



# “HCL Technologies Limited Earnings Conference Call”

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**Moderator:** Ladies and gentlemen, good day and welcome to the HCL Technologies 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 at the end of today's presentation. Should you need assistance during the conference call, please signal an operator by pressing "\*" followed by "0" on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Vineet Nayar. Thank you and over to you, sir.

**Vineet Nayar:** Good evening, everybody. Welcome to the fourth quarter and the annual results conference. The quarter and the year both have been pretty good. For the year we have demonstrated a 17.1% year-on-year growth and we have also crossed \$4 billion in revenues. Our EBIT is \$679 million which is 36.3% year-on-year growth and net income is about 31% year-on-year at very close to \$500 million, which is a benchmark by itself for us.

Our quarter has been quite good with volume growth of 4.6%, sequential growth of 3% in dollar terms and year-on-year revenue of 12.1%. EBIT also crossed \$200 million with a growth of 40% and net income also crossed \$150 million with \$156 million, year-on-year growth of 36.3%.

What is very interesting for this quarter and this year is the fact that there is a broad-based growth across all service lines. And one of the reasons the growth there is because of a couple of strategies which we had adopted.

The first was that we were focused on the renewal market which was only going up. If you look at the latest data which has come in there is \$14 billion of contracts which got restructured in H1 of calendar year 2012 which is 40% YoY growth and there is \$27 billion of new spends where there is a 20% YoY reduction in the H1 period. Since we were focused on the restructured market, which saw an upside and as we have been announcing, we won a lot of deals and we have gone into a lot of doors, so that is one reason we did well.

The second strategy which we have been talking to you about is that once we get inside the door our ability to be able to expand cross-sell and upsell and we shared with you the multi-service adoption index, and how that was helping us grow, would result into a lot CTB being sold to the existing customers and therefore our ability to sell them high value services and also expand our margins within those customers.

The third was our focus on new geographies like the Continental Europe and new service areas like Healthcare and Utilities which contributed to significant growth for us. With that you saw Enterprise Applications, Engineering Services, Custom Application, BPO, everything grow and BPO was a story of restructure which again we have executed quite successfully over the last one year.

We saw growth across the board in the verticals also and we will touch upon some significant verticals today, the Financial Services we are going to touch and Energy and Utilities we are

going to touch. There was scope increase in the geographies also, both Americas and Europe increase.

What is commendable about these results is that the industry has seen a lot of growth in BPO services which is not true with HCL predominantly because we are restructuring the whole service and therefore this growth story despite BPO not contributing is a very interesting growth story. A lot of our peers in the industry have also grown substantially in ROW, where we focus more on Americas and Europe, predominantly because we saw a great opportunity and once again our growth if you only look at incremental revenues added in Americas, incremental revenues added in Europe, it again presents a very interesting story. So, overall, we are very happy with the growth trajectory.

One of the resultant impact of this growth was the increase in large customers of HCL. And the very fact that we were able to increase \$100 million customers from 1 to 5 indicates the fact that we were able to grow our businesses very rapidly. Strategy is, one, enter those accounts, number two, grow those businesses very rapidly, because all these \$100 million accounts are actually old contracts which we had signed one or two years ago, where we have been able to upsell and scale up quite rapidly.

And also the fact that Top 5 customers grew at a 5.5% sequentially and Top 10 at 4.5% sequentially above the company average also points to the fact that not only we are good at winning the deals but we are also good at expanding service lines within those deals.

The last point I am going to make before I hand over to Anil is the fact that there were lots of concerns expressed in terms of the fact that are we winning the deals on pricing. I had already explained this fact that we are competing in the industry with IBMs and Accentures and CSCs and Capgemini of the world where margin profile is between 11% to 14%. Therefore as a conscious choice we have taken a choice of being in the industry which is structurally at lower margins industry. And this decision results into restructuring of HCL's margin.

Having said that I had also said that once we entered the door into those companies and reached steady-state, our ability to use margin levers and expand the margins into steady-state accounts is quite high. And what you see in this quarter is demonstration of the fact that we are capable of doing this, as some large accounts move from transition to steady-state, we were able to expand the margins. That in summary will be our strategy going forward. We have a significant amount of new deals which are coming under execution. And as more and more of these deals reach steady-state we would have enough headroom for growth on margins. Now, we do believe that as a conscious strategy, we need to invest in our future. If you look at the \$4 billion performance of HCL today, a billion dollars has come from infrastructure, which was incubated as a new business and we rapidly grew it from \$70 million to a billion dollars in the last seven years and another close to a billion dollars has come from Enterprise Applications which we acquired three years ago at about \$400 million and rapidly grew it by incubating the acquisition. So the question of growth tomorrow is going to lie not just in organically growing on the rebids or the restructured contracts which are coming on the table but it comes from

incubating new businesses and investing in incubating these businesses for our growth. Now, to do that we would utilize some of the headrooms which we potentially have from the margin levers we can exercise on the deals which will come up. Once they come into a steady-state we will be able to invest in new businesses so that we can incubate the next big businesses. Therefore when we meet you again five years from now we have similar stories like an Axon story or similar story like an Infra story or any other story because that is where the growth is going to come from.

So, with that I hand over to Anant to go over the explanation of the Infrastructure Services.

