

KPIT CUMMINS INFOSYSTEMS LTD.
Q2 FY05 EARNINGS CALL
OCTOBER 21, 2004, 4 P.M.

Moderator: Good evening ladies and gentlemen I am Parul the moderator for the conference. Welcome to the KPIT conference call hosted by Tower Capital. Mr. Sandeep Shah of Tower Capital is your call leader today. For the duration of presentation, all participants' lines will be in the listen-only mode. I will be standing by for the Q&A session. I would like to hand over to Mr. Sandeep Shah of Tower Capital. Thank you and over to Mr. Shah.

Sandeep Shah: Thanks Parul. Good afternoon everybody, on behalf of Tower Capital, I welcome you all to KPIT Cummins Q2 FY05 earnings call. We have with us today senior members of management team including Mr. Ravi Pandit, Chairman and Group CEO, Mr. Kishor Patil, CEO and Managing Director, and Mr. Anil Patwardhan, General Manager Finance. Without taking further time, I would now like to hand over the call to the management, over to you Mr. Ravi.

Ravi Pandit: Good afternoon everybody. I trust you have received our investor update and the performance matrix. What I would like to do is to very quickly take you through the information that we have given to you without going into the individual details. I would comment on some of the major variations that have happened and after about 10 minutes of my talk maybe we can then get down into question and answers. If you look at the broad parameters of performance what we have talked about in our update is we have talked about the revenue, we have talked about profitability, we had talked about our verticals and clients and practices, and thereafter we have gone for a new guidance, for a revised guidance. You would notice that on the top line basis on a consolidated basis our revenues have gone up 107% as compared to last year, which is inclusive of the growth coming out of Panex. If you exclude the Panex growth then our growth on year on year basis is in the region of 60-65%. Inclusive of Panex our quarterly growth rate, sequential growth rate is roughly about 1.5 %. Exclusive of Panex, our sequential growth rate is 8%. Let me comment on this first and then go down into the composition of the growth, consolidated and un-consolidated. You would recollect that in our initial guidance for Panex we had said that at the end of the year we would have a total top line of roughly 13 million USD, where as in the first quarter our top line was almost 4.1 million USD. So, we had anticipated total top line of Panex going down over the year primarily on account of two reasons, which is what we talked about last time, one is increasing offshoring from Panex to India, thereby reducing the top line, and secondly on account of some unusual project, one-time project that we had in the first quarter, the result of that has been seen now and the total top line of Panex has come down for the quarter from 4.1 to 3.5. This is in accordance with our initial estimate. If you look at the growth within KPIT outside Panex, then on a quarter on quarter basis our top line has grown by roughly 8.37%. This is inclusive of the growth that has happened in Cummins account as well in non-Cummins accounts. Our growth in Cummins account has been to the tune of roughly 26%; where as our growth in non-Cummins account has been only about 1%. The 1% growth in non-Cummins star accounts essentially relates to the ups and downs that happen on account of various milestones, and we believe that individual account-wise, there is a strong growth and growth potential in the quarters to come, whereas there has been some matching of ups and down within them as a result of which on an average we have grown 1% outside of Panex. Coming to the profitability part, the increase in the total top line of a little over a crore, crore and a half, from last quarter to this quarter has two compositions, one is increasing offshoring from Panex to India, and secondly slight increase in the total top line. The combined result of both of

them has been additional creation of contribution more or less all of which has been added to the total bottom line, as a result of which the profitability has gone up, that has resulted in slightly higher return on sales during the quarter as compared to the sequential quarter. During the quarter, we have also added some customers, two in the auto-embedded practice and two in the risk management practice, and I will talk about the risk management practice in a minute. So these have been the new addition during the quarter, four new customers during the quarter. A major new practice, which has been started during this quarter, is the risk management practice. As a matter of fact, we have been working on building this practice for the last two and three quarters and we are seeing some growth coming from this practice during this current quarter. The practice is driven by the fact that increasingly larger numbers of companies are now concerned with compliances and risk management, a main driving factor therefore being Sarbanes Oxley compliance. So considering our accounting background, we have found it easy to grow into this area. The services that we deliver in Sarbanes Oxley related areas relate both to pure IT as well as into the control area. So both these areas have picked up as a result of which you know we see some growth in this area. This being the initial part of the practice, a lot of the work is done onsite and you would also see this reflected in our onsite-offshore composition. We have also begun efforts to make this practice more offshore based, the results of which we will see after sometime. So we see this as a good growth area and a growth area, which over a period can give us substantial advantage as well as some degree of uniqueness. We had mentioned in our earlier call about the VLSI practice and we had mentioned that we have started building a Bangalore Development Center. During this period, a small amount of billing has begun on the VLSI practice, but it is nothing very significant as of now and we believe that till the end of the year we will see some movement in this area. During the quarter, we have added 127 employees taking out total number to 1247 inclusive of Panex. We had spoken in the last call about the infrastructure that we are building. We are building the first phase of our infrastructure, which will now house 1500 people and a total premises of about 150,000 square feet are getting ready. We believe they will be operational by the end of this calendar year. We have also given a revised guidance for the year where we have upped it inclusive of Panex, we have upped it from 230 crores or 2300 million to about 2450 million. We believe we should be in a position to be in step with this guidance. With this I have covered the broad areas about the current quarter's performance, I will be most happy to take any question going forward. Thank you very much.

Moderator: Thank you sir. We will now begin the Q&A interactive session, participants who wish to ask questions please press *1 on your telephone keypad. On pressing *1 participants will get a chance to present their questions on a first-in-line basis. To ask a question, please press *1. Our first question comes from Mr. Sanjeev Kapoor of Sharekhan.

Sanjeev Kapoor: Hi, I just wanted to understand, you said that, if I look at the star customers other than Cummins, I am getting a decline, if you could elaborate on that.

Ravi Pandit: Yeah Sanjeev, as I mentioned to you different customers billing during a particular quarter depends on the milestones that get crossed during that quarter. So there are cases where work continues to be done but the milestone is met after the end of the quarter and the billing gets done later. In the project that we are doing with all our customers, there is no decline in the number of people who are working on projects, but some of that billing has got postpone because of different milestones. So this is relating to general ups and downs that happen from account to account. In addition to this what has happened during this quarter, and this is what we had anticipated, was that the Panex onsite work has gone down as we had anticipated. So a part of that total star customers

billing which related to Panex onsite work has also gone down, so these are the two factors which has contributed to the de-growth in the non-Cummins star customer accounts.

