"HCL Technologies Limited Q4 FY'18 Earnings Conference Call"

May 2, 2018

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Moderator: Ladies and gentlemen, good day and welcome to the HCL Technologies Limited Q4 FY'18 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 touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. C. Vijayakumar – President & CEO, HCL Technologies Limited. Thank you and over to you, sir.

C. Vijayakumar: Hi! Everyone. Good evening, good afternoon and good morning to all of you. Welcome to HCL Tech's Fourth Quarter Earnings Presentation which also covers the annual results for FY'18.

Today, I am joined by several members of the HCL leadership team; some of them in the room and some of them on the call.

So, let me get started. In terms of an overall financial summary for FY'18 from a revenue perspective, we grew 12.4% YoY and for the quarter ended 31st March we grew 2.5%, from a constant currency perspective it is 10.5% revenue growth and 1.2% revenue growth on a sequential basis. Our EBIT margin for the whole year came in at 19.7% and for the quarter ended 31st March came in at 19.6%. Overall, this is the second consecutive year of consistent execution of our overall strategy. We have met our guidance on the revenue and margin over the years. So we feel very satisfied with our overall performance. It is also signified by some important milestones; we crossed run rate of $2 billion quarterly revenues and for the first time HCL crossed Rs. 50,000 crores in revenue in this year. Overall, we are happy that we have ended the year with industry leading growth meeting guidance on revenue and margins.

If you look at our performance trends over the last five years, fairly consistent performance, CAGR of 11.5% in terms of revenue, on the headcount grew 7.3%, continuing to demonstrate significant non-linearity in our business model and this has been further accelerated in the last two years driven by our Mode-2 and Mode-3 services. We have had a consistent growth in EBIT and an even greater growth in our net income, really focused on continuing stable and profitable growth trajectory in our business.

If you look at the performance in different segments for the last year and the last fiscal, the growth has been consistent and broad-based. Some of the real highlights are 13.3% industry-leading growth in Financial Services, a lot of this is enabled by digital services, both in our existing clients and in new clients. A lot of our customers are looking at us as a disruptive service provider and are looking at replacing some of the traditional providers within our offerings. The growth has been fairly secular in most other verticals in FY'18. Healthy growth across all geographies, led by US, close to 14% YoY growth. Engineering and R&D Services grew 37.6% enabled by all three dimensions which is organic growth IP partnerships and acquisitions. During the year, we reorganized our sales organization, part of which was already vertical-led from a go-to-market perspective. Now we have completed the reorganization across the board, HCL sales teams for the IT Services are now organized by a vertical and this is primarily done to address the market opportunity on Mode-1, Mode-2 and Mode-3 in a much more cohesive manner and we expect this to enable a good momentum that is already in progress in the Mode-2 and Mode-3 businesses.

Moving on, just a snapshot of how we have performed over the last three years in terms of our Mode-1, 2, 3 strategy: In FY'16, we had 15.9% of revenues coming in from Mode-2 and 3, it increased to 18.6% in FY17 and in FY'18 it came in at 23.4%. Our Mode-2 revenues grew 29.4% YoY in FY'18 and Mode-3 grew 68.3% and a combined Mode-2 and Mode-3 services grew by 41.5%. So we believe our Mode-1, 2, 3 strategy is continuing to make a considerable progress and the results are very visible by the growth metrics.

We signed 15 transformational deals in Q4, consisting of all our services, geographies and verticals, for the year we signed about 63 transformational deals. As we had indicated earlier, we are seeing a strong increase in the number of deals and the deal sizes in our Mode-2 services with 26 customers in Mode-2 with revenues greater than $10 million in FY'18, together contributing to 49% of our Mode-2 revenues. In Mode-3, we continued our initiatives. We launched the first wave of managed services edition of some of the products apart from adding several products to our portfolio through a mix of home grown organic IP acquisitions as well as IP partnerships.

Moving on, a quick review of our client partnership program has progressed. We have demonstrated significant growth in our top-5, top-10 and top-20 clients. This has happened across different geographies and verticals. We continue to increase our wallet share from many customers where some of the traditional programs are being optimized and the spend is being diverted into some of the next-generation services. So this is clearly a strong success metric and we continuously track this to see how we can fine-tune and continue to improvise on our client partner program.

I want to cover a couple of Inorganic Updates: The first one is C3i. The strategic rationale is pretty similar to what we shared earlier. The C3i is a leader in customer engagement services in Life Sciences and Consumer Packaged Goods industry. They have very special capabilities in clinical, pharmacovigilance and pharma sales support domains. We believe HCL's Mode-2 digital capability combined with C3i's depth to be more patient-centric will help us to offer services to IT as well as business stakeholders to improve healthcare outcomes. I think one very strong strategic rationale is our ability to access business stakeholders in several client organizations in addition to the CIO organization was one of the prime drivers.