**Anant Gupta:**

Good evening, everybody. Last fiscal was a milestone year for infrastructure management services finally on three counts. Firstly, the revenues crossed a billion dollars which is a great milestone and as Vineet mentioned from \$70 mn to a billion dollar in seven years track would put us amongst the fastest in the industry across IT Services.

Second area which is again a milestone for us is really a significant booking during the year, close to about 23 customers added with five Fortune 100 companies added.

Third and the most important one is the customer satisfaction. The infrastructure management services customer experience index which is conducted by an external agency is at an all-time high and has been called out as best-in-class in industry for second year in a row.

Coming back to the numbers, the Q4 revenues grew 6.6% sequentially to \$268 million; the EBIT grew to \$47.9 mn, up 31.7% QoQ. In terms of manpower we added 6200 people on a gross basis.

A couple of other points which I thought would be important to mention, while we continue to see a significant churn in the rebid market we also continue to record a near 100% renewals of our existing contracts given that we have now been in the industry for seven years.

All the large engagements that we have signed last year are transitioning and being executed well. So, they are on track I would say. The market traction in Europe continues to be strong with significant market share gain in Nordics.

From a trends perspective – no significant difference in the trends from previous quarter. The demand continues to be robust both in the first time outsourcing market, companies like we announced Statoil which are outsourcing for the first time as well as in rebid market.

The other key thing which we are seeing in the marketplace which got recognized well is MyCloud investments which is HCL's IP and cloud orchestration. It is positioning us very well in the transformational-led outsourcing engagements given the fact that we would see some adoption of public cloud services, the private cloud, all co-existing and therefore HCL is looking at how we could, orchestrate and manage their entire enterprise across the diverse world.

With that I will hand it over to Steve.

**Steve Cardell:**

Thanks, Anant. So I will make some comments first on Enterprise Applications and then I will talk on on public sector. So, we saw another strong quarter of growth, 4.8% QoQ on a constant currency basis. Growth is balanced between Europe and Americas but we saw quite a different profile of business coming out of the two geographies which reflect the macro conditions in those geographies.

So in Americas, the four trends that I am talking about since last few quarters, coming out of both SAP and Oracle, for are focus on engineered systems like SAP's HANA solution, Oracle Exadata and Exalogic solution, Big Data Analytics, Clients Computing and Mobility. A lot of the growth we saw in North America came from both emerging technologies and the integration of those into some of the more traditional back office ERP systems that were in place. In Europe, what we saw was a much better cost focus, the concept of Brownfield implementation. So, customers who are already using SAP, Oracle in their back office, maybe old installations or maybe multiple instances are running consolidation projects to reduce cost, are then moving back office into front office to improve returns or they are upgrading from old versions again to achieve the long-term run cost of those systems. So from a geographic point of view, similar growth in the major geographies but from a very different profile business.

From a vertical point of view, the wins that we saw in this quarter were primarily in Retail, Aerospace, Defense and manufacturing that helped us grow the top-line. And we continue to see what has been true for most of this year which is a fairly stable pricing environment.

We are highlighting a couple of trends that we are seeing on the technology side. Oracle and to some degree SAP are moving from being a single integrated ERP to having a stable of best of the products that integrate well. For Oracle, this has been a fusion story that they have been moving down to several years and we just completed our second fusion implementation we implemented SCM solution last quarter and HCM in this quarter.

And we are also starting to see both SAP and Oracle move more heavily into some cloud-based offerings and some pay per use based offerings. So, SAP's acquisition of Success Factors and Oracle acquisition of Talent, see really the whole HCM segment moving to a cloud-based offering from both of those providers.

And then finally, on the technology side, mobility which has been quite a story for the last few quarters is becoming quite standardized in almost all of our major business. So the solutions that we are offering contain the ability to deploy both data and applications on to mobile platforms and also discreet mobility projects where companies are looking to gain advantage of making a back office solutions more applicable.

And just a couple of comments on probably the key ones to highlight are in this quarter we saw both Gartner and IDC re-release the SAP magic quadrants. HCL AXON ranked in the leaders quadrant in Gartner, again the only Indian headquartered firm to be rated as a leader on the

SAP market and IDC also ranked as again third in that quadrant in the major player category. Well it is encouraging that both Gartner and Forrester came out two quarters ago, where HCL AXON was ranked as No. 1 for customer satisfaction which has been a good focus for us.

Just a few remarks on public services vertical aspect. We have had two extremely strong quarters of growth on the public services side. 9.6% QoQ this quarter coming up after 8.3% QoQ last quarter. A big part of that has been coming from our utilities practice, where in the last six to 12 months we saw a lot of discussion about the deployment of Smart Grids and the need to align platforms to enable Smart Grids to operate, we are starting to see that really generate volume of projects for us and we build a particular niche in taking the meter readings through EME to technology into the back office systems and redesigning those to enable Smart needs to happen. So, utilities practice has been a strong differentiator for us and a strong growth engine.

So, on that note I will pass over to Rahul.

