"HCL Technologies Limited Q3 FY'20 Earnings Conference Call for Analysts"

January 17, 2020

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Moderator: Ladies and gentlemen, good day and welcome to HCL Technologies Limited Q3 FY'20 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchstone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Sanjay Mendiratta – Head, Investor Relations, HCL Technologies Limited

Sanjay Mendiratta: Good evening and good morning, everyone and welcome to the Q3 FY'20 Conference Call for HCL Technologies. We have with us today Mr. C. Vijayakumar – President and Chief Executive Officer; Mr. Apparao – the Global HR Head; Mr. Prateek Aggarwal – Chief Financial Officer; Mr. Darren Oberst – Head, Products and Platforms along with key leadership team at HCL.

I would now hand over the call to Mr. C. Vijayakumar to discuss the performance for the Q3. Thank you very much.

C. Vijayakumar: Thank you, Sanjay. Good evening and good morning to all of you. Welcome to our Third Quarter Results Announcement. We have had a very good quarter. We are very happy to report that our annualized run rate has crossed a $10 billion. It is a great milestone and we are very proud. Thanks to the contribution of 150,000 HCLites across the world. As you can see, our revenues grew 16.4% year-on-year to 2.1% quarter-on-quarter at constant currency and this quarter we again delivered a strong operating margin performance which now stands at 20.2%. We have now delivered two consecutive quarters of (+20%) EBIT. This has come through strong value proposition that we have to our clients, efficient operating model and cost management and also better portfolio mix that we have achieved as you can see in the segmental results.

To look at a little more details on the segments, highlights of the quarter is HCL Software business delivered an outstanding performance which has helped the products and platforms segment to grow by 16.8% quarter-on-quarter in constant currency. This business scaled up impressively added close to 4,600 customers across all parts of the globe including some geographies where we are not present. While we were always very confident of our strategy in investments in the software products business, this quarter is a fitting validation of what this business can do not only in terms of growth in revenues, high profitability and also excellent cash conversion which Prateek will highlight subsequently. Darren will also talk a little more about the software business subsequently.

Coming to Engineering and R&D Services and IT and Business Services, our team has worked very hard during the last two quarters. We delivered a very high growth. So this quarter our employees and customers took a little more time off. So the furlough impact was a little higher. In spite of that, our Engineering business grew 12.8% year-on-year and 0.7% sequentially in constant currency and IT and Business Services grew at 10.4% year-on-year and was almost constant sequentially on the constant currency basis. Of course, IT and Business Services also had a furlough impact. And also in the beginning of the year, we had identified a few non-strategic engagements which were not delivering the desired margins and had made plans to exit out of them, some of that is playing out. Given that we have a strong organic growth momentum, we believe it was the right time to slightly strategically fine-tune our revenues.

This quarter also was a very good showcase of a balanced portfolio mix that we have built. Our business model has really delivered which helps us in mitigating seasonal peaks and troughs in growth. As you can see the top performance in products and platforms has helped us deliver better growth than the market expectations.

In terms of the quality of revenue getting better by every quarter with the better contribution from recurring services stream, which will make us more and more immune to economic cycles.

We continue to deepen our propositions to take advantage of the cloud and other digital opportunities, one example is the Google partnership which we signed as a preferred solution in several verticals that we operate.

In terms of Mode wise performance, combined Mode-2 and Mode-3 revenue stands at 34% of our overall revenues; Mode-2 grew 23.5% year-on-year while Mode-3 grew (+55%) year-on-year.

In terms of geographies and verticals, five of the seven verticals posted double-digit growth, in fact, some of them are in the 30% range and Life Sciences and Healthcare delivered high single digit growth, as you can Manufacturing, Energy and Utilities and Public Services, have delivered stellar growth. In terms of geographies, all the three geographies, US, Europe and RoW delivered a double-digit growth on a YoY basis and RoW led the growth with 27.3% YoY in constant currency.

This quarter we closed an integrated previously announced acquisition, Sankalp. This acquisition will enable us to expand faster in the semiconductor vertical.

If you look at the clients, the 100 million plus clients have increased from 10 to 15 on year-on-year basis, so are several other clients categories where we have seen an impressive increase in the client buckets.

If you look at the wins this quarter, we continue to see a good traction in the market. However, this quarter we experienced a dip in bookings which I see is a timing issue as some clients have taken a little longer to decide; however, the good news is our qualified pipeline is at an all-time high in the recent past and we were expecting a higher conversion of pipeline to booking this quarter. If you were to ask me how much is your booking lower than last quarter, the obvious answer is, I am not going to give you a specific answer, it is a little bit lower than last quarter, but we are very confident of higher conversion this quarter on a very high pipeline that we have.

