"Tech Mahindra Limited Q3FY19 Earnings Conference Call"

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MANAGEMENT: **MR. CP GURNANI** – MD & CEO, TECH MAHINDRA LIMITED
MR. L. RAVICHANDRAN – CHIEF OPERATING OFFICER
MR. MANOJ BHAT – CHIEF FINANCIAL OFFICER
MR. HARSHVENDRA SOIN – CHIEF PEOPLE OFFICER
MR. MANISH VYAS – PRESIDENT (COMMUNICATIONS BUSINESS, MEDIA & ENTERTAINMENT BUSINESS), AND CEO, NETWORK SERVICES
MR. JAGDISH MITRA – PRESIDENT (ENTERPRISE BUSINESS)
MR. RITESH IDNANI – PRESIDENT (BUSINESS PROCESS SERVICES)

Moderator: Good day, ladies and gentlemen, and a very warm welcome to the Tech Mahindra Limited Q3 FY'19 Earnings Conference Call. As a reminder, all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. I am now glad to hand the conference over to Mr. CP Gurnani – Managing Director & CEO of Tech Mahindra. Thank you and over to you, sir.

CP Gurnani: Good evening, good morning, everybody. Thank you for joining the Tech Mahindra Q3 FY19 call. As you all have the results right in front of you, to me it is a milestone quarter for Tech Mahindra associates, it is a milestone quarter that we clocked $1,261 million run rate which effectively makes that we have finally crossed the annualized 5 billion revenue run rate.

The other salient point for me has been that growth has been robust both for Enterprise sector and Communications sector and you have seen that Enterprise business was up 4.1% QoQ, Communications business showed a positive traction and grew 2.6% QoQ. So overall, good results on margin front. L Ravi and his team have delivered 50 basis points growth on the back of high focus on automation, high focus on R&D with our automation tools, and in general I am quite happy with the way we have signed the deal and the way the quarter went down. More important to me is our digital revenue, our revenue through the TechMNxt platform, which as you know, is a combination of established companies like Altiostar or the Cloud RAN where we have either invested or collaborated to create a whole ecosystem.

Further, just a quick update is that Ritesh who was handling BPS and who has shown spectacular results, is now being given an additional responsibility of handling the platforms, all the digital platforms, software-as-a-service now comes under Ritesh Idnani along with the BPS responsibility. Manoj Chugh who has had a lateral move to Mahindra & Mahindra, has handed over his responsibilities to Jagdish Mitra. Jagdish Mitra is on the call but I consider his job to be more of harnessing the energy of the communications sector as well as enterprise sector because our world of connected experiences, connected solutions and connected market, can only happen when we harness our energies together. You have Manish Vyas, you have Harshvendra Soin -- our Chief People Officer, all of them on this call. Unfortunately, I would not be staying through the call but Ravi will officiate for me, and between him and Manoj Bhat, I think they will marshal the company resources to answer any questions you have regarding our company.

So, thank you guys again for the confidence and thank you again for seeing the company continuously deliver seven quarters of margin expansion and to some extent revival of the communications sector.

So, I am going to hand it over to Manoj to take you through the results in detail.

Manoj Bhat: Thank you, CP. Good evening to all of you. As you see from the numbers growth of about 3.6% and our revenues are about Rs.8944 crores, the cross-currency impact was about 80 basis points, so on a constant currency basis it is about 4.4% of growth. If I look at Enterprise, it grew 4.1% QoQ and Communications was up about 2.6% QoQ.

One thing to highlight is our Digital revenue moved to about 33%. So it is a 10% sequential growth. So clearly, our efforts and our strategies and our investments and also trying to put together the TechMNxt strategy in terms of offering the latest through collaborating with several partners is really showing out in the results in terms of growth in the digital revenue.

Moving on the margin side, clearly, margins went up about 50 basis points. I think predominantly it came from some improvement in our operational expenses on the SG&A side and also about utilization which was helping to the tune of about 40 basis and really some of the headwinds, I wont call them really heawinds, there are investments in terms of the deal ramp-ups because I think last quarter for example Q2 we had deal wins of $550 million and this quarter we have had deal wins of $440 million. So clearly, there are deals in transition. Second is of course the business mix has changed and this is causing some negatives on the margins which will start to come through when the cycle converts to revenue as we go forward and the transition is complete.

