23rd Jan, 2003 – 5:45PM IST

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

Girish Pai; Good morning, good afternoon, good evening to participants joining from the US, Europe, India, and Asia. I am Girish Pai, on behalf of SSKI Securities welcome the participants to HCL Technologies' second quarter FY-03 results conference call. I would now hand over to the HCL Technologies' senior management team for the preliminary presentation. Over to you Sir.

Shiv Nadar: Thank you. Good afternoon. Thank you for joining us on this conference call to discuss our financial performance for the second quarter of fiscal 03. Joining me in this call are Mr. Arun Duggal, Chief Financial Officer, Mr. S. L. Narayanan, Corporate Vice President - Finance, Mr. Raj Sirohi, CEO of HCL Technologies – America, and Mr. Sujith Baksi, CEO of our BPO services who will provide an overview of our BPO operation. The scheme of the presentation will be as follows: I will begin with the key highlights of this quarter and then Arun will spell out the finer details. Thereafter Raj Sirohi will brief you on the happenings in the US, still the largest market for all of us in the industry, Sujit afterwards will conclude the session with updates on our BPO business. Let me begin now.

In the past couple of quarters we were able to firmly establish clear trend lines at some of our recently acquired entities. I am pleased to report that these trend lines have been further extended during this quarter, most noticeably at DSL Software, which has managed to beat it's previous quarter sequential revenue growth rate and that too with a higher gross margin. DSL continues it's pursuit of widening it's range of offerings as also it's geographical foot print with in the DB organization.

Secondly, our BPO business consisting of HCL eServe and HCL Technologies, Northern Ireland, has recorded smart turnarounds in this quarter. As I had mentioned to some of you in the recent meetings, we are at least a couple of years behind with other competitors in this space. I therefore expect the BPO business will necessarily have to go through it's preoperative phase before it enters a different orbit when it starts turning free cash flows positive. Allow me to assure all stake holders that this business of ours is well on its way to the financially viable levels.

At HCL we have always been decisive in our strategic intent to build scale and capabilities and our approach towards the BPO will be no different. We are on the paths of putting together a holistic frame work, something that will bring together the right people, a state of art delivery apparatus, and highly focussed sales organization for a preferred client access to take out a dominant position in a rapidly growing space.

During this quarter we had to encounter certain developments as regards our joint venture with Perot systems and quite naturally many of you had some apprehensions about the prospects of this JV. I am pleased to state that all the issues have been resolved with a renewed commitment to preserve and grow a very valuable franchisee that has been created in the past two years by the HPS family. Indeed, it is a matter of satisfaction that the latest quarter ended December 31, 2002, it has seen a sequential revenue growth of 9.5% at HPS to $24.93 million, which translates to a run rate of about $100 million per annum. As compared to the revenues in January 2002, the last months' billing have risen by 45%, which also points to strong undertone in the recovery stage in the second half of the year. We have considered several extra-ordinary one time charges in the latest quarter, which may cause some concern, but I can say with some assurance that the underlying business at HPS is on very well founded and sound fundamentals. I would conclude with an important message, it is with regards to the inevitable lead times involved in going through an integration phase while acquiring new companies. This is caused from our side, which in terms of people and revenues is much larger, and hence it takes some time before the new entities adapt to our process step and breach the cultural differences. It is not apparent whether it takes at least a couple of quarters if not more before newly constituted entities get successfully integrated into the operational fabric of the extended HCL Technologies organization. This has aptly grown out by the lead time that we saw at DSL, before we started accelerating the revenues. This time span becomes much larger to between 6 to 8 quarters when we are dealing with totally green field ventures like BPO services or globalising infrastructure services. In BPO we are through a 5 out of the 8 quarters which all companies in this space have taken before turning profitable, we have got 3 more left.

As regards to our infrastructure services under HCL Comnet, we are in the process of expanding to include a global delivery capability. Here we plan it would take 6 quarters and so far we have completed 3 out of those. Once it has reached the high yield orbit is where these businesses will be like the rest of the software services business. During these turbulent phases, however, I anticipate that our income levels should be stable as in this quarter or would start improving. I would like to assure our stake holders that your company is not new to such challenges nor it's management is new to facing similar changes in the industry. We will spare no effort to apply mid-course corrections, if at all required, to steer the coast towards sustainable, long term share holder value. Thank you. Now I will hand you over to Arun Duggal, our Chief Financial Officer. Thank you.

Arun Duggal: Thank you Shiv. Good afternoon. I would like now to run you through our key financial and operational matrix for the second quarter of financial year 2003.

