“KPIT Cummins Earnings Conference Call”

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Moderator

Ladies and gentlemen good day and welcome to the KPIT Cummins Q2 FY11 results conference call hosted by IDFC Securities Limited. As a reminder all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today’s presentation. If you should need assistance during the conference please signal an operator by pressing * and then 0 on your touch-tone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Hitesh Shah, thank you and over to you sir.

Hitesh Shah

Thank you Faisal and good afternoon everybody. On behalf of IDFC Securities I would like to welcome you all on the call to discuss the results of KPIT Cummins for the quarter ended September 30th 2010. We have KPIT Cummins management with us on the call. Mr. Ravi Pandit - Chairman and Group CEO, Mr. Kishor Patil - CEO and Managing Director, Mr. Girish Wardadkar - President and Executive Director, Mr. Anil Patwardhan - Head and Vice President, Corporate Finance and Governance, Mr. Sunil Phansalkar - Senior Manager - Investor Relations. With that introduction I would like to now invite Mr. Sunil Phansalkar to take the discussion forward, thank you and over to you Sunil.

Sunil Phansalkar

Thank you very much Hitesh. A very warm welcome from KPIT Cummins to all of you on this post earnings Q2 FY11 conference call. We also take this opportunity to wish you family and friends a very Happy Diwali and a very Prosperous New Year ahead. We will have the opening comments by Mr. Pandit on the quarters’ performance as well outlook for the remainder of the year and we will throw the session open for question and answers. So, once again a very warm welcome and I hand it over now to Mr. Pandit, thank you.

Ravi Pandit

Good afternoon and welcome to everyone. Our investor update I trust is with all of you. I believe that the investor update is fairly comprehensive that is attempt that we have been making over the last few quarters. So, what I would like to do is to cover in my opening remarks, some broad areas which probably needs some highlight. At the end of that we can go into the detail questions that you may possibly have. In my opening remarks there are four areas that I would like to deal with. I would like to deal with revenue, I would like to deal with the net profits. I would like to
talk about the operating margins and then I would like to talk about some of the resolutions that our board passed in the recent board meeting. Talking about revenues, last quarter showed a fairly healthy organic growth. On a year-on-year basis in dollar terms our revenues went up by 40%. On a quarter-on-quarter basis on dollar terms our revenues went up by 13%. In terms of constant currency the revenues grew by 10% on a quarter-on-quarter basis. The volume growth was about 8%. We crossed 50 million revenues mark per quarter in this quarter. The numbers that I spoke about do not include any inorganic growth from the recent acquisitions that we made and that we announced, which includes CPG in the US and in2soft in Germany. Both these companies would be consolidated from the first of October and we would see the benefit of their revenues in the H2 of this current year. At the beginning of the year, we had mentioned what would fuel our growth during the year and our growth has been quite in line with what we had anticipated at the beginning of the year. We had said that our growth will come from our SAP line of business, the SAP SBU. We had also said that our automotive and embedded SBU, which talks about really the engineering business would also grow and we had said that the emerging market will grow.

During this quarter the SAP SBU grew by 27%, the automotive and allied engineering SBU grew by about 13% and the emerging markets grew by about 20%. As I mentioned in line with our anticipation at the beginning of the year. Our growth during the H1, meets and I should say slightly exceeds our expectations, with this the growth in the first part, we are confident of reaching and may be exceeding the 25% organic growth number that we had projected for the current year. If one adds to it the roughly $8 million of revenue that we will get during this year that is in the H2 from our inorganic revenues we believe that we should cross 200 million revenue mark during this year, giving us growth in excess of 30% for the year. We believe our growth for the year will be good. In addition to that qualitatively also, we believe that our growth has been good. During this period we became the premier members of JASPAR consortium, probably the only Indian company to be premier member of both European as well as the Japanese consortium for definition of automotive standards. We also became members of Tensilica to become their authorized SoC Design Center which we believe will help our customers significantly.
We became the gold partner for Oracle and thus in all the areas for operations we believe we are strengthening our position. So, both in quantitative terms as well as qualitative terms we are seeing the growth that we have been projecting. Coming to the second point, mainly the net profit after tax, it grew by 23% on a quarter-to-quarter going basis, mainly aided by the revenue growth and reduced ForEx losses. Our PAT margin also improved by 71 basis points to reach 10.11%. The third area that I would like to cover is the issue of the operating margins, where our performance has been somewhat subdued. The operating margins during the quarter stood at 15.5% and they were a bit subdued on account of two or three factors and let me talk about them. In this quarter as we had mentioned at the beginning of the year, we continued to do significant additional hiring. You would recollect that we had stated that we would have a strain on profitability during the first two quarters especially because we are recruiting a significant large number of people, especially freshers whose cost will fall due in this quarter, whereas the revenues will not come. So, in line with our expectations we added significantly to our people’s strength. The net additions that we added, the net addition that we had during this quarter was 609, I would say amongst the highest number of people added in our history, not all these employees were billable. Our utilization was around 70%, you would recollect that in the previous periods our utilization levels have been as high as 75%-76%. The extra people during this quarter cost us about 14 crores, not all as I said of them were billed So, this was one reason which impacted our operating margins.