Sanjeev Kapoor: I know if I have just to say that you know there is been shift of lets say largely the HP work which is done onsite at Panex has been shifted to offshore that is what you are saying.

Ravi Pandit: That is one part of the reason.

Sanjeev Kapoor: Okay; now if I look at your onsite-offshore revenue, okay, I see a decline in offshore revenue.

Ravi Pandit: Yeah, as I mentioned a significant part of the increase in the onsite revenue is on account of the risk management practice that we have started. And in the first phase of this practice relatively larger number of people are onsite. We see that practice getting more offshore over a period of time not in the immediate time. So the total onsite-offshore numbers are inclusive of multiple factors, not all of that is relating only to the HP offshoring.

Sanjeev Kapoor: No, what I am saying Ravi is that if I look at your HP account, it was somewhere around 15.2 crores last quarter, it has come down 12.3 crores. Correct? Now, if I look at the offshore revenue it has declined from 18.9 to 18.5, if I have see that 15.2 going down...

Ravi Pandit: No I don't know how did you get to the HP revenue figure.

Sanjeev Kapoor: I am talking about the top client 20% of your revenue.

Ravi Pandit: Anil can you...

Anil: See I believe you are referring to the top client other than Cummins as HP.

Sanjeev Kapoor: Yeah, that's right.

Anil: Yeah, so we were at 25% compared to that now we are at 20% in Q2 and as mentioned by Ravi, we have seen certain projects which were executed in Q1 that was the feature of Q1 only, and going forward we are continuing with our business, which we intend to finally offshore.

Sanjeev Kapoor: No, you are not getting, the 15 crore has come down to 12 crores, it is because of offshore.

Ravi Pandit: Yes, as I mentioned two things have happened in the Panex area, you would recollect that in the first quarter our total Panex revenues were 4.1 million.

Sanjeev Kapoor: Correct.

Ravi Pandit: Our guidance for the year on Panex is not 16 million but it is 13 million. As I mentioned, the decline in the guidance as compared to the first quarter was on account of two factors, one was change in the onsite-offshore mix, and second is the completion of some one-time projects, which existed in first quarter which we did not expect to continue during the rest of the three quarters. That is reason why we gave a guidance of 13 million for the whole year as opposed

to 4.1 million in the first quarter. Now both these factors anticipated earlier have cleared out during this period. That has to a certain extent contributed to the reduction in the HP account. The increase in the onsite as compared to the offshore is the net of various factors, which includes on one side a certain amount of increase in the HP offshoring but a large amount of increase in the onsite on account of some of the new practices as well as the increase in some work in our other star customers where at the initial phases we are doing some more work onsite.

Sanjeev Kapoor: Ravi, I am understanding on the Panex front, what I am asking is, if there is a onsite being shifted to offshore of 10x, I would have seen some improvement in the offshore absolute number, which I am not seeing.

Ravi Pandit: No, as I have explained to you the offshore actual absolute numbers are a composition of variety of factors, it's not just a single factor, which has contributed to it.

Sanjeev Kapoor: So is there a particular account, which has degrowth in.

Ravi Pandit: Yes, you know, we had made a discussion on this in the last call. See if one were to look at individual accounts billing going up and down, one would see that quite often the billing is affected by the milestones in a particular period.

Sanjeev Kapoor: Okay.

Ravi Pandit: And some milestone get achieved before the end of the quarter some after the end the quarter. At the last conference call, we were at pains to explain that the fact that Cummins has not gone up does not mean that there is no potential in Cummins, but we had said that there are milestones, which don't match with the quarter end. We have a similar situation in other accounts.

Sanjeev Kapoor: Okay, and secondly if I look at, is there decrease in Panex employee size.

Ravi Pandit: Yes.

Sanjeev Kapoor: Okay, there has been some decline of some 20 some odd number which gone up, because if I look at this I think your total addition has been somewhere around 127 but if I look at along with Panex it is 100, so there is 27 people who have left Panex.

Anil: Yes. Basically as I told you in Q1 we had a project, which was executed in that quarter, and naturally at the end of the project, those people have not been with us.

Sanjeev Kapoor: Okay, so this is some trend, which will continue with more and more offshoring happening.

Ravi Pandit: As I mentioned earlier this is a composition of two factors, one is one-time projects not continuing and second one is some offshoring, so composition of both of that we play out during the year.

Sanjeev Kapoor: Okay, thanks a lot.

Ravi Pandit: Thanks you.

Moderator: Thank you sir. Our next question comes from Mr. Pratish Krishnan of SBI Capital Market.

Pratish Krishnan: Yeah hi, can you just give an update on the VLSI center in terms people, in terms project, like you know client addition kind of things.

Kishor Patil: Yes, on the VLSI center, we have got now about 35 people currently based in Bangalore, and we have started two projects, one with existing customer and one with new customer and basically these are kind of a pilot projects. What we have been in the position to do is setup our processes, setup our methodologies for VLSI business and contact all our existing and prospects, which are targeted customers. We have got project managers and you know other management team in place and infrastructure in place and we believe that this pilot projects will give us more referencable projects in future from the 10 customers and other customers.

Pratish Krishnan: And you know, on the Panex front, I mean, if you will be able to quantify you know in terms of the offshoring, I mean like out of this roughly \$3 million, I mean how much you will do offshore and kind of...

Ravi Pandit: As we had mentioned last time, on an annual basis, we are looking at a total top line of Panex to the extent of 13 million.

Pratish Krishnan: Okay.

Ravi Pandit: We are excepting total offshoring by Panex to India to the tune of 1.5 million.

Pratish Krishnan: Okay.

Ravi Pandit: As compared to 600,000 in the last year in terms offshoring to India and as compared to 9.25 million of the total top line for Panex last year.

Pratish Krishnan: Okay, but totally you are on track or...

Ravi Pandit: Yes we are on track.