In terms of analyst recognitions, we continue to win number of analyst recognitions from the top Quadrant as a leader especially in a number of new areas, Digital, Cloud, IoT, Cyber Security and several other things. And in the Everest, Talent Readiness for Next Gen IT Services, HCL came out on the top, demonstrating our readiness to deliver digital transformation engagements.

That provides an overall commentary and I will ask Prateek to walk through some financials, after that Darren will talk about the products.

Prateek Aggarwal: Thank you, CVK and happy new year to everybody on the call. I would give a quick commentary on the key financials, starting with the revenue number of at 10 billion run rate, $2,543 billion for the quarter revenue from 16.4% year-on-year at constant currency, 2.1% sequentially, and organic growth was just under 10% for the quarter and about 0.3% for the sequential. EBITDA is up at 24.7% for the quarter, about 124 basis points, higher than the previous quarter and EBIT at 20.2% is 28 basis points up from last quarter. Optically it looks like 20 basis points, but it was 19.96 and now it is 20.24, so 28 basis points. And this quarter we faced a headwind of 6 bps actually. And therefore the underlying normalized EBIT improvement was actually of the order of 34 basis points. And the largest contributor to that improvement was the added revenue and EBIT from the HCL Software, the P&P segment at 32.9% EBIT, addition of that 50-odd million revenue drew that itself amounted to 22 basis points improvement. And the rest was obviously from IT and Business Services while ERS reduced a bit.

In delivering all of that, we overcame the impact of the annual salary increments that were given during the quarter which amounted to 60 bps which was all overcome through similar time of 60 bpsof better productivity largely in the IT BS as well as in the P&P segment.

Net income for the quarter came in at 16.8%, up 160 basis points quarter-on-quarter and 23 basis points year-on-year. There is a table in the presentation that gives the explanation of some of the movements in the tax rates. It is basically the difference between Indian GAAP IND AS and US GAAP accounting. Basically, US GAAP allows you to account for corporate tax reduction. Only once it has been passed by the parliament whereas in the Indian GAAP tax estimates we had already taken the benefit in the last quarter as per IND AS and IFRS regulations. That is the reason for the $9 million difference that you see in the middle of that page on the website right now. And that explains why the number has suddenly jumped up as far as US GAAP is concerned, it has jumped up in tax expense, it has gone down. Otherwise if you look at the total YTD FY'20 both by the IND AS as well as US GAAP ETR is now at 22%. You will recollect when we started the year I had guided towards 24% as the ETR expected for the year. It has come down to 22% basically driven by the corporate tax rate reduction by the finance minister at the parliament which has got baked into it and the reason for that as you may remember was basically the high amortization of the goodwill and the intangibles which as part of the products we acquired from IBM. So just to clarify the 22% YTD that you see in the ETR as per book methodologies is in the guided range for the full year as well. And that is why the net income for the quarter is 16.8%, building in the cumulative benefit through the three quarters.

I then move on to the cash conversion. And we have a Page #17 in the slide again which basically puts together the three quarters of this fiscal and cumulative numbers in the last column. And as you can see for the quarter, OCF is $709 million to be precise and on a three quarter basis, as you can see in the second last row last column the OCF net income ratio is now at 109% for the three quarters put together. This is what we have been commenting about guiding towards all about the better cash generation partly because of the contribution from HCL Software business is as opposed to the services business. In the software business, you bill first and then recognize revenue later as opposed to the services business where you do the work first, bill later and then collect 60 to 90-days later. So that cash conversion is starting to play out as we enter the second quarter of the software business. And also the fantastic work that the teams across the company have done in terms of billing early and collecting early and leaving no, I mean, the minimum amount of unbilled revenue in the books. I am sure you will pick up from the balance sheet the unbilled revenue that we have is amongst the lowest in the industry. So that has all aided great cash conversion at 109% of net income during the first three quarters. And if you look at free cash flow, just above the 109%, that has crossed billion dollars for the three quarters put together. And just for the Q3 it is $657 million which is again a very heartwarming kind of a number. And FCF as a percentage of EBITDA is also at 61% for the three quarters put together. So all this cash conversion has made the net cash now move up to 1.1 billion, up from $496 million for the last quarter. So that is an addition of more than $600 million just in the quarter. $657 million free cash flow has obviously helped that and we return some of the loans that we had, etc., and added $600 plus million to the net cash balance.

The DSO is at 83-days now including the unbilled which is down 7-days versus the last quarter which was at 90-days. Like I said, due to significant reduction both in UBR and also in the billed receivables, both unbilled and billed receivables improved significantly.

That is the last 12-months cash EPS which is now at Rs.48.7 per share which is up by 21% on the same LTM basis for calendar year '18. Calendar year '19 over calendar year '18 had gone up 21%, Rs.48.6 per share. And EPS is at not very far off, Rs.4 difference; it is at Rs.44.8, up by 16.6% year-on-year.