The second element was also, this has given us access to a lot more pharmaceutical clients and a few select top-leading brands in the CPG industries. As we had disclosed, the revenues of this organization has been coming down in the last three years at approximately 10% decline rate. So in our outlook for FY'19, we have factored in a decline of about 10-12%. We believe there are good opportunities to grow the services. We expect the growth momentum to pick up in FY'20. In the current construct of C3i, due to the parent company, several other pharmaceutical companies did not outsource work to this entity because of the competitive nature of the parent company with some of their businesses. We believe this will unlock some synergy and we will find some new growth opportunities. So we expect growth to be coming in FY'20. Margins of this entity is very low; we had EBITDA margin of 6% and the EBIT margin would be a couple of percentage points lower at this point. We expect the margins to reach HCL company level margins in three years. This will happen by a combination of growth in revenues which we think will happen in FY'20 & '21, and there are also significant costs out opportunities which are there in some of the SG&A line items. All this together will contribute to improving margins over the next three years.

On the next acquisition, Actian, primarily our focus and the strategic rationale for acquiring or deciding a definitive agreement to acquire Actian is primarily our interest in the area of data. We believe Hybrid Data Management is a very important area. As more and more hybrid operating models come into place with some of landscape on **premise** some landscape on the public cloud. So, Actian owns several market leading products as Actian Vector, Actian Data Connect and Actian X, some of them are extremely rated highly from a performance perspective. We believe it enhances our Mode-3 offerings and combined with some of the HCL's Mode-2 solution offerings, it offers powerful proposition to harness the power of hybrid data.

In terms of "Financial Outlook", the regulatory approvals are in progress. We expect this to complete by August 2018. In terms of revenue trajectory, though it has been declining for the last two years, we expect the revenues to be stable because we are already seeing some growth in the second half of the FY'18. So we expect revenues to be stable in FY'19 and growth expected in FY'20.

Now, I will hand it over to Anil to provide some additional commentary on the financials for the last year.

Anil Chanana: Thank you, Vijay. Hello! Everyone. Good morning, good afternoon, good evening. So a quick recap on the performance. A very strong quarter; we grew by 2.5% in reported terms and this was on the back of a very strong quarter, October-December quarter where we grew by 3.1%; we crossed 2 billion as a milestone on a quarterly revenue basis. In constant currency terms, we grew by 1.2%. There is a very strong client addition on YoY basis as well; three new clients added in the 50 million plus category and 6 in the 40 million category, 9 in the 30 million category and 55 in 1 million plus category, strong client addition across categories.

On annualized basis, we grew by 12.4% YoY and on a constant currency it was 10.5% as this was when we meet the guidance range we had obtained. Going to the margins, the margins this quarter have been flat at 19.6%. There has been variation in the margins between the service lines; the Software Services margins declined this quarter; Software Services comprises of Applications and Engineering Services. The Infrastructure margins improved this quarter as there was also improvement in the BPO margins this quarter. The Software Services margin as I said comprise both the Engineering margins as well as the Products and Platforms margins and Applications business margins. There is an element of seasonality when the October-to-December period, the margin in the Products and Platforms business significantly increased, there are a lot of renewals which happened in the quarter. So generally, if you look at just like September quarter the Software Services margin was at 20.2%, it went up to 21.3% and in JFM quarter it came to 19.5%. One of the questions I got during the day was, "Why there is a variation?" This variation is due to the seasonality and also to some extent due to higher payroll taxes in the US which normally hit in the first quarter of the calendar year and that goes on from there on. For very similar reason, SG&A also increased by 80 bps QoQ, higher payroll taxes, higher CSR expenditure in the quarter and professional cost associated with the M&A activity which happened. On annualized basis on the margin side, we have been within the guidance range of 19.5% to 20.5%. Our net income went up by 7.7% while our revenues went up by 12.4%.

I will touch upon the shareholder returns. So while you see the net income growing by 7.7% the earnings per share if I remove the impact of one-time tax benefit we got in the financial year '17, the earnings per share increased by 9.4%, it was about 46 million of benefit which came in the financial year '17. The return of equity stands at (+25%), so pretty good return on equity. In terms of payout, we will be paying 50% of the net income, and this is what we have stated that we will be striving towards.

With respect to the effective tax rate, we expect the tax rate in this FY'19 to be between 22%-23%. With respect to hedging, there has been improved performance of hedging, for the full year, the net hedge gain has been 83.5 million which is more 196% over last year and this quarter it was 24.6 million, we continue to follow a layered hedging program and we have mark-to-market gains of 26 million on held-to-maturity gains of 200 million in our balance sheet.

Going further, in terms of cash flow generation, the net income to operating cash flow generation has been 99% in full financial year, it was higher in this particular quarter at 123%. With respect to cash, the free cash flow-to-EBITDA ratio for this particular quarter has been at 80%, for the financial year it has been 65%.