Pratish Krishnan: Okay, and lastly in terms of the embedded revenues, I mean, what is the contribution from the embedded revenue, percentage of sales.

Ravi Pandit: Actually, we don't look at individually areas and revenues there for, but we have a significant team, almost to the tune of roughly 180-190 people in total embedded area.

Pratish Krishnan: Okay, the reason I was asking you know you got up before I mean you had two clients addition in the embedded space.

Ravi Pandit: Yeah.

Pratish Krishnan: And probably if I am not mistaken, we had something like 20% from embedded coming through, broadly as it improved, I mean, like have this client started billing and...

Ravi Pandit: Yes, but you know in the initial phases for the first or three quarters, the growth is not to be substantial because the pilot projects keep on happening and that has been the trend over the last three quarters, two-three quarter or so. During this quarter we have added two more client on the embedded side, but here again we will see substantial numbers coming in only after two or three quarters.

Pratish Krishnan: Okay, thanks a lot.

Ravi Pandit: Thank you.

Anil: Thanks Pratish.

Moderator: Thank you very much sir. Our next question comes from Mr. Vikas Mantri of SBI Capital.

Vikas: Hello Ravi.

Ravi Pandit: Hi Vikas.

Vikas: Yeah I had a question, in the sense if you, when you are offshoring from Panex, those revenues are booked under Panex account or is that under KPIT Cummins.

Ravi Pandit: Yes, actually what happens is that they booked in Panex, and when KPIT does the billing they are obviously booked as expense in Panex and income in KPIT and then we consolidate we eliminate the double billing.

Vikas: So your \$3 million are only onsite income of Panex.

Ravi Pandit: No, it includes the income of Panex from end customers, a part of that is on account of offshore services, so that gets booked as also an expense in Panex and income in KPIT and we nullify that when we consolidate.

Vikas: Okay, and I see your guidance for the revenues and PAT figures. Your guidance is just around if you see growth that you are expecting is just 3% in the top line which could be explained by the offshoring that you were doing, but your PAT margins or PAT also increased is just 3 to 4%, so I do not see that coming into your PAT.

Ravi Pandit: Yes that is true. As a matter of fact we are expecting that our investments in various areas will continue to happen during the rest of the year and we would rather charge off those expenses on an ongoing basis.

Kishor Patil: And we are also having our major facility, which is getting occupied during this period. So we are also factored in some additional expenses on account of that in the initial period till it is fully occupied and utilized.

Vikas: Okay and what is your employment plan, what is the kind of numbers are you looking forward in next two quarter and thereafter, people that you will be taking in.

Anil: By close of year we are looking at anywhere close to 1400 people and currently we are at 1240.

Vikas: Okay.

Anil: I see almost 100 or close to 100 people getting added over next two quarters.

Vikas: Okay, thank you Ravi.

Ravi: Thank you.

Moderator: Thank you sir. Next is a follow-up question from Mr. Sanjeev Kapoor of Sharekhan.

Sanjeev Kapoor: Hi Ravi.

Ravi: Hi Sanjeev.

Sanjeev Kapoor: If you look at Cummins account, the numbers have been very good in this particular quarter, you are always doing somewhere around 5 million this quarter. If I annualize it, we are looking at about 20 million number. If you could just say how do you see this particular account in FY06, particularly...

Ravi Pandit: Sanjeev, I would caution against multiplying the quarterly figure to an annual number. We have estimated Cummins till the end of the year to be in the region of 17-18 million. A particular quarter the billing happens, in the next quarter the billing may not happen although the work may happen. So I would not kind of extrapolate from this one quarter to the whole year. Our initial anticipation for Cummins was 30% growth over the last year which was like 17 to 17.5 million, we are expecting a marginal increase when we have given the revised guidance but we are not saying that Cummins will end at 20 million at the end of the year.

Sanjeev Kapoor: Can you just say what will be the growth would be in the Cummins account in FY06.

Kishor Patil: When we had, you know, acquired Cummins Infotech, at that point of time we had given a take that by 07, we expect Cummins revenue to go up to 30 million, I guess you should do something in between.

Sanjeev Kapoor: That is 30 million by FY07.

Ravi Pandit: Yeah 06-07.

Sanjeev Kapoor: Okay, thanks sir.

Ravi: Thank you.

Moderator: Mr. Kapoor.

Sanjeev Kapoor: Yeah, that answered my question.

Moderator: Okay, thank you sir. Participants who wish to ask question, please press *1. Next is a question from Mr. Rahul Chadda of Aviva Life Insurance.

Rahul Chadda: I am saying congratulations on good set of numbers.

Ravi Pandit: Thank you Rahul.

Rahul Chadda: Just couple of queries, what is current utilization rate and also if you could tell us in terms of the traction with other key clienteles which is Unilever, Capital One, Deutsche Bank, and BNP Paribas, in terms **of are** we increasing the size of the engagements and what are the works we are doing with these clients.

Ravi Pandit: In terms of the utilization numbers, we continue to be in the region of about 75-76% offshore and 96-97% onsite. In terms of individual customers, I would request Kishor to take that.

Kishor: Yeah, I mean, we are looking at year-on-year growth in most of our star accounts. I think on quarter to quarter basis sometimes there is always ups and downs, but in all these accounts we are expecting average more than 50% growth on non-Cummins customer accounts. So we are looking at good growth in all these accounts and even next year, now there may be a variation in the individual accounts, but as a group of non-Cummins accounts we are definitely looking for growth of more than 50%.

Rahul Chadda: ...times into different geographies also or is it the same entity within the group, which is increasing in the client engagement size basically.

Kishor: We are definitely penetrating different businesses and different geographies for these customers. We are also looking at getting in to new and different practice areas for these customers, and our increasing the practice offering is inline with that. So we are looking at penetration in terms of geography, businesses, and the new practice areas. So we are definitely making progress on most of these accounts with all the star customers.

Rahul Chadda: Also you were looking in the past to tap sister companies of strategic relationships of Cummins, what has been the development on that front.

Ravi Pandit: As I mentioned last time we would continue to be on look out for a strategic alliance but we don't have anything on the anvil or on the horizon right now.

Rahul Chadda: And you said you see a visibility of at least 50% growth for next two years in the non-Cummins star customer's profile.

