



“Mastek Limited Q1 FY16 Earnings Conference Call”

July 16, 2015



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MODERATOR: **MR. DIWAKAR PINGLE – MANAGING DIRECTOR, CHRISTENSEN INVESTOR RELATIONS PVT. LTD.**



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Moderator

Ladies and Gentlemen, good day and welcome to the Mastek Limited Q1 FY16 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 phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Diwakar Pingle. Thank you and over to you, sir.

Diwakar Pingle:

Thanks Darryl. Good morning and good evening to all of you. Welcome to the Q1 FY16 Earnings Conference Call of Mastek Limited. Joining us today on the call is top management from Mastek represented by Mr. Sudhakar Ram – Managing Director and Group CEO, Mr. Joe Venkataraman – Chairman, Mastek UK Limited, Mr. Jamshed Jussawalla – CFO of Mastek and Mr. Anant Thakrar – Senior Vice President Finance of Mastek.

To begin with – Sudhakar would give you a brief overview about the quarter gone past, this would be followed by an overview of the LPT business by Venkataraman and then Anant would possibly go into the financials in brief before we throw open the floor to question-and-answer session.

With that said, I will now hand over the call to Sudhakar. Over to you, sir.

Sudhakar Ram:

Thank you Diwakar and good evening to all of you on this Q1 Earnings Call. It has been an eventful quarter and results here are now for the Mastek standalone business which is only the Solutions business with all the Insurance Business having been demerged into Majesco.

So for Mastek this quarter I think the key highlights are, one is the acquisition of Indigo Blue. You are aware that our aspiration is to be involved in large and complex programs and today a lot of digital transformation is happening across the different verticals and customers are expecting results fast and agile is the way of delivering these results. So we have invested in agile methodologies over the last two years and now the acquisition of Indigo Blue which is an award winning agile program management consulting firm, I think it adds very well to our credentials as well as capabilities and track record. The advantage is that we see not just cross-sell and up-sell for the existing customer base of Mastek and for the customer base of Indigo but also the fact that Indigo adds about three to four customers every quarter, they have a robust customer acquisition method and both of us can leverage that to build our business in the UK mainly and we could look at leveraging Indigo's capability in other parts of the world as we expand. So I think that's a good thing that has happened this quarter.

As far as the core business goes with the uncertainty on UK elections right from February, we know that Government business has been slow, there we have not added any new deals, and it has just been expansion of existing business. But with the majority Government now in place and the Government ready to restart on its IT initiatives I think the pipeline has started building up, but by the time we see results of that from a revenue growth perspective it will



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probably be the second half rather than the first half. So the first half from a growth perspective will remain muted and it is only from the second half that we will see growth and correspondingly we will also have impact on profitability.

From an India business, I think it has been steady, we have not had too much movement since the last quarter. We have made the business more profitable but the growth is yet to happen, we are expecting a few large orders there which will get us back on to a growth momentum.

In terms of our segment of revenue, I think Government has been pretty muted over the last two quarters, Retail has started picking up not so much from revenue as much as the fact that we have added a number of new logos, at least 3 new logos this quarter were Retail and those are small pilot programs with very prestigious large Retailers and we do expect them to start growing over a period of time.

On Financial Services with insurance exiting, we had to pretty much re-strategize our position there, we have an existing base of business there with customers like IPF who are in the micro lending space but we have now brought in a new Financial Services head to re-strategize that business and spearhead the growth for us in that segment within the UK.

The other interesting part has been our Legal Practice Technologies (LPT), our JV with the Law Society and I will hand it over to Joe Venkataraman to take us through the details of that JV.

Joe Venkataraman:

As you are all aware, this JV is 60% owned by the Law Society and 40% by Mastek and we have been on this journey of creating a conveyancing portal that will completely change the way the conveyancing practice are rendered in this country and it is one of its kind. We have been developing this product over the last 9 months. So what we decided was it is important to have the right launch of this product because you have to launch it right whenever you start a business of this nature. So we have decided a three stage launch, one is to do a soft launch then to do a controlled launch and a full launch as the three steps in this process. The soft launch has already been done on 26th May'15. We have had some initial feedback on the product and we are using Agile as a development methodology and these feedbacks are being incorporated and the next release have been done in a matter of months. So before the end of this month we will be possibly doing a controlled launch with some of the conveyances who are interested in this product and then we will be having a launch sometime in the month of September for a full launch.

