

**Transcript: Post Q1FY2011 results conference call, Mastek Ltd**  
**14th October 2010, 5.00pm IST**

*Presentation Session*

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**Moderator:** Good afternoon ladies and gentlemen. I am Gopal, moderator for this conference. Welcome to the post results conference call of Mastek Limited. We have with us today the Mastek management team. At this moment, all participants are in listen only mode. Later, we will conduct a question and answer session. At that time, if you have a question, please press \* and 1 on your telephone key pad. Please note this conference is recorded. I now would like to hand over the conference to Mr. Abhinandan Singh, Head Investor Relations, Mastek. Please go ahead, Mr. Singh.

**Abhinandan Singh:** Thanks Gopal. Welcome everyone to our post results conference call. The quarter under review for us is our first quarter of the fiscal 2011, as ours is a June-ending year. Present with me on this call are Mr. Sudhakar Ram, our Chairman and Managing Director, Mr. Mrinal Sattawala our Group President and Mr. Farid Kazani, our Group CFO. We will begin today's forum with opening remarks by Mr. Ram and then we will open the lines for your questions. After the call ends, within a few hours, we should have the audio replay of the call available for listening to, at the access numbers mentioned in the conference call invitation that was sent to you earlier. The transcript of the call should become available in a few days time, sometime next week. With that, I would request Mr. Sudhakar Ram, our Chairman and Managing Director to initiate the call. Over to Mr. Ram.

**Sudhakar Ram:** Thank you Abhi. And welcome all to our Q1 results earnings call. As you are aware that this has been a disappointing quarter, there were some rude surprises that we ourselves faced. And there were a set of events which actually bunched together quite unexpectedly causing revenue decline as well as possibly the first loss that we have posted since we went public. So, before I get into qualitative things, I would like Farid to take you through the numbers, explain the deviation between our last quarter, Q4 financial year 2010 and Q1, so that you get a feel and put the whole thing in context. So, over to you Farid.

**Farid Kazani:** Thank you Sudhakar. I'll just cover some of the headline numbers and also give you all a brief summary analysis on what happened during the quarter. Overall, total income

ended up at 151 crore as against 165 crore in the sequentially preceding quarter. In terms of profitability and PBT, as against 2.6 crore profit of last quarter, we ended up with 11.3 crore of loss in the quarter under review. And if I add back the forex gain in both the quarters, the PBT before forex is actually was 7½ crore profit last quarter as compared to a 14.9 crore loss in this quarter. Let me try and give you a quick overview of the impacts, starting with revenue. We have seen revenue impacts, larger impacts being in the UK and some in the India-Asia markets. In the UK, it has been largely due to a drop in revenue in the project in Capita. And in India & Asia-Pacific, it's been due to some accounts where we have had specific issues, one of which is a revenue reversal that we had to take in a specific client linked to the delivery and confirmation issue. And second is in terms of project overruns that have happened in India & Asia-Pacific region. There has also been a minor impact in the US. To provide you a break-up, UK is down by a little over 6 to 7 crore, India & Asia-Pacific lower by close to 6 crore and US by roughly around 2 crore. So, that's the bridge for the revenue impact of 14 crore between the last quarter and this quarter under review. On the PBT before FX, the bridge is roughly around 22 crores. And the larger part of the impact is on account of the salary increase and some due to headcount that increased in this quarter. We had mentioned at the start of this quarter, in fact in the last earnings call that we will be implementing a salary increase with the clear objective of retaining our best talent. We have gone ahead and given salary increase from 1<sup>st</sup> July, which is close to an average of 20% for the offshore employees and roughly 3½% for the onsite employees. The impact of salary increase and head count put together is roughly around 11 crores to the P&L in this quarter compared to last quarter. The second major impact is on account of higher product development expenses that have got incurred in this quarter, which was roughly 3 crores higher and that's primarily in our insurance vertical linked to our rollout of the program with Foresters in North America. As I mentioned, the India & Asia-Pacific reversal of revenue accounts for roughly 1½ crores, the projects overruns in India, Asia-Pacific and some bit of in North America accounts for roughly 3 crores. And the balance of around 4 crores is linked to the revenue shortfall, where the gross margins obviously have not come in. So, this accounts for roughly around 22½ crores. The other headline numbers include the order book position which ended up with 312 crores as against 306 crores and that is a positive sign, and a lead indicator of how we will expect to perform in the next few quarters. On the head count, we ended up with 3360 employees compared to 3243 employees in the last