The second reason that impacted our operating margins was that the relative share of the SAP SBU in the total pie has increased, it has increased from 31% of our total revenues in Q1 to about 35%. At the operating margin level, the onsite was that we do in SAP SBU has a lower EBITDA and EBITDA of 13%, which is what we had shared with you in the initial stages. We believe that this EBITDA will grow to the extent of about 18% or so by the next year and our current growth rate and our margins are in line with what our initial expectations were. But the higher composition of this in our total as a part of our total revenues had its own impact on the operating margin. The sales and selling and general expense, administrative expenses have increased by 14% and this was largely on account of front end hiring, we have added people in our sales functions as
we had mentioned earlier. We also had increased travel, moreover we had increased legal and professional charges in connection with acquisitions which we wrote off, so these are the factors which impact our operating margins during this quarter. You would recollect that at the beginning of the year we had stated that our EBITDA margins would be lower in the first two or three quarters and we expect the margins to improve in the subsequent part of the year. We believe that we should be the range of 18% to 20% EBITDA till the end of the year subject to how the foreign exchange moves, but our improved utilization, our better employee pyramid and our revenue growth should help us improve EBITDA margins as we go forward.

The last thing that I want to talk about is the board resolution that we have passed, so in the board meeting, we passed two resolutions, one which increased our authorized capital and the second is an enabling resolution, allowing the company to issue fresh equity over a period of next 12 months. As you are aware, we are a profit making company, every year we are improving our cash balance, so we would not be needing additional cash for our normal day-to-day operations, we are however continuously looking at appropriate acquisitions which fit into our strategic focus. For the funding of these acquisitions, we may have a need for increase capital. Our current level of authorized capital did not permit us to do so, hence the increase in the authorize capital. We have also mentioned we have passed a resolution for enabling the company's management to enhance the capital by further issue shares under various possible means that are available under the law and that enabling resolution has been passed. We would go for an actual additional equity as and when we feel that the cash is required for the operations of the company. So, these are the four broad areas I wanted to share my thoughts with you about. As I mentioned we have given a fairly detailed investor update and I am sure that you would have questions. So, we will be now open to receiving questions from you, thank you very much.

**Moderator**

Thank you very much sir. The first question is from the line of Bikram Mahajan from Bay Capital, please go ahead.

**Bikram Mahajan**

Sir, you have almost always judiciously structured amenities with staggered milestone with payments, now with regard to your recent acquisitions in this quarter, I believe that CPG total consolidation is 600 million and
IntoSoft is 185 to 190 million both over three years and total payment that you have made in this quarter is 373 million. So, if you could just split this payment between purchase consolidation for CPG and In2Soft and going forward what will be the payment schedule?

Ravi Pandit

Basicallly I think the numbers which you have quoted are may not be the right and CPG US, we have upfront consideration of $6 million and in In2Soft case we have paid €1.7 million as an upfront consideration and the remaining consideration is milestone based consideration over a period of two-three years.

Bikram Mahajan

And sir what are these milestones?

Ravi Pandit

These are milestone in CPG’s space which is based on the offshore revenues how do we move and certain EBITDA margins, how do we move so this will be assessed over a period of next three years and then remaining payment will be released.

Bikram Mahajan

Over next three years are they front loaded, back loaded or smooth over next 3 years?

Ravi Pandit

So, there is a milestone update, in 18 months time then there is a payment after three years, so there are two milestones, one is after 18 months and the second is after three years.

Bikram Mahajan

Okay and you also mentioned that both these acquisitions put together will add $8 million in H2 about 7% to 8% of your top line so what would be the profitability profile, 15% to 16% or is it different?

Ravi Pandit

So, during this period basically, there are two expenses we are looking at one time, so one is naturally integration expenses and second expenses we are looking at investments we are making into sales team, so the purpose for these acquisitions is naturally to make and build a global practice and from that perspective we are making certain investments in those items. So, with that the marginal improvement during these six months will be marginal, it will be naturally a normal after in the next year, calendar year. So, during this period may be 3% to 4% kind of net margin we are expecting in next six months, net of naturally all these expenses and in the next year we would go back to the full margins.
Ravi Pandit: One comment I would like to make at this stage at 8 million for the year this would contribute to roughly 4% of our total annual revenues.

Bikram Mahajan: Okay so 8 million is in H2 only, right so that will be around 7% to 8% of your H2 top line?

Ravi Pandit: Yes that is right.

Bikram Mahajan: And sir lastly, please correct me if I am wrong, this offshore realizations have increased by around 10% since last quarter, so can you please explain the reason attributable to the significant improvement?

Ravi Pandit: See, we look at it and if you look at growth in constant currency terms that growth has been around 10.5% to 11% against 13% which is in US dollar terms and about 8% of that is volume growth. So, we are looking at 2%, 2.5% growth because of the increased in realized rates. Now, this is a combination of change in mix of revenue because as we know our SAP as well automotive rates are higher than the average business IT rates and as the proportion of these SBU businesses goes up in the total pie, the average realized rate as a company level also goes up.

Bikram Mahajan: So, sir in this quarter what has happened really to include these realizations or is this lag effect of previous deals that you have signed and are executed in this quarter?

