

## MPHASIS LIMITED

### Q2 FY09 EARNINGS CALL

17 OCTOBER 2008

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Moderator: Good morning ladies and gentlemen. Welcome to the Mphasis Q2 2009 Earnings Call. We have with us today Mr. Jeya Kumar, CEO, Mphasis and Mr. Sushanto Banerjee, Interim CFO, Mphasis on the call. I would like to hand over to Mr. Jeya Kumar. Thank you and over to you sir.

Jeya Kumar: Good morning. Thank you and welcome to the call. Really appreciate everybody taking the time to join us on this call today. In all, this has been a very solid quarter. The Mphasis Group consolidated revenues at 836 crores for the current quarter ended 30<sup>th</sup> September. That is about 39.3% increase year-on-year over the same quarter. Operating profits for the quarter ending September 30<sup>th</sup> was at 132 crores versus 74 crores in the same quarter year ago. That is a growth of nearly 79% year on year. During the same period, net profit increased by 113%. In keeping with the spectacular growth results, Mphasis reported the highest ever EPS in the company's history. To reiterate, this is the second straight quarter where we are setting our EPS records. Sequential quarter growth grew at about 12.6% to revenues of 742 crores. Operating profit for the quarter increased by 58.5 to 132

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crores. Net profit for the quarter increased by 141 crores. This is a growth of 79%.

For the half year ended September 30<sup>th</sup>, the group recorded revenues at 1,578 crores, a growth of 39% over the same period last year. Net profit for half year grew by 87.1%.

If you look at our lines of business, our core Apps business continues to grow from strength to strength with a solid growth across all industries. We grew at 14.2% quarter on quarter. Mphasis Apps still holds the primary role in our business at about 64% of total revenues.

ITO, I think for the last few quarters we have been mentioning it, ITO is our growth area and we are continuing to see very strong growth. We grew at 17% quarter on quarter. ITO now represents 15% of our total revenue. We are focusing on increasing our services in these areas. We are specially encouraged by the growth of the domestic Indian market, and we hope to see increased traction here.

BPO continues to grow at about 5.5% quarter on quarter and is about 21% of our total revenues. We have about 49% of our total BPO revenues coming from non-voice work.

We also saw a good growth in our core verticals and despite the current global situation, BFSI grew by about 3% quarter on quarter. Prime verticals like telecom, manufacturing, retail logistics, and healthcare continues to be flat with moderate growth holding our bottom lines.

In terms of geography, we continue to see growth in the US markets. We grew US by 2% quarter on quarter. The revenues from the US markets stood at 68% while markets in Europe, Asia Pacific, and Middle East continued to show good traction.

During the quarter, the group added 20 new clients including 15 through EDS relationships. This included clients in manufacturing and retail, banking and financial services. The group's client relationships have not only grown in size but has also become much more broad based now. We have now 98 clients with annualized revenue of greater than a million dollars and there is also growth in our top client rate. We now have 9 clients exceeding 20 million dollars.

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In terms of headcount, we are continuing with our headcount hiring plans. Year on year, we have hired close to about 4,800 employees. We have made huge strides in our utilization, which we are offsetting against our original hiring plans. For the year, we will still stay on course to go to about 7,000 to 8,000 people year on year.

Our Apps utilization, I think it is the best we have seen for a long time. Our Apps utilization for the month of September, we closed at 80%.

We would also like to inform you about the change in our accounting period. MphasiS Board has approved a change in our financial year from April to March to that of November to October effective November 1<sup>st</sup> 2008. This would mean that MphasiS would close the year at the end of October 2008 for a month quarter and seven months year.

To reiterate, we are very satisfied with the successful results. We believe that we are taking several initiatives to integrate our business and are bullish about the future. With that, let's open up for Q&A.

Moderator: Thank you very much sir. We will now begin the Q&A interactive session. First in line, we have Mr. Srivatsan from Spark Capital. Please go ahead.

Srivatsan: Now with EDS being acquired by HP, where will the Delta business go - to HP India or MphasiS? Is there some sort of demarcation internally about which business MphasiS will chase and which business HP India will chase?

