"Mphasis Q4 & FY19 Earnings Conference Call"

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Moderator: Good day, ladies and gentlemen, and welcome to the Q4 & FY 2019 Earnings Conference Call of Mphasis. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded.

If you do not have access to the webcast link, the same presentation of the webcast is also available on Mphasis website, www.mphasis.com under the 'Investor' section. The same is also updated on the BSE and NSE website. I now hand the conference over to Mr. Shiv Muttoo from CDR India. Thank you and over to you, sir.

Shiv Muttoo: Thanks, Margaret. Good afternoon, everyone and thank you for joining us on Mphasis Q4 FY'19 earnings conference call. We have with us today Mr. Nitin Rakesh -- CEO; and Mr. V. Suryanarayanan -- CFO of the company.

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 detail statement in this regard is available in the 'Q4 FY'19 Results Announcement Release' that has been sent out to all of you earlier.

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

Nitin Rakesh: Thank you, Shiv. Good afternoon, everybody. Thanks for joining our call today. Trust you had the opportunity to go through our Q4 as well as Full Year FY '19 Results and Other Operational Information in our MD&A.

Before I dive into Q4 and our FY'19 full year earnings, let me begin with an overview of the macro trends that we are seeing as well as the impact of this on our clients and how we are preparing to stay ahead of it.

As a customer obsessed technology organization, our aspiration is to help enterprises adopt and apply technology to keep them relevant to their end customers. We have chosen our purpose to be the 'driver in the driverless car'- the software that powers the world to every enterprise.

Consumers are driving the real disruption with the changing demand from enterprises. Need for agility by our clients businesses to meet their ever increasing competitive pressures and to enable them to launch products and services quicker is driving a very different pattern of consumption of technology. By design, the technology consumption patterns have moved away from big multi-year decisions focused on heavy upfront CAPEX-style investments and the build-out of on-premise applications, custom or off-the-shelf to technology consumption that is now mostly done on a "pay-as-you-go" basis with measurable results and all the while having the flexibility to quickly divert investments to a business case where the outcomes match the need of the customers.

Since our business is a reflection of the way technology is consumed by the enterprise clients, this change has huge implications on our future especially as the pace of change accelerates. Consider a traditional application outsourcing deal, which called for building a new system over a three-year period with cycles of dev, test, deployment and production resulting in a multi-year opportunity. This is now history! We have been asked to help build a rapid deployment model starting with a minimum viable product, leading to a business case approval to build further and funding being released in phases with the business choosing to have the option to adapt and adjust the functionality at any point.

While the client business gets more agile this way, the nature of our business changes, demand for new-gen skills increases and the requirements for investment escalates.

This dynamic is amplified for all our clients, creating a seismic shift in the way we must plan, manage, run and invest in the business, and this dynamic is not limited to Mphasis alone. But is industry wide encompassing all forms of technology companies not only services companies. Of course, this very disruption comes with unprecedented opportunities. As such, we continue to invest in staying ahead of competitors in positioning ourselves as enablers of the "new normal" This, however does result in many short to medium-term challenges and the dynamics should be managed with the size of opportunity on one hand and the risk of obsolescence on the other.

Cloud companies like AWS, Google and Azure are accelerating the development of additional capabilities that make the consumption of cloud services far richer as well as accelerate deployment of new software and adoption of Cloud, providing new opportunities while accelerating disruption of traditional service lines.

IT services companies like us need to have a distinct value propositions in cloud, devops, native app dev, migration and cloud ops as well as build capabilities across the stack.

We, at Mphasis, have come a long way in managing these dynamics and still have a lot further to go as we continue to navigate the future in helping our clients make the same transition. The next phase will require combination of skills, scale, smart, maturity and, above all extreme nimbleness to adjust and adapt.

We have used the twin themes of consistency and transformation as we have navigated this journey over the past two years.

There is no better validation than our annual performance that clearly indicates consistent growth. Consolidated gross revenue grew 22.6% on a reported basis and 14.2% in constant currency in FY'19. This is the highest growth for the company in the past 10-years. Consecutive years of double-digit growth in Direct Core and DXC/HP has helped our transformation and is driving consistent overall growth as we dwell deeper into these units in a short while from now. The net revenue for FY'19 grew 18.1% on a reported basis.

We have been able to deliver consistent double-digit growth in both Direct Core and DXC/HP business and an overall margin improvement of 100 basis points in FY'19. On a quarterly basis in Q4, consolidated revenue grew 2.2% on a reported basis and 2.9% in constant currency terms. Direct Core revenue grew 2.9% QoQ on reported basis and 3.7% QoQ in constant currency terms. DXC/HP business was flat on reported basis sequentially and grew 0.4% in constant currency. Digital Risk business revenue grew this quarter. We also have had significant deal wins from this business in Q4. We are confident of stabilizing our Digital Risk business and bringing this back to our stated revenue band of $28-30 million as we progress through FY'20.

New deal wins which is another key lead indicator of our sustained growth continues to see momentum. In Q4'19, Direct International TCV stood at $146 million and totals to $616 million for the full year FY'19. Of this, 79% of new deal wins are New Gen Services, showcasing our continuing transformation of service portfolio is right in the middle of driving growth.

On the back of strong revenue performance, the other key financial metrics improved as well. We are pleased with the growth in operating profit. We delivered an increase in operating margin by 100 basis points in FY'19 and our operating profits grew 25.9%. Let me re-emphasize that this margin growth has been achieved despite headwinds from hedge losses resulting from rupee depreciation and volatility in the Digital Risk business. The operating margin for Q4 remain flat at 15.8% due to higher employee benefits and related expenses to some deals in this quarter.

