



Persistent Systems Limited - Analyst Conference Call

Q1 FY18 Results

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MODERATORS

Dr. Anand Deshpande

Chairman & Managing Director

Mr. Mritunjay Singh

Executive Director & President - Services

Mr. Sudhir Kulkarni

President - Digital

Mr. Atul Khadilkar

President – Corporate Operations

Mr. Sunil Sapre

Chief Financial Officer

Mr. Mukesh Agarwal

Chief Planning Officer

Mr. Amit Atre

Company Secretary

Moderator:

Ladies and Gentlemen, good evening and a very warm welcome to the Persistent Systems' Earnings Conference Call for the first quarter ended June 30, 2017. As a reminder, all participant lines will be in the listen-only mode. 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 '*' followed by '0' on your touchtone phone. Please note that this conference is being recorded.

We have with us today on the call Dr. Anand Deshpande, Chairman and Managing Director, Persistent Systems. We also have with him Mr. Sudhir Kulkarni, President - Digital joining from the US; Mr. Mritunjay Singh, Executive Director and President - Services; Mr. Atul Khadilkar - President, Corporate Operations; Mr. Sunil Sapre - Chief Financial Officer; Mr. Mukesh Agarwal - Chief Planning Officer, and Mr. Amit Atre - Company Secretary. I am now glad to hand the conference over to Dr. Anand Deshpande. Thank you and over to you, Sir.

Anand Deshpande:

Thank you very much and welcome to all the participants on this call. We had a board meeting today and I am happy to share the results of the quarter that ended on June 30, 2017. Let me share with you very quickly some of the highlights of the quarter and then I am going to request Sudhir Kulkarni to share a bit about the view from the Digital business and what he sees from the US side and Mritunjay will explain on the services side and some of the excitement he sees there. I am going to request Sunil after that to share the financial details of the quarter and then I will come back and share with you whatever is missing and address potential questions that we pre-empt and after that we will open it up for Q&A.

In terms of the results for the quarter, the consolidated revenue for the quarter was USD 112.97 million which is a 3.6% QoQ growth. In terms of rupees, it was INR 7,280.15 which is a 0.1% QoQ growth. The PAT was INR 750.89 million which is a 3.2% sequential growth. In addition to this quarterly numbers, we also are very delighted to announce the acquisition of PARX, which is a Salesforce certified platinum partner in Europe that focuses on its customer's business models, strategic and operational objectives. This is in continuation with the global expansion of Persistent, which includes the recent openings of development centres in Mexico, Israel, and new locations in the US. Acquisition of PARX follows last year's acquisition by Persistent of Australia's leading Salesforce partner, PRM Cloud Solutions and we already a Salesforce Certified Platinum Partner. Let me now invite Sudhir Kulkarni to share with us some of the excitement from the Digital business.

Sudhir Kulkarni:

Thanks Anand. Good morning and good evening everyone, during FY17 as we set up the Digital unit in line with our strategy as a company to focus on enterprises in their journey to become software driven, we found a lot of success in doing exactly that. We had a healthy growth over the year FY17 with the focus on Digital transformation and healthcare and financial services and on platform partnerships underlining this transformation for our customers. We announced two significant wins or shall we say collaboration towards the end of FY17, which you all know about, which is with USAA and Partners Healthcare, both innovative ways to co-create IP with industry leaders in line with our own shift from effort-based work to more innovative IP-centric work in the Digital unit.

Now coming to Q1 FY18 or the recent quarter, I am happy to see the progress that we are making in our collaboration with both USAA and Partners Healthcare. We are today in multiple customer conversations for the offering that we have built based on patented technology from USAA. I am confident that I will have key wins and possibly a formal launch to talk about in my update next quarter. The collaboration with Partners Healthcare is off to a strong start and we have begun building the Open Source Healthcare Platform as well as the first clinical application for congestive heart failure. The goal of this initiative or collaboration is to lower the barriers of knowledge exchange across healthcare providers and enable a new generation of decision support system in the clinical environment. The IP we are building positions us very well for Digital transformation in healthcare and also in financial services based on the platform that we have built. During Q1, we added over 15 major customers, these include a large U.S.-based home furnishing company, a healthcare products' company, and a large mobile carrier all of whom are working with us to build transformative Digital experiences and solutions for their consumers and internal stakeholders.

In one of our new customer win for a Pharma company, we are leveraging artificial intelligence and machine learning to develop a global regulatory science and policy intelligence application based on IBM Watson to respond to enquiries using chat bot services. Along with our friends in the IBM ecosystem, this is also a great example of how new technologies and data come together to make new Digital experiences possible. This is a constantly recurring theme for the Digital business at Persistent. Revenue for the quarter though came in flat compared to the previous quarter, however, the growth trajectory for the full year looks very strong based on the momentum of new customers, new IP development, strengthening of our consultative selling theme and our strength in specific industries and platforms for the Digital business. Before I wrap up, I do want to mention the announcement that Anand talked about, how we are expanding our presence in Europe through the acquisition of PARX, a Salesforce Certified Platinum Partner in the DACH region of Germany, Austria, and Switzerland. PARX has a long history of building business solutions on the Salesforce platform for over a decade and has built a strong customer base on a solid reputation in the region. PARX has worked on newer technologies with no footprint in legacy technