"Mphasis Limited Q1 FY21 Earnings Conference Call"

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MANAGEMENT: MR. NITIN RAKESH – CHIEF EXECUTIVE OFFICER, MPHASIS LIMITED
MR. MANISH DUGAR – CHIEF FINANCIAL OFFICER, MPHASIS LIMITED
MR. SURYANARAYANAN V – EX-CFO
MR. VIJU GEORGE – HEAD, INVESTOR RELATIONS, MPHASIS LIMITED

Moderator: Good morning, ladies and gentlemen. Thank you for joining the Mphasis' Q1 FY 2021 Earnings Conference Call. I am Lizann, your moderator for the day.

We have with us today Mr. Nitin Rakesh – CEO of Mphasis; and Mr. Manish Dugar – CFO. As a reminder, there is a webcast link in call invite mail that the Mphasis management team would be referring to today. The same presentation is also available on the Mphasis website, www.mphasis.com in the Investor section under financial and filing, as well as both the NSE and BSE websites. I request you to please have the presentation handy.

As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Shiv Muttoo from CDR India. Thank you and over to you, sir.

Shiv Muttoo: Thank you. Good morning, everyone. And thank you for joining us on Mphasis Q1 FY'21 Results Conference Call. We have with us today Mr. Nitin Rakesh – CEO; Mr. Manish Dugar – CFO; Mr. Suryanarayanan – Ex-CFO; and Mr. Viju George, who has come in earlier this week as the head of investor relations.

Before we begin, I would like to state that some of the statements in today's discussion may be forward-looking in nature and may involve certain risks and uncertainties. A detailed statement in this regard is available on the Q1 FY’21 results release that has been sent to all of you earlier.

I now invite Nitin to begin the proceedings of this call forward. Over to you, Nitin.

Nitin Rakesh: Thank you, Shiv. Good morning, everyone. Thanks for joining us on this call this early. Before I start, I would like to welcome Manish Dugar, our new CFO, to this call. As you are all aware, Manish took over last quarter from Surya, who has been with us for over a decade. Surya is on the call as well and will continue to support Manish until he superannuates in October 2020. I would also like to welcome Viju George, who recently joined Mphasis team as Head of Investor Relations, and he will soon be interacting with many of you.

We will walk you through the presentation, which is also available on our website. I trust you had the opportunity to go through our Q1'21 results and other operational performance information in our MD&A. In addition to the MD&A, we have published an annexure, which highlights the changes in the way we report our numbers as well as uploaded the historical trends in the revised reporting. The MD&A reflects how we run our business. To mirror this, we have made the following changes:

- Aligned to the discussions on our last earnings call, the clients with whom Mphasis has a direct contract, which were earlier included in the DXC/HP business, have been moved to Direct Core business. As such, DXC will now be reported on a standalone basis compared to the DXC/HP classification earlier.

- Client metrics have also been aligned to reflect Mphasis' direct channel clients. All clients that are coming through the DXC channel are now clubbed under the DXC standalone reporting.
- Alignment of the definition of some of our cost allocations with the industry standard definition of gross margins and SG&A. There is no impact of any of these changes on EBIT or EBITDA.
- Some additional information has been provided in revenue breakup, including segment and project type.

Moving on, talking about the customer behavior and the migration to digital, the COVID-19 pandemic has massively driven people, organizations and governments to digitalization and digital platforms as we all try to cope with the disruptions the outbreak causes in our lives: societies and businesses. Some of the biggest shifts in the market share occur coming out of downturns when new industry leaders and new industries often emerge. Most CEOs have already taken the most important first step: make the safety of employees and customers the top priority, beyond travel limitations, in-person meeting restrictions, temporary closure of facilities and rigorous protocols to protect essential operational teams. The rapid adoption of new technologies in times of crisis isn’t new. Still, in this reality in which we now live, the scale is quite unprecedented and has accelerated digital transformation across several areas of society and businesses indeed.

COVID-19 has become the perfect storm for digital acceleration. The pandemic has exposed a clear digital divide. Those companies which had already invested in digital operating models and enablement have fared much better than those which have not. In fact, for many businesses, the continuity of operations critically depends on their digital capabilities. We have seen an acceleration across many segments of enterprises, with the biggest impact being seen in deployment of technologies to enhance customer experience in the new contactless, faceless world of consumer interactions and transactions. As such, what used to be known as an omni-channel experience is quickly transitioning to a digital-first or, in many cases, digital-only experience.

This has created a very quick and massive change in the already shifting consumption of technology amongst enterprises with a huge reallocation of resources into areas such as customer experience, data and personalization, workplace modernization, predictive analytics and as-a-service economy to leverage cost and time-to-market efficiencies, as well as massive transformation programs to reduce the technical debt that has been built up over decades. This also translates into massive shifts in spend from run to change and transform, thereby creating short- to medium-term dislocations in the way enterprises use IT services partners and vendors. The short-term impact has been reallocation of budgets, cuts in hitherto discretionary spend in some areas and the focus is on must have solutions. The long-term tailwinds of legacy modernization across applications, infrastructure and data have also seen massive acceleration and, as such, are creating some large bundled transformation deals.

Mphasis offerings along the tribes, especially zero-cost transformation, where we take on large bundle of client applications and apply service transformation to release operating efficiency to reinvest in change areas, has been a huge area of traction in the recent past. While digital transformation is more necessary during the crisis, not less, that does not mean it will look the same as it did before the pandemic. Resources, both in terms of talent and money, will likely to be constrained. Digital initiatives may need to be reprioritized based on relevance in the current environment. New problems and opportunities may come to light with greater urgency. For some businesses, the forces of disruption may be so great that the long-term strategic vision may need to be overhauled as well. And any digital transformation road map that does not deliver value at every increment will need to be reimagined. The key has been continuing to experiment, innovate with digital solutions front and center. With the right approach, businesses can come out of the fray stronger, more agile and more customer-centric than before.

Companies in all industries plan to reduce IT spending, but those in healthcare, retail and industrial manufacturing saw the deepest cuts in the last quarter. Spending for on-premise hardware and software suffered the most, while investments in SaaS and public cloud increased. While airlines and hospitality verticals faced the largest impact of the ongoing pandemic, sectors, including banking, life insurance, consumer products, etc., faced lesser impact and are expected to recover much faster. These have been highlighted as green zones in the chart. Around 66% of Mphasis' revenue portfolio falls in the green zone with lesser near-term impact and faster recovery.

We have spoken about Mphasis' focus and leadership in core technology areas led by the Mphasis Tech Council, which constantly tracks new technology developments and customer adoption of such technologies and capabilities. This results in appropriate revisions to capability building and go-to-market motions. The adoption of tribe and squads to develop the power of eight from FY '19 has yielded good results and has been much appreciated by our customers. Based on the recent events and feedback from what our client needs are, we have further enhanced the tribe's focus to cover areas such as:

- Next-gen IT operations: Taking a digital approach to both infra as well as application maintenance allows enterprises to save on run budgets and use these savings to power digital transformation. The next-gen IT ops tribe is focused on working on creating these services and, at the same time accelerating adoption of cloud.
- Cyber security: With more and more adoption of digital channels, cyber security has become very critical. The COVID situation has only accelerated this. Cyber-sec tribe is focused on providing this to our customers.
- NEXT Ops. This tribe focuses on business operations. Total rethink of operations by using advances in automation tools, digital devices and AI/ML, helps not only to optimize cost, but also to dramatically improve customer experience and reduce errors

and risks. The NEXT Ops tribe brings the combination of domain specialization and digital and operations knowledge to redefine business operations.

We have also identified certain capabilities and instruments in all the tribes and cut across many of these services. We developed these via guilds, which are made up of people from various tribes and practices.

There are a number of areas where we are focused on enhancing our capabilities. One of the areas was blockchain that we started focusing on a few years ago. This year, we have also started doing work in quantum computing by building accelerators and doing pilot programs with our customers. Increasingly, a large part of the economic value created is coming from digital innovation, ecosystem propositions and new technologies. The roles of future will be built on a triad of skills; domain/functional skills, digital skills and professional skills. This is an opportune time for organizations to reflect on the digital talent base and leverage the downtime to build a pervasive digital skills foundation.

Our revenue performance for the quarter has been impacted to some extent by the ongoing COVID pandemic and softness in DXC. Despite these market challenges, we have been able to grow our business 3.8% Y-o-Y on a constant currency basis in Q1 '21. Excluding the nonstrategic ATM business, revenues grew 4.5% Y-o-Y in constant currency.

- Direct International revenue grew 19.8% Y-o-Y and 2.1% Q-o-Q on a reported basis in Q1'21, and 10.8% Y-o-Y and declined 0.5% Q-o-Q on a constant currency basis.
- Direct Core revenue grew 15.5% Y-o-Y and 0.5% Q-o-Q on a reported basis. Revenue grew 6.9% Y-o-Y and declined 2.1% Q-o-Q in constant currency.
- DXC revenue declined 8.7% Y-o-Y and 12.6% Q-o-Q on a reported basis, and declined 14.3% Y-o-Y and 15.8% Q-o-Q in constant currency terms.
- Net profit grew 3.9% Y-o-Y to Rs. 2,751 million and declined 22.1% Q-o-Q.
- EPS grew 3.8% Y-o-Y and declined 22.1% Q-o-Q. However, a decline of 11.5% on an adjusted basis over Q4 to Rs. 14.75.

As we continue to navigate through this challenging and uncertain environment, we made significant breakthroughs in our TCV wins this quarter. I will talk about these in a few minutes.

We continue to see strong growth momentum and positive outlook in our key focused vertical of banking and capital markets. The segment reported yet another strong quarter and double-digit growth with 12% Y-o-Y growth. We believe this is best-in-class growth in that industry segment and was broad-based across segments of BCM as well as in Digital Risk. This demonstrates the strength of Mphasis as a preferred services provider in banking and financial services industry.

As noted in our MD&A annexure, we are segregating logistics and transportation sub-vertical from the erstwhile emerging industries segment beginning this quarter. Logistics and transportation vertical has been the flag bearer of growth in the emerging industries segment and has grown at a CAGR of 24% since Q1'18. We expect logistics and transportation segment to continue to be a long-term growth driver. We have limited exposure to airline industry at less than 1% of our overall revenue and no exposure to hospitality.

As mentioned on our previous calls, Europe region is a focus area for us, and we are pleased with the fact that our increased sales efforts and investment in this region are yielding good results. Europe region revenue has grown 17.5% Y-o-Y this quarter in constant currency terms. We are seeing good traction here and expect this region to continue to be a growth driver for FY'21.

Moving on to Direct International business and the deal wins:

As noted earlier, Q1'21 TCV wins of $259 million with 79% of deal wins in new-gen areas were the highest ever TCV wins recorded in a quarter, an year-over-year growth of 66%. Q1'21 deal wins include one deal of over $100 million TCV. We have talked about it in the past how our improved GTM sales motion and customer centricity are helping us in winning in the marketplace and in the areas of choice that we desire. This deal stands testimony to both the facts. We have also seen continuous ramp-up in the deal sizes, and since FY'18 we have seen a steady flow of deal wins in the large deal category as defined by greater than $20 million TCV deal sizes. Because we report our TCV on a net new basis only and exclude renewals, we see a robust correlation exceeding 0.8 between revenue and TCV for Direct International. Thus, as we find success in increasing our TCV wins, we believe that this would commensurately translate into higher revenue.

Next-gen services continue to be a focus area and has recorded a Y-o-Y growth of 67% in TCV wins. To give you color on quality of some of the new deals, let me mention a few from the first quarter.

- One of America's largest home improvement retailers signed Mphasis to help set up an implementation factory and operations COE. A new logo for Mphasis, this addresses the clients' priorities of reducing cyber risk while, at the same time, creating synergies across portfolios.
- In a large deal with America's top bank, Mphasis will help clients in managing the home preservation applications process that is receiving increased volumes emanating from mortgage loans going into forbearances. Mphasis will bring domain technology and operations teams together to deliver a bundled approach.
- Another large Tier 1 bank in America chose Mphasis as their partner to deliver strategic programs such as modernization and accelerating cloud adoption project amongst new business programs.
- One of America's life and annuity providers also signed up Mphasis to set up a testing COE that will help the client conduct testing in this annuity product platform. This will enable the client to be nimble and launch new products in the market at a faster rate.