Kishor: What I mentioned last time was that we are looking for more then 50% growth on year to year basis in this year over last year in non-Cummins accounts, and we expect a significant growth even in future from these accounts.

Rahul Chadda: Fine sir.

Ravi Pandit: Thank you.

Moderator: Thank you sir. Next we have a question from Mr. Deepak of Wow India.

Deepak: Sir, what we were wanting to know is the US economy is still in kind of, or situation where things are not clear as to whether it will go which side, now would slowing US economy make Cummins business grow faster for us or things would just stop as it did three years ago.

Kishor Patil: See this, I believe that the scenario is different for different types of customers and depends upon their strategy. Now, you know, there are certain customers who are committed to you know what you can say global sourcing, and once they have decided on a medium to long term strategy, they look at accelerating this growth. So in terms of Cummins, Cummins is committed to global sourcing and, you know, working with global vendors on outsourcing of different services. So I believe that it will not have much relevance in terms of overall performance of economy, and I guess we would continue to grow.

Ravi Pandit: You would also recollect possibly the press release and the media meet that Cummins' chairman had and were they explained that they are looking at 150 USD millions of offshoring to India of various parts and components inclusive of software. So Cummins as a global strategy has decided to go for global sourcing and for which we see business coming our way.

Deepak: Could you please comment on this auto embedded space as to when you said you got two customers, could you just tell us what is the kind of growth you are seeing there, or is this just one off niche product where the growth will probably be large in initial years and then just you know taper off, or could it be the business engine growth for the next may be 10 years for KPIT.

Kishor Patil: See in the auto area there are various trends that are taking place. One of them is definitely; overall in the industry there is quite a cost pressure. So most of these companies have been pioneers in setting up or working with global vendors into R&D efforts. This pressure is also building up on account of two reasons, one reason is more and more electronic switches being embedded into cars, and hence the need for embedded software. And the second is the emission guidelines, which are coming into US as well as Europe. So we believe that there will be a significant opportunity for at least next five years in this sector, and in order to tap this we are focusing on to all the geographies, which are very relevant and important, one is United States of course, and we are also increasing our efforts in other markets like Germany and Japan.

Ravi Pandit: If you look at the electronics in automotive, the prediction is that by the end of this decade average car will have \$4000 worth of electronics. These electronics will come for better fuel efficiency, it will come for less emission, it will come for global positioning system, it will happen for safety, for security of the cars, for infotainment, and all these areas present phenomenal scope for growth in electronics, and we believe that this is an area which will grow. We are, however, focused essentially on engines and on power tray. So these are the areas where we are focusing on and we see growth in the years to come.

Deepak: Sir when you said \$4000 worth of electronics, what's the component of software in that, what is the billable part....

Ravi Pandit: See, if you see the growth in the electronics industry, a significant part of all electronics is in the form of software because the hardware is getting streamlined, and you see this electronics in large, in up-market cars just now, you would see going forward that coming into the mid market cars, that is what the industry is predicting.

Deepak: What's your revenue from that segment as of now and say from five years from now do you see that maybe growing five times?

Ravi Pandit: I am not sure whether we can say it will go to necessarily five times but we see significant grow going forward, Kishor!

Kishor: Yeah, I mean this is one area where we are looking at more than average growth as compared to other practices.

Deepak: What would be revenues form this stream as of now, sir?

Kishor: About 20%.

Deepak: 20% of total?

Kishor: Yeah.

Deepak: It's about 18% in terms of number of people.

Kishor: Yes.

Moderator: Mr. Deepak, are you through with the question sir?

Deepak: Yeah. 20% of the total revenues from this segment sir, or the number of people are almost about 17% or 16% of the total?

Kishor Patil: Yeah, its in that range, you know, yeah.

Deepak: Okay, that's all from me thank you.

Moderator: Thank you sir. Next in line is a question form Mr. Depen Shah of Kotak Securities.

Depen Shah: Congratulations on a very good set of numbers.

Ravi Pandit: Thank you.

Depen Shah: In fact most of the questions have been answered, but just one, in fact, I was slightly late on the call, so I apologize if it is the repetition, but can you throw some more light on new service line which you have started that's in the finance segment, and the two customers which you are right now serving in risk management, just some flavor over what kind of work are you doing?

Ravi Pandit: Essentially Depen, what we are working on is in the Sarbanes Oxley area. This involves laying down control objectives in the light of section 404 of the Sarbanes Oxley Act.

Assessing the existing controls, IT-enabling those controls, and working out systems to make sure that those controls are in existence going forward. That's the nature of work that we do in Sarbanes Oxley. The people that we have working in this area are IT specialists and some others are control specialists, so that is the area that we operate on.

Depen Shah: And any flavor about the type of customers, which you have right now?

Ravi Pandit: Actually this is for almost for all range of customers, and every company listed in the US has to go through the Sarbanes Oxley compliance reports, so we see this for every US based customers.

Depen Shah: And any successes on the Basel II front or are both the customers in...

Ravi Pandit: No, actually presently we don't have any significant work on Basel II, it's more on Sarbanes Oxley, but we see that as a potential opportunity.

Depen Shah: And just reconfirmation of points which we have discussed earlier, the margins, operating margins have moved up by about 200 basis points during the quarter, is there any, as to, how much can it improve further, what's the target for the company?

Ravi Pandit: You know, till the end of the year we have kept more or less the same guidance on our ROI. There might be some improvement but I think there will also be investment going forward.

Depen Shah: But say over the next couple of years, do you see yourself...

Ravi Pandit: Over the next couple of years, we do see growth happening driven by the increase in our scale, but as far as this year is concerned we have kept the ROI guidance more or less the same as to where we are now.

Kishor: We also definitely intend to increase our offshoring percentage over next few years and that will also increase the margin.

Depen Shah: And any take on having a strategic partners like Cummins in the BFSI space.

Ravi Pandit: We have, Depen, if you remember we have always said that that is something that we will look for, but that is not something which is on the horizon right now.

Depen Shah: Oh it's not on the horizon as yet, I thought you were just looking out for somebody right now?

Ravi Pandit: Yeah, we are looking for somebody, but we don't have a candidate on the horizon Depen.

