28th Apr, 2003 – 5:30PM IST

Moderator: Good evening ladies and gentlemen, I am Prathibha the moderator for this conference. Welcome to the HCL Technologies' conference call hosted by Edelweiss. Mr. Ajay Mathrani of Edelweiss is your call leader today. For the duration of the presentation, all participants' lines will be in the listen-only mode. After the presentation the question-answer session will be conducted for international participants connected to SingTel. After that the question-answer session will be conducted for participants in India. I would like to hand over to Mr. Ajay Mathrani of Edelweiss. Thank you and over to Mr. Mathrani.

Ajay Mathrani: Good morning, good afternoon, good evening to participants joining us from the US, Europe, India, and the rest of Asia. On behalf of Edelweiss Capital I welcome all of you to HCL Technologies' March quarter earnings conference call. We have with us the senior management team of HCL Technologies and now I hand over to them for the preliminary presentation. Over to you Sir.

Shiv Nadar: Thank you. Good afternoon. Thank you for joining us in this conference call to discuss our financial performance for the third quarter of fiscal 2002-2003. Joining me in this call are Mr. Arun Duggal, our Chief Financial Officer, Mr. S. L. Narayanan, Corporate Vice President - Finance, Mr. Paul Lanham, the CEO of HCL Jones, our JV with Jones Apparel group, he is participating for the first time to speak in some detail about our retail vertical, and finally Mr. Ranjit Narsimhan, Chief Operating Officer of our BPO operations, who will provide an overview of our BPO business. The scheme of the presentation will be as follows: I will begin with the key highlights of this quarter, there after I will request Paul to talk about HCL Jones, and then Ranjit will give you an update of our BPO business. Arun will conclude with a discussion on our financials. Let me begin now.

The highlight of the current quarter is a strong showing in our BPO operation with marked improvements in all key operating parameters. I had shared with you in a previous conference call the need to invest with the long-term perspective and our plans to build scale as well as diversified skill base. You may recall my comments on the typical characteristic of a green field venture and the consequential financial implications in the short-term that may cause some anxiety. But we are safely and surely on course. As you all know the segments will create new pastures for Indian IT players. We have firmly established ourselves as one of the leading players in the space - our association with British Telecom being just one of the many enabling drivers that we have today. We have also won other sizable orders besides the BT contract, and the fruits of these are likely to show up in the coming quarters. Some of you have some concerns with respect to our organic software business. As I had highlighted in my earlier interactions with you, we were to endure the effects of a major client rationalisation program to redirect sales management to a more promising but newly acquired set of clients. This has had some impact on the revenue growth rate of our organic software business. Market conditions do remain tough, but we are adding both staff as well as additional infrastructure based on the ramp up plans of our key clients and remain focussed on growing our franchise. Of course, the basic construct of the business model has undergone a sea change, with newer issue such as a weaker dollar, higher rupee cost, for a different profile of recruitment with more lateral entries and mostly consisting of domain experts. The challenge ahead would be in retrofitting the traditional cost structure to fall in line with the emerging price points for the industry. Now I will hand you over to Paul Lanham, who will brief you on HCL Jones. Paul, can you take it up from here please.

Paul: Yeah, thank you very much Shiv. Good morning and good evening ladies and gentlemen. I am Paul Lanham, Chief Executive Officer of HCL Jones Technologies, New York, by the way I am also Senior Vice President and Chief Technology Officer of Jones Apparel group. It is very much pleasure to be on call with all of you. Now I would like to take a couple of views and share my thoughts on this technology joint venture, which we formed with HCL Technologies. Now at the outset I would like to mention that this joint venture is of very great importance to Jones Apparel group in our efforts to derive more value from our IT budgets. We also have an objective of focussing MIS management time on group's core business area in the apparel and retail manufacturing where we are.

In HCL we found the ideal partner in terms of offshore technical capabilities. We had worked with HCL before the joint venture was formed and were extremely happy with their work. Even in terms of culture, I see a significant similarity in the two companies in terms of the entrepreneurial drive shown by the key employees and the way they do business. We have a high degree of commitment to this venture which can be seen from the fact that I have moved to head this and have brought in a team of highly experienced domain consultants from Jones Apparel Group.

As you would have seen from the financials, within a very short span this venture has managed to reach a healthy run rate in terms of revenues and profits. Currently our focus is tapping the IT work within Jones Apparel Group. In the short term, I would seek to establish credibility with Jones' business segments. Later, we would look at external clients. Going forward, we also have plans to productise our offerings to generate additional business.