I think on the other points, other income was about 11 mn which has FOREX loss of about 11 million compared to a gain of 7.4 million in the past quarter. The primary reason is of course the sharp appreciation of the rupee during the quarter.

Coming to tax, the effective tax rate is down to about 18%. During the quarter we had some tax reversal which actually gave us a benefit of about 7.5% on the effective tax rate. So on a normalized basis, tax should be about 24.5% or so in terms of the tax rate.

Other than that, I think coming to the balance sheet side, our DSO was down about 5-days compared to the last quarter to about 107-days, consequently free cash flow was very strong at about 161 million which is about 94% of PAT. Cash and cash equivalents were about 1.25 billion as of December quarter. In terms of the hedging strategy, we continue to follow a consistent strategy and the hedge book total of about 1.56 billion. Just to reiterate, we go up to two years and we cover up to 75% of our exposure on the basis of a rule-based strategy and that is what we have been doing consistently for several quarters.

So from almost all perspective, it has been a quarter where there has been growth and there has been operational improvement and then we have also managed to actually do some improvements on the balance sheet side. So it has been a satisfactory quarter.

With that, I will throw the floor open for questions.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. Some The first question is from the line of Ravi Menon from Elara Securities. Please go ahead.

Ravi Menon: SG&A has seen a sharp dip QoQ in absolute terms as a percentage of revenue, I think it is the lowest since FY'15. Do you expect more SG&A leverage or should we now start seeing some based on marketing investments or something?

Manoj Bhat: Our endeavor, Ravi, would be to keep SG&A between 14% and 14.5% roughly. So it could be a marginal uptick, but the small quarter-on-quarter variations might happen. So, I think it will be a good assumption to take a range between 14% and 14.5% for SG&A because there will be some investments we make as we go forward.

Ravi Menon: ROW revenue seems up very strongly. How much of this is due to the 5G deal with Rakuten; is there anything else that is where it helps?

Manoj Bhat: No, actually, it is not one reason, if I look at the ROW revenue of course, you know Comviva, has a strong quarter, lot of the revenue comes from the ROW region. Second is I think as you correctly said deals like Rakuten, if I look at some of the other deals in APAC, there has been ramp-ups on that on the Communications side. So it is a combination of various reasons which is causing this ROW growth to be high, not one single isolated.

Ravi Menon: Attrition seems to be high at 21%. Cost seems like there was a wage hike for the rest of the employees also been rolled out. If you could give the margin impact of that?

Manoj Bhat: So our wage cycle in the June quarter, we have not worked out a number but Harsh if you are on the call, can you talk about some of the measures we are taking on attrition and while it is always a challenge to manage but I think from a planning perspective, we always assume a slightly higher number…….

C P Gurnani: Before Harsh comes in, I can only say is that to me wage hike will not be something which I would consider it as unusual phenomena. Sometimes during May or so, we would decide what the exact wage increase will be. We are obviously going to take the industry trends into account, but our overall focus on operating metrics, our overall focus on correcting the pyramid, our overall focus on rotation, I think should offset some of the cyclical expenses like wage hike. But Harsh, you may go ahead and share your part.

Harshvendra Soin: Thank you. So basically what we have seen is due to the upticks in the IT sector, this has led to an improved market where we see most of the organizations on high attrition level. We have our own detail SBU wise plan to address it; however, it is an important point to know that attrition of high performers is much-much lower, and I think that is a very healthy sign So that is what I mean probably we are dealing.

Moderator: Thank you. The next question is from the line of Sandeep Shah from CGS-CIMB. Please go ahead.

Sandeep Shah: Just wanted a breakup of the TCV of 440 million in the Communications and Telecom space?

Manoj Bhat: About 240 or so is Communications and about 200 or so is Enterprise.

Sandeep Shah: Manoj, the full year outlook for the Telecom, are we still saying flat to a marginal growth for full year because that requires as big as 7-8% QoQ growth in the fourth quarter for Communications?

Manoj Bhat: I think if you look at the currency movement, it is a bit of math there but clearly more than anything else I think we do expect that the momentum because of the deal wins there will be momentum going into the fourth quarter also in terms of the Communications vertical.

Sandeep Shah: Can you give some color in terms of the type of wins of this $240 million, is there a traction coming through 5G-related or is it more to do with what we say that preparation before the 5G is being rolled out?

Manoj Bhat: Sandeep, I will request Manish to comment on what we are seeing in the market and also the type of wins we have had.

