"Mphasis Limited Q1 FY-18 Earnings Conference Call"

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Moderator: Good day, ladies and gentlemen, and welcome to the Q1 FY '18 Earnings Conference Call of Mphasis Limited. As a reminder, all participant 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 for an operator by pressing * then 0 on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Varun Divadkar from CDR India. Thank you, and over to you.

Varun Divadkar: Thanks, Sid. Good morning everyone and thank you for joining us on Mphasis's Q1 FY18 results conference call. We have with us today Mr. Nitin Rakesh, the CEO; and Mr. Suryanarayanan – the CFO.

Before we begin, I would like to state that some of the statements in today's discussion may be forward-looking in nature and may involve certain risks and uncertainties. A detailed statement in this regard is available in the Q1 FY18 results announcement release that has been sent to you earlier.

I now invite Mr. Nitin Rakesh to begin the proceedings of the call.

Nitin Rakesh: Thank you, Varun. Good morning everyone and thanks for joining the call. I hope all of you had the opportunity to go through our MD&A, which provides the details of our operational and financial performance for the quarter ended 30th June 2017. I would like to begin with stating that this quarter we witnessed many highs in our quarterly performance. We have the highest sequential revenue growth, highest TCV deal wins, highest percentage wins from new gen services and highest quarterly HP/DXC channel growth.

We have started the year on a solid note recording our highest ever TCV of new wins in a quarter in Direct International at $183 million in Q1 FY18, higher by 91% year-over-year as compared to $96 million in Q1 last year and $365 million for the full year in FY17. What is even more encouraging is that majority i.e 88% of the deal wins, are in our focus areas of digital, GRC and next-gen services. As indicated earlier, we had significant traction in the deal wins in the Blackstone portfolio during the quarter with some of the deals being transformative in nature. They are nothing but a focused approach here to build our pipeline and expect the deal wins to continue as we progress further here.

We are also pleased to note that the TCV wins have been broad-based and inclusive, coming from new clients, strategic accounts, as well as Blackstone portfolio. These deal wins put us on a strong footing and provide good visibility to drive above industry growth in the Direct Core segment.

In the HP/DXC channel, we are building strong momentum by leveraging on the strength of our decade long partnership and our accelerated GTM efforts. During the quarter, we won significant deals that have contributed to the growth, which as I mentioned, has been the highest in the recent past.

Moving on to Q1 FY18 financial performance, consolidated revenue grew 2% Q-o-Q on a reported basis and 4.8% on a constant currency basis. Direct Core, which contributed 78% of Direct International revenue in Q1 FY18, grew 1.2% on a reported basis and 4.1% on constant currency basis. As mentioned earlier, the deal wins and pipeline in this area of business is robust and we are confident of driving above industry growth this year. Direct International recorded moderate growth of 1.2% Q-o-Q adjusted for rupee appreciation impacted by the decline in Digital Risk and the product portfolio due to cyclical issues.

HP/DXC revenues grew 6.8% Q-o-Q on a reported basis and 10.1% on a constant currency basis. The outlook in the HP/DXC business remains strong and after several years of decline, we will see growth back in the HP channel in FY18. Digital Risk is operating at levels indicated earlier and we do not anticipate any significant headwinds with focus being on continuing to stabilize the topline and improve the margin profile in the near-term.

Moving on to margins, operating margins have dipped 80 bps Q-o-Q to 13.8% largely on account of transition impact from large deals won, decline in the product business margin and currency movements. While we focus on continuing to find opportunities and closing TCV to accelerate revenue growth, we are confident of improving our margin trajectory as we start delivering and building scale on these large projects and bringing in efficiencies.

Total cash on our balance sheet stood at Rs. 21,162 million i.e., $328 million as we completed the buyback of 17.4 million shares for a total consideration of Rs. 11,030 million i.e., $169 million. Adjusted for the outflow towards share buyback, net cash generated during the quarter was Rs. 1,981 million or $30.7 million.

To conclude, this has been a solid start to the year with record TCV as new wins and good execution driving robust growth. We are optimistic of our prospects and are well poised to continue to see growth in our Direct Core and HP/DXC businesses as our deal pipelines continues to be strong with good traction in cloud-based and digital services across our Direct Core channels and HP and DXC business.

We are also stepping up our investments in Europe which currently accounts for about 10% of our revenues as we believe there is strong opportunity for growth for us in that region. We will continue to bring in differentiation through innovation in helping customers transform their application landscape, helping them continue to work with getting closer to their end customers with consumer-facing technology.

On that note, I thank you once again for your interest and I would now request the moderator to open up the line for questions.

