"SQS India BFSI Limited Q4 FY17 Earnings Conference Call"

April 28, 2017

MANAGEMENT: **MS. AARTI ARVIND -- MANAGING DIRECTOR & CHIEF EXECUTIVE OFFICER, SQS INDIA BFSI LIMITED**
MR. N. VAIDYANATHAN – EXECUTIVE DIRECTOR & CHIEF FINANCIAL OFFICER, SQS INDIA BFSI LIMITED

MODERATOR: **MR. DIWAKAR PINGLE – CHRISTENSEN**

Moderator Good Day, Ladies and Gentlemen, and welcome to Q4 and Full Year FY17 Earnings Conference Call of SQS India BFSI Limited. As a remainder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

I now hand over the conference call over to Mr. Diwakar Pingle from Christensen IR. Thank you and over to you, sir.

Diwakar Pingle: Thank you, Margreth. Good afternoon to all the participants on this call. Welcome to the Q4 and Full Year FY17 results earnings call of SQS India BFSI Limited. Please note that we have emailed the results and the presentation, and the same is also available on our website. In case any of you have not received the same, you can write to us and we will be happy to send the same over to you.

To take us through the results and to answer your questions, we have today, Ms. Aarti Arvind – Managing Director and CEO, SQS India BFSI and Mr. N. Vaidyanathan - Executive Director and CFO, SQS India BFSI.

We will start the call with a brief overview of the quarter and the full year gone past, which will be given by Ms. Aarti and this will be followed by the detailed financial explanation by Mr. Vaidyanathan. Post which, we will throw open the floor to Q&A.

I would like to remind you that everything that is said on this call and any outlook for the future which can be construed as a forward-looking statement must be viewed in conjunction with uncertainties and risks that we face. These risks are included and are not limited to what we have mentioned in our prospectus filed with SEBI and subsequent annual report which you can find on our website.

With that said, I now turn over the call to Ms. Aarti. Over to you, Aarti.

Aarti Arvind: Thanks, Diwakar. Good afternoon, everybody and thank you for joining the call. As Diwakar mentioned, I would be providing an overview of our business performance for the financial year as well as for the last quarter. And then Mr. Vaidyanathan would take you through the financials.

The last 12 months have been quite eventful, to say the least, with political and economic changes across regions. First, we had Brexit which was unexpected, and this had an impact mainly due to the depreciation of Pound and with 25% of our business from the UK, this has impacted our growth of what could have been a growth during the year. The change in the political environment in the US has resulted in indecision, which is always detrimental to investment in IT. We see these challenges continuing in FY2018 as well. The US continues to be our focused geography and our group's local offices become more important due to the change in immigration regulations, so this becomes very critical for us in the year ahead. At a broad level, the year 2016-17 has been a mixed bag. We started the year with our strongest quarter, with revenue of $10.9 million US dollars, since we had a couple of large onsite engagements which were at a peak across multiple regions. The revenue in subsequent quarters was lower with some of these engagements moving offshore as well as others ramping down based on the project lifecycle. Overall, we had a flat year on a constant currency basis at $40.20 million on constant currency terms, compared to $40.17 million in the previous year. In terms of profitability, we were able to manage expenses in such a way that we maintained our EBITDA at 19.7% for FY2017.

I would first cover the quarter's performance and then our annual performance. The last quarter was quite challenging for us with revenue being much lower than the previous two quarters. The full impact of the ramp downs in certain engagements in Middle East as well as a lull in some of our European customers has been felt in this quarter. In the last quarter, we felt the full impact of these ramp downs, and with these behind us we look forward to the better quarter going forward. I will take you through some of the highlights of Q4 FY17. Revenue for the quarter was at $8.66 million and on a constant currency basis at it was at $9.18 million. Offshore revenue has gone up marginally to 41% compared to 38% and onsite has gone down by 3% correspondingly. Despite lower revenue for the quarter, we have optimized expenses to ensure that our EBITDA has gone up, both in terms of quantum as well as a percentage compared to the previous quarter. It has increased from 16.2% in the previous quarter to 20.3% in Q4 FY17. Revenue from UK has increased and this has also helped to improve gross profit. Revenue from Asia Pacific also went up in this quarter, India was especially lower during this quarter. Practice wise revenue has changed a bit. We had talked about cards and payments being slightly higher than previous quarter, which turned out in the last quarter. Insurance and treasury capital markets were also picking up in this quarter and we expect this trend to continue. Banking revenue has decreased compared to earlier, since some of our Middle East engagements was primarily banking and these projects have come to a logical closure. Group revenue has increased from INR 103 million to INR 106.88 million, regional mix has changed and one of the customers we started working with in Ireland has increased and the US revenue from the group has gone up slightly. As a percentage of revenue, group revenue was close to 19%. Utilization during the quarter was higher at 71% compared to 66% in Q3 FY17. We also started adding more people with technical skills so that we could cater to the new requirements which are coming up. We also added people in certain locations, specifically in Mumbai, so that we would be able to better cater to our clients in India. Attrition continued to be in the range of 20% to 22% annualized, though it has gone down marginally in the last quarter compared to the previous month. Debtor days continued to be at healthy levels of 57 days and we see this sustain and I think this is something which we have improved considerably during the year. During the last quarter, we had our annual planning exercise called Odyssey in February and we also had our sales meetings kick off where we had sales team from across the globe, across all regions participating in this in Chennai where the objective was for us to focus on what are the offerings that we would take to the market in the coming years as well as make sure that there is connect between the global sales teams and the delivery teams as well as the vertical teams. So this was something which was important which took place in the January to March quarter, we have this every year and this was important for us as a planning exercise for the year. These are the main highlights of the quarter.

