"Mphasis Limited Q2 FY 2021 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. VIJU GEORGE – HEAD, INVESTOR RELATIONS, MPHASIS LIMITED

Moderator: Good morning, ladies and gentlemen and thank you for joining the Mphasis' Q2 FY'21 Earnings Conference Call. I am Janice, 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 call over to Mr. Shiv Muttoo from CDR India. Thank you and over to you, sir.

Shiv Muttoo: Thank you, Janice. Good morning, everyone. And thank you for joining us on Mphasis Q2 FY'21 Results Conference Call. We have with us today Mr. Nitin Rakesh – CEO; Mr. Manish Dugar – CFO; and Mr. Viju George – Head, 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 Q2 FY'21 results release that has been sent out to all of you earlier.

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

Nitin Rakesh: Thank you, Shiv. Good morning, everyone. Thank you for joining us on the call today. At the beginning of the year, all of us expected a very different 2020. However, here we are in October, with just a couple of months to 2021. I hope you and your families are staying safe and healthy.

I would like to focus my commentary on four key items today; first, brief macro trends; next, our response to these trends and progress with the implementation of our strategy; third, our second quarter operational and financial performance; and lastly, a summary of our near-term outlook.

Companies in every industry took steps early in the pandemic to protect and support employees, customers and their businesses while trying to plan for an uncertain future. In the technology sector, it created new unexpected growth as people around the world scrambled to replicate their lives in a virtual format with the help of technology. Companies are now positioning themselves for a world of continued turbulence and regular shocks to the system, where adaptation and resilience will matter most.

At the same time, the pandemic has spurred enterprises to reshape many aspects of their businesses. While the immediate term focus was on resilience, enterprises have now begun to

move on from being in crisis management mode to accelerating the transformation to stay in lockstep with the consumers as well as to adjust to the new reality. If I were to sum up the phenomena in one sentence, it is a shift in stance from almost every enterprise and every industry, moving from trying to be “omni-channel” to adopting a “Digital-First” and, in many cases, a “Digital-Only” business model. From examples in media and entertainment, financial services, to all forms of retail, even including auto sales and restaurants.

Retooling the supply chain and engagement model to support this pivot has become an urgent priority for many leadership teams. They want to make them nimble, responsive, and customer-centric, not just cost effective, and are accelerating and programmatically scaling up their transformation programs.

With customer centricity as the pivot, we introduced Mphasis Front2Back, (or F2B as we call it) over three years ago. While customer centricity may sound like every company's purpose, our F2B solutions enable clients to achieve scalable, digital future-ready operations faster. Our solutions combine multiple transformation levers to deliver quick returns on investments while lowering the overall total cost of ownership. F2B not only helps drive digital transformation for existing clients, but it is also giving us access to new accounts and larger deals. We invested at the right time in building capability and scaling up our sales and marketing engine for large deal wins.

As we move forward and talk about some of the transformation pillars, we have redefined our transformation along four key dimensions:

- First, Portfolio Next: We have spoken about our tribes and squad model in the past. Now we are transforming existing tribes and creating new ones to capitalize on changing customer needs. These new offerings are driving increased pipeline and large deal motions with higher deal value on an average, as we will shortly see in the next few updates.
- Secondly, on the Go-To-Market Transformation: We have been steadily expanding share of wallet and winning against competitors in key strategic accounts. Many of our top accounts have gone through vendor consolidation exercises, and we have managed to retain preferred vendor status in all of them. This includes accounts in our top five list as well. Our hunting teams have also been realigned to focus on high-growth verticals and on a cloud partner-driven go-to-market strategy. As we look towards upping our go-to-market motion, we have adopted a number of approaches to adjust to the digital format, including retooling our fields, ability to conduct workshops, assessments and design studios in a virtual mode, as well as introduced deal constructs that allow multiple levers to be used in engaging with clients on specific opportunities to align with the need for agility, resilience, transformation or cost. We continue to generate new leads from existing and new clients despite the current environment, contrary to the popular belief that the crisis would dent the hunting process, especially in new clients.

- Thirdly, on Delivery Transformation: While we are sharpening our GTM and solutions, transforming our delivery unit with next-gen practices has been a priority. Our delivery-next project is tasked with digitizing delivery, while reimagining the model for a remote world, like the one we are currently in.
- Finally, on Talent Transformation: We have been on this journey since 2017, and it is imperative to upscale and train our digital workforce that is aligned to our new portfolio offerings. You have seen and heard of our Talent Next platform in the past. Through this, we have trained two-thirds of our workforce, including certifications and active requirements. This has continued to be an extremely powerful supply chain and operating lever for us.

While the cloud infrastructure is getting commoditized, enterprises have been increasingly adopting cloud technology into their digital journey, thus driving growth in the cloud sector. We doubled down on cloud as a focus area for partnerships and have reorganized our go-to-market approach to focus on selling via the partner channel as well. Our industry expertise and our tribes leverage these partners to build an end-to-end offering. Our cloud-focused partnerships have helped expand our pipeline with the contribution of cloud to the overall pipeline at 36%. This slide here shows you the impact and the movement we have witnessed in our pipeline.

- We have relentlessly strengthened our relationship by having dedicated channel teams to align with our partner go-to-market teams and bring in product road map visibility to generate early pipeline.
- We have also built capabilities and scalable solutions to stay relevant for our partners such as AI/ML-led competencies, infra management for AWS, etc.
- Finally, we have invested significantly in improving brand positioning and recall, thanks to our hybrid cloud offerings around the key objectives of leveraging the best innovations in enabling agility, resilience and cost savings for our clients. Case in point is Mphasis' proprietary cloud management platform, InfraGenie^{TM}, that offers intelligent predictive analytics and has helped several enterprise clients achieve a zero-touch operations state.