Manish Vyas: Sandeep, thank you for the question. You are right, on the second one, these deals have two characteristics to them – One, they are widespread, in the sense they are cutting across our digital network and the software transformation footprint and two, in many ways they are all in preparation for the upcoming transformation, which is 5G and even before 5G whatever transformation will happen on both the network as well as on the business model side;because 5G is still being tried and trialed in many major tier-1 operators at this point, mostly in the US and few other parts. We still have to wait for some more time for the uptick on that one. But otherwise, these deals for all practical purposes are transformative.

Sandeep Shah: Last question, Manoj, where are we in terms of a margin journey? Can you give us some brief because do you believe the large deal ramp up cost may continue and your gross margin may continue at a current level or you believe that gross margin has an upside potential and the margin upward journey may continue going forward?

Manoj Bhat: Sandeep, as we had mentioned that there will be six to eight quarters journey of margin improvement andI think we have met that seven quarters. Our goal would be to increase the margins but clearly I think the levers will be different. So there is upside but of course there are some adverse pressures also. So to me I think the goal would be to try and see what we can do most. But given how much we have achieved, I think the pace might be a lot slower and much more muted and then we will keep updating you as the quartersgo by, but clearly the initiative we set off to do about seven or eight quarters ago, I think that is obviously showing results. In terms of some of the levers, of course, I think the business mix and yield management and as more digital revenue comes in, there are some positive levers there. The second is our portfolio company synergies and how that impacts our margins positively. And clearly when we look at the entire workfo rce pile as well as locations, more importantly the locations, onsite and offshore, those are things which we need to probably find some more. And of course on the other end is the wage hike. So I am not giving you a number but I think directionally that is where we are headed. That is how we are thinking about margins.

Sandeep Shah: Just a follow up, Manoj. Do you believe the onsite supply side issues which has been highlighted by many companies, will it be a new headwind even for Tech Mahindra looking at the demand uptick or you believe it is already a known headwind and we can manage it going forward?

Manoj Bhat: I think ultimately if I look at that full phenomena of talent, the recovery of that through increased realization, follow with a lag I suppose. As we go through that journey and this is in, I think isolated pockets, that is something which we will have to closely watch, but it is not a very severe impact for us so far.

Moderator: Thank you. The next question is from the line of Ashish Chopra from Motilal Oswal Securities Limited. Please go ahead.

Ashish Chopra: Manoj, firstly, could you throw some light on roughly a billion dollar odd worth of deals that you have won in the last couple of quarters as to how would it split between maybe your largest customers versus smaller ones or the new ones because I think despite the ramp-up we do not see that kind of growth in the top-5 in this quarter, so just wanted to know how these deals will split and what can we expect from the top customer bracket?

Manoj Bhat: I do not have a full analysis in front of me, but let me try and give you some color. Clearly, in our top customers there is going to be a pattern which will be different QoQ I would presume, but clearly lot of the wins have also come outside the top customers and that is a quick answer I can give you but unfortunately I do not have all the billion dollar deals worth but Manish or Jagdish, you want to give some color if you have in terms of where do we see opportunities, Jagdish, on the Enterprise side and maybe Ritesh can follow with something on the BPS side?

Jagdish Mitra: From our perspective, Ashish, there are a few areas that I think we have seen a trend and as Manoj said, cuts across existing as well as new customers, for example, lot of this is either digital enabled transformation or digital at the heart of it. So depending on the vertical or the industry and the market that we are operating in, it is a different flavor, right. So Manufacturing has a lot of flavors in terms of factory of the future, there is smart workforce and so on and so forth while Healthcare, Banking and Retail have lot of focus on the analytics related to the retail customers experience. So, we had even fairly large deals coming in from verticals which are not exactly amongst our top-3, probably logistics and utilities and so on and so forth. So it is actually quite wide spaced. It is driven primarily by digital transformation and now slowly we are starting to see that the digital transformation deals are no longer small but starting to be at the core and fairly large, large in the sense they are sometimes coming close enough to double digit million dollar deal.

Ashish Chopra: If I may ask this maybe in a slightly different way, deals are actually bifurcated between both large accounts and the smaller ones. Would there be a couple of accounts maybe in our top-10 list which are maybe sizing downwards which could explain the offset from them or would it largely be broad-based traction across?