Our gross revenues increased by 17% year-on-year and 6% quarter-on-quarter to reach Rs. 4.7 billion. Our net income for the quarter at Rs. 806 million is up 6% sequentially but down 35% year-on-year.

Our software services business grew 3% quarter-on-quarter with a 1.5% growth in the core software services business. During the quarter we have added 545 people in our core software business. DSL Software, as Shiv mentioned a few minutes ago, has once again come up with the stellar performance this quarter, with a 23% growth in revenues and 63% growth in net income. DSL's current annualized revenue rate is $35 million, which is almost double of that it was in September 01, when we acquired the company. They have also upped their head count by 11%.

This quarter has also seen an excellent performance by our BPO business. Though on a small base, HCL E-Serve revenues have grown 93% quarter-on-quarter and its financial matrix has improved significantly.

HCLT, Northern Ireland, has shown a 28% quarter-on-quarter growth and it has become profitable at the EAT level. BPO revenues for the quarter are up 33% sequentially in total.

Our infrastructure management entity, HCL Comnet, after facing a downturn for a couple of quarters has registered an impressive growth of 25% of an quarter-on-quarter basis, and the net income margins have also improved significantly, which is now at 10% as compared to 3% for the previous quarter.

The profitability of our nonorganic business has improved significantly with their EAT growing by 70% and contributing 16% to our total earnings after tax. This definitely reconfirms the validity of our nonorganic group strategy. As we had expected once the initial integration issues are sorted out these entities can and will deliver profitable growth for us.

In the quarter there has been a 0.9% decrease in our blended bill rates, which just reflects the market condition. We have been able to keep our SGA cost fairly stable. In our last conference call we had mentioned steps that we would be taking to reduce our accounts receivable and improve our DSO. Those efforts have yielded encouraging results for the marked improvement in our collection cycle. Our DSO now stands at 67 days vis-à-vis 82 days in the previous quarter.

Our client addition remains strong. We have added 21 new clients in this quarter. On the recruitment front also we have continued to increase our manpower strength. On a consolidated basis for the company, we have added around 988 people, which takes the total manpower strength to 7788 up from 7156 last quarter.

I will now hand you over to Raj Sirohi who will share with you the latest developments in the US market and give you a feel for our business there.

Raj Sirohi: Thank you Arun. Good afternoon everyone. I would like to share with you the market trends from our US operations perspective and also some of the new customers acquisitions in the last quarter.

The markets in the US have been mixed. There have been some promising trends in the last quarter and also some signs of slow growth. Recovery of the IT segment has been slower than anticipated. A number of companies have been able to trim down their expenses through the standard practices like closing down offices, closing down unprofitable lines of operation, and laying off full time employees, but they still have a long way to go in the cost rationalization initiative in order to be in line with the reduced revenues. The good news is that there are signs of technology companies increasing their R&D budgets to be ready to jump-start their profits and add momentum to growth when their economy reverses. Based on the sales funnel analysis of HCL Technologies America, semiconductor companies seem to be leading this trend. Spending in the technology sector is likely to be in predictive technologies giving offshore companies an advantage. Strategic outsourcing with offshore providers coupled with increase in budgets in the pockets of technology is good news for HCL.

The process of the IT outsourcing is becoming more mature with every opportunity. Organizations are looking at outsourcing as a way to transfer their assets, forward a capital expenditure, and reduce their costs. Enterprises are shifting their spending from capital budgets to operating budgets. Budgets are on the table for both IT and engineering to spend, but there is caution in the air to ensure that they get more 'bang for the buck'. Just like last quarter extreme due diligence on vendors and elaborated negotiations in the form of every deal, customers expecting contract structures that ensure delivery of the intended business outcome rather than IT solutions or SLA. With the size of outsourcing deals increasing customers are moving towards one stop shop which can offer IT, infrastructure, BPO call center services, rather than dealing with multiple vendors. India still remains a favorable destination, but India is not the only game in the town. We are seeing RFPs where countries like Philippines for call center work and China and Russia for technology work are on the buyer's evaluation list.

The growth areas for HCL America; we have witnessed growth in revenue in the quarter ending December 2002. We acquired 12 new customers in this quarter, and I would like to share with you some of the new engagements of this quarter. For a world leader in information storage system we have been chosen for product engineering and sustenance in the enterprise storage management products. For a leading provider of content management solution, we have started a new engagement for redevelopment, sustenance, and testing of selected range of products.