Depen Shah: Okay, you don't have a candidate.

Depen Shah: Okay, I thought it is on the back burner now. Okay, thanks very much and all the best.

Ravi Pandit: Thank you Depen.

Moderator: Thank you sir. Next is a question from Mr. Ravi Dharamshi of Rare Enterprise.

Ravi Dharamshi: As you mentioned earlier that there was some part of work, which was done for non-Cummins account, which was not billed during the quarter, if you would just quantify that part of it, because essentially that shows, otherwise the non-Cummins accounts, the growth has been somewhat sluggish in that sense or..

Ravi Pandit: See Ravi as we mentioned last time, if one were to look at the figures of billing of individual account on a quarter-to-quarter basis, it actually does not give a clear indication about the nature of growth in that account. Because some part of the billing is milestone based and only some is purely time related. In our accounting system, we do not capture work done but not billed; we capture only the work billed.

Ravi Dharamshi: Sir, could you quantify the volume growth there?

Ravi Pandit: We can't quantify that and we don't want to put it also as a part of our accounts because its not an as firm a ground as actual billing that we do. So I would rather keep it on the basis of actual billing that we do than on the basis of you know quantification of the work done but not billed.

Kishor: And As we have said earlier, I mean, our non-Cummins accounts are expected to grow faster than Cummins during the year, and we are continuing to expect that growth from non-Cummins account during the year.

Ravi Dharamshi: Thank you.

Moderator: Mr. Ravi.

Ravi Dharamshi: Thank you mam.

Moderator: Thank you sir, next inline, we have a question from Mr. Sukhwinder Singh of Amit Nalin Securities.

Sukhwinder: Hi good afternoon, congrats on good set of numbers.

Ravi Pandit: Thank you.

Sukhwinder: Sir it is regarding the Panex account like when we work out the net profit margins of Panex it appears to be in the range of 3 to 4%, which is very low compared to the average of 11 to 12% of the whole company.

Ravi Pandit: Yes.

Sukhwinder: How much improvement we can have from hereon and any timeframe for that to happen.

Ravi Pandit: Yes, if you were to look at our guidance for Panex, you would see that even for the US \$ 13 million top line, we are predicting a marginal quarter of a million dollars of total bottom line, but that is not the total profit that we get from the Panex merger. As I mentioned earlier, we are expecting some offshoring of the revenues from Panex and the profit of that is captured in KPIT books. So we don't look at Panex merger from the point of view of reported profits in Panex alone, we also look at it from the point of view of the income that it generates within KPIT Cummins because of its offshore model.

Sukhwinder: What is the reason for the increase in equity capital from 6.03 crore in June to 6.47 crore, and I also want to know regarding the attrition rate of the company.

Anil: See basically the increase in equity is on account of two things, if you remember in the last call we mentioned about the Cummins options getting exercised, so that is the part of my equity as of 30th June and now going forward the Panex has exercised their first lot of options which is 76000, which is also a part of my equity as of 30th September, so as of end September our total equity is close to 6.4 million.

Sukhwinder: Attrition rate.

Anil: Attrition rate is between 16 to 18% as of now, and as I told you that attrition also within the good performance people, which are say at the higher end of the performance and the people who are at below performance, the attrition rate is again different in that.

Sukhwinder: Okay thanks.

Moderator: Thank you sir. We have our next question from Mr. Sundhanshu of B&K Securities.

Sudhanshu: Yeah, hi sir and congrats on the good improvement in profitability.

Ravi Pandit: Thanks Sudhanshu.

Sudhanshu: I just wanted to understand something about the Cummins account. See as far as the milestones are concerned, maybe getting reflected in offshore revenues or in particular account specific accounts, you know, we haven't seen any of this thing in the last year if I am not wrong.

Ravi Pandit: Can you explain what you mean?

Sudhanshu: What I mean is that as far as the growth rate is concerned, okay, or may be some accounts remaining flat in non-Cummins or in Cummins, we haven't seen that kind of a thing happening last year as far as, you know, milestones varying with quarters and therefore the billing getting reflected, so my question really is that is it that within Cummins account our incremental work is really based on project and not the annuity stream, which we were getting last year and therefore we have, you know, therefore quarter on quarter incremental projects renewal maybe onsite, that is what is making a difference and increasing the billing with us.

Ravi Pandit: No actually, see it is only in the case of Cummins on account of our special relationship that we speak about the billing for Cummins on a quarter-to-quarter basis. When that gets spoken, the ups and downs that happen normally in any account, kind of, get highlighted. If you

were to see, in the case of any normal company, quarter-by-quarter billing for any individual client, you would in all probability see this ups and downs happening everywhere. What happens typically is that when you lump all the clients and put them together, then you see an overall global trend. If you would recollect, we had a discussion on this in the last conference call, and I tried to explain to you that the fact that we had low billing in Cummins in the last quarter does not mean that the growth potential in Cummins has gone down. We believe that the total numbers of Cummins will continue to be what we had initially estimated. Similarly, we also believe that the total numbers in non-Cummins will also be on the lines that we estimated, but we urge you not to look at individual customer's performance on a quarter-to-quarter basis because the realization variation, the billing variation is a fact of life with almost every account.

Sudhanshu: Sir, certainly, you know I appreciate that, but in our case what happens is that Cummins contributing, say excluding Panex contributing 45% plus to our revenue, so that account really is under the microscope.

Ravi Pandit: I appreciate that.

Sudhanshu: So what I really I am looking at is that you know over the last year the growth has been pretty phenomenal in that particular account. We have mined it very well. We have gone to maybe you said not to annualize it, but still we have gone to revenue momentum of close to \$20 million. So, what I am looking at is that now as far as the Cummins account is concerned, you know, quarterly variations definitely will happen, but are we saying that on a yearly basis, value-based growth will it happen or not is it difficult to say? You know what I am saying right.

Ravi Pandit: No, I don't understand.

Sudhanshu: You know what I am really trying to understand is that do you expect Cummins account say for the next one year, I am especially looking at say FY06, the kind of visibility we have, would you say that the growth will now be contingent upon us tapping the various partners or affiliates of Cummins rather than Cummins itself?