Ravi Pandit: No, this is an larger effect of change in the business mix as I said, so if you look at the growth SAP has grown by about 27% quarter-on-quarter and auto embedded SBUs has grown by 13% quarter-on-quarter.

Bikram Mahajan: Okay and sir lastly, I missed that part where you mentioned your dip in margin Q2 increase in SAP revenue share, so what are SAP’s gross margins or EBITDA margins you want to quote here?

Ravi Pandit: The onsite SAP EBITDA margins are up to 13% as of now.

Bikram Mahajan: Alright thank you so much.

Moderator: Thank you. The next question is from the line of Shraddha Agarwal from B&K Securities, please go ahead.
Shraddha Agarwal  
Sir, firstly on EBITDA margin, I think you said that you would be ending the year with 18% kind of an EBITDA margin, so what is you were referring to organic EBITDA or you are referring to EBITDA including the two acquisitions?

Kishor Patil  
So, Shradha as you would see the two acquisitions, do not really contribute very substantially to the total revenues, so I think they will have a relatively less impact on the overall margins, so when I talked about 18% or the near about, I am talking about the total.

Shraddha Agarwal  
Sir, but if I am not wrong though the acquisitions are coming in at a comparatively lower margin, I mean if I am not wrong probably CPG is coming at a 12%, 11% EBITDA and you were at 15.5% EBITDA margin and then on organic basis this quarter, so meaning to say you would organically or rather even after building in these acquisitions you would be able to jump from 16% to 18% that is 200 bps kind of an improvement in two quarters?

Kishor Patil  
Ms Shradha first is both CPG and InfoSoft if you look at operating margins they are 15% plus, what we said is there would be some investments which will be happening in front end which may happen in H2 and the contribution by these deals might not be that significant but they are not as lower EBITDA margins, so CPG at 15% plus and in2soft is close to 16% operating margins.

Shraddha Agarwal  
Right. What are the various levers available for the company to show such kind of an improvement in margins in the second half?

Kishor Patil  
So, as we said there are three-four main reasons, obviously first is the utilization number which we talked about so we have enough scope for improvement in utilization and as the 550 plus freshers which we have added in H1 gets delivered, some of them have already started getting billable, get billable and then the utilization levels will go up and we can see improvement in utilizations at 3% to 3.5% over the next two quarters. Obviously when these pressures spread into the system and that will help us to improve our employee pyramid which means that the lateral additions would be lower to that extent, which will help us to improve our gross as well as operating margins. And the third factor obviously is the revenue
growth which will come in H2, so these three are the prominent reasons why we believe that operating margins will go up in H2.

Shraddha Agarwal  Okay and how many employees would come on board through these two acquisitions in the next quarter?

Kishor Patil  Sorry.

Shraddha Agarwal  How many employees would be joining KPIT through these two acquisition integration in the next quarter?

Kishor Patil  So, we should have close to 100 people.

Shraddha Agarwal  From both the acquisitions combined?

Kishor Patil  Yes correct.

Shraddha Agarwal  Okay and we would have the consolidation for the full quarter or would it be for some months?

Kishor Patil  It will be for the full quarter, starting October 1st.

Shraddha Agarwal  Okay and how is the tax rate change after building in these two acquisitions into our model?

Anil Patwardhan  The tax rate Shradha would continue to be the range bound, because the impact on the bottom line is as explained by Kishore would be minimal, so tax rate would remain same.

Shraddha Agarwal  Sure and lastly if I could-

Kishor Patil  And just to come back on the EBITDA margins, it is also dependant on the realizations rate point, so if the rupee appreciates further then it might have an impact on the EBITDA margins.

Shraddha Agarwal  But when we are guiding for such EBITDA margins we are building in what Rs.45 kind of an exchange rate?

Kishor Patil  Yes, so if the spot rate is where it is today close to 45.
Shraddha Agarwal: Sure that is helpful and any update on Revolo, I mean what is the progress there?

Girish Wardadkar: So, since we spoke last couple of movements, number one the approvals that we have received from the ministry of road transport for putting the vehicles on the road for tests we have already received it, some vehicles we have put on the roads for testing. The second is in terms of progress on the operations to set it up by the unit in Pune, so we have localized few options on the place and the whole unit will be up and ready in the beginning next quarter. The third update is additional vehicles in terms of models for trials. So, these three specific movements between last quarter update and now.

Shraddha Agarwal: Right that is helpful and that is it from my side thank you.

Moderator: Thank you. The next question is from the line of Dipen Kapadia from PUG Securities, please go ahead.

Dipen Kapadia: Actually, when I was going through the software development expenses it has risen by 100 basis point and could you give me a break-up of what is the impact because of SAP and what is the impact on onsite because our onsite revenues have actually gone down in terms of, to the total contribution and the onsite cost has gone up, so could you give me a small break-up of how many percentage points has this onsite cost added to this software development expenses?

Anil Patwardhan: So, Dipen if you look at it, it is difficult to have a split but if you look at an absolute onsite revenues they have gone up, even though the share of onsite revenues has come down and the absolute onsite revenues has gone up, so the increase in onsite revenues of SAP is complemented by reduction in onsite revenues in other SBUs, all the growth in automotives has happened through offshore. So, as said by Mr. Pandit earlier the total increase in cost into additional manpower plus close to 14 crores during the quarter. Now, there is a mix of natural increase in cost because there was an increase in the revenues and there is some cost which we look at investment for the future typically the fresher’s cost, so that - out of the 20 odd crores, which are increased during the quarter of our 14 crores can be attributable to the net employees addition during the quarter.
Dipen Kapadia: Okay the other thing is how much have we hedged for the next quarter and what about the future hedging?