Our labs and dedicated center of excellences build value-adds and accelerators on top of the partner technology. We leverage our partner ecosystem and have creative engagement structures to take a higher level of accountability in helping customers adopt large transformation programs with ease. This continues to be a sustained GTM effort in this ecosystem going forward as well.

As we all know, one of the most differentiating aspects of Mphasis' competence has been the tribes and squads agile org design that we adopted a couple of years ago. This has provided extreme scalability, technology depth and agility in bringing our high-touch high-tech client engagement model to life. We have continuously evaluated new areas to scale our investments by creating new tribes and transformed some of the existing ones.

This also enables us to bring sharper differentiation in our solutioning, while also positioning us well in deals requiring multiple competencies. For example, our next-gen IT ops tribe merges our application management and infrastructure management services tribes, to position us for larger integrated deals. Very often, given the nature of our deals, several of our tribes work in unison to bring multiple competencies together. As such, if you look at the Next-Gen App Dev tribe, it has been expanded to cover the platform-driven enterprise approach, with significant need from traditional enterprises wanting to pivot to a platform approach using the network orchestration business model as against building "applications or software".

In just the past few quarters since our launch, our tribes-led approach is having a significant impact on our deal pipelines, with over 75% increase in our overall deal pipeline compared to a year ago. Transforming existing tribes and creating new ones, like Experience, to capitalize on changing customer needs and driving large-deal motions has been a good success for us.

As you can see from the deal TCV wins growth, the bets we made in doubling down on areas such as DevOps, cloud, automation, modernization and data has paid rich dividends, as clients look for pivots to their enterprise IT buying behavior and look for partners who can not only execute to their needs, but partner with them and, in fact, lead them in new tech adoption and transformation. The architecture, design and engineering-led approach has truly stood out for our clients as a key differentiator.

Moving on to our key financial highlights for Q2:

- Our gross revenue for this quarter at $327.4 million is higher than our pre-pandemic peak.
- Our revenue grew 6% Q-o-Q and 6.7% Y-o-Y in constant currency terms. This represents the highest sequential organic growth in over a decade.
- Direct channel has powered growth in this quarter, growing 9.7% Q-o-Q and 25.2% Y-o-Y on a reported basis, and 10.9% Q-o-Q and 18.4% Y-o-Y in constant currency. Direct business is now over $1 billion in annualized revenue run rate as of Q2 '21.
- The strong showing in Direct has helped us manage the decline in DXC, the contribution of which is now reduced to 16.2% of revenue.
- DXC revenue declined 14.9% sequentially and 23.9% Y-o-Y on a reported basis, and 15.5% sequentially and 28.9% Y-o-Y in constant currency terms.
- EBIT improved 9.5% Q-o-Q and 13.1% Y-o-Y in Q2 to INR 3,924 million. EBIT margin improved 50 basis points Q-o-Q to 16.1%.

We believe that DXC continues to make great strides in the strategic road map and the New DXC approach. Mphasis is well aligned to the New DXC's strategic direction, and we are working closely with their operational and business leadership in driving synergy across the two companies. While DXC has publicly stated their goal to reduce third-party spend, Mphasis is and will continue to be in the mix, and we continue to work jointly on a plan that gives longer-term flexibility to DXC as well as longer-term business continuity and visibility to Mphasis through

this partnership, potentially even well beyond the September '21 time frame. We expect to update you all further as we go through the current phase, which was marked by COVID-related impacts for us.

We continue to see strong growth momentum and positive outlook in our key focus vertical of banking and capital markets. The segment reported yet another strong quarter with double-digit growth, with a 17.4% Q-o-Q and a 25.2% Y-o-Y growth in dollar terms. We believe this is the best-in-class growth in this industry segment and was broad-based across segments of BCM as well as Digital Risk. This demonstrates the consolidating strength of Mphasis as a preferred service provider in the banking and financial services industry.

Insurance grew 2.5% sequentially. We have built a robust pipeline in this domain over the past few quarters and expect to convert this into revenue in the coming quarters as well.

As you can see from the industry performance in the Direct business, Q2 growth is broad-based across all segments with a very strong performance in all barring one vertical of logistics and transportation. We saw some spend realignment due to base alignment from previous quarter and continue to be placed well with all our clients in that segment, strategic and new, and expect it to recover starting Q3.

As mentioned in our previous calls, Europe is a focus area for us, and we are pleased with the fact that our increased sales efforts and investments in this region are yielding good results. Direct in Europe has grown 23% Y-o-Y this quarter in constant currency terms. Our pipeline in Europe is very strong, especially with new clients, and we expect this region to continue to be a growth driver for FY '21 and beyond.

Our Direct TCV for this quarter is $360 million, an all-time high. This represents the third straight quarter of $200 million plus net new TCV, not including renewal deals. Our net new TCV has now exceeded $1 billion on a trailing 12-month basis and is up 74% over trailing 12 months. We believe that our rising TCV trend is a testament to our improving track record in scale and frequency of large deals.

Specifically, I would like to make two points about the TCV composition as we see it today:

a) There is an increasing component of large deals in this. These large deals are transformation-led and increasingly integrated in nature, requiring us to stitch multiple elements, such as applications, infra, DevOps and operations to deliver an integrated solution.
b) There is also a heavy new-gen services portion in our net new TCV with contribution of 73% in this quarter.

Because we report our TCV on a net new basis and exclude renewals, we see robust correlation of 0.85 between revenue and TCV for Direct. Thus, as we find success in increasing our TCV wins, we believe that this should commensurately translate into higher revenue as we saw in Q2.