We were able to successfully deliver on our optimization plans through the year and this has given us the headroom to make significant capability investment in Talent Next, NEXT labs, Stelligent etc.

Further during FY'19 we completed another buyback with an outlay of Rs.9,949 million as part of our overall philosophy to enhance the shareholder value. The growth in operating profit helped us deliver strong EPS growth for FY'19 at 31.4% to Rs.56.1.

With this, I am pleased to inform that the Board of Directors have recommended a dividend of Rs.27 per share subject to shareholder approval which gross of dividend tax represents payout of 58% of FY'19 net profit consistent with our past practices.

Our operating cash generation remain strong, and total cash on the balance sheet as on 31st March stood at Rs.19,864; approximately $287 million.

Now let us look at the DXC/HP business. Many still have historic overhang of constant decline in revenues in the period up to FY'16-'17. This is behind us. We are now encouraged by the continued and healthy growth in this channel. Our strategic client engagement partnership, focusing on capability backed and solution-led approach to go to market is yielding good results.

We won significant large transformation deals with DXC/HP during the year FY'19. Revenue grew 32% on a reported basis and 22.9% in constant currency, making a consecutive year of (+20%) growth in this channel.

Over the past eight quarters, we have purposefully transformed our relationship to stem the decline and make it a growth channel. This coupled with our current MSA which runs up to 2027 provides us a powerful platform to continue this journey.

The Three Themes of our Transformation as laid out at the beginning of FY'18 were: Move from a traditional outsourcing supplier to a strategic partner, expand geographical footprint, and be a growth partner by being in the path of revenue for DXC. Let us see how we have faired in our transformation journey.

As you can see in FY'16, our footprint was predominantly Americas and in the ITO segment. In FY'17, we brought on new leadership, addressed the relationship issues and changed our mindset to that of growth. This is what we call the "work for segment" of our business. This resulted in DXC announcing us as the "Apps to Cloud Strategic Solution Partner" to transform and modernize enterprise applications for public, private and hybrid cloud. This partnership is built on our ability to deliver faster transformation, lower costs and right skills to transform the business in a digital world. This was the start of the "work with" segment of our business. This was also a testament to our teams working well with DXC, the consistent delivery track record and Next Gen IT offerings brought to the clients built on DXC and Mphasis IP.

In early FY '18, we won our first services transformation deal engagement, a multi-year complex contract based on delivering business outcomes. Also, we laid the foundation for penetration into Europe while re-establishing our presence in Australia and UK. In FY'19, we further strengthened our DXC growth partner status by announcement of DMX (DXC – Mphasis Next)where our teams worked alongside DXC directly in their accounts, expanding application footprint for them. This is the "Work As" segment of our business.

As you see, our transformation of business mix is continuing, and currently we have less than 30% of the work which is traditional outsourcing. The shift is towards outcome-based, multi-year service transformation contracts with upfront investments. Our geographical footprint has expanded, and currently one-third of revenues are generated from non-America geographies within DXC. All of this is reflected in our compounded quarterly growth rate which has grown at over 5% over the past eight quarters.

You will notice transformation, consistency and maniacal focus towards our clients and they are in this journey. This is a showcase of Mphasis' clarity and strategy, relentless execution and testimony to the trust and relationship we built our clients.

Based on our transformation track record, we are in a vantage position to continue our growth by placing the following strategic bets.

Let me start with service transformation: The objective of this vector is to partner for DXC in their value capture journey by reducing their cost of run business. We extensively deploy automation, cognitive assets for both DXC and Mphasis to achieve contracted outcomes. Naturally, there is a gestation cycle for this investment driven deals. This also gives us a good play as DXC looks to reduce non-strategic vendors and their spend there.

The second vector is to 'Accelerate Applications' growth for DXC. We plan to double down on our "work with" and "work as" motions. That is provide strategic solutions coverage in select areas and increase coverage for DXC end customers. We also see opportunity in jointly pursuing legacy modernization of client IT estates. Our combined strength put us in good shape to lead this market.

Finally, we are also expanding our vertical footprint. We have already started with insurance because we believe we have the ability to replicate the Ingenium CoE model that we currently run for DXC for other products. We all know that DXC is a market leader in insurance and we see potential in this investment. We are also exploring additional vertical specific areas that could add growth head room.

With the above bet and our past eight quarter track record, this segment continues to present growth proposition for us at Mphasis.

Switching to Direct Core segment, which is our primary driver for long-term growth. In our investment thesis laid out at the beginning of FY'18, we had called out for accelerating Direct Core as a primary vector of long-term growth. Direct Core revenue grew 25.4% on a reported basis and 16.3% in constant currency in FY'19 which has been the highest growth in this segment ever with the compounded quarterly growth rate accelerating to 4% over the last eight quarters in a consistent manner.

The tremendous success of Direct Core is pivoted around three main pillars for growth -- Strategic Customers, Blackstone Portfolio, and Our New Client Acquisition Group. We are happy to report that all three growth engines contributed significantly towards strong results in FY'19.

Strategic accounts are marquee clients who represent a significant portion of our Direct Core business. Over the years, we have built on strong relationships and deep domain expertise in our client businesses which has enabled us to expand our engagement and gain wallet share. Another vector that was added was through differentiation in service offerings.

In Blackstone channel, on the back of strong execution of some of the large deals won in FY'18, this group has almost doubled in revenue and witnessed strong growth we anticipated. We continue to add more clients in this channel and believe there are continued opportunities to the existing Blackstone client base as well as the ever-expanding Blackstone portfolio.

For new client acquisitions, we registered significant revenue growth of over 80% in FY'19. This has become a strong growth engine contributing meaningfully to the Direct Core growth and is a testimony to our differentiation in the market. As you can see from the data, all three segments of Direct Core, as called out in FY'18 investment thesis have meaningfully contributed towards acceleration in this segment and the segment is not dependent on any one category, thereby giving us confidence in the continuation of consistent growth theme at above market rates.