Ravi Pandit: We had looked at Cummins account to the tune at \$17-18 million during the current year. Our growth in that is on target and it is not contingent upon some factor that we don't have a firm handle on just now.

Sudhanshu: You know, maybe I was looking at beyond this year, this year definitely we will get there if we show a decline

Ravi Pandit: As we said a little while earlier, we expect Cummins to contribute roughly \$30 million in the year 6-7. We expect it to contribute \$17-18 million this year and we expect the middle year to be somewhere in the middle.

Sudhanshu: Okay, you know, sorry to beat so much on this particular factor, but just wanted to understand one more thing that Cummins as a customer, I mean who was the major global vendors who right now work with Cummins will be having some perspective because I think there was a recent news item about it, renewing its contract with one of them. Does that have any impact on us?

Ravi Pandit: No we don't expect that.

Kishor Patil: See any global corporation of Cummins size has a multi-vendor strategy and even companies who have their own fully owned kind of center in India, they do organize other vendors. So, there is no impact on us at all of this strategy, of any such renewal of relationship, and actually you know to answer your question in a different way, all our business in any of our business is based on client relationship, it is based on our multi-year contracts, but ultimately, the business comes on project-to-project basis and the variation is only on the basis of fixed-price projects, but in future also we do expect that the Cummins continue to move work more offshore and we get a fair share of that.

Sudhanshu: Okay. No, I was only asking it on the perspective that so many global vendors are actually building up such a huge offshore base, so that does have any impact on us, no surely, okay I appreciate that. Also, on the non-Cummins star customers, can you comment broadly upon the nature of work, you know what is the kind of niche or specialization that we are offering to them because all the names are like multibillion US dollar corporations?

Ravi Pandit: Yes, can you ask the question.

Sudhanshu: Sure, Ravi my question really is that within the non-star Cummins customers; broadly speaking could you just underline that which are the service lines or what are the chief areas of work in which we service those customers; you know because all of these customers are really youth customers and surely, you know, we have seen preference across the vendors, across the clients or large vendors. So, what is the specialization or niche that you are offering them, if you could just comment on that?

Kishor Patil: See we have all these star customer some kind of a long-term relationship and we are definitely trying to focus on our niche skills in the different practice areas. So, we are looking at areas such as business intelligence, data warehousing. We are looking at, and as you know the Panex has also added to our abilities in this area especially on SAP. We are into auto embedded area, automotive and embedded area; we are into pure embedded work which is for industrial automation; we are into work such as ERPs; we are into work in terms of e-business area; so, these are some of the areas in which we are working, and broadly this work could also fall into areas such as development projects and maintenance projects, so what you call as build the corporation and run the corporation, so we have a fair share of both these kind of work based on the budgets of this company.

Sudhanshu: Okay, and I request Anil now, if you could just take us Anil through the balance sheet, you know after especially the assets or rather Panex has been integrated, how does the balance sheet look now?

Ravi Pandit: Can you explain, when you say balance sheet, what part of balance sheet you are looking at?

Sudhanshu: Basically I am looking at you know in terms of data or has any goodwill come in, how have the assets gone up, just the rudimentary skeleton balance sheet if possible, could you give out the figures; what is the cash we have?

Anil: Okay, just to answer your question with respect to receivables and with respect to the cash, as I mentioned in my matrix also, we are currently at 81 days and our receivables are close to Rs.45 crores, okay, at a global basis, and we have the cash balance of close to USD 3 million in our balance sheet, and because of Panex merger, there is absolutely no goodwill in my books; what we acquired is their net worth and whatever stocks or options we have given, that is our investment in that subsidiary as of the investment date.

Sudhanshu: Okay, sure. Thanks a lot.

Anil: Thanks.

Moderator: Thank you sir, next we have a follow-up question from Mr. Sanjeev Kapoor of ShareKhan.

Sanjeev: I was just going through your press release; you spoke about increase in selling expenses, if I look at your marketing people, there has been decline; can you just tell me about that?

Ravi Pandit: Can you explain where you say there has been a decline in the marketing people?

Sanjeev: If I look at your matrix, you support, your marketing subsidiaries, I look at down from 21 to 20 and including Panex is 28, they have gone down to 24.

Kishor Patil: Yeah, the first thing is there are few things which we are doing, one is we are moving most of the share services work for our subsidiary also back in India and we are investing more into separate staff which is based on account management as well as new sales. So typically, the staff that is based on account management does not fully reflect into our marketing staff because this staff is more focused on getting more business out of existing customers. So, our overall expenses on marketing have increased and the type of people that we are engaging, it is also different than what we had. So basically, we are definitely making sure that what we are investing into different subsidiaries and offices is more for new account penetration and the other kind of staff is staff functions are moved to India.

Sanjeev: And why there has been a decline in general and administration expenses from Rs.10.8 crores last quarter to Rs.10.2; tell me what has really happened there?.

Anil: See, there is prominently only one reason, is in the last quarter, we have hired some new facility, okay, and in the quarter which we had the facility, certain administrative costs are higher for that facility, which has got stabilized in this quarter, that is number one, and number two is the tight control over overheads has certainly resulted in some cost savings.

Sanjeev: Okay, and if you could just tell me, though we discussed earlier, that some of the people with a project, the people with reduction in Panex, so could you just tell us the type of people who have left?

Kishor Patil: This staff change is not at any level such as practice head, domain heads, or senior level consultants; this is at the programming level or executive level which are more engaged in the specific customer assignments.

Sanjeev: Okay, thanks.

Anil: Thank you Sanjeev.

Moderator: Thank you Sir. We have our next follow up question from Mr. Rahul Chadda of Aviva Life insurance.

Rahul: Sir just one small question, and this will be around the clientele for Panex, could you elaborate on the nature of work you are doing and the kind of repeat orders you are going to witness over next two to three years, for Panex only Sir?

Kishor Patil: Yeah, sure. There are two types of major revenues, which we get, one is on a major star account and second is based on the practice area. Now definitely this star account, which we are working with, the whole model is about the repeat customer model. In the practice area where we are focusing more on a SAP assignments mainly in the data warehousing or business warehousing that which is called specific to SAP, so we are focusing on these kind of assignment; and what we are trying to do is once we give a broad-level consulting services to these customers, we try to move more part of this work offshore and then cross-sell some other services to these customers to be delivered out of offshore. So, as we had mentioned sometime, maybe last quarter or quarter before, that we have already started working with a customer where we had sold SAP BW work and we have started them servicing out of India.