I am also pleased to announce that in addition to the Q1'21 record TCV of $259 million, we have signed another large deal in July of $216 million in TCV spread over three years. This is a global deal, covering multiple geographies and spans across tech services and involves service transformation elements and was signed with an existing client to expand our wallet share. This deal will be reported as part of our Q2'21 TCV wins.

In line with the TCV and revenue growth in Direct International, the broad-based nature of growth is also showing up in our client metrics that are improving consistently. We have been continuously improving the client pyramid and increasing the number of clients across key buckets. In Q1'21, we added one client in the greater than $100 million bucket and three clients in the greater than $75 million bucket since Q1'18. Please also note that these top accounts are our marquee clients with long tenure relationships, some over 15 to 20 years. Further, to strengthen the future growth by creating new drivers, we have added three clients in the greater than $10 million bucket, four clients in the greater than $5 million bucket and twenty clients in the greater than $1 million bucket. Many of these clients are new additions to our portfolio. We have seen good improvement in all these categories compared to Q4 FY'20 as well, as you see on the chart here. We are confident that we would be able to continue to move more accounts into higher buckets through our proven account mining strategy.

This acceleration in revenue and deal wins provides good visibility for future expansion of the Direct International business. It also addresses a key area of long-term concern with all our stakeholders, the concentration of revenues. As you can see from the client metrics, we have added significant diversification in top clients as well as seeded new relationships across the client pyramid. The recent deal wins from Q1'21 as well as the new large deal from July has provided us with the opportunity to consciously restructure our revenue concentration, and as such, de-risk our exposure to DXC from an overall growth standpoint. We also believe that the backstop available over the next few quarters from the MRC construct will provide downside protection to any headwinds. As such, we expect to continue to focus growth in the Direct International business, while we continue to work towards being a strategic partner to DXC and their clients. We believe our long tenure; delivery track record and the complementary nature of our portfolios are amenable for a continued long-term partnership with DXC beyond the MRC tenure.

We are also excited that our relentless focus on technology leadership using architecture and design as well as service transformation and the solution-led approach to go-to-market, coupled with geographical diversification and industry vertical market focus is yielding good results in our Direct Core business. The strong deal win momentum that we have witnessed in the past few quarters has resulted in accelerated growth in our Direct International business as well. Growth has been driven in Direct International by both Digital Risk and other segments of Direct Core such as strategic accounts, new clients and Blackstone portfolio. New clients, including Blackstone portfolio revenue, grew 40% year-over-year in Q1'21.

Moving on to the earnings growth and the cash position:

Q1'21 operating margin has been impacted to a certain extent by the slowdown in revenue and the resultant drop in utilization. Despite the challenges, operating margin improved 20 bps Y-o-Y, driven by operational efficiencies. While we believe we should be able to find more efficiencies in our existing businesses, we are focused on growth opportunities and the ramp-up investments needed for large deals that we have signed recently. As such, we expect to operate in the range of 15.5% to 16.5% EBIT for FY'21. As the market situation evolves in the current crisis, we expect to provide a more updated FY'21 visibility on margin.

Our cash generation continues to be strong. Cash and cash equivalents increased by Rs. 2,747 million during the quarter to Rs. 27,488 million, i.e. $364 million. Adjusting for the Rs. 455 million net loan repayment, net operating cash generated during the quarter was Rs. 3,202 million, i.e., $42 million, highest in the past 15 quarters and a testament to our operational rigor. As such, we also have a very healthy DSO at 62 days despite the current environment.

Moving on to the execution update:

We continue to focus on prioritizing growth, especially in a year like FY'21 when growth will be at a premium and wallet share gains are extremely important. We kept the Q1'21 operating margin stable and expect to continue to operate in the 15.5% to 16.5% range for the rest of the year. We have closed several large deals this current quarter. Our focus will be on executing those deals by ramping up and further expanding our pipeline with new deal wins. We will continue to execute against our plan for FY'21 and beyond.

- Firstly, we continue to focus on accelerating Direct International channel growth with an intent to have growth across all segments of DI. We are also seeing continued expansion in sales pipeline and continued focus is on executing the pipeline to closure and revenue conversion.
- Secondly, we have also set a strong focus on continued improvement in client metrics, as I mentioned before. We have added clients across categories in our client pyramid, driven at the top by gain in wallet share in top accounts, while we continue to add new clients throughout the rest of the pyramid and deploy a well-proven account mining methodology.

Along the same lines, we will also continue to focus on expansion of wallet share at DXC by ensuring long-term partnership construct well beyond MRC, as I mentioned before.

To summarize, I would like to leave you with five points.

- One, growth has bottomed out, and we see growth rates improving sequentially here on.
- Two, our DI growth will continue to be supported by robust TCV that we have added across verticals. In fact, our TCV this quarter is at an all-time high, 40% higher than

the quarterly average in FY'20, not counting the additional $200 million-plus deal that we won in July, which provides us further visibility into near-term growth.

- Three, our track record in wining large deals greater than $20 million is consistently improving. Our client mining metrics across revenue buckets are improving, and we seem to be doing a good job of winning new logos and farming them as well.
- Fourth, we are consciously managing and de-risking our exposure to DXC. This account is likely to see softness, but the backstop due to the MRC till September 2021 gives us enough room to manage this exposure. Going forward, as the center of gravity continues to tilt towards the faster-growing DI piece, the impact on overall growth from DXC's exposure will only continue to lessen.
- And five, margin stability. We have operated in a steady margin band in the recent past. Our margin stability ensures the revenue growth translates into EPS and PAT growth and consistently rising free cash flow generation.

Before I conclude, I would hope that you and your families are safe. And as the world faces health and economic consequences of COVID-19, Mphasis is working to bring the full force of our core business and expertise to support our communities, employees, clients and all stakeholders affected by this crisis. I want to thank all of you for your interest in Mphasis and for joining the call today. We truly appreciate it.

Operator, I request you to please open the line for questions.

Moderator: Thank you very much. We will now begin with the questions-and-answer session. The first question is from the line of Mukul Garg from Haitong Securities. Please go ahead.

Mukul Garg: Nitin, very strong deal wins in Q1 and likely in Q2 as well. So the first question is on that. Is there anything which was more of a near-term change from your end? Did you do something different during the lockdown for the deals to ramp up so much? Or should we see this as an indicator of growing appetite for technology spend by corporates? And will this lead to any change in duration of your deals?

Nitin Rakesh: Sure, Mukul. Great question. For the last couple of quarters, we have seen elevated pipeline. What we saw in the last 120 days since the crisis began was, I would say, a certain sense of urgency on the client side, especially anything involving transformation, digital, tech debt reduction, customer experience. They were already on a journey, and this was a major accelerant. So many of our clients have actually called out for accelerating their programs, and they look for partners that they think have the right service offerings and the right capability set. So, a combination of having the right capabilities, having the right experience and expertise, the right talent, the right relationship and having worked on a number of these deals that were in the pipeline for the last few quarters helped us to close many of those deals and bring them on this quarter.

And your other question was around the expectation going forward. So as we speak, the pipeline continues to be very healthy. In fact, despite the conversion of these deals, we have a fairly strong TCV number in the pipeline. Normally, what you see is after closure of couple of large deals you see a shrinkage in the TCV number, but that number is still holding steady. This means we are generating new deals and closing them as well. So that gives me confidence that we should see some of this deal win momentum continue at least in the near to medium term.

Mukul Garg: Great. And another part, nice work with the reclassification. There were a lot of changes you guys did this quarter, especially on DXC and the cost allocation side. Is this mainly a reporting change? Or has this led to greater streamlining internally in terms of the respective teams' responsibilities and how they operate?

Nitin Rakesh: So I will tell you two things. One, the changes were mostly to reflect the way we run the business. And hence, the client metrics and all those related items have been cleaned up to reflect the direct portion of the business. On the cost allocation side, again, most of the changes really are to bring it closer to industry practices. Because there is no impact on EBIT, EBITDA or PAT, I don't think there's anything more to read in that. The changes were really to simplify some of the metrics, and we have received some constant feedback from a number of our stakeholders in trying to simplify the metrics in a way that they can understand the business better. So, I think that was the attempt here.

Mukul Garg: Understood. I think it was quite well done in terms of streamlining and taking out some redundant data.

Moderator: Thank you. The next question is from the line of Sandeep Shah from CGS CIMB. Please go ahead.

Sandeep Shah: The question is in terms of DXC. Nitin, do you think that this 15% Q-on-Q decline was a negative surprise? Or you were anticipating this as a whole? Because if we look at on a quarterly annualized basis, this works out to be close to a 16% decline if we just annualize the Q1 run rate and divide by the FY '20 run rate of the DXC business as a whole.

Nitin Rakesh: So, two things to think about. One, not a surprise because we have seen this softness in the last three or four quarters. We are comforted by two things, one, there is a backstop available from a minimum revenue perspective, so we still have additional five quarters from now to continue to realign our client metrics in a way that it continues to work in our favor. Two, some of this was a reflection of the environment and the end clients' own business situation. Did it surprise us? The answer is no. Again, as I mentioned, it's a reflection of their end-client environment. But at the same time, given that we have seen some robust deal wins in Direct International, we are fairly heartened by the fact that we can continuously chip away at this concentration issue without making it a massive growth headwind. So from that perspective, we are still growth oriented. We think we can disproportionately continue to grow our Direct International business to account for some of the headwinds that we have seen. And clearly, we know what the backstop number in DXC looks like, so even if the softness persists, at least there is a backstop available to us.

Sandeep Shah: Okay. Just to follow-up, is it an element where some of the work, which has been subcontracted earlier by DXC is getting insourced? Or this is largely a phenomenon where DXC is not able to retain the wallet share because of the pandemic?

Nitin Rakesh: I think it's more of the latter. And again, the bulk of what we are seeing is really a combination of discretionary spend cut or, in some cases, some industries or some regions have been fairly severely impacted. As such, we are not losing wallet share. We are still one of their top partners, and we expect to continue to be so.

Sandeep Shah: Okay. And just last follow-up, Nitin. Looking at deal TCV in the Direct Core, it's very heartening. So you believe this would be net positive after factoring into a decline of DXC? Or you believe, no, this was required to compensate the DXC growth headwinds which are coming? And the net positive impact may not be that big what you were seeing now versus what you were seeing maybe three, four quarters back or maybe three months back?

Nitin Rakesh: So, I mean, I think the question is, how you should think about growth for the year versus what should be the net impact of the two units, is that the question?

Sandeep Shah: Yes. So are you more positive now on the growth outlook for FY '21 on overall consolidated revenues versus maybe three or four months back when these deal wins were not in the bag?

Nitin Rakesh: Yes. So basically, having pipeline is one thing. This is I think our third quarter of over $200 million in TCV wins. But this quarter is, obviously, a blowout quarter and plus we have an additional deal from Q2 that we have already announced at $216 million. So overall, I am more positive now than I was at the end of last quarter. We already called for growths having bottomed out. We do see for the company and, of course, for our overall direct business sequential growth starting Q2. So our expectation is that despite the challenges that we have seen in the short-term from the DXC softness, we do expect to end the year in positive growth.

Sandeep Shah: Okay. And congratulations on a very good order book.

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

Mohit Jain: First is on the reclassification. So, the DXC revenue that you disclosed now on a quarterly basis, this is not be considered as part of MRC?

Nitin Rakesh: Sorry, I lost you there for a minute. You said the DXC revenue that we are disclosing on a standalone basis is actually the only portion that is considered MRC?

Mohit Jain: Is it directly MRC-related revenue or is there some component?

Nitin Rakesh: Yes. I mean, the DXC portion is the only portion that will go against MRC, there is no other client that is reported under the MRC number anymore.

Mohit Jain: Okay, perfect. Second on pricing, what is your view there? Given that we have not seen any price realization change so to say in 1Q, now are things stable? Or you think there could be something coming in third quarter, which is built into your outlook?