**Rahul Singh:**

Thanks, Steve and good evening, everybody. I will talk to you about the Financial Services vertical. I think it is important to note here that we closed the year with revenues exceeding a billion dollars and this is the first time that for the annual year revenues for Financial services were at a billion dollar. For the quarter we ended at about \$257 billion which is a 5.2% growth on constant currency on a QoQ basis, again reflecting a reasonable momentum in the Financial Services market. Important to note here that if you take a three year CAGR, HCL has recorded 22% growth on a compound basis in Financial Services and it puts us amongst the top three outsourcing providers in India. Reason for that essentially is our expansion of new service lines in existing customers. In fact, 90% of our revenue today comes from F500/G2000 customers. So, we have been able to grow incremental service clients into existing accounts and that caused the revenues to go up from the existing customers plus we have added some new logos as well, based on satisfaction levels which were low with existing providers.

Now, if you look at Financial Services as a whole and there are lots of questions coming up on HCL's strategy on Financial Services versus the rest of the peers in the market. Now, the overall commentary is that Financial Services is stressed in the US and Europe markets. There is a top-line issue which Financial Services firms are facing, so which is resulting in the spend of the CIOs moving towards trying to optimize RTB spends, and there is a focus towards reduction of cost including efficiencies, and HCL's ITO focus on infrastructure and application services is a fit for that. To improve the utilization of the outsourcing, the customers got to optimize the RTB spends. At the same time, our customers are taking the money out from RTB and are investing in what we are calling as prudent CTB because as the discretionary spend has come down across our clients, there are certain expenses that they still need to incur, especially around risk management regulatory and also around improvements of customer experience, because customer experience is where they get their growth. So we are trying to focus to the business in these two growth areas on the regulatory side as well as the customer experience. Our investment in terms of appropriate solutions around Mobility, Big Data and improving the

CRM from a customers perspective are places where we are seeing certain amount of growth coming in.

On an overall basis, the key things that we have been able to position for our customers are value-centric solutions, we have invested in front-ended solutions and people which are more domain oriented, industrial client partners, that has enabled us to get higher traction from existing accounts, as I mentioned also get some new businesses. Also, as we have repositioned some of the geographies like Europe and US, we feel more traction coming in, in from Central Europe, eastern European countries.

From the point of view of recognitions and value propositions a couple of platforms that we have got like Capital Stream etc. have been nominated as best-in-class in their service lines. But more importantly, we have been focusing on innovation as a differentiator, we have started innovation labs for some of our customers where we are able to build together newer technologies and demonstrate that to customers, and also work in areas which are more value-added and transformational in nature. So some of our solutions on vendor experience, money movement, compliance, etc. are what we are focusing as well.

With that I like to hand over to Anil.

**Anil Chanana**

Thank you, Rahul. So the results this quarter, \$1.08 billion in revenues and net income of \$156 million, the revenues up by 3% QoQ and the net income up by 28% YoY. If you look at year-on-year it becomes a very interesting story. So, 17.1% growth in revenue and 31% growth in net income. Our margins, we were in FY11 at 10.7% net income margin and 14% EBIT margin, this year we have closed the year with 12% net margin and 16.4% EBIT margin. This has been an expansion in this year. In this year there is an expansion at all levels from gross margins, EBITDA, EBIT and net income.

Other thing which is notable his quarter is the EPS. In rupee terms, EPS is Rs. 49 per share annualized. Last year same time AMJ'11 it was Rs. 29 per share. So, the earnings per share has gone up by 70% YoY.

Moving on to the next slide, where this revenue growth came from. So, in this quarter there has been an increase of close to \$32 million in revenues which is a volume-led growth. Exchange took away 160 basis points from the revenue.

If you look at where exactly this margin expansion happened from, at EBIT there was an exchange benefit which accrued 223 basis points and outside the exchange we had 149 basis points of productivity gains and SG&A optimization. At the net income level, the hedging had an investment of 28 basis points to have impact of 92 bps outside of exchange with negative on account of lower other income and higher tax charge. So net-net it was an improvement.

Going further, if you look at the fund position, so now we have \$0.5 billion of cash in hand as of 30<sup>th</sup> June and our loan funds are \$345 million. Loan consists of foreign currency loans of

\$176 million and rupee loans of \$169 million, so almost half-half. The cost of these funds pretax is 5.1% while the return on the funds we are getting is 8.6%. The table below gives how it has moved over the quarter, last quarter net cash was \$83 million and currently, we are at \$158 million in Net funds.

Moving further, in terms of conversion of net income to operating cash flows, it is a third consecutive year where our conversion of net income into operating cash flows has been in excess or equal to 100%. The other feature has been that this year the free cash flows as a percentage of EBITDA have been at 42% and the free cash flows in value terms have been \$330 million which is significantly higher than what it were last year. If I look at the return on equity we have moved up from 21% in FY10 to 22% in FY11 to 26% in the just concluded financial year, which is the highest in the last five years.

Moving on to the next slide in terms of receivables, our receivables were at 80 days and the billed receivables were at 57 days. There was an improvement of one day as compared to JFM'12.

Moving on to the hedge book, so we have a hedge book of \$1.4 billion. Our balance sheet hedges are \$250 million and cash flow hedges are \$1.1 billion. \$536 million of hedges are less than or equal to one year and \$600 million more than one year. The average rate is 55.83 US\$/INR and the M2M rate which has been applied here is 60.63 US\$/INR while the quarter end rate was 55.64 US\$/INR. If you look at the instrument mix it is predominantly forward and partially Options. Range Options are between 52.50 to 55.33 US\$/INR. Significant of these hedges are in USD/INR.