Manoj Bhat: The nature of large accounts is they grow in step function. So you will have periods where one or two accounts might not be growing. So that is a mixed portfolio. That is what I am saying that from a perspective of largest accounts every quarter you will see some slightly different behavior but overall I think we believe that whatever we are doing in terms of digital, in terms of our run-change-grow growth strategy as well as in terms of overall growth, I think it is balancing itself out across the portfolio.

Ashish Chopra: So based on the order book now that you have after these deal wins, how should we look at the trend in headcount going forward especially on the base of a fairly sharp cut over the last couple of years in software headcount but a significant growth in BPO, could we expect more of the same or do you expect the headcount growth to be more balanced across these two segments?

Manoj Bhat: I will ask Ritesh to step in on the BPS please because obviously BPS has done extremely well for us. Ritesh, do you want to talk about what is happening there and then how are we thinking about the question around future growth and will it be headcount led or not?

Ritesh Idnani: Thanks, Manoj. So, thank you for the question. I think BPS over the last two quarters has had exceptionally strong growth, we have had double-digit sequential growth of 16% in Q2 over Q1 and about 11% in Q3 over Q2 QoQ and while continuing to maintain industry leading profitability. I think the key thing to bear in mind there is that it is a strong validation of a value proposition in the marketplace, particularly around being a leader in customer experience. And given that that is a board room priority, our proposition of using technology to drive transformation in the front office and acting as the catalyst for one office transformation itself is resonating well in the marketplace. That is resulting in us winning business both from large Global 2000 companies as well as digitally native organizations as well. One of the things that we are seeing in the current technology shifts that are playing out in the marketplace is also a share shift away from pure play contact center companies who may not necessarily bring the technology to that extent. What does that translate in terms of headcount? We are creating what is digitally human workforce. So while on one hand this quarter we added upwards of 4,000 people QoQ and close to about 8,000 people over the last two quarters in the business, we have also continued to expand our footprint of bots in the workforce where we are more than 4500 bots in the workforce today and given the productivity that these bots bring to bear which is about 2.5x the human productivity. That is a substantial part of our total organization. So today we are close to about 44,000 people in the workforce. What I do see is that the demand environment continues to be robust as people keep looking for opportunities to infuse technology in the way they run their front office but also their overall one office including mid and back and they are looking for technology to play a pivotal role to drive the transformation. I think TechM and the BPS organization there has a pivotal role to play in facilitating that. And that is something that I think we are being made beneficiaries of.

Moderator: Thank you. The next question is from the line of Pankaj Kapoor from JM Financial. Please go ahead.

Pankaj Kapoor: Manoj, just wanted to get a sense in terms of our headcount addition in the IT Services side. It was down almost 750 QoQ. So, I was curious to understand what is happening there – is there any kind of one-off thing which happened in terms of transfer out of some headcount that you had acquired earlier which led to this kind of a fall? The related question to this is that given the utilization which is now running almost at 83, 84%, how do you see the headcount scenario going forward?

Manoj Bhat: Thanks, Pankaj. I think on the headcount clearly there are two trends playing out. While the headline number is the headline number but I had mentioned this a few quarters back also that as our automation platform starts maturing in each of these customer engagements, we will start seeing some benefits of that coming in terms of resources and people being available to be redeployed. So some of that is happening. Second thing is of course the decline might be a temporary timing kind of thing. There is no specific event which comes to mind. So, on an overall basis, from an IT perspective, we do believe that we have done some work on the automation side and our platform is installed across most of the customers, but clearly there are some more benefits to come through. And the second thing is that from a model perspective we have also been using subcontracting as a balancing factor and that has been historical also. So I think that is the way to look at it that we are managing this through a combination of both of these.

Pankaj Kapoor: But if I look at the subcon cost also, that seems to have come down QoQ which is quite in contrast to what the other players are seeing. So again was curious to see what you are doing different over there?

Manoj Bhat: On the subcon cost, I think the way we classify it is there are obviously resource-based subcon and there are task-based subcon. So in many of our implementation kind of engagements, there might be turnkey subcons, but there will be some quarter of fluctuation on that but if I really see overall maybe our subcon as a resource base might have gone up during the quarter.

Pankaj Kapoor: On the margin outlook, so you mentioned the headwinds of transition in the large deals which will continue. Any kind of quantification around that like where you see margin stabilizing, what could be the kind of a target margin band that you are looking at which you will be more comfortable with on a steady state basis?