As you would know, the retail and apparel manufacturing sector has always been one of the fast adopters of technology and now it is reaching a level of maturity that demands innovative service models. Most industry experts indicate that this domain would remain a key buyer in the technology market. I am confident that our expertise in terms of our domain and technical capabilities and our ability to execute aggressively would help us to stand apart from the competition and emerge as an important player in our chosen domain. That is my comments, and I would like to hand you over to Ranjit for the next part of the call please.

Ranjit: Thanks Paul. Good morning and good evening to everybody. I am the Chief Operating Officer for the BPO operations of HCL Technologies Limited. In the third quarter we have seen some very encouraging performance in the BPO segment. The revenues from our Noida facility have almost tripled sequentially and our Belfast operation also shown good growth. Consequently, the P&L numbers have also improved. The highlight of the quarter obviously was the new contract singed with BT, the largest ever by an Indian BPO company. I would like to share with you that we have had some important sign ups outside BT in this quarter in our chosen verticals namely, financial services, retail, telecom, and healthcare. We have added six clients in the quarter, which includes a large project from a UK based property services major and a technical help desk project from one of our top clients in IT services. We are in the running for some other large projects also, which we hope to close in the current quarter. To cater to the increased flow of business, we have set up two additional centers in Noida with one of them being dedicated exclusively to BT. A new facility based in Chennai, which will also become operational shortly.

Today we are positioned as one of the leading non-captive BPO players in the country with four delivery centers in India, one in UK, and another one in Malaysia. We have a wide mix of processes spanning voice, web, and back office, and a geographic mix that is optimally dispersed, thereby optimizing the shift utilization. Our client base includes a number of fortune 500 and global 1000 companies, with multiple, multi-year, multi-million dollar engagements. We believe that we have the right ingredients to corner a sizable stake of the emerging BPO opportunity in India. We are also quite conscious of growing profitably and we hope to reach cash break even in the next quarter. To sum it up, we look forward to very exciting times for our BPO operations going forward. Thank you. I will now hand you over to Mr. Arun Duggal, our Chief Financial Officer.

Arun Duggal: Thank you Ranjit. Good afternoon. Let me run you through our key financial and operational metrics for the third quarter of financial year 03.

Gross revenues at Rs. 4.7 billion remained at almost the same level as that of last quarter. Our net income before extraordinary provisions stands at Rs. 799 million, which is again close to the last quarter's figure. The net income after considering extraordinary non-cash charges for the quarter was Rs 604 million which is down 25% sequentially. In this quarter we have to recognize some extraordinary provisions related to reduction in the carrying value of our investment in HCL Perot as also diminution in the value of our venture capital fund holdings. These amounted to Rs. 143 million and Rs. 48 million respectively. Our software services business declined by 3% quarter-on-quarter due to a 5% decline in the organic software business. As Mr. Nadar had already explained the drop in the organic software is primarily due to a client rationalization program. There have been some unplanned delays in commencement of new projects as well. The quarter has seen a record addition of 514 people on net basis in our organic software business. The key on organic entities in the software services namely DSL Software, HCL Jones, have again come up with strong performance this quarter and a good sequential growth rates both in revenue and profits.

The quarter has seen an excellent performance from both of our BPO entities as Ranjit explained to you a little while ago. BPO now contributes to a sizable 9% of our revenues and profitability net rates in this segment are steadily improving. In this quarter there has been a 4% decrease in our blended billed rates, this is primarily due to a fall in onsite component of our offshore centric business and to some extent on actual billing rate decline.

Our DSO in the current quarter has gone up marginally to 71 days as compared to 67 days in the previous quarter.

Our client addition remains strong. We have added 26 new clients in this quarter. On the recruitment front we have had a record addition to the head count. In a consolidated basis we have added on a net basis 960 people, which takes the total man power strength to 8748, up from 7788 last quarter. Thank you, and I will now hand you over to the moderator for the Q&A session.

Moderator: Thank you very much sir. At this moment I would like to hand over the proceedings to Sinub at SingTel to conduct the Q&A for international participants. After this we will have a question and answer session for India participants. Thank you and over to Sinub.

Sinub: Thank you Prathibha. We will now begin the Q&A session for participants connected to the SingTel bridge. Please press *0 to ask a question. Our first question is from Mr. Mandeep Sachdeva of Citi Group, Singapore. Go ahead sir.

Mandeep: Thank you. My first question is on sequential decline in core revenue and appreciate if you could go into some specifics and also give us some idea of what sort of visibility do you have for the next quarter and the next year. Thank you.

S.L. Narayanan: We have been impacted by some of the after effects of the client rationalization program. If you recall we had disengaged from almost 84 clients up to December 2002, and plus also we have had certain unplanned delays in commencement of some of the newer projects, but as you could see from the additions in the manpower for this quarter, we remain reasonably optimistic about the prospects for the coming quarter and unfortunately we cannot go into specifics in terms of a specific guidance, but I would just say this much that our pipeline looks reasonably good and we look forward to the next quarter with confidence.

