

N. Chandrasekaran: Pankaj, we don't share the billing rates as you know already, policy. The thing that we have done is that the consulting offering that has been carried out at TCS in the domain groups and in the technology and in the process areas are all being consolidated at this point in time so that we can have greater synergies and also increase the portfolio of offerings that we are able to offer to the customers. During the quarter or during the next quarter we will be able to share more details specifically on this.

Pankaj Kapoor: Fine, just one last question to Paddy. On the hiring that we are looking for the overall year, what is the lateral to fresher mix that you have in mind?

S. Padmanabhan: We are looking at 60% freshers and 40% laterals.

Pankaj: Thanks a lot and congratulations on the numbers again.

S. Padmanabhan: Thank you.

Pratibha: Thank you very much sir. Participants are requested to kindly restrict to one question in the initial round. Next question comes from Ms. Divya Nagarajan of Refco.

Priya Rohira: Hi, this is Priya here. Just wanted a comment on the sales cycle which you mentioned on the elongation in the UK geography, if you could comment on how this compares with that in the US geography, and more so on the transition management phase, and what are the additional investments in terms of the sales team which you are looking at on that side?

N. Chandrasekaran: In general, the difference between the large sales cycles in the US and Europe in general and UK also included in Europe is that there are employment issues that the outsourcer or the company which is outsourcing the deal has to very-very carefully plan in Europe, which is not there in the US. The regulations are much tougher in Europe and in UK, so the cycle tends to take longer. That's the fundamental aspect that you have to keep in mind. Apart from that, the usual things like the risks involved in transitioning very-very large contracts, etc. Then in terms of the investments, for all the large pursuits, what we do is to form a specific deal pursuit teams wherein we have to invest quite a bit in terms of building the prototypes and number of other sales things that are required in order to be able to demonstrate the overall proposal, so it is very-very specifically deal driven more than geography driven.

Priya Rohira	Okay. I also wanted to know on, what is common client base which your international business and that of international business of Tata Infotech would have in terms of, if there are any similar service offerings to the similar clients?
S. Mahalingam	We will come back later on that. We just announced the merger process yesterday and it is going to take a little time, so we will come back.
Priya Rohira	Fair enough, thank you and wish you all the best.
Pratibha	Thank you very much madam.
S. Ramadorai	Last question.
Pratibha	Sure sir. Last question comes from the line of Mr. Supratim Basu of Deutsche Bank.
Supratim Basu	Hello, thanks, good morning guys. My question actually goes back to this whole salary issue. Could you just explain once more for me please exactly what you are doing with international salaries and how that is going to affect margins for the next quarter, all other things being equal?
S. Padmanabhan	Okay. Starting July, as I explained, in the US all our people who are there will get a consolidated US salary. In the past, we were giving an Indian salary and a US allowance. Now from July, it will be one consolidated salary. Now the reason why this is done is many factors, we are aggressively hiring in our overseas geographies, and to make sure that we have uniform salary and compensation benefit structure for everyone in that geography, this is the method to do it. In terms of overall impact, as I said, for the year we have planned an India wage increase of 11% and overseas increase will be 4%, and that increase as a result of this consolidation is already factored into that 4%. We have already done that in Australia, we have done that in China.
Supratim Basu	Right, so basically you are going to roll this out in US from this quarter, that is for the September quarter and that will have an effect on your numbers for the September quarter, both for the quarter itself as well as back pay for the June quarter.
S. Padmanabhan	No it will have an impact starting July for the next three quarters.
S. Mahalingam	There will no impact on the April to June quarter.
Supratim Basu	Okay, there is no back pay involved in this.
S. Padmanabhan	That's right.

Supratim Basu	Okay, and just one clarification on this. From what I have understood in the past is that you would pay an allowance to the US employees, which would be net of taxes in the hands of the employee. Now when you are paying him a consolidated salary, is this going to be gross of social security and taxes?
S. Padmanabhan	Yes, it will be a consolidated salary like any other US employee, and this would take care of the 401 K requirement, the local social security, insurance, and a whole lot of retiral benefits and packages.
Supratim Basu	Right, thank you very much for taking my question. Good luck guys.
S. Padmanabhan	Thank you.
Pratibha	Thank you very much sir. At this moment, I would like to hand over the floor back to Mr. Arjun Marphatia for final remarks.
Arjun Marphatia	Thank you very much. Ram would like to conclude with his remarks.
S. Ramadorai	This is Ram again. Thank you very much for being on this call on a Saturday. A lot of you were questioning about our announcement of the results on Friday, whether we had something to hide, I think the results speak for themselves in terms of what we have presented. It was only when it was convenient to the board, we could meet together on a Friday evening. We had the press conference last night and this is the first analysts call. Any others one-on-one meetings will take place and we also have an analysts call on Monday for the international investors from the US and Europe. Thank you so much for being with us.
Pratibha	Ladies and gentlemen. Thank you for choosing WebEx conferencing service. That concludes this conference call. Thank you for your participation. You may now disconnect your lines. Thank you and have a nice day.

Note: This transcript has been edited to improve readability