

L&T Infotech Limited
Q1 FY17 Earnings Conference Call Transcript

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L&T Infotech

MANAGEMENT: MR. SANJAY JALONA – CHIEF EXECUTIVE OFFICER & MANAGING DIRECTOR
MR. ASHOK SONTHALIA – CHIEF FINANCIAL OFFICER

Moderator: Good Day, Ladies and Gentlemen, and Welcome to L&T Infotech Q1 FY17 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. And 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. Please note that this conference is being recorded. I would now like to hand the conference over to Ms. Sunita Iyer from L&T Infotech. Thank you and over to you, Ms. Iyer.

Sunita Iyer: Thank you, Mallika. Good morning, Good afternoon and Good evening, everyone. Thank you for joining us today to discuss L&T Infotech's financial results for the first quarter of fiscal 2017. The financial statements, press release and quarterly fact sheet are available in our filings with the stock exchange and in the investor section of our website.

From our management team, we have Mr. Sanjay Jalona – CEO & Managing Director and Mr. Ashok Sonthalia – Chief Financial Officer on the call. Sanjay and Ashok will give you a brief overview of the Company's performance followed by a Q&A session.

As a policy, we do not provide specific revenue or earnings guidance and anything said on this call which reflects our outlook for the future or which could be construed as a forward-looking statement must be reviewed in conjunction with the risks that the Company faces.

I will now hand over to Sanjay to discuss the results. Over to you, Sanjay.

Sanjay Jalona: Thank you, Sunita. Hello, everyone. And thank you for taking the time out to join this call. I am at our headquarters in Mumbai, I am joined here by my leadership team as well. This is the first time we are meeting on this Earnings Call, so let me start with a quick background before getting into the detailed discussions on this quarter.

In about 10 days I will complete one year with L&T Infotech, and what a year it has been. I am amazed everyday by the dedication and perseverance of the team and their passion to build a great organization. The Business-to-IT Connect and the real world expertise that LTI brings to its clients is unparalleled. In the last year we have embarked upon a journey to build next generation IT services company, focused on solving complex challenges at the convergence of physical and digital.

We have seen many significant milestones to this journey and I want to name a few of them. One, we inducted several new leadership team members, including our CFO, Ashok, and our Chief Operating Officer, Aftab. We also have Manoj Biswas who is Head of HR and our Chief Marketing Officer, Peeyush Dubey, all of whom are on this call. We have inducted two new Chief Business Officers, Rohit for Manufacturing and Siddharth for Consumer, Media & Entertainment and Technology. Further, we have inducted many sales and leadership team members as well.

Number two, working closely with McKinsey, we defined the five-year strategic roadmap for differentiation and growth, what we call as LTI 2.0. At the nucleus of our corporate strategy is client centricity. We have always worked hard to enhance the value of our clients, we are now raising the bar several notches to bring innovation and co-creation in our everyday routine. We have launched a companywide global initiative called Beyond, where each employee will think new ways to bring innovation to clients. Through this

initiative, we aim to engage every employee in the organization to walk the extra mile and generate new ideas within their scope that will help us exceed client expectations. Beyond will be implemented at an account level and we have initiated our pilot with four of our key customers.

Third, with client centricity at its core, our strategy revolves around three core principles. A) Helping clients leverage the convergence of physical and digital, B) Making LTI the best place to learn and grow; and C) Becoming a technology and domain leader.

Fourth point, having defined a clear strategy for growth, we undertook transformation initiatives across four key areas that I will talk a little briefly on - sales, HR, delivery and marketing. These initiatives are progressing well and early results are visible across the Company.

With all of this in mind, we have identified the following key priorities for the year and they are as follows:

First, we will keep focusing on growth from our existing accounts. This is really our pot of gold; we have seen tremendous potential for growth within our current clients. We have launched an initiative to mine the clients better. We have also launched an initiative that we called ADEA which is Analytics and Digital in Every Account, that is proving to be very effective for growth of these service lines. We will continue to focus on our top accounts and strengthen our relationship with top 50 accounts by investing proactively in their priorities.

Second key focus area for us is, is to focus on new Logo Acquisition from Global 2000 prospects. We opened 12 new logos in Q1 and 24 in Q4. The parent company has strong connects that help us open doors in large corporates and we are seeing very good traction on our digital, analytics, industrialized IoT, business process automation offerings as wedges to open new doors for us.

On the capability focus front, we are investing in building differentiated offerings and competencies that are aligned to client demands and spend. Our strategic intent is to build significant strength in five areas of growth for us - digital, analytics, IIoT, cloud apps and automation. We have deep capabilities in Industrialized IoT and cloud apps and we are going to market with renewed energy on these. We will continue to further enrich our IP based MOSAIC platform which stands for Mobile, Social, Analytics, IIoT and Cloud and its group of offerings for these areas. MOSAIC is a powerful differentiator for us and we are launching three new MOSAIC offerings in Q2 –

- MOSAIC Automation for Business Process Automation, IT Services Automation and SAP AMS Automation
- MOSAIC AI for Artificial Intelligence, which is a powerful offering bringing power of artificial intelligence to legacy systems, and
- MOSAIC Decision Science, our data and analytics platform that helps Company generate meaningful, compelling and actionable insights.