Anil Patwardhan: We have $84.75 million of hedges outstanding as of end of this quarter, with USD 23 million hedges maturing till FY2011.

Dipen Kapadia: Okay sir thank you sir, thanks a lot.

Moderator: Thank you. The next question is from the line of Nawaz Sarfaraz from Arihant Capital please go ahead.

Nawaz Sarfaraz: To start off, can you give some idea of the kind of traction that we are seeing in the global market, the deal pipeline and deal convergence cycle and adjusted for seasonality, how would you compare between Q2 with Q1?

Ravi Pandit: Yes, so as we had said at the beginning of the year, we are seeing traction in all areas, however our pipeline for the first quarter, the growth has been very strong for SAP as well as the automotive engineering and we believe our overall pipeline is the strongest, I mean it grew by about 30% to 40% overall in terms of over quarter one. We see a very strong pipeline in all the areas, SAP seems very strong, we see a very strong pipeline for automotive engineering and on the other parts also there is certainly a good pipeline and growth, so the growth is all over. The pipeline in the emerging markets especially Asia Pacific, India is also very strong. We see there is a marginal growth in Europe and US shows a very strong growth also as compared to what it was for the last year. So, I would say the overall growth has been very strong both in US as well as APAC region and Europe is marginally higher.

Nawaz Sarfaraz: Okay but sir, I had been listening to commentary that has come from the top three IT companies and they are seeing good business uptick happening in Europe, especially in your strong hold Germany and France and in the manufacturing sector itself. So, what is your take on it, I am asking this question because over a last few quarters, we have been seeing a decline in revenues from you both in absolute terms and in proportional percentage term also, so what is your take on it?

Ravi Pandit: So, this quarter if you see there is a growth in Europe and again about 4% growth during quarter-on-quarter during the second quarter, so we
naturally expect a growth also in Europe, yes France pipeline seems much better, Scandinavia is a good market, so these are the markets which we feel there is a good pipeline in the European side.

**Nawaz Sarfaraz**

Okay, sir correct me if I am wrong, I believe your revenues in Q2 from Europe is around 10.08 million, whereas in Q1 it was around 11 million so there has been actually a decline, not an increase?

**Sunil Phansalkar**

Nawaz there has been an increase in terms of revenues, I will give you the exact numbers, I will just mail them across to you.

**Nawaz Sarfaraz**

Okay fine. Sir, my next question is with regards to your top line Cummins, the revenue contribution has increased quite a lot this quarter, so going ahead should we expect this kind of growth to continue or was it the one-off quarter or so, what will be the future be like from this particular client?

**Ravi Pandit**

Cummins has one of the very good years this 2010 and however they continue to have the similar lower IT budgets during the year, so we are getting some growth. But certainly I think from next year onwards we would see higher IT budgets from Cummins and both on IT as well in engineering area and mainly in engineering area because we believe that the larger part of the growth will come from that area.

**Nawaz Sarfaraz**

So for next two quarter, we should expect revenues to be flat at current levels?

**Ravi Pandit**

See, I mean more or less I mean there will be some growth but marginal.

**Nawaz Sarfaraz**

Okay, sir one more question considering the fact that we have taken about two companies which will be contributing to revenues next quarter onwards, are we going to increase our bottom line guidance of 5% y-on-y that was given in the beginning of the year?

**Ravi Pandit**

So, we would give a revised guidance at the end of the next quarter.

**Nawaz Sarfaraz**

Okay, so we had plans to add around 1100 employees in FY11, which we have actually done in the first two quarters itself, so what is the outlook for the next two quarters, are you going to take and move the employees, are you going to increase the employee intake?
Yes, certainly we are looking at increasing number of employees. We will continue to do that and as I said our pipeline seems strong, we will certainly look forward to adding more headcount.

Okay sir, can you put number to that sir for the next two quarters, how many employees should we expect?

I think we will give you those numbers by the end of this quarter.

Okay sir lastly, coming to SAP SBU, you have mentioned that you will be seeing lower traction in SAP implementation, so are we expecting SAP revenues to remain flat in Q2 or is there a chance of it declining?

So, it will only in Q3 we have said that what we are seeing is that see if you really look at the SAP revenues, they have really exceeded all the numbers significantly in Q1 and Q2 than the expectation, the SAP revenues are largely based on large project implementation which has transformational projects in our verticals and these are large transformational projects and so because of the cyclical nature of these projects we have said that in Q3 the revenues will be less than the Q2.

The growth rate actually numbers what we have said is, we have seen 27% growth rate in Q2 we have said that the growth rate will not be that high in Q3. So, it is not that there is an absolute slow down but the growth rate would not be that high and second to your earlier questions if you look in rupee terms the Europe revenues last quarter were 448 million, this quarter they are 467 million, so there is a 4% growth. If you look in dollar terms there is a 3% growth absolute numbers.