Moderator: Thank you, sir. Ladies and gentlemen, we will now begin with the question-and-answer session. The first question is from the line of Nitin Padmanabhan from Investec. Please go ahead.

Nitin Padmanabhan: A great quarter, great deal wins. Just wanted your thoughts in terms of how do we expect margins to evolve going forward. You had mentioned about margins improving as we gain scale. So from a margin perspective, considering that Q3 is a wage increase quarter, how do we sort of see margins evolving in the near to medium term?

Nitin Rakesh: Sure, Nitin. As I mentioned, the record deal wins have basically had an impact as follows. Our utilization is lower than where it was last quarter and last year almost by 4% YoY and the primary reason is we are building up essentially for staffing these deals as we won. There is probably going to be a higher component of onsite. It was already evident in Q1. And that is because as we start these deals, especially the new gen service deals, there is a heavier onsite element required and then we will bring offshore leverage at the steady state of those deals. We also think that the product portfolio margin should actually improve Q2 onwards. So those three basically mean that we are right now at the lower end of our EBIT guidance of 14 to 16. It might take us another quarter or so to continue to bring in operational efficiency to fend our wage pressure in coming quarters. But we still think we will end up in the operating band of 14 to 16 EBIT we talked about.

Nitin Padmanabhan: Sure. That's helpful. Just two more data points, one is on the Direct, the Digital Risk revenues for the quarter actually.

Nitin Rakesh: Yes, I think we guided you to 28 to 30 million quarterly revenue run rate. We are just at about the lower end of that right now. We do believe that we have entered into a period of stabilization for DR and the expectation in the next couple of quarters is to continue to see stability in revenue. We did have some deal wins last quarter as well as this quarter, that should actually help in bringing some more focus on the topline. More importantly, we think that we will be able to improve the bottom-line as well. So overall, we think DR should actually be stable from a topline perspective and marginally improving from bottom-line perspective.

Moderator: Thank you. The next question is from the line of Rahul Jain from Emkay Global. Please go ahead.

Rahul Jain: Firstly, on this strong new logo addition, what is driving this momentum and which areas are this engagement for us?

Nitin Rakesh: As I mentioned in my prepared remarks, the growth is fairly broad-based. Not only did we see a very healthy new logo addition, we also saw a good growth in our strategic accounts. We also saw good contribution from the Blackstone portfolio that added to the new logo addition. We have also seen decent traction in the HP/DXC channel. So it is fairly broad-based, that's a good news. Also, most of the wins are in new gen areas. When we talk about 88% of the wins coming in our focus areas of next-gen services, there is a very heavy element of what we call services transformation that we are starting to see in almost every deal that we are bidding in. We are driving towards that. The recent announcement on winning an award by ISG in the Imagination category in Europe where our service transformation application using InfraGenie, which is an AI powered infrastructure automation management service, is a good example of how we are applying services transformation to legacy IT and building the bridge to new gen services. So that I would say is a very common trend that runs across. The other areas where we are seeing good traction is consumer-facing tech, the whole front to back transformation for digital and cloud-enabled deals.

Rahul Jain: Okay. And do we need to make some investment in building teams for more verticals beyond the BFSI and TMT because now we would have renewed focus in HP/DXC as well as Blackstone, which is much wider from a vertical standpoint?

Nitin Rakesh: Yes. I think. I see the two core vectors of go-to-market. One is what you mentioned which is vertical, but I think there is a very strong emerging vector of going to market with the front to back transformation in cloud and cognitive capability. And I think that has actually become a common thread for us to apply to almost every vertical. So, our focus areas will still continue to be predominantly BFSI-driven in our Direct business. And as we see opportunities, we will continue to invest in cloud and cognitive, and we did talk about expanded investments in NEXTLab for clouds last quarter. We have also expanded our capabilities on the whole cognitive deep insights front using our NEXTLab capability. And we'll potentially look at making some tuck-in investments and acquisitions to augment our capability over the next couple of quarters.

Rahul Jain: Understood. And lastly on this deal TCV. Is it much bigger in terms of the time spread versus what it used to be in past, and is this momentum in HP/DXC has led to this pricing improvement in the onsite and what would be the trend going forward?

Nitin Rakesh: Again, as I said, the quantum of TCV deal wins is much higher, part of the reason is because we have added more engines of growth. I don't think there is anything to call out on tenure or duration that is unusual. I think it is fairly standard. But the one thing that as I said was the common thread is almost every deal that we are touching today has an element of services transformation or digital transformation in there.

Rahul Jain: And the pricing part on the onsite?