Our pipeline is at a record high with 75% increase Y-o-Y, despite healthy deal conversions in the last two quarters. And it still comprises of multiple large deals that are in motion.

To give you a color on the quality of new deals, I would like to mention a few deals from this quarter:

- An American multinational company signed Mphasis as a development partner for cloud platform development and process improvements.
- One of America's premier financial services company was in their final phase of a multiyear core banking transformation. Mphasis was chosen as a strategic partner for the QA and surrounding digital interface development as they implement the core banking platform.
- Thirdly, an American bank holding company signed their maiden end-to-end mortgage transformation project with Mphasis post their merger with another financial services organization.

Coming to our client metrics, our track record in migrating clients from one revenue bucket to the next continues to be healthy. Specifically, 50% of our $10 million or above clients are now $20 million or above. 50% of our $20 million or above clients are $50 million and above. And 50% of our $50 million or above clients are $100 million and above, indicating a high conversion rate at each stage, as you can see from the chart here.

We are especially pleased with the strengthening position with several top clients post vendor consolidation. We continue to believe that our wallet share gains emanate from our competency driven positioning in these clients as well as in the overall market. In the past 12 months, we have added two clients in the greater than $75 million bucket.

Our investments in “tribes and squads model” are driving accelerated growth in the Direct business. Growth is broad-based across all units within Direct. New client revenue grew just under 30% in the quarter. We are enthused by our strong growth in Europe as well, as I mentioned before.

EBIT saw a healthy Y-o-Y growth of 13.1%, and EPS grew 8.7% Q-o-Q and 9.3% Y-o-Y in Q2 '21 to Rs. 16.04. Second quarter FY'21 EPS reflected reduced other income from lower investable cash due to dividend payout during the quarter and lower yields due to our preference for liquid, safe current investments during the pandemic. We will continue to prioritize safety and liquidity in deploying our surplus.

EPS growth profile is consistent with our margin philosophy. Our EBIT margin at 16.1%, are in line with our stated intent of maintaining EBIT in the 15.5% to 16.5% band, as we continue to invest for growth. The revenue growth performance of Direct, the improving trend of our TCV and our ability to manage stability and predictability of margin profile at lower volatility bear testament to the success of this philosophy.

To summarize, I would like to leave you with six points:

- One, our revenue growth in this quarter at 6% sequential constant currency rate is the highest sequential organic growth rate that we have seen in over a decade, with revenues being higher than our pre-pandemic peak.
- Two, our Direct business grew double-digit percentage sequentially. Our Direct growth will continue to be supported by robust TCV that we have added across verticals. Our TCV in this quarter at $360 million is an all-time high. On a trailing 12-month basis, TCV of over $1 billion is 74% higher than that recorded over the prior period.
- Third, our track record in winning large deals is consistently improving. The nature of our large deals is increasingly transformation-led, and our pipeline is up over 75% Y-o-Y, at an all-time high with multiple large deals in motion.
- Four, client mining metrics across revenue buckets is improving. In several of our top clients, we have gained share post consolidation. We have a very high conversion rate of 50% to move clients from one bucket to the next, as I talked about before.
- Five, we are working on building visibility in DXC beyond September '21.
- Finally, margins, we have operated in a fairly steady margin band and have articulated our intent to invest back in the business. Our margin stability ensures that revenue growth translates into sustainable EPS and PAT growth and consistently raises free cash flow generation.

On that note, I would like to have the operator open the lineup for questions, please.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the questions-and-answer session. The first question is from the line of Mukul Garg from Motilal Oswal. Please go ahead.

Mukul Garg: Nitin, the first question was on the impact you had in the DXC business this quarter. There was a very sharp fall and you attributed that to COVID impact. Can you help us break that into the color of impact on business which is committed by DXC to you versus what you guys are winning on top of that?

Nitin Rakesh: So Mukul, I think we talked about it over the last two quarters. When we called out the number in our FY '20 closing call, we said there was between 1st April 2020 to 30th September 2021, there was a $300 million roughly revenue that was still to be consumed. We provided a similar update in the last quarter. So the revenue consumption between now and the end of MRC is around $200 million right now. So that's kind of the backstop over the next four quarters. There'll

definitely be some variability on a quarterly basis, but that's the way we have constructed, at least our thinking, and we will continue to update you as things change.

Mukul Garg: Right. So I was not looking for numbers. I just wanted to get a sense of the relative impact which you might have seen from DXC with the portion of the business which comes under MRC and the portion which does not come under MRC. Was there a difference in the impact, which you saw between the two groups?

Nitin Rakesh: No, nothing else to call out in that segment. I gave you recent color over the last two quarters, and I also talked a little bit more about how we are shaping it. There is nothing more to add to that.

Mukul Garg: Okay. Fair enough. The other question was on the relative growth, which you saw this quarter between the BPO, IMS and Applications. A lot of this was driven by the BPO portion of the business. It would be good to have your thoughts on exactly how we should see this going forward, why there was such a massive disparity between the three categories?

Nitin Rakesh: There are two things to note there. Firstly, as you see, the shift happens between DXC and Direct, most of the decline is actually in apps and infra, of course, the Direct channel growth is broad-based. So that sudden shift that you are seeing is partly attributable to that. Secondly, I talked about the fact that a number of our large transformation-led deals are integrated deals, a number of them require ops and tech integration. And what you are seeing right now is the early phases of transformation where we have transitioned in many cases some of the work and in some cases we will continue to apply the transformation levers as we transform the user journeys and the customer experience. Thirdly, of course, the DR business is still tail winded, also that is adding to some of the uplift that you are seeing there. But there are still also a number of deals that are integrated between ops and tech, even within the DR book of business. So there is a significant portion of transformation-led deals in the mortgage industry that we are beginning to win, as I gave you an example in the prepared remarks.