Moving on to the tax line, this quarter the tax charge was 22.8%. For full year, we had guided around 24%-25%, and we are at 24.5%. For the next two years we are anticipating it to be between 23% to 25%.

Moving on in terms of employee stock options outstanding, we are close to 3% of the outstanding capital, out of which 1.17% are vested and 1.81% are yet to be vested.

The option charge likely next year is \$16.6 million before the tax benefit and \$14.8 million after the tax benefit.

I would also like to highlight that the Board this time has declared Rs. 4 dividend per share. We have been declaring quarterly dividend and this is the 38<sup>th</sup> quarterly dividend. This particular quarter the quarterly dividend has two components. One being the quarterly in nature and the second being the annual dividend. So, the board decided this time that both will get paid at the same time after the Annual General Meeting. The annual dividend as a practice will be decided by the Board with reference to the performance of the company during the year and the need for cash in the company.

So, with this I will hand over to the operator for questions. Thank you.



**Moderator:** Thank you. Ladies and gentlemen, we will now begin with the question-and-answer session. The first question is from the line of Anantha Narayanan from Credit Suisse. Please go ahead.

**Anantha Narayanan:** I had a couple of questions. First one, is over the last three years, HCL Tech has been signing a lot of fairly large and complex projects. The scope and scale which would have been fairly new to HCL Tech as it has been to the off shore IT Services segment as such. Given the fact that you are competing with companies that are operating at relatively low margins, could you maybe just run us through some of the risk control measures that have been put in place, how do you ensure, for example, that execution is flawless and how these margins may not slip from these levels?

**Vineet Nayar:** Ananth that is a great question. Cumulatively, we would have signed in the last four years closer to about \$8 billion of such deals and majority of them have already been executed by us. What we do is as follows: Number one, for transition we have a dedicated team which focuses only on transition and takes the customer from the contracts to steady state and then moves on to another contract. So, these guys are best in the world and have come from the best companies in the world and have done the best transitions for us and therefore we de-risk our selves by creating a dedicated fairly large transition team and then steady-state is easy for us to do.

The second we did was we spent a huge amount of money about five years ago and then keep on spending -- it is about 300 which works on tooling for automated discovery of access to customer location and automated knowledge management, so therefore in every interaction with the customers we document a knowledge and it gets uploaded in the tool and the tools self learns itself and therefore the knowledge repository keeps building up. And electronically the customer has to sign off the knowledge to be correct and therefore, there is an accountability at the customer end that the knowledge transfer is complete. Most transitions which have gone horribly wrong for our global bigger peers is that they have not handled the knowledge management right and what we did was we converted that into a fairly sophisticated tool on transition management which the customer has to sign off. That is a second thing we did.

Third thing from pure contracting point of view, we have ensured that the rights and we have a full function called the business finance function and it is headed by a corporate vice president. The business finance function, only job is to contract these deals, they do not do anything else. So, they get involved in pricing, they get involved in estimation, so they have also a group of engineers which is part of the business finance function, they do the estimation, they do the pricing, they do the contracting and then they do the handover of transition till steady-state. So, it has handed over to what we call the global finance organization only after we finish the transition and it moves to steady-state. So the entire contract management is a specialty function under business finance and I think we are the only company which has a business finance function and it is embedded inside the finance function.

Then, the fourth, we have the specialist organization which is what we call the transition management organization for HR. This is again what we call the business HR function. So

they get involved at the time of scoping, upgrading, of contracting, of transitioning of employees and managing the transition and managing them through transition and into steady-state, because the biggest problem in a lot of transition is that you lose a lot of employees who will go away or an employee will sue you predominantly because you did not follow the process or you lose a lot of money because you cannot offshore a lot of work. So, there is a dedicated business unit which does just that.

Also, we have a very robust methodology of what we call the 'Governance and Management' with a customer which we insist, and that is embedded inside the contract. So, we have what we call a weekly hot call with the customer, which looks at all transitions and all elements of the transition of how it is going, we have a monthly executives meeting with the customers which is face to face, and we have a quarterly meeting with the corporate sponsor. In certain cases, I am the corporate sponsor, in certain cases, some other corporate officer is a corporate sponsor. So we insist on those meetings, those meetings document what is going, red, green and amber, so that the customer cannot go back and saying, this is not going fine, and these have identified the issues well in advance, it increases our interaction with the customers, and it increases us to document the trail of anything going wrong.

And the last, I think the most important issue is that we, over a period of time, do not take margin risks with new deals. So therefore our ability of putting more onsite than we believe are required, more laterals even if we believe there are pressures, so we do not take risk in the customer contracting, especially if we are doing something for the less than ten times and we do not take a risk. The risk only comes in and margin expansion comes in only after the steady state. So in the transition, the entire emphasis of HCL is to get the transition right because steady state is very easy. So I hope I have answered your question.

**Anantha Narayanan:** Just my final question was, in your opening comments you mentioned that you have some headroom for margin improvement but at the same time you need to make more investments for incubation of new businesses. So if you look at it say two or three years out from now, what is the margin level that you will be comfortable with?