On our annual performance, some of the highlights are – one, FY17 revenue on an absolute basis was lower at $38.77 million compared to the $40.17 million we had done earlier. But as mentioned earlier, on a constant currency basis we remained flat at $40.2 million. The revenue mix changed for us having higher revenue from UK, India and Middle East. Despite Brexit, our UK revenue grew over the previous year, while in the US we did not gain the expected momentum. Despite lower revenue, we maintained our EBITDA for the year at 19.7% compared to the previous year of 20.5%. We had more revenue from Middle East and India where the gross profit is slightly lower, but efficient cost management helped us to ensure that we remain profitable. Onsite revenue increased marginally to 63% from 62% in the previous year. Revenue from group grew significantly where it changed from 11.6% in the previous year to over 17% in the last financial year. Overall, we have increased revenue across the regions and also increased the spread of regions that we work with, where most of the clients that we service currently at a group level are from Australia, UK, Ireland and South Africa, as well as the US. But these were ones that we added during the year and some of the new customers are growing well.

On a financial year basis, practice revenue really did not change much, except for insurance increasing a bit, because we had a good traction in the UK and Asian markets. Whereas, if you look at the other practices, it has pretty much evened out or it is average compared to previous year. But as I mentioned earlier, I think they are expecting a lot of traction in Insurance, cards and payments, treasury and capital markets is also growing well. Banking has been 50% of our revenue in the past and we would focus on adding more engagements in this space. Our debtor days has improved quite a bit and has gone to 57 days by the end of March, 2017. So, these are some of the salient points for the financial year 2016-17. What we see as important going forward is, one, in line with how the market is changing, our focus has been and will continue to be in developing our digital offerings and devops offerings which are in line with the change in corporate and retail consumer behavior and what both our customers as well as their end customers expect as offerings. As a group and as an entity, we would continue to focus on growing our footprint in the US. There is uncertainty in the market but since our footprint is small we hope to grow despite the environmental changes and political changes which are taking place. Automation and industrialization will help us to optimize our efforts, as well as offer customers better value for money. So, these would be three of important areas going forward. These have been focus areas for us in the year, the last year as well and this we would continue.

So, to summarize, the year gone by was quite flat on a constant currency basis with positive emerging in the UK, Europe and the Middle East. The US market was challenging with the changes in the political as well as economic environment. We have added to our market offerings, both in terms of digital solutions, accelerators and tools. It has been a challenging time but we have managed to optimize our expenses to make sure profitability has been maintained, though our focus continues to be on how do we grow the top-line profitably, that is the main objective that we have. The ramp downs at certain engagements are behind us and we expect to grow in the current quarter.

With this, I would request Mr. Vaidyanathan to cover some of the financial highlights.

N. Vaidyanathan: Good afternoon and thanks for joining the Q4 FY17 earnings call of SQS India BFSI Limited. As Aarti has covered some of the financial highlights, I will quickly take you through some of the quarterly numbers, annual numbers and then open the floor for Q&A.

The revenue for the Q4 FY17 in INR terms was at Rs 575 million compared to Rs 609 million, which is a de-growth of 5.6%. However, in dollar terms it stands at $8.66 million compared to $9.0 million of last quarter, down by 3.8%, but at constant currency basis the revenue stands at $9.18 million. In terms of the full year, the revenue in INR terms is Rs. 2,599 million compared to Rs. 2,642 million last year, which is 1.6% de-growth, but in constant currency in dollar terms, as Aarti pointed out, it is almost same, $40.2 million for FY17 as against $40.17 million in FY16. In terms of margins, the quarterly EBITDA margin has improved to 20.3% in Q4 compared to 16.2% in Q3 FY17 at Rs 117 million. The yearly EBITDA margin stands at 19.7% compared to 20.5% of last year.

During the year, we saw a roller coaster or rather a downward trend in terms of the major currencies which we are dealing with, namely US Dollar, GBP and Euro. Compared to last year, in current year GBP has depreciated by almost 15%, Euro by about 8% and US dollar by 2.2%. This has resulted in exchange loss for the year of Rs.103 million as compared to exchange gain for last year of Rs. 54 million. For Q4 FY17 the exchange loss was Rs. 38 million. However, in terms of the efficiency of operations and cash conversion have been pretty satisfactory and good with bank balance at Rs. 890 million compared to almost the same level as of last year. In terms of debtor days, it has reduced from 62 days in previous year to 57 days during the year ended 31st March, 2017. The number of clients at the end of the period stands at 76 and for the quarter it is 58. The number of clients with $0.5 million to $1 million stands at 10, $1 million to $3 million at 10 and above $3 million at 1. Repeat business was 88%. The top clients constitute 19% of the revenue with top ten clients constituting 61% of the revenue. The number of people at the end of the period stands at 919 compared to 1,076 as of last year. In terms of revenue mix, efforts was at 36% onsite and 64% offshore and for the year and in value terms it is 63% onsite and 37% offshore. The blended utilization stands at 68.2%, almost the same level as of last year. The utilization for the quarter has improved to 71.2% as against 66.3% as at last quarter. These are some of the financial highlights. Now, we throw the floor open for Q&A and then more information can be provided. Thank you.

Moderator: Thank you very much. We will now begin with the question-and-answer session. We have the first question from the line of Ankit Pandey from Quant Capital. Please go ahead.

Ankit Pandey: Thanks for taking my question. Maybe we can discuss a little bit about what our discussions have been with the top ten clients and maybe we could also talk about how we are looking to add employees and in which areas, are we looking to grow? And where the onsite work, which is roughly two-thirds of our revenue contribution, where this is likely to head, could you just comment on these things please? Thanks.