Manoj Bhat: Pankaj, we do not want to obviously guide any margin band but clearly from our perspective, it is something which we keep continuously working on to find opportunities which can obviously benefit the customer and benefit us. So I do not really want to put a number to that. But clearly, as I said, it is both growth and profitability are equal weight I would say, as we think about the quarters going forward.

Moderator: Thank you. Our next question is from the line of Divya Nagarajan from UBS. Please go ahead.

Divya Nagarajan: Most of my questions have been answered, just a follow-up with headcount question on software versus BPS. This is a trend that we have seen in the last several quarters that there is consistent drop on the software side and increase on the BPS side. How should we think about what that means for your mix of businesses between these two segments? That is question number one.

Moderator: Divya, sorry to interrupt, your voice is not clear.

Divya Nagarajan: Yes, so my question was on the trends in headcount between software and BPS, with decline in the former and increase in the latter for the last several quarters. My question was for the medium-term to long-term what does this mean for your business mix, could you help us understand that. Question number one. And two, the outlook that we are seeing for contracting, I think the last few quarters they have definitely seen a pickup in contracts, how do you view that continuing against the macro backdrop that we are seeing right now, especially in some of your markets?

Manoj Bhat: So, Divya, I think on the headcount question, I will refer to the revenues, BPS has grown very nicely, and even IT has grown for us in terms of revenue. And as I said, it is a balancing act. So over a period of time I definitely see this headcount going up as the revenue goes up. But it is something which from our perspective, as I said, there are two or three factors, one is, what the redeployment possibilities; second is, how do we think about our partner ecosystem and our collaborative efforts through them. And then finally in terms of our campus recruitment program and people added there and how do they come into workforce. But over a period of time I do see it increasing. So, on the other question in terms of market and deal momentum, I think the best thing would be I would ask Manish probably to talk a bit about farms and how he sees the market from that perspective and what our communication service provider is thinking about in terms of investments. And maybe Jagdish, if you could give a flavor, on the other side of some of the other verticals. Manish?

Manish Vyas: Sure, Manoj. Absolutely, I think Divya, the investment cycle in telecom is largely built around continuing to strengthen their network. I think everybody without exception realizes that there is still enough value, enough oil in that pipe. And with 5G and more dynamic type of networks coming through the door, clearly everybody is focused on ensuring that they do not dry that investment out. So that does not necessarily mea n massive new CAPEX, there will be lot of repurpose and some new CAPEX that will happen. So second type of investment that is coming, and some of the deals that we are signing, are indicative of that, are about putting together a digital platform for customer management, for supply chain management, for device and inventory management and essentially entire ecosystem that will have to change around a digital footprint. And the third is around automation, because there will be a very strong need to continue to drive the cost down in major markets where the revenue growth in the industry is still going to be sluggish , at best. And hence they will have to find better free-cash-flow and better OPEX type investment. Which, the good news is, if you read all these three things that I said reverse, actually aligns with what we call as run, change and grow, in the reverse order, which is to find more cost via automation, to find more speed and velocity of transformation and to find more growth opportunities via leveraging and harnessing the power of their core asset, which is the network. There of course are other investments which are in the value added services space, whether it is IoT or the industrial internet, but they are more very specific, I wouldn't call a spe cific trend that is cutting across the industry, it varies between company to company in terms of their relative strength and vice-versa. I hope that answers your question, Divya?

Divya Nagarajan: Sure.

Jagdish Mitra: Similarly on the enterprise side, I think obviously it has different flavors, as I mentioned earlier, that are driving business clarity. So for example, in manufacturing a lot of smart products for consumers, there is definitely a direction towards shrinking the whole product development cycle which is obviously requiring significant amount of investment which is smart products. And actually, we are well-enabled, I think, in some of these because of our investment into companies like Pininfarina and BIO, especially Pininfarina part of designing what is connected products and smart products. And that we think will probably help us in good stay. On the workforce, I think there is a significant amount of work that is happening, especially data on some of the manufacturing. Analysts suggest that about 150 million of blue-collar workers will retire in the next 10-odd years and about 50 million will be replaced from there by automation. So there is an opportunity there to come in with very significant amount of machine analytics, the digital trend and so and so forth where investments are. And similarly, in Banking, Financial Services, or Insurance, for example insurance seeing world-wide low interest rates, which means things like digitized underwriting, automated claims processing, again, some of these things we are sort of prepared to see that we will be well prepared to give that service and industry requirements and so and so forth in themes like Retail and Healthcare. So, you can feel that when we talked about 3-4-3, we had called out a few transformational bets, and I think those transformational bets in terms of customer experience, in terms of platforms, in terms of the ability for the core networks is starting to play in all aspects, they take care of work because in enterprise they are starting to play a role.