Mandeep: Yeah thanks. I also wanted to check on the trend in the pricing decline in the market. Is it due to the competitive pressure in the market or just clients are just coming back for renegotiations and all.

S.L. Narayanan: Yeah it is now almost a industry feature cutting across almost all the players, I mean you have seen the trends emerging from rest of the peer group as well. There is this pressure which is very much here to stay and that is something which is impacting on the realizations. But I expect that at some point this thing should get corrected and that is perhaps at least a couple of quarters away, because at some stage when the dollar gets weakened and the rupee inflation is starting to impact, this could perhaps lead to a new price discovery and that is something which could bring in a new element of discontinunity.

Mandeep: Okay thanks sir.

Sinub: Thank you. Our next question is from Mr. Bhuvnesh Singh of CSFB, Singapore. Go ahead sir.

Bhuvnesh Singh: Hi, sir. Good evening gentlemen. I wanted to understand basically the impact of this client rationalization program, could you sort of indicate that what is the impact in million dollar say in last three quarters, how many million dollars of revenue was lost because of this.

S. L. Narayanan: Bhuvnesh, it becomes very difficult to put out a specific number here, but we had attempted this and I think I probably shared this with you at an earlier occasion. We perhaps lost about a couple of million dollars in the quarters of September and December. You remember our growth rate was roughly about 5% for the quarter ended 30 June, 2002, and from there in dollar terms we slipped to about 2% sequential growth in September and December. On a base of roughly about 65 million dollars, our estimate was it was at least a couple of million dollars in each of those quarters. But typically what happens is when we are disengaging there are certain ramp downs that happens, so the fuller impacts have actually been realized in this quarter and this is some thing which was inevitable because we had to redirect some of the sales and distribution bandwidth to the newer clients where there were much better prospects and this is something which is a good thing to do in the long run.

Bhuvnesh Singh: Okay. And sir the second and the last question, could you just tell me that when exactly would we get the other income which you were saying it would come at may be the end of the year, could it be the next quarter or the quarter after that?

S. L. Narayanan: This is something which you know we are looking at again very carefully because we would like to do things which are good in terms of the post tax realization. We would keep a close watch on both the market as well as the unrealized gains, and we do things which would be the most optimal. At the moment our total unrealized gain is somewhere around $11 million, and the treasury corpus is around $286 million.

Bhuvnesh Singh: Thanks a lot sir.

Sinub: Thank you. Next we have Mr. Dillon of Arete Research with a question, go ahead sir.

Dillon: Hi. Just a couple of questions. What is the future impact that your customer rationalization program, you mentioned that you have taken 84 clients out in the last few quarters, how many more you are looking to take out in the next quarter or two. The second question would be where do you see long-term margins going down. And the third question would be if you could just give a outlook on your BPO operations, what is the sort of breakdown in your voice versus non-voice revenues there at the moment.

S. L. Narayanan: Yeah, I will deal with the first part of the question. The client rationalization program was complete, we don't anticipate any further disengagements. The second part of your question is something which perhaps too premature to predict now, if your question is the long-term trend lines for EBITDA margins, that is something which would perhaps become more apparent as we step into the next financial year. We have one more financial quarter for the current year to go through, so my guess is at this moment margins could probably decline marginally, but we hope to make that compensate through our top line growth. Third part of your question, at the moment we are fairly heavy on the voice side of the BPO business, but going forward we would see a gradual rebalancing with more of data and help desk kind of operations coming in.

Dillon: And sort of what would be the percentage be at the moment, sort like an 80%-90% voice at the moment?

S. L. Narayanan: Ranjit, would you like to take this question?

Ranjit: yeah. See, currently we have 45 processes going in, out of which 31 are voice based process, 4 are web based process, and 10 are back office process. In terms of revenue mix, currently it is 80% will be voice based and about 20% will be from non-voice based, as S. L. Narayanan put it, going forward we look forward to higher rate of growth coming from non-voice process, that is transaction processing system.

Dillon: Alright, thank you sir.

Sinub: Next question is from Mr. Sandeep Dhingra of Morgan Stanley, Singapore, go ahead sir.

Sandeep: Yeah, hi this is Sandeep Dhingra at JP Morgan, I haven't yet changed my loyalties, but just a couple of questions, one is you know your cover picture has been playing for a while, we pause to soar higher, now the way I look at it this pause is getting longer and longer, you know, we have seen quarter after quarter where you have told us that probably the client rationalization is complete, probably you know core business is stabilizing now, when do we really see the soar higher part of the whole equation.

Shiv Nadar: Sandeep, you know we have been pretty clear about each of the businesses. We did mention how long it will take to for the BPO business, which is a green field venture to get into break even. We did say it will take between 6 to 8 quarters, and even in the last call, I have stated this. We believe that the September quarter is one from which we should start seeing profitability in BPO business. Even the government business, we did mention that it will take that long before it stabilizes. Let me just, while I am at it, let me just state this, BPO business you saw the contract, okay. It is a 160 million contract spread over a period of 5 years and it would not get evenly spread, in the first year may be it is 20 or 25 million, and then going up to 35 – 40 million stabilization rates. That is a pretty good contract and there are more contracts that the company has won. So, whatever infrastructure that we have spread out for the BPO business in terms of cost of reach, which means the sales organization and the current existing even core business sales organization whose efforts have been diverted for this purpose for longer term contracts, because you know going to the existing customers, that is the best way to do it, is quite substantial. And, we are definitely seeing the first part of it in these businesses, which is getting our order book, because here order book is multiple, and firmly contracted pieces. BT is only one of them and there are quite a few which have been signed. Now, the next thing is to convert it into revenue, for which we have build the facilities and that is why you would watch that the depreciation rates are going up constantly. The second part, the government business, it will take another quarter, not only current quarter another quarter, before it turns profitable. The reason for going into the government business I have outlined below: Most of businesses which we are dealing with are competing with peers in India where we compete with Indian cost, whereas the government business is very little done by the Indian peers, largely driven by the local companies, thereof largely driven by the local cost. Evidently, we are interesting in widening the pie, so we are taking time. Even if you take the profitability of the business is as we talk today, which is DSL, Jones and the core business, our profitability should be in the neighborhood of about 20% or so. You subtract that from that the losses which are there in the green field ventures, you arrive at the current level of profitability. And we have added this number of people in the core business because of the pipeline looks extremely robust. So, I do believe that in the next fiscal, we should start seeing growth rates similar to the industry, and I want you to bear in mind that 2001 we could have taken one simple decision that let us just ride out the technology down turn and from 300 million take the revenue down to somewhere around 150 to 180 million, in stead we decided to go into the enterprise segment, acquire some companies and draw vertical segment, and then jump into it full fledge. That has kept our revenue going up to 400 instead of falling down. The basis there now it is for us to grow them at the industry rate at the very minimum. So, I believe next fiscal year should see growth rates both in profits as well as in revenue similar to industry norms, of companies which are this size are larger.

Sandeep: Right. So, Shiv are we saying that you know most of the pieces of the puzzle if you like, you know, core business, the newer initiatives you wanted to be in, you are saying everything is in place, everything looks to be on the right track if you like, and as you go into the next year we wouldn't have these you know conflicting trends that the core business is declining while the rest some of it is doing well, some of it is not, so, everything firing in the same direction. Is that a correct assumption to make.

Shiv Nadar: That is a correct assumption Sandeep.

Sandeep: Okay. Just one more thing Shiv, you know, one of the comments in your investor release, you have said that the challenge ahead would be the task of reengineering traditional cost structures and aligning them with emerging price point for the industry. Now, what exactly are we referring to, are we looking at you know severe cost pressure, or we looking at business coming in much lower than averages, so you need to continuously, you know, this could be the next area which can lead to another set of say restructuring or transformation the business may have to move.

Shiv Nadar: What you are talking about is peculiar trends for the industry, and it is something to do with the overall economic trend as well. This is the first 12 months I have seen since I have been in this industry for 27 years that the rupee has strengthened against the dollar. It gained almost 2.7% and if I take the revenues in dollars and if I put any continuing trends of rupee appreciation, which is not infeasible, because when we talk to our bankers and advisors, they say it is not infeasible, it may stay same, it may decline, some people say that it may increase. I have never ever heard this before in all these years because I have been in the IT industry which the earlier part was very import intensive and the later part in the last four years which is very export intensive, and to all of us it was quite natural to factor in our pricing that 4%-5% will get made up by rupee depreciation, which has happened all this years. Now, if the rupee appreciates anything more than 2.7% is it a possibility? At the moment we have only bankers advise, and we have advise from JP Morgan itself, and if you see your advise, it says, it is pretty ambivalent, it says actually by March next year it may stay where it is and if you go back last 20 years of advise which we have received from JP Morgan, it is always you know put up expect about 5% to 7%. Now, is it going to happen, if it happens what is the impact on this, will the customers be willing to pay something extra, I am not able to predict. The customers will be willing to pay extra for reason which I have put forward in front of you, judge if for what it is worth. There are 400,000 people who are working in this industry, and out of this there are something which is like every 6th person would be a project leader or project manager, and that leaves a bench of 70,000 to 80,000 people working as project managers or project leaders in the whole industry. Now, all the incoming people of freshers, if the industry grows by 25% as projected and adds another 100,000 it will call for 15,000 – 16,000 people at this people. Are we going to move laterally and bring in care or we going to be coming in from external countries, that is a second thing which is posing as a question mark for companies which don't have very good middle management strength. We have, but many may not have. Will that force going to ask for a higher price? The possibilities are there. And will it happen? Like price grow up happened, there is a potential for this to happen because there is a natural need out there, based on these two factors which I have outlined. It is clear, there is a good probability it is going to happen. This is what we meant.

Sandeep: Right.

Sandeep: I think the 26 new customers we have signed, are they coming in at lower than your company average billing rates or they coming at higher than company average. I just understand to see the direction of the pricing in the last quarter.

Shiv Nadar: It is lower.

Sandeep: And could you tell us how much lower?

Shiv Nadar: I cannot give that Sandeep, but you can talk to SL and he may be able to cull it out and provide it to you.

S. L. Narayanan: This is quite a mix bag Sandeep, it may be very difficult for me to say what is the percentage, unless you weighted with volume. It is quite possible that there are some engagements where the volume is larger and therefore the pricing could be at a different level. It would be difficult at this stage to, I mean suffice is to say that you know they are definitely lower than the current average.

Sandeep: Sure, thank you.

Sinub: Our next question is from Mr. Edward Castle.

Edward: Thank you very much for this, letting me ask a question. Can you talk a little bit about the in US dollar terms what the hourly billed rate is now that you are seeing for applications work and how that compares to your average of your company. And my second question is can you tell us about any change in the competitive landscape particularly some of the larger global players like Accenture and IBM. Thanks.

S. L. Narayanan: Our current offshore centric rate is at about $4630 per man month. Here I must say that the way we calculate this, this includes the onsite component of offshore centric projects. So, this also includes minor proportion of staff who have visited the client location and therefore are billed at onsite rates. So, this would roughly be around at 158 hours a man month, it translates to roughly about $27 per hour. This declined by about 3.5% during the quarter. Your second part of the question was how does it compare with the newer contracts which we are signing, the newer contracts, I wouldn't be able to recall the industry average for applications at this moment, but I could certainly attempt calculation sometime tomorrow and I welcome you to call me sometime tomorrow and I could give you some feedback on that part of the question. The third part of your question is where do we see the competitive dynamics in terms of Accenture and EDS taking more aggressive positions in India in the coming years, I would request Mr. Nadar to give his comments on that.

Shiv Nadar: That is something that we have factored. We expect that to happen and we had always expected that to happen, and the impact on that in rates for total projects, because their approach normally is to go for total projects, total solutions, I beg your pardon, and would be to address them at a combined rates, whereas when HCL goes for a project or when most of the Indian vendors go for a project, the projects happen to be segments of them, which is highly offshore centric. So, like-to-like there are very few instances where we would be in my opinion run into them in the next 12 months or so.

Edward: Thank you.

Sinub: Next we have Mr. Dipankar of ICICI Securities India.

Dipankar: Hi good evening. My first question is possibly for SL, could you please explain the charge on account of HCL Perot Systems, because I understand the tech fund part of it, but why is this charged against investment in HPS.

S. L. Narayanan: HPS actually closed their accounts after the last quarter results, and one of the things that the auditors wanted to consider was a write down in the carrying value of investments made by HPS in HCL Technologies Limited. They were carrying some shares, which were acquired around the IPO time at the split-adjusted price of 290. So, that has been marked down to current market, and there was also another acquisition, which was made by HPS in a company by the name of Kay Software and in the earlier occasion we had taken a partial impairment. Currently, we have taken a full write down of the goodwill.

Dipankar: Okay, the second question is regarding Comnet, what I understood about a couple of quarters ago was that Comnet is also possibly going through some kind of a client rationalization in the sense that it was trying to internationalize itself more. Considering that the third quarter is seasonally probably the strongest for Comnet we would have expected much better performance. Can we have an update there?

Shiv Nadar: Yeah. See, Comnet cycles, let me talk about their domestic business and let me talk about their global business. So far the global business is concerned, we have stayed with our basic policy that either we will be dealing with product-oriented solutions or we would stay with remote work which can be done in a remote way, and evidently we will go through some pilots and cycles and I believe given the fact that it is a new area, it shows promise. So far as the domestic business is concerned, see it runs like this. If a year has a very good domestic business, in the subsequent year we see the collections of annual contracts, and year 3 we see the benefits of profit out of that. Now, we had a weaker year as a matter of fact two years ago. Last year, actually, was a good year and that would result in our billing larger quantams during this year but it won't count as accrued revenue during the current year because as the US GAAP is to be strictly on an accrued basis. So, it is a next year in which you will see the result of strong showing last year. This year also the showing is quite strong so we believe that the year after also should be reasonably sound. Did I answer your question?

Dipankar: Right, thank you.

Sinub: At this moment, there are no further questions from participants at SingTel. I would like to hand over the proceedings back to Pratibha.

Moderator: Thank you Sinub. We will now begin the Q&A interactive session for India participants. Participants who wish to ask question, please press *1 on your touch-tone enabled telephone keypad. On pressing *1, participants will get a chance to present their questions on a first-in-line basis. To ask a question, please press *1 now.

Chetan Shah: Can you please update us on the acquisition of the software exports business of HCL Infosystems? Also can you provide an update on various segments of the core business?

S. L. Narayanan: Yeah, the HCL Infosystems Software operations that transfer is going through the regulatory motion, we have the court process and the subsequent meetings and all slated for the month of May. It should come in due course perhaps by mid May we expect all the approvals to be in place. Thereafter, it would take you know certain other approvals from the shareholders and others to come through. It is a regulatory thing and therefore you know it may not be possible for us to precisely give you an estimate of time. We except to know more when the first meetings before the court takes place sometime in May. And, as regards the second part of your question, I think, it is a very broad sweep you are wanting. Can you be a bit specific in terms of your question?

Male Participant: Yeah, basically, I was pointing to the technology development services and the network computing services. On that front, how is the scene in the market and whether it is stabilized?

S. L. Narayanan: Yeah, what has happened is about a year back we were going through a very difficult phase when we had some degrowth up to March and thereafter we have gone back to many of our established customers and we have presented newer business models and better business propositions, whereby we have been able to offshore more work into our centers in India and simultaneously we have taken a strategy of laterally expanding in each of these verticals. About a year back, we didn't have more than two or three clients in each of the technology verticals. Last few quarters, we have added several names in especially semiconductor equipment manufacturing, aerospace, and avionics. So, many of these initiatives, which have been seeded in the last two to three quarters are expected to show fairly substantial tractions in the coming quarters in expectations of which we have done the recruitment in the last two quarters.

Male Participant: Okay, and lastly, I would appreciate if you can also give the financials of HPS on a quarterly, the provisional numbers from next quarter probably.

S. L. Narayanan: See, it will be a very difficult thing for me to do because the official position as mandated by our board is we don't take any kind of guidance. So, it will be difficult for me to answer that question at this moment.

Male Participant: No, no, basically I was saying that whenever you are declaring the results, if you can also give some provisional number of HPS also. That's a suggestion here.

S. L. Narayanan: Okay, we will note that.

Male Participant: Yeah, thank you sir.

Moderator: Thank you very much sir. Our next question comes from Mr. Sanjay Kumar of Prabhudas Leeladhar.

Sanjay Kumar: This is on just a delay in new software projects. Basically, I wanted to understand a bit more as to what was your assessment as to when this project would start and where exactly did things did not go as per your plans?

Shiv Nadar: Okay. It is not exactly things not going according to our plans. See, recently, there has been an imposition that some one has to be in an employment for six months prior to getting either US or UK or most of the western country visas, and HCL already had a very large proportion of people deployed in the offshore centric projects in current projects who could not be relieved to go and bring the work form overseas back to India. Normally, these things come and go. These kinds of restrictions come and go depending upon time, but now with the Iraq war pending at that time they became very very much tighter on this six months' regulation. They pretty much don't make an exception. Earlier on they used to make a whole series of exceptions to most of the people. You want to see this in the light that in terms of billed hours, okay. This is a key statistics for all of you. In terms of billed hours HCL has 78% of its billed hours going from offshore whereas the peers have something like 55% to 56% on an average going as billed hours, which are billed purely on offshore. So, our onsite people base is already low and it is very much offshore centric. So, we had to stop them up or wait till six months period, so that the turnaround of projects, which have been assigned by customers, could take place. That's one of the reasons why there are some delays.

Sanjay Kumar: Okay, and when exactly can we expect this project to start?

Shiv Nadar: These projects will begin in the current quarter and will start ramping up from next quarter onwards that means July's quarter onwards.

Sanjay Kumar: Okay, and which area does this projects belong to, is it application development or TDS?

Shiv Nadar: Any of these projects need the first round is before you write the statement of works, you discuss them with the clients before you move the statement of work, and there have been definite delays on that.

Sanjay Kumar: Okay, has there been any ramp up from any of the existing clients other than the rationalized clients?

Shiv Nadar: Nothing that I can name.