MphasiS: It is an ongoing discussion, but we don't see it as a strategic significance to change the cause of our growth. We have close to about 28,000 employees and our business is growing. We will continue to support our current clients and grow our core verticals. On the whole, we see a lot more positives for the whole group.

Srivatsan: The hedging amount has gone up significantly from the last quarter to this quarter. Could you just elucidate what the hedging policy is and what are the positions as of now and the average rates that you have booked it at.



Mphasis: Traditionally we used to hedge for the underlying transactions in the balance sheet. So, approximately it used to be about two months of revenues that we used to take forward contracts for.

This quarter i.e. July to September, we embarked on a hedging program for future revenues, but we were very conservative because the market continues to be favorable to us. The Rupee continued to depreciate. Currently the hedging position is about 150 million dollars. We will have a close watch on the market and tune our strategy accordingly.

Srivatsan: What was the exchange rate for this quarter?

Mphasis: For this particular quarter it was approximately, Rs. 44/-

Srivatsan: There is a forex gain of 14 crores in the P&L, is this mainly because of the restatement of debtors?

Mphasis: Yes, it is because of restatement.

Moderator: Thank you very much sir. Next in line, we have Mr. Hitesh Shah from Kotak Securities.

Hitesh: If you could please break up the revenue growth into volumes and pricing. The prices seemed to have almost remained the same, but please could you elaborate on the volume growth and currency impact.

Mphasis: Approximately the volume and price will be 7% and out of that close to about 1.5% will be price, rest of that is volume. If you see the blended rates that we have reported in our MD&A, the offshore rates are holding but onsite rates have gone up. The offshore rates also have moved decimal places which has contributed to about 1.5% quarter on quarter.

Hiten: On a qualitative basis, can we expect similar kind of growth rates going ahead, maybe like was there any blip in this quarter or may be these are kind of sustainable rates subject to seasonality next quarter.

Mphasis: Essentially we don't give forward guidance, so we will not be able to state exactly what kind of growth we are looking forward to. The market is also very uncertain. As we have been saying in the past, there are pricing pressures, but it all depends on how well we can solution our services. The situation is very dynamic as of now, and it is difficult to predict what the future holds. The plan is ensure we continue our growth story.

Moderator: Next we have Mr. Manik from Emkay Shares. Please go ahead.

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Manik: Just wanted to seek a clarification on the hiring outlook. You mentioned that your gross hiring for the year will be at something like 7,000 to 8,000. If I just look at your numbers, your first half net hiring is around 1,800 odd people. If I could just have the gross hiring during the first half of the year.

MphasiS: In the first half of the financial year, the gross hiring would be about 3,500 people.

Manik: You are talking about hiring 7,000 to 8,000 people, are you giving this as an indication for the next year as well?

MphasiS: We always keep on talking about the hires and the numbers around the hires, but essentially it hinges upon how well we can operationally balance our levers. For example, in this particular quarter, there was a tremendous drive to improve the utilization. So, wherever we saw there is a potential to improve the utilization, we pulled the brakes and we improved the utilization and grew the business. To the extent, possible, we will continue with that initiative, and as a result of this, the net hire number or the gross hire number will get tuned. Going ahead, our hiring numbers will depend on what operational levers we have. So, it would not be fair to forecast a hiring number straight away.

Manik: Sir, if I look at your employee breakup on IT services side, the number of employees onsite has gone up significantly. I wanted to understand your view on this.

MphasiS: The reason that you are seeing the uptake in onsite is because there is a lot more transition work that is going on before the work actually gets offshored. We see that as a very positive thing for us in terms of our forward growth opportunity.

Moderator: Next in line, we have Mr. Pratish from DSP Merrill Lynch. Please go ahead.

Pratish Krishnan: On the EDS revenue, what would be the share of EDS revenues during this quarter as compared to last quarter?

MphasiS: The EDS revenue share was 40% this quarter and last quarter it was 41%. It typically dances in that range. This is not a negative growth, but growth in the other channels were far more than compared to the EDS channel.