Moderator: Thank you. Our next question is from the line of Vibhor Singhal from Phillip Capital. Please go ahead.

Vibhor Singhal: Most of the questions have been answered, I just wanted to get a bit of feedback on the HCI acquisition, how is that panning out? I think last couple of quarters we have seen some ramp down in that, so are we close to bottom on that or there is still pain left in that?

Manoj Bhat: So, Healthcare vertical has grown for us and of course HCI is a big part of vertical so it has also done well this quarter. So as we said before, I think the ramp down of those deals were more of a lifecycle nature. And as new deals came in this quarter we have seen the growth come back.

Vibhor Singhal: And you believe that would be sustainable until of course, I mean, barring the cyclicality of the businessthe ramp up that we saw in this quarter should be sustainable?

Manoj Bhat: So, yes, I think it seems so. So the question I would probably answer differently, fundamentally there is nothing wrong with the business, we actually saw huge amount of ramp-up. There was some volatility because some of the projects ramped down and it will come back up and that is what we had said and we maintain that, from overall thesis and from overall synergy perspective we strongly believe over a period of time it will do well.

Vibhor Singhal: Just my last question, Manoj, if you could basically, I know we would plan the wage hike as you mentioned in June quarter, so there is still some time left for that. But given that our attrition has been in the high, I mean, more than 21% in this quarter, do you believe that this time around you might have to do with a bit of more of wage hike on the higher side, given that we have had kind of a stagnant period for the last two to three years?

Manoj Bhat: So, I think I will have to defer answering that because we are doing a full deep dive into that. And then as we mentioned probably the decision will be later in a few months in terms of what we need to do exactly. So I will just hold off on answering that.

Vibhor Singhal: Okay, so if I can ask that in a different manner in terms of 21% attrition, does that worry you? And if that is yes, then apart from let's say doing the deep dive for salary wage hike, are we contemplating some other measures?

Manoj Bhat: So, I think if I look at our historical attrition rate, we have hovered between 17% and 21%. So, 21% is obviously I would say a zone which is at the high end of the range. So clearly, I think, and as Harsh mentioned sometime back, the first cut analysis, the attrition on certain type of people is much lower. And as with anything else, when something reaches the upper part of the band it is definitely a cause for concern. And from a talent perspective, would I ever say that talent availability is easy and we can easily manage? It has always been a challenge, it will continue to be. So, having said that, it is at the top-end of our range and we will have to do the proper analysis and then take the call on what we need to do going forward to bring that down.

Harshvendra Soin: And just to add, basically what is important was that it feels obviously at the higher end so we are doing a deep dive. But it is important to also note that it is heartening for us that our top performers have been on the lower end on the attrition, and that is an important data point for all of you to also note down.

Moderator: Thank you. Our next question is from the line of Srini Rao from Deutsche Bank. Please go ahead.

Srini Rao: I have two questions. One, does the issue of Huawei ban, does it have any impact you are seeing on potential 5G deployments? So that is my first question to Manoj. Second is to Manish, your DSO obviously historically also has been higher than your peers, A, is it on account of the different business mix or your DSO is comparable to your peers in verticals like BFSI? So any feedback on that would be helpful.

Manoj Bhat: So let me handle the DSO question first, and then hand it over to Manish. You are right, I think the vertical mix and the geography mix plays a role in the DSO. So if I look at the communication vertical is one vertical where the credit periods are longer than some of the others. So, short answer is yes, but if I look at like-to-like and some of the other verticals, I think the DSOs are more comparable. Having said that, can we improve? I am sure there is a fair possibility of improvement, and that is what we are working on, this quarter we have improved it by four or five days and hopefully with all our efforts we will try to bring it down a bit more going forward. Manish, you want to pick up the question on Huawei and 5G and what could be the potential impact?