On the talent focus front, we want to be the employer of choice providing our people opportunities to learn and grow. We will also continue to invest in training and re-skilling of our employees and take steps to contain attrition.

On marketing and branding front we are working with a leading global brand consulting company to define a new brand strategy, messaging platform and visual expression. This exercise will infuse fresh energy into our brand. Also, we are now leveraging the best-of-breed marketing technologies to improve the effectiveness of our targeting and demand generation initiatives.

On the partnership ecosystem front, in addition to GE Predix and Pivotal, partnerships that we announced this week, we have also expanded our partnership ecosystem to several path breaking companies like Pega, Coupa, PROS and ThoughtSpot.

Last week, we completed a very successful IPO, winning trust of more than 3 lakh investors who have joined LTI family.

Overall, this has been a period of intense thinking, planning, creating, designing and very methodical execution that has enabled unlocking the value of a fine organization which is now well positioned to achieve its true potential.

So even though we will be talking about one quarter only, a lot has gone into making this quarter possible. With that background, let me now switch to the current quarter and give you a flavor of our results.

For the first quarter of fiscal 2017 Q1, the quarter-on-quarter growth in services alone has been a robust 4.2%. After including the licensing and hardware cost which weighs down on growth, the overall quarterly growth is 0.6%. Most importantly, our disciplined execution has resulted in an improvement of 120 basis points in our operating margin.

Coming to specific verticals –

- Banking and Financial Services grew 2.1% sequentially. As banks are burdened with increased demands of the regulators in the US and UK, they continue to spend on risk, finance and compliance technologies. Big focus seems to be on reducing the operational spend, especially in the areas like Anti-Money Laundering (AML), Know Your Customer (KYC) and Financial Reporting.
- Insurance saw a growth of 4.6% sequentially. In this sector we are seeing clients differentiate themselves on three fronts - product innovation with features like usage based on demand and peer-to-peer insurance, on distribution channels like leveraging social media and specialized aggregators and through customer experience by creating a consistent experience across all channels and Anytime-Anywhere access.
- CPG, Retail and Pharma grew by about 7.5% sequentially. In this segment, companies are focused on driving efficiencies through smarter supply chains and manufacturing through technology and process consolidation. To drive topline growth, CPG companies are relying heavily on our rationalized product offering; leveraging the power of digital to create consumer engagements and on analytics. Pharma companies on the other hand, are gearing towards a scenario where the patent pipeline are not as strong and patient outcomes become important.
- Hi-Tech, Media & Entertainment segments grew by 2.1% sequentially. Hi-Tech companies are making a significant spend on cloud, IoT, analytics and mobility. There is also a strong focus on building digital engagement with customers. The Media & Entertainment segment is witnessing a massive shift towards the cloud as that is

fundamentally changing the way they do business from content creation to distribution. Role of analytics is becoming central to this transformation.

- Our Energy vertical declined by 1.7% sequentially. However, it is important point to note that service revenues were positive here as well. Clients in Oil & Gas segment continue to face pressures due to falling oil price. The industry is focusing on optimizing current assets as opposed to creating new assets. Downstream companies are doing relatively better because of the lower feedstock and raw material prices.
- In our Auto, Aero and Others, where “Others” includes Engineering & Construction, Plant & Equipment, we saw a decline of 6.5% sequentially. Within this segment, Auto and Aero were almost flat and the decline came from engineering and construction clients where there was a drop in hardware and licensing in Q1 compared to Q4. Automotive sector is facing several disruptive trends ranging from vehicle autonomy, to ride-sharing, to connected vehicles. These trends continue to drive spending in R&D, analytics and customer experience related domains.

Moving on to our Service offerings –

- The growth was led by our Analytics and Information Management (AIM), Enterprise Integration and Mobility service lines that grew close to 8% sequentially
- Testing service line also grew upwards of 8% sequentially. Enterprise solutions grew by 1.5% sequentially. ADM was more or less flat, but grew by 0.2%
- IMS declined by over 11%, mainly on account of a decline in pass-through revenues
- About 22% of our projects were based on digital technologies, so this is a significant area of growth and focus for us

From a geography perspective, we had sequential growth of 2.3% in North America and 1.6% in Europe.

After this deep dive into verticals and services, let me now share some of the key highlights of this quarter:

If you look at macro environment, the industry has been facing challenges posed by uncertainties in the global macro environment due to Brexit. We remain cautious about discretionary spending, especially in the financial sectors, in the UK and Europe. It will be difficult to articulate the overall impact of Brexit as yet, it will evolve over the next two years, but we continue to watch the developments very closely. It could very well be an opportunity for IT companies as systems are segregated but things will unravel in the next two years on what Brexit really means.