Mukul Garg: Great. And if I may squeeze in one last question, more on the strategy of the company. If we look at the margin profile this quarter from Mphasis versus its peer group, we can see a big difference. While you guys have been broadly stable, they have taken the margins up materially. Is there a difference in strategy? You have been alluding to a stable margin band, do you think you guys are approaching the market differently and can see dividends in the longer term?

Nitin Rakesh: So, the approach is very straightforward. We are basically using the opportunity to double down on investing for growth. That's number one priority for us right now. And some of that is visible from the elevated levels of TCV wins that we have declared in the last two quarters. Third quarter of over $200 million, this quarter obviously was a big blowout quarter. Some of it is also driven by the large deals, which also is a very conscious choice to pursue some of them. Secondly, as we have converted these deals to revenue in the last four, five months, we have also had to take some of those costs in our P&L because there is a ramp-up cost, in some cases a transition cost

and in some cases, a recruitment-driven cost, given that the supply chains are still fairly constrained. And that's why you see utilization also has dropped for us compared to the last quarter, which is in a way kind of contra-cyclical. It's easy for us to increase utilization and increase our profitability in quarter, but that's detrimental to the longer-term ability to convert deals to revenue and find growth. And finally, we are making a significant investment in competency because that's our secret sauce. As I explained to you in the tribe section, we have actually expanded our tribes model to include new competency areas. And that's obviously going out of our P&L as well in terms of in-quarter operating investments.

Moderator: Thank you. The next question is from the line of Sudheer Guntupalli from ICICI Securities. Please go ahead.

Sudheer Guntupalli: Nitin, congrats to your team for a good quarter. First question is, strong and broad-based performance you talked about in BCM segment. Across banking and capital market sub-segments, if you can kindly help us understand what are the underlying demand drivers?

Nitin Rakesh: Okay. Again, this is not an aberration, but we have, I would say, quite sustainably shown growth in BCM in double-digits for almost six, maybe eight quarters. And what's driving that for us at least is our ability to lead clients in applying transformation, in adopting new technology, in changing customer journeys and customer experience. And in many cases, helping them think through what the future technology consumption road map should look like, given the need for agility, resilience and cost. So for us, it's a systematic approach. Of course, that number has been elevated dramatically this quarter. If you look at the Direct business, it's almost a 19% growth just sequential, very, very strong growth. And that is happening on two accounts. One, as the crisis hit, customers gravitated towards partners that they thought were more inclined towards helping them with digital adoption. Two, as I mentioned in my remarks, many of our large clients, again by virtue of the fact that banking is a big segment for us, many of our large clients have gone through consolidation exercises, and we are seeing share gains there as well. The good news for us is, as long as we continue to see share gains in our top clients and of course, we continue to win business outside of the top five as well, including new logos, we will stay in good shape from an overall growth perspective.

Obviously, this segment is also a segment that has been very active in insourcing commodity work. And I think by virtue of the fact that we have played on the cutting-edge of technology transformation work, that has also kind of helped us avoid some of that demand disruption that some of our peers saw from an insourcing trend perspective.

Sudheer Guntupalli: Sure. That's very helpful. And second part to the question. Over the last couple of quarters, large global banks seem to be engaging in a lot of systems reconfiguration work given the herculean task of distributing stimulus funds within a short span of time. Also, some of the large capital market firms seem to be spending to catch up on the Robinhood servicing aspect. So, any color on how much of these phenomena, which may be, let's say, one-time in nature would have helped our banking and capital markets' performance? And lastly, any sense on the kind of vendors we

are displacing here during the consolidation exercise? Are they tail vendors or some of the large, let's say, Mphasis size players as well? That's it from my side.

Nitin Rakesh: Sure. So the short answer to your first question is, typically, most of the work we are doing is not one-time in nature, it's longer-term sustainable revenue. Of course, there will be ruthless prioritization in spend and some areas of spend that are happening today will probably not happen a year from now. But in general, we have not really seen a massive lift from one-time stimulus-type businesses. Secondly, on your question about, what was your second question, sorry, I forgot?

Sudheer Guntupalli: Kind of vendors we are displacing.

Nitin Rakesh: Vendor consolidation. Yes. Again, keep in mind, right, the banking business is probably the most cutthroat competitive landscape, most mature buyers. And in terms of the type of vendors we are displacing, again, different story in different accounts, but the competitors is not just companies like us, but actually, in many cases, companies bigger than us, much bigger than us. And the issue isn't so much size driven for our clients today, the issue is more competency driven. And that's a big difference in this crisis versus the financial crisis of 2008 and 2009, where because it was a financial crisis, safety of a vendor and longevity of a vendor was more important. This time around, the competency, capability of a vendor is more important and, of course, you have to have a certain financial profile which we do. So we are really winning against almost every category of competitors, global multinationals, India-centric players, small niche providers, in-country players and on-site players as well.

Moderator: Thank you. The next question is from the line of Nitin Padmanabhan from Investec Capital. Please go ahead.

Nitin Padmanabhan: Congrats on a great quarter. I just had one question with regard to, how much of the revenues that have come through in this quarter is based on the accelerated accretion of revenue from the deals we signed in the prior quarter? Because I think earlier the sense was the pace of ramp could be slow. So has most of it already accreted or we think that a lot more will come going forward based on deals that are closed in the prior quarter?