quarter, reflecting a net addition of 117 employees. We are looking at taking necessary actions, some of it has already been kicked off and I'll ask Sudhakar to take you through with some details on that. Thank you.

**Sudhakar Ram:**

Thanks Farid. Clearly, we are looking at urgent and focused action, a set of steps to get back to growth and profitability. Broadly, the actions are in three areas. One is in sales. With Sattawala coming on board, the fact that we already had a strong sales team, I think we put a renewed focus in terms of more tighter controls, better sales processes, regular reviews and so on, which should help us increase our own coverage in the field and focuses to add new accounts. Top of that we had revamped our account management processes to ensure that the coverage on our top strategic accounts is much better, the kind of c-level relationships that we build, enhance and that we can actually mine more revenues aggressively in these accounts. The third thing which we have brought into place is an integrated go to market approach between the services businesses that we have, especially in North America with the insurance product solutions business to ensure that all the existing insurance accounts, both in Life and Annuity as well as Property and Casualty are penetrated with a strong, wider basket of portfolio offerings, so that we can grow these accounts more aggressively. So we are taking steps. This has already started at the beginning of the quarter and should help us improve order book and improve revenues going forward. On the projects front, typically we have had strong margins, but in this quarter we witnessed 3 or 4 different things coming together which impacted us. Some of them are one time, but we are putting in steps to see how we can improve margins even on the accounts which are doing well, to counter the salary increases impact and provide for the investments that we have. So, under our CDO (chief delivery officer) that is the concerted action plan, which is put in place to improve margins on existing accounts. The third area is obviously in terms of discretionary costs. We have kept it under check, but we will put it under a microscope now to ensure that only the necessary expenses in terms of travel and other discretionary expenses are done till we get over this setback. And we will obviously continue to invest in Elixir development, especially with the customer commitments we have in Foresters and a great break we got in the North American market. We see market opportunities, so we do need to continue investments in product development. So, while it may take us a couple of quarters to get back both top line as well as bottom line and get to a healthier position, fundamentally the business strategy is sound,

the kind of accounts that we are going after are in line with that, there is differentiation that customers perceive in our service offerings. And now that we have the breaks in North America also, we are pretty confident about our mid to long term prospects, but we do need to weather these short term issues and come back to profits, which is what the entire team is committed to doing. With that, I will open the floor to questions now.

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*Question and Answer Session*

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**Moderator:**

Thank you sir. Ladies and gentlemen, we will now begin the question and answer session. Participants are requested to adhere to one question in the initial round and come back to further questions. To ask a question please press \* and 1 on your telephone key pad. If your question has been answered before your turn and you wish to withdraw your request, you may do so by pressing # key.

The first question comes from, Mr. Biplab Chakraborty from B&K Securities.

**Biplab Chakraborty:**

Thanks for taking my question. The top line has been shrinking over the past eight quarters or so. I was wondering if you could share your thoughts about reversing this trend.

**Sudhakar Ram:**

The set of steps we spoke about is exactly around that. Right from July onwards we have reorganized ourselves. We have put lot more sales focus and the teams are in place, including at the leadership level Satta coming on board, we have Barry who is running the UK, Mike Dufton in North America. And the next level of leadership in insurance including P&C, reinforcing Capita and so on. So, we have actually strengthened the leadership team across and improved our sales process during this quarter, quarter-and-a-half. Now what we are attempting to do is, firstly and obviously, get new deals. And that is the focus on Insurance, on forging new partnerships in Government, as well as going after the broader Financial Services segment. So, that thrust continues. The second thing is that while customers used to come to us because of our strong delivery record, we were being bought rather than we really selling. So, we have reinforced the account management process and increased our coverage on our large accounts, increased our level of relationships, which is already in force and that's leading to a better pipeline visibility today. But it will take some time for it to translate to order booking. So, that's already in place. The third is, although we are a solutions company, we do have a strong services portfolio as obviously all our customers also use