**Vineet Nayar:** I think we have stated very clearly we do not give any margin guidance for the future, I think we just want to indicate to the market that we are in structurally a different margin profile business, at the same time we are also indicating that in this business also once we get in, there is an ability of selling higher margin business, other than that, Ananth, I do not want to guide.

**Moderator:** Thank you. The next question is from the line of Pankaj Kapoor from Standard Chartered Securities. Please go ahead.

**Pankaj Kapoor:** I understand that we have been of course more focused on the total IT infra outsourcing deals. But just wanted to get your sense if you are seeing any abnormal increases in the vendor consolidation-based deal for pure application management work, especially in the last few months and how are we approaching such opportunities?

**Vineet Nayar:** The answer is yes, we are seeing a significant increase in vendor consolidation in the Financial Services sector. And that is about it. So majority of the vendor consolidation deals are coming in Financial Services and they are coming very, very thick, means there is a lot of traction. And this is what I call a less than one year phenomena and if I am right we would have won about seven of them this year, which are pure MSAs and then after you sign the MSAs you become a strategic vendor, after you become a strategic vendor then you hunt your way into whatever the billion dollar spend is.

**Pankaj Kapoor:** Just following up on that, I believe in January you had spoken of some four MSA wins in the large Financial Services firm. So, I was wondering if it will be possible for you to give an update on them, in collectively like what kind of run rate are they currently on and are we gaining from any vendor consolidation deals in those specific names?

**Rahul Singh:** This is Rahul here. We have won both kind of deals in the last one year. We have won certain amounts of deals which are RTB which is basically large contracts where the client is actually dissatisfied with his existing vendor and he transfers to HCL because he believes that we could do it more profitably from his perspective. And we have guided last quarter that we had about \$1.4 billion of total wins in Financial Services, out of which some of them are RTB kind of deals. We have also won some PSL deals, which Vineet spoke about where we have become a preferred supplier. Now, the preferred supplier deals however tend to take time to ramp up. So it is not that you end up kind of having a large run rate coming in the first couple of quarters. So there the growth rates are slower from a total new business perspective, but we have been making good progress on them, and we have a shot now at multiple RFPs, etc., which come out from those clients, but the rate of growth will be slower because it is not as a transition of full business happening, it is to be ramped up as time will go by. Does that answer your question?

**Pankaj Kapoor:** I was actually more focused on those four MSAs, if you can give some color....

**Vineet Nayar:** I can, I just computed this on very quickly, Pankaj, they are not significant part of our revenue in April-May-June, and it is still early days for those four deals.

**Pankaj Kapoor:** And last question is on the currency pass-through that we saw in this quarter, was wondering what will be your approach for FY13 if one has to project out, if rupee continues to be in the Rs./US\$ 54 - 56 kind of a band, how does this change our stated level of around 14% of EBIT margin that we have spoken of earlier, is 16% the kind of a new-normal for us?

**Vineet Nayar:** I think obviously, the 14% does not hold at these dollar margin, that is a fair assessment, and the current margins levels should hold for the future, is all I want to say right now.

**Moderator:** Thank you. The next question is from the line of Mitali Ghosh from Bank of America. Please go ahead.

**Mitali Ghosh:** Just following up on the previous question, Vineet, on the margins, so if I understood that correctly you are saying that assuming let us say constant currency from these levels, you feel the margins should be sustainable?

**Vineet Nayar:** The annual margins, yes.

**Mitali Ghosh:** And the context of my question really was that we have obviously seen some of the outsourcing deals that ramped up earlier reaching steady-state and that has obviously contributed to the expansion, but just thinking that the \$2.5 billion that you have signed in the last couple of quarters, as those ramp through the year and also as you had stated that you intent to do a fair amount of lateral hiring, should one assume that those two things could result in any kind of dip in margins on an annual basis?

**Vineet Nayar:** Based on all what we know today, our guidance is there is no probability of the margin dip on an annual basis at the current dollar rates.

**Mitali Ghosh:** Secondly, Vineet, just wanted to understand on the pricing environment, there has been a lot of debate lately what is the pricing environment in the industry and what we really keen to understand is whether you are seeing a price disruptive behavior from competitors, so what is the competitor behavior is like versus what is the pressure you maybe facing from clients?

**Vineet Nayar:** I just want to go back to the original question. My guidance is with reference to year, I hope you are aware that we give our annual increase in the July and October cycle and therefore you should bake in 200 basis points dip spread over two quarters, so on annual basis at the current dollar rate, of whatever knowledge we have about the market there is no probability of a dip in margins. Coming to competitive, I do not see any aggressive pricing behavior as a competition because that is not the basis on which the total IT outsourcing decision gets made. In the Financial Services and vendor consolidation, yes, there could be some kind of pricing on T&M resources to be provided onsite and offshore because Financial Services has largely been a T&M oriented workplace. But on total IT outsourcing, the customers are extremely sensitive on who they choose and therefore the price negotiation only happens with the final two or final three and people who arrive at the final two and final three are conscious about the commitments they are making in delivering, and there we have not seen any change in the pricing over the last two years.

**Mitali Ghosh:** And just finally, two quick questions, one is you had stated some months back that you have taken a decision on acquisitions to defer that for a while given the volatility in the macro environment as well as in the currency. Any update on that?