Aarti Arvind: Sure. I think if you look at our top-ten clients, these are clients who have been with us mostly for multiple years and their revenue has grown steadily over the years in these clients. And compared to what we were looking at these clients in terms of revenue potential over the year based on the discussion that we had in the previous year, I think in most cases we have done more than what we were expecting in these clients. And what we have found is these clients are quite sticky in terms of what they come to us for in terms of opportunity, so the discussions with these clients are quite positive because they look at us as a valued service provider whose part of their teams to deliver on their requirements for the year. Some of these clients are ones where we have multi-year engagements as well as concrete plans for the entire year. There are some of them which are in this mode. There are some of them whom we know that they will have multiple releases during the year, but at the same time as we get closer to the quarter as well they would commit on their revenue numbers for the year. But I think we engage with them and make sure that we have multiple discussions with them constantly to see how their projects are moving and how their expectations are moving. There could be some customers also in this group who when we started the year last year one of the major changes was Agile. So, some of the customers also decided to change their strategy mid-way through the year. So, when that happens, typically or if they have a change in for example a data center movement, then they do change their plans even mid-way through the year, but this is more in terms of based on changes in their strategy. And some of these are ones which you need to support the customer because after these changes there would be more business which comes in. So, there are of course changes during the course of the year with multiple clients, but the top ten clients are ones whom we have had for multiple years and we continue to deal with them and engage with them on an ongoing basis to see what are their annual plans and how we work with them and support them in that. So, this is on the top ten clients and the discussion that we have with them.

On the employee front, we do add employees as and when we feel that we need more people in a particular period in terms of certain numbers or certain skill sets or certain locations. And currently we have started adding, even in the last quarter as well as currently we are adding people with more technical skill sets which we have started sometime back. We do have technically qualified people, but there are certain areas which we felt that in addition to training we need to have people who are experts in their space, so we continue to do that. We are also looking at adding people in Mumbai, which is important for us from an India perspective where a lot of our India clients are based in Mumbai, so we have started ramping up our teams over there, because it makes sense to have more who are local over there. And in addition to this, I think the adds based on the need, based on the level or the skill sets, for example, sometimes you will find that you will need more domain experts because the kind of engagements that you are getting into are more domain focused. So, at that time we plan six months in advance and add the domain team. At the same time, if you find that you are adding more quality assurance professionals, then we may add them pretty closer to the date. So, I do not think I could give you the specifics of when we are recruiting, how many we are recruiting, but we are definitely adding people based on the skill set and the location that we need people in. So, this is on the employee part.

On the third question, the onsite part, I did not get it, what was the question?

Ankit Pandey: Well, if I could just follow-up first. You discussed when you talked about top-10 clients you did say that we have to grow with them a little bit more than expected in the past, is that a fair fact that those growth areas or those green shoots are behind us or those were one-off Greenfield development, so to speak, with the clients, is that the way to interpret those?

Aarti Arvind: It may not be consistency across the board, because there could be customers who had the existing projects also extending, there could be new projects which came up during the year, not all would be Greenfield, they may have had a release which happened and then they may have wanted us to get involved a little bit more in the same release. So, not all would be Greenfield implementation but of course there were some where it was a completely new project which came up during the year which the customer may have planned, but sometimes they share the entire year's plan, sometime what they plan during the latter part of the year you will get to know a little bit maybe a couple of quarters before. So, it is a mix, it is not one or the other, the maintenance business as well as the Greenfield projects which were there, it is a combination.

Ankit Pandey: And just a follow-up of sort on the employees' front, when I was asking about the onsite-offshore I just meant that are you looking to grow more onsite than more offshore, that is one way to look at things, whether we are going closer to the clients or whether those engagements are transferring offshore? That was my interpretation of it.

Aarti Arvind: See, if you look at our onsite-offshore ratio compared to the previous year, it was slightly higher. But at the same time if you look at our onsite-offshore ratio over the years, compared to the Q3, Q4 was slightly lower, so we had bit more off-shoring. If you look at our absolute offshore numbers in Q4 also it was higher than the previous quarter, so we do have more offshore happening. But at the same time, we are not expecting dramatic changes in the year going forward in terms of onsite offshore mix, and there will be some changes of course, but not dramatic. We are not expecting at present more onsite business coming, but it depends on the number of new customers that we add and where the engagement is. But it will be a mix of onsite and offshore and we are not seeing any dramatic changes in terms of this mix going forward either.

Ankit Pandey: I understand, that last comment was helpful.

Moderator: Thank you. Our next question is from the line of Janani Rajasekaran from Securities Investment Management. Please go ahead.

Janani Rajasekaran: My first question is, increasingly we seem to be seeing a kind of vendor consolidation, so can you give us some color on what is the key differentiation for SQS versus other large competitors? Where does SQS really add value to the clients?

Aarti Arvind: I think there are multiple differentiators, both at SQS India BFSI as an entity level and at a group level, maybe I will just elaborate on couple of them. One would be our strength in handling our globally delivery model, because we are very strong across multiple regions, multiple geographies. And even if you take Europe, we have a very strong team in multiple countries in Europe, so we are able to look at the customer requirement whether it is onsite or offshore and have the right mix of people across locations. And this is getting more important globally because with all the regulatory changes which are coming up in immigration, I think the ability to service a customer with local talent from each geography is becoming very important. So, this is an important factor which not too many of the larger SIs would have, and it is also because we have grown in Europe and are very present there, it is possible for us. That is one of the differentiators. Apart from that, in the QA space if you look at a group level or at an entity level, our thought leadership as well as our track record in this space is unparalleled, we are the largest QA organization in the World. And the experience that we bring and the thought leadership that we have, we are way ahead of our competitors in terms of what we deliver to the market, it could be the offerings, it could be the solutions, and it could be the accelerators. So, I think our ability to think of the future and predict what our customers could want definitely, and we are able to kind of benchmark across customers to tell our customers, look others in your space are doing this, this is how they are working on their engagements, not only in terms of QA but in terms of business, so that we are able to offer lot of consulting advise to our customers globally. So, this is something which we are strongly growing that business at a group level. At entity level if you will look at it, one of our strengths definitely is our domain expertise, because we have completely been focused on BFSI from the inception as an organization. So, the depth that we have of the domain is unparalleled where in our organization we have close to 20 to 25 people who are from the operation side. So, that combined with the technology team that we have who understand IT systems, who understand technology, who are able to bring in the digital flavor, the combination of technology and domain is very key. So, I think that is definitely a strength that we bring. So, these are some of the key differentiators that we have in the market compared to others.