The significant capability built around New Gen Services helped us deliver strong TCV growth in FY'19. Direct International business won new deals worth of $616 million TCV with 79% of these wins in New Gen Services. I am happy to state that New Gen Services now contribute 46% of Direct Core revenues in FY'19 representing YoY growth of 45%.

We are also building a strong ecosystem of best-in-class partners, such as Amazon Web Services, Pivotal, Esgyn, Camunda, etc.

Recently, we were named Gold Partner with Microsoft for Cloud Application Development and have also partnered with Google Cloud for Joint Build and GTM. These relationships have enabled us to generate a strong deal flow with 30%, a healthy portion of our wins involving the partner ecosystem, especially in New Gen services, consistent with the transformation theme.

With the knowledge that every business is a digital business, we are proactively providing a roadmap for our clients to help them in their digital transformation journey.

Given the current state of enterprise IT and operations businesses, the critical role of enabling our clients for digital IT readiness falls squarely on firms like us. We will continue to expand our offerings across "Services Transformation" to help bridge legacy IT to digital IT. Applying automation to all aspects of core IT from QA to infra to applications, becomes a key aspect of this offering.

We launched a unique corporate strategy framework of bringing the "T back into IT" as we architected the front-to-back digital transformation approach, our customer-centric transformation framework involving and providing hyper personalized customer experience.

Digital technologies, especially consumer facing tech, driven by the immense focus on end customers leads us to also continue to expand our focus on this segment, commonly known as Front End Digital technologies, cloud native app development, analytics, DevOps with CI/CD etc.

In terms of packaging these offerings, we believe that trends such as hyper-cloud, hyper-personalization and use of a "Customer First" approach, means that Cloud & Cognitive become the two foundations of this approach, combined with our unique strengths in certain business domains, (or industry sub-verticals) – the outcome is a T-Shaped solution offering – a unique value digital proposition, tailored to our industry focus i.e. horizontal + vertical

I am enthused that we have aligned ourselves to some of the megatrends using the front to back approach, which lends itself very nicely to the trends of customer in the center of everything. It powers many tenets of true digital experience and most importantly enterprises that are looking to monetize pre-existing IT assets, including legacy.

The approach calls for an iterative, non-intrusive and domain-contextualized approach that leverages on our ever-expanding library of IP assets. Complemented with service transformation framework, this approach prevents a compelling proposition for an end-to-end IT services platform.

Talent is another big area of transformation, and I will cover that separately in a few minutes.

As explained above, the way clients are buying technology is fundamentally changing. We made many choices over the past two years, and the approach we have taken to build a cloud-native cognitive first business model with investments in areas like platforms and building IP assets using NEXTlabs, Talent Next as well as adopting client-centric org design, with a clearly defined purpose continues to give us confidence that we are on the right track.

With scale built through strong revenue growth in Next Gen services in the past couple of years, we have created core portfolios with the objective of creating truly world-class capabilities in areas such as DevOps, Next Gen Cloud-Native App Dev, Legacy Application Modernization, Enterprise Automation and so on. We continuously scan the market and our client base to explore and evaluate how best to identify areas of further investment and focus.

The application of cutting-edge technology is the driver of our success as we relentlessly strive towards becoming world-class across all of our focus portfolios. We also decided to apply an agile approach and pivot our go-to-market around a portfolio-led Tribe and Squad model.

Tribes are cross-functional teams focused on developing, evolving and building Next Gen offerings. Each portfolio Tribe has cross functional squads that come together on a need basis to focus on specific milestone development or live deals using agile methodologies. The Tribe-Squad Model has significantly changed the way we engage with our clients bringing agility and innovation to our engagement. Design Thinking, Workshops, Hackathons and Co-innovation have become the new normal with our client base.

All of this coming together and becoming real for our clients is extremely important. Let me give you a couple of client examples: Our Modernization Tribe accelerated the pace of legacy modernization for a Fortune 50 company by leveraging cloud-based capabilities and frameworks including containers. This client had limited time as well as lack of adequate upfront investment funds to transform the core system, thus losing market share to competitors. Post our transformation project, the client has experienced high velocity phase modernization and the ability to fund the same while reducing the cost of run through extreme automation. Similarly, leveraging our Next Gen App Dev Tribe, we built a Cloud-based high transaction, high performance global payment system at a Fortune 50 bank. The bank had a large number of organically grown systems but was unable to roll out products fast enough because of risk they were losing business to competition. Post the transformation project, the client was able to rapidly scale the daily transaction volume as well as accelerate the speed to launch for new payment products in new territories both for integrated, high value and low value payment transactions. The results speak for themselves.

The creation of IP and reusable artefacts is structured around three main areas of focus: Cognitive Computing, Cloud-Centric Solutions and large-scale Services Transformation. Our innovation labs have built several extremely effective IP assets and have also been recognized by leading analysts and raked up a few pretty impressive awards. We are also proud to announce that Mphasis has been now granted first US patent this year.

Finally, no transformation would be complete without people transformation. Let me give you a brief overview of the same. Talent Next is a companywide program to build and proactively develop New Gen skills internally. It was launched in FY'18 with the aim of upskilling and cross-scaling our workforce, having learners certified on Next Gen skills and effective deployment of the same certified pool i.e by reducing fulfillment latency becoming the high level objectives of this program. Since inception, we have had five successful sprints, including the two that are currently running. Across them, we have had over 60 skill proficiency solutions. A large portion of our associates have been certified and continue to increase their proficiency levels through the continued use of the platform, creating a flywheel of opportunities and fulfillment in New Gen skills. Our focus is about "bringing the T back in IT" for talent as well. Our approach to leading solutioning with architecture, engineering and design is paying rich dividends and creating a culture of continuous learning and development.