The guidance is the next thing I want to quickly cover. We had guided at the beginning of the year to 14% to 16% which we increased last quarter to a wide range of 15% to 17%, and in this call we had broken it up saying that inorganic was going to be 5% to 6% and now we are confirming that at 6% the very top end of that guided range. And organic guidance that we had given was 10% to 11% and we are now guiding into the top half of that range as well; 10.5% to 11%. So in total, we are 16.5% to 17% in constant currency is guided for the full year with one quarter left to go. And similarly, on the bottom line, the EBIT side, we had guided to a range of 18.5% to 19.5% at the beginning of the year. And we are happy to raise that also to the top half of that range which is now at 19% to 19.5% and we are happy to have two solid quarters under the belt with 20% kind of numbers which helped us raise guided range number from 19% to 19.5%.

I am also very happy to share we secured (A-) credit rating from S&P Global. These are global credit ratings with stable outlook. Just for comparison, this rating is three notches above the sovereign which is at BBB- so we are three notches above at 'A-'.

The last thing I want to talk about is the dividend. And as we had announced doubling of shares in the last quarter as 1:1 bonus issue, we are continuing with the Rs.2 per share kind of payout on double the number of shares this quarter. And that is the dividend that the board has declared for the quarter.

With that I will hand over to Darren to take you through the great performance of HCL Software.

Darren Oberst: Very good. Thank you, Prateek. We wanted to share and give a little bit of commentary on a few highlights. As both CVK and Prateek noted, this was the second quarter since closing the acquisition of the IBM Software Products. And then probably the overall headline is that we continue to see good progress in terms of the transactional momentum.

To share just a few data points and simplify that, we gave a data point in the second quarter of around 1,500 total transactions that we completed in the quarter. By virtue of comparison in Q3, it was over 5,000 transactions. So over a 3x increase is the transactional volume. And as CVK noted in his opening, we have now onboarded and transitioned over 4600 customers over the course of the last six months. That actually represents customers and transactions have crossed over 90 countries around the world with large scale customer wins and proof points in every major geography, especially notable to us was some of the large wins that we saw across Europe, Middle East, Africa as well as Latin America, Japan and parts of Asia. Last quarter we talked about our partner base. We built partner base of 1,300 onboard ready to transact partners in our first quarter. That grew almost another 50% in our second quarter. We now have over 1800 ready to transact partners and resellers all over the world. And when we have also built out what we believe is really good foundation and starting point to support high volume in a transactional business like this and to give us the foundation to continue to grow in the future.

Just to share one data point that we thought illustrated that. We built out an eCommerce system and a set of processes around that. and in just Japan alone in the last quarter we completed over 700 eCommerce transactions. Hopefully that gives a bit of a flavor for just a sheer volume and scale of transactions that we have completed within the first two quarters. But I think what was really heartening to see in this quarter what was the quality of those wins. And I will spend a minute and talk about this. We saw some larger transactions, we saw some growth transactions and I think most excitingly we saw a lot of new footprints. Customers for the first time making a strategic technology decision to embrace one of these products. So again just to give maybe a couple of data points around that. AppScan, one of our applications security products in a fast growing market, very well positioned product, AppScan alone brought on 27 new customer footprint wins in this quarter. And that was the most of all of our products. BigFix which also is in a different part of the security market, had 23 new footprint wins. Looking a little bit beyond that our business partners, one of the health metrics that we have been really focused on is not just signing a partner up or seeing that a partner will support us with a renewal transaction, but really looking for signs of partners working with us to grow. And we are really happy to have reported in this quarter; we had over 700 new license transactions that came through our business partners. Now this represents sales both to our existing customers who are expanding their employments as well as new footprint customers. And again from our point of view, it is just the beginning. It is a really nice validation point that across that partner community, there is confidence in HCL, there is confidence in these products and that they are looking at to grow with us in the future.

In addition, we saw an increase in million dollar plus transactions. For those on the call that are used to looking at services numbers, million dollars might seem like a pretty small deal, but for software license transaction or renewal transaction it is pretty decent size. We saw significant increase in those transactions in this quarter. And in addition, we saw many customers that were larger scale, million dollars and up, choosing to expand their deployments along with increases in overall deal sizes. Underpinning a lot of these, of course in the last six months is a lot of regeneration in marketing. Just in the course of this quarter, we had 28 webinars, we participated in 21 events and conferences, we actually had over 150,000 unique visitors, have come just to the HCL Software website to learn more about our products.