Okay sir, will it be possible to give me the proportion of the implementation and maintenance revenue from SAP what kind of and what is-?

See, it is about 85% is in implementation revenue and 15% is about the maintenance revenue in case of SAP.

Okay fine sir thank you and congratulations once again.

Thank you. The next question is from the line of Shikha Jalan from SMIFS Securities, please go ahead.
Shikha Jalan My question relates to Revolo, what kind of investment have we done in Revolo till date?

Anil Patwardhan Basically, I have like invested till end of September around Rs.22 million.

Shikha Jalan Sir, I am sorry but I am not able to understand, I think though the voice is not very clear, you said that Rs.22 million has been invested in Revolo till date and sir what part of it has been charged to P&L account or are we recapitalizing it till now and we will be charging it to P&L account when it is launched completely?

Anil Patwardhan As I told you basically these are the R&D investments made by KPIT in Revolo, which could be capitalize in KPIT books and that is the amount that I mentioned and from capitalization of joint venture perspective initial capitalization will be 15 crores each by both the partners, out of that first three crores, capitalization is being done now.

Shikha Jalan Okay three crores, okay sir. Also sir, how are we planning to secure our revenues from Revolo now that we have, vendors in line and I think how are we planning to basically what are the revenues we are expecting from Revolo A and B and how are we securing it?

Girish Wardadkar Yes, so to answer your question on the securing of the revenues as we had mentioned in some of our calls before, we are taking two approach, one we are already engaged in active discussions with OEM, both Indian as well as non-Indian OEM, so that is one. The second one of course is on the retrofit. The retrofit will be through the channel, so the dealers that we will be appointing to distribute and service the customers, so that is about how we will go about acquiring. The third part of acquisition is corporates and we are in active discussions with a few corporates for direct selling of the products so that we fit them in to the cars of either their employees or the vehicles which are used for business transactions on the day-to-day basis, does that help you to get the answer to the question?

Shikha Jalan Around that sir, when you are speaking about discussion with OEM sir, any contract do we have for let us say two years, I mean particular number of years or particular number of amount of the quantity of the product or something like that or it is just on an ongoing basis?
Girish Wardadkar Right now, it is on ongoing basis until such time that the OEM and us come to a conclusion in terms of start date of production, so it will be difficult for us to share.

Shikha Jalan Okay and when is that expected launch date sir for Revolo?

Girish Wardadkar As we had said we will be having the commercial launch in the fourth quarter of this fiscal year or the first quarter of the calendar year, next year.

Shikha Jalan Okay sir that is all from my side and in case I have anything else I will follow up, sir thanks a lot sir.

Moderator Thank you. The next question is from the line of Madhu Babu from Systematix Shares, please go ahead.

Madhu Babu Sir, what are the nature of the projects we are doing in emerging markets like India and what are their implications on margins and debtor days?

Kishor Patil Yes, so in India we are doing different types of projects, I mean if I look at all the different business units we have, in case of SAP we are doing end-to-end implementations for automotive groups as well as industrials, so these are the two segments we are doing end-to-end implementation. The second part, we are doing is in case of automotive and engineering space, we are doing product engineering for Indian products as well as we are also focusing on some of the defense projects as well as government projects which are with the similar technologies, which is where we have expertise in automotive engineering area. So, that is the second part we are doing. In case of IES also I think these are again implementation in case of Oracle or otherwise some eBusiness opportunities in case of government, so these are the typical areas in which we are focusing on. Most of the areas in which we are focusing is in the same vertical which we have and the same service areas which otherwise we have. Apart from that the only other vertical, which we focus in India is defense and government.

Madhu Babu Sir, what would be the implications on margins and debtor days ramping up these businesses?

Kishor Patil Yes, so what we have seen is the margins are marginally low, I mean about 5% or so, I think that is where the margins are low. Over the period we are
in a position to really catch up on that and in DSO also it depends upon the DSO days are also about-

Anil Patwardhan  
DSO is close to little about 90 days for India as a territory, whereas the company level DSOs are 68 days.

Madhu Babu  
Okay, sir and we were talking of necessity to raise equity, so we have done a good amount of acquisition for the last 1.5 to 2 years so where are the gaps for us to do more acquisitions and is it to scale up to a next level or could you talk more about that equity raising?

Ravi Pandit  
Yes, so the strategy of our acquisitions had been to focus exclusively on the customer verticals that we are inching at and to provide them more and more product range of services for their customers and the purpose of the acquisition has also been to acquire customers in our verticals in different geographies. And the gap that we have filled so far are in the area of SAP, in some areas of automotive engineering which is the latest one being a diagnostic one, however, there are gaps in the kind of services which are needed by our set of customers, multiple gap still, so those are the gaps that we are looking at filling going forward. There are areas in ERP implementations for automotive and manufacturing customers that we are not completely taken care of. There are areas in product life cycles, which we have not completely taken care of, and there are areas in manufacturing execution systems which could fit very nicely with what we are doing. There are again areas in after market for the customers to whom we are selling, so there are the multiple gaps. We believe that without existing kind of verticals there is a phenomenal potential to be much larger than what we are.

Madhu Babu  
So, what could be the expansion need equity, I mean are we looking at 15% dilution on equity when you raise capital?