I would like to take a moment to reflect on the past two years of our transformation, especially as it relates to a competitive positioning in the market with above-market growth signaling that our clients are continuing to work for us with their business as well as getting recognition from industry analysts and opinion makers.

Overall, we are pleased with the execution of our strategic priorities of this year with strong revenue growth across all major business segments on the back of strong TCV wins. We are also pleased with the health of our pipeline, the build-up of our capabilities, both organically and inorganically which we have built across service offering portfolio as I just talked about and our continued strong execution in New Gen services.

There are a few metrics that are noteworthy as I have discussed over the past few minutes. We will continue to execute on our plan for FY'20 and beyond with continued focus on our primary growth drivers -- Direct Core, where we expect to outgrow the market, as well as DXC/HP where our focus as discussed will be on continuous transformation of the relationship, so we continue to see growth. Besides that, we will continue to focus on operational execution and margin optimization to fuel growth with expected EBIT in the 15-17% range for FY'20.

I thank you for all your support and interest in Mphasis, and as always, I request the operator to open the line for questions.

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

Gaurav Rateria: Nitin, three questions: The first question is on DXC. While we understand that there is a lot of room for penetrating more into this account and you outlaid many such engines for the future growth. How should one think about the framework of renewal of the MSA relationship in 2021? Can there be any discussion around productivity sharing benefit with the client or is this a completely different kind of arrangement where one should not think about a normal contract renewal kind of a thing?

Nitin Rakesh: Gaurav, thanks for that. Good question. As I mentioned in my remarks, MSA actually is valid until 2027. So, there is no MSA renewal clause coming up. The only thing that changes at the end of five years which is in 2021 is the minimum revenue commitment actually goes away. For the MSA does not have to be renewed, MSA will actually automatically renew and be valid until 2027. So, you should not think of a binary event that is coming up that actually risks this channel. Secondly, as you look at the way we are driving transformation through the GTM partnership, doing deals which are primarily service transformation, expanding geographically and more importantly, partnering with them to find new avenues of growth for DXC. This is a completely transformed relationship.

Gaurav Rateria: Fair to say that there will be no such discussion around pricing, etc. in 2021 when MRC goes away?

Nitin Rakesh: So, Gaurav, again, if you look at the vector that is driving the growth is multi-year service transformation type deals which means, one, we are helping them reduce their cost to serve which basically means that I bundle a bunch of services on outcome basis which by definition means that there is no rate card involvement in those deals because we have already bundled them as outcome based deals. So, the more we continue to use this vector for growth, the less risk there is for any pricing-related discussion causing disruption. But you and I both know that in all commercial agreements, there is almost always possibility of having a pricing discussion even during the term. So, there is no guarantee that there will never be a pricing discussion or ongoing commercial negotiation. But having said that, the reason why we gave this detail to you is because we are shifting from being just back office ITO services provider to actually being a true partner that is driving long term growth, and more importantly, giving them the operating leverage, they need in their business to execute.

Gaurav Rateria: Secondly, on the Direct Core, any trends with respect to what is happening on the BFSI sector? Any sub-segment-wise color on that? Have you seen any behavioral change from clients with respect to pushing out of the deals or taking longer time to make their decisions?

Nitin Rakesh: The environment for New Gen Services is pretty healthy. There is definitely more and more appetite for adoption of the consumption-driven technology models. Cloud becomes the center of that. There is definitely not a whole lot of demand in traditional core IT services, the outsourcing deals. So, there will always be churn in deals. But for the right set of skills and capabilities and the ability to adopt new tech, the environment is actually fairly healthy.

Gaurav Rateria: On the margin side, you had laid out a program to systematically improve margins consecutively for the three years you said. FY'20 is going to be the third year. In that case, the guidance or the outlook looks to be of stable margin. Are there any specific headwinds with respect to supply side challenges in the US? Any details around that will be helpful.

Nitin Rakesh: Gaurav, again, we are just at the beginning of the year. We will continue to find ways to optimize operating efficiencies, but at the same time, continue to invest in building capabilities in the business. So, it is important to note that we want to keep some leverage with us. On YoY basis, the trajectory has been what we called out for at the beginning of this transformation journey in FY'18 and directionally we are still committed to finding continuous improvement.

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

Nitin Padmanabhan: Nitin, in your initial remarks, you mentioned that there will be certain investments required in line with the changing shape of IT. When you say 15-17%, I also understand that the hedge gains will be better for FY'20 on the revenue line. So, in that context, are we suggesting that part of those would be reinvested or how should one think about it?

Nitin Rakesh: Again it is too early in the year for us to decide where the hedge gain or loss will end up depending on where the currency stays. You can see from our MD&A the average hedge rates around 70 for FY '20. We are just at about breakeven right now, but yes, the thinking is if we do get some tailwind from hedge gains, that gives us the operating leverage to invest not only in building capability but more importantly in making sure that we are able to use some of that for investment into some of these large deals.

Nitin Padmanabhan: On the DXC business, that business has evolved quite a lot since we had earlier discussed. Two things there -- One is there is this 'as and with' which you described. If you could just explain what is the difference between as and with is? Within that, there is also this increasing share of their own subcon spends in terms of gaining share within that system for us. So, if you can split both portions of that and how should one think about growth there? Finally, do you think assumptions of a mid single digit growth in that business is completely misplaced in the context of the opportunity?