Nitin Rakesh: So Nitin, obviously, Q1 was difficult from a conversion standpoint because it was early in the crisis. I think as things progressed through June, July, we started seeing some better ability to convert, ability to do remote transitions. I would say that the correlation that we have given you should actually help you do some of that math. That correlation has been updated as of Q2. But from the standpoint of, is all the upside taken? Obviously, answer is no, because we also had deals that we signed in Q2 that will play out. Typically, these are still deals that are three, four years in nature, in some cases; in some cases, of course, they are shorter-term projects because they are quicker transformation programs or short burst programs. So, it's a fairly, diverse set of deals in that pipeline. Of course, the large deals drive some of the ramps, but those large deals also sometimes take time to ramp up. So it's really, again, I don't have a clear answer for you, but

the correlation should give you a clear answer of whether all of it is taken in or will continue to ramp up. But at least, good news is that given the nature of the TCV wins, the nature of the conversion to revenue and, of course, the nature of our pipeline, we definitely have good visibility at least in the short to medium term.

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

Mohit Jain: Sir, one thing I missed in the initial remarks. So you mentioned in the first question that there was some shift from the DXC, is that correct, to the Direct business?

Nitin Rakesh: No, no. I said the mix change is driving, the question was around IT versus non-IT business. And as DXC business has declined, that was predominantly IT. There is no shift in terms of classification at all this quarter.

Mohit Jain: What you are saying is, to calculate IT services recurring growth, we should actually look in the context of decline in DXC accounts in this quarter?

Nitin Rakesh: Correct.

Mohit Jain: Okay. Second, sir, on the offshore, what is your view? Because for us, offshore percentage has not really gone up. What are your thoughts around offshoring and increase of it in your capital markets?

Nitin Rakesh: Yes. I will tell you, at least, I mean, the previous question was around conversion of deal to revenue. We have prioritized conversion from deal win to revenue because there is always a shelf life, and there is a risk. If you don't prioritize that conversion, we may end up risking the deal itself, even after we win it. So, what we have done at least in the short-term is, we prioritized conversion. As we get the ability to apply some transformation levers, migrations, offshore leverage will come into play there as well. But predominantly, at least in the short run, I don't really have a very strong ability to have the supply chain revert back to normal. So, we have no choice but to do in-market or remote in some cases. The good news though is that the leverage has improved marginally in terms of offshore percentage, but that's been fairly steady for us as we have driven transformation deals. And given the nature of our deals, despite the current environment, we do believe that proximity and customer centricity for the design and engineering teams is still very important. So we don't expect that to change dramatically going forward.

Mohit Jain: And third, for Manish, so given that you do not expect, you have also put it in the presentation, your margin band, which used to be in 15% to 16% range, I guess, continues to be the same. Is that correct?

Manish Dugar: 15.5% to 16.5% is the current range.

Nitin Rakesh: And we retain that.

Manish Dugar: Yes, we retain.

Moderator: Thank you. The next question is from the line of Dinesh Mehta from Emkay Global. Please go ahead.

Dinesh Mehta: Congrats on a very strong execution. I think a couple of questions. First about the Digital Risk, if you can say what was the revenue run rate, and how you expect that business to play out considering the interest rate scenario? And what risk mitigation things, because right now origination is significantly growing, but what risk mitigation policy you are putting in place when that type of business would not have any volatility?

Second question is about deal wins remained very strong and healthy. What difference at Mphasis? You partly alluded, but if you can provide more perspective. And what kind of competition typically we face in such large deals? And any change which you are witnessing in average tenure of deals?

Nitin Rakesh: So yes, I hope I remember all the four questions. But first question was around Digital Risk. It's getting extremely difficult for us to completely delineate a pure DR deal because over the last two years we have really truly integrated mortgage as a sub-vertical in our overall BCM business. So yes, while there is some tailwind in the DR business, even if I actually had to sit down and start allocating percentages to DR versus non-DR, I think it's getting harder and harder for us to do. Case in point is the mortgage transformation example I gave you from my earnings call script, where two banks have merged and they have appointed us to apply transformation to the mortgage business, end-to-end. So the answer to your question is actually in execution itself. Because we have taken an integrated approach, our ability to stitch large deals that go beyond just originations is already being witnessed, as we speak. And we expect that to be the primary diversification, risk mitigation strategy, and we will continue to execute that as best as we can.

Second question was around the differentiation. The primary differentiation, as I mentioned, and I explained in some great detail on how we have constructed our technology-led, the tribe and squad model. The bet we took two-three years ago was that given the shift of focus from the business side of enterprises, not the IT group but the business group, the focus that they have put on customer centricity and agility. Agility meaning, I want to be able to launch product quicker, I want to make changes to my product portfolio faster, I want to respond to my clients quicker versus the one to two-year cycle that most large enterprises had in product launches. That focus meant that their IT consumption shifted dramatically away from on-prem CAPEX driven five-year project type programs to consume-on-demand everything as a service. For us, for example, cloud is nothing but compute as-a-service. Instead of having the compute infrastructure in a data center, you plug into a cloud provider and you actually get compute-on-demand on tap as much as you want, at a price that is on a per unit workload basis lower than the price you can get in your own data center.

So those are the bets we made. And the corollary to the bet was, not only do we want to help clients apply this migration or ability to consume tech differently, we want to actually help them identify what's the best infrastructure and application environment that they need, how do they architect it, how do they design for it and how do they execute on it. So that's been, to me, the ability to not just wait for a client to give us an RFP or a requirement document, but actually work with them through design workshops and solution studios and help them figure out what is the best solution that can be applied to their environment is really what makes it very unique. And that's the reason why our proactive deal percentage is very high. We gave out some statistics last year, where 80%+ percent of our deal new TCV wins were proactively driven, which means we were not waiting for the client to define the problem, but we are actually helping them in identifying where the interventions are needed and what kind of interventions are needed. When you have that level of proximity, and I called it high-touch, high-tech, that's truly the differentiation that our clients are starting to see.