us for services -- not just in application development & maintenance, but also in testing and data warehousing and so on. We are going with a systematic campaign to leverage our existing P&C accounts, where we have our billing and policy admin solutions as well as our Vector accounts to see how we can improve the footprint, get them to buy a larger portfolio of services from us. So, those are the three steps which are underway from July onwards. And we have seen that it is helping us build the pipeline, but obviously it's not translated to very strong results as yet. But, we do expect that to payoff in the coming quarters.

***Biplab Chakraborty:***

If I may follow up on that, maybe your thoughts on the levers that you think are available to return Mastek to profitability. And if I may, what would be your reasonable timeframe for the same?

***Sudhakar Ram:***

I think the levers are clear. The first lever is to get our top line back, because our utilization has dropped and we have that bandwidth, both from a sales perspective and from a delivery perspective, we have very strong bench strength. So, we have the bandwidth which can support a much larger base of business. So, getting back on to a revenue growth, which obviously the first step is the order book, is the first lever. The second lever is, we do expect to be able to improve productivity on some of the key accounts and manage some of these risks on the existing programs, any thick width program has its share of risks, but we have put in tighter risk management processes to be able to manage that better. So improving margins, gross margins on existing projects is the second lever. The third lever is other discretionary expenses. Now how fast this will return as to profit is something that we can't exactly talk about right now. But, the attempt is to get back in the next two quarters, latest three quarters.

***Biplab Chakraborty:***

Sure. Thanks. That's all from my side, thank you.

***Moderator:***

Next question comes from Mr. Pratish Krishnan from Bank of America.

***Pratish Krishnan:***

May I just understand this revenue loss from Capita? You mentioned about some work being stopped, can you elaborate on this?

***Sudhakar Ram:***

It's actually not stopped. We have had a new arrangement with Capita on the Elixir development. We have got into a capacity deal. The level of development work and the level of staffing has come down by about a million pounds this quarter as compared to the previous quarter. Still there is

a fair amount of revenue which is being generated on Capita on the product implementation. So, it's just a reduction, not a stoppage.

**Pratish Krishnan:** So, this just the revenue run rate has now come down, is that the way one should look at?

**Sudhakar Ram:** That's correct.

**Pratish Krishnan:** Okay. And this was driven by whom, in the sense I understand Zurich Life was one of the clients which was in transition to the new platform?

**Sudhakar Ram:** That's right. And that has been implemented. And now there are other customers which have to come online.

**Pratish Krishnan:** So, those have not come online or probably there are delays?

**Sudhakar Ram:** No, there is a process here, because Elixir implementations, any insurance platform implementation actually, takes time. So, it's going as per our planned schedule. It's just that the nature of work coming to us has changed, profile has changed this quarter.

**Pratish Krishnan:** Okay. So, for the original contract value which we had announced, would that change now?

**Sudhakar Ram:** The contract is still active. Basically, it's not a one year contract, the entire contract value is over a two year period.

**Pratish Krishnan:** Yes, but you would have assumed something in the order book for this year? So, I am just wondering would that assumption change or anything.

**Sudhakar Ram:** Not really. Our order book position remains intact.

**Pratish Krishnan:** Okay. And second is the revenue reversal from the APAC clients, maybe for this kind of payment, frankly we have not seen a revenue reversal.

**Sudhakar Ram:** Basically, it's actually we had to put a, between the client and us we decided not to go ahead with the contract, because there were some issues which both of us couldn't resolve. So, we had started work on it, but we decided it was not feasible to continue working, so we had to stop the contract and reverse the revenue.