Nitin Rakesh: So, you have multiple questions in that but mostly all through DXC, so let me just explain. When we say "work for", "work with" and "work as", think of that as an evolving way of representing what Mphasis brings to that partnership. "Work for" basically is we are an extension of delivery, not visible to the end customer. "Work with" means that we jointly go and do solutioning. And "work as" means there are maybe deals where we are actually exclusively starting to deliver those deals. That basically means that the end customer has good visibility and appreciation of the partnership. Of course, they continue to be DXC customers, and we are very-very respectful of that because that is the best way for us to build a long-term partnership of trust. As it relates to the subcon spend, we have actually turned that headwind into an opportunity, because we have partnered with them over the last year or so, as they started to look at their cost to serve and given them the ability to derive some of those savings through the structured service transformation deal which do require some upfront investment and there will be some volatility on QoQ basis especially as it relates to making those investments because some of them do have an element of rebadging. Finally, we will be happy if we continue to have an at-market type growth for this channel. So, that should give you a pretty good directional sense of where we are driving.

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

Mukul Garg: Nitin, just on the Blackstone, you mentioned that you have doubled the revenues. How do you see the opportunity going forward -- Do you think you will be able to reach the 10% revenue share from Blackstone in FY'20/21 or do you think it is still long-term goal for you?

Nitin Rakesh: Mukul, again this is only the second year. This year we had a good monetization of the deals we sold early on in the journey in FY'18. I still think that this is a fairly early stage in our penetration into the channel. Good news is that, that portfolio of potential clients is ever expanding pool because Blackstone now has over 100 companies that are potential opportunities for us. So, the short answer is the opportunity is fairly long-term. We have been fairly diligent about the way we engage. So, we do not create a very long tail, but at the same time have meaningful partnership type client base in that segment. Again, if you look at it, about 3% of the Direct Core growth came from that channel. It represents about 5% of Direct Core revenue right now. We can continue to see that go up meaningfully over the next two to three years.

Mukul Garg: On the BFS side, how was the growth this quarter excluding the digital risk portfolio? What do you think about BFS -- Is it slowing down compared to what you have seen over the last few quarters? Are there any incremental risks which you are seeing as you enter FY'20? Can you give some more clarity?

Nitin Rakesh: It has been a fairly steady quarter from BFS portfolio perspective. There are segments of banking. They are obviously investing more ahead of the digital investments scale, especially consumer-facing payments, wealth management, retail, mortgages, all of them are at least investing in digital capabilities. So, even if I exclude DR, again, DR is very much part of that portfolio, the growth was fairly strong. It is actually above company growth in that segment for us if I look at the core IT business.

Moderator: Thank you. The next question is from the line of Ruchi Burde from BOB Capital Markets. Please go ahead.

Ruchi Burde: I wanted to check regarding the onsite revenue. So, if you look at the two data points, there is a reduction in our onsite headcount by about 200-odd people. However, the growth in onsite revenue was strong in the quarter. So, I was curious to know what explain these two contrasting data points?

Nitin Rakesh: The only answer as you can also see from our disclosure in the MD&A is that we are getting good pricing lift especially in New Gen areas, and that is actually reflecting in the revenue contribution going up from onsite which of course is a good news because it gives us the operating leverage we need to keep investing in those skills.

Ruchi Burde: Regarding the headcount reduction, was it planned?

Nitin Rakesh: It was planned because as I said we are signing a lot of service transformation type deals that require some element of rebadge, and then we actually transform those deals with either reduction through automation efforts and in some cases just by increasing the offshore leverage.

Ruchi Burde: Second thing I wanted to check is Digital Risk seems to have done well this quarter. You mentioned about a couple of deals. So, does it give a line of visibility that now revenue would be kind of stable, not fluctuate much as we approach the target band of revenue that you mentioned?

Nitin Rakesh: The best way to think about it is to think about sequential growth in that business at least in line with the company growth. That is the way we are bringing it back to that range.

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

Rahul Jain: My question is given the widening opportunity in newer areas and sustained traction in the existing capabilities in client, Is it fair to say that the growth rate should potentially expand ?

Nitin Rakesh: Clearly the New Gen Services are driving the growth, of course, at (+40%) YoY growth, that is the primary vector and that is where we are also selling most deals. So, the right way to think about it is that we need to continue to transform the balance 50% of the portfolio and the more we can use things like service transformation or F2B to bundle some of those into transformation deals, the lower the drag will be from the non-growth in a sub-segment of the portfolio. So, that's very much the attempt. That is why if you look at Direct Core, with increasing portion of New-Gen Services that growth is actually starting to show acceleration as well. So, we have gone from just about under 10% growth two years ago to about 16.5% growth this year.

Rahul Jain: One thing on the DSO have jumped up in this particular quarter. Is there any specific reason? And also the loan, if you could give any clarity on that?

V. Suryanarayanan: On the DSO, some of this is the year-end ~~type~~ effect. But we are confident that we will be back to 65 to 70-days DSO in the coming quarters. And the loan is just a packing credit taking advantage of arbitrage of the rates.

Rahul Jain: So, what is the typical difference we observe on a portfolio basis loan versus what we earn?

V Suryanarayanan: Normal spread of about 2% or so.

Rahul Jain: Risk-free?

V. Suryanarayanan: Yes.

Rahul Jain: On profitability: Nitin, if you could see, given the portfolio, the way it is shaping up, do you think there is a like-to-like opportunity of margin expansion or is it a more complex thing? So, one should be linking it with the growth rate rather than the mix?

Nitin Rakesh: As you rightly said, there are multiple moving parts. Directionally we would love to continue to work towards the continuous improvement in operating margin profile. As I said, it is a little early in the year. We want to see the first quarter or two to see how we can balance the dynamics. The one thing that we are really focused on is continuous investment in building capability because that is the only way we can keep our differentiation going and the momentum of competitive wins in clients where the intensity obviously, is fairly high. So, to me those are the two major dynamics that we will continue to manage. Nothing specific to call out for. Of course, there is always going to be pressure on finding the right skills in the right market at the right price. But that is very much part of what we do to balance business every quarter.