I am pleased to say that the sales team has done well to have an initial interest, even before they have seen the product of about roughly 130 firms interested in it, so that gives us a positive and a good outlook towards how we can develop this as a business. So that gives me great confidence about the future possibilities, but the most important thing is for us to get the product right and so we are taking it as three step process and ensure that the live is successful sometime in September'15.



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So I think that's a brief update on where we are at this point of time and I am happy to take on questions once Anant takes you through the financials.

Anant Thakrar:

Thank you Joe, thank you Sudhakar and good morning and good evening to all of the listeners. So look, the first thing I will note is I will take you through the highlights of the Q1FY16, the first quarter as a standalone business for Mastek. In the presentation that we put out we also showed the numbers for the last quarter but it is important to note those last quarter numbers were for the total company including the Insurance Products & Services business. So they are not comparable as such but for reference purposes we have put them there.

So let me just take you through the financials here:

For the quarter we ended up with total income of Rs 139 crores in rupee terms as compared to Rs 277 crores for the previous quarter. In terms of profit, PAT was Rs 4.4 crores against Rs 6.4 crores in the last quarter. And from an earnings perspective we saw Rs 16.6 crores which is 11.9% of total income against the previous quarter of Rs 14.8 crores, so we are seeing an improvement there against the previous quarter.

As Sudhakar mentioned, we added 5 new logos in the UK and the pleasing thing was that 3 of them were in the Retail sector and this is an area that we started up a couple of years ago and we are starting to see some really decent traction there. The Retail environment in the UK is very tough but we are starting to see some good business there. The other 2 clients were added through our acquisition, through Indigo Blue and as Sudhakar mentioned in terms of the rationale associated with Indigo Blue we will want to see good progress with that over the coming quarters once it has been fully integrated into the business.

This means that in total our client count is 69 including the clients of Indigo Blue. In terms of our 12 months order backlog, it is Rs 212 crores as of 30th June, 2015, and in constant currency terms that would have been Rs 197 crores. Our top 5 clients contributed close to 61% and our top 10 contributed 82%.

Joe talked about the JV and in the current financials we have included a share of the JV losses as we have done in previous quarters and this amounted to the actual losses with the JV amounted to Rs 3.4 crores against Rs 3.7 crores previous quarter. But in terms of sales we have taken a full total loss for the quarter of Rs 10 crores and so if we look at our PBT at this moment of Rs 10 crores and if we take that out, our overall PBT was closer to the Rs 20 crores mark.

We have taken some exceptional items in the P&L to the value of Rs 1.83 crores which are restructuring and demerger cost in India and the exceptional items in the P&L for the previous quarter was Rs 2.63 crores.



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Just going a bit further down in terms of the high line metrics – our DSO stood at 73 days, that was high this quarter but predominantly it is mainly because we had billed a large amount in the UK in the last month in June, so, it is higher and we would expect that to come down.

Cash and cash equivalents have been fairly steady. We ended up at Rs 155 crores and this includes our investment in the Majesco business and that's at Rs 18.8 crores. Mastek hedges were pretty well-positioned, we hedge close to £17 million at about Rs.107.5 to the pound.

Sudhakar mentioned the verticals we are in, in the UK and this comprises of the Government vertical which is around close to about 60% wherein Financial Services which is about 17% and in the Retail space we are about 14.4% and the rest is other services.

The last point I just want to talk about is the acquisition of Indigo – Sudhakar talked about it. We paid a consideration for acquiring that business on the 30th April, 2015 and there is a future consideration based on revenue and profit targets over the next 3 years.

And the final point in terms of the progress of the demerger at Majesco, it is in a process of listing on the BSE and the NSE and we are expecting probably mid-August when it should be listed. But clearly that is dependent on approvals and regulatory authorities.

So I think that's all from my side in terms of the financials. So let me hand it back to the operator for questions and answers. Thank you very much.

Moderator: Thank you very much. We will now begin the question-and-answer session. Our first question is from the line of Srivathsan Ramachandran from Spark Capital. Please go ahead.

Srivathsan Ramachandran: Hi, Srivathsan here. So just wanted to get your commentary on the UK Government business. The Government has this whole G-Cloud initiative which was more favoring smaller vendors, the last two quarters lead up to the elections and it was not a great time period, how do you see? Do you see Government actually starting up some of the projects which they had put on cold storage lead up to their election and how do you see the pipeline from that point of view come back, would second half be substantially better than being a flat kind of a growth, could you see kind of double-digit growth from the Government business in second half or maybe into FY17?