And then one another kind of symbol and signal point that we wanted to share is we have really started to roll out cross-selling, up-selling, collaborative selling with our colleagues across the services and core business of HCL. We wanted to call out one win in particular which was a new logo win both for HCL Software and HCL Services around BigFix. Just a nice proof point and a nice example of some of the synergy that we hope to build upon in the future in terms of finding collaboration across our business portfolio. Hopefully that gives a flavor for some of the transactional momentum and through the quality and caliber some of the deals that we saw.

Finally, I do want to take a minute and we will do this every quarter in our readout is really talk about products innovation. Because at the end of the day it is a life blood of any software business is continuing to have velocity in your roadmaps and bringing new innovation to your customers. This quarter we had a one very large product release. It was a new major release of Domino v11. The announcement was on December 4th and it really represents from our point of view another major milestone and proof point of the commitments that we made when we first got involved in this product to 15,000 customers around the world that we are going to be investing and supporting our customers to be successful. But more importantly, really helping to modernize and innovate. It is a very large application ecosystem around this development platform. There are over 10 million enterprise grade Domino applications all over the world. And so the Domino v11 release really focused around major new capabilities around application development, making it very easy and almost seamless to build mobile and then client applications with Domino, really extending Domino's that it becomes easier to federate, integrate Domino with other applications within the enterprise and then also really excitingly building out new business user tooling to make it much easier from a no code and low code point of view to deploy new Domino applications.

Now, a couple of early data points around this rollout. The event hosted in Tokyo where we have many large customers across the Japanese market. We also ran a series of digital viewing parties where we had over 50 business partners around the world, actually bringing together their customers to participate virtually in this kick off. We had over 10,000 replay views of the keynote announcing the launch of Domino v11. And probably more significantly again in the symbol and signal category of where we are looking to go, some of the momentum that we have seen around this is in the third quarter we had 18 customers come back to Domino. That is a really meaningful number to us. These were customers and there are many thousands of customers that used the product in the past. And for one reason or another, did not see the pace of innovation and investment and they had lapsed the use of the product. And with the investments that they are seeing, some of the acceleration they are seeing from HCL, we had 18 customers restart with Domino in the past quarter. And within just a first few days post the announcement of v11, we had several dozen more come to us in our pipeline. So again a very nice I think signal of the kind of momentum and validation of the strategy that we have been rolling out. So, still early days, we are learning, every week, we are really focused on getting better and then really building great value for all of our customers and partners. It was very fulfilling to see again some of the very early signs validation of that strategy within this quarter.

C. Vijayakumar: Now we can open up to questions-and-answers please.

Moderator: Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Sudheer Guntupalli from Motilal Oswal AMC. Please go ahead.

Sudheer Guntupalli: Just wanted to double check, Prateek, at the beginning of the call, you said the incremental revenue of $50 million from the IBM products came in during the quarter; however, your sequential increase in Mode-3, looks like it is just $37 million. So, if I adjust for the incremental revenue, this segment has actually reported a decline sequentially, that too in a seasonally strong quarter for products. So any color on this?

Prateek Aggarwal: I was talking about the P&P segment. That has grown quarter-on-quarter in constant currency by 16.8%. That is the growth I was talking about.

Sudheer Guntupalli: Yes, Prateek. So what would be the inorganic component in this because last quarter if you remember we have not recognized the ideal run rate of revenue from the IBM acquisition, I think $106 million was recognized in the previous quarter, so what is the incremental revenue that came from this segment in this quarter?

Prateek Aggarwal: Sudheer, in the products business, typically you cannot look at it on a quarter-to-quarter basis. I guess that is where the difference in thinking maybe. What I was talking about is just the increase more on year-on-year basis which team has delivered that $50 million extra is what I was talking about.

Sudheer Guntupalli: Yes, sir. So, just to be clear on this, is there any incremental revenue which came in from IBM deals in this quarter or the run rate is just $106 million?

Prateek Aggarwal: Sudheer, I think $105or $106 million which we talked about was September quarter '19 over September quarter '18, right. So I wasn't talking about incrementality right now, I wasn't going down that path. I was just talking about the increase in the products and platform revenue.

Sudheer Guntupalli: Sure, sir.

Prateek Aggarwal: We will go forward we will come back to you, Sudhir, on this.

Sudheer Guntupalli: Sure sir. And my second question is on some of the large deal ramp-ups which came up in the first half of this year. So that has actually set up a high base in terms of organic growth. And this year we did not seem to have announced any mega deals like the way we announced towards the end of the previous fiscal.

In conjunction with the U.S. election related uncertainty, how do you feel about the organic growth for the next 12 months, given the deal wins or deal pipeline we have in front of us? I am not asking for any quantitative guidance, but directionally, how do you feel about organic growth shaping up, an acceleration trend or deceleration trend?