Rahul Jain: The TCV data is strong, is a much larger number than what it used to be till FY'17, but looking at it from a pure growth-to-growth basis, how can we try and read this number in absolute as well as growth, trying to compare it with the revenue number?

Nitin Rakesh: There is obviously a correlation between TCV wins and revenue growth. But keep in mind, not all of these deals are the same duration and the same type of business; so, some of them are lumpy, some of them are digital projects that get consumed fairly quickly, and the others obviously are longer-term deals. So, yes, there is a correlation, but the fact that we continue to see healthy wins in New Gen areas should give us the confidence that actually bodes well for the growth of Direct Core at above market rates.

Rahul Jain: But then this number on a broad lens should be seen on an annual basis or GTM basis should be seen as growth what ideally, we should do around for the Direct Channel basis?

Nitin Rakesh: Not necessarily, TCV growth 14% does not mean that will translate to 14% revenue growth in the next one year because some of these deals may be one year in duration, some may be three years in duration, some may be five years in duration. So, I wish there was a better way for me to give you complete breakdown of TCV, but that is the reality of our business. Good news though is that we do not include renewals in the TCV wins. At least you get a very clear idea of how we are doing in winning new deals. So, if you can use that in the guidelines that at least gives you a good sense of the growth momentum.

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

Sumit Jain: Nitin, firstly, wanted to ask about the DXC channel. In the last two years, you won some really large transformation-related deals. So, how do you see the pipeline of such deals in FY'20 because the DXC has called out a very long-term plan of margin improvement?

Nitin Rakesh: Sumeet, let me answer that question slightly differently. The opportunity within that partnership to help them reduce their cost to serve is actually fairly large. The only limiting factor is how much of that can be absorbed in any given quarter given some of the investments required and in many cases just to manage the operational risk of the business as well. So, the limitation is not so much on the opportunity. To be very fair, DXC has been a great partner in giving us very good visibility into their plans and their areas of focus. Question really is how much of that can we continue to execute and monetize. Keeping in mind not only the operational risk and the deal dynamics, but also just broadly continue to focus on the fact that we want to continue to also find good growth outside of that channel so we manage the concentration risk a little bit better.

Sumit Jain: Also DXC are doing a lot of vendor consolidation at their end and doing quite a lot of in-sourcing. And based on our growth with DXC channel, it is clearly visible we have gained market share within that vendor base. So, how do you see actually the markets share gains will continue in FY'20/FY'21?

Nitin Rakesh: Sumit, the spend is over $3 billion, we are still under 10% of that spend. Even if they decide to use multiple levers, such as in-sourcing, the opportunity of that spend is so high that we think we can continue to find growth. So, I do not see that as competitive because just from a share perspective, there is a lot more to do. The question really is how can we execute that in a way that is valuable to us.

Sumit Jain: Regarding your client concentration if I look at the last 8-10 quarters, your top-5, top-10 client concentration has been consistently going up, it does come with a margin benefit, but how do you see that risk panning out over the next few years?

Nitin Rakesh: Sumit, this is an issue we discussed extensively internally, but as transformation and New Gen becomes the primary norm, it is natural to assume that clients, where we have tribal knowledge, domain knowledge of their systems, understanding of their priorities, relationships, we will probably be the first ones to adopt and bring us into some of those transformation deals. It is the right way to do it because if your existing clients do not buy new things from you, then it is very hard to go to the market with completely new things with no track record. So, it is a great reference point, it is a great way to expand on our wallet share, and most importantly, it is a great validation of the fact that we have set of services that our existing clients find useful. So, we are very happy with the growth, it is very much part of our strategy, it is not accidental, and most importantly, we are completely focused on making sure that we stay very strategic to these clients.

Sumit Jain: How do you see the tech budget starting out at these top clients for FY'20?

Nitin Rakesh: There is a two-part answer to that as I also earlier mentioned. Most of the growth is only in transformation or engagement that improve their customer experience, agility, and in some cases gives them the ability to launch services and products much faster. By definition, that means the things like investment in CAPEX-driven IT projects is virtually non-existent. Almost across the board, we are seeing a reduction in spend areas like data centers. They are very constant, committed and focused on driving out operational expenses through adopting automation, and more often than not, these two themes will continue to play out. So, from a spend perspective, good spend, good growth in areas, where it impacts their end consumer, but really no spend or no growth or no pricing power in traditional older type deals.

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

Madhu Babu: Sir, apart from the BFSI, the other vertical: the travel and, logistics, so how has been the large deal wins and would you start carving out them as a separate vertical, considering that it is a different skill?

Nitin Rakesh: We are tracking that internally, we obviously, talked about ceding some new areas also all of that is right now sitting in the emerging industries, there is travel logistics, there is healthcare, there is hi-tech. As we get a little bit more scale individually in those, we might start carving them out maybe towards the later part of this year.

Madhu Babu: In terms of capital allocation, we have been slow on acquisitions barring one we did last quarter. So, if at all we require acquisition, which are the areas where we believe that we need to spend and what could be the size of the acquisition? Or would we continue to prefer the buyback route in terms of giving out money to shareholders, buyback and dividend?