Nitin Rakesh: We are happy with the fact that we have stable to-slight uptick in pricing. Some of that is related to the next-gen services, some of that is related to the fact that fine services transformation. So, on a realized basis, we are able to actually do better. We still have some work to do to make sure that we are able to turn that efficiency into margin over the next few quarters.

Rahul Jain: And the gross margin in this quarter was weak for the ICT business, is it related to product?

Nitin Rakesh: No, I think it is primarily related to the fact that as I said, we expanded our teams and our utilization dropped. And the reason for that was primarily because we, in anticipation of some of these wins and the fact that we are converting business for this transformation aspect, so initial phases will probably take a higher cost and as we bring in efficiency, offshore leverage will become higher as well as the application of automation will be heavy. So it is a good place to be. So now the effort really is to execute them in a way that we want to, which is focusing on sort of transformation.

Rahul Jain: So effectively you would be accreting margin more probably couple of quarters from now then?

Nitin Rakesh: Yes, I think that probably is a good trajectory that we will end up with. So again as I said, we focused on identifying pockets of growth and adding channels. We put growth above everything else and we essentially invested in making sure that we were able to lock in the deal wins. And that's what we've delivered this quarter.

Moderator: Thank you. The next question is from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria: Nitin, couple of questions. Firstly, material increase in the deal wins, was this helped by better win rates or was this helped by expanded pipeline? And if you could throw some color on how much of that was helped by the Blackstone channel?

Nitin Rakesh: Sure, Gaurav. I think you hit on all the key aspects right there. So firstly, we have added new channels of growth, Blackstone was one key channel, but that was not the only channel. As I mentioned in my remarks, it has been fairly broad-based across existing clients and new logos. As you can see, we added 12 new customers in the quarter, which is a new high in almost 12 or so quarters, as well as the fact that we are actually able to stitch together a next-gen capability or a transformation capability in every deal. So, I think that also helps in win rates, but I think the number one reason really is that the funnel has expanded significantly because of these new channel

Gaurav Rateria: Sure. On the DXC part, could you help us understand whether the key driver was the new partnership which you signed recently or something else. And how should one think about the current status of pipeline with the DXC work? Is this a steady state fast growing business again?

Nitin Rakesh: Sure. So we talked about it in the last call, let me just recap that. There are three or four things at play here within the HP/DXC. Firstly, HP is no longer just one large monolithic relationship. Now we have four distinct strategic accounts within the HP channel, starting with HPE, HPI, DXC and the to-be-formed Micro Focus of the spin merge of the product business. So, I think we now have four distinct large strategic relationships that we are focused on mining. We have a pretty good capability in the company of account mining and that's what we are applying to HP channel as well. So some of what we are seeing is coming from that, restructuring of the way we run that relationship. Secondly, we did talk about the signing of the new partnership in May this year and that has contributed to some of our momentum this quarter. Our pipeline has expanded nicely in the partnership funnel as well, but there is also an element of elevation of our relationship and the fact that we are now at the front end of number of these deals. From a trajectory perspective, we were in the low to mid $50 millions of quarter revenue in HP/DXC FY17. We have moved this to the $60 millions range. This quarter is almost $60 million-plus. So I think it is fair to assume that the run rate will obviously be sustained at this level. The deals that we are signing are not one-off or short-term, we typically have a longer-term duration. But as I said, it is work in progress, there's a lot more to be done to monetize all the four relationships.

Gaurav Rateria: Sure. Last question on the Digital Risk, you talked about margin improvement. Where are the margins currently versus the peak levels? And even if the revenue growth doesn't come back, what initiatives you have taken for that to help on the margin part?

Nitin Rakesh: Yes, I think the reason where I said that margin should expand, one, we think that the topline should actually get a little more tailwind from the deal wins we had in the last quarter and this quarter. So the margins that were in the mid-single digits at an EBIT level, expected to actually climb towards high-single digits over the next couple of quarters. And that's a combination of not only revenue, but also the efficiency efforts that we have underplay, both from a cost perspective and leveraging our offshore centers.

Moderator: Thank you. The next question is from the line of Dipesh Mehta from SBICAP Securities. Please go ahead.

Dipesh Mehta: Sir, just want to understand about the deal intake. I think you covered it earlier, but just to get more sense about what is working well for us, mining or hunting, if you can provide color from that perspective? And how do you expect it going forward, where you expect more effort required to continue to have this kind of strong deal win? Second question is about DXC. You had touched upon about four areas, but if I look service-wise, we have seen significant traction this quarter from help desk related services. So if you can, provide some color there as well.