On client profiles, our focus on deepening client relationship has been one of the key drivers for our growth. During the quarter, we added 12 new logos, taking the count of active clients to 259. We have 49 clients that are global Fortune 500 customers, our top 10 clients grew by 1.1% quarter-on-quarter. We added two clients in USD 5 million band and two clients in USD 10 million band as well.

On talent, we always try to create a conducive work environment which enables us to attract and retain talent. Our headcount stood at 19,292 people as of June 30th, 2016. Our utilization, excluding trainees, improved to 78%. Similarly, utilization, including trainees, also went up to 77.4%.

We announced two significant wins which are there in the earnings release. One is for Central Board of Direct Taxes and the second one is Elkjøp which is in the Nordic area. The details are in the Press Release.

On key engagements, we have listed many cool things that we have done as part of our key engagements with our clients, but I want to just call out a couple.

- One, a leading Hi-Tech major chose us as a strategic partner for their global MES roll-out, which is a Manufacturing Execution System
- A large CPG company selected us for their BPA, RPA offering. This is split into multiple SOWs but we won a \$35 million engagement with a global bank in the area of finance, risk and compliance, which is why we did not call it as a large deal, but is a combination of many SOWs.

On partnerships and memberships, we announced two strategic partners – GE with digital to provide industrial outcomes and with pivotal for big data and analytics.

We received many awards and recognitions, notable among them is the award that we received for our Annual Report which is a Gold Award and many analysts from Gartner, IDC and Everest named us in their reports

In closing, I want to mention that our relentless focus remains on delivering consistent performance, drive leading growth and building capabilities in the new growth area. Let me now hand it over to Ashok for his comments before we take your questions. Thank you.

Ashok Sonthalia:

Thank you, Sanjay. Hello, everyone. This is Ashok here. We have been engaging with many of you in the last few months in preparation of our IPO, and now that we are listed, it gives me great pleasure to speak to all of you on our maiden quarterly results post-listing.

Quarter one FY17 was characterized by strong execution led growth in our IT services portfolio. Let me first go through the headline numbers:

Our USD revenue has grown 10.8% year-on-year basis and 0.6% sequentially. In rupee terms, revenue in Q1 at Rs.15, 550 million saw a growth of 16.6% YoY basis. Our IT services portfolio revenue grew strongly at 4.2% quarter-on-quarter which is not very apparent from the headline number but there is a common theme reflected in our various cuts of revenue, be it geography vertical, or services lines.

On the profitability front, we had a good performance. The operating margin for the quarter stood at 18.6%, implying an increase of 120 basis points over quarter four FY16. This was mainly due to improved efficiencies as reflected in levers such as improved utilization, automation, etc. Reduced pass through also helped. The margin improvement was achieved in spite of seasonal visa cost affecting margin adversely by about 110 basis points. Our PAT has grown strongly during the period by 35% year-on-year and by 3.3% on a quarter-on-quarter basis. We continue to deliver consistent PAT margin which stood at 14.8% for Q1, rising by 50 basis points on a quarter-on-quarter basis and 220 basis points on a year-on-year basis.

Our utilization, including trainees, has improved by 150 basis points over quarter four to 77.4% while excluding trainees we have improved by 90 basis points to 78%.

The effective tax rate for Q1 has gone up to 21.2% and this is largely due to the completion of the five-year tax holidays for four of our SEZ units during fiscal 2017.

The diluted EPS for the quarter stood at Rs.13.85 as against Rs.13.47 for quarter four of FY16. The return on equity was strong at over 42%. Operating cash flow generation was at 18.7% of revenue on the back of better collections. Our DSO has improved to 70 days in quarter one as against 73 days in previous quarter. Cash and liquid investments as of June 30th stood at Rs.4,283 million.

Impact of IND-AS adoption - the new accounting standard applicable from April 1, 2016, has been detailed in the reconciliation provided in the published financial statements and is available to all of you. While there is uncertainty around the impact of Brexit on the industry, we have had limited currency impact due to a strong hedging policy and limited exposure to the region with Europe contributing only 18% of our revenues as of quarter one FY17. In terms of currency, our exposure in cable is less than 2%.

With these comments, we would now like to open the floor for your questions.

Moderator: Thank you very much, sir. Ladies and Gentlemen, we will now begin the question-and-answer session. Our first question is from the line of Priyanka Sarkar from Motilal Oswal Asset Management Company. Please go ahead.

Priyanka Sarkar: Sir, just wanted to ask a couple of questions. On the headcount front, I see there is a reduction in technical as well as in the sales people on a year-on-year basis as well as on a quarter-on-quarter basis. So just wanted to figure out why there has been a reduction, is it a case of automation or is there some other reason?