Moving up the value chain for a new customer we did bench marking and GAP analysis with industry standards for a leading outsourcing infrastructure company and this was a good acquisition for HCL Technologies in this quarter. We have also acquired several new projects from a world leader in document management software, which includes development of program interfaces, connectors, and maintenance of image management product. A key new engagement in this quarter is with the premier electronic contract manufacturer for design services, which includes board design, ASIC design, and related engineering work. In the area of medical electronics we acquired two new customers engaged in surgical equipment and accessories. To both these customers we are offering embedded software. We also experienced good success in our package implementation practice in this quarter. We acquired new projects in the area of data warehousing, data mapping, implementation, and consulting on Oracle, PeopleSoft, and Sieble, both in existing customer base and also with two new customers. We also have commenced a large application management outsourcing project with a significant insurance group.

What are some of the opportunities and challenges that we are facing? The pressure on price levels continues to exist and we are mitigating this presence and its pressure by moving up the value chain and offering more complete solution rather than project and project execution.

Our sales pipeline looks very strong and the leading integrators are positive compared to two or three quarters back and we are experiencing more project starts now than a couple of quarters back.

We have been successful in leveraging the existing alliances and partnerships and acquiring new customers and revenue stream. This will remain a key component in our strategy for growth in the future quarters. In conclusion, we believe that there are definite positive signs from the technology companies towards R&D spending and we are positive on growth both in the short and the long term for the offshore services. Thank you. Over to you Arun.

Arun Duggal: Thank you Raj. Sujit if you could commence with your presentation please.

Sujit: Thanks Arun. This is Sujit here, I look after the BPO operations for HCL. This quarter has been a satisfactory performance on the BPO front for us. Both our Belfast and Noida operations have seen sizable sequential revenue growth and a consequent improvement in profitability. We recall that we were losing money in the first full quarter of our Belfast operation, which is HCL Technologies, Northern Ireland. In the subsequent quarter we moved to cash break-even and in the last quarter OND we are PAT positive. HCL E Serve is also poised for a rapid ramp up in numbers and all this has been possible because of some good client wins we have had during the quarter. We are looking at additional capacity creation in the current quarter. Some important projects that we have bagged during the quarter which we will be executing out of our facility at Noida include for a Fortune 50 retail chain in the US we are doing customer feedback analysis back here in India, this is in transaction processing area; we have won against a global bid collection processing for a large US receivable management major; we have won from a US network security solutions company a web based help desk work; we have won an inbound help desk work for a global education and testing company based in the US; we have won back technical support for a financial product company which is seasonal; we had lost one order last year to a local competition in India and the client has come back to us again this quarter for antivirus product because we lost it on price issue but got it back on quality issue; all these orders that I described right now are orders with potential to ramp up to more than 100 seats each.

Our Belfast center is operating very smoothly and we are currently working with five different groups within British Telecom out of Belfast. We have also started work in Belfast with non-BT customers and we currently have processes for four such clients, out of them two of them we are providing language support in 8 different languages after the center. Needless to say BT has been a very satisfied customer and we have started work at Noida for them on processes, which have migrated out of Belfast.

The market for BPO services in India looks quite promising with large global corporations exploring options to move their back office operations into India. Even though the market remains competitive, larger players like us are invariably going to get a major share of the market. We are undertaking major quality initiatives like Purdue Benchmarking and COPC Certifications. This, along with specific process initiatives, is helping us deliver better services to clients and also control costs. We are enhancing domain specialization in our chosen verticals to act as a differentiator in our service offerings. Finally I would like to say that our pipeline looks very healthy than it was ever before, and that should translate into good times for our BPO operations going forward. Thank you and I will now hand this over to the moderator for the question and answer.

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

Azeeza: Thank you Prathibha. We will now begin a Q&A session for participants connected to SingTel bridge. Please press *0 to ask a question. Thank you.

Our first question comes from Mr. Mandeep Sachadeva from Citi Group, Singapore. Over to you Mr. Mandeep.

Mandeep: Thank you. Hi Sir, I just wanted to ask in your core software services business you showed a 2% quarter-on-quarter growth and you are still continuing your client rationalization program. How long do you foresee this process continuing.

Arun Duggal: As we mentioned last time, we are expecting to conclude this by the end of the current quarter.

Mandeep: Okay thank you sir. There is one more question, there is a decline in the gross margins by about 250 basis points, what would you attribute that to?

S.L. Narayanan: This is in line with the general trends that we have witnessed in the industry, and in our case we did not have much of a bench earlier on, during the last two quarters we have added a lot of people and so if you actually look through the release our utilization has dropped by a couple of percentage points. So, this is basically on account of building a bench because today we are able to see a much more predictable funnel and we need to build in capability and capacity in order to execute down the line after two quarters. Plus, also there is the effect of pricing drop during the quarter.