From a competitive standpoint, again, as I mentioned, right, this market is very, very mature, crowded and competitive. But given that we have managed to find ways to be very proactive and continued to make sure that we avoid all of this intensity that comes in after an RFP is put out, that's been a really helpful area for us. We do compete with almost every player that you can think of on the planet when it comes to servicing large enterprises. And whether it's a global multinational, India-centric players, Europe-centric players, in-country, local niche players, pure-play cloud or data players, all of the whole landscape is our competitive landscape. Hopefully, that answers all your questions.

Dinesh Mehta: One question about any change in average tenure of the deal, which you are witnessing?

Nitin Rakesh: Yes. So typically, the size of the deal sometimes increases and the tenure increases. We have deals in the mix and in the pipeline that are in some cases, slightly longer term. But so far, between Q1 and Q2, I don't think there is a dramatic shift. Typically, three, four years is probably the outer limit. But clearly, we have deals in the pipeline that are much, much longer term as well. And we will continue to kind of give you some more color on those as we go forward.

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

Sandeep Shah: Nitin, just on your comment regarding working on building a visibility plan within DXC beyond September 2021, so what does that exactly mean? Are you really worried that post September 2021 there could be a material decline? What is our strategy, focus regarding this?

Nitin Rakesh: Sandeep, I am not worried, but I think all of you are worried. So that's why I am talking about giving you guys some visibility and building that visibility and giving you some more color as we progress through the next couple of quarters. So, from my standpoint, just like we have every other client relationship, this is a client relationship. And I have said this many times before, there is no other client that gives you any guarantee. Every day, we have to fight, compete and

win business, and this is no different. So our intention is to continue to make sure that we have longevity and sustainability of our relationship for the long term.

Sandeep Shah: Okay. And any perspective in terms of Blackstone channel revenues, how it has performed in the 1H with the pandemic? And how do you see that channel revenues performing in the 2H as a whole?

Nitin Rakesh: Again, we decided not to keep calling it out separately because, again, as you know, every cycle, every deal win, every channel has its own lumpiness, variability, but it's obviously sitting well within our Direct business. It definitely contributes to our new client business. So, from that perspective, We are very pleased with the performance, and we continue to be very favorably inclined towards making sure that we continue to invest in that channel as well.

Sandeep Shah: Okay. And just last question. Any view on wage hikes as the whole industry is announcing the same?

Nitin Rakesh: Yes. When we have something material to announce, we will. So far, we have not made any comment publicly.

Moderator: Thank you. The next question is from the line of Manik Taneja from JM Financial. Please go ahead.

Manik Taneja: So, I just wanted to check with regards to the comment that you made around the pipeline in Europe. So Nitin, basically, we have seen some subdued performance in terms of business from Europe in the first half of this year. Should we read that in conjunction with the pressure that we are seeing on the DXC business?

Nitin Rakesh: Yes. I broke out that number for you. If you go back to my prepared remarks, and there is a slide on our Direct business, where I call out Europe growth ex-DXC. The direct business in Europe has actually grown very strong, and so has the TCV conversion.

Manik Taneja: Okay. Thank you. The second clarification was around the BPO business. So given the strong sequential growth that you have seen, if you could just give us some qualitative sense of how much of that would be supported by the cyclical rebound in the mortgage business side or the DR business?

Nitin Rakesh: Yes, in general, the assumption that all BPO business comes from DR is not a good assumption because we have a very strong non-DR BPO business as well, and we have strong leadership that we put in place in that business also over the last couple of years. And that business is an important one because if you see a number of large deals that are announced by the industry, including our peer group, including some of the recent very large deals announced by some of our competitors, they do end up having a significant operations transformation component because that's how the user journeys get transformed. So the right way to think about it is that not every dollar increase in BPO revenue is attributable to DR.

In terms of the split per se, I won't be able to give you the exact breakup because that's not how we actually manage it on the business. So the way we manage it on the business really is on a client-centric basis. So each client unit has a P&L for us. And that client unit continues to focus on driving wallet share gains across multiple service lines. And of course, bundle them all together is one of the best ways to do it because that way we can get more sticky, longer-term revenue with transformation deals. So that's the right way to think about the bifurcation that we have talked about.

Manik Taneja: Okay. Just one quick clarification. So DR was about 50% plus of your overall BPO business as of last quarter. Would that understanding be correct?

Nitin Rakesh: Honestly, as I said, right, it's getting harder and harder for us to even delineate pure DR revenue. So don't think I have a ready answer for you. Because that's not the way we, as I said, run the business per se.

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

Abhishek Shindadkar: Congrats on strong execution. Nitin, just a question related to what was asked by an earlier participant. First, thank you for sharing the cloud pipeline. So one, if you can just compare it or just give us a perspective about how it has moved, that could be helpful. And the second part to it is, in the past, one of the larger peers had said that a dollar spend on cloud creates a 3.25 on the ecosystem spend. In your perspective is this a concurrent spend or it is one after the another would be helpful?

Nitin Rakesh: Yes. So the right way to think about the expansion in the pipeline is the best proxy for that is to look at the overall pipeline expansion. But I have actually talked about the fact that we have seen a 3x increase in our cloud pipeline in the last one year. And that's highlighted in the slide where I talk about the cloud business per se. So a 300% jump in the cloud pipeline is attributable primarily to the massively increased adoption and consumption that we are seeing, especially we do a fair bit of work with both AWS and Azure, and that's what is driving that growth in both pipeline and in the actual TCV won for us.