Rahul: Sir, out of the total revenues for the Panex which you indicated for this year of \$13 million, how much would this star customer account for, first part, and the second question, are you seeing the size of the engagements with the other customers increasing and are you adding new clients on that front?

Anil: As far as star customers inclusive of Panex, that would be close to 50% of my total business in Panex would be from star customers.

Rahul: Are you seeing increase in the size of engagements from other customers in the Panex?

Kishor Patil: Actually, there is definitely, you know, what we have tried to do after the acquisition is let go the business which is not non-core to us and bring the growth which is very focused relating to some star customer or potential star customers and specific to practice. So definitely we are seeing that some of these customers who we have been engaged on SAP BW, we are seeing increase in the engagement.

Sanjeev: And also one just final piece sir, for the company as a whole, what would be the attrition rate?

Ravi Pandit: Our attrition rate, Anil's figure was not quite right. Our attrition rate last quarter for the company as a whole was in the region of 25.5% to 26%. Of this, when you exclude the people who have been with the company for less than six months or less than 12 months, then the rate comes down to in the region of 15.5% to 16%. Almost 70% of our attrition is in the first phase when a person who has joined recently. We are now targeting our efforts of organizational development at the new joiners and we are trying to make sure that their association or their mental affinity with the

company goes up through a variety of mechanisms, so that our attrition in the initial phase goes down.

Rahul: With the MNCs also looking at recruiting the same set of people, are you really facing the necessity to increase your salaries across the board to retain talent?.

Ravi Pandit: Every year, in the month of April, we give our increments. When we give the increments, we take into account what are the reasonable salary levels across the various companies. We believe that our steps to fix the attrition issues are not related to salary levels because our attrition happens actually in the first six months, largely in the first six months of a person joining, and that attrition is more related to the nature of the work that a person wants to do vis-à-vis the nature of the work that he is actually doing; how much time he spends on the bench as opposed to getting on bench in training as opposed to getting direct project experience; where his other colleagues go and whether he wants to stay in India or wants to go abroad for his education, so these are some of the more important driving factors of attrition in the initial phases of a person's working life. We are fixing that.

Sanjeev: Perfectly fine sir.

Ravi Pandit: Thank you sir.

Moderator: Thank you sir, we have our next follow up question from Mr. Sudhanshu of B&K Securities.

Sudhanshu: I just have two more questions. First of all, I wanted to understand that when you say that we are going to make certain investments in new areas, avenues, service and practice lines, except for the VLSI practice, could you explain that you know what is the road map like, which are the new service lines practices which you are going to invest in?.

Ravi Pandit: Sudhanshu, typically we experiment with variety of practices. It is only when we see that there is a good match between that practice and with our potential customers, potential star customers, then we go little deeper into the practices, and in that context, you would recollect that we started talking about embedded about four to five quarters ago and we saw it grow. We started talking about VLSI two quarters ago and we have seen it grow. I have talked now about risk management because we are now seeing it grow although we have started working on it for the last two quarters, but this is what we are looking at right now. Only when we see a good strike rate within our end customers, we will actually start talking about what the practice is, where it is targeted, which customers are we going to go in for. Right now, actually we have nothing more to announce in the new practice area because they are really under trial as of now.

Sudhanshu: And could you quantify sort of what is the quantum of the investment in the rest of the year that you are going to make investing in these new service lines perhaps?

Ravi Pandit: Over the next two quarters, we expect about 2% of our top-line as the investments in various practices or new tools and technologies, etc. But since we treat this as an ongoing investment in new areas, we write them off, because that is the right way of doing it.

Sudhanshu: So you are saying, even in the current quarter that must be present around the same amount?

Ravi Pandit: But Sudhanshu you should also expect that happening on a quarter-to-quarter basis hereafter as well.

Sudhanshu Okay, great sir, and my second question was really to touch base again upon something about attrition rates, you say that it is predominantly in the people who joined the first six months, so and if I remember correctly, I think over the past two quarters, we have been saying that we are moving away from a predominantly lateral recruitment strategy to a fresher strategy. Do you see that making a difference, I mean, you know, what really is happening, are more and more laterals for example getting pulled away by MNCs or do you see more freshers, you know, just wanted to understand and get your prospective on that.

Ravi Pandit: You are right that last year we made additions of people more at a lateral level because you need to build a middle layer of the pyramid before you can take a lot of people at the lowest level. We have increased our recruitment of the youngest level of the pyramid during this period. It is also true that relatively higher attrition happens with fresher during the first one year as compared to the attrition that happens with more experienced people during the first one year because they have kind of seen the world, have seen what working life is and their expectations are a little more mature, whereas in the first year, the attrition rates are going to be higher across all the segments, but they will relatively higher in the fresher as compared to the more experienced people.

Sudhanshu: Thank you sir. And sir just talking a bit more, except for IT services, you know, do we have some plans to get purely into BPO or ITS kinds of work?

Ravi Pandit: As of now we are not looking at general BPO. We are also not looking at putting up BPO unit per se. As we have mentioned that our strategy on BPO will be completely client driven, when one of our existing customer says he wants us to work with him in the BPO area, that is when we will get into it, and when we get into it, again we will focus on our core areas which should be in the area of accounting or HR, and it will not be a normal call center of an area. But today as of now, we do not have a contract on those areas on hand and we do not really know when we will get into that area.

Sudhanshu: Sure, thanks a lot.

Moderator: Thank you sir. Next is the follow-up question from Mr. Sanjeev Kapoor from ShareKhan.

Sanjeev: Ravi, there was a question asked earlier regarding, you know, MNC client renewing a contract with Cummins internationally. I just wanted to know if you have seen if Cummins IT growth, that is your growth as compared to the other two clients, offshore vendors in India. You will have to comment on as to how the growth has been at Cummins at KPIT in Cummins account as compared to competitors?