Nitin Rakesh: Sure. So let me address the first question. I think, let me give you a little bridge on the TCV side. The TCV wins that were consistent in the range of $90 to $95 million quarterly, now at about $180 million plus this quarter. So we are effectively seeing almost doubling of the funnel. What was working well for us in the last couple of years was the wallet share gain in our existing relationships, especially Strategic Accounts within Direct Core. I think that will continue. That has continued to contribute and we are continuing to do well what we did well. What has added from the $90-ish number to the $180-ish million number is two more levers that we applied; one, we had some good traction in new logo wins both within Blackstone as well as outside the Blackstone. Outside of the Blackstone, again, I think it is an effort. We have chosen our areas within banking and insurance, wealth management, consumer banking, mortgages, as well as the P&C insurance and I think that's where we are starting to see our focus and specialist approach with doubling down on the cloud and cognitive capability. So that's helping us win new clients in both US and Europe. Secondly, within the Blackstone portfolio, we talked about the four wins that we had between Q4 and Q1 when we did the last call, and that has actually become another engine of growth that is adding to the TCV. So what we are really doing is we are keeping our focus on strategic accounts in existing relationships, we continue to focus on winning more market share, but added two more dimensions of growth. And we still have a lot more work to do in the pure hunting side as well. Yes, we have done well in the Blackstone portfolio, but that's not the only place that we want to go and hunt, we also want to go hunt in the open market in our chosen areas in our chosen geographies. So that is the little bridge from $90-ish to our $180-ish million TCV this quarter. Coming to your second question about the DXC/HP wins, as I mentioned to you, the focus that we have is to look at traditional or core IT areas and apply an element of service transformation. So what that may appear to you as service desk or core infra, apply the same logic example I gave you on InfraGenie with the ISG Paragon Award that we announced where we are automating using AI, the whole infra management piece, and that is kind of a focus that has actually worked well this quarter with HP/DXC. As well as I think there's an element of the partnership deal wins that we talked about that has started deploying. Again, early days for the partnership on cloud and application transformation, but I think that will become a good contributor to growth over the next three to four quarters.

Dipesh Mehta: So broadly on DXC related engagement is what is reflecting into our help desk kind of thing, that's what you're alluding to?

Nitin Rakesh: No, I think it's not just DXC, but I said there are four vectors of relationship in HP, some are doing better than the other, some have still some more work to do because we are still within the first quarter of actually applying those core strategic growth engines. So I think it's fair to assume that the focus right now is on finding growth across those four segments.

Moderator: Thank you. The next question is from the line of Apurva Prasad from HDFC Securities. Please go ahead.

Apurva Prasad: My first question pertains to the Direct Core part of the business; I mean I am presuming most of the TCV would largely be in that pocket. So do we see the current TCV level sustainable going ahead? That's one.

Nitin Rakesh: Thanks for your feedback. You are right, we have seen very significant deal wins in the Direct Core business. As I explained, that is kind of coming from those distinct engines of growth that we have talked about. There is an element of DR wins there as well. We called for one large deal win in DR last quarter as well and we have had some wins this quarter. But I think the trajectory in Direct Core has clearly moved higher by a significant amount. So the way I look at it is that if we continue to execute well on strategic accounts, new logos and the Blackstone portfolio, we should be able to continue to seean elevated level of deal wins. Now not every quarter is going to be a blowout quarter with 100% growth on deal wins, but I think it's fair to assume that from a trajectory perspective, if we can get into the 100 plus million deal wins quarterly, that will obviously aid revenue growth on a go-forward basis.

Apurva Prasad: Great. That's helpful. Also on the DXC side of it, I mean, counterintuitively, is there a margin risk now based on investments required to sustain growth, now that you know we are looking at growth within that portfolio?

Nitin Rakesh: Life is all about constraint, so obviously we have to make sure that we are able to find opportunities to grow the revenue. And as I defined the four dimensions of growth: sustainable, profitable, differentiated and inclusive, we are firstly very pleased that we were able to find growth in a challenging market environment where most of our peers have struggled to see this level of growth. I think it is our level of confidence in applying our service transformation capabilities, our ability to then use that automation and cloud opportunities to then find margin as we monetize this growth is fairly high. So our focus really as I said is to put growth above everything else, but at the same time we will find ways to continue to find profitable growth.

Moderator: Thank you. The next question is from the line of Madhu Babu from Prabhudas Lilladher. Please go ahead.

Madhu Babu: Sir, can you give the timeframe for execution of this 183 million TCV? Is there any one big lumpy order which is going to be executed over five- six year period kind of?