And sir second, I wanted to ask is on wage hike, does it come in this quarter or is it supposed to be reflected in next quarter?

Sanjay Jalona: Let me start with the second question, the wage hike for us is applicable from July 1st, so it will come in Q2. Now on to your first question on headcount reduction, we have undertaken various initiatives to improve the operational efficiency which has helped us to improve utilization. Campus additions and outsourced partnerships are planned for Q2 onwards, we expect to add around 700 graduates joining us in Q2. Automation has helped us tremendously, so far we have reduced over 200 FTEs and we will continue on this journey rigorously. Internal fulfillment has also led to less external hires and voluntary attrition and performance related exits have been limited.

Moderator: Thank you. Our next question is from the line of Nitin Padmanabhan from Investec. Please go ahead.

Nitin Padmanabhan: If you look at the top 10 and top 20 clients, any thoughts in terms of what you see in terms of their broad spending plans for the year, their budgets and how do you see things going forward? Because this quarter appears to be quite weak versus the previous year's wherein quite a bit of contribution actually came from them.

Sanjay Jalona: Nitin, we are extremely focused on the top 10, top 20 and going on to top 50 accounts. Every account behaves differently and they might come from financial services or insurance or oil and gas or whatever sector you talk about, they have their own priorities on how they want to use the digital technologies and make an impact on what they want to do with their businesses. If you look at our top clients, our top client is Citibank and this is a known fact from our filings. We have grown quarter-on-quarter there, we are focused on finance, risk and compliance in the banking financial areas which is seeing a good amount of traction. Another area where we are seeing a good amount of traction is the Robotics Process Automation. As you know we do not have a BPO service line so we are really, really excited about the tool sets and automation that we have built including machine learning on disrupting the commoditized people doing lending, mortgages, etc. in a very meaningful way.

Now on budgets, as far as the companies go, they are spending in the new areas of analytics, digital, IIoT, etc. and we are seeing good amount of focus with customers in various verticals that I talked about when I gave the sectoral description on those areas. For example, BFS clients have cut down on operations and increased focus on digitization, finance risk and compliance since customers are struggling to figure out what they are entitled to with lot of new changes and regulations coming in the sector. Oil and gas companies are focusing on better asset utilization and reopening the capital projects that had been put on the hold for many quarters. **Nitin Padmanabhan:** Just one more thing from margin perspective, any color in terms of what kind of a margin band you would like to operate at going forward, anything you would like to talk about from that perspective?

Sanjay Jalona: Margin band, we have always maintained and throughout the year we would want to keep it at the same margin band. We have used a few levers in the last few quarters to improve the utilization, roll ratios, automation etc. There are many levers still pending with us and we will use all of them to keep our margins at the same band while investing in the business.

Nitin Padmanabhan: So sir the band would be around last year's number or looking closer to what we did in the current quarter?

Ashok Sonthalia: Overall for the full year basis, we have said that our net income has been in the range of 14% to 15%. That means quarter-on-quarter, there can be minor ups and downs around the band, but that is what we want to do consistently.

Sanjay Jalona: For the year we will be in the band of 14% to 15%.

Moderator: Thank you. Our next question is from the line of Vikas Sharda from NT Asset Management Company. Please go ahead.

Vikas Sharda: Could you just quantify what is the decline in the revenues of hardware and other pass through which you mentioned?

Ashok Sonthalia: In quarter four, we had about 6% of our revenue coming from hardware and pass through which has gone down to less than 3% in quarter one.

Moderator: Thank you. Our next question is from the line of Nandish Dalal from IIFL. Please go ahead.

- Nandish Dalal:** The hardware revenues which has led to the decline in revenues during this quarter, is it a seasonal thing? Because in Q1 FY16 also we are seeing a muted quarter, so is this what we should factor from in from going forward?
- Ashok Sonthalia:** No, I do not think there is any seasonality to this. It is just project cycle, the way they get delivered. And particularly in India, in the infrastructure segment, where we are doing certain projects, it completely depends on the project cycles. In quarter four, we had some large projects where hardware and license delivery took place which has not happened in quarter one. As Sanjay spoke about one large win, the Central Board of Direct Taxes, that is again a full project where we are responsible for hardware, data center, everything. We will be setting up everything for them.
- Nandish Dalal:** And Ashok, wage hikes will impact your 2Q, could you just quantify how much it would impact and what is the wage hikes you are giving?
- Sanjay Jalona:** We are going for 8% to 10% with good performers and the high potential people getting more. And onsite is in the range of 2% to 3%.
- Nandish Dalal:** And what will be the impact on margins, a rough range?
- Sanjay Jalona:** So we talked about this Nandish. We will continue to use the levers that we have and throughout the year we want to be in the band of 14% to 15%.
- Nandish Dalal:** And just a book keeping question, Ashok could you just help me with the hedge balance during the quarter and the rate?
- Ashok Sonthalia:** The hedge is about \$650 million in our books at this point of time. I will not be able to give rates because we believe that is a sensitive and competitive information, but we continue to deliver through consistent hedging policies, insulating cash flows, profit & loss on the margin front.
- Nandish Dalal:** And what would be the hedge balance sitting in the balance sheet in your hedge reserve?
- Ashok Sonthalia:** We'll get back to you on that.
- Moderator:** Thank you. Our next question is from the line of Manik Taneja from Emkay Global. Please go ahead.
- Manik Taneja:** While you have alluded to your target margin range, if you could help us understand how the investments that you have talked about in terms of account management, sales and marketing and what kind of impact or what would be the focused verticals here?
- Sanjay Jalona:** So we operate in the verticals that we have defined and the two focus areas for us as an organization is, one, to drive profitable growth, so revenue is very important but you need to have a profitable growth. And the second big important thing is for us to have a very resilient portfolio.
- Now, some time ago, banks were struggling, so banking industry was down 2007 onwards, then you have oil and gas which continues to be under stress and tomorrow there will be some other vertical. So the idea is to continue focusing on all verticals, but most importantly focus on the clients that we have. I referred to 250-odd MSAs and the