Ravi Pandit  
We do not know an exact number, as I mentioned the number will come up when we know what is the investment we are making in the near future. So, we do not expect it to a very large addition, may be 15 to 20%, may be a reasonable one, because when you know finally when you refer both debt and equity are available to you.
Madhu Babu  Okay, sir this star customers have shown up 4.5% growth that is underperforming. So what is the outlook there and just regarding the integrated enterprise solution, that has also shown a lower traction. Would they continue to so moderately lower growth these two parts of the business?

Kishor Patil  If you look at it, today we are more looking at our top 45 customers whom we have with us and if you look at our top 10 customers they have also shown good growth on quarter-on-quarter, even though the values are percentage terms they are saying that in absolute numbers there is a big growth happening there, so we see good traction coming from the customers which are in the areas which we have mentioned as growth areas for us and we will continue to see that traction happening. At a company level, we more so looking at, I just say about 40-45 accounts which are our top local accounts where we want to do the mining and grow there and we are saying good traction in most of these accounts.

Madhu Babu  Okay sir, thanks.

Moderator  The next question from the line of Amar Moriya from Inindianivesh. Please go ahead.

Amar Moriya  Just had a follow-up question about the integrated enterprise solutions, I wanted to know what is the contribution from the global business solutions. I believe integrated enterprise solution it includes the global business solution revenue as well?

Anil Patwardhan  Global business solutions revenue is a part of the IES SBU and that today is about at a run rate level, it is about 7 to 8% of our total revenue.

Amar Moriya  So if I exclude 7 to 8% of our global business level also integrated enterprise solution is about round about 27%of the total revenue, So, there is in terms of percentage, If I see total revenue as percentage of sales it is significant decline from 32% to 27%.

Anil Patwardhan  So this is the decline you are talking in terms of Y-o-Y?

Amar Moriya  No quarter-over-quarter. Like 32% integrated business solution contributed 32% in Q1 financial year 2011 and if I exclude 8% out of 34.95% that is the
total integrated enterprise solution revenue which include 8% of the global business solution revenue.

Anil Patwardhan  
I am assuming that you are reducing 8% from Q1 and Q2.

Kishor Patil  
So, if you remove 8% from both the quarter then the decline remains more or less the same.

Anil Patwardhan  
So, GBS numbers have been flat so whatever 3% Q-o-Q growth we have seen in IES, it is non-GBS revenue growth, it is that way you have to look at it.

Amar Moriya  
Can I get some break-up of what you know the fixed contracts and time and material contracts between the integrated enterprise solution, auto-engineering, semi-conductors if you can give break-ups?

Kishor Patil  
The exact percentages are not... if you look at our semicon and automotive we will have a large sale of fixed price contracts as compared to IES,

Amar Moriya  
So like in semi-conductor and auto what percentage will be coming from?

Kishor Patil  
50% plus of the revenues would be fixed price if you take both the auto and Semicon together.

Amar Moriya  
Thanks a lot and congratulations once again for fantastic quarter.

Moderator  
The next question is from the line of Pankaj Chopra from Iden Advisors. Please go ahead.

Pankaj Chopra  
Thank you for taking my question. My first question is, I wanted some comments from you on the attrition rate you foresee and how are the salary pressures shaping up now?

Girish Wardadkar  
The attrition during this quarter was very high. It was in 30s and there was an attrition certainly at different levels especially at the lower pyramid, lower levels which are like 2 to 4 years experience, I think that was the growth where we saw the large attrition. However, we have seen is we have been in position to replace most of these. See what has happened for us is, we had not really done a campus recruitment last year and much in the sense, as we would do otherwise and from that perspective we have been in a position to replace people one from the campus recruitment...
which we have done and some of the people from the lateral recruits. So, our average replacement cost is lower than the salary cost of the attrition and that is how we see it and that is the reason we see that the margins will improve from the next quarter as there pyramid gets adjusted.

Pankaj Chopra

You know when you replace freshers; it would affect productivity as well. I guess it plays out in both sides of the equation. When you try to replace get in low cost employees with necessary experience that is one issue and do you foresee HR or human resources remaining as a challenge as we go ahead and would you place it as one of your biggest challenges or if you have the solution to it in your hands?

Kishor Patil

Certainly, HR is one of the challenges and that is for the whole industry and it remains the area of focus for us certainly. What we have seen is that the attritions for the last one month or the last two months has come down so we can see that downward trend starting and it has started significantly coming down and we expect that the attrition would be much lesser in Q3 as compared to Q2

Pankaj Chopra

What about salary pressure, are we hiking salaries, or we intend to do that anytime soon or it has already been done?

Kishor Patil

No our increments have happened in the first quarter and now the increments will happen in the quarter one of the next year.

Anil Patwardhan

We follow a quarterly promotion policy and some percentage of people of course get promoted every quarter and that is what we have been following for many quarters now and we will continue to do that and follow that quarterly promotion policy going ahead.

Pankaj Chopra

Do you have some numbers in percentage of promotions in this quarter?

Anil Patwardhan

Typically about 5-6% of the total population that gets promoted every quarter

Pankaj Chopra

The second question it was a bit of a disconnect. As you mentioned that your margins where lower because of SAP going up and being onsite the margins are lower but if you see the offshore portion of your business, I thought saw there was an increase in the off-shore and there was quite a
large percentage increase. I do not remember the numbers now, I probably have it some. The offshore went up to...