Nitin Rakesh: Yes, as I said earlier, there is nothing to call out on the duration. Most of these are multi-year deals. The average duration of most of our deals is three years, and this was fairly consistent with that. So there is no one large deal driving this. I think it's fairly consistent across those multiple channels I talked about.

Madhu Babu: And considering the good start we had this year, so are we looking to beat the NASSCOM growth rate for the overall company level?

Nitin Rakesh: Yes, I think the way I've answered that is that within Direct Core we had a good track record last two years of beating the NASSCOM growth fairly handsomely. We will continue to focus on that for this year as well. HP was a drag on our growth last few years. FY17 was a year of stability; we saw flat-lining of revenue on a sequential basis even though on a YoY basis it was still declining. Now that we are starting to see growth in HP on both sequential and YoY basis, that will contribute to growth. Our aspiration would be to bring HP channel at least to market growth and Direct Core to above market. Obviously, there will be some offsets to that through our other businesses, but that's kind of the way we are driving internally.

Madhu Babu: And sir, what is driving the growth in the top client, as well as the insurance which is seeing a weakness in a large client. Can you give an outlook on those two accounts?

Nitin Rakesh: Yes, there is robust growth in all our top relationships. We also had some decent client concentration numbers in terms of the trajectory. So again very stable growth in all our top relationships. So again we see every account as a growth account and that's the mindset we are taking to every large relationship. On the specific client that you talked about in insurance, we did say last quarter that we still see couple of quarters of work to be done. I think there is effort that are continuing on both sides on our end as well as on the customer end to find stability and I think in next quarter or two we should see hopefully better outcome.

Madhu Babu: And sir, our reported margins have been by the hedge gains, which have been good for us for the last two to three quarters and which are likely to continue another two quarters. So how do we see margins after that hedge gains evaporate. I mean, because that topline is being benefited from the hedge gains as well. So by that time do we expect that onsite transitions will be over, and you can come into steady state?

Nitin Rakesh: Yes, so I'll tell you the broad approach and then Surya will give a little more detail. The broad approach really is to, as you rightly said, use a couple of quarters to find operating efficiency, as well as offshore leverage to the deals that we are winning and apply service transformation. I think we are also moving the needle slowly but surely on the fixed price component. Right now, we are at about 21% which has marginally increased over the last quarter. Hopefully we will see that slowly inching up and that gives us more flexibility in the way we run the operation. On the hedge side, Surya can give some comments.

V. Suryanarayanan: So Madhu, you are right, the hedge gains will not be at the same levels a few quarters down the line. But as Nitin mentioned, combination of factors of these deals which will be shifting more into offshore once they reach a steady state and also the increase in the fixed price type of deals along with increased utilization will help us offset the lower hedge gains in the following quarters.

Nitin Rakesh: I think the other thing to keep in mind is we did say that our revenue growth and our headcount growth will actually be delinked. So if you see this quarter also I think that is actually how well we can execute on that, especially with offshore leverage is really going to determine over the next two quarters how well we are able to monetize this particular trend.

Moderator: Thank you. The next question is from the line of Priya Rohira from Axis Capital. Please go ahead.

Priya Rohira: My first question relates more to the deal wins. Are we seeing it more because of you mentioned about the four vectors of growth. Is there a certain trend which you're seeing because the US geography contrary to the BPOs you have showcased quite a good strength, is it because you accelerated investments you have made over there? And more so in terms of the pipeline, how would we see various geographies kicking in?

Nitin Rakesh: Thanks, Priya. I think almost 80% of our business is in North America within that US, so that's clearly an area of strength and we continue to operate from that position. The investments that we are making on repurposing in many cases obviously are raising. As I said, we had good capabilities in mining our relationships and we are now adding to the capabilities in hunting and using our position within the portfolio of Blackstone companies. So I think those two have definitely helped. Very large portion of Blackstone portfolio happens to be US centric, so that obviously skews that towards the US as well. We are happy with the progress we made in Europe, but as I said, my internal goal with the team and our focus is to expand Europe faster than company growth. So we will be making more investments in the current quarter in that geography, especially in client-facing and solution teams. We had some good wins to-date, but I think there is more to be done. So hopefully Europe will contribute faster to growth through the remainder of the year as well as FY19.

Priya Rohira: Sure. That's helpful. And secondly, is it possible to get an update on Blackstone, you mentioned about four inroads in Q1, and I am sure there has been a good decent progress reflected in the 183 million deal wins, but any color in terms of lead tractions or converts which you have seen this quarter?