Nitin Rakesh: No. So, what you see is the headline number. It's been a mixed bag. In some cases, where there has been pressure from clients on the legacy business to fund the new digital development or transformation work, there I think we have had to deploy some constructs like zero-cost transformation, where we managed to find them operating expense savings to deploy and, of course, in return for longer-term deals. So we have used the crisis to construct larger deals. We have used the crisis to get deeply embedded with some of these clients in helping them find those savings and, in the process, gain wallet share as well. So as such, we have converted some of these pricing headwinds into opportunity areas. I think it's a work-in-progress. The pandemic is far from over, so depending on how long the things continue, we may see in pockets some of these conversations pick up again. But broadly, the reason we are calling for stability in margin is because we do believe that given our service portfolio and our ability to run our tight shift from an operations standpoint, we do believe that we should be able to maintain margins.

Mohit Jain: Okay. And third on G&A cost; there was a big decline on a Q-o-Q and Y-o-Y basis. When do you expect some of these costs to start coming back?

Nitin Rakesh: Yes. I think bulk of the G&A decline was due to one-time costs that we had for professional services in Q4, which we don't think will come back fully in the cost anyways. But having said that, the new abnormal will give us some tailwinds from savings perspective, especially in areas like travel. We are not probably going to go back to the levels that we saw before, but at the same time there are other headwinds from things like technology expenses, cyber security. So in a way, we are basically using the puts and takes to ensure that we keep margins stable.

Moderator: Thank you. The next question is from the line of Rahul Jain from Dolat Capital. Please go ahead.

Rahul Jain: Congratulations on very strong order book momentum. Just one question on the same. Could you share more inputs on what has been driving force in terms of your service offering or market positioning? You have said about meeting the demand, the kind of demand that the clients are seeing. That is one aspect, but if you could give more on that.

And secondly, I believe current quarter wins include a large win from mortgage segment. If that is the case, then just wanted to understand what is the fixed or variable element on deal size. Because in Digital Risk we have seen much different outcome if environment changes on the actual realization of the deal. So just if you could share on that.

Nitin Rakesh: Yes. So it's two distinct questions. Let me take the first one. Basically, what you are asking is, what is the differentiation that leads us to be able to close these deals from a competitive standpoint. So if you remember in my script, and it's actually on Slide 6 of the deck that we laid out today, we have talked about leading with certain technology areas. We call them technology tribes. And we have continuously upgraded those tribes, invested in innovation and experimentation through our NEXT Labs, focused on creating a tech council-driven approach. So the focus on design, architecture and engineering-led approach, where, as clients are looking for agility and nimbleness in their business because the time pressures are very different right now, the way they are consuming technology is dramatically shifting. And we are a services provider in helping them consume tech. So, if they are going to consume technology differently, they are going to also need a different partner who can actually help them think through how to consume these new technologies. So bulk of the pipeline origination happens through this early engagement by helping them think through the right problem to solve, not waiting for them to put out an RFP. I mean, in the past we have also talked about the fact that +80% of our net new TCV has been proactively generated. And being this thinking partner, thinking doer, a partner who can help them think through the problem and then execute the solution has been a great position to take versus waiting for them to define the problem and then run a competitive RFP process that creates longer sales cycles and very competitive pricing pressure. It's a whole different way to sell. So, we have taken the approach of really investing in upfront capability and leading the clients through this changing in IT environment.

On your second question around TCV wins and one of the large deals coming from mortgage, I think we have also restructured, and I have called for this sort of consistently in the last five or six quarters. We have restructured the way we run that business quite dramatically on three fronts. Firstly, we have integrated the entire client go-to-market as part of our direct channel. It's an integrated selling model. Mortgage services happens to be one additional sleeve of services we offer, so that's the first big difference. Second, we have also bundled a number of transformation services along with mortgage operations. So that basically means that you end up creating a much stickier longer-term transformation program, and the idea is to get longer-term visibility into some of these deals. And thirdly, we have also added additional areas that some of them are countercyclical and some of them are cyclical. In the sense, if some of those areas, for example, refinance is interest rate sensitive, so interest rates go down, refinance volumes go up. We also have added sleeves like loan processing, home equities, which is completely countercyclical to refinance and origination, which is also countercyclical to refinance. So the idea is to build a portfolio of client services that are bundled into our overall GTM, monetize the same relationship, because in the end the banking relationship is the same. The banks that we are dealing with are still the large banks that have a large spend in both tech and ops and continue to win wallet share by cross leveraging these capabilities.

Rahul Jain: Right, that's quite helpful. If I could ask one more. You shared more inputs now and broken up the DXC segment. So, if I see the three elements which we used to share long, long back, I see the direct contracting part of that channel has been impacted the most in the last one year. So, is it just more a conscious choice? Or is it just too small a data to think on that?

Nitin Rakesh: Yes. I mean, 80% of the channel anyways was DXC, and it was getting a little jumbled, so we wanted to clean it up. The non-DXC piece, primarily the HP pieces were anyway is now directly contracted, there is no correlation to the shareholder agreement or the MRC So we thought we will do a clean cut. We have, in line with that reclassification, also reclassified the client metric because even though client metric used to create a lot of confusion as to how the top clients are performing because there were puts and takes there as well. So this is the way we run the business, this is the way we monitor the business and our growth, and this is the way we want to report it so you can actually track the same growth that we track.

Rahul Jain: Okay. Thanks for simplifying the metrics also. Just a small suggestion if you would like to consider sharing dollar revenue data also.

Nitin Rakesh: Sure.

Moderator: Thank you. The next question is from the line of Sumit Jain from Goldman Sachs. Please go ahead.

Sumit Jain: Congrats, Nitin, on a great execution. So, my first question is on your large deal of $216 million. Can you just let us know was it in the pipeline going into the COVID situation? And in which vertical is that, is it your existing client or new client? And was it done virtually so that we can understand that such kind of deals can come up while the pandemic is ongoing?

Nitin Rakesh: Sure. So, I would say, the initial phases of the deal was in there in March, maybe February-March time frame, but the deal really picked up steam and got shaped, I would say, in Q1. Secondly, the deal is with an existing client, we will give you more details on that in the Q2 call. But effectively, this is a long-standing client relationship and will position us very well to become a major preferred partner with that customer. It is not in the banking segment.