In terms of other question about the pull-through revenue, again, it depends on how you count it. The ecosystem impact is it comes primarily from, again, definition of what goes into the cloud revenue, what does not go into the cloud revenue, do you put Snowflake and Salesforce into the cloud revenue or you put in the data revenue. So there is a lot of commonality. That's why we don't call cloud out as a separate tribe because multiple underlying capabilities from platform to modernization to data go into forming what we call the cloud guild. So from that perspective, I can definitely see a 3x to 3.5x type pull-through revenue. I think that's probably in the ballpark, even though I haven't really looked at the exact numbers because, as I said, it all depends on how you run the business and how you manage the pipeline.

Abhishek Shindadkar: Just a clarification, I read the 3x jump on a year-on-year basis. What I was more looking from a perspective about how things have evolved from January, March quarter I mean during COVID and post-COVID, if you can just give a perspective, that would be helpful.

Nitin Rakesh: Yes, I will give you a qualitative perspective. The bulk of this jump, at least in our business, we have seen, I would say, in the last seven months or so. So, whether it is directly linked to COVID or it is linked to our efforts in the channel or it is linked to clients actually getting more mature, I think it's all of the above.

Moderator: Thank you. The next question is from the line of Vibhor Singhal from Phillip Capital. Please go ahead.

Vibhor Singhal: Congrats on a great set of numbers. So, my question was more on the BPO business. Given that almost the entire incremental growth in this quarter came from the BPO business, there appears to be too, I mean a higher cost for it in the sense that our on-site headcount seems to have doubled Q-on-Q in the BPO segment as we report.

So would that be the reason that in this quarter, despite such strong growth, we could not see a commensurate kind of a margin expansion because probably this high on-site cost is the growth that could have led to some margins? And the related question is that how do you then see this BPO business, which entails basically such high proportion of on-site employees in terms of margins vis-a-vis the company average.

Nitin Rakesh: Yes. I addressed the first question earlier, which is look at the Direct growth, you will actually be able to see the IT growth as well as BPO growth. What you are seeing is the decline that happened in the DXC channel is actually eating into the IT growth in the Direct channel on a net basis. So the right way to look at it is to look at just Direct versus just overall. Secondly, As I mentioned earlier, a large part of the growth is, given the transformative nature of the deals that require both ops and tech transformation, some of it is definitely driven by the continued growth in the DR-type business, in mortgage related businesses, including the mortgage transformation deals that we talked about. And I think if you look at the cost element, if you look at our gross margins, they actually did go up 160 basis points Q-o-Q. So I don't think there is a straight-line correlation that like you have drawn between BPO on-site and margin. The two major things that really we have used this quarter: one is lower utilization, which basically means that we have decided to invest a little bit more in making sure that we have the ability to ramp up our deals. Some of it is also the migration between skill types as we have ramped down one part of the business and the other part of the business has gone up. You can never perfectly time these things one to one. Secondly, we have very consciously made additional investments, especially in competency, capability and go-to-market. And we guided you to a stable margin band, and we stayed to that only because that's consciously a choice we took to prioritize growth over putting everything back from operating leverage into the P&L.

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

Ashwin Mehta: Congrats on good set of numbers. Most of my other questions have been answered. Just one question, Nitin, in terms of availability of staffing specifically on clients' side for ramping up these large deals exactly seeing there and given the immigration-related challenges, how is the situation there? And could there be some element of overinvestment right now in terms of costs, given that we want to get the transitions done properly?

Nitin Rakesh: Yes, great question. So I referenced that in one of the earlier questions around the fact that we are prioritizing deal conversion to revenue over anything else right now, given just the fact that supply chain is not fully where it needs to be because travel is still very restricted. So that definitely puts a little bit of pressure on local hiring, local staff up and local ramp-ups. But we have also found, and as I mentioned, we have managed the operation in a way that, that really hasn't impacted our gross margin, in fact, it has gone up sequentially as well and also fairly stable on a longer-term basis also. So that's definitely a factor, but we have managed the operation in a way that we work around it. But you picked up on the right item, we have definitely prioritized our ramp-ups over cost because that's where the real opportunity to gain wallet share and growth.

Ashwin Mehta: Okay. That's fair enough. And just one follow-up. So in our BPO business, what proportion of our business or the non-mortgage side of business, what is the kind of work that we are doing, which you are indicating with our insurance...

Nitin Rakesh: Yes. A fair bit of work we are doing, we have presence in almost all key segments, banking, non-mortgage banking also, we do a fair bit of work in wealth management. We do a fair bit of work in payments. We have a pretty significant insurance operation where we run for some large global insurers, large parts of their middle and back office activities. We also have undertaken some significant customer engagement and transformation deals that cuts across ops and tech as well. So it's fairly widespread. Back in the day, it used to be a very large portion of our revenue. Over the years, it obviously got deprioritized in favor of tech. But as we saw opportunity in servicing our clients jointly, we have actually been able to build that back up again, and it's become a fairly strong growth driver. It also gives us a little bit more leverage because operating leverage is a little bit higher in BPO. So as that stabilizes and as we apply the transformation levers, that's definitely a business mix item that will help us from a longer-term perspective as well.

Ashwin Mehta: So essentially, do you think the on-site bump-up in terms of headcount can over a period of time move towards offshore improve BPO profitability?

Nitin Rakesh: Yes. Also keep in mind that as we keep converting the newer deals, there will be a steady flow of the same motion, right? You convert the deals, if you need people, you staff them up locally and then you apply the migration and transformation levers. So, depending on how this deal win cycle moves over the next two quarters, you may see some variability, but the longer-term opportunity to continue to apply transformation and offshore leverage definitely exists.

Moderator: Thank you. The next question is from the line of Nitin Padmanabhan from Investec Capital. Please go ahead.

Nitin Padmanabhan: Some peers have been suggesting potentially exaggerated furloughs in BFS in Q3. Are you seeing any such thing within your portfolio?