A Quick Update: There is a question, whether we have done any IP deals this quarter and whether we did any payment relating to any new deals this quarter? There have not been any new deals this quarter and no new payment has been recorded, whatever payments are recorded are relating to the deals we had done earlier, we have about 200 million-odd still payable against the deal which we have signed in the earlier quarter.

With respect to verticals, we will be making small change. We currently classify the Manufacturing and Hi Tech together. We intend to align Hi Tech more with the Telecom, Media and Technology, TMT segment rather than the Manufacturing segment because there is synergy between the two. So, it will come as part of the Telecom, Media, Entertainment vertical, this we will be sort of updating going forward.

The other change we will be doing is we will be providing you the Mode-1, 2, 3 revenue every quarter so that you can see the progress what we are making with respect to each of these mode of services we are offering to our customers. We are also trying to work out at a certain level either at a gross margin level, we are still figuring out, trying to work out through our ERP system, what is the data we can provide, we will come back to you on that.

There will be certain disclosures which over a period of time have become redundant like bank wise calendar date and facility hedges, etc., which we would be discontinuing. We will be engaging with you before sort of making a disclosure during the quarter and then make the changes going forward.

One of the items I would like to touch is, there have been questions during the day with respect to our guidance and I would like to answer them and to the extent I am unable to answer, we will cover it in the Q&A going forward, I would also request Vijay to step in as I am explaining here. So, with respect to revenue, we expect our revenues to grow between 9.5% to 11.5%, this is using the average exchange rate for financial year '18. If I use the March end exchange rate, this works out to 10.5% to 12.5%. This includes both organic as well as inorganic contribution which is likely to flow in this 9.5% to 11.5% range. There are two acquisitions which we have already announced; the acquisition being the Actian and C3i. While we will be doing these acquisitions, we had informed you that India business is where we are reducing our emphasis and there will be a further decline in the India business which will be happening. So there will be a net-net impact of both on the overall revenue. So there will be positive flow which will happen from the new acquisitions which we have done and there will be negative so far as the India SI business reduction is concerned. We also did some acquisitions last year where the revenue benefit did not go for the full year last year, so part of the benefit will flow into this year. So net-net we anticipate for whatever we have inorganic activity we have done so far are committed to C3i acquisition and Actian acquisition where we have 400 basis points benefit which will flow. If I use the middle point of the range which is 10.5, 5.5-5.6 is supposed to be coming from organically and 5.5-5.6 is supposed to be coming from inorganic. So 4% will come from Actian, C3i and the last year acquisition adjusted for the decline in SI business. So about 1.25% of the inorganic revenue for which the deals are in the pipeline and which we will be announcing as we will be finalizing those deals, and we are very confident that we will be meeting that mid, I am just using that midpoint for the purpose, which is 5.25% inorganic growth, this could be 4.5-6.25, this is the range we have given to you.

In terms of margins, we expect our operating margin to be between 19.5%-20.5%. This is the same margin range which we had taken as a target last year. It assumes the average exchange rate for all the currency other than in the USD, INR which is at Rs.66 we have taken. We have factored in the impact of C3i which Vijay just explained which the margins were minimum and we will be improving the margins as we go forward. I have already told you about the tax rate which will range between 22-23%. So this is a complete color on the guidance.

C. Vijayakumar: I think you covered all the elements. Before we go to the Q&A, we have a couple of more sections. We wanted to provide an update on little more details on the progress that we are making in Mode-2 as well as Mode-3. So we will have Anand Birje talk about overall Mode-2 updates followed by Darren and a quick HR Update after that we will go into the Q&A. Over to Anand.

Anand Birje: Thank you, CVK. Good day, everyone. As CVK talked about earlier, this has been an inflection year for us…the past year for Mode-2 services and I thought it is appropriate to kind of recap something we had done three quarters ago, help explain what Mode-2 services comprise of and how they work in enterprise digital transformations, creating business outcomes for enterprises. So, there is a slide that was kind of put together to demystify that, we always talked about Digital and Analytics, Cloud, IoT and Cyber Security. Those core pillars, the four services within our Mode-2 services that are enabling enterprise utilization. If you look at it really what it means is that enterprises are rethinking their value chains there, business processes that are critical to be innovated upon so that they can transform and stays where the market and compete in the market. On these value chains, they are rethinking these value chains with human center design with user experience at the core to reimagine processes in these value chains. Whether it is a user value chain in how they interact with their users, internal users, external users and the consumers, their asset value chain depending on the industry they are in, all their service value chain. So user experience based process rethinking is the core capability that we bring, that is allowing us to work with enterprises on this value chain rethink. But the enablement of these value chains is happening through our composable digital platforms that are getting built with API, micro services and the core, our new technologies such as AI and Blockchain, Virtual Reality and augmented reality at the core and at the base of it, data as a fabric, CVK talked about our focus on data because the increasing importance of data has a foundation to digital transformations, both building data as a fabric and then really using insights from the data, whether the data comes from the business operations or from the machines and things that are in the enterprise, is a very important element of our analytics strategy. Obviously, we have always been deeply involved embedded systems provider on the devices side and so our IoT Works capabilities are very important element of digital transformation both in terms of integrating the devices in the value chains and getting insights and data from the devices in transforming these value chains. As digitalization is happening in the enterprise, the security profiles of the enterprises are changing and our focus on dynamic enterprise postures and creating new cyber security, our services for enterprises is an important element of digital transformations and finally the foundations of the enterprise are also transforming and moving from on-prem, discrete infrastructure to cloud and cloud-like infrastructure or API infrastructure and our cloud topology and Cloud Native services are helping enterprises sort of rebuild their foundations as they digitalize their value chain.