Sumit Jain: Got it. Got it. No, great, Nitin. And secondly, on the Blackstone portfolio side, I mean you guys had a 40% growth out there. So, can you just help us understand what contribution Blackstone portfolio has in your direct channel, firstly? And secondly, as a proportion of Blackstone portfolio companies, how much of them have you reached out and how much are yet to happen?

Nitin Rakesh: So, Sumeet, we stopped reporting BX separately because that was ending up becoming a secondary segment. So what we are now doing is we are not reporting new clients and Blackstone separately because all of those clubbed in are basically new clients which were all acquired in the last 12 to 18 months. As of Q4 exit, Blackstone contribution to overall company revenue was between 4% and 5%, and it is growing at a steady clip. From a penetration standpoint, we are still only scratching the surface because we have talked about north of a dozen clients. But given that even if we assume that we are doing $50 million, $60 million a year or so number as of Q4 exit, if we assume that the spend is very, very high, probably north of $1.5 billion, then of course we are still at low single-digit wallet share. Now of course, there is no one buyer, the buyers are fragmented across (+200) companies. But this is a very steady sales motion. We have created a separate go-to-market engine around it, we have dedicated teams focused on it. And we see a steady clip of those deals in our pipeline as well as our conversions every quarter, including this quarter. So there is a long road ahead. And I have routinely said that we can double it and then double it again in the next three years. So it's a fairly strong visibility and runway ahead. The question really is to continue to execute it, because these are discrete buying entities, so you are selling to each individual operating company versus a centralized buying unit.

Sumit Jain: Right. No, great execution on that side. And lastly, I wanted to understand around your outlook for the BCM vertical, where you had a very strong growth, and on the insurance side, where we actually saw some weakness.

Nitin Rakesh: Sure. So insurance weakness was probably a little bit more discretionary spend-led. We do expect both BCM and insurance to have good sequential growth because, both of those have been in the pipelines that we have converted and we continue to execute on. I think the ramp-up periods were a little delayed in the early part of Q1 because even though we were ready to do remote onboarding of employees, our clients took some time because they were not equipped to remote onboarding and remote transitions. So some of that will also get a little bit more addressed, has been getting more addressed over the last four to six weeks and will continue to keep getting better because now this remote operations have become a little bit more routine and stable. So we do expect both BCM and insurance to have sequential growth from here on.

Moderator: Thank you. The next question is from the line of Ashwin Mehta from Ambit Capital. Please go ahead.

Ashwin Mehta: Congrats on strong deal wins. Nitin, just wanted to understand the competition profile in these large deal wins. And what were the ingredients that helped you against possibly strong large players in these deals?

Nitin Rakesh: Great question, again, Ashwin. A few minutes ago I talked about the fact that the best way to win a deal is by making sure that you understand what is it that the client is trying to solve for, and that only comes with early engagement and deep engagement with clients along the principles of design and architecture. This means if we know what they are trying to solve for: are they trying to solve for a business problem of cost, which almost always is the case, but almost never is the only thing, or are they trying to solve for a certain other problem that may be a lot more acute in the current environment. So this extreme obsession with early engagement and originating a deal when clients are thinking about problem-solving versus them having defined an RFP, they may choose to do an RFP later. But that doesn't mean that we may not have been in discussion with them for that particular area much before the RFP was constructed. So this early engagement is, I would say, the biggest thing that helps us. Not easy to do because it requires a very different profile of people, whether architects, design engineers, domain consultants, digital designers, and a whole bunch. So that is the investment that I talked about having made over the years in the whole tribe model.

Second thing is, you asked me about competitive profile. Everybody from the Tier 1 global providers to large India-centric players to global system integrators to niche European players to midsized companies, I think the competitive profile is pretty much anybody and everybody you can think of is typically in some account or the other. And most of the large deals that we are winning are actually against some of the very large companies that we end up competing with, because typically clients bring in a champion and a challenger to do a break-off. So, from that perspective, I think it's been very heartening to beat some of the very large players in their own accounts, where they actually have a longer-term presence or a much bigger presence than we have had.

Ashwin Mehta: Sure. My second question was on DXC. So, we have an MRC of around $200 million. We are probably running around 20% higher than that. So, going ahead, historically, we have been ahead of that MRC number in terms of our performance. Do you see this approaching the MRC numbers? And secondly, how should we think about the DXC relationship post the MRC?

Nitin Rakesh: So, Ashwin, the reason I called out for the $300 million pending MRC as of the end of March, which basically means $300 million over six quarters, so we have $250 million more to go between now and September 2021. So that number, you can think of that as a backstop. What the backstop basically means that that's the comfort line, and that's how the deal was constructed when the transaction happened between the two shareholders back in 2016. Do we expect to continue to find opportunities to work with them between now and September and beyond September 2021? The answer is yes. Because, again, keep in mind, tenure, business portfolio, understanding of those clients, domain, geography, a number of these things, we are not a plain and simple subcontracting staffing provider to many of these relationships. So, I think we have a very good collaborative understanding of where we bring value in these relationships, how we can help them find growth and so on. So the way to think about it is that, yes, the risk exists that we will tend towards MRC in the current environment, given whatever is the market situation and whatever their clients are going through. But the fact that we have another five quarters, the fact that we have some backstop ability and the fact that we continue to grow everything else around it fairly aggressively with deal wins should give us a nice landing zone over the next five to six quarters.

Moderator: Thank you. The next question is from the line of Ravi Sundaram from Sundaram Family Investment. Please go ahead.

Ravi Sundaram: Congrats on the excellent set of numbers. Sir, just one question. My question was, let's say we are having these deal wins right, $20 million deal wins. Now if I have to spread out the revenue visibility in my calculations, how should I look at it?

Nitin Rakesh: So the typical tenure of the deal wins is anywhere between two and three years, because none of these are shorter-term programs or projects. You can't really construct a very short-term deal with a very large number. So if you look at the over $20 million deals, they will typically have a tenure of between two and three. In some cases, there may be a five year deal, but that's less common to go beyond. As we get into some bundled deals where we are doing tech transformation, IT operations and business operations, we may even have the opportunity to do more than five year deals as well. So that's the reason when we talked about the $216 million July deal, we called out for that to be a three-year deal. So, if you look at the best way to plot this is by using the correlation that we provided between TCV wins and revenue growth, and that correlation stands at 0.83 right now.