Manish Vyas: Absolutely. I think the industry players and their relative positioning with different market, different customers is always in that state of evolution. It is not complicated by of course, rather made interesting by the geopolitical scenarios as well. But that said, from our vantage point, we have always taken pride that we are a technology agnostic company, product agnostic, integration and platform company. And we partner with almost all the major technology providers in the network business, with of course in some areas we have taken our own investment approach so that we can have a seat at the table as well, right up front as the technology roadmaps are happening. So yes, it is an interesting time and it impacts some market than the others, particularly the market that are likely to join and adopt the 5G rollouts earlier. But one market where it probably will not have an impact either ways is going to be US, because in the US we have not had much of a presence of some of these companies. And US is likely clearly to be the first one to adopt 5G with the trials going on as we speak at this point. So, I think the vendor base and the industry players, that situation is evolving, not just between this top five or six traditional OEMs, but also the disruptors that are coming through the door. For example, in Japan with Rakuten, the entire RAN is not built on any of the five major established OEMs, but a completely new software-based RAN company like Altiostar. So I think it is an interesting scenario. I would request you to join us and observe this very closely as we see this evolving and we will definitely have a good seat at the table as this thing evolves.

Moderator: Thank you. Our next question is from the line of Sumeet Jain from Goldman Sachs. Please go ahead.

Sumeet Jain: Firstly, I wanted to understand around the BPO space. As you mentioned that you are using lot of RPA tools and automation in your latest BPO deals, so generally we have seen that leads to higher revenue per employee over the several quarters. But if I look at your revenues in the BPO space and the BPO professionals that we provide, your revenue per employee in that space has largely been in the range of around $9,000 to $10,000 per employee. So can you comment like is there a significant room for improvement out there or it is already at the maximum efficiency level?

Manoj Bhat: Ritesh, you want to pick that up?

Ritesh Idnani: It is a great question. I think some of it is a function of the business mix that we have, so we do have some percentage of our business that comes from the markets such as India as an example where the typical price realization per employee tends to be on the lower side, relative to what you get in markets outside of India. And to the extent that you end up having that, that does have a bearing in terms of the overall revenue per employee realization itself. Now, that being said, one of the things that is very conscious in the way we are also executing several of these deals is to bake in a committed transformation benefits on account of technologies such as automation, point solutions, platforms, etc, which are baked into the overall proposition going to clients itself. So, what it does help is even if the revenue realization at a point in time ends up being lower, your EBITDA ends up being accretive as a consequence of that. So, I think there are a couple of factors that are playing out simultaneously at this point in time. That said, I do think that over a period in time as our business mix shifts towards getting more and more revenue as well in other markets and also more expansive use of technologies as well, I do think that the revenue realization per employee will also continue to move upwards.

Sumeet Jain: So, maybe can one assume that within the BPO space your offshoring component is a bit higher and probably because of that the revenue per employee is lower but your profitability is higher?

Ritesh Idnani: That would be correct at this point in time.

Sumeet Jain: And secondly, Manoj, wanted to understand from you, you said that subsidiary portfolio level improvement is still one of the levers for your margin improvement. So can you highlight to what profitability levels have your key subsidiaries achieved, particularly LCC, which had losses in FY18?

Manoj Bhat: So, Sumeet, I do not want to go into each subsidiary level. So, I think I will go back to something I said sometime back that if I look at that entire bucket it was probably at around mid-single-digit level and we wanted to get it to double-digit. I think we are getting close to that level and the next move would be that how do we move closer to the company level margins as close as possible, considering of course a location and type of service constraint. So, I think we have probably covered I would say 50% of the ground there and I think 50% would be left, that is just a qualitative assessment, if it helps.

Sumeet Jain: And any tailwinds you are seeing for LCC, particularly given the initial rollouts of 5G in US?

Manoj Bhat: Again, I will request Manish to answer the question in terms of network services, including LCC and how the rollout and the network rollout market is evolving.

Manish Vyas: I think the simple answer is yes, we are starting to get engaged in several conversations. In fact, we are in the advance stages of closing smaller deals, but it will be a strategic deal because it is in that what is called the fixed wireless access area which in many ways is going to be the corner stone and foundation of lot of 5G rollouts. However, we are also being selective about where we play, who do we work with, what kind of terms do we pick up, but the short answer to your question is that there is attraction in that space.

Moderator: Thank you. Our next question is from the line of Ashwin Mehta from Nomura. Please go ahead.