Sudhakar Ram: Yes, so it is fortunate that the Tony Government has come back and there is already a set of policies in place so it was not revamping everything and redoing the policy from scratch. So now that they are in position we have already seen department start-up, the whole process, it is more at the peaky queue which is intention, RFI kind of a thing rather than real tender now. But within this quarter we expect actual tenders to come and then G-Cloud, the procurement process is pretty quick. So we do expect that the order book should improve in the quarter and revenue should improve in the second half.



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Srivathsan Ramachandran: Okay. And on the LPT JV, just wanted to understand in terms of revenue model, what kind of revenue model would this be? Any broad indication as to, are there any competition? What could be the market opportunity or in terms of number of transaction that typically happen in the UK real-estate market or just wanted to understand that slightly better?

Joe Venkataraman: Yes. So as you know that the real-estate transactions can vary but roughly it is in the order of around 800,000 buy which means the total transaction volume of 1.6 million, buy and sell or both, I am including them in the transaction now that's the size of the market and what we have initially started with is transaction model which has been announced at £20 per transaction right now. And on top of it we are charging a user fee which is based on number of users and how large the firm and these are the two thing by which the LPT business will earn revenue. There are other revenue options we will be looking at, but at the start these are the two things that we are considering.

Srivathsan Ramachandran: And 1.6 million you mean effectively on a monthly basis?

Joe Venkataraman: No, it is an annual transaction.

Srivathsan Ramachandran: Okay. And in terms of the losses we are having, it is more as the LPT JV is put in place, the platform is being developed. Post going into live do you think similar losses will continue or do you think that can substantially reduce given that products are up and running, most of the cost will predominantly be towards some maintenance and possibly the sales and marketing cost?

Joe Venkataraman: For this product, the sales and marketing and those things have to continue and you have got to have a hardware platform and a software licensing in place and we should also have a team to support, all these costs have to be incurred before the product take up happens. So what we are expecting is that, as I mentioned in my earlier statement there are three phases by which we are launching it, we have finished with Phase-1, Phase-2 and Phase-3 are going to take place between now and end of September'15, so we have to be incurring cost till then so that we can be supporting whomsoever we take on for providing that support.

The run rate we are controlling consciously wherever possible but I think this kind of products is best to give you update on quarter-by-quarter basis rather than raise an expectation or set a below par expectations. So if we can wait for one quarter, end of September we will have a lot more clarity in terms of how this business will take up. All I can say is that, even before I repeat myself to say that there are 130 firms who have signed an intention to sign an order, so that gives us positive feeling.

Srivathsan Ramachandran: And just continuing on that, are there any competitive portals similar to this or it is one of a kind of portal?



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Joe Venkataraman: There are three or four portals that are available in the market but the differentiation that we are bringing to the market is, there is something called a Deal Room and a Chain View, these are not available in the marketplace at this point in time which are very-very crucial and this is the real problem in the market because the chain breaks and the entire process has a systemic failure so that the people in the chain will be impacted by this. And also the Law Society brand is backing us up which has got council members and their only role to the conveyance is to how to simplify the entire conveyances process. So we are backed by a good brand and that's where the confidence is.

Srivathsan Ramachandran: Okay. So on the cash bit, you had at end of June quarter Rs 155 crores of cash, I think there was a comment saying it includes investment in Majesco, just want to understand is it just a cash infusion or like inter-company loan that has been given to Majesco i.e. Rs 155 crores include or is it the stake that is reflected in that Mastek India owns about 13.8% in Majesco, the value of it that's included in cash and cash equivalence?

Anant Thakrar: Exactly correct, that's the stake that Mastek holds in Majesco which is that sort of percentage, which is Rs 18.8 crore.

Srivathsan Ramachandran: 13.8% I presume.

Anant Thakrar: Yes 13.8%, and Rs 18.8 crores which is the amount.

Srivathsan Ramachandran: So Rs 18.8 crores is then the book value effectively, it is not the market value?

Anant Thakrar: That's right.

Moderator: Thank you. Our next question is from the line of Mohit Jain from Anand Rathi. Please go ahead.

Mohit Jain: Hi sir, first is on the revenue side. Earlier when we spoke last quarter I guess your aspiration was to grow at closer to industry level, but Q1FY16 looks quite slow on organic basis given that you have consolidated for two months. So on my calculation it is actually a dip on a QoQ basis, so what should we expect for FY16 going forward?

Sudhakar Ram: So Mohit as you know we do not give any guidance on the numbers, but like I said that given the election thing the first half will be pretty flat in terms of revenues and we will see growth in the second half.