customers as a pot of gold, that is our focus area and they span all across all the verticals that we operate in. So we are investing with key client partners, key delivery partners, consulting partners on those accounts doing opportunity workshops, creating rigorous account plans, taking new ideas on digital and transformation to them and creating a mind share with them. So that was one question, what was your second question?

Manik Taneja:

Sir, I was just inquisitive to understand what kind of investments are you making in terms of account management and sales and marketing and how should we be thinking about that playing out over the next 18 - 24 months?

Sanjay Jalona:

So we are definitely increasing the investments on sales and marketing while reducing the G&A cost through delivery excellence. We would like to reduce our cost of delivery, using automation as a big lever. Using all of these, we would invest back into the business in the form of sales and marketing. We are hiring the right set of people, you would have seen over the last two, three quarters we have had a decline in the sales cost because we actually got the right set of people to work there. So we moved a whole bunch of people to the delivery organization, we created proper KPIs for them, we hired a lot of new talent in the market place and we will continue to invest in bringing more sales focus into the top 50 accounts and new logos as well. But what is very important to understand we will use all the delivery excellence initiatives that I talked about utilization, role ratios, automation, 'n' number of levers that are there and G&A cost etc. and funnel it back to the business and sales and marketing.

Moderator:

Thank you. Our next question is from the line of Mukul Garg from Haitong Securities. Please go ahead.

Mukul Garg:

Sir, I have two questions. First, on digital side you mentioned that it is at 22%, can you give us a flavor of what kind of growth you are seeing in that business and where this growth is coming from, which industry? And the second question is, just a clarification on the hardware and licensing impact, what portion of revenue is that on a full year basis, how much it was last year and how should we see on a full year the impact happening in the current fiscal year?

Sanjay Jalona:

On digital I think we always had strong digital presence. But digital is a new terminology, I actually would like to call it exponential technologies which includes social, mobile, analytics, cloud, Industrialized IoT, 3D printing, machine learning, robotics process automation, etc. And we have given details of how we have grown quarter-on-quarter. Analytics has been a growth engine for us for many, many quarters, we grew close to 40% last year. And we are seeing a good amount of demand over there as well. One area where we are strongly differentiated is the Industrialized IoT. Nobody understands the physical world the way we do, because at L&T as a group we operate power plants, nuclear submarines, do manufacturing, build airports and are into hydrocarbons and so on so forth. At the intersection of both physical and digital, we see the way one uses IoT and Industrialized IoT to put sensors, beacons, listening devices for collecting all kinds of data, what a compressor is spitting out, when is that platform likely to fail, what an intelligent pipeline looks like, what a power plant is doing and how do you actually optimize it using the machine learning technologies. While most of the IT companies typically talk about IT, we also understand the operational technology (OT) in the fields that we operate in, so that physical and digital translates to IT plus OT. That is the place where we are seeing tremendous amount of growth.

Another area of significant growth in digital where we seriously differentiate is the entire BPA area, this whole Business Process Automation and Robotics Process Automation, especially if you look at the BFS sector. Anywhere where you have thousands of people doing lending, mortgages, etc. from digital side. So they are doing mundane work, how do you digitize that process, how do you use the technologies whether it is OCR, Blue Prism, Automate First or the machine learning tools that we have built, how to significantly reduce 30% - 35% of that manpower or thousands of people within weeks is another area of serious differentiation for us.

In the verticals, I think digital is impacting all the clients across verticals in a very uniform way. Some are trying to optimize cost, with BPA as an example that I have talked about, some are trying to interact with the consumers in a new way using better analytics, on time decision making, connecting with the consumers in a different way, in a digital way. So we have different industries and different customers using these technologies differently. But I think it is a universal phenomenon and impacting all customers across all service lines and verticals in a very uniform way.