So again to recap, Digital and Analytics, IoT Works, Cloud Native Services and Cyber Security Services are really becoming the pillars of our Mode-2 services in digital transformations of enterprises. Some of the commentary on Mode-2, some detail in terms of where the growth came from and what are we seeing in the market. As I said, a lot of the growth is coming from three or four of these services coming together in helping enterprise creating those business outcomes, those digital transformations. CVK mentioned earlier, we had a fairly inflection and healthy year last year; 29.4% growth YoY in these space of services, led by Digital and Analytics. What was more important to us, we had extremely healthy, 40+ wins across verticals, across geographies, across US, Europe and Asia Pacific geographies. Quite a lot of these wins came from net new customers where we were displacing traditional vendors who are providing traditional IT Services in these customers.

Another important aspect and this is also a change that is happening in the market in the last few years is enterprises moving away from digital programs and digital projects to really ongoing scale digital partnerships. So, sufficient amount of our experience in that area has helped us over the last few years where almost 26 of our customers are in scale digital partnerships with us where we are not just delivering projects but multi-year digital programs across Digital, Cloud, IoT and Cyber Security Services.

Some of the investments that we have made that we have talked about in the past that we wanted to highlight and give some color to that on the last slide really. Both in terms of building new capabilities organically and building new technology and lab infrastructure, that are very-very core elements of digital transformation that enterprises seek. We have invested over $100 million over the last two years in building a variety of labs across US, Europe and India, experience centric labs for process redesign IoT labs for sensors, transducers, iotization of enterprises and processes, Cloud Native labs for cloud-based modern app development and cloud transformation that enterprises are embarking upon and then more specific labs like imaging and digital design lab or cyber security labs that we have built across the markets. These labs are also places where enterprises are coming to do co-innovation, prototyping, POCs with us in the start of their digital journey or during their digital journeys. We also really robotized our capabilities in design and user experience, bringing in leaders, bringing in practitioners and subject matter experts from the industry who came from mainstream design agencies from mainstream marketing transformation agencies across the world and they have become critical elements of our design studios and digital labs across the world.

With that, I will hand it this back to CVK. Thank you.

C. Vijayakumar: Over to Darren for a Quick Update on Mode-3.

Darren Oberst: Great, thank you, CVK. We thought as we close the fiscal year and as we embark on a new one might be a good opportunity. Just to set the context more on the strategy in terms of where we are and where we are going. There are still a lot of interest over the course of the last several quarters. All the activities that we had in the market from various IP partnerships and acquisitions. So we were to give just perhaps a broader view of how we are stitching together these areas, initiatives and investments into a much larger strategic transformation. So when you take a look at what are some of the key elements of the strategy and here we are looking to go. It is guided by a set of core principles and first among those is that we see this as a long-term transformational play for HCL, really instilling IP DNA across the organization, whether it is within Mode-1 and Mode-2 service offerings, what new products and assets that we will be bringing to market directly. It is a multi-pronged strategy with multiple ways to win. This is very consistent with the way that we look to incubate new businesses throughout our history. It is both about diversifying risk, it is also a way that we can accelerate entrepreneurial energy, building capabilities, both organically as well as through whole series of inorganic activity and across multiple parts of HCL. At net-net, I think it is important to emphasize this is we see this as a win both in the short-term something that benefit HCL in FY'18 will be a benefit from the revenue and profitability in FY'19, but really in terms of the long-term value, and the long-term value will get into some of the details to follow, but really how we start creating more transformational and new offerings for our customers and our partners.

And then finally, on this slide, just wanted to emphasize the fact that it is not a single strategy, this is something we are looking at technical areas across all of HCL's service businesses, both in terms of horizontal technologies, area that play to core competency matters like IT, Automation, DevOps, Data and Analytics, Legacy Modernization, Collaboration, Security, but also vertical solutions as well, whether it is in the banking industry, telecom or in other vertical areas, each of areas where we are looking to harvest and develop organically and inorganically key vertical solutions.