Kishor Patil  See there has been an overall growth of 40% in USD terms quarter-on-quarter. Obviously, both onsite and offshore have grown. If you look at the onsite pie of the total company business the SAP share in that pie is increased even though at a company level, the onsite revenue have not increased in double digit. At the company level the onsite revenues have increased by about 2 to 3% but the SAP share in that part has gone up significantly because there is a corresponding reduction in onsite business from other SBUs. So, the mix of onsite pie had changed which has led to a higher SAP business in that pie leading to an overall lower EBITDA margin.

Pankaj Chopra Thank you, just one last area of questioning is you know you have a statement in your update which says multiple OEM programs in progress for factory fitters Revolo solutions. Could you give us some sense of what this OEM program and at what stage, could we even think of an OEM launch may be in a years time, is that possible in the realm of possibility?

Girish Wardadkar Typically as you know, OEM programs are ranging between 18 to 24 months. So even if we let us say signed up with an OEM today, the launch of their car would be as close to may be 18 months from today and at worst levels say it be 24 months today. OEM takes longer in terms of validation, homologation, and localization of components as you know. So, the process is bit longer, but I think the good news is as OEMs approve and also accept the product into their vehicles it kind of builds a much bigger case for us in the retrofit market. So that is the biggest advantage from a perspective of engaging with OEMs at this stage.

Pankaj Chopra I understand. So, I was wanting to understand whether how close are we to the sign-up, I am not saying that 18 months launch. How close do you think there could be a sign-up, could it be in the next one year where we can announce that we signed up with one OEM or within or outside India?

Girish Wardadkar You could expect it to be much faster.

Pankaj Chopra Okay. That is very nice. The final thing is essentially on you mention that you have been doing some work with some global OEMs as well. Now my question is whether is it a company initiative to go out and meet out these
OEMs or has there been even some enquiries from OEMs towards such a product from your end?

Girish Wardadkar  Both pull and push part.

Pankaj Chopra  Okay. Good. Thank you very much and all the best for you.

Moderator  The next question is from the line of Debashish Mazumdar from Techno Shares & Stocks. Please go ahead.

Debashish Mazumdar  Just wanted to understand in this quarter of total employee cost, what is the percentage of cost coming from operational employee and what is the cost of SG & A employee?

Anil Patwardhan  So, the 14 crore which was stated in all direct employee addition cost. Because that cost is a part of the software development expenses before gross margins.

Debashish Mazumdar  I mean almost 89% of your total personal cost coming from this operational cost? I need a break-up between the personal cost related to the direct operation and personal cost directed to SG&A?

Anil Patwardhan  If you look at the direct cost, which is software development expenses, in that if that cost is 100, then are close to about 85% of that cost is personnel cost and the enabling function cost would come more as a part of SG&A.

Debashish Mazumdar  Okay. So how much would that percentage of SG&A?

Anil Patwardhan  My guess is it would be close to about 60% but I will get back to you with the exact numbers.

Debashish Mazumdar  My second question is what is your expectation of tax rate for FY11 and FY12?

Anil Patwardhan  FY12 tax rate would be definitely higher, because we will be out of tax holiday on STPI units. So I believe it will be in the range of 24-25% of PBT.

Debashish Mazumdar  For FY11, it has remained the same level of 13-14 percent?
Anil Patwardhan  
It will be lower. FY11, I have indicated that our PBT-PAT ratio from tax prospective will be 17 to 17.5%. It would be lower than what we have estimated.

Debashish Mazumdar  
The attrition rate of 30% what you have mentioned, is it quarterly annualized figure?

Anil Patwardhan  
Yes. That is right.

Debashish Mazumdar  
Okay. That is it from my side. Thank you.

Moderator  
The next question is from the line of Sangam Iyer from Alf Accurate Advisors. Please go ahead.

Sangam Iyer  
My question is regarding the guidance that you gave during the early part of the call, as a line of was not very clear so can you repeat that. You say that around 20% plus growth?

Ravi Pandit  
What I stated was that at the beginning of the year, we had stated that we anticipate about 25% growth in our revenues as compared to the last year and what I mentioned that in addition to that, we would get about $8 million of revenue from the acquisition, which kick-in in the H2 and I mentioned that both of them put together could therefore take our revenues to a little over $200 million, which may result in little over 30% growth. Our indication from the H1 shore that we might be able to better the 25% growth rate that we had initially predicted at the beginning of the year.

Sangam Iyer  
Right. Sir, on the utilization front, what would be and ideal utilization that one could be looking at in the second half of the year.

Kishor Patil  
So 74-75% is something which we can achieve.

Sangam Iyer  
Okay and in terms of the margins when we talk about 18% kind of margin level, was it the exit rate that you are talking about or that was the margin for the full year that you are talking about?

Anil Patwardhan  
So 18-20% was the exit rate, which we were talking about.

Sangam Iyer  
Okay.
Ravi Pandit But I must add here that it also depends on the FOREX rates. One is beginning to see rupee becoming stronger and it may have some impact on.