Shiv Nadar: Can I add one more point. It is very peculiar for this quarter, 70% of our business comes from US and this quarter saw two extended shut downs, one is during the Thanksgiving time and another is during the Christmas time, and during both these periods we have to carry our staff cost, where as there would have been a reduction in revenue. A combination of these three factors is what would have cost us this margin drop.

Mandeep: Okay thank you sir.

Azeeza: Once again for participants connected to SingTel bridge if you have any questions please press *0. At this moment there are no further question from participants at SingTel. I would like to hand over the proceedings back to Prathibha. Over to you Prathibha.

Moderator: Thank you Azeeza. We will now begin the Q&A interactive session for India participants. Participants who wish to ask questions please press *1 on your touchtone enabled telephone keypad. On pressing *1 participants will get a chance to present their questions on a first in line basis. Participants are requested to restrict it to two questions in the initial round of Q&A session. To ask a question please press *1 now.

Our first question comes from Mr. Anantha Narayan of Morgan Stanley.

Anantha Narayan: Thank you and good afternoon to all of you. My first question was on HCL Perrot, it is exceedingly gratifying to know that the issues have been resolved, but can we have a run down on what exact issues were and what are the changes that have been implemented to resolve these?

Arun Duggal: HCL Perot as you know is a joint venture that we have with Perot Systems for over five years, and in the recent past there were some differences in opinion relating to the structure of the management process. One of the requirement that Perot had was that the organization has grown in its size and its business has become of such a nature that the management team which is managing this business should not have any overlapping responsibilities with HCL's business. Though the senior management team members were deputed from HCL originally hence they were carrying on some minor responsibilities with HCL. So, after some discussion and negotiation, we have agreed to have the CEO of the company Mr. Vineet Nayyar, who has really led the building of this excellent enterprise to focus solely on the business of HPS and relinquish his responsibilities in HCL including his own position on the board of HCL Technologies. In addition, there were some issues relating to the processes of governance within the joint venture and on those we have reached an agreement with Perot System as to how we are going to jointly manage and grow this business, and I am very pleased to report that since we had that little bit of a rough spot in our relationship, the relationship has improved very significantly and there is a renewed vigor to continue to grow this enterprise, which is evident in the results of the last quarter.

Anantha Narayan: Thanks Arun. Secondly, you had mentioned last quarter that the higher effective tax rate in September was on account of larger contribution from DSL Software plus some of the exemptions running down as far as 10-A and 10-B were concerned. Now, the DSL contribution has increased further this quarter, yet the effective tax rate is down quite a bit, so what is the reason for that?

S.L. Narayanan: Actually Anantha they had a redemption of part of their mutual fund portfolio and since they had some carried forward looses, so in effect did not pay tax on that part of the other income, which is why you see a reduction in the effective tax rate. And the second one is in line with their growth. They have taken some newer facilities in Bangalore and since they have got the STP certification so projects delivered out of those facilities qualify under section 10-A. So because of a mix in the incomes from the older facility and the newly certified facility the effective tax rate has dropped.

Anantha Narayan: Right. Just the final question, again during the conference call last quarter you had indicated that the ESOP Trust had acquired about 5 million shares at an average price of 160 to 170. Has there been any further purchases in the December quarter?

S.L. Narayanan: I do not think so, nothing. Zero purchase.

Arun Duggal: In fact, there has been some issue of shares out of the ESOP Trust for the employees.

Anantha Narayan: Right and how much is the company loaned in total to the trust so far?

S.L. Narayanan: About Rs. 76 crores.

Anantha Narayan: So, which is basically all being used at acquiring, there is nothing left with the trust at this point of time?

S.L. Narayanan: No, the trust in fact, whenever the trust transfers shares against exercise of options whatever money they realize gets returned to the company.

Anantha Narayan: Okay. Thanks a lot and wish you all the best for the future.

S.L. Narayanan: Thank you very much.

Moderator: Thank you very much Sir. Next in line we have Mr. Manoj from JP Morgan.

Manoj: Good evening Sir. This is Manoj from JP Morgan. My first question relates to a core software business. We saw 2% quarter-on-quarter growth this quarter. I was just wondering as to what is the outlook on the business because some of our peers have shown a much stronger quarter-on-quarter growth with respect to ramp up from existing and new clients. How is the outlook looking?

Shiv Nadar: As Raj mentioned who is the CEO of HCL America and from the rest of the world outlooks looks quite positive, you know, the finance looks pretty good and the orders booked in this period again look pretty good.

Manoj: Okay. So, would we have any impact of this client rationalization process again last quarter or was that the reason why growth this quarter was only 2%, would have been higher if the client rationalization would not …..?