**Vineet Nayar:** We still do not have any acquisitions, so we will take the decision on a quarter-by-quarter basis. As we speak, we do not have any acquisition under the active consideration.

**Mitali Ghosh:** And finally, if I may and congratulations, Anant, on your additional role as COO, just wanted to understand if you could elaborate a bit in terms of the additional responsibilities and sort of additional focus maybe at an organization level that this reflects?

**Vineet Nayar:** I will ask Anant to explain the way we are thinking about it. Let me start by opening this conversation by saying that at HCL we have always thought through about any changes to be building competitive advantage. Our big mantra in HCL is to win and the only way to win is by building competitive advantage way ahead of the market. So, when we were thinking through our competitive advantage there were a few ideas which were floated within the organization that some amount of changes in our senior management focus would create a competitive advantage. So, let us walk through that detailed thinking about the strategy and then I will add towards the end.

**Anant Gupta:** I think, it is important to get a background first on the reasons, as Vineet had mentioned....

**Vineet Nayar:** And there is a slide which we have put on the live meeting for those people who are following live meeting.

**Anant Gupta:** The whole objective was going of doing additional role is really about building competitive advantage and therefore it will be important to just kind of get a sense what has been some of the key success factors that have worked for HCL. The first is, as you are all aware that we have a fairly balanced portfolio of services which obviously, comes from the fact that our organizational design, our independent business, business units driving excellence, focus and innovation in their respective service lines. Therefore, looking at different geographies, different segments and differentiators to make sure that they are best-in-class in their respective area. The second, what has worked really well for us has been the innovation and organization culture which is built around the entire employee first, customer second framework which essentially is, the objective is about infusing, encouraging and enabling our employees so that they can at the end deliver higher value to the customers and also drive some growth for the company. And the third area has been ability to kind of look at early indicators in terms of businesses, it is very different from the concept of looking at incremental technologies to participate in but fundamentally looking at businesses that could be potentially million dollar of growth engines of the future and where we have a first mover advantage in there, with examples of organic being Infrastructure and the Engineering Services and from an acquisition perspective, EAS as well

What we are seeing has changed in the environment, obviously, our strategy has been to lead into an engagement with a dominant service line for that specific opportunity or the requirement of the customer and over a period enlarging that into a multi-service delivery framework. And obviously, you are seeing some of that reflecting in the movement of customers in different revenue streams that were shown earlier. So what this is really resulting in is there is significant interfaces that are required between the multiple service lines that need to be in tandem. And therefore, the success and the value deliver to our customers will really be in the value that we deliver at this interface.

And finally, it is about technology-led business transformation which is what we are seeing. We have been hearing concepts of RTB which is optimize industrialize operations and CTB which is how it could impact and change the business but increasingly we believe that the market landscape will change into what we believe as grow the business. So, while these are early conversations with businesses, there is an imperative need to look at what will drive growth for our customers and therefore what services will ultimately get created over there.

So keeping these two backgrounds in mind in terms of what has worked and what has changed, there are three imperatives for us, for these specific areas. One is, how do we create competitive advantage in the interface which is by industrializing this, so each service line on its own right is industrialized, the scale and size is large but how do we make sure the interfacing between these independent service lines will actually be more industrialized in the next phase of growth. The second is really maintaining our growth momentum which we have created over the past three years, both through customer satisfaction and customer wow and therefore ensure that we continue to grow that momentum in individual business lines without any change, but making sure that the areas where fungibility is there we bring that advantage at the table. The third key aspect is given the fact that these multi-services will look at different ways in terms of how we could optimize it, so the third real agenda is looking at how we could rethink some of the cost structures in delivering and executing some of these multi-service engagements.

**Vineet Nayar:**

So given that understanding we see imperatives for us to succeed, so there is an agenda which each business leader has which is growth and profitability, then there is a COO agenda which are these three which Anant articulated and there is a CEO agenda which is the business leaders agenda, the CEO agenda and there are three other agendas which we need to do well. If you look at the \$4 billion of HCL, a billion from it has come from infrastructure which did not exist and almost a billion has come from enterprise application and business intelligence services. Now, both were incubated, one through two acquisitions and one through organic build-up. So, if we ask ourselves five years from now what is the world looking like, obviously, the churn in the run-the-business market would have died out because all these churns are happening in the pre-recession contracts which by 2014 is going to die down and 2015 is going to be a tough year for churn. So, ideally we would have got into the businesses, whichever businesses we want to get into, whichever customers we wanted to get in, by that time we would have got in and our customer profiles of Fortune 500 would have increased. But what do we do with that? And if we do not incubate new business ideas which are going to be cutting edge like the infrastructure management and enterprise applications, we will lose momentum and somebody else will come and eat our lunch. So, therefore incubating new businesses is going to be one critical success factor.

Number two, the organization culture will have to undergo transformation. Is it going first? The way it is implemented adequate or it needs a structural change especially because we are going and hiring a lot more global employees first when this whole theme was conceptualized.

And the fourth is that IT spend across the board is 3% to 6% depending on the industry you are. But if you look at other spends like the marketing spend it is 8, 9% of the revenue of the company. And with data analytics coming in, with social media coming in, with mobility coming in, it is possible for marketing for IT to be able to address the marketing budget rather than just do the IT budget and similarly, there will be enough opportunities as IT and technology solve business problems to be able to look at some other budgets and not just on the IT budgets. All these three ideas are very vague right now, all these three ideas have no basis but they have to be incubated and they have to be incubated and they have to be formed and they have to be invested and they have to be given shape and that is going to be a critical success factor going forward, and that is going to be an added agenda of this year.