**Pratish Krishnan:** So when you say reversal, this was recognized last quarter or the present quarter?



- Sudhakar Ram:** Last two quarters. So, it had been recognized over two quarters and that we had to reverse.
- Pratish Krishnan:** Okay. So is there any debtor or payment issue which one should probably be aware of?
- Sudhakar Ram:** No, it's all reversed out, so there is nothing there.
- Pratish Krishnan:** Okay, okay fine. Thanks a lot.
- Moderator:** Next question comes from Mr. Abhishek Shindadkar from ICICI Securities.
- Abhishek Shindadkar:** Thanks for taking my question. Sudhakar, I have seen the bookings number, not a significant jump in the bookings number, so is it that we have started to bill the bookings number in third quarter? Or is that, how should we read into those numbers?
- Sudhakar Ram:** If I look at the bookings number, that's actually the good leading indicator for us now. One part I agree with you that it's not moved up robustly, but when you look at 310 crores, then in constant currency terms it's about 322 crores, so there has been a marginal shift in the booking number. There have been some paperwork issues. Our bookings could have been better if all our contracts were exactly signed as of September end, but this is something that we expect to improve in the next 2-3 quarters. So, this has been our complete focus that we want our order book to be very strong by the end of this financial year, so that we have a good platform for growth next year. So, that's what I talked about in July, when we started the year and that remains our focus.
- Abhishek Shindadkar:** Okay, but then marginal conversion of the bookings has started to take place, right?
- Sudhakar Ram:** Marginal conversion of bookings to revenue, you are saying?
- Abhishek Shindadkar:** Yes.
- Sudhakar Ram:** Obviously, yes.
- Abhishek Shindadkar:** Okay. And the second thing which I would like to know is, we estimate that the prices, the billing rates have declined substantially, probably 5% to 7%. So, is that a cause of concern and what are we doing in terms of that?

- Sudhakar Ram:** See, given the nature of our business and the large fixed-priced component in our revenues, it will be difficult for you to compute billing rates. There has been no change in billing rates through the quarter. We took a hit on one account in January which we had talked about, in terms of reduction in the billing rates, and that was in the US. That is the only thing. If you do a last year comparison that will be lower. But, on an overall basis, there has been no issue on billing rates, but the margins have come down because of these revenue reversals and project issues. And FX has also created its own fluctuation, but billing rates have remained steady.
- Abhishek Shindadkar:** Okay, thanks for taking my questions. Thanks.
- Moderator:** Next question comes from Ms. Shradha Agarwal from B&K Securities.
- Shradha Agarwal:** In terms of following up on the earlier question as to where do we stand against our earlier communication of at least 25 million pound of bookings from Capita in the next two years, is there any change, when you talk about some development work being stopped on Capita account?
- Sudhakar Ram:** See as of now there is no change in the contract. And we do expect that the contract terms will be adhered to.
- Shradha Agarwal:** So, you still maintain that 25 million pound run rate from Capita?
- Sudhakar Ram:** That's right.
- Shradha Agarwal:** And what is the status, apart from Zurich, what is the status of implementation of other accounts? Are we in the process of implementation?
- Sudhakar Ram:** Yes, the next account, the development work, the customization work is going on.
- Shradha Agarwal:** Okay and that account would be prudential?
- Sudhakar Ram:** No, it's Coop.
- Shradha Agarwal:** Okay, okay and how about the status of implementation of the third account there?
- Sudhakar Ram:** No, right now the work is on the second one.
- Shradha Agarwal:** Okay, so you still expect some kind of lag to happen on the third account?