Shiv Nadar: Precisely. I mean it is precisely because of the rationalization process and the disengagement of some of the clients that the growth sequentially is about 2%, otherwise it would have been much higher. There is also one more reason I must point out. During the quarter there is definite reduction of working hours because of extended layoffs during the Thanksgiving and Christmas holidays. They were applicable largely to technology companies. Therefore, their impact on our company, which still derives about half the revenue from the technology services business, impact on us would be larger. It is the combination of these two factors. Second factor was peculiar for the last quarter, I mean, there is no such thing which will repeat itself in the current quarter or the next quarter.

Manoj: Sure. My last question just relates to a pure onsite component of the business. How much of this business are we doing for customers where the work is purely onsite without any offshore component?

S.L. Narayanan: Very little.

Manoj: If you were to put a number on that roughly how much would that be?

Shiv Nadar: Can we send that number to you.

Shiv Nadar: We can come back to you on that Manoj.

Manoj: Sure. Thanks a lot Sir.

Moderator: Thank very much Sir. Next we have Mr. Trideep Bhattacharya from UBS Warburg.

Trideep: Hi, very good evening. You talked about clients rationalization. How many clients actually did we rationalize in this particular quarter?

S.L. Narayanan: Fourteen.

Trideep: The last quarter if I remember correctly the number was 33?

S.L. Narayanan: Yeah.

Trideep: Okay. The second is on the pricing. Now as we start this new calendar year, how does the pricing vis-à-vis last year look like to you in terms of, like you know, because our existing customers are asking for fresh cuts in pricing in the core business and also in the BPO space how do you see the pricing pressure? I mean in ITES area?

Shiv Nadar: Raj can you answer this question?

Raj Sirohi: Sure. There is pressure on the pricing both in the technology area and in the BPO area, and the two reasons for it. The first reason is that most of the deals vis-a-vis before the previous time, the most of the deals are in terms of large quantities in terms of revenues and people wise, and also they are for extended period of time. We are looking for multiple year deals now, that is what the customer looking for, and hence there is a push towards pricing pressure to come out from there. Number two reason is because of the budgets that are already at a very lower level for the company both in the technology companies and in the IT segment, they have less money and they want more work to be done, and as per understanding as in US consulting companies also there is a pressure on pricing, and that pressure on pricing is continuing with the offshore companies also. So, these are the two reasons why we have seen a pressure on the pricing.

Trideep: If I may just persist a bit, when you are talking about pricing and at the same the contract size is increasing, I am sure, since you interact with the customers, the net impact on the gross margins of the projects that you do in such places. Is that gross margin that you are encountering now is lower than as compared to last year or do you think that the larger volumes is kind of offsetting the impact of pricing?

Shiv Nadar: This question I can answer for you. See wherever multiple year contracts are done, typically in the subsequent years, the OPEX corresponding to its revenue will not exist, because the OPEX will not be required in multiple year deals. So there is an advantage going forward, that is one. And two, when there are pricing pressures which exist now, this is totally a personal view not really a corporate view, we believe that the pricing pressures that are existing now during the second half of 2003 will start releasing because the clients are wanting to do business more and more with larger companies and the larger companies have very high increase in people pressure. Given these two, my estimation is six months from today this pressure would start easing. This is the view that we carry. On the BPO business, Sujit can you respond to this query please?

Sujit: I am not very clear. Can you repeat the question once again?

Shiv Nadar: Are the pricing pressures, I mean, compared to the last 12 months in the last quarter of 2002, did you see any increased price pressure compared to the first three quarters?

Sujit: Compared to the first three quarters, there are a lot of small players who are bidding at very low prices, made it very competitive. In the last quarter we have seen that in the major bids that we are there or we are participating or the deal has happened, the smaller players are not there at all. It is large players, and I think price as far as I am concerned what I see the price point will definitely go up because larger players are participating and the small players are not there in these deals.

Trideep: I see. My last question has got to do with the margins. Now, we have seen the gross margins or EBIDTA margins kind of coming down on a sequential basis for quite sometime. Now, as a client rationalization process is gradually coming to an end, when do you see the margins actually looking up purely because on a company specific basis, I know there could be pricing pressure etc. But purely on your client rationalization and returning back to normalcy kind of…

Shiv Nadar: Between client rationalization and the pricing pressure, which has been described, I believe we would start seeing some stabilization.

Trideep: Okay. I mean from the next quarter onwards. Is that a fair assumption?

Shiv Nadar: Yes.

Trideep: Okay. Thanks a lot.

Moderator: Thank you very much Sir. Participants are requested to restrict to two questions in the initial round of Q&A session. Our next question comes from Mr. Dipen Shah of Dolat Capital.

Dipen: Thank you. My questions were related to the software services business and they have been already been answered. Thank you.