Nitin Rakesh: Dividend is something that we have consistently kept. Buyback is almost always on an opportunity or use of cash basis. So, at this point in time, any which ways we just finished buyback four, five months ago. So, there is no possibility for another 12 months or so. So, as things open up from ability to do something, we will consider it and the board will evaluate it. But on the M&A side, we have been fairly focused on finding tuck in capability driven acquisitions, things like Stelligent that gives us very strong leading capability in areas along the vectors of the investments that I talked about, whether it is DevOps, Cloud Native App Dev, Modernization, Enterprise Automation and the like. So, right now the thinking is much more capability-driven tuck in acquisitions and there is another $200-odd million cash in our balance sheet, we are fairly well placed for that.

Madhu Babu: On the sub-segment within the New Gen, is it more cloud migration and apps in the cloud that kind of what we are winning or is it on the user experience transformation, CX transformation, etc.? What are the sub-segments?

Nitin Rakesh: Subsegment-wise if you look at the conceptual framework of what we define as front to back digital transformation, there are three core elements. Clearly, there is a lot of investment going in deploying technology in front of the consumer. It is not just user design, but actually it is making the interface much more cognitive and intuitive and in many cases contactless. So, it goes beyond just design. It is all about infusing technology and AI embedded in the interface itself. Good example of that is things like voice, facial recognition, motion detection, and in many cases, we are using a combination of these factors. Then another huge area of investment is really in the entire personalization that is driven by data in motion. That involves gathering data from transactions, pulling data out of the core systems, and of course using that data to derive insight and in many cases create propositions in real-time in many cases on the fly for the end consumer. So, the investment is really-really big in these two areas and of course the final area of investment as it relates to New Gen skills is the whole rearchitecting application base with micro services which then starts to get into the whole application modernization area.

Moderator: Thank you. The next question is from the line of Ravi Menon from Elara Capital. Please go ahead.

Ravi Menon: Just segmental margin for IT communications and entertainment. That has declined nearly 70 basis points QoQ but other segments that has been pretty decent, just down about 100 basis points or so. So, what has led to the sharp decline in segmental margin for IT, Communications and Entertainment?

Nitin Rakesh: Again, we explained that in many cases there are certain transformation deals that require an upfront investment and those obviously have an in-quarter impact as we transform those, in this quarter, it happened to be in that segment, and as we transform those by either applying extreme automation or by offshore migration, you will see some of that come back into the margins. So, the right thing will be to focus on slightly longer-term trend versus just the QoQ trend at each segment or even actually for the overall margin trajectory.

Ravi Menon: Just thinking about what you said, the utilization has been flat QoQ. So, should we say that utilization for this particular segment was much lower or how should we think about that?

Nitin Rakesh: Not really, I do not think it is utilization issue. Think of it as a signing a new deal that require an element of rebadging onsite resources that come at a lower margin and a higher cost, and then as you apply the transformation, that will shift.

Ravi Menon: DXC itself is struggling to achieve market growth. So, how long do you expect to continue growing this channel -- would it be like two, three years or do you think that there is at some point would you say that unless they grow should you actually not grow anymore with them?

Nitin Rakesh: Ravi, I gave a fairly detailed update on what we are doing to drive the transformation. I do not think going back to a mindset that we do not want growth in any segment of the business is the right mindset to take because that adds new risks, and not wanting growth does not take risk away on anything. If anything by having a growth mindset we can actually manage a lot of the other risks. So, that is the mindset we are going with. Two-three years is long-term in the business the way that things have evolved and changed especially introduction of new tech. So, my advice will be to not overanalyze and complicate the thinking in long-term what happens after three years type discussion. Of course, we have to continue the transformation. We are very much work-in progress when it comes to many parts of the business. From that perspective, focus on the two themes that I talked about which is consistency and transformation.

Ravi Menon: One last question on G&A. That has come down quite significantly to just about 4.1% of revenue. So, do you see further scope of optimization there or should we see this flat?

Nitin Rakesh: We are fairly well-optimized on that front already. I would not expect that to go down any further, in fact, we may even see a little bit of an uptick there only because we have to kind of use various levers that we have to manage the QoQ impact, but we are fairly well optimized.

Ravi Menon: Do you think that you need to add some onsite facilities given all this talent pipeline issues there?

Nitin Rakesh: I do not think facilities solve the talent problem to be honest. Because just having an onsite facility does not necessarily open up the talent pool. We are very-very nimble about making decisions on where to invest in having our own facilities, creating co-location centers, opening client-dedicated OTCs, and we are already present in multiple geographies worldwide following the principle. So, as I said on a need basis, we are very nimble in making these decisions.

Moderator: Thank you. The next question is from the line of Rishi Jhunjhunwala from India Infoline. Please go ahead.

Rishi Jhunjhunwala: Nitin, just quickly, if you can tell again in terms of what is the growth outlook you are looking for in DXC and what are the likely margins that you are looking for next year even if not an absolute number but directionally?

Nitin Rakesh: Rishi, I talked about the EBIT guidance we have actually maintained in the 15-17% range, we came out at 16.1% for FY '19. As I said, there are a few things that we want to watch out for in the next quarter or two to give you any updates on that. For now, we are maintaining the same guidance range. On growth, I was again fairly consistent I have been and we continue to feel that the Direct Core growth will be the leading driver. We will continue to find above market growth in that business, and our aspiration for the DXC/HP business is to at least have at market growth.

Rishi Jhunjhunwala: When you look at the margin range, how do you treat your FOREX gains and losses? You have hedge book already for the next 12 to 18-months with an average hedge rate of about 72.1. So, on the flip side, if I say, for FY'19, excluding your FOREX losses, your EBIT margins are actually 17.1%. So, when you look at 15-17%, are you baking in the gains that could possibly come assuming currency remains constant? How do you factor that in?