Nitin Rakesh: We took a systematic approach for the Blackstone portfolio, identifying companies where they had the scale or a boiling platform and where we had a good complement of capabilities and overlaps. We talked about the number of clients last quarter and we are now announcing the TCV wins that are included in our overall $183 million number. So good traction in this quarter. We think there will be good traction as we go through the next couple of quarters as well. But that's not the only engine of growth that we either had or we want to focus on. So it will be included in our overall Direct Core growth as we move forward and we are very pleased with the early progress and the momentum we are seeing there.

Priya Rohira: Sure, and just a last more book keeping type of question. In the information, technology and the communication and entertainment vertical, there seems to be a substantial decline in the margin this quarter. Was there any one-off which came in this quarter?

Nitin Rakesh: I think it's linked directly to the deal wins. You see there's also the highest growth in that segment. So it's really a combination of those two things and the ramp ups that we had to do to start servicing that deal.

Moderator: Thank you. The next question is from the line of Ankit Pande from Quant Capital. Please go ahead.

Ankit Pande: Nitin, could you just talk about the rearrangement of the sales force in the way we are approaching, is that sort of completed? You talked about the approach being changed to more sort of across the board strategic IP-led approach, so is that completed? And secondly, if you could just roll over to the focus of deal wins; whether resulting from some single source deals or some self-ideated deals has that come through?

Nitin Rakesh: Sure. I think the reorganization or the reorientation of our investment dollars in client-facing teams is work in progress. We'll continue to repurpose, refocus because there are lot of moving parts in the market, there is still work to be done in playing some renewal deals. We just initiated that process. I think the ISG Paragon award win was kind of reflective of the fact that we are now elevating our position and our branding in the marketplace with the investments towards that purpose. So there is still more work to be done. I talked about expanding our footprint in Europe, so that's still work in progress. My expectation is that through the remainder of this financial year, we will continue to adjust and tweak, because we obviously have a quarterly rhythm and business to run while we make that reorientation. So this is not going to be sudden one swift jerk movement, it's a continuous adjustment that we'll repurpose. But I think the start has been good and thus reflecting in our wins and the focus on hunting as well as finding new engines of growth to complement on Strategic Accounts is very strong. On the second question about the wins and whether they were sole-sourced, I think it's a rarity to get large deals on a sole-source basis; even where we have very strong references or inroads or existing accounts, I think it is very rare. But clearly there are opportunities that we monetized this quarter. So I think no one side, it's a combination of multiple approaches. Even if there is a proactive deal that we created, we have had to go through price benchmarking in some cases, we had to go through competitive bids and RFPs and other cases. So it's a fairly mixed bag, but there are deal wins that are full source and there are obviously a number of competitively won deals as well.

Ankit Pande: Great. Thanks for that. And just a couple of small clarifications. The question earlier from, I think, Dipesh on service technical help desk moving up and contribution to revenue by 3% points, would I read your comments as that is likely to normalize and it's just an outcome of the new deal wins?

Nitin Rakesh: Yes, I think it will normalize, because as I said, what we are really doing is we are using our capabilities that have been built up over the last couple of years very strongly right now to disrupt some of these traditional IT service areas and building a bridge using automation and cognitive. So it will normalize, but there may be something else that may show up, because again, I think one of the advantages we have at our price and scale is that we can be fairly disruptive in some of these deals because we have the capabilities and the track record.

Ankit Pande: Sir, just to add to it, do you think that the increasing concentration in this particular service line was a little bit of a drag on the margins?

Nitin Rakesh: I think it would have been the same outcome even if it was some other service line, because as I said right when you have such a large traction, again, keep in mind, not only did we show you almost a doubling of deal wins in Direct channel, we also showed you double-digit sequential growth in the HP channel. I think that's bound to have some impact on your ability to actually fund staff and execute, so I think that's kind of what you are seeing right now actually.

Ankit Pande: Great. Okay. And the other clarification was related to, you talked about operating margins maybe hitting high tens in coming quarters. Was that pertaining just to Digital Risk?

Nitin Rakesh: We are talking about high-single digit of operating margins.

Ankit Pande: High-single digits.

Nitin Rakesh: Yes, high-single digit for Digital Risk. I think at the company level we did say EBIT of 14 to 16, I know and we are at the lower end of that right now, but we're still maintaining that band at a broad level.

Ankit Pande: Great. Thanks, thanks a lot for that clarification. And just one margin related question. Are the wage hikes expected to come next quarter?

Nitin Rakesh: That is our typical cycle, yes.

Ankit Pande: Any quantification of the amount of wage hikes?