C. Vijayakumar: Sudhir, the reason we have not announced large deals in the last few months is really because not every customer is comfortable about releasing a PR related to a large deal. So, a lot of them wanted to keep it confidential. So that's why you will not find a large deal announcement in the last few month. However, the first half we had a decent booking, I mean, obviously, I mentioned there is a dip in booking this quarter because if you look at the last year, we had two big peaks. So, we had a couple of $1 billion deals in the last fiscal. Obviously, we have not had a $1 billion deal this fiscal. However, we had a good booking.

And most importantly, the pipeline at this point is that it's peek. And I am very positive about the conversions that will happen. In fact, we are literally signing large deals as we speak. So I feel confident about a good booking this quarter, which will help us end the year with an overall good booking. It may still be lower than last year because of very large deal wins that we had. So overall, at this point, I would not be able to comment on what FY21 organic growth will look like. We have, anyway, provide you guidance for the coming quarter, that should give you an indication of the exit numbers. And we will really give you a good view when we come in next quarter.

Sudheer Guntupalli: Sure, sir. One last questions. So one of the key concerns earlier was the low EBIT margins in Mode 2. So this seems to be inching up over the last couple of quarters. So any color on what is driving this increase and what would be the steady state EBIT margin expectation for this segment? That's it from my side. Thank you.

C. Vijayakumar: As we said, as we scale this business the EBIT margins will go up, because there is obviously a set of investments which we have done, and we continue to do. And that gets a little better spread out when the business scales. However, I think you will see a sharp increase in margins in Mode 2 this quarter, do not take that as a trend. We should wait for a couple of quarters more to kind of see if the margins are going to be higher in this business. However, whether it is Mode 1 or Mode 2, I mean, in the beginning of the year we did make a decision to drop some business, and you will see that reflecting in our margin improvement across the board, whether it is engineering services or even in digital. Because if you look at the skills for digital, they are becoming more expensive, so we really need to get the right rates to deliver the right margins. So to that extent, we have done a little bit of strategically selective and dropping some businesses. So you will see that moderating revenue a little bit, but definitely it's all in the right direction. And these strategy which we can very safely adopt in a year when we have had a historic growth, so that's really what is driving both an improvement in margin and whatever, slightly lower growth in the Mode 1 business

Prateek Aggarwal: And Sudhir, just coming back to your first question. So, the number for P&P in the last quarter was $290 million, 2-9-0, and that number has gone up to $334 million. That increase of $44 million just pure quarter-on-quarter is the kind of number I will talk about. I rounded it up to $50 million colloquially speaking. That's the number we are talking.

Sudheer Guntupalli: No, Prateek. I think so when we acquired by IBM products, we were expecting $625 million dollar run rate. So $625 million for the first year and $650 million for the next year. And on a quarterly basis, it should roughly be around a $150 million dollars. In September I think we recognized only $105 million. So my question is more about, in December quarter should have we recognized that delta $45 million, $50 million odd?

Prateek Aggarwal: So that, let me come back to you separately, because I really haven't looked at the incremental commentary that we had given earlier. The $50 million which you asked about, I have just clarified, that was just the simple quarter-on-quarter increase, and that is after taking into account some about $5 billion dollars of Forex impact as well. So the total growth is of the order of $50 billion on quarter-on-quarter basis in the PNP segment. Regarding your other longer-term question about that $625 million, it is something I will have to check on that and come back to you separately on one-on-one basis.

C. Vijayakumar: And just to add to what Prateek said, I mean, obviously, the HCL Software business has grown, which is also reflected in the P&P business very smartly. And we are pretty much close to the run rate that we would expect in this business at this point in time. So that should give you a good indication of where we are.

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

Sandeep Agarwal: CVK, I have just one question basically around some weakness which we have witnessed in this quarter on Mode 1 and Mode 2 services, number one. And also some weakness we have seen in the U.S. as a geography, whether there is a correlation to that. And similarly, some comments and technology services and life sciences. Now, is it purely because of the base effect or it is something else? So if you can throw some light on this correlation of these two services with the geography and the Mode 1 and Mode 2.

C. Vijayakumar: Yes. So Sandeep, as I highlighted earlier, the furlough impact has been a little bit more in, both Mode 1 and Mode 2 business. IT and BS and Engineering and R&D, for both the furlough impact has been a little higher. The second thing is, I mean, we have dropped some business, in fact, it's not that we did it this quarter. If you see Q1 when our margins came down to 17.1%, or even before when we planned for the year we were a little bit concerned about the drop in margins.

So we did consciously take a call to drop some accounts, which were not yielding much strategic value. So some of that, obviously, did not happen at that time, it is happening gradually.

Other than that, if you look at a normalized organic growth in ITBS and Engineering Services, it's very good. And we are very confident of good momentum in our core services as we move forward. Geographies, again, I think the two aspects that I highlighted that plays out a little bit more in the U.S. in this quarter, and that's why you will see U.S. as a little soft. I hope that answers your question, Sandeep?