Janani Rajasekaran: And second question was, can you give us some clarity on the arrangement with the parent going forward in terms of really sourcing incremental business in the US and Europe for instance, how does the model work really, do we offer services directly to our clients and then we pay a sales and marketing fee or what?

Aarti Arvind: It would be a combination, for example, if you take the US, the US market I think both organization, both the parent as well as this entity are present. So, when we pitch to the market we pitch as one, there are no two sales team, there are no two delivery team, there is a single organization when we pitch. When we get a proposal or when we look at a solution based on our TP study that we have done and the transfer pricing guideline which are there on who takes the contract, it is decided completely based on the parameters in the transfer pricing study. So, based on that one of the two entities, either the Group entity or our US entity would take up the contract. Then if it is through the Group entity then of course the sales and marketing cost would be with the group, so that the transfer price that comes to us would be less than sales and marketing cost because we would not have spent that. Whereas, if it is taken directly then we would bill the end customer directly for that, and may be if sales and marketing is done by the Group then you would need to compensate. So, there is a very well defined study which we have done with a large firm, based on which we figure out who is going to take the contract. And the rates that each one pays to the other is also defined by that. So, that is already established and it has been in place for the last three, three and a half years or so.

Janani Rajasekaran: So, you have a common sales team to pitch for projects across the world, is it?

Aarti Arvind: Yes, correct. Because it makes sense to leverage the local team and have a single face when we go to the market.

Janani Rajasekaran: And in a recent con-call you had highlighted certain plans to scale up your share of group revenue to about 50%. Is there some kind of time frame we are looking at here and what is going to drive this?

Aarti Arvind: Sorry, could you repeat that please?

Janani Rajasekaran: You said that your target is to scale up the share of group revenue to 50%. I am asking is there some kind of time frame to this and what is going to drive this kind of scale up?

Aarti Arvind: I think in the previous calls as well as investor meetings, I do not think I mentioned that we are looking at increasing group revenue to 50%. I think we said that it will move to 20% to 25% and in the previous financial year it was 11.5% and last year it is around close to 19%. But I do not think we are expecting it to be 50%, we are expecting it to be in the range of 20% to 25%. So I am not sure where the 50% came in from.

Janani Rajasekaran: Okay, but the incremental business that you are expecting, you are going to get that from outsourcing or are you getting it from incrementally new business coming in?

Aarti Arvind: It could be a mix where the revenue that comes from the Group, of course, there would be some existing customers who the Group as well as the customers want to look at offshore. Apart from that there are a lot of new business that we pitch for along with the Group, so it is a joint effort that is there which could have an onsite as well as an offshore component. So, it is always a mix of new customers as well as existing customers that we look at servicing. And even at a Group level it is not only offshore that we do, the Group business that we do is both onsite as well as offshore because quite often the skills and the capability or the knowledge that somebody could have gained in capital markets may be required by the Group also at an onsite location. So, even the business that we do with the Group is a mix of onsite and offshore.

Moderator: Thank you. Our next question is from the line of Abhishek S. from Equirus Securities. Please go ahead.

Abhishek S.: Aarti, did I hear you saying that you could see growth in the current quarter? And if yes, then could you highlight what is driving that confidence?

Aarti Arvind: Right Abhishek, I did say that we are expecting growth in the current quarter compared to the previous quarter. One, even in earlier calls I talked about, one of the customers in Europe where we had a lull for a couple of quarters because we had done a large transformation project over the last year and a half, and they did have a lull in the product because it was over and we were supporting them from onsite as well as offshore, but the size of the project scaled down because it tapered off. Now, we have signed a three-year agreement with this customer and we would be servicing them and that has started from April, May that is the timeframe for this, so we do expect that to kick-in in this quarter. And apart from that there has been traction in terms of other accounts, so, we are sure that I think last quarter we also got hit by multiple ramp downs as well as a lull in certain existing customers who were not finishing the project but there was not too much of an activity happening there. So, we are definitely expecting to improve in the current quarter.

Abhishek S.: And as a follow-up to it, with the Q4 despite having a decline in the revenue we saw a good improvement in the margins. And now with anticipation of growth in first quarter how should we look at margins, I mean are these margins sustainable or you would also look at investments once the growth starts picking up?

Aarti Arvind: Abhishek, I think in terms of investments and the spends that we do, we would definitely not look at containing any expenses which are business related which are critical for growth in terms of the business, so that is something we did not do even in the last quarter and we would not do that going forward. But at the same time there could be certain expenses that you may need to incur on a regular basis which we may not have had in the last quarter which we may need. So, I think expenses would be in line with our revenue and our overall profitability expectations, but we may not have the same revenue to profitability ratio that we had last quarter as a standard going forward.

Abhishek S.: So, the interpretation is the margins may not be sustainable, is that the way we should read it?