Now on your second question on hardware licensing and whether you can put in the model, I think Ashok will give you specific numbers. The important part as we talk about is, we are not just buying hardware and licensing and just passing through, the basic concept is, we are executing these large programs for our customers and CBDT as an example, Central Board for Direct Taxes where the government wants to increase the percentage of people paying taxes from 2.9% to higher. We have got to understand that the government works in a holistic form, you will get to buy infrastructure, buy licenses and deliver to them on an outcome basis per transaction. I believe this is one of the most complex, mother of all the analytics programs that probably anybody has done, and it is a real game changer. What we are going to use technology and the power of analytics to establish linkages. We will link information from social media, foreign travel, purchases made, etc. If you have gone to Paris and you are not paying taxes it is a potential red flag, if you spend Rs. 20,000 on geo-fencing and GIS but not paying tax, if you have an electricity bill of Rs. 20,000 but don't pay tax, all these linkages help raise red flags and identify potential tax evaders. This deal will use Analytics to bring tax evaders under the tax lens.

But in order to execute these programs for some for some of these turnkey customers, especially in India, you need to provide infrastructure, so for example in CBDT you will have to provide servers, setup a datacenter, setup a BPO operations, buy SaaS licenses and do a number of open technologies. These will get into the quarterly numbers during the project cycle that is being defined for that project.

And Ashok, you want to add anything on numbers?

Ashok Sonthalia:

So the same way as the last year also, we have been doing two large programs in India and predominantly because of that these things have come in. Overall, for the last year on a portfolio basis, hardware and licenses contributed about 3%, but in quarter four as I explained you earlier, the number was higher because of the project lifecycle. But as we are doing some more projects, we do not see this number moving too high going forward. That is why we are not disclosing it separately because it is still not a large portion of our portfolio, it is still hovering around 3% which has started from last year. So we will take an appropriate call on the disclosure, if it becomes sizeable.

- Moderator:** Thank you. Our next question is from the line of Abhishek Bhandari from Macquarie Securities. Please go ahead.
- Abhishek Bhandari:** Sir, I have a couple of questions, I will ask them one by one. Number one, will it be possible for you to quantify the deal wins in terms of rupees or maybe dollars?
- Sanjay Jalona:** So I can talk about CBDT which will be upwards of \$100 million. And I talked about the finance risk and compliance wins which has come in multiple deals, and will be upwards of \$35 million in 18 months. Elkjøp deal is around \$15 million which includes infrastructure transformation to cloud as well as for S/4HANA from the legacy SAP side.
- Abhishek Bhandari:** Sir, the second question is, while you do not give a guidance, I understand that, but do you expect the dollar growth for this year to be better than last year? Because if you look at last two years, we were somewhere around 8.5% and 9.5% for two years, do you think we can see double-digit?
- Sanjay Jalona:** We have a strong pipeline, we like the conversation that we are having with our customers, we want to lead the growth for the year.
- Ashok Sonthalia:** Just to add on this, if you would have analyzed our last two year growth, energy has been a big drag for us in last two years and as we have seen, it is kind of now coming to a situation where it is flat to biased towards slower growth. So that drag has gone away from our portfolio and to that extent, you can expect better performance.
- Abhishek Bhandari:** Sir third question is, while you have given a net profit margin range of 14% to 15%, any operating number you are working with at the EBITDA level?
- Ashok Sonthalia:** You can back calculate on the numbers we are working with, I am sure. What we are saying is that 14% to 15% PAT because some people have been bringing FOREX gains after EBIT, but we believe that it is part and parcel of our revenue because we have a very differentiated hedging strategy and that is why we chose to give some sort of a guidance on a net income basis, because that is the purpose and objective of our strategy.
- Abhishek Bhandari:** Actually that was my last question as well, if you look at your other income last year out of Rs. 290-odd crores roughly Rs. 200-odd crores was the FOREX gain, do you expect the trend to continue even this year because this year Rs. 33 crores - Rs. 34-odd crores in the first quarter is around 140 - 150, do you think similar amount of gains can be continued?
- Ashok Sonthalia:** Last year it was not 200, it was almost Rs. 275 crores out of Rs. 290 crores. There is the IND-AS accounting change which has a FOREX premia accounting. Earlier the premia was accounted through P&L and now it is directly going to hedging reserves. Hence, comparative number of quarter one was Rs. 44 crores and against that we have delivered Rs. 34 crores. For us it is not important what number appears at that line, for us it is more important that whether it is insulating our revenue from any FX fluctuation and thereby helping us to maintain our margin profile. And that is what you will observe from our previous results that we are able to do that - sometimes the FOREX line is fatter, sometimes it is leaner and sometimes it is in negative, but our margin is always around that. So that is the purpose and philosophy of our hedging strategy.