Sandeep Agarwal: Yes. Thanks a lot.

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

Sandeep Shah: Just one question on the product side of the business. Is it possible to tell us what proportion of the total client base would be Tier-1 and what could be their contribution to the products and platforms? Tier-1 means, I mean to say the larger client base.

Darren Oberst: I don't know if I can give you an exact number. But this is enterprise software, and generally speaking, all of the customers are large enterprises. And again, I don't have an exact breakdown. Certainly, there are the exceptions, but there are a few smaller entities or academic institutions that may be customers of the product. But generally speaking, the sweet spot of that customer base who we are selling to tend to be the sort of Global 5,000 customer profile.

C. Vijayakumar: And again, the client base is far wide and deep. I mean, as diverse as a bank in Indonesia to railways in Brazil, and it's quite wide, and governments. But if you look at our core markets, U.S., a large part of Europe, Australia, Singapore and Japan, I think if you look at our, let's say, if I define the target market as Global 2,000 companies, both sort of listed companies and Global 2,000, but if I just take a similar profile of companies may be top 5,000 companies, at least half or more will be clients of the software product.

Sandeep Shah: Okay. And I do agree that in the Analyst Meet we clearly said that we are not looking for a joint selling and you want to keep the sales and marketing function separate. But is there any roadmap, strategic plan in terms of tapping some of those larger customer where on an organic basis we don't have a presence, but we can go through a product side? And any initial success of that?

C. Vijayakumar: So, I think as we highlighted, I think the first focus is to ensure we sign up contracts with all the customers. So, it's going to take us at least two more quarters to sign up with possibly 90% plus of the customers, and the 10% will be a long tail because some of them have signed up for three year deal, so their renewal will come later. So I think next two quarters we will still remain very focused on maximizing our reach out to the acquired client base and signing the software business.

So while I am saying that, there is already some level of cross-sell that's already happening, like for a BigFix customer could be getting serviced on AppScan. And Darren did talk about lot of new footprint. What does that mean? I mean, they are already a customer for one product, we are able to sell another product. And there are also a number of new customers that we have signed up. So in terms of services synergy, I think it's going to take at least two more quarters. We are working on creating a services sales engines in a number of geographies where we have access to clients through the software channel, but we may not have services sales presence, so we are trying to build those presence, which will set up very nicely in a couple of quarters from now to completely look at new markets for traditional services and digital services.

Sandeep Shah: Okay. And CVK, just on the large outsourcing deal wins, especially on the infrastructure management services. We have seen last time when the election happened in the U.S., those announcements got pushed out. So are you witnessing that same could be a possibility in CY20 where the big bang outsourcing deals may not be announced or may get delayed?

C. Vijayakumar: Actually, if you really look at the history, it's only after the election results the dynamics change. There wasn't too much of a change in the outlook, even maybe three months before the elections things slightly started changing. So, I would think it's a little early, in a couple of quarters from now I think we will have a better view of that. At least for the next six months, I mean, this quarter and the next quarter I am not seeing any change customers change. Customers are truly making their decisions on what makes sense for their business. And even in the current scenario after the initial hesitation, lot of customers went back to doing what is right for their business and not necessarily getting constrained by the political undertones.

I largely see a similar thing happening, which means they will continue to take decisions based on business case rather than getting concerned about the political undertones. However, we should wait for another two quarters before really taking a view on that.

Sandeep Shah: Okay. And just last follow-up. One of your large global peer in the last earning call have said that the pressure on traditional outsourcing services is getting stabilized. So are you witnessing the same, especially for contracts which you have signed on infrastructure management services which are coming for renewal?

C. Vijayakumar: See, especially on renewals, we have had a fantastic renewal season. In fact, last quarter many mega deals that we have with large accounts renewed exceptionally. I wouldn't say the competition in renewals is the moderating, I see not only global players, Indian players getting quite aggressive. So obviously, as I mentioned earlier, I mean, we are definitely very keen to maintain our margin profile. And we do believe our prices are very competitive, our automation strategy is very strong. But sometimes it's possible that some of the players get very aggressive, so we wouldn't definitely compromised on the margin profiles that we want.

So that's the strategy that we have taken, which has worked well. Last quarter we renewed everything. But if we need to drop some business because of margins, we will drop.

Sandeep Shah: Okay. But the inward enquiries from the clients on automation or in terms of pricing pressure, is it reducing?

C. Vijayakumar: I think it's stabilizing, I would say. Because, I mean, I think there was a euphoria when there was a 5% year-on-year reduction expectations that has gone to 15% and 20%. But I think that's kind of normalized I would say, and it stabilized.