Aarti Arvind: I do not think that is exactly what I said, it is more in terms of last quarter we had a different ratio in terms of revenue and the profitability. But these could not be your typical indicators of the revenue as well as the profitability going forward. If you look at the last year quarter-on-quarter, for example the first quarter we had a very heavy revenue and the profitability was high, subsequent quarters we had higher revenues, but it is not a straight one where you could say that the last quarter is an example or will be the opposite of that. So I do not think it is that. The revenue and the profitability that we maintain will be in line and the profitability and expenses would of course be in line with our revenue.

Moderator: Thank you. Our next question is from the line of Rahul Jain from Systematic Shares. Please go ahead.

Rahul Jain: My question is specially on the cost front, so we have seen a very strong savings that too in absolute terms, both on the employee cost line as well as in SG&A and this is like back to back. One, I understand because of the number of people would have joined mostly at the end of the quarter but just if you could share your thought that how we manage this and how the run rate looks like going forward?

Aarti Arvind: I think on the employee cost side, it is not just the number of people which makes the difference but it is also the onsite offshore ratio and the region mix. Because, as we had a little bit less onsite in the last quarter, so as you move people offshore the quantum of salary goes down. And we have also had a slight decrease in the number of employees. But as a percentage of revenue also employee cost has gone down, so we have managed that well. But the cost for employee going forward would be determined by the region mix as well as the onsite offshore mix that we have, though we would optimize it. And this is also better because of the utilization that we have, we have higher utilization for the revenue that we achieved. So, all these parameters as a joint thing contribute to lower percentage of employee cost as a percentage of revenue. So, this is something we managed during the quarter and expect that we keep it in line with whatever is required in terms of the quarter. What was the second part of your question?

Rahul Jain: You actually partly answered that, because this would be a function of how the mix of new hiring would be, that would determine the employee cost per employee kind of thing. And from this people on-boarding process we have seen a sharp decline and addition in several quarter where people count have gone down by 100 people, which is like around 8% - 10% for our employee base. So, how we run, it is like annual cycle campus, continuous process, why this churn is very fast in certain quarters and how we manage this?

Aarti Arvind: I think if you look at the quarterly number of people who have left, the last quarter we had fewer people leaving in the previous quarter when it was higher. But, you do also have a cycle in terms of when the number of people who leave during the year, there are different points at which people chose to leave because the industry changes and the cycle changes. But, I think we are quite a mature organization in managing this, and though we would not like very high attrition, I mean that does not work for anybody, but at the same time certain amount of attrition will be there, we plan for it, we manage it and we also tend to expect in certain quarters, certain levels. So, I think we are pretty good at managing that and also managing when do we need more people because going forward it is not just a liner progression of the number of people that you add to the revenue that you get, it is not always linear, in some projects it could be, some projects it may not be. We do a six-monthly forecast of the number of people that we need, not only based on the revenue but the kind of projects that we deliver, the regions that we deliver to, that makes a big difference in terms of number of people that you need. So, based on all this data and parameters and how many we need when we recruit, we do recruit certain skill sets in advance, for example, domain we never want to be short, we want to make sure that we have enough domain and technical capability, that is another skill. Whereas if you look at the general population whom you may add in the general testing space, that we would do closer to the couple of quarters in advance, so, that is how we typically do it. So, it is a fine balancing act that we do to make sure that we are not doing too much, but at the same time we never want to be short so that you are not able to service opportunities or deliver well.

Rahul Jain: And one question for N. Vaidyanathan, we see this interest income is low, is it because most of the cash are overseas or is it on current accounts?

N. Vaidyanathan: See majority of the cash balance, almost like 85%-90% of the cash is in foreign currency and with overseas entities; of course we are also looking at GBP and Euro to come back to a little better level for conversion. Some conversion has happened during last quarter at the optimum levels. In the last 15 - 20 days both the currencies have started looking up a little bit. So, when the conversion happens, then the deposits might take place during this quarter.

Rahul Jain: And we know that this is the practice at the group level that we do not hedge, but if we see the kind of FX that we have for the year is quite significant, given the total profits of the company. So, is there a way that we are trying to assess and view that strategy? And of the Rs. 10 crores odd of annual losses on FX how much of this is on balance sheet reinstatement?

N. Vaidyanathan: Rahul, actually there is a correction to that it is not that we do not do hedging, even at the group level hedging is advised at appropriate time. In fact we take the help of the group treasury head in terms of the hedging and also currency movement. During the quarter what we have also done is, some cross-currency movements to take advantage of the arbitrage between GBP and US Dollars by reducing it. And to add on to the point, for the quarter the entire FOREX loss is unrealized, it has to be on mark-to-market basis.

Rahul Jain: Sir, this is mostly the reinstatement of the assets?

N. Vaidyanathan: That is right.

Rahul Jain: And as you said you have been doing hedging, is it more like based upon the treasury call or is it like we are doing something like six month of receivable or any fixed strategy in mind?

N. Vaidyanathan: No, we just leave it to the treasury head at the group level who has an overall view of the different currencies in different geographies and proportions. And based on that we get advice either for cross currency conversion or hedging, we go by that. Because if you take the value in terms of the BFSI alone, the quantum is pretty low.

Moderator: Thank you. Our next question is a follow-up from the line of Janani Rajasekaran from Securities Investment Management. Please go ahead.

Janani Rajasekaran: My first question is really trying to understand the APAC, Middle East, India market, what is the market size here and how are we positioned, how is India BFSI positioned in this market?