Nitin Rakesh: So good question, Nitin. This is definitely going to be a seasonally challenging quarter. I think what traditionally used to be primarily banking, I think we might see some of that play out in some other segments as well. The question really is how best we can manage it. And we are still working with our transition teams to assess the impact per se. But definitely, there will be an element of seasonality that will come into Q3.

Nitin Padmanabhan: Sure. Any way to characterize, is it higher than what we have seen in the past or how would you characterize it?

Nitin Rakesh: Some of it is given that a number of our clients have kind of gone through a significant spend reprioritization, some of it might seem a little bit higher than last year because there's a double whammy impact here. But, as I said, it also depends on the type of work you do and the discretionary versus necessary nature of the work that you do. So my expectation is there will be impact in some verticals, including banking. There may even be an impact in some other businesses that traditionally were not there, and that's what we are working towards. So this definitely is an issue for the current quarter.

Moderator: Thank you. The next question is from the line of Hiten Jain from Invesco AMC. Please go ahead.

Hiten Jain: I have one question. So the G&A expense has grown higher than the top line, both sequentially and on a year-on-year basis. So one would have thought that given that offices are not 100% operational, there would have been cost savings on G&A, and even the discretionary travel is also limited. So, what explains that?

Nitin Rakesh: Okay. Manish, can you take that question? Yes.

Manish Dugar: Yes. Hiten, Manish here. First of all, if you look at it as a percentage of revenue, G&A is at the same level where it was pre-pandemic. We had some investments that we have made and seats that we kind of create, which are not yet allocated for operations, continue to be accounted under G&A. And from an overall cost perspective, there were some savings or there were heightened levels of savings that we got in quarter one because of pandemic, some of which are getting reduced. So, what you see is not an increase in G&A. It is actually getting back to normal or investing to kind of make sure that we are able to execute and scale the deals that we have won. As you would have seen, the TCV pipeline and wins that we had in the last three quarters has been all-time high. And this quarter is where we started seeing some of the execution, some of it is yet to come.

Nitin Rakesh: And there's also an element of bench costs that is sitting in G&A. That is the corporate bench that we don't allocate to direct cost. So that also is contributing with reduction in utilization this quarter.

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

Rahul Jain: Congratulation on a great execution. I just have one question, which is like, since we have a relatively lower margin aspiration, and we are winning deal against some of the larger names in the BFS space, does that have some impact in the way the pricing in this space could change with peers? Like you are winning important deals, will that disturb the situation on the pricin g side to some degree?

Manish Dugar: So, Nitin, I can take that, maybe you can add to it.

Nitin Rakesh: Yes, go ahead.

Manish Dugar: So, first of all, like we had mentioned earlier, most of the deals that we win are proactive and they are not necessarily won on the basis of price. And in many cases, we are not actually the cheapest service provider. Having said that, given the investments that we are making, our stated philosophy is to stay in a band of 15.5% to 16.5%. It's not that our aspirations on margins are lower. And philosophically, we would prefer to kind of invest as much as we can so that we can continue to deliver leading growth rates, which is reflected in our TCV wins, and in fact, if you look at the pipeline growth and the kind of revenue that we have delivered. So, the idea is eventually, EPS is a function of EBIT and revenue. And if we can get revenue growth as big as we can while sustaining the profitability, I think we could probably deliver the best EPS growth that the industry can see. Sorry, Nitin, you would like to add something?

Nitin Rakesh: It's more competency-driven, value-driven pricing. It's not really for us, it's not a price discounting game that is underway, and we will probably never go there because that destroys your own brand and your own perception with clients. And the fact that we are winning consolidation battle in many of our top clients is testimony to more capability and competence than just price because our ability to cut price will never match the ability to cut price from somebody else. And that's just the nature of the business. Secondly, the margins you are seeing is the composite margin. There are obviously underlying businesses that have different margin profiles. We talked about the fact last time that our highest margin business actually was growing well. So that does give us a little bit more operating leverage. But, consciously, we have taken the choice to continue to focus on growth. And that's why if you look at the Direct business, it's grown at almost 11% sequentially and 18-plus percent on a Y-o-Y basis, which is industry leading. So, it is a very conscious philosophy. It is not from a pricing or a discounting standpoint, it's more from price to value but gain wallet share because this is a great opportunity for us to use our competency-driven approach.

Rahul Jain: Right. If I could ask one more. With the kind of TCV traction that we have seen, which also matches with the in general accelerated thought process that we have in the market, does that change your internal growth expectations from what we did in the last, let's say, couple of years versus what you would aspire to deliver in a couple of years?

Nitin Rakesh: Yes, acceleration in growth is definitely the focus. As we saw, there is an internal realignment going on between Direct and other channels. As we see continued opportunity, we will continue to take that opportunity. From the crisis, we have recovered quite smartly with our revenue crossing the pre-crisis peak quite smartly this quarter. So, the thinking is well aligned towards accelerating the growth.

Moderator: Well, ladies and gentlemen, that is the last question for today. I would now like to hand the conference over to Mr. Nitin Rakesh for closing comments. Over to you, sir.

Nitin Rakesh: Thank you, operator. So, to wrap up, even though there's been recent macroeconomic data that has been more constructive than we would have expected earlier this year, there remains a significant amount of uncertainty as well. So, we continue to prepare for a broad range of outcomes while focusing on servicing our customers, clients and communities through this time. I think our strong performance in both pipeline, revenue and TCV continues to give us strong reason to believe that we are making the right investments in the business. Wishing you all happy and safe festive days ahead and stay safe. Thank you.

Moderator: Thank you. On behalf of Mphasis Limited, that concludes this conference. Thank you all for joining. You may now disconnect your lines.