In terms of some of the updates, we highlighted in discussions, we proceeded this some of the investments that we have made, the new acquisition at Actian. We have also highlighted on quarterly basis the IP partnerships. I think I just want to take a moment to emphasize and do that in the next couple of slides as well. All the organic capabilities that we are building, this is both capabilities that have existed within and across HCL varied within our service practices, but also additional investments that we are making in building up the talent and skills and capabilities across the end-to-end software product value.

If we move on to the next slide, we wanted to give a slightly deeper view of this. Again, the key phrase that I would emphasize is “Multi-Dimensional”. We are not looking at it in a monolithic way, we are not looking at it as with that IP partnerships, it is about acquisitions, but let me try to take it up this in a holistic way that how we can incubate and develop capabilities towards this long-term transformational vision around Mode-3.

So I wanted to give you a view perhaps just segment into three major blocks: The first block is all the work that we have done in harvesting, developing and extending IP assets that have been created across HCL, whether it is in our infra practice to next generation IT service management, within ERS, lot of the capabilities around DevOps, testing excellence, application development practices, within our application businesses within our various verticals. Harvesting, incubating, developing and investing in innovation assets, and we then organizing this business under the overall framework of DryICE where we have really leading-edge capabilities with the focus on next-generation, service management and delivery, autonomics, lots of capabilities we have been building around AI, Machine Learning and how to really push the envelope for the next-generation of IT and cloud automation.

The second major thread that I would highlight is the products and platforms capability which houses today the major IP partnerships, focused on five major areas – DevOps, really the integration of the application development tool chain with application security, automation, collaboration, mainframe and legacy modernization and then data and marketing platforms. These are the five core proven scale products and platforms within this business unit. We have really focused on a playbook that we have developed over the years within HCL -- Energize, Modernize and Innovate. What we have seen course of the various IP partnerships that we have done is significant and concrete improvement of both in the underlying capabilities in the products and the associated revenue curve and value that customers are seeing from it. In conjunction with this, we have been building a lot of wrap around capabilities that are fundamental to building long-term successful product business. Whether it is product management, product marketing, capabilities around UI and UX enhancement and building modern experiences around a product portfolio, cloud enablement, product sales and professional services.

And then finally the third major pillar here on the right is a whole series of investments and initiatives that we have across HCL. We highlighted Actian in previous quarters, we highlighted acquisitions like Alpha Insight, Geometric, investments that we have made in the start-ups like Moogsoft, there are vertical software capabilities and IP partnerships associated with that. Again, the key point I would emphasize here is we have been looking at how we can close, how we can incubate in all of our service lines with Mode-3 offerings in IP-intensive businesses. The summary from this is what we see this is a long-term strategy around future proofing our business and over time building transformational solutions and capabilities across all of HCL. And then finally, what do we highlight for the quarters to come are increasingly a lot of these proof points in terms of new capabilities that were bringing to clients as a result of these various initiatives.

If we move to the next slide, I just wanted to take a minute, and this is perhaps in a very high level that we have thought it is calling out in emphasizing, a lot of new enabling capabilities that we have been building. From an investor point of view, you heard about an acquisition, you heard about an IP partnership. What is perhaps less visible is all of the connective tissue that we are building internally through hiring and developing of new talent and new skills into organization. It is a lot of the areas that we have been focused on in terms of initiatives, things like product packaging, it is product management, it is new innovative licensing models, it is building a lot of capabilities to be a leading edge with a product provider for the future. It is a lot of these initiatives and a lot of this work are going to be coming live over the course of the next several quarters. I just wanted to take a moment perhaps to catch the light on this in conjunction with a lot of the inorganic activities.

With that, I will turn things back over to CVK.

C. Vijayakumar: Appa will cover a few updates on HR and then we will go to the Q&A. Over to you, Appa.

Apparao VV: Thanks, Darren, thanks, CVK. A quick update on the HR front. We had a pretty decent year in terms of attrition; we exited in the last 12-months, we are at 15.4%, this is 140 basis points improvement over FY'17. Our increasing employee engagement is helping us. Another thing is the growth what we are seeing in Mode-2, Mode-3 areas, requires skills and scale, which we are not finding in the market, whatever little we are finding, is at a very high cost. So to accelerate the deployment into the new deals what we have. So we accelerated Mode-2 training programs and in FY'18 we have trained approximately 27000 people and 90% of them are deployed gainfully in various engagements, and we will continue to accelerate this program so that it is in line with our growth aspirations in Mode-2 and 3. We also have embarked on some huge technology interventions from the HR automation processes, such as talent acquisition, talent development, talent management. Today, we have pretty much integrated of the talent acquisition part. So from requirement raising to onboarding, we have already cut the size by 13-days and we hope to increase this a little more and then probably come below 15-days in terms of recruiting which will help us in terms of accelerate acquisition of talent. Workforce transformation and work place transformation are the areas where we are focusing. As part of that we took up a slew of measures on improving the gender diversity and we move the needle a little and today we stand at 24% and we would like to continue this focus in the coming year. We have been quite heavily focused in terms of localization in various geographies with all the incumbent problems we have in work across the globe and in one particular instance we were able to increase our localization from 52% to 58%, and we expect this to move a little further in FY'19. The amount of automation what we are doing, efficiencies, processes, streamlining, we continue to improve the revenue per employee which have increased by 5% to $66,000 over FY'17. So, this will briefly sum up the updates on HR, and I will pass it to CVK.