Aarti Arvind: If you look at APAC, India and Middle East, these are markets that we handle directly because the Group presence wise it is more of us being present in these regions and driving them directly. And if you look at our growth over the years in these markets has also been good where India is a market which has a lot of potential because there is a lot of change happening in the financial services industry. So, India is a market that we expect good growth in terms of business in the years to come. India is also a challenging market from a market characteristic perspective, because it is also one with lot of competition, rate pressures are extremely high and the expectations could also be high in terms of what is given, because you have that many competitors. So, it is kind of a different market but the potential is huge because you have so much change happening in the environment, so, India market is something where everybody is looking at growing, including us. If you look at Middle East market, this is a market where we have done well in the last two years, but it is also quite challenging because the oil prices have not increased and overall the economies are not doing very well in the Middle East, because unless oil prices correct and improve significantly they will continue to have challenges in terms of economic growth. So, this is a market where we are looking at a certain amount of revenue, but it may not be as high a growth as it was earlier. It is also a very project driven market where you have large projects during the year whereas the next year the revenue from that customer may be very minimal. So, it is a matter of getting in the large deals, large projects which will help to drive the revenue across multiple years and multiple periods. So, this is on Middle East. And Middle East, presently, that is also affected a bit by Brexit because a lot of the investment in the UK is also in the Middle East. So, with Brexit coming in and the Pound depreciating, that also is something which has affected that market.

Asia Pacific is a market where the revenue is also a little bit more onsite, Middle East is also extremely onsite centric revenue. Asia Pacific, we are finding it to be a good market where there is potential to grow with customers coming out with plans in terms of we have good traction in insurance in this market in cards and payments also. So, we are finding good potential over here, though Asia Pacific price we focus primarily on Singapore, Malaysia and based on opportunities in certain other countries and we do a bit of work in Australia as well. So, this is a little bit about how we are expecting these markets to grow and also how we have done in the last year whereas the last year I would say our revenue from these markets was higher and that also adds to a bit of challenge because the gross profit or the rates that you make and the margins that you make in these regions would be lower than your UK, Europe or the US. So, we try to maintain a mix across regions so that you get your revenue, you de-risk from being too dependent from one region, but at the same time we need to make sure that our revenue from some of the markets such as UK, Europe and US go up.

Janani Rajasekaran: Right. So, in terms of growth do we have any kind of targets we are looking over the next three or four years over here, in these markets?

Aarti Arvind: We do not typically give any forward-looking guidelines in terms of growth for these markets, because there is a lot also dependent on the dynamics and what changes in the economy. So, we typically do not give any forward-looking growth projections.

Janani Rajasekaran: And would you be able to tell me approximate size of the market in these regions?

Aarti Arvind: I think these are very diverse markets, very spread out markets, so, I think market size depends upon the opportunities that we are looking at and what potential they have for the future. So, if you talk about India this will be much larger than what it was a couple of years back, whereas, if you look at Middle East it could be smaller. So, these are changing quite a bit, so, I do not think we have a clear number which we can state saying this is the exact market size which will be there a couple of years down the line.

Janani Rajasekaran: Broad approximate, I am not going to hold you on this.

Aarti Arvind: I do not think we have a number to give couple of years down the line in terms of what exactly these markets would be or what percentage of it we would have, so sorry about that.

Janani Rajasekaran: Okay, alright. And my second question is, given our changing revenue mix, our focus on increasing offshore, what are the kind of sustainable margins in this business and what would drive this kind of shift, is it going to be managed services or high automation levels or what is value added services, how would that work?

Janani Rajasekaran: If you look at the onsite-offshore mix, I mean, we would look at trying to see how much more we can offshore, and quite often now with the various immigration regulations kicking in and most customers would look at how much more they can offshore, not only from the cost perspective but also from the ease of doing business perspective. So, when offshore increases typically your margins would improve, at the same time with immigration rules becoming more challenging you would need to make sure that you have local workforce which you need to figure out in terms of how much it is going to cost you. So, whether overall between the onsite and the offshore changes, may be that would compensate, so, you may not make more overall but definitely more offshore is good from the business risk perspective and decreasing the risk as well as cost and efficiency management. So, that is something which we definitely would be looking at doing and optimizing. And even at a Group level we are clear that we want to see how much more we can offshore to our delivery centers, it is not only for BFSI we would be the one, if you look we have a Group entity in Pune which is primarily focused on BFSI and a couple of other delivery centers in the Globe. So, we definitely look at more and how much we can offshore.

Janani Rajasekaran: And are we looking at managed services and automation levels being a significant contributor to margins going forward or not at the moment?

Aarti Arvind: Yes, definitely. Because if you look at our business mix we have quite a good chunk coming in from managed services which is close to 55% and above being in managed services category where there are a lot of the projects which the way you build could be different, but the way you deliver on the project is more of managed services. So, these would be the ones that we try to focus on and increase over the years, because it also helps you to build your capability and also optimize both for yourself as well as the customer. So, managed services of course would be a focus area for us, it has been and continues to be. If you look at automation, the amount of automation that is happening, the market has increased where you may have per release you may have less efforts because you are automating, but every organization now is doing more releases than ever before. Some of them earlier market used to do quarterly releases of products and application, whereas, now they have gone to monthly and some of the larger sites even have every 11 minutes there is a release. So, that is the extent of QA that has to be done in each case. How this will change? Automation will help to bring down the cost per release, but the number of releases will go up, the complexity will go up. So, we are not expecting any decrease in QA, but how the customer spends and on what they spend will change.

Moderator: Thank you. Our next question is from the line of Rishabh Ghia, he is an individual investor. Please go ahead.

Rishabh Ghia: Could you please explain what is the kind of projects we undertake in the BFSI domain? I had gone through the website and also publicly available documents, but it is at a very high level. I would like to understand some more color in detail on the kind of projects we undertake in BFSI?