Moderator: Thank you very much Sir. Next we have Mr. Apoorva from Karvy Stock Broking.

Apoorva: Hello. My question is regarding the breakup that you have given for software services and government practice. Could we have comparable numbers for Q4 of FY02, top line and bottom line numbers?

Shiv Nadar: 02, we did not have the government practice, but software services, may be S. L. you can respond to that.

S. L. Narayanan: Which one do you want? Do you want government practice or also software services?

Apoorva: Basically, it is the software services segment that has been broken up into software services and government practice from this quarter onwards. Is that correct?

S. L. Narayanan: Yes.

Apoorva: I just want comparable number for Q4 of FY02 for either one, let us say software services or government practice.

S. L. Narayanan: See we will have the number for the software services. I do not have it ready right here because we were prepared for a sequential analysis, but as regards the government practice since the transaction itself was closed from time towards the end of Q4 of last year, we would not have a comparable number.

Apoorva: Okay. That's it. Thanks.

Moderator: Thank you very much Sir. Next in line we have Mr. Pramod Gupta from Inam Securities.

Pramod: Thank you for giving me a chance. A couple of things I wanted to know. Is the company still likely to go for more acquisitions and if so what are the likely areas where company is likely to acquire companies?

Shiv Nadar: See we have already outlined the areas in which we would be having acquisition plan. Let me be specific about this, in the BPO space, we do not plan to acquire anything now. What we are intending is only organic growth. What we needed to acquire, what alliances we needed to have, we already have. Now, we would be expanding marketing alliances there, but they all will be alliances. There would be no acquisitions. In the infrastructure services again, which is new, there is no likelihood of any acquisitions in the near future. In the software services, we have done one which is to buyout the entire HCL Infosystems space of business, and the global business, which would take place during the next six months, but that is an announced deal and it is not new. We have also made some strategic investments with some very small companies like Aallayance where for capability expansion we have done certain strategic investments. Because of the reason immediately we are not seeing any acquisitions, which are new, outside the software space, but in the products space over the period of 2003, there would be some.

Pramod: Thank you very much.

Moderator: Thank you very much Sir. Next we have a question from Mr. Chetan Shah of Quantum Securities.

Chetan: Hello gentlemen. In the first few presentations Mr. Raj as well as Sujit had talked about the pipeline. Can you quantify the pipeline in both of the businesses?

S.L. Narayanan: That would be a very forward-looking statement Chetan, I mean, we cannot say anything more than this that would be a problem.

Chetan: Okay, and regarding these Tech companies R&D spending where you are seeing some semiconductor companies leading the trend. I just wanted to understand how many semiconductor related companies are your customers and whether there could be any threat from some specialist countries like Taiwan or some advanced companies?

Shiv Nadar: Raj. Could you please answer this question?

Raj: Sure. When we talk about semiconductor segment, we are talking about two. One is the companies who have the infrastructure equipment of the semiconductor industry. Where we have, if we look at the total large number of semiconductor equipment companies are about 20, we are working with about 11 of them as of now and we are looking forward in terms not expanding into with new acquisition in that area, but looking at growing our business on existing customer base as far as infrastructure companies are concerned. When you look at the semiconductor industry per se which is just after the equipment manufactures, we have two very significant engagements already in place and we working on RFPs which are already in hand and we are the short-listed vendors of some of the RFPs with two new engagements in the semiconductor organizations.

Chetan: Yeah, and the second part actually since certain other countries may be, they are manufacturing most of the equipments also and part of ….., whether competition can be seen from those kind of countries?

Raj: No actually the other countries are more in the manufacturing of chips and Ics, they are more in the fab area. We are looking at our work is more with the semiconductor companies either in the IT way or from a technology point of view which is developing or they develop the software or the hardware products. So we are not likely to be in competition with companies in Taiwan or other ones who are more in the manufacturing side.

Chetan: Okay. Thank you Sir.

Moderator: Thank you very much Sir. Our next question come from Mr. Sanjay Kumar of Prabhudas Liladhar.

Sanjay: My first question deals with client rationalization. Now, if you look at your core software business it has grown by 1.5% and the growth is quite muted compared to the peers. Now, this client rationalization has been continuing for sometime and basically bidding out of unprofitable clients. So logically that should extend to improved profitability, but your margins for this quarter for the core business has been down. Can you explain that?