Pratish Krishnan: On the financial services side, clearly you have a huge exposure there, roughly around 40-41% revenues, I mean can you offer,

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some commentary of what you are seeing in terms of this phase.

Mphasis: If you have noticed quarter on quarter our financial services grew 3%. We are not seeing any trend differently from what we have been talking about for the last three quarters. The decision cycles are taking longer. No change from what it was two quarters ago or three quarters ago, but the projects are also not getting cancelled which is positive. Therefore, you are seeing a lot more growth in onsite income.

Over the last few weeks you wake up every morning to know how the world has changed, but that is creating a lot more opportunity..

Pratish Krishnan: Is there further more scope in terms of, improving the utilization numbers.

Mphasis: It all depends on what kind of project, it all depends on the business that we enter into with the customers. So, as and when the business changes, the utilization matrix also will change.

Our Apps business closed September, at about 80%, that we believe is the highest in the industry and that is what you see translating to our bottom line. We are trying to hold that and are looking at that as possibly plus/minus 1% therein range. It can get impacted when we have fresher intake coming in the first quarter of next year.

Pratish Krishnan: In terms of the margins, is it possible to split in terms of how much came from rupee, utilization or any other levers that you had?

Mphasis: Approximately about 2% to 2.5% is on account of the rupee and the rest is on account of utilization and price.

Moderator: Next in line, we have Mr. Jigar Walia from Parag Parikh Finance. Please go ahead.

Jigar Walia: Can you please give us some outlook on the salary front which happened in the current year and the rationalization. Anything expected for the new hires, going ahead.

Mphasis: It all depends on how the market behaves, and how the inflation rates move. Maybe next year we will be looking at 13% increases in line with the inflation that we are getting to see.

Jigar Walia: There has been an increase in your fixed price contracts from 3% to 6%, is it a quarterly aberration or is there a trend which can possibly be going ahead?

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Mphasis: It is more of a trend because we will be seeing some of the big contracts which are being entered into fixed price.

Jigar Walia: Between your three segments, application, ITO, and BPO, if you can rank actually which of these segments will grow at a faster pace.

Mphasis: It will be ITO which should be growing at a faster pace because the base is smaller and also this is a new business and we have got a tremendous potential within the EDS family to grow this business. Year on year ITO grew about 80%, Apps at about 34%, and BPO around 31%.

Moderator: Next in line, we have Mr. Ashwin Mehta from Mangal Keshav Securities. Please go ahead.

Ashwin Mehta: In terms of our other expenses, expenses other than staff, they have contributed almost 230 BPs to our margins with travel being a big contributor. Do you see that to be sustainable and in terms of our facilities, consolidation, where are we currently?

Mphasis: In terms of travel costs, there is an initiative to control the travel expenses both in terms of cost and volumes of travel.

On the account of the consolidation of the facilities, we are still working on that particular plan, but we may not consolidate all the facilities in Bangalore as we may have indicated earlier. We are exploring more options and will then take a decision. The strategy of real estate consolidation, has not changed. We are in the consolidation phase, but we are also seeing real estate rates dropping which gives us a better opportunity now to renegotiate and stay in some of the locations which we earlier thought of.

Ashwin Mehta: On our BPO, do we see further scope in terms of the shared services work moving to us or given the consolidation between HP and EDS or that is something that could possibly get cannibalized.

Mphasis : Right now, we don't see any shift. We are aware that HP has a shared services portfolio. We continue to work on EDS shared services. It is too early in our relationship to actually talk about this.

Moderator: Next in line, we have Mr. Ruchit Mehta from HSBC. Please go ahead.

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Ruchit Mehta: How are you seeing business growth coming from the EDS channel. Do you see that accelerating over a period of time, or do you think the other channels will grow faster.

Mphasis: Both our core channel and our EDS channels are growing. We envisage that there will be better, bigger opportunities coming through the EDS HP.

Ruchit Mehta: In terms of the BFSI space also, if you could just comment, how are you see deal flows especially in the last one odd month. Are you still seeing deals in the market or things have just completely collapsed and existing deals on the table have also been withdrawn?