C. Vijayakumar: We can take question-and-answer. Over to the operator.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question-and-answer session. We will take the first question from the line of Ankur Rudra from CLSA. Please go ahead.

Ankur Rudra: Just a question on the performance and the guidance. The organic and constant currency growth appears to have slowed down a bit over the course of FY'18 especially in the last two quarters. Your guidance does not appear to bake in any kind of acceleration in organic growth, you said 4.25 to 6.25. Is there a reason for caution even though your client relevance appears to be improving and the success of your Mode-2 and Mode-3 strategy that you have been highlighting, if you can elaborate on that? Also, specifically, if you can highlight what is the drag from India baked in for FY'19 what it was in FY'18 as well?

Anil Chanana: India has been I would say about a percent in financial year '18, but it will further come down because of the fact that we have not participated in the SI deal, I see this almost significantly somewhere sort of reducing there, so that is 1 percent.

C. Vijayakumar: From overall organic growth perspective, while we continue to remain very positive about the traction in our Mode-2 and Mode-3 services, as well as the traction in winning new logos in traditional services, we also have a large book of business and there are renewals pipeline which is there. So basically the level of compression in the existing book of business is driven by the volume of renewal. I think if we just factor that kind of little bit account for some improvement, we have factored very similar levels of organic growth accounting for some of the pressure in the renewals based on the volume of renewals that was expected or even the renewals that happened in the last quarter. So, all of that overall provides an outlook as Anil highlighted around 5.5% organic growth in FY'19.

Ankur Rudra: If you look at the next two, three years, CVK, is it fair to assume that level of compression will stay in your business or will that slow down or accelerate in terms of the headwind you face from these renewals?

C. Vijayakumar: Ankur, we have not very precisely estimated the impact in FY'20 & '21, but just looking at by common sense overall the book of business and it goes up to that extent the pressure on renewals will be there because with every renewal there is more expectation on productivity, more expectations on automation as to amount of cloud migration, not just in infra business but also in the software business, some applications moving to SaaS. All of that makes the renewal a little smaller including new deals a little smaller. So I would say there will be a slight increase in this as we move forward, but I do not have a very precise estimation of this, this is just a thumb rule answer that I give.

Moderator: Thank you. We will take the next question from the line of Divya Nagarajan from UBS. Please go ahead.

Divya Nagarajan: My question is to CVK, how do you think about longer-term organic growth momentum for the company – do you expect the renewals start to ease you should be able to get a high single digit or possibly even early double digit kind of growth rate here. If yes, which segments in particular will drive that growth or do you think that is now not the case anymore, you continue to reliance on M&A, how are you thinking about it in three years, five years?

C. Vijayakumar: First is we have done very careful estimation of what is expected to happen in FY'19. I would not have done a forecast of FY'20 and '21 and even longer-term, but I think the true growth will accelerate only when next generation services are really going to be the growth drivers. In the traditional business, we will continue to gain new logos but the deal sizes are becoming smaller. So I think the growth momentum in existing services I do not see it accelerate in the near-term, maybe marginal increase or decrease but the incremental growth will come from next generation services.

Moderator: Thank you. We will take the next question from the line of Ashwin Mehta from Nomura. Please go ahead.

Ashwin Mehta: CVK, just wanted to check in terms of we had earlier indicated that IMS would improve from 1H. Do we still stand by that expectation? Secondly, what exactly is driving the deceleration in terms of app services because our legacy exposure in app services should have ideally been lower compared to our peers?

C. Vijayakumar: The first is on the infrastructure services, I had highlighted that in H1 we will see pick up in the growth, I think we maintain the same commentary depending on the deals that is closed in the second half of FY'18, I do believe in FY'19 it will accelerate. But overall, India is going to create a little bit of dampening effect to the infra business probably in FY'19 to some extent but after that it will not be the case. So I will not be able to provide a very precise how much the infra business will grow in FY'19 but it will definitely be better than FY'18 because we are seeing all the trends in line with growth momentum. Barring the fact that the deal sizes are becoming smaller, so that is going to kind of overall reduce the growth rates, but it will definitely be better than what we had in FY'18. From an application business perspective, I think there are two, three elements as I said, the traditional application support, the component of that is fairly small which is fairly similar kind of dynamics like infrastructure business more around automation and more around some applications moving to Cloud. Our enterprise package, while we saw some growth and we continue to see some growth on the cloud implementations, but traditional large implementations are not happening. So I think some growth in next generation services is getting offset by some of the compression and large SAP type of transformational programs not having at the same level as it was in the earlier years.