Ashwin Mehta: Just one question in terms of the BPO, our segmental margins in BPO are better than our IT services margins which is not the case generally, so just wanted to understand specially in the backdrop that your headcount addition is higher than your revenue growth, what is the nature of work or is there a particular skew in terms of verticals which is helping you make margins better than your IT services margins here.

Manoj Bhat: Ritesh, let me pick that up first, just give some context and then I will hand it to you. So, I think if you look at the classification within IT, a lot of our subsidiary companies and so on and so forth come in. So I think if I really look at it from that perspective, it is one of the reasons. But having said that, the reason for our BPO margins and how we have introduced automation, RPA and what are the tools to drive margins, I will leave Ritesh to answer that.

Ritesh Idnani: So, I think Ashwin you are going down the path of some of the value levers that we are aggressively looking at towards driving industry leading profitability. Automation certainly is one part of it. But we are also constantly looking at opportunities in every deal to try and drive the transformation so as to do the right thing for our customers. And what that means is that there are opportunities to cannibalize potentially our own business in the hope of getting more volume and taking share from our competitors, that hypothesis for us has been playing out extremely well in the market place. And particularly in an environment where there are technology shifts like what we are witnessing right now in the sector, we do find that there are a lot of pure play companies who may not be going aggressively on leveraging the technology and maybe on defense. And from our standpoint our strategy of being on offense out there and introducing this proactively and doing the right thing for our customers is certainly resonating with our client base, and that in turn is driving incremental volume growth as well, which in turn therefore improves profitability as well. That said, I think the second part of your question was that, which verticals if any are we seeing the growth? I think what you would find is that the growth is coming broad based, we are seeing certainly in some of the verticals, the TechM corporate level like as communications media and entertainment or Retail CPG or Banking Financial Services and manufacturing certainly continue to be big driver. But at the same time we have also seen significant success with some of the digitally born companies as well and all of that is also being helping us in terms of significant expansion, which in turn also creates some operating leverage which in-turn also improves profitability also.

Ashvin Mehta: Okay, fair enough. And just one follow-up, Manoj, to one of the questions that was asked, your standalone EBIT margins have touched close to almost 18.8% levels, so would you say the incremental improvements on margins will largely be coming through subsidiary profitability improvement or you think there is more scope of improving the standalone margins also?

Manoj Bhat: I think I answered the margin lever question and I spoke about some of those. So instead of trying to look at it standalone, consolidated, subsidiary, portfolio, I think there are those two or three levers which I spoke about at the beginning of the call, I think leave it that because these are just structures which are legal structures but I think our delivery models are more integrated today than ever before. So I would not like to look at it as consolidated versus standalone versus subsidiary, etc.

Moderator: Thank you. We will take the last question from the line of Nitin Padmanabhan from Investec. Please go ahead.

Nitin Padmanabhan: Two questions actually, the first one is, Manoj, if I just look at same time last year this time around our deal wins I presume would be at least 50% higher than last year if I look at this quarter Q3 and Q2 put together. And in that context if I look at our utilization rates and the sub-con that has come down with the higher volume that we anticipate. Do you think that there will be any execution issues or do you think that is taken care of?

Manoj Bhat: So, I think in our estimation, in our planning, we do not foresee any execution issues coming through. And of course, the surge for talent and getting the right capabilities is always going to be a challenge, but I do not think there is any specific challenge which we foresee as we think about executing on these deal wins.

Nitin Padmanabhan: And just one more if I may, Manish, do you think going into this calendar, do you think opportunities around M&A related integrations will pan out and how are we placed within them?

Manish Vyas: Yes, I think I expect M&A related integration activities will pan out at least in one or two major ones that have happened and are also in the works at this point. And the type of work is going to be very synergic with what we have done in the past, are going to be around migration, integration, business process, rationalization, and in some cases now that we are doing networks, also in terms of from farming of network assets and providing them inventory management support and so on and so forth. So yes, there will be some activities, I, of course will not be able to quantify or even give you a broad order of magnitude at this point because some of these deals are also embedded as part of the larger transformation objective that customer drives.

Moderator: Thank you. That was the last question. I now hand the conference over to the management for their closing comments.

Manoj Bhat: Thank you everyone for joining the call. I know that some of you might not have got a chance to ask the question, so please do reach out to us on phone or by email and we will try to get any unanswered queries answered. So thank you again for joining the call and good night.

Moderator: Thank you. Ladies & gentlemen, on behalf of Tech Mahindra Limited, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.

Note: The above transcript has been edited for better readability

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