Mohit Jain: Okay. And second in terms of margins, we also saw a lower margins in this particular quarter, Q4FY15 exit rate was quite good for us, any specific reason for that?

Sudhakar Ram: Nothing, I think partly the margin is, I mean revenue remaining flat, some projects getting over, and some variations in terms of project profitability. So there is nothing exception



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margin, it will pick up as the revenue increases. And overall the big chunk which is Rs 10 crores is because of the LPT which was higher this quarter than last quarter. So we do expect that over a period of time that LPT investment will come down and hopefully before the year end we will see revenues from LPT.

Mohit Jain: So 9% to 10% is the new range till the time growth picks up. And second on restructuring charges, are we completely done with it or do you expect a few more expenses to come up in the next few quarters?

Sudhakar Ram: At Mastek level we are completely done with it, I do not think we will have any more restructuring charges in Mastek.

Mohit Jain: Okay, understood. And lastly I saw the sudden rise in tax rate, so any specific thing that happened in this particular quarter?

Sudhakar Ram: See, this is the normal tax rate. The thing is that we have to remember that tax is on the gross that we cannot take LPT losses because that's a separate entity which will carry forward its own losses. We have to take the full PBT before LPT which is like Anant pointed out almost Rs 20 crores, tax rate on that.

Moderator: Thank you very much. Our next question is from the line of Shubhankar Ojha from SKS Capital. Please go ahead.

Shubhankar Ojha: Hi sir. So basically the restructuring cost that you mentioned for the quarter, you said this was related to Majesco, right, Rs. 1.8 crores?

Sudhakar Ram: Linked to Majesco, linked to the entire demerger process and some redundancies which happened because the need for certain corporate functions and things came down, so that also severance payments.

Shubhankar Ojha: Right. So I mean to say the merger related cost and this is not a recurring item, right?

Sudhakar Ram: No, this is a one-time item.

Shubhankar Ojha: Secondly, so in terms of the, I mean some color in the margin outlook, we have seen smart recovery in the margin, 11.9%, can you improve upon this margin which you have seen in first quarter, are there levers in place which can bring it to 12% to 15% level?

Sudhakar Ram: There are three levers, one is obviously business growth which will lead to better SG&A productivity, better leverage of cost. The second is, LPT starting to stabilize and generating revenues which could have a good impact on Mastek margins. And third is in terms of executing projects in a tighter manner that our gross margins and projects improve. So those would be the three levers and we do expect margins to improve quarter-on-quarter.



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- Shubhankar Ojha:** Right. And finally in terms of the quarterly run rate for Indigo Blue, I mean can you share the quarterly numbers, you got Rs 10 crores for May and June.
- Sudhakar Ram:** Yes. So in the Revenue Analysis sheet we have shared that the two months revenue for Indigo Blue is about £1 million, around Rs 10 crores and that's a typical run-rate for that business, so about Rs 5 crores a month.
- Shubhankar Ojha:** Okay. And this business also would have similar margin?
- Sudhakar Ram:** No, Indigo Blue right now would be at a lower margin but not significantly lower.
- Shubhankar Ojha:** And finally, when is the expected listing for Majesco Limited in India?
- Sudhakar Ram:** Mid-August, if things go well.
- Moderator:** Thank you. Our next question is from the line of Amar Maurya from India Nivesh Securities. Please go ahead.
- Amar Maurya:** Sir first question is about the order backlog which we are having. Can you help us understand about what is the kind of deals which we have in this order backlog? And secondly, if we can add a bit more about the new logos which we had won during this quarter?
- Sudhakar Ram:** I think the order backlog is fairly representative of the business mix that we have, break it down by vertical but it will have roughly same proportion of Government Retail and Financial Services. So five new logos, three of them are from Retail and two of them are for the Agile program management for Indigo Blue.
- Amar Maurya:** Okay. So meaning through this Indigo Blue there is a little bit of cross selling which we had started, right?
- Sudhakar Ram:** No, this is not cross selling, this is Indigo Blue's own business.
- Amar Maurya:** Okay, own business. Sir but then the acquisition which we did of Indigo Blue is primarily because by this we will having opportunity of cross sell as well as extending the line of our services. So can you give us some flavor about when we can see the impact of this actually percolating the whole system?
- Sudhakar Ram:** Our business always takes a couple of quarters before you can see that, but there are opportunities which we see in the market.
- Amar Maurya:** So sir what will be the growth trigger, when we say that in the last quarter that industry we'll be either matching industry level growth and considering that the first quarter is quite muted,



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are we still confident or what makes us confident that we will be actually meeting that industry level growth?