Aarti Arvind: I think we undertake a range of projects because right from requirement, documentation to even we support customers in even evaluating multiple products to see which one will work better to them. We are product agnostic, we do not recommend but we help customers evaluate which one might work for them. So, we begin with that range of the spectrum and we also move in to SIT (System Integration Testing), the user acceptance where the users of the bank or financial institutions, instead of them participating in the final round we have business and we say that we understand the business as well as you do. So, we can provide people or we can manage an entire project where it is like a user doing it. Sometimes we do a mix where some of the bank users participate and we manage the UAP, so, that is another kind of engagement that we do. We also do non-functional testing which could be performance testing, performance engineering, security testing, we do automation, regression testing. So, it is a whole range of services that we offer and we are also looking at a group level and our entity level, how do we get involved in robotic process automation where we have tied up with the tool vendor and we are working with them on offering, this is a solution to multiple customers, a couple of POCs have done it at a group level. So, the entire range of solutions is what we will be able to offer. And one change which has dramatically happened in the QA space is, you cannot just say I will offer you one portion of the piece of QA, you have to offer end-to-end, right from you have to find what is the problem in the port, not only reported but you have to help to fix it. And if you come to performance engineering, earlier it used to be performance testing where you find out what is wrong or where it is wrong, tell the customer yes the application will be able to take that many users or not. But now we get into figuring out where the problem is, what tuning they can do to improve the performance. So, we get lot more into depth compared to what we did earlier. So, I would say QA is a very broad space and there are lot of services in this and we pretty much offer them the entire spectrum of that.

Rishabh Ghia: Few of the programs that I can relate to is like you mentioned credit cards, so if a bank is rolling out a credit card program do you do end-to-end of that and is that what is called as managed thing?

Aarti Arvind: See, there are two parts in credit cards, one could be we test for the product company. So, you might have a credit card product company which has an application which caters to the card industry, you have multiple product companies or you may have an end client who is implementing the particular card program. So, we would test it for both and every application provider would have quarterly releases or upgrades based on compliance changes which have happened based on customer needs which come up. So, when the product company makes these changes we would also test it for the end clients because they would like to test these changes before they roll out. So, it would be the entire spectrum of this that we could test.

Rishabh Ghia: Can I assume like the credit card program, things like global transaction banking and other components of banking and a financial institute business, we know the process end to end and that is where we go and do the QA. Would that be the right understanding?

Aarti Arvind: That is perfectly the right understanding, because that is where a good chunk of our employees, between 20% to 25% of our employees are people who come from banks and financial institutions. So, they understand the banking process well because they are ex-bankers, it could be ex-bankers or people in insurance organizations or credit organizations or even capital markets, they could have been in mutual funds, any of these. So, we practically can understand the business, we can talk the language, we know how the processes are and that is what helps us to test on behalf of the organization, bank or financial institution so that we are able to test as they would like the product to be.

Rishabh Ghia: Given the high domain expertise that we have and on top of that a large canvas, like BFSI, these really do not map the revenue trajectory that I have seen in the last three, four years. What is missing, I mean this is a large market, India in its own is a big market for BFSI, but on such a small base of revenue we are not seeing growth. So, instead of being bogged down by the onshore-offshore and all of those technical metrics or operational metrics, could you give us a simple answer as to why is the revenue not kicking up?

Aarti Arvind: I think if you look at the last couple of years, we had good growth in between where quarter-on-quarter our growth was extremely high during the 2015-2016 period, we had quite high growth. And even in the last financial year the first quarter was much higher than the previous quarter and the subsequent quarters we had some decrease in terms of revenue. So, we have grown well in certain quarters and in the last couple of quarters we have had a challenge. At the same time there are lot of market changes which are happening which also affect the revenue and the profits that you make, and certain market forces which are there in certain regions. So, it is a mix of factors which affects us, so, it is not that we have not grown in the last couple of years, we have grown but last couple of quarters have been challenging. At the same time, I think we had a couple of quarters where we had ramp downs, we had a lot of onsite before that and these have moved to offshore. So, when you are doing this transition, yes there will be certain challenges and there will be a decrease that you face, but I do not see this as a limiting factor for us in terms of growth because we have done that before. Even in our earlier growth trajectory we had one quarter, two quarters which have not been great, but overall I think we have grown well, added new clients, delivered extremely well and have done it profitably.

Rishabh Ghia: You said that transitionary period is more or less over and behind us?

Aarti Arvind: We are expecting to do better in the current quarter, and I think in terms of adding client as well as growing we do expect it to be better this year.

Moderator: Thank you. We have the next question from the line of Ravi Naredi from Naredi Investment. Please go ahead.

Ravi Naredi: Thank you, my question has been answered.

Moderator: Thank you. Our next question is a follow-up from the line of Ankit Pandey from Quant Capital. Please go ahead.

Ankit Pandey: Aarti, I did look at the PPT more closely and there was a section explaining that we are looking to expand our US footprint organically. Could you just give us more specifics here, are these new clients or are these existing clients who are taking you to a new location? Are these through partnerships, are these through new sales channels? And is the existing bouquet of offerings going to suffice or are you looking to develop new offerings altogether? Thanks a lot.

Aarti Arvind: I think if you look at the US market, I am also combining the Group because US is important to look at it as holistically. At a Group level, we had two acquisitions in the US in the last year and a half or so, and that has helped us also to grow in the last calendar year 2016 revenue to around $50 million in the US, not for this entity but more at a Group level, which is also a good chunk of revenue and helps us to have a certain minimum base in the US. So, I think the acquisition has helped. At the same time, we are looking at adding clients which may be existing clients of any of these acquisitions, because a good chunk of them would also be in BFSI where we look at how we can support and what we can do. And it is not that those have not happened, there are a couple of clients that we are servicing who are in the Group in US also. Apart from that, at a Group level and our level we are looking at growing organically as in looking at adding new clients as well as looking at the existing portfolio of clients in the US to grow the existing clients as well as adding new clients. I think in the BFSI space, yes we are definitely looking at adding more clients, we have had quite a few good meetings, we have had a senior sales person joined us a couple of months back. So, there is a lot of traction, a lot of activity which is going on. But as I said before, for revenue really to be significant and to be able to contribute to the top-line significantly it will take a couple of more quarters. And it is in the second half of financial year 2018 that we expect this to improve or kick in, but at the same time it is not as though we need to wait till then for adding new clients. So, that is something which we would be doing and are doing in the process in the US. So, US would be organic growth that we are looking at, it would be through existing as well as new clients and we have a good mix of sales team members who understand the domain and we are looking at banking opportunities, insurance, and cards and payments US is a very large space for that. So, these are all the areas that we are focusing on in the US.