Kishor Patil: See, we have been growing at a faster rate actually as compared to our other vendors in Cummins account and we being a strategic partner, are really involved into all the areas of strategic

importance to Cummins, and in a nutshell, our growth has been far better than the other vendors in Cummins account, and Cummins as a company is also growing and I think they have a very good year and I believe that that will further improve the overall IT spend.

Sanjeev: Okay, and the earlier stand which we took in terms of a 70-70, which you were talking about earlier, what particular share do you think the off-shoring now; do you think that it is likely to change anything in that particular front?

Ravi Pandit: Sanjeev, it is not a standard. We took, it is a policy that Cummins has and we do not know of any change in that policy from Cummins. I think they are pursuing that policy quite vigorously.

Sanjeev: What I am saying is your size in that particular pie, do you see that the way the growths have happened increasing?

Ravi Pandit: Yes we see our pie growing, but that 70-70-70 does not speak about an individual vendor's share. That 70-70 speaks about how much will be outsourced; how much of that will be given to three vendors; and how much of that will be off-shored and they are on track for that.

Sanjeev: Off-shoring amount total is somewhere around \$49 million or is it less than that?

Ravi Pandit: Let me just go back to the original model. We had explained that the total business IT spend of Cummins was a little over \$100 million, 70 of that was planned to be outsourced that would come to \$70 million; 70 of that would be given to three companies, that would from a spend perspective come to roughly \$50 millions. 70% of that would be offshore, which at the first value would be \$35 million, but obviously would not remain at \$35 million, it would come down quite substantially when the off-shoring happens. So the total of all the three vendors put together initially estimated only for the business IT would be in the region of \$35 million. This year, we are expecting our share of Cummins to be in the region of \$17-18 million. I would also like to reiterate that this whole 70-70-70 relates predominantly to the business IT whereas we also do work outside the business IT, that is, in area of embedded software that stands outside this \$100 million kitty.

Sanjeev: Just one thing, you said 35 is for the three vendors when you are saying this includes both onsite and offshore?

Ravi Pandit: That is true.

Sanjeev: Okay, and can you tell me what is our debt level currently.

Anil: We are currently at 0.45:1 as of September end.

Sanjeev: Can you just quantify the debt amount as such?

Anil: It is close to Rs.35 crores.

Sanjeev: Thanks a lot.

Anil: Thank you.

Moderator: Thank you sir. Participants who wish to ask questions, please press *1. Next we have a follow-up question from Mr. Deepen Shah of Kotak Securities.

Deepen: Anil, this is a follow-up question to the last answer that you gave, there is a debt of Rs.35 crores.

Anil: Yes Deepen.

Deepen: I believe that is mainly towards your facility which you have setup recently and I just wanted to know like any plans regarding paying it off in the next year and whether you have any cash flow projections so that you think that this debt level should come down in the next year.

Anil: As I told you this includes my working capital debt as well, and going forward, we will generate the internal accruals, which would certainly take care of my working capital needs. So year down the line, unless we go ahead with some new debt for our say further expansion, I see the debt component going down.

Deepen: And how much is the working capital out of Rs.35 crores?

Anil: Out of this, close to Rs.12 crores would be working capital and remaining is the term loan.

Deepen: And the average cost would be in the range of 5 to 6%.

Anil: Correct. You are right Deepen.

Deepen: Okay, thank you very much.

Anil: Deepen.

Moderator: Thank you sir, participants who wish to ask questions, please press *1.

Sandeep: I have a couple of questions.

Moderator: Yes sir you can go ahead.

Sandeep: I just wanted to know about the billing rate in the risk management practices, is it lower than number of current average or I think because this service seems to be a generic service nothing like a niche we will be providing?

Ravi Pandit: I do not know whether it is generic or niche Sandeep, but our rates are better than the normal rates.

Sandeep: Okay, so the billing rates here will be higher than the normal average rates?

Ravi Pandit: So far the experience has been that. We do not expect them to lower than the normal average rates.

Sandeep: Okay, okay, and sir, as you have mentioned that though the billing for the fixed-price projects in the non-Cummins star customers have not happened because of the milestone, is it true for one customer or is it true for across all the non-Cummins customers?

Ravi Pandit: See it happens at various point in time with various customers. You would recollect last time it had happened in the case of Cummins, this time it has happened in the case of one or two other customers.

Sandeep: Okay, so that one customer is affecting your growth.

Ravi Pandit: I said not one, I said one or two customers.

Sandeep: So that has affected our growth with six to seven customers.

Ravi Pandit: It has affected our billing change with reference to one customer.

Sandeep: Okay. So, we can expect that billing to happen in coming quarters?

Ravi Pandit: As we mentioned earlier, we expect non-Cummins growth to be the tune of 50% during this year.

Sandeep: Okay sir, and this is a question to Mr. Anil, what will be the depreciation amount in Q4, I think it will increase significantly?

Anil: No Q4, we have factored the depreciation; we take into account on account of capitalization of our Hinjawadi new project. I believe one quarter depreciation would be say almost close to Rs.0.5 crore, that kind of depreciation I am looking at, but we have factored that while giving the guidance.

Sandeep: The half a crore for the new facility?

Anil: Yeah as I said, this is my rough estimate, but we have factored that in our guidance.

Sandeep: Okay, and sir the last question is the current operating margin of around 13.8%, where do you see this to shape up in the coming quarters?

Anil: It will be even in the next two quarters.

Sandeep: Okay, because as the implied guidance the H2, that is the second half that also gives an indication that the margins will be maintained.

Anil: Yeah, we are maintaining those. Current margins will be maintained as I see it going forward, for FY-05.

Sandeep: Okay, so the additional offshore benefit will be invested in the practice areas?

Anil: Yeah, as mentioned by Mr. Ravi, we will continue to invest in the practices, which we have identified as relevant for our existing customers as well as both the verticals.

Sandeep: Okay, thank you sir.

Sandeep: Parul we have any further questions?

Moderator: No sir, there are no further questions from the participants.

Sandeep: Mr. Ravi, can we close the call?

Ravi Pandit: Thank you very much Sandeep.

Anil: Thank you very much.

Moderator: Ladies and Gentlemen, thank you for choosing CyberBazaar's conferencing service. That concludes this conference call. Thank you for your participation. You may now disconnect your lines. Thank you and have a nice day.