- Sudhakar Ram:** See, these are development schedules Shradha, so this is planned by Capita and they will be executed as per their plans.
- Shradha Agarwal:** Sir, that's right. But then I am really curious to understand why Mastek has been hiring people quarter on quarter, despite we not seeing a very significant jump either in the order book or any positive feelers coming in from our clients, so why such kind of a hiring coming in from the company?
- Sudhakar Ram:** In fact most of the increase this quarter has been on trainees. As a company, we do need to flatten the pyramid, and we have been taking on trainees and they are undergoing training and they will come into productive use during this year.
- Shradha Agarwal:** But what is the visibility we have, to be hiring people?
- Sudhakar Ram:** What you see is the 12-month order book. Our visibility is based on the complete order book picture as well as the pipeline, which is not obviously visible to you.
- Shradha Agarwal:** If I look at your order book number versus our historical trend of order book to next quarters revenue of 35% to 40%, where do we stand now in terms of that number?
- Farid Kazani:** I don't think, that would have changed in any way, we are still in the 30-35% range.
- Shradha Agarwal:** Okay. And secondly, Farid I am not really sure of what do you mean by project overruns in this quarter?
- Farid Kazani:** There have been some accounts where we have had higher cost linked to the delivery that has happened in some projects in India, Asia-Pacific and one account in North America. So, that's what I mean by project overrun.
- Shradha Agarwal:** So, this is a one off cost of close to 3 crores?
- Farid Kazani:** yes.
- Shradha Agarwal:** Okay, okay. And secondly on the tax number, what is your assumption on tax for the entire FY 11 and 2012, if you could share something there?
- Farid Kazani:** On the tax for this quarter, it's been roughly around 2 crores and the future tax will be based on how the revenue and profitability pans out for the US and the UK as that's where we pay tax. So, it's difficult to hazard a guess right

now. It will all depend upon the top line and the profit that comes out of the business in UK and US.

**Shradha Agarwal:** Yes, but as of now we do not expect the company to come back to profitability at least for another 1-2 quarters, is that a right assumption?

**Farid Kazani:** The tax is not linked to just the Mastek Limited numbers, because we pay taxes on our local revenue and profit in UK and the US.

**Shradha Agarwal:** That's right sir. Thank you.

**Moderator:** Next question comes from Mr. HR Gala from Quest Investments.

**HR Gala:** I am not sure whether my name had come earlier, because the line is so bad, half of your discourse I could not hear. I believe that your transcript will be proper. My question relates to the new paradigms which are coming on the horizon in the IT services area like cloud computing etc. Now how are we prepared to address those, when our clients demand that?

**Sudhakar Ram:** In fact, we are building up expertise in that area. And there may be certain specific solution offerings that we are actually getting ready to prepare for the cloud around the Government and Financial Services verticals that we have. But it's premature to talk about it, because these are internal projects right now.

**HR Gala:** Okay. Now, in this IP-led enterprise solutions which we are harping upon as our main thrust area, when it comes to the competition, who are the major players against who we have to contend?

**Sudhakar Ram:** In insurance it's largely Computer Sciences Corporation and now Oracle, and in Government it is players like Logica.

**HR Gala:** Which is the first one, CSC?

**Sudhakar Ram:** CSC, that's Computer Sciences Corporation, which is a US company.

**HR Gala:** Okay and Oracle?

**Sudhakar Ram:** Oracle, yes.

**HR Gala:** And in Government vertical?

- Sudhakar Ram:** It's Logica in the UK.
- HR Gala:** But there aren't any Indian companies which are?
- Sudhakar Ram:** Maybe, but not very directly. TCS does something in insurance in UK, but by and large on a global basis we face CSC and Oracle.
- HR Gala:** Okay, these are the major competitors. Now sir, apart from the financial services as one of the additional verticals that we intend to get into, don't you think that in order to de-risk our business model from these two main verticals, we should expand to some other verticals and lend some sort of sustainability to our revenue?
- Sudhakar Ram:** We are looking at that. This quarter one of the new additions we have is actually in the healthcare business in the US, based on our expertise on NHS. We see that it's a small deal for now, but we see that it is strategically important to us. And over the next year or two that's something we are looking at as we know that healthcare is going to be a major IT spender. So, it gives us a good base.
- HR Gala:** And which is another one?
- Sudhakar Ram:** The other one is in financial services.
- HR Gala:** Okay. Sir, does your business model and the kind of engagements that you get into, does it render, make it possible for you to render the high value IT enabled services to the same set of clients, having given the license of your product?
- Sudhakar Ram:** What we do is actually use our IP along with partners who have that BPO capability. For instance, Capita is one such partner who has leveraged our IP in the UK market. We announced a relationship with Genpact in the US and so we are hoping to do some business along with Genpact, going to market with them in the next year or so.
- HR Gala:** Okay. Will you sir give some guidance for this FY 2011?
- Sudhakar Ram:** No.
- HR Gala:** You don't give any guidance?
- Sudhakar Ram:** Yes.
- HR Gala:** Okay. What kind of capital expenditure plans do we have?