Ashwin Mehta: Anil, the licensed IPR gross carrying value seems to have gone down by around 20-odd million. Wanted to check what is the reason for that?

Anil Chanana: Could be exchange, that is what I can think of, I do not have the exact numbers in front of me, but we can certainly talk of like, but exchange will always be happening.

Moderator: Thank you. We will take the next question from the line of Ashish Chopra from Motilal Oswal. Please go ahead.

Ashish Chopra: CVK, just wanted to understand from you, I think some of the examples that you cited in the Mode-2 services in Cloud Native, referring to the three deals it was mentioned there, so could you just throw some light on were these existing IMS customers which are now into the Cloud Native services or are you kind of winning new customers as far as the IMS Cloud business is concerned? The second question is just in terms of the deal sizes, how the dynamics change, not to know about the sizes of these deals but just to get a clearer understanding of an incumbent account goes into Cloud Native services, what is the kind of compression or addition that you are able to get when you are actually offering migration to workloads to the Cloud?

C. Vijayakumar: Let me take the Cloud Native services question. I think we announced three deals on Cloud Native services; one was professional services based in Europe, that this was an existing client where we provided data centre services. So here we are migrating the large part of the data centre maybe 60% of the data centre to cloud and for that component it was approximately half in terms of the existing revenues to the new expected revenues. The next one was Europe-based pharmaceutical company. This was an existing client but a small part of the state is moving at a large pharmaceutical company. I think the impact on this migration would not be much, it is probably less than 15% of their estate which we expect to migrate to Cloud. Next one is a US-based company. I do not have the exact details on this. I think this is a new client where migrated to Cloud migration.

Ashish Chopra: On IMS, I think last year in the first quarter you had mentioned the impact of productivity benefit can you gave in a large deal like Volvo. Should we kind of bake that in our 1Q expectation from IMS or does that no longer have a material impact?

C. Vijayakumar: Like in April we have the same impact because last year in JFM quarter we had YoY reduction as a part of the overall program, that is definitely there in this year as well, maybe the quantum is not the same as last year, it is little lower but it is there.

Moderator: Thank you. We will take the next question from the line of Ravi Menon from Elara Securities. Please go ahead.

Ravi Menon: First question is to CVK, the Volvo deal we were expecting to see better traction from the higher win rates over there but this year's growth seems to be slightly lower than what we had anticipated. So anything subject to probably some of the deal compression that we are seeing in Europe in renewals?

C. Vijayakumar: I think from Europe perspective, in the second half of FY'18 we definitely saw the win momentum significantly increasing. The number of deals that we have won in Europe in the second half of FY'18 is significantly higher, it is among the highest, but the deal values are significantly smaller. So I think that is primarily because some of the clients by nature are smaller clients and also the new deals are coming in with the assumption of 30% or 40% public cloud component as a part of the overall outsourcing deal, I think that is what is showing some weakness. But I expect FY'19 Europe to be better from an infrastructure perspective certainly than what it was in FY'18.

Ravi Menon: Secondly, you did talk about last quarter about some synergy revenues starting to come through into services side from the IP deals. I assume that should come in the Application Services. So should we expect to see slightly better growth in Application Services in FY'19?

C. Vijayakumar: I think Darren highlight few wins that has happened; however, the revenue impact of that maybe marginal. Darren, do you want to highlight some of the services deals that we won in alignment with the overall IP partnership?

Darren Oberst: I think that is exactly right, we are certainly seeing good volume, customer uptick on the product related services, but in terms of the aggregate revenue impact, it is still relatively small, then you would see both standalone deals at times going in and working with the customers around implementation, upgrade, training, integration, in some cases some small managed services, the customers working for hosted solutions in some form of premium, support of customer development work. So you will see some of those as standalone deals. We also are beginning to see customers that are traditional application services or ASM customers of ours expanding and finding additional growth opportunities to start bringing product related professional services into those much larger ASM programs. So it certainly falls into those categories, but at least as of today the aggregate revenue impact is still relatively small.

Ravi Menon: I can understand the aggregate revenue impact and the deal sizes are fairly small for some of the deals that you have taken up, some of the software you have taken up from software vendors, system integrators, but for the vertical specific software, should not the deal sizes be much larger from the services component I mean?

Darren Oberst: I think in general that is true, with vertical applications and what business range of applications the deal sizes will be larger, also on infrastructure oriented tools, the deal sizes you will see more out of that but the relative size will be a much smaller.

Moderator: Thank you. We will take the next question from the line of Sandeep Shah from CGS CIMB. Please go ahead.