S. L. Narayanan: See, it does not mean that the rates are going to be marginal or anything. It is more because we want to focus on the larger players and we want to make sure that our resources are focused on the larger opportunities. See, these are clients who we had picked up during the earlier days when they were all very promising and they were funded by very large corporations or very prominent venture capital funds, and today as the market has changed, they have become somewhat marginalized, and many of them are on very small scale of operations. So it's purely to redeploy our resources especially the SG&A resources on the bigger opportunities that we have taken this conscious decision to shed some of these engagements. If anything, some of those rates were also quite superior, but we did not see the prospect for them going up to 100-man engagements or a 200-man engagement, and that is one of the main reasons why we consciously took the decision to shed these customers.

Shiv Nadar: There are other three reasons, S. L. already mentioned. One is rate drop which is 0.9%. Two, a larger bench and lower utilization which is deliberate during this period. Three, in the technology space extended closed periods because of Thanksgiving and Christmas in US.

Sanjay: Okay, and would it be fair enough to assume that once the client rationalization process is over, your growth would be in line with that of the top tier companies, given that your billing rates, utilization, and to some extent man power addition is comparable?

Shiv Nadar: Our manpower addition would be comparable commensurate with our size even today. With reference to the growth in revenue, if I say anything, it will be a forward-looking statement, which we said that we would not be making. You will have to bear with us in this period, but we are confident that the future is bright.

Sanjay: And could you talk about the ramp up from existing clients in technology development services and software product engineering. Has it been in line with your expectation in the last quarter?

Shiv Nadar: Yes.

Sanjay: Would it be fair to say that the worst for technology development services and software product engineering is over?

S. L. Narayanan: In terms of growth, we would be facing lower growth rate in the next two quarters at least compared to the application segment. So as a piece of the total revenue we expect end-user segment to improve.

Sanjay: Okay. Thank you.

Moderator: Thank you very much Sir. Next, we have Mr. Shekar Singh from DSP Merrill Lynch.

Shekhar: Hi Sir. Just wanted to understand, the last quarter there was very good piece of data which was given that the top 20 clients have grown by some 22.5% quarter on quarter. I just wanted to know, this quarter how has that been because it at least from the face of it does not look like the growth has been so strong?

S.L. Narayanan: Yeah. See the top 20 customers have grown by about 4%, the top 5 customers have grown by about 8%, and top 10 customers have also grown by about 4%.

Shekhar: Okay. Secondly, I just wanted to understand in case of Deutsche Software that is DSL Software. Now, we have reached almost like $35 million of annual run rate. What is the scope in it for further expansion? Can it become a $100 million sort of run rate client?

Shiv Nadar: See, we could answer this question in a slightly more macro context. Instead of just putting a precise number, I would only recall what we said some quarters ago. DB is a very large user of IT services and their revenue budget alone runs into about $2 billion annually. So at a time when everybody is looking for very cost effective solutions and moving some of these engagements offshore, offshore is almost synonymous with India today. So we have something which is ready as a catchments and I cannot put a precise number saying that this milestone we should be at X million or Y million, but I think the logic and the rationale, the strategy behind the acquisition is one which was guided by this large opportunity and also getting domain specialists from DSL. And the rest is a matter of deal we need to execute and we need to deliver and delight the customer and the potential is pretty immense.

Shekhar: Okay.

Shiv Nadar: I can give you a different fix for the next four quarters. We are likely to have one of the highest growth rate of the industry. When I say highest, the very best.

Shekhar: Okay. That's very nice to hear. Secondly, I just wanted to understand like we have been looking at some of the semiconductor companies like Intel and all and their recent plans have been in terms of cutting down on the capital expenditure which in turn means that the direct impact is going to be on the semiconductor equipment companies as has been just mentioned that HCL Tech works with somewhere close to 11 of these semiconductor equipment companies. In light of this sort of a scenario emerging, whether the revenue of these companies are going to get impacted in the near future? Do you see that the revenue of HCL Tech might also get impacted, one in terms of the amount of business, and second in terms of increased billing rate pressure?

Shiv Nadar: Increase in the billing rate pressure in this area can come only if there is an alternative. Correct?

Shekhar: Pardon.

Shiv Nadar: Increase in billing rate pressure in this area can come up only in case there is an alternative.

Shekar: Okay.

Shiv Nadar: We are probably the only one who are serving this space.

Shekhar: Okay.

Shiv Nadar: That is one. And two, in terms of whether the revenue is likely to go down? The answer is, we do not think so. Is the growth likely to be like what is stated DSL software one of the highest in Industry? The answer is it may not be.

Shekhar: Okay.

Shiv Nadar: However, in these companies, we are likely to gain opportunity to spread ourselves into the application and BPO space. From the client, our revenue may go up but not necessarily in the area of design itself. We are seeing that happen.

Shekhar: Okay. So if I am right, like, if you can just share with us what is the sort of signal that you are getting from company like say Kulicke and Soffa so far in terms of the pressure that they are facing and how they are trying to mitigate those pressures?