Mphasis: Current trends will hold for a while, we don't see any new cancellations. We are seeing customers taking longer to make up a procurement decision. The size of deals, given the industry consolidation, are going to be much bigger than I think anybody had planned or imagined.

Ruchit Mehta: Do you see there is a greater opportunity for yourself, especially considering now that EDS has been acquired by HP? Also HP has a large center in India, any idea as to what is going to happen - would the entities merge or would they continue to operate separately?

Mphasis: For now Mphasis and HP in India are two separate legal entities. Mphasis is very independent, with our own operation although we have a great go to market plan with HP and EDS. So, for us, this is business as usual, no change. Also as stated earlier, as of now, HP is not legally required to make any kind of open offer to Mphasis.

Ruchit Mehta: What would be your CAPEX plan for the year as a whole, any changes to that and how much have you spent in the first half?

Mphasis: Our capex plan for this financial year is roughly about 50 million dollars.

Moderator: Next in line, we have Mr. Atul from Tata. Please go ahead.

Atul: Can you share the order book in hand which can be executable in say next 12 months and the value of those orders in hand?

Mphasis: We do not give forward projections neither do we discuss our order book.

Moderator: Next in line, we have Mr. Hitesh Shah from Kotak Securities. Please go ahead.

Hitesh Shah: This balance of 3,000 to 3,500 gross headcount additions which we are looking at, are these going to be largely laterals or have

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we having campus recruitment also coming in during the next couple of quarters?

Mphasis: Both, it is a combination, We are looking at about 500 freshers this quarter.

Moderator: Next in line, we have Mr. Sandeep Shah from ICICI Securities. Please go ahead.

Sandeep Shah: In the second week of September, HP and EDS announced the merger completion, so is there any thought in terms of what is their offshore plan for the India arm?

Mphasis: We are continuing to have the discussion. I think we are hoping to get closure over the next couple of weeks or so. You would have seen that they also made announcement of huge headcount reduction. Mphasis in India is the largest offshore delivery center for EDS.

Sandeep Shah: Is it fair to assume that because the slowdown is impacting most of the Indian vendors? Is it so that because of our parentage and our potential in terms of business from the parent, our growth rates are likely to be higher than the peers going forward?

Mphasis: This quarter the EDS revenue is about 40%, last quarter was 41, I think two quarters ago was 43. So, it has gone from 43 to 41 to 40. It is not because the volumes have gone down but because we are growing a lot more aggressively in our market phasing channel.

The EDS-HP relationship gives us is access to a broader market that we can grow in. We can solution and win deals on our own steam in those accounts and that is what is driving our value.

Sandeep Shah: Assuming that the rupee remains at the quarter two levels, do you believe, that the EBITDA margins are sustainable in the coming quarters?

Mphasis: We don't give any forward guidance.

Sandeep Shah: With the fallout of the leading insurance company in US, any impact on EDS/Mphasis?

Mphasis: We are not seeing any impact currently. I think we all need to be conscious about is the longer decision cycles and if you look at the following quarter we may have a seasonal impact. With Thanksgiving and yearend holidays one may not get any major decisions coming out.

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Moderator: Next in line, we have Mr. Nimesh Mistry from MS Global. Please go ahead.

Nimesh Mistry: Your Apps business has grown about 14% this quarter and last quarter the growth was relatively lower. Apart from utilization what is actually leading to this kind of growth? Are you seeing this more from EDS side or is it due to joint efforts on your part?

Mphasis: I think it is a combination of all. The Apps business is growing both through core channels as well as EDS. We see a growth momentum as our teams are aggressively driving existing projects, pushing up utilization as well as seeking new business.

Nimesh Mistry: Could you throw some more light what kind of solutions you work on and what verticals?

Mphasis: Our main vertical remains BFSI. We are strongly placed across verticals like manufacturing, logistics, healthcare, and pharma.

Nimesh Mistry: On the HP EDS side, HP has given an offer to EDS at 25 dollars per share, so considering that, it seems to be an acquisition. But technically why can't see an open offer here?

Mphasis: I can't really comment on that. The HP EDS deal is a merger. EDS has written it to us that the arrangement is that of a merger versus an acquisition. We have already submitted that to SEBI, and I think SEBI is fine with that.