Moderator: Thank you. The next question is from the line of Abhishek Shindadkar from Elara Capital. Please go ahead.

Abhishek Shindadkar: Congrats on great execution. Just a question on the segmental results that you gave. Margins on some of the segments like logistics and emerging industries seem to be far ahead than the other average. So how should we read it? Is there a scope for margin expansion in the other segments? Or maybe if you can just give the puts and takes, that could be helpful. And I have a follow-up then.

Nitin Rakesh: Sure. Yes. So, the way to think about it is, it's a reflection of the nature of work we do. I think there was another question from one of your peers earlier on, which basically was, there was a little bit of confusion saying logistics and transportation should be a headwind in industry in this environment. A lot of the work we are doing really is in enabling things like e-commerce, last mile and online delivery. So it's really the nature of the digital work that we are doing. And, of course, the way we have constructed some of those relationships to have a little bit more leverage in terms of the profitability profile. So it's a combination of skill type, delivery type, location type, contract type, that gives us the ability to drive that kind of profitability in those segments. Is there an ability to drive that same profitability in other segments? The answer is yes, but I think some of the other segments are a little bit more hypercompetitive, especially the BCM segment. So I think there is probably a little bit of a cap in expanding margins there, unless of course we find deals that give us the same construct that we have applied to in some of the other verticals.

Abhishek Shindadkar: That's helpful. And the second one is just a clarification. With the change in the segmentation between DXC and the direct portfolio, does that also change our client classification as well? Last quarter, you had mentioned that DXC was the large client. So, does that also change now? Thank you for taking my question.

Nitin Rakesh: Yes. So if you look at the client metric chart in the MD&A, we have a chart that talks about client concentration and that chart does not include DXC. We have already called out DXC to be 20% of revenue, but that's outside of that chart. So, all the clients that you are seeing in terms of concentration, so the top client at 12% is not DXC. Because we have already called out DXC as a standalone 20% number. So, this is a complete Direct International client metric only.

Moderator: Thank you. The next question is from the line of Rishi Jhunjhunwala from IIFL. Please go ahead.

Rishi Jhunjhunwala: A couple of questions. One, just wanted to understand your cash generation has improved significantly over the past three quarters. And we can see a sharp decline in the debtor turnover days as well. Just wanted to understand what is the reason behind that, is it due to the change in business mix probably declining DXC share? Or have we done significantly better in terms of working capital management?

Nitin Rakesh: Yes, Rishi, that's a great question. It's a combination of everything you have talked about. Also keep in mind, I called out in the last earnings call the fact that there was a misconception on segmental profitability as well or the secondary segmental profitability. And given that we are starting to see a higher contribution from the direct business in the overall revenue, that also means that the overall contribution to profitability is much higher as well. So that helps. And then of course, better rigor and execution of receivables, contracting and invoicing helps as well. So we have just continued, especially in the current environment, profitability and cash flow was a very strong area of focus for us as we entered into March. And I am very glad to see that both for Q4 2020 and Q1 2021, we have done a great job in managing cash flow and receivables.

Rishi Jhunjhunwala: Great. And secondly, I think, in your initial remarks, you mentioned that the $200 million-odd deal that you have signed in July is for a period of three years. Just wanted to understand when do you expect that to ramp up? And lastly, a bookkeeping, if you can give the hedges amount with the realizable case?

Nitin Rakesh: So, I will answer the first one, and then I will have Manish maybe take a couple of minutes to answer the second one on the hedges amount. The three-year deal ramp-up should start in Q2 and probably take till Q3 end to do full ramp-up, because there is a transition period of between three and six months. So that's the way that deal is structured. And Manish, can you quickly talk about the hedges and the amounts?

Manish Dugar: Sure, Nitin. So, from a policy perspective, we have taken a conscious call that we would take simple hedges coverage for 100% of the exposure for the first year and declining percentages over the subsequent years. As we speak, and I am not getting into the cross-currency hedges, on a dollar basis, we currently have that coverage fully taken at an average exchange rate of about Rs. 75.5.

Moderator: Thank you. We will move on to the next question that is from the line of Madhu Babu from Centrum Broking. Please go ahead.

Madhu Babu: Sir, On the large deal we have signed, what is the amount of rebadging of employees if at all it is there,?

Nitin Rakesh: Sorry, is the question what is the amount of rebadge?

Madhu Babu: Yes. Are we taking over any employees as a part of the deal?

Nitin Rakesh: No, we are not taking over employees as part of the deal, we are transitioning employees.

Madhu Babu: Okay. From the client to us or from another vendor?

Nitin Rakesh: Other vendors.

Madhu Babu: Okay. And second, on the health care, retail and manufacturing verticals, sir. I mean, so what are the areas of strength? And can you elaborate more on that vertical since we are not discussing much on that?

Nitin Rakesh: Yes. it's something that was led by our healthcare product business. But what we have done is slowly but surely, we have built a small services business around that, and we are using that to create an entry into mostly the health insurance side of the house. So, while it's been a growing business, it's still a little bit subscale, and we will continue to create additional scale in that business as we execute.

Madhu Babu: Would there be any acquisition in these verticals? Because all of three are subscale, and that can actually diversify our vertical footprint.

Nitin Rakesh: Yes. I think acquisition strategy is a little bit longer term than just based on vertical strategy. It's a little bit more focused towards capability. I mean, if you look at the track record, we have created, for example, a completely new vertical out of the emerging verticals with logistics and transportation. So, I think that's a good way to continue to create new verticals that can give us growth. If we do find an opportunity either for geography expansion or for vertical expansion, we will look at that. But right now, the focus is more on capability buildup through M&A. And in some cases, if we can find a way to add clients, add revenue, add verticals, we will be looking at that as well.

Moderator: Thank you. The next question is from the line of Ashish Aggarwal from Principal AMC. Please go ahead.

Ashish Aggarwal: Sir, most of my questions have been answered. Sir, just one clarification on the deals which we report. Do we include the incremental deal where the duration of the deal has got increased maybe in the second year or after second year?