Sangam Iyer Sir, on the hedging that you said you have $23 million odd for the second half for the next quarters, at what rate is it there?

Anil Patwardhan Rs. 44.5 rupees per dollar.

Sangam Iyer The balance 84 million that we have, which is for the next year?

Anil Patwardhan Next year, beyond FY11, the average rate would be Rs. 45 plus.

Sangam Iyer Okay. Thanks a lot Sir.

Moderator Thank you. The next question is from the line of Hiral Sanghvi from Dalal & Broacha. Please go ahead.

Hiral Sanghvi Just wanted to know what is the current size of oracle practice?

Ravi Pandit Current size of our oracle practice is about $30 million before the acquisition.

Hiral Sanghvi Right and what is the size that we are expecting to take it to over the next couple of years?

Ravi Pandit We are looking at anywhere between 80-100 million in the next 2 years.

Hiral Sanghvi Okay. What will be the one time component of legal expenses due to acquisitions in the current quarter results?

Kishor Patil We would not like to actually give you the deal level expenses, but what we said that the cost which we incurred in Q2, over the deal have been expensed out.

Hiral Sanghvi Right. So to that extend, gain in expenses would be lower coming H2?

Kishor Patil Some of the expenses will flow into H2.

Hiral Sanghvi Okay fine. That is it from my side. Thank you.
Moderator: The next question is from the line of Abhir Pandit from Parag Parikh Financial Services. Please go ahead.

Abhir Pandit: My question is related to the new areas, which you have said would be the Defense in government. So my question is, is this a system integration type of business because that type is mostly a very capital intensive business?

Ravi Pandit: It is not presently the systems integration. There is a lot of automation, which is now getting into Defense products and there is work such as on night vision, there is work on hybridization or on battery management systems, acid development, etc. This is the nature of the work that we are doing. We do not expect to see at least in the immediate future large systems integration work.

Abhir Pandit: Okay. That is all. All my other questions have been answered. Thank you.

Moderator: The next question is from the line of Krishna Mahale from Keynote Capital. Please go ahead.

Krishna Mahale: I just wanted to ask how would Jaspar membership help you in the medium-to-long run?

Ravi Pandit: Certainly if you really look at the OEM customers, naturally we first had last year OEM customers in US first, then some in Europe and some in Japan. What had helped us in Europe was to have a very strong Autosar product recognition and that helped us to really build a very good relationship especially at the OEM level along with the tier-1. So we believe that the same benefit we will get in the Japanese market and that will allow us to really what it could be many of these OEMs and the tier-1s in this market. So it gives us tremendous brand recognition as well as the entry into the overall new customers and a very strong recall with these customers.

Krishna Mahale: Sir, is there any significant difference between Jaspar standards and Autosar standards?

Ravi Pandit: So, large part of that are similar, but some of the protocols are different and so that is one major change, but philosophy is similar.

Krishna Mahale: I just wanted to know the IP contribution in your Q2 FY11 top-line?
Anil Patwardhan  IP contribution has been close to about 2%.

Krishna Mahale  Okay. Thank you Sir.

Moderator  Thank you. The next question is a follow-up question from the line of Debashish Mazumdar from Techno Shares & Stocks. Please go ahead.

Debashish Mazumdar  Just wanted to understand what are the billable employee numbers in this quarter?

Sunil Phansalkar  If you look at our investor updates, you will as stated the total number of development stuff. So if you look at 5189 is the total development team average, that is the billable team.

Debashish Mazumdar  Okay. Thank you.

Moderator  Thank you. There is a follow-up question from the line of Sangam Iyer from Alf Accurate Advisors. Please go ahead.

Sangam Iyer  Sir, just a follow-up on the SG&A, if you look at it and the absolute terms, there has been a slight increase. Is it that any incremented cost because of acquisition, etc. that is also a part of this?

Ravi Pandit  Sir, there is some cost, which is a part of that and that is what we mentioned that we have expense out some of the cost related with that division.

Sangam Iyer  How much would that we would share then which would be non-recurring?

Anil Patwardhan  Basically it was explained by Sunil earlier, here the part of cost will also flow in quarter three and there is like deal related cost, so would not like to give details at the deal levels.

Sangam Iyer  Okay, but would it be fair to assume that SG&A at the current level is something that there will not be much increase from the current levels going forward.

Anil Patwardhan  That is true.
Moderator  Thank you. Ladies and gentleman as there are no further questions, I would now like to hand the phone back to Mr. Hitesh Shah. Thank you and over to you Sir.

Hitesh Shah  On behalf of IDFC Securities, I would like to thank you KPIT Cummins for giving this opportunity to hold this call, and also thank all the participants for dialing in with that I hand over back to management for closing remarks.

Sunil Phansalkar  Thanks Hitesh and thanks everybody for participating in the conference call. I hope we have been able to answer all of your questions and queries. If you have anything else, which you want us to answer, please feel free to write to us and we will be very happy to get back to you. On this note, I once again wish you a very Happy Diwali and a Prosperous New Year ahead and enjoy the holiday. Thank you very much.

Moderator  Thank you very much Sir. Thank you gentleman of the management. On behalf of IDFC Securities Ltd, that concludes this conference call. Thank you for joining us and you may now disconnect.