Nimesh Mistry: Because in a merger, there has to be some kind of a equity swap or something like that, but there is nothing here. so I am trying to understand why is it technically termed as a merger and not an acquisition.

Mphasis: You may want to go into the HP analyst site or the EDS analyst site and read what are the actual details of that merger.

Moderator: Next in line, we have Mr. Vikas from Motilal Oswal. Please go ahead.

Vikas: I need some clarification on the forex gain, if you can please explain that again, I mean you have about 150 million dollars of hedges and you ended up with a gain, can you please clarify?

Mphasis: It is essentially the restatement gains. We restated our assets and liabilities as on the balance sheet date. There have been gains because of the rupee depreciated against the dollar.

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Moderator: Next, we have a question from Mr. Srivatsan of Spark Capital. Please go ahead.

Srivatsan: Just seeing that tax rates have fallen significantly to 5%, was there any tax write-back during this quarter?

Mphasis: If you look at the last quarter and this quarter, it is pretty consistent. Recognition of def tax assets also influences net tax provision

Srivatsan: In terms of the investment side, how are you placed in terms of the revenue breakup, if possible, potentially between STPI and SEZs we have?

Mphasis: Right now, in terms of revenue, it will be about maybe 80:20 mix

Srivatsan: And the Delta growth is happening in SEZ, is it a safe assumption to make?

Mphasis: Yes, that is what our intention is.

Moderator: Next in line, we have Mr. Krudant from Valley Quest. Please go ahead.

Krudant: Any reason for change in the accounting period?

Mphasis: HP's accounting period is November to October. Though there is no statutory requirement for us to change it from April to March to November to October, but it is better we realign to that same account year for internal purposes. It eliminates confusion, and will align all systems towards one set of time period

Moderator: Next in line, we have Priyank from Edelweiss. Please go ahead.

Priyank: One quick one on your cash balance. There has been a significant reduction this quarter compared to last quarter and

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the trend is more or less down if I look over the last six-seven quarters. Could you throw some light on that?

Mphasis: One is because of the CAPEX investments. Second, we had dividend payout in this quarter and third, we made an early payout of our salaries because of the holidays in the beginning of Oct.

Moderator: Thank you very much sir. Next in line, we have Mr. Shekar Singh from Goldman Asset Management. Please go ahead.

Shekar Singh: Yeah, hi sir. Just wanted to understand the revenue growth of 12%, like what percentage of that was contributed by the currency?

Mphasis: It is close to about 4.5% to 5% is on account of currency.

Shekar Singh: The Mphasis core business used to be lot of project-based business. So, in the current environment, that business should have got impacted significantly. Can you just comment on that?

Mphasis: I think the project work in the Apps space continues, not much is being changed, but we are also building out in terms of the much bigger projects and bigger workflows in the 20-million dollar range. What we see is that project work continues, there is no cutback in those workflows, but there are delays in terms of when the projects get implemented and because we are driving our utilization so hard, the revenue realization is faster. We are not seeing any slowdown or cutback in that space. In fact, that actually gives us a lot more stability.

Moderator: Next in line, we have Mr. Kunal Sangoi from Edelweiss. Please go ahead.

Kunal Sangoi: Last quarter we discussed about eBPO services that we are planning to launch, what has been the progress on this?

Mphasis: We launched our eBPO services and are working with our top 20 clients with our new solution. There are various Proof of Concepts going on right now and we hope to see materialization of those efforts quickly.

We are currently reviewing other solutions and products also such as email solutions where the marginal cost of delivery will be minimum. Such solutions will help us move away from

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headcount based work to automation and give us phenomenal margins.

Moderator: Thank you very much sir. At this moment, there are no further questions from participants. I would like to hand over the floor back to Mr. Jeya Kumar for final remarks.

Jeya Kumar: Once again, thank you all very much for taking the time to be with us on the call. I think your questions gave us a lot of insights on things that we should also be focusing on. I look forward to talking to all of you again in a month's time. Thank you.

Moderator: Thank you very much. That concludes this conference call. Thank you for your participation.

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