Nitin Rakesh: So basically, we will only include the net new portion of any deal. If we were in a client and we sold a $10 million deal, and in year two, if we sell another $5 million in the same project, we will report the $5 million.

Ashish Aggarwal: Okay. Sir, my question was that, let us say it's a three-year deal, and in the second year, it got extended for another two years, that incremental two years will be included in that part?

Nitin Rakesh: No. We treat that as a renewal.

Ashish Aggarwal: Okay. And how has been the renewal? Because we started to see a lot of deals signing from somewhere in FY '17, FY '18. A lot of those deals would be coming up for renewal. So how has been our renewals been?

Nitin Rakesh: Yes. I think again, if you look at the correlation between TCV wins and revenue growth and the correlation is 0.83, which means that our renewal rate is actually quite high because, otherwise, we will only be backfilling previous deals that are not renewing. That's why we gave out the correlation between TCV wins and revenue growth. We should be able to back calculate the renewal rate from that.

Ashish Aggarwal: Okay. Got it. And lastly, on the margin side, because the DXC proportion will keep on declining, will that be a margin lever for us going forward?

Nitin Rakesh: I mentioned earlier that the contribution of Direct International in both revenue and operating profit will continue to increase as this migration continues.

Moderator: Thank you. We will move on to the next question that is from the line of Apurva Prasad from HDFC Securities. Please go ahead.

Apurva Prasad: Nitin, I think you clarified this, but just wanted to recheck again. So the $216 million July deal, would this entirely be in new scope for the 3-year deal which you mentioned? And secondly, just the Digital Risk revenue for the quarter and the outlook in that segment.

Nitin Rakesh: Yes, Apurva. Absolutely. We only report net new deals. So, if I am reporting a $216 million deal, that is only net new revenue, that does not include any renewals, but it is with an existing client. All of that $216 million is net new revenue. And again, I mentioned, that does provide us a little bit more comfort against the short-term weakness that we are seeing in the other large client. On the Digital Risk business, I think it's seen some robust growth sequentially, and I think the earlier band we had given was the $28 million to $30 million band. We are far north of that band right now, and we do expect that the current revenue from Q1 still has an upside bias, I would say, over the next two to three quarters.

Apurva Prasad: And what would be the current revenue for the first quarter in DR?

Nitin Rakesh: Manish, can you give the DR revenue for Q1, please?

Manish Dugar: Yes, Nitin. It is $35.5 million.

Moderator: Thank you. The next question is from the line of Rishit from Nomura. Please go ahead.

Rishit Parikh: Congrats on good execution. Nitin, just wanted to understand on the Blackstone portfolio. It's been about 4% to 5% of the revenues for a while. What is the additional level of investments which would be required, which can help propel growth in this segment? Because I think this could be an important growth driver in the next, say, three to five years for us, right?

Nitin Rakesh: Yes. It used to be 3% to 4% of direct core revenue. Now it is 4% to 5% of company revenue. So it's actually not been static, it's been growing. And it's been growing in an environment where the rest of the company is also growing, but it's growing faster. So the fact that we talked about growth rates in excess of 40% should give you a sense that it's actually become more and more meaningful. So the confusion always happens whether it's 4% of overall or 4% of direct core. When we started talking about it a few quarters ago, we were only talking about a percentage of direct core. Right now, it's between 4% and 5% of overall company revenue, which I think it was 4% to 5% of direct core revenue only.

Rishit Parikh: Right. And from an additional investment...

Nitin Rakesh: So yes, I mean, there is always a maturity curve in these sales motions, go-to-market motions. We have made adequate investments. We will continue to scale it up as we continue to succeed in the channel. If you just add manpower without having the right strategy, the right track record, and the ability to actually engage, then that wouldn't have yielded results. So we are fairly focused on continuous investment, and that's the reason why we continuously keep seeing additional deals and conversion in the pipelines.

Operator, we will take one more question, and then we will close the call because I actually have to get on another engagement call.

Moderator: Thank you. All right, sir. Our next question is from the chat window from Nitin Padmanabhan from Investec. Please go ahead.

Nitin Padmanabhan: The question is are margins likely to be weaker than the stated range in the interim, considering the large zero-cost transformation deal wins?

Nitin Rakesh: So Nitin, the fact that we are guiding to a 15.5% to 16.5% EBIT range means that we expect to operate in that range for the remainder of the year. As I mentioned, there were puts and takes on the margin side both from a savings perspective as well as certain headwinds. But net-net, I think the way we are managing this business is to make sure that we are able to manage all of those and reinvest whatever we have saved to keep the margins steady in this range. So we expect the range to hold for the remaining three quarters. And of course, we will get a better idea and, if there is a change, we will update you in the coming quarters as well.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to Mr. Nitin Rakesh for his closing comments. Please go ahead.

Nitin Rakesh: Thank you, operator. Given that the core business of the company is in providing technology solutions to global enterprises, we have in the past few years made several strategic investments in next-gen technologies, with a unique customer-centric front-to-back transformation methodology, anticipating the needs of a future-ready business. New emerging technologies were changing the way businesses operate, and we were helping organizations to reflect the same in the right infrastructure by leveraging a cloud-first, cognitive-first targeted approach. This foresight and the resulting pivot have climbed the company to leverage the current opportunities, unearth new areas of engagement and make significant gains.

Going forward, there are certain trends that are likely to be secular tailwinds for our business. Digital workplace, digital commerce in all industries, cyber security, automation and, most importantly, the ability to apply this transformation to traditional business models. To that effect, we launched a new Mphasis brand positioning with the Next Applied in 2018 and are now launching our next campaign around accelerated transformation of enterprises to help our clients apply this transformation with speed, agility and efficiency. Just like our brand re-launch, we are focused on strengthening our position through this period of uncertainty and are excited about our company's competitive strengths and differentiated offerings.

Thank you for staying invested in Mphasis, and we hope to meet you all in person sometime soon. Thank you so much.

Moderator: Thank you. Ladies and gentlemen, on behalf of Mphasis Limited, that concludes this conference. Thank you for joining us. And you may now disconnect your lines. Thank you.