Shiv Nadar: They are expecting us to take wider range of software, but Raj why don't you answer that question.

Raj: Sure. I will do that. When you are talking about companies like Kulicke and Soffa, you are right in saying that their book and billing ratio is coming down because of the orders that they are getting from companies like Intel and other ones. But like Mr. Nadar mentioned our strategy of cross selling within that account itself is paying of. We are going into other areas within that same account, number one. Number two, is also with that pressure coming in for them going offshore makes more sense now. They are getting the revenue pressure, they are getting the top line pressure, so their budgets are being more strategically spend on companies like HCL and offshore companies which are going to give them the cost advantage or get more for the dollar that they are spending across. So, we do not feel that there is going to be any decline in that segment from our side at least.

Shekhar: Sorry for persisting with this question, but in the past we have seen other EDA companies like Synopsis, they have actually gone in for the route of setting up of their own centers in India and expanding within their own centers. If you can just give some idea whether these companies, who are some of the bigger clients on the semiconductor equipment side, are they also planning something of this sort in future so that the growth, HCL Tech might continue, but the cream in terms of the business that actually goes to their 100% subsidiaries?

Raj: In our customer base we are not seeing that trend in this segment.

Shekhar: Okay, and one last question was, in terms of these subcontractors we were earlier told that the subcontractor man-months will be coming down going into the future, but on a quarter on quarter basis we have just seen a very marginal decline from 509 man-months to 492 man-months. So, I thought that it was a part of the client rationalization exercise and therefore this should also comedown quite substantially.

S.L. Narayanan: No that may not be so directly correlated with some of the marginal clients. It should it is coming down, but you are right, it is not coming down as sharply as it was made out to be but it is on its way to getting reduced.

Shekhar: One last question related to your effective tax rate, since we have seen the effective tax rate jumping quite a bit quarter on quarter because of various reasons, but on a more steady state sort of basis what do you think will be the effective tax rate?

S.L. Narayanan: That's a very difficult one to put out because it is a play of several factors. We have certain jurisdictions where we end up paying tax, and then you know, this quarter we had the effect of creation of a deferred tax asset as such because that became apparent after the conclusion of the tax order, then it had to be put through the books. As far as possible we don't try to manage the provision because we have to exactly reflect the way it is based on information becoming available, and two quarters back we did not disclose the extraordinary effect, and this time we have taken care to actually disclose what is the extraordinary effect because of the reduction in total provision. But it becomes very difficult to put a number because there are several variables that work such as onsite-offshore mix and STP-non STP mix, and also inclusion of entities, which work outside jurisdiction. So, I will be finding it very difficult to make it a very predictable number.

Shekhar: Okay. And any plans of pulling out money from the debt mutual funds?

Shiv Nadar: Debt funds?

Shekhar: Yeah debt funds.

Shiv Nadar: No.

Shekhar: Okay. Thanks a lot and congratulations on a very good result.

Moderator: Thank you very much Sir.

S.L. Narayanan: We will have one last question because we are almost an hour since we started.

Moderator: Sure Sir. Our next question comes from Mr. Amit of Birla Sunlife Securities.

Priya: Hi this is Priya here. Just wanted, last question, in terms of your investment if you could give us some breakup between long term and short terms as well as how much of it is in debt fund.

S.L. Narayanan: We could give it you offline. I don't have the numbers here. We could disclose those details to you.

Priya: Fair enough.

Moderator: Would you like to take another question?

S.L. Narayanan: Yeah one last question.

Moderator: Sure Sir. We have Mr. Chellappa from Franklin Templeton.

Chellappa: Good evening Sir. Regarding our BPO business could you give us the number of clients you have for HCL E-serve and HCL Northern Ireland?

Sujit Baksi: Yeah I will answer this question. This quarter HCL E-serve out of India was servicing 15 clients and we have 24 processes as compared to 11 clients in the last quarter and 19 processes that we had. So we have added four more clients and five more processes. In Northern Ireland, we have onsite against 8 customers that we had within BT and outside BT and JAS'02 we have 9 customers and in terms of processes onsite we had 21 onsite processes last quarter and we have 22 onsite processes this quarter.

Chellappa: Okay. I just want one more question. What is the cash and treasury investment as on 31 December 2002?

S.L. Narayanan: About $285 million.

Chellappa: Thank you.

S. L. Narayanan: Thanks Chellappa. I think we will terminate the call at this moment.

Shiv Nadar: Ladies and gentleman thank you very much for joining our call today. There may be more questions, if you can just mail them to either S.L. or Sujoy, we will be happy to answer them very very promptly. Thank you. Thank you again for joining us.