Sanjay Kumar: Okay. Finally, the margins, which you have already reached at about 20 odd percent, you have indicated further decline going forward. Could you give us some idea of how exactly you plan to tackle this margin decline, what would be face-for-face and the extent of it?

Shiv Nadar: See, we never said that there could be a margin decline. We stated that there would be a billed rate decline, and given the fact that we have a large number of people who are on standby currently to go off and bring back the projects, if the utilization goes up, it can balance even billed rate decline to some degree. So, at the moment, if you project that we would be projecting the profitability altogether which is against the policy of our company.

Sanjay Kumar: Okay, in terms of billed rate decline you indicated that your new clients were at lower rates than existing ones. Any other category you see this billing rate pressure coming from. For example, the existing clients who were ramping up asking for discounts with volume and is it that you have some clients which are at very high rates and you find these clients coming back and saying these rates are unsustainable in the present environment. Basically, I was trying to understand, which category of clients is the billing rate pressure coming from.

Shiv Nadar: The newer client is the one which in which you know it is coming across the place, but newer client is a one in which these symptoms are stronger, the people who are coming into India for the first time.

Sanjay Kumar: Okay, what you are saying is also refers to that the clients who are ramping up are not asking for substantial volume discounts.

Shiv Nadar: See, the clients who have already been engaged with us will tend to value the services that we render a lot more because of the sheer quality of what we execute, and this is relative, the pressure from the existing clients would be lower than any new clients that we are adding because they haven't seen. Most of the new clients that we are adding are first time to India.

Sanjay Kumar: Okay, just on the TDS part of the technology development services and software product engineering, I mean, we did discuss something about the business environment, but generally saying would it be a fair assessment to say that we are seeing the worst in this area and possibly can look forward to growth?

Shiv Nadar: I should think so, because the technology sector as such seems to have seen its worst.

Sanjay Kumar: Okay. Thank you.

Moderator: Thank you very much sir. Our next question comes from Mr. Chellappa of Franklin Templeton.

Chellappa: As per the revenues from your top 20 clients, see the top five clients have grown enough in this term, but the top 6 to 20 have declined over the last two quarters. So, how do you hope to grow the revenues in the core business when the top 6 to 20 clients have declined over the last two quarters?

S.L. Narayanan: Yeah, your assessment is right, but this is something which has happened because of a whole host of factors and also one thing which has created a slight change is if the offshore work from onsite to offshore, there could be almost a 50% fall in the revenues on a like-for-like basis, but that is something which will be more than made up for by improvement in margins. So, this is a figure which is impacted by those factors and that has to be seen in the light of that.

Chellappa: Sir, could you tell us regarding this HCL Illinois and HCL Massachusetts Computers, why HCL Illinois has made losses in the last quarter and then there has been a drop in revenues of Gulf Computers.

S. L. Narayanan: If you recall, a short while ago, Mr. Nadar has made a mention of the fact that the many of these newer entities have been invested in with a view to a longer-term perspective. See, the government services business is something, which is very strategic for HCL Tech and this is something that we analyzed and researched and we made that acquisition sometime in June 2002, and typically we expect at least 6 to 8 quarters of running before it turns profitable. It is the fact that they also are now reorienting themselves to a slightly more rigorous process approach as a result of which the integration has taken a slightly longer time. So, between these two factors: a) the need to fall in line with the revised set of working, the process matrix and the quality standard, it has taken a slightly longer time and additional investment. Simultaneously, what we have also done is because we see a larger potential we have invested in additional sales management force to penetrate some newer states. They have been present in about seven states, we added another two or three states to increase the footprint for the government services verticals, and this is something that has been done with a view to expanding the franchise. As regards HCL Illinois, it is basically a temporary phenomenon because there is some pressure there, but it will come back on track. It is transient phenomenon. So, it's a one part of phenomenon. Hello.

Moderator: Hello, Mr. Chellappa. Does it answer your question sir?

Chellappa: Thanks, it answers my question.

Moderator: Thank you very much sir. Next in line, we have Mr. Ananth Narayan from Morgan Stanley.

Ananth Narayan: Good evening gentlemen, my first question was on DSL, which has reported a very good performance, but if we look at another high quality peer namely Infosys in terms of financial services division of that company, it has had declining EBITDA margin for a few quarters now and the margins are well below 30%. Can we assume that these DSL's current high margins are not sustainable and they could be at risk to an extent and also could you discuss this company's future plans regarding business outside the Deutsche group?

S. L. Narayanan: Let me just caution you on this comment. See, the margins that you see for the current quarter have been influenced by a one-time reversal of some accrued payroll taxes, so if we take that additional 7% out, we are looking at a gross margin, which is 54% as against 52% last quarter, and EBITDA margin of 36%, which is against 35% last quarter. Of course, this reversal has flown through fully.