- Farid Kazani:** Nothing major actually, because we don't need any further capacity expansion. And our normal capex, which is maintainable capex, is roughly between 10 to 15 crore rupees per annum.
- HR Gala:** Okay, because the type of business model we have, I think you don't need to recruit very many people I believe.
- Farid Kazani:** That's one reason and we already have capacity with us.
- HR Gala:** Okay, fine. Thank you very much.
- Moderator:** Next is a follow up question by Mr. Biplab Chakraborty from B&K Securities.
- Biplab Chakraborty:** Could you please give some more idea about or rather the reasons behind the project overrun, that will be really helpful. And my second question would be about the declining share of fixed price projects, if you could please throw some light on that?
- Sudhakar Ram:** See, the project overruns can happen in any fixed price project. If you have an Elixir implementation or a billing implementation, then you fix price it and sometimes the work goes over what you thought it would be. So, in some you gain and in some you lose. So, it's part of life. The fixed price has actually gone down as the percentage in the last couple of quarters, but 1 or 2 deals can change the whole picture. So, that would vary quarter on quarter. But, as you know our normal attempt is to do 50% of our business on a fixed price basis.
- Biplab Chakraborty:** Okay, thanks. Thanks a lot.
- Moderator:** Ladies and gentlemen, to ask a question please press \* and 1 on your telephone key pad.
- Next is a follow up question by Mr. Abhishek Shindadkar from ICICI Securities.
- Abhishek Shindadkar:** Hi Sudhakar, in terms of hiring, are we done with our hiring for 2011 or what is managements view on hiring front?
- Sudhakar Ram:** See, we are not a head count driven business, so our hiring will be based on order booking and the kind of skill set that we need. If we have those skill sets in house and we have the capabilities, we won't hire. So we don't plan hiring except as a derivative of the order book and revenue projections.

- Abhishek Shindadkar:** Okay. If I do the math and just a follow up on Shradha's question, you said that for next two quarters the profitability seems to be more or less similar to Q1, which implies that apart from wage cost, the decline is probably from the volume or probably the revenue lines. So is the math right or there is something which we are missing out?
- Sudhakar Ram:** If you look at profitability, there is not going to be too many changes from profits perspective in the short run. But, we are looking at the increased order book and therefore an impact on revenue. In fact, there are deals which we expect should close in this quarter or next quarter, which would then have a good impact on revenue going forward.
- Abhishek Shindadkar:** Okay, okay, thanks for taking my question.
- Moderator:** Next is a follow up question by Ms. Shradha Agarwal from B&K Securities.
- Shradha Agarwal:** Sir, just one short question. How has the attrition been for this quarter?
- Sudhakar Ram:** It's been much better, given the wage hike.
- Shradha Agarwal:** And what that number would be?
- Sudhakar Ram:** We don't share the numbers Shradha.
- Shradha Agarwal:** Okay, not a problem. Thanks.
- Moderator:** There are no further questions. Now, I hand over the floor to Mr. Sudhakar Ram, Chairman and Managing Director, Mastek, for closing comments.
- Sudhakar Ram:** Thanks once again for your interest in Mastek and continued support. Now, we have been going through some tough times over the last 7 to 8 quarters, but we are optimistic that we have the team in place, as well as the strategy in place, to be able to reverse this trend within the next couple of quarters. So, stay tuned and we do hope to share good news with you by the next couple of quarters. Thanks once again.
- Moderator:** Ladies and gentlemen, this concludes your conference for today. Thank you for your participation and for using Door Sabha's conference call service. You may disconnect your lines now. Thank you and have a pleasant evening.

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3. *1 crore = 10 million*