- Moderator:** Thank you. Our next question is from the line of Prasad from Investec Capital. Please go ahead.
- Prasad:** Sir, can you give us sense about the acquisition strategy, like any specific service areas or geographies that you are looking to strengthen?
- Sanjay Jalona:** So acquisitions will be an integral part of our growth strategy. Let's divide acquisitions into two buckets so to speak, one would be scale acquisitions where we could look at anything up to \$100 million or even a little bit more than \$100 million. And few areas that we would look under that will be new age infrastructure, not the old age infrastructure but the new age cloud based infrastructure transformation kind of work. We could look at vertical consulting capabilities in the US and especially I am calling out US. We would also look at customer and market geo access. We are not that strong in UK and Germany, so if there is a good asset in UK and Germany we might look at it. And if there is a company or an asset that is available in the verticals that we operate in where we can further strengthen our case, we might look at that. So that will be on the scale side. If you look at capabilities, we would look at cloud apps which is Workday, Azure, Salesforce.com kind of capabilities. We are strongly differentiated in IoT and analytics and if there are additional capabilities that we are able to get to build our platform further and enrich it, we would look at that. We are strong in verticals that we operate in, if there are platforms which help strengthen our case, say for example in Insurance – Guidewire, Duck Creek, in financial services – Murex's Calypso or in horizontals like Pega, etc., we might look at that. So these are some of the examples of scale and capability acquisitions that we are looking at.
- Moderator:** Thank you. Our next question is from the line of Sagar Rastogi from Ambit Capital. Please go ahead.
- Sagar Rastogi:** Wanted to understand your organization structure a bit better, so how decentralized is decision making in terms of pricing, investments and so on?
- Sanjay Jalona:** The first thing that I did after joining was to create a new structure where we put the customer at the center and we created the Chief Business Officers by verticals. This structure is for US, and will be extended to Europe and Emerging Markets when we attain some size where we could go to global verticals. The pricing decision is totally left with the Chief Business Officers and their respective teams on the ground. So in this way the decision making is decentralized. We obviously have our metrics of what they can do and what is the right thing and everyone has a goal to meet the company-wide numbers. What is really important to explain here is, we put our rigorous KPI process for the leadership team, sales guys are very driven on revenue, margins, DSO and client satisfaction and the entire leadership team is very focused on driving growth and differentiation, delivery team is focused on capability building, sales team is focused on revenue growth.
- Sagar Rastogi:** And my second question was on your hedging strategy, so is it right to assume that you hedge 100% of your net exposure? And for what time duration do you hedge?
- Ashok Sonthalia:** We have a long-term hedging plan in place which is basically 12 quarters. And the second aspect of this policy is that it is on a net exposure basis. The third aspect is, we are heavily hedged for the first four quarters and it is lighter as we go further. Cross currencies are

fully hedged for the current year. Most hedges are cash flow hedges. But once the receivables come on the balance sheet, they are fully hedged. So for cash flow hedges, there is a ratio within which treasury operates. The bands are given for first four quarters, next four quarters, and last four quarters within which they are supposed to be operating.

Sagar Rastogi: Just one quick follow-up, so the percentage that you are hedging, that you expect it to remain consistent over time or do you think it might change depending on market conditions?

Ashok Sonthalia: No, market condition only allows to operate under that band whether they are on the lower side of the band or the higher side of the band. I think any hedging policy is successful in the long-term only when you are consistent with it. Until and unless some structural changes happen somewhere, I do not think we have any plan to review this policy in the near future. So we will kind of continue to follow that.

Sanjay Jalona: I want to just add a couple of points. One, at L&T Group we have a very strong treasury department. Number two, the finance team does a very regular and a proper monthly review and I do a quarterly review to make decisions. So this is a very rigorous process, very deeply looked into and an area of significant differentiation for us based on the investments the organization has made.

Moderator: Thank you. Our next question is from the line of Sandeep Shah from CIMB India. Please go ahead.

Sandeep Shah: Ashok, wanted to drill a bit on the FOREX side, so you have given most of the answers, but if you look at last year Indian GAAP, full year PAT margin was 15.8% and now we are seeing 14% to 15% as per the IND-AS. And I do understand looking at the reconciliation the major reason for change in the accounting for the FOREX in the IND-AS. So just to get this clear, is it now only the realized FOREX gain which will go to the P&L and the unrealized which will go into the balance sheet? And is it the difference versus earlier where everything used to go in the P&L?

Ashok Sonthalia: Yes, you are right. Three, four elements, of which one element now goes to balance sheet which is premia accounting which was earlier going through P&L and now it directly goes to balance sheet through MTM including premia. With respect to the realized hedge settlements and revaluation of debtors, they will still continue to go through P&L.

Sandeep Shah: And in revaluation of debtors, you have hedges.

Ashok Sonthalia: Earlier we were doing only cash flow hedges. Starting this year now debtors are also completely hedged.