Ankit Pandey: But are we looking to sort of develop new offerings? So, will we have more people offshore or onsite,that is kind of what I am getting at there?

Aarti Arvind: If you look at offerings, it is across the board, once every market that we look at the offerings could be different. If I look at the Middle East market compared to the US market, what we offer from a practice point of view is very different, the markets are in different maturity level. So, what you may need in the US is more technical skills, you need people with DevOps skills, you might have performance testing, performance engineering, you may have people who need to know agile very well, and a lot more technical in their requirement. So, that would be the need in the US market for which we definitely look at different offerings for the US market, if you talk about robotics process automation, it would be something which works well in the US where the need would be there. So, even our pre-sales teams and our sales teams in the US would be people who understand technology a lot more, who are focused, who are very local and understand the local needs. So, you are right, our offerings for the US would be very different from our offerings from other regions. There would be commonalities across the board, if you talk about agile that requirement is definitely there across countries, may be less in some, more in some, but we would have common offerings, we would have specific offerings which are regional, not only for the US but for other geographies as well. But in specific for the US we are very conscious of what the market needs, what are the skills required, what are the kind of engagements that work and we are very aware of that and that is what we are focusing on to get our entry points done.

Ankit Pandey: And could you give me the CAPEX numbers that we have incurred and maybe our plans from next year?

N. Vaidyanathan: For the year gone by you are asking, 2016-2017?

Ankit Pandey: Yes.

N. Vaidyanathan: 2016-2017 we had a CAPEX of approximately Rs. 7 crores.

Ankit Pandey: Any guidance for the next year, please?

N. Vaidyanathan: Next year, see last year we had expanded to the ninth floor in the same building with another 250 seat, so there is an extra expenditure involved. For the year 2017-2018, it is going to be normal capital expenditure which will be approximately in the region of about Rs. 2.5 crores.

Ankit Pandey: And Aarti, just a couple of questions more. You did mention that you have a six monthly forecast for your employees and while I would not expect you to share the numbers exactly, but could you help me understand at least from the risk perspective how we should view this particular activity of the firm, are we well covered from the risk perspective and what are the challenge that we are facing in hiring?

Aarti Arvind: I do not think we have any challenges in hiring, because you do have people available in the market and it is a matter of figuring out when you need them and when you need to get them onboard. So, if you look at our people numbers even in the previous year 2015-2016, we hired quite a few people and we ramped up because our revenue was growing quite a bit across the quarters. So, ramp-up has not been a challenge for us and we do not see a challenge going forward. So, specific skill sets you may take longer, so, certain skill sets I may choose to recruit six months in advance whereas certain skill sets which are more generic we may do it closer to the date. So, I do not see any risks or challenges in recruitment because this is not something new for us, this is something which we have done and I think we know how to get that and set that into motion once we have the need.

Ankit Pandey: And lastly one, if I may. Could you talk a little bit about the length of engagement typically with new clients and do you see that change? And you did mention a little bit about the competitive pressures and otherwise, pricing pressures, so could you talk a little bit about that and how that is shaping up for you? Thanks a lot.

Aarti Arvind: So, I think the length of the engagements, it is a complete range. There are some customers whom we are looking at engaging for the next three years where they are looking at us being a partner for three years. Then it is a three-year deal, though you may get the visibility on the next year as you get closer to the year and based on their IT plans. So, some customers it could be long-term. Whereas, some customers you may initially start off with them with a very small engagement, they want to try out and see does it work, are we able to really deliver on what we have…

Ankit Pandey: If I could just interrupt here Aarti, if you could just compare that with the last year that could really help me, maybe this position and this point of time in the last year that could really help. Thanks a lot.

Aarti Arvind: I think that is a little difficult to do because we have a wide range of engagements even with the existing customers I assume the revenue is 1 million. You could have five, six projects running with the customer whereas one could be a project which is running with a couple of people the entire year, whereas another project could be a one-off project which is just 15 days, 20 days. So, I think it is very difficult to generalize saying this is the average size or average duration of an engagement, because it completely depends on the project. You could have a Middle East engagement with a customer which is one and a half years, the same customer we might have an engagement which is one month. So, I think it is very difficult to compare between the previous year and this year and say this is longer or that is shorter, engagements vary based on the project or the kind of rollout that we are doing with the customer. So, I think it is very difficult for me to compare when the range is extremely huge.

Moderator: Thank you, ma'am. Ladies and Gentlemen, due to time constraint that was our last question. I now hand the conference over to the management for closing comments.

Aarti Arvind: Thank you. I think I would just like to conclude by saying that it has been a year of change not only for us but for the entire industry and the customer expectation, not only our customer expectation but the end client expectation, that is all what we expect from our banks and financial institutions to offer us a change. So, in line with that, banks and financial institutions, what they offer to their clients vary and based on that what services we offer also changes. So, it has been a time of significant change across the industry and I think with some of that settling, though there are other political and economic environmental changes, we look forward to a year where we will achieve success in areas we have invested in over the previous years. Thank you all for joining. Have a great weekend.

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