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

Rahul Jain: Congratulation for a very strong execution, especially on the P&P business side. I would appreciate some clarity you may add to our understanding here a here. A, when we say we added 500 more partner addition that is taking the count to 1,800, is it re-signing of some of the existing partner IBM had or many of them are absolute new people and that is increasing the total canvas opportunity beyond this 5,000 aim that we are talking about?

Darren Oberst: It's a great question. Now that you have asked, I should have come prepared with the answer. The short answer is, I don't know how many are incrementally new partners. I think it is safe to assume that the overwhelming majority are partners that had a history working with these products and in products. In some cases, these are partners that have worked with the products for 10, 15, 20 years, all over the world. And that is certainly the lion's share of the 1800. We will track that, and so actually next quarter we will try to report out on how many of the total partner base are truly new and incremental partners.

Rahul Jain: Right. And also, would you think you need to add more metric around this business, because this business has a very different metric than what we typically add on the services side? And of course, you said that it's too early to talk about the $625 million number, but the first six months into the business are we seeing this to be much better than what we initially thought? If you want

Prateek Aggarwal: So, Rahul, let me put it this way. It is a huge transaction volume that we are talking about. We have been talking about clients of the numbers of 15,000 plus. And some of the transaction volumes for the quarter and for the previous quarter that Darren shared, are huge. And whatever amount of planning you do, when the actual transaction volume hits you, it's another story. So, I just look at it as a pragmatic businessman as a baby is starting to crawl before it sets up and starts walking and starts running. So the last quarter was the crawl phase, this quarter is starting to walk phase. And I am sure we will hit the running phase very soon, maybe soon maybe next quarter itself.

So, $625 million, $650 million are all great numbers. Maybe we will actually exceed them over a period of time. It's not just I am shirking away from having a report card like a good student. I would just say, just give that one gap of quarter and look at the four quarters starting October, October to September, and you will have a number of much better than $625 million, I believe.

C. Vijayakumar: And in addition, we had called out the first quarter. I mean, we had underestimated the effort required to re-contract with a lot of customers, right? So that's why you saw the first motor was soft. And as I said, this quarter we have reached the run rate. So we hope to maintain the run rate and that should give you an indication of where we are likely to land.

Rahul Jain: Thank you. And on the same analogy, I think you would have a marathon run on this very soon. Thank you.

C. Vijayakumar: Thank you for the wishes, Rahul.

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

Dipesh Mehta: I have two question. First on the BFSI. If you can provide some perspective about how you are seeing demand outlook in financial services? This quarter seem to be bit softer, partly maybe furlough. But if you can provide some better clarity about how one should look financial services?

Second questions is about the effective tax rate. Can you help us understand what should build ETR for the current year and next year? Thank you.

C. Vijayakumar: Yes. I will request a Rahul to respond. And then Prateek, who will talk about the ETR.

Rahul Singh: So, I think the point about the furlough is absolutely correct. Because in financial services we deal with large clients as global clients, the client which have got a global footprint. And furlough was larger this year as compared to previous years, that impacted us. At the same time, the outlook continues to be strong. Because of our pivot to Mode 2 and at the right time, a lot of our clients which are in the retail space especially, we have seen their increased spend coming in the digital side. So former retail clients perspective we are seeing a good momentum. We have lot of deals in the pipeline. And I am talking about deals within the existing client base, because the client already is there and we are expanding our footprint within their retail digital journey.

On the Capital Market side, cost constraints were there last year. We believe that those have now been contained, in the sense that more or less what had to be reduced, etc., has happened. We are now seeing spends happening in the Capital Market side on the regulatory and compliance digitization. So we are seeing inputs coming in and furloughs also as items where the Capital Market clients are opening up postings to spend money on compliance and on regulatory, and digitizing those activities. So we think that flows also into the future. So, I think last quarter is aberration because of the furlough I think going forward should be quite okay.

Prateek Aggarwal: Dipesh, on the ETR, the number is 22 % for fiscal year 2020. At this moment of time, we really haven't built the annual plan for FY21. We will guide you to that number next quarter. But, for this quarter, it is 22% as opposed to the 24% that we had guided at the beginning of the year. And this number has come down from 24% to 22% because of the tax rate cut basically.

Dipesh Mehta: Yes, earlier I think, Prateek, you indicated about tax rate likely to inch up when we enter into FY21. That holds true even now or it requires a rethinking?

Prateek Aggarwal: Dipesh, I will reserve comment at this moment of time. It's time one quarter, let me see what pans out. I am not giving you guidance for FY21 right now, I will come back next quarter.

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

Mukul Garg: Again, sorry to come back to the product and platform, this is regarding CVK's last comment, that you guys have said the run rate in the inorganic business and you will continue with that in Q4. So, is it fair assumption to take into account that this is partially because of the seasonality where Q3 is stronger? And given that you guys will probably add lot more customers in Q4, that seasonality impact will limit incremental revenues coming in Q4 from Q3?