Sandeep Shah: CVK, I think post the Q3 result in many of the interview comments as well as earlier comments you said that the FY'19 growth would be better than FY'18, but if we look at your guidance it has actually been lower at the lower end versus what you grew in FY'2018. So what has changed post your last comment and giving the guidance despite you had two new acquisitions been announced post your Q3 results?

C. Vijayakumar: In terms of new deal wins and the momentum that we are seeing and the optimism, I continue to remain optimistic, but when you really factor in the existing book of business and the impact of renewals, this is where we believe we will land, so that was the real basis of guidance. But as we progress, we will continue to keep you updated on how we are doing on this.

Sandeep Shah: Anil, can you just once again clarify the guidance portion which you actually given in the initial remarks and your presentation?

Anil Chanana: We were talking about the revenue guidance here; revenue guidance in constant currency terms is 9.5% to 11.5%, I am picking up the middle of the range which is 10.5%. The two acquisitions we have announced which is the C3i which is already consummated and Actian which we are hoping will conclude by this year. So we will have seven months of revenue growing from Actian and then their acquisitions which were completed in the course of the year for which the full year benefit will flow in this financial year. So all put together and the impact of India SI decline is 4% sort of inorganic. So if I take 10.5% being the middle of the range, I am just cutting it exactly half, 5.25% is organic and 5.25% is inorganic, 4% is already in a way done assuming Actian closing in August. So we will need further inorganic revenue of 1.25% and the rest which is 5.25% will be the organic growth. Since I picked up the middle of the range, this will be 4.25% to 6.25%, I am just making it more mathematical sort of equation, of course, there will be rounding up here and there, but this is why it looks like.

C. Vijayakumar: Add to it, there are many assumptions which has gone into arriving at this guidance. So I think at this point you should take this as an overall kind of estimation from a thumb rule perspective, still there was a lot of emphasis on organic, inorganic in some of the questions that we receive.

Sandeep Shah: Just a follow up in terms of the IP investments. This quarter there has not been any partnership announced. So how should we read in terms of the intent, are we done in terms of the portfolio where we wanted to have so those kind of an IP, are we done with that or are we looking for more such kind of an investment? Second follow up, CVK if we just look at the growth of the standalone IPs, it would be mid single digit. So at a board level or at a company level how you actually quantify the synergy benefits on ongoing basis, whether these investments are moving in a right direction or not, because just for 2%, 3% or 4% kind of a growth such a price to sales multiple of 3, 3.5x looks really expensive even with the IRR of 15, 16% when actually alternative investment in the digital companies, the growth could be upwards of 15, 20%?

C. Vijayakumar: We continue to look for growth inorganic opportunities in Mode-2 and Mode-3. It just so happened that last year it was almost skewed towards Mode-3; however, we remain very optimistic about some of the possibilities in Mode-2 during this year. In terms of overall business case, there are different products drive different types of dynamics and we have made those assumptions and we finished six quarters in some of them five and we are tracking to the business case but the best way to really look at or review an investment will be at least after a year completion. So for the first two investments where we have made, one, we are very close to the business case and another one we are much better than the business case. The first question that you asked was, "Are you done with the IP investments?" The answer is no, as Darren explained this is really a long-term transformational initiative that we have both organic and inorganic IP as per the acquisitions. So we continue to look for right areas where we can invest in acquisitions as well as IP partnerships. So as and when we succeed, we will keep you updated.

Moderator: Thank you. We will take the next question from the line of Anik Mitra from Stewart & Mackertich. Please go ahead.

Anik Mitra: Can you throw some light on your business in ER&D space in terms of your geography wise presence as well as your outlook on ER&D space, and what are the verticals you are serving in ER&D space?

C. Vijayakumar: GH Rao who is on our call who heads our Engineering and R&D Services. GH, would you want to answer that?

GH Rao: To answer the first part of your question, today, we are mostly tilted towards North America in terms of geography presence; however, we do see good traction in Europe and we have very strong presence in Japan, so these are the three geographies in which yearly services are present. Secondly, from verticals perspective, I think we have very broad-based exposure right from telecom to online to aerospace, medical devices, we are pretty much there with very good critical mass and distribution of our revenues are very decent across all industries in ER&D space.

Anik Mitra: In terms of recent H1 visa policy, do you think that it might impact your revenue growth or business going forward?

GH Rao: We do not see any significant impact of H1 visa policy here, we have been already having more locals as a part of our workforce as part of the overall HCL's policy.

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

C. Vijayakumar: Overall, we have had a good year and I think we are very happy with the way we have executed and the direction in which our business is moving, all the right metrics in terms of what we want to achieve we are progressing. Organic and inorganic both remains core part of our overall growth strategy; however, we are very committed to continue to maintain the return on capital employed as well as our margin profile. So, with that I continue to remain positive on what we can deliver in FY'19 in line with the guidance that we have provided. So look forward to interacting with you through the year and thank you very much for joining the call today.

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