Nitin Rakesh: I think we'll update you in the next call.

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

Sandeep Shah: Just one query like most of the growth in this quarter has been largely driven through ITO and generally we have seen that whenever the ramp-up comes on the ITO, the onsite contribution does not go up. So is it like the nature of the growth in the ITO was much different? And if it is driven through automation, why the gross margins have declined? Why this has led to an onsite driven cost?

Nitin Rakesh: Again as I said, there is a certain rhythm and a trajectory. When you win new business, you transition it, and while you transition it, you transition it on an as-is basis and then you apply service transformation to it. So we are taking a fairly transformative approach to applying, the InfraGenie capability that I talked about which was recognized even by the market, is primarily in the ITO space. We don't differentiate growth if it comes from any of our service lines. We are actually fairly pleased that we are able to capture market share and use our disruptive capability to demonstrate a position that actually gives us a very strong reference to be in the market as well. So I would not get too worried about whether it's in apps or ITO. I think the question is, is it in the right areas and are we actually applying the right set of capabilities to it.

Sandeep Shah: Okay. Just on the TCV, is it possible to break down what TCV through Blackstone and Digital Risk in this quarter?

Nitin Rakesh: The way we are reporting it is through Direct International and I think we'll keep it at that consolidated level, because on the like-to-like basis, you are able to see what it was and where it is. So I think that is kind of the norm that we'll continue to follow.

Sandeep Shah: Okay. And for the full year we still expect 14% to 16% kind of EBIT level margin, right?

Nitin Rakesh: Yes, I think we are at the lower end of that right now. We will obviously update you as we progress, it's only been one quarter. As I said, we have a lot of work to do to ensure that we execute the deals as we expect them to, but it's fair to assume that we will stay in that band;

whether we end up towards the lower end, midpoint of higher end, we'll continue to update you through the quarters.

Moderator: Thank you. Next question is from the line of Shashi Bhusan from IDFC Securities. Please go ahead.

Shashi Bhusan: Over the last few quarters our deal closures have been predominantly in new gen services but our growth in the quarter was in tech help desk and transaction processing. Can you please help me reconcile this and the nature of work we are doing here?

Nitin Rakesh: Let me answer that and then you can go to the second one. And the reason is, I think what I'm trying to tell you is the bridge between what used to be legacy or core and new-gen. I could still do app management or app development. But if I am able to apply DevOps automation to development process that actually turns it into a cloud-enabled application development cycle, and that turns into new gen service. If I am able to apply cognitive and AI to infra management, I mean, for example, again I'll refer you back to the publicly announced award that we won last quarter and we'll circulate that announcement once again, so you can actually understand what that capability does. Idea was to actually apply cognitive and predictive analytics using AI to an infra management piece where the effort elimination was to the tune of almost 52%. And the primary reason for that was because we are moving away from just using a reactive ticketing process to a predictive analytics on whether the application or the infrastructure will crash. So I think that is a transformative approach, so when we say that it's new gen with applying AI or cognitive to a traditional IT service, I'm actually turning it into new gen service, because I can then operate it in a new modern way. So I think again, we'll have to do some work to make sure that our segment reporting while we want continue to report the segment that you are used to see, we will also obviously have to find ways to continue to disseminate information about how we are transforming our core business because that also leads to protecting our core because unless I'm able to transform the core using service transformation, that core of what we have done over the last 20 years, almost always become a drag or risk.

Shashi Bhusan: And second part of my question is again linked to that. Now, revenue from these services should be linked to the headcount addition, and that has not happened during the quarter. Any color on this would be helpful, sir.

Nitin Rakesh: Which is exactly what I just explained right. If I am able to actually eliminate effort, then the headcount required to deliver those services will be as of lower than what I was doing it with or even if I am transitioning it, it will be with a much lower headcount. So I think you will see efficiencies and optimization. The ability to apply these capabilities to our existing book of business and continuously transitioning them to new gen services is a very conscious effort that we are undertaking right now.

Shashi Bhusan: And during the quarter, was there any positive surprise or we anticipated at the beginning of the quarter this kind of growth to be delivered?

Nitin Rakesh: I think, the May call we talked about FY18 to be a growth year, we talked about growth coming from multiple channels. I actually talked about HP channel turning into growth. Obviously, there was a healthy skepticism which is good. And I think we have well begun, we have had a good initial success. Personally, we were not surprised with the momentum because we worked harder there and we could see the result coming through the last few weeks, but clearly I think it's well begun, it's half done, but it's only half done, because there's a lot of work to be done to execute and to continue the momentum as well.