C. Vijayakumar: Yes. I think in the model that we had earlier, where our partners had last quarter as Q4, which is OND quarter, it was very customary to have a big peak in December. That need not be true in our model. I do think it will be more stable. There could be a little bit of peaks, but it will be more stable. That's what we foresee at this time. But I think we will need to really look at this for eight quarters to really build a robust model on the seasonality. But as we see, we do have reasonable visibility for the next two quarters, and that's why I said we have kind of hit the run rate. You could always have a little variations, but I think we are at the right run rate on this business at this time.

Mukul Garg: And if I may just follow that up with just a quick clarification from Darren. Darren, you mentioned earlier on the call that you have now signed up about 4,600 customers. If I believe the number earlier, total number was about 25,000, is that growth something which is satisfactory in your view? You have any sense of over next two quarters given that you are planning to target about 90% of the customer base. Should we expect a very accelerated sign-ups over next two quarters?

Darren Oberst: So, I think in the short answer, yes. I think we are satisfied with the progress we have made over the last six months. I think it is largely on track with what we expected it to be. Just in terms of the overall transaction volume and the number of customers that have moved over. And I think, again, we will try to be as transparent as we can be, this quarter and next quarter on these totals. We would expect, as CVK mentioned, that from a total customer number point of view, in most of those customers are on annual cycles. So upon the one year anniversary of the closing of the transaction, we would assume that the overwhelming majority of customers would have migrated over. But there is a long tail of some larger customers. So that is disproportionate to the value. Some of the large customers purchase multi-year ELAS, and so that transition process will continue all the way through 2020 and into 2021, even into 2022.

Mukul Garg: And just a clarification, CVK. I think you mentioned on the TV interview that, I think, similar to your peers you are also quite positive on the demand environment. Is that reading right?

C. Vijayakumar: Yes, I mean, my reflection on the demand environment is less based on macros, it is more based on the pipeline that we have and the client engagements. So as I said, the pipeline is at a historic peak, based on the past several quarter data that we maintain in a certain way. And I think that's why I am positive about the demand environment. The closure timings could very little bit here and there, but overall the pipeline is very good.

Moderator: Thank you. The next question is from the line of the Diviya Nagrajan from UBS. Please go ahead.

Diviya Nagrajan: My question is on what you talked about exiting some businesses in Mode 1 and Mode 2. Specifically you spoke about exiting some digital work as well. I am trying to understand the rationale behind it. Did you feel that that kind of work was never going to be profitable? Is that why you exited? And could you kind of also tell us what kind of services those were?

C. Vijayakumar: So, Diviya, thank you. And it was largely in Mode 1 and a little bit in Mode 2 as well. But like in Mode 2 while they are executing to a client in the global model, I mean, it may not be meaningful for us to engage with them in all geographies due to certain reasons. So some of that we have dropped, while initially we picked up on a global scale. We found it was not making sense for us to do certain programs in certain geographies. So that we dropped in digital side. But I think a lot of it is largely in Mode 1. And in fact, I mean, even on the traditional side, in one of the renewals where we didn't believe that we will make meaningful margins if we continue with engagement, we decided to not bid. So I think these are some examples. I hope it helps.

Diviya Nagrajan: Yes, thank you. Just a quick follow-up on margins. I think since we have had the IBM products come in, there has been a definite improvement in margins. Just trying to understand how much of your margin is coming in at the top end of the range is driven by that? And what kind of organic improvement we are seeing in margins for the year as well?

C. Vijayakumar: I mean, you can see we have a segmental P&L. Even in ITBS the margins have improved, Engineering Services previous quarter it was a big uptick, this quarter it is slightly moderated despite wage increase, despite furloughs. So I think there is a very healthy improvement in margins in the core organic business. And I am sure a lot of that was expected, because when we started the year, we had reduced from the previous year to 19.5% to 20.5%, 18.5% to 19.5%. So we took several measures to improve margins. And lot of that is playing out. I mean, while giving guidance we were a little cautious, but we were definitely executing very strongly to ensure that our margins improve. Not only margins, cash flow, cash conversion, all of that right has been very, very diligently planned and driven. And you see that delivering results now

Moderator: Thank you. Ladies and gentlemen, that was the last question for today. I now hand the conference over to Mr. C. Vijaykumar for closing comments. Thank you and over to you, sir.

C. Vijayakumar: So overall, I mean, as I said all through the call, we have had a fantastic nine months, industry-leading growth, both organic and a very good execution of the largest acquisition that we did. So we are very happy with where we are as a company. And there is a lot of optimism that is lying ahead. So thank you for joining us and look forward to talking to all of you during the next quarterly results and the full-year results. Thank you, and goodnight, and good day.

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