So by structuring ourselves between the business leaders, the COO agenda and the CEO agenda I think we have very interestingly carved out different growths and responsibilities for different people and we would be able to spend a significant larger bandwidth in new areas which will transform the company and make it more competitive each year. So that was the thinking behind bringing about this change.

**Moderator:** Thank you. The next question is from the line of Ashwin Mehta from Nomura. Please go ahead.

**Ashwin Mehta:** I had a question in terms of the \$2.5 billion deal flow that we won over the last two quarters. Just want to get your sense in terms of what proportion of the transitions of that have got reflected and possibly would it be fair to assume that the Q3 deal wins have not necessarily reflected in terms of revenues as of now?

**Vineet Nayar:** I think all CTB components of the \$2.5 billion are already reflected in this quarter, they are already picked in, because they virtually start immediately. All short cycle transitions which are what we call 60-day transitions especially in the areas of infrastructure have been baked in into this quarter at different points of time. The longer transition which is application transition which are six months transition are not fully baked into these numbers.

**Ashwin Mehta:** And would the longer transitions be a substantial portion of this?

**Vineet Nayar:** That would be paramount to giving guidance, so we are not sharing that split right now.

**Ashwin Mehta:** Second question for Anil, what is the OCI balance currently?

**Anil Chanana:** If I take the MTM phase which is Rs. 60.63 it is -\$85 million but if I take the closing rate, it was Rs. 55.64, it is -\$4 million. So, HTM is -\$4 mn and MTM is -\$85 mn.

**Moderator:** Thank you. The next question is from the line of Nitin Mohta from Macquarie Capital. Please go ahead.

**Nitin Mohta:** My question, Vineet, was on the win ratios that we are seeing in the marketplace, earlier in the day you have commented that 70% of those churn wins are actually coming from international

players. When I contrast this with Accenture's commentary on their call where they have also talked about winning market share, I was just trying to understand where exactly are you getting this win from, is it specific to the Europe market or are you seeing that even in US?

**Vineet Nayar:** We are seeing this across US and Europe. If you look at the deal names which we have announced, I think you would be able to understand where we are winning from, so we have announced AstraZeneca, if you do a Google search, you will know who AstraZeneca was with. I do not want to say this on a conference call but if you look at the deals we have announced, the large deals we have announced and you search to which vendor they are you will come down to two companies which are losing a substantial market share and losing a lot of client base. Two companies in US and I think one company in Europe.

**Moderator:** Thank you. The next question is from the line of Ankur Rudra from Ambit. Please go ahead.

**Ankur Rudra:** My question is on the SG&A spending. I notice that it has been a bit light for the last two, three quarters, especially for the first time I think in a long-term Q4 has been lighter in the entire year, I was wondering how much of this is permanent efficiencies versus a function of your lack of aggressiveness?

**Anil Chanana:** What happens is, we had stepped it up before the deals started coming in. So, if you would have seen last year towards the middle part of the last year it was high because that was the time to put a pedal on it, we were putting bid together, these are big bids, we have to do a due diligence and so on and so forth. So all that costs went in and having won, we said that we slowing this and focusing more on the execution. So, this is something which will keep on varying from quarter-to-quarter, because the nature of the business is I mean basically you are trying to get into more annuity based revenues which are long-term in nature and you want to be sure that is part of the risk mitigation exercise that you do not take any wrong bet, so that is the whole outlook.

**Ankur Rudra:** So at least part of this sustainable on a YoY basis?

**Vineet Nayar:** No, we will increase at it. Please be very clear, you use the word, 'lack of aggression for HCL' be very careful with that word.

**Ankur Rudra:** I was using your word that you gave us a couple of quarters back, Vineet.

**Vineet Nayar:** No, October-November-December we are arriving back in the playing field.

**Moderator:** Thank you. The next question is from the line of Rishi Maheshwari from Enam. Please go ahead.

**Rishi Maheshwari:** I have got two questions. One that I have seen large variance in almost all of your peers on the Indian side in terms of the volume growth. Your comments on whether you are also winning market share against them. Secondly, given the last four, five years that I have seen HCL's



history you have always managed to beat NASSCOM's guidance on the upper end. Any indication in terms of this year will be more or less the same trend?

**Vineet Nayar:**

I do not want to talk about NASSCOM's guidance predominantly because that is going to be giving you guidance. I just want to step back and explain there is a different commentary from the industry as I understand it and I maybe wrong about it, I think what has happened is all of us have chosen different business models to grow. And if you look at the portfolio, some portfolio is under threat in terms of it is coming down, some portfolio is increasing because they are in the right market and the momentum is behind us, some customers we are acquiring new, some customers are under threat predominantly because they are going through a rebid process. So, depending on what percentage of your business is in what portfolio you see different commentaries coming from companies across the world. So, an Accenture is giving a very bullish commentary so is some Indian players, and some other may not be giving a bullish commentary depending on what percentage lies and what bucket and therefore it is not the quality of the company or the strategy is just the fact that they find themselves in different sets of portfolio. At HCL, fortunately, we have a larger portfolio in the growth momentum where we are participating in the market, we structured ourselves to a lower margin profile so that we can participate and grow faster, we are not facing competition in our existing customers because we were the first off-the-block to restructure those contracts in 2008-2009 ourselves proactively. So, so far our strategy is working and we are able to also cross-sell and upsell because of the integrated services, structures which we put together over the last three years and focus on bonuses, on cross-sell and up-selling mixes so the whole strategy for HCL at least in the short-term especially till the market continues to behave the way it is seems pretty good. Now, will we meet or beat or be below NASSCOM guidance? I do not want to guide about it.