Ananth Narayan: Sure. It is still about 7 or 8% points higher than Infosys financial services division?

S. L. Narayanan: Right. The answer to that is see it is a company, which is focused on a one client at the moment and therefore its opex ratios are not comparable to a company, which his looking at a whole host of clients. But having said that we do have plans to expand the franchise. We are looking at newer opportunities within the extended DB system. There are certain additional very interesting projects that are coming our way and beginning maybe another two quarters we would be also pursuing certain opportunities outside of Deutsche Bank as well.

Shiv Nadar: Ananth, let me just give you expectation. I want to caution, anytime when I say expectation all the forward-looking statements issues are involved. Our expectation is that next year out of the revenue pattern it has, between 10% and 15% should come from external clients, likely to come from an external client.

Ananth Narayan: Okay. Secondly, could you discuss whether any accounting treatment is required for the shares purchased by the ESOP trust, given that these are now trading in well below the acquisition price?

S. L. Narayanan: Yeah, there is nothing to be done at the moment. If the shares do get transferred and there is a loss that loss would be routed through stockholder equity under US GAAP. It will not be a line item under P&L**.**

Ananth Narayan: So, it is transferred to whom S.L.

S. L. Narayanan: To the employees in pursuance of the…, that was your question right?

Ananth Narayan: Yeah, that's right.

S. L. Narayanan: So, assuming that the average price is held in the trust at a price less than the price at which it will transfer, the loss arising on account of such transfers would be routed through stockholder equity upon consolidation.

Ananth Narayan: Okay, and my following question was you know once again on the technology development business. We have seen some significant declines from the contribution of this business in this quarter. Is it on account of some one off things or why is it declined in this quarter?

S. L. Narayanan: As Mr. Nadar mentioned you know there has been also certain delays for newer projects and also it has been complemented by certain transition of work from onsite to offshore, so for every dollar that gets transition from onsite to offshore there would be a 50% fall in realization and therefore that could be one of the reasons.

Shiv Nadar: Relaxation meaning revenue.

Ananth Narayan: Okay, thanks a lot.

Moderator: Thank you very much sir. Our next question comes from Mr. Shekar Singh of DSP Merrill Lynch.

Shekar Singh: Some idea about the new clients, which have been added and which verticals they have come in from?

S. L. Narayanan: Shekar, at the moment, I don't have that split up, I can give it to you tomorrow.

Shekar Singh: Secondly, has there been any provisioning in the HPS account like onetime or something?

S. L. Narayanan: Yeah, in fact, we did mention that you know post the last quarter based on more information that became available during the quarter, we have marked on the carrying value because of certain adjustments that was put through in the books for goodwill impairment for one of their acquisition and the investment value in books that was written down to market.

Shekar Singh: So, in this quarter because of this provisioning?

S. L. Narayanan: Right.

Shekar Singh: Secondly, I just wanted to have some idea regarding this BPO operation though there was a mention about it being cash break even in the next two quarters. I just wanted to know what will be the profitability at the PAT level in the more steady state?

Shiv Nadar: Steady state of this business' level of profitability you know it keeps growing as the utilization grows and this business is more like how much of capacity gets used and how well the capacity utilization gets managed because it is quite capex intensive and the number of shifts utilization, unlike software business, determines the profitability. When it does, its profitability would be similar to that of software business. We have time for just one last question.

Moderator: Sure sir. At this moment, I would like to hand over to Mr. Ajay Mathrani for the last question.

S. L. Narayanan: Yeah, Ajay.

Moderator: Hello, Mr. Mathrani. Please go ahead sir.

Ajay Mathrani: Hello, yeah, I had just one last question. Given that we have about Rs. 50 of cash in our books and that our valuation multiples are lower than peer's, apart from targeting you know revenue and earnings growth, are we planning any other measures to unlock in a shareholder value?

S. L. Narayanan: Yeah, the only thing is you know I just want to reply to that. Your observation is absolutely right, at about 880 million dollars in market cap if we remove about 305 million dollars of cash which is there on the balance sheet in terms of cash flow per share, the company is now being valued at 6.5 times. That is an issue in fact we find that that is something which is extremely low given the fact that we still continue to make about 16.5 to 17 million dollars of profit each quarter. And that is something, which we would be examining more closely in the coming quarters.

Ajay Mathrani: Okay, right, fair enough sir. Thanks to all the participants and the management team of HCL Technologies. Over to you sir for your concluding remarks. Thank you.

Shiv Nadar: Ladies and gentlemen thank you very much for joining us in this conference call and we look forward to more interactions in the future. Thank you.