Moderator: Thank you. The next question is from Ashwin Mehta from Nomura Securities. Please go ahead.

Ashwin Mehta: I had one question. You indicated that you are transitioning deals as is and then transforming them through automation. So would that result in revenues reducing on these deals when you start to disrupt these deals and margins going up? And secondly, would these margin benefits will then be passed on to the clients, how are you kind of structuring these deals?

Nitin Rakesh: I think there is an element of transformation in most of the deals, but obviously the impact for us is that when we transition the deal or when we win a new deal, we are baking in that element of automation. So I don't think the idea is to start at a higher level of revenue and then lower it ourselves. I think the idea is to price it and structure it in a way that we are able to actually monetize therefore the opportunity. So on the revenue side, the new wins, I don't think we'll see sequential drop from the same deal. However, there is still a healthy portion of core business that we are running traditionally. I think the attempt there is to also continue to transform those and bundle that with a higher wallet share. And that's what also the effort in our strategic accounts. On the margin side, I think, yes, the expectation is that over the next couple of quarters we should be able to find efficiencies. And the way we are pricing them is to bake some of that. Yes, obviously, we have to be value-add accretive to our customers and that's the only reason we are winning, but at the same time we also have to generate value for our own P&L. So that is the reason why I said over the next couple of quarters we will continue to execute towards that charter.

Ashwin Mehta: Okay. And just one follow-up, so when you win up these services or help desk services and then you're looking to transform them, is there a movement of people or a people takeover element involved in such deals?

Nitin Rakesh: It's a combination, and in some cases there is an element of restructuring; in some cases there is an element of looking at transitioning in max and then optimizing. So it depends on the type of the deal, the location, the duration, the difficulty in transition where there is an existing service line or not, but most of those deals will have a combination of many other things.

Moderator: Thank you. The next question is a follow-up question from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria: Nitin, what percentage of current revenues in Direct Core come from the digital next gen services? And could you help us understand the margin profile for this part of the revenues?

Nitin Rakesh: I think more than one-third of our revenue in Direct Core is new gen services and the effort is to continue to move that needle. Obviously, with such a high percentage of deal wins coming from those areas we'll see this needle moving surely, but certainly. On the margin front, we are not breaking it out by new gen versus core right now, but as I mentioned to you, I think the attempt and the charter for the teams internally is to apply transformation give value back to the client, but then also be able to shift some of that value back to us.

Gaurav Rateria: Sure. On the deal, can you highlight some quantification or some qualitative comments around what could be the deal wins in the HP/DXC channel and at what level you need to reach to get this part of the business to above industry growth rate like you mentioned $100 million as the quarterly number for Direct Core. Similarly, what could be that number for HP/DXC channel and where are we right now?

Nitin Rakesh: Yes. I think historically, we've not broken out the TCV wins in HP/DXC. I think it's still premature for us to start breaking that out. Maybe we will start giving you that data point over the next couple of quarters once we get into a sustainable steady state with the new revived strategic focus that we have on those four large relationships. But I think the single biggest barometer for you should really be the quarterly run rate until we do that. And this quarter obviously has moved from $53-point-some to almost $60 millon. I think the effort will be for us to continuously move that needle higher on a sequential basis.

Gaurav Rateria: Sure. Lastly, can you help us understand what was the impact of currency was there on the margins and net of hedges, what would be the impact for this quarter?

V. Suryanarayanan: Yes. So since we had a good hedge, the overall impact to the margins because of FX movement was very marginal.

Moderator: Thank you. Next question is a follow-up question from the line of Sandeep Shah from CIMB. Please go ahead.

Sandeep Shah: Yes, I just wanted to confirm that the TCV wins which we report are largely for the new business, it does not include any renewal as we continue to report on same basis what we used to report earlier?

Nitin Rakesh: Yes, that is correct.

Moderator: Thank you. As there are no further questions, I now hand the conference over to Mr. Nitin Rakesh for closing comments. Over to you, sir.

Nitin Rakesh: Again, thank you all for joining us. As I said, we are glad with where we started the financial year. We still have a fairly heavy agenda through the rest of the year both in terms of our servicing, our ongoing customers, executing on the deals we won, continuing to build the pipeline, and finally continue to convert that pipeline. So we look forward to talking to you again in the next quarter. And in the interim if there are further follow-up questions, please feel free to reach out to our CFO and our IR team. Thanks a lot.

Moderator: Thank you very much members of management. Ladies and gentlemen, on behalf of Mphasis Limited, that concludes this conference. Thank you all for joining us and you may now disconnect your lines.