**Rishi Maheshwari:**

Let me phrase it this way that as an active participant of the industry do you think that the NASSCOM has projected the right guidance or is there scope for it to go higher or lower?

**Vineet Nayar:**

I do not have a visibility on the basis on which they guided, hence I have no comment and plus unfortunately I do not have a visibility on what other companies are planning inside. If I had that I would have definitely giving you the guidance.

**Moderator:**

Thank you. The next question is from the line of Deepesh Mehta from SBI Cap Securities. Please go ahead.

**Deepesh Mehta:**

I have two, three questions. One is, I am trying to understand about BPO business. When do we expect BPO to return to growth trajectory? Second question is about wage hike can you quantify wage hike would be given this year? And last is data-related. If I see your foreign currency loan, earlier we suggested around May 2011, it would be eight equal installments. So this quarter our numbers are slightly different. So, any change or restructure that happened in that?

**Rahul Singh:**

Let me respond on the BPO question, I think we had guided earlier that we are looking at restructuring the BPO business and we were looking at breaking even in terms of margin

profile as of date in this calendar year. So, we are happy to report that both the JFM quarter and for the AMJ quarter, which ended on EBIT-neutral basis. And that is a substantial improvement from previous year where we had almost \$22 million of losses in the BPO business. So, I think there is a substantial improvement that has happened. Looking at the future we do continue to have two kinds of businesses within the BPO. One is what we are defining as growth business which is focusing on certain vertical-based transaction processing-based BPO which we intend to and are growing already. We have won significant contracts last year in that segment. And the second business is the one that is still progressing in certain amount of drag for the portfolio which is more a call centric-based and here is where the margins are low. So, our target is to have a BPO at company level in terms of margins, the entire restructuring will take two to three years to complete but what we are happy to report here is that we have moved substantially in terms of recontributing the BPO, there is new business which are sitting in there, which are doing very nicely and as a result of which we have been able to almost wipe off all the losses from the rest of the business.

**Deepesh Mehta:** Just to continue about BPO, on two, three years from here on or where are we in that journey?

**Rahul Singh:** What we are saying it will take 24 months to 36 months for the BPO business to be at company level margins, that is what we are trying to say. So that you have seen it has been improving every quarter. So, quarter-on-quarter there has been improvement coming and the reason why the improvement is coming is because the newer businesses we are doing are at higher margins as well as the higher realization because they are in the focused verticals, we are focusing on Healthcare, Banking and Insurance as focused verticals and are doing more transaction-based work in those segments.

**Vineet Nayar:** Just to answer your question with reference to the wage hike, the offshore wage hike we have announced is 8% and the onsite is 2% which will impact the margins by 180-200 basis points and it will be spread equally between July to September quarter and October to December quarter. So, we have two cycles for wage hike.

**Deepesh Mehta:** And about foreign currency loan?

**Vineet Nayar:** With reference to the foreign currency loan, you rightly observed that we have restructured it, meaning we have partially repaid our foreign currency loan and replaced it with another cheaper loan, which was available. So you will find that another \$75 million loan appearing and the foreign currency loan which was the earlier loan has got reduced. So, it is a restructuring and nothing else.

**Deepesh Mehta:** Because earlier we said Q4 would be more towards execution, how we define Q1 to be, to be more towards execution or more towards chasing the deals.

**Vineet Nayar:** Execution.

**Deepesh Mehta:** And where do we expect chasing the deal would be significant, second half of the year or first half?

**Vineet Nayar:** Yeah, second half of the year.

**Moderator:** Thank you. Due to time constraints we will take the last question from the line of Shekar Singh from Excelsior Investments. Please go ahead.

**Shekar Singh:** Just wanted to know is there any impact that we can expect post the US Presidential Election in terms of like increasing the pace of offshoring as well as increase in fresh development projects?

**Vineet Nayar:** I do not think so. It is difficult to say, but I do not think so. I do not think that is preventing from any of this happening, there is a lot of noise in media about it. But is that impacting any decision in the corporate world? The answer is no. And therefore are we going to see an upside after that? I do not think so. I truly believe that the future of the IT industry is going to be the ability to create local jobs, that has got nothing to do with the election, that will be seen by most of our customers to be behaving in a socially responsible fashion and the pressure will continue. So, I do not know but sitting right now I think there will be no difference.

Thank you, ladies and gentlemen, thank you for joining us for the conference call and look forward to speaking with you next quarter.

**Moderator:** Thank you, gentlemen of the management. Ladies and gentlemen, on behalf of HCL that concludes this conference call. Thank you for joining us and you may now disconnect your lines.