V. Suryanarayanan: Rishi, as you said, we do have the hedge at around average rate of 72. But for FY'20, it is around 71 because we do a two-year layered hedge. Of course, we will have tailwinds from hedge realization in FY'20. But at the same time, as Nitin had mentioned earlier, we are also making lot of investments in Talent Next, training and on platforms and tools. So, for the time being, we are keeping guidance for margin between 15-17%. After a couple of quarters we will come back with any revised range if required at that point of time.

Rishi Jhunjhunwala: On DXC, you mentioned at industry rate and you are already growing at this point of time at 20%. So, just wondering, that looks like a material deceleration in the YoY growth, of course, it comes off a pretty high base as well. But do you see that the outlook that you have provided with a sense of conservatism or that is how you think it will play out?

Nitin Rakesh: Rishi, again, there is obviously going to be growth built into the run rate. I mean it is easy math to do. Even if we stay flat for the next two quarters, you will still see growth because clearly on YoY basis, you will still find run rate growth. When we say that our aspiration is to grow at least at, that basically means that we do not want that channel to dilute the company growth. For the last two years, we have actually seen really-really strong growth. All I am guiding towards is I do not expect another (+20%) year growth in that segment because one, the base effect is higher, and two, we want to manage some of the dynamics that I talked about and continue to shift our focus on accelerating the Direct Core business. So, from that perspective, do not read that as a guidance that growth is decelerating, or we have a problem at hand. But it is just from a point of view of managing the portfolio and making sure that at the very least we use that channel to stay growth accretive.

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

Ashish Chopra: Nitin, I just wanted your help in understanding how the visibility compare when we look at Direct Channel vis-à-vis the DXC channel. So, like a TCV that you give up net new wins of \$616 million with an average duration that you may have. Does DXC also offer visibility of similar sorts or does the fact that some of this would be their own orders with their customers that would make it slightly challenging? Or given that some of the nature of the world being subcontracting may come in at a point of time without you having much visibility on that, just wanted some color there?

Nitin Rakesh: Ashish, the dynamic is a little bit more complex of course at DXC because, in a way whether we are doing “work for”, “work with” or “work as”, all said and done the end customer contracts are with DXC. So, yes, that adds a little bit of complexity. The way we manage the dynamic is by making sure that if we have visibility into some of the runoff, we find business to refill because the opportunity as I said is still fairly large given that we are still less than double-digits in the spend with partners. So, we basically use that to manage and make sure that from a sequential basis we continue to find growth.

Ashish Chopra: If you could share the attrition rate and how would that have compared maybe a year ago?

Nitin Rakesh: Attrition rate is actually nothing to call out for, it is fairly consistent, we have not seen any major spike especially given the investments we are making in Talent Next, that has actually been a fairly successful program.

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

Apurva Prasad: Nitin, the duration of the deal wins this year FY’19, would that be different from the deal wins that you had in FY’18, because the New Gen composition seems to be similar?

Nitin Rakesh: Apurva, not in a dramatic manner because again there are certain deals that are more lumpy, then there are certain that are slightly longer term. But on an average two to three years is a fairly consistent way to think about it.

Apurva Prasad: So, would two to three years be the duration in FY’19?

Nitin Rakesh: On an average, yes.

Apurva Prasad: In the ROW region, anything that is driving growth? That is growing pretty strong.

Nitin Rakesh: Some of these are global accounts. So, the way we classify that is business from that region, clearly again small base. Again, I talked about growth in DXC, outside of the Americas, some of that is being driven through that channel as well.

Apurva Prasad: On the Digital Risk revenue for the current quarter if you can help me?

V. Suryanarayanan: It is around $23.5M for Q4.

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

Nitin Padmanabhan: I actually had a couple: One is, lot of banks appear to be talking about insourcing and sort of cuts in outsourcing and so on and so forth. So, in that context, within our banking clients, do we see any of those kind of commentary actually impacting us in any way?

Nitin Rakesh: Nitin, again when you look at commoditized legacy traditional type work, that dynamic is at play, but keep in mind one of the primary vectors of using partners like us for banks is to actually bring us in for transformation deals because that is where they are also looking for ideas, help and innovation. So, you can tie that back directly to the earlier comment I made about where growth is in banking. The growth is really in New Gen Services because that is where they are looking for ideas and help.

Nitin Padmanabhan: The second one was on the drop in gross margin this quarter. You did allude to the fact that it is because of people causing some deal related cost. So, there is nothing to do with the compensation increase this quarter, right. It will be all deal-related because on the earlier comment, the onsite head count has come down, but it's quite unusual to see the drops that we have seen in Q4 for us. So, just a little more color on the gross margin and how much is recoverable?

Nitin Rakesh: It is mostly to do with deal dynamics and again I also alluded to the fact that we continue to make investments in our re-scaling program. So, the way we are thinking about it is to make sure that as we expand that talent pool, we also have to put in place retention measures. Some of that you will see spread across some quarters but in most cases what you are seeing in Q4 is really deal related.

Nitin Padmanabhan: Just a find for the broader audience as well. There is a lease accounting change that is out there on rental, and from what I understand our rentals are relatively higher than peer group. So, in that context if you could explain the potential impact there and how does this accounting change actually work?

V. Suryanarayanan: Nitin, IndAS 116 is applicable from 1st April 2019. We are working out the impact, but based on the initial estimation, we are not seeing any major impact on the EBIT or net profit. It is just a shift between the rental into depreciation and amortization and interest component. We will come out with the details during our Q1 earnings call. But as I mentioned, the impact is very marginal.

Moderator: Thank you. I now hand the conference over to the management for closing comments.

Nitin Rakesh: Thank you, everyone for your interest and continued appreciation of our work. We look forward to talking to you in the next quarter. Thank you all.

Moderator: Thank you. On behalf of Mphasis, that concludes this conference. Thank you for joining us and you may now disconnect your lines.