Sudhakar Ram: See basically we have to see how the pull through revenues out of Indigo Blue come which can be a step up and we are expecting some large Government programs to close which could be another.

Amar Maurya: Okay. So meaning Indigo Blue is one trigger and Government program will be another one which will help us to... So by then we can see this Government program rolling out, probably in the second half or the first half?

Sudhakar Ram: Second half of the year.

Amar Maurya: Second half of the year, is that correct?

Sudhakar Ram: Yes.

Moderator: Thank you. Our next question is from the line of Pooja Swami Span Capital. Please go ahead.

Pooja Swami: Firstly on the LPT JV, as you mentioned this quarter we have recorded a loss of Rs 10 crores from that business, this is the soft launch of this business, further on when we are planning to do the full launch by September do you think as soon as we launch the full version of this will we be profitable or we will continue with the losses for some extent?

Joe Venkataraman: So the breakeven point has to come later in the year and it is all a question of when the take up happens and what level of take up happens. But one thing is that we are not going to increase any cost of operation between what we have been incurring now to what we are going to be in the next quarter. In fact we are trying to cut down the cost so that most of the costs have been in the area of development which has been taken away now but the support cost do exist. So I think as I said instead of predicting how the market take up is we would like to wait for this quarter to see how the initial, the next two launches are and you will get a fair reflection of where we stand at that point in time.

Anant Thakrar: So Pooja, I will just add a couple of points on to that. I think we have made a significant investment in the JV and it is a mid to long-term play there, so we expect value coming from it over a period of time and I think it will be valuable to the organization but I think it is a mid-term play there, so that's where our expectations should lie.

Pooja Swami: Okay. But the 1.6 million transaction on an annual basis what you said, so for a breakeven kind of result what is the minimum transaction you would expect?



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- Joe Venkataraman:** There are various plays, what I would request you is that to hold on to this for a quarter, we are trying to breakeven at as low volume as possible. But if you would not mind we will come back with a clear picture to you in a quarter's time.
- Pooja Swami:** Okay, that would be fine. Secondly sir on the Indigo Blue, in the Press Release that type of acquisition we had run rate of GBP 6 million of yearly revenue for Indigo Blue, right?
- Sudhakar Ram:** That's right.
- Pooja Swami:** With the present quarter Rs 10 crores of revenue what we have added gives us the same color, so for the year what is the kind of growth you expect in this business, like is it expected to add a similar kind of revenue or do you expect some kind of growth in this business?
- Sudhakar Ram:** So right now we are looking at a revenue run rate at about £0.5 million a month and it should improve over a period. But there are integration issues, market acceptability, all those things that will take time for the market to completely understand the story but we have pass it up about the impact of that on Indigo's core business.
- Pooja Swami:** And are you planning to bring out this business to other markets of our Mastek?
- Sudhakar Ram:** Yes, we are but not immediately, once we establish ourselves and we have that momentum then we will bring it to other markets.
- Pooja Swami:** Okay. And final question sir, on the cash what we are holding at present around Rs 155 crores, any investment plans in recent or any inorganic plans?
- Sudhakar Ram:** As you know we are looking for inorganic opportunities and that Rs 155 crores is not fully cash because it includes Majesco investment.
- We will have to time Majesco investment and see what are the strategic opportunities that they can leverage if they ever want to divest that holding of Majesco. So we are obviously looking at growing both organically and inorganically.
- Pooja Swami:** And any specific markets you are focusing for this inorganic growth?
- Sudhakar Ram:** Right now it is certainly the UK, at some point we will have to make a strategic investment in the US because as of now Mastek has no presence in the US, whatever business we had is now under Majesco so we need to restart our business in the US.
- Moderator:** Thank you. I now hand the floor back to Mr. Sudhakar Ram for closing comments. Over to you sir.



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Sudhakar Ram:

Thank you and thank you all for attending. I know that there are a series of calls today so stay tuned, I think we are pretty optimistic about the Solutions business as we are about the Insurance Business and we will see this line of business also stepping up and growing over the next few quarters, but we will keep sharing it with you every quarter. Thanks and see you next quarter. Bye.

Moderator:

Thank you very much sir. Ladies and Gentlemen, that concludes the Mastek Limited conference call. Thank you for joining us and you may now disconnect your lines.