Sandeep Shah: And on the tax rate we continue to expect similar rates going forward?

Ashok Sonthalia: We have indicated our outlook for FY17 in the beginning of the call that our four SEZs are coming out from 100% to 50% tax holiday, so we expect 22-23% tax rate to continue in the foreseeable future.

Sandeep Shah: And Sanjay, just a question on the business side, if you look at the enterprise solution, it is upwards of 23% for you as well as the IMS which is a growth area in the traditional outsourcing business, it has been slightly lower at 10%. So do you believe these are

hurdles for you in terms of scaling up your business because there could be leakages in the enterprise solution or you do not foresee that?

Sanjay Jalona:

No, actually I see opportunities here. If you look at enterprise solutions, it grew by 1.5% when the entire industry is seeing a little bit of pressure on this. People have written death of SAP and Oracle but I think these companies are doing a lot of transformation for themselves, coming out with more and more cloud based products. It is very important to note that they will keep using SAP and Oracle as the backbone of their enterprises, but small pockets where they were implementing SAP will probably implement a cloud version of that, but the backbone will continue to stay. So for a company of our size, if we have a couple of enterprise solutions deals in SAP and Oracle, that will give us enough momentum in the business. And again in enterprise solutions we are seeing a lot of pipeline on our cloud apps and the new age work like S/4HANA that we are doing for Elkjøp, all that will drive all that growth.

In terms of infrastructure, yes it is a 10% area, I have already articulated this is an area where we want to do a sizable acquisition, especially the new age IMS. But it is also important to note that we are also again trying to differentiate ourselves in this area. Everest just co-authored a paper with us on converged operations using the infrastructure as a differentiation in the market place. So these two areas are the backbone for the Company and that will continue to be the case. IMS, we will make investments, what is really important to note that the world over infrastructure deals are getting smaller as the companies move from traditional on premise to cloud based. And we are at a size where we can actually go after these deals in a significant way. So the market has actually flattened for us to be competitive there.

Sandeep Shah:

Just last few things on the BFS, I think you work with large logos, so Sanjay any recent discussions with the client gives you any kind of a worry especially for maybe a global bank for their operations in the Europe?

Sanjay Jalona:

In Europe or overall?

Sandeep Shah:

Europe, because I think it looks like the near term headwind could maybe Brexit and the impact on the operations and the plans for the IT spend there.

Sanjay Jalona:

We are actually bullish on BFS globally, so let me just say that. We are bullish on BFS globally. As I said, two, three areas where we are definitely doing a lot of work, one is on finance, risk and compliance which is an area to invest in, because of the burden the regulators have put on the banks. And we have helped one of the large banks clear the CCAR, which is the Capital Adequacy test and that gives us a lot of knowledge to go after other banks and we are in constant engagement with a few of them. Second area which is serious differentiation as I talked about is the whole BPA, RPA area where we are doing a lot of work on the off-site. On European BFS side, while there is definitely a little hesitation currently on the Brexit side, but the number of discussions that we are having with the customers on ops side with BPA, RPA or on finance risk of compliance or digital banking is tremendous. Another huge growth area where we are seeing much differentiated opportunities is in the area of analytics. Some of the cool work that we have done, for example for one of the European banks for helping them manage their HNI. They were never able to get a grip on what the HNI pool looked like and how do you

actually communicate and interact with them. And these are all digital pieces of work that has gotten a good amount of traction with us.

Sandeep Shah: And last question on the energy and process, can you give us a breakup of the upstream, downstream exposure we have?

Sanjay Jalona: I do not have that handy with me, but I can tell you upstream companies are significantly large companies, so they are the larger spenders. So I am just taking a guess here, 70-80% odd of the work will actually be with the upstream companies and 20% of the work with specialty chemicals and mid-stream companies. That percentage will increase over a period of time. But I again want to call out that upstream companies have also understood a new norm that oil prices are not going to go to \$100 anytime soon. And how long can you keep the capital projects on hold. So five, six months back we won a large deal in oil and gas upstream company. In the consolidation that has happened in the last couple of years we have only gained because we have differentiated and strong capabilities built by L&T group in the hydrocarbon business. And we are excited, it is not a drag anymore as in the last two years, so we have seen a growth from Q3 to Q4 and Q4 to Q1 in services business. And I think it will do all right.

Moderator: Thank you. Ladies and Gentlemen, that was the last question. I would now like to hand the conference over to the management for their closing comments.

Sanjay Jalona: Thank you, Mallika. Once again folks, we would like to thank you for joining us on the call today. We look forward to talking to you again over the course of the quarter and see you again in the Q2 investor call. Take care. Thanks. Bye.

Moderator: Thank you very much, members of the management. Ladies and Gentlemen, on behalf of L&T Infotech, that concludes this conference call. Thank you for joining us and you may now disconnect your lines.

(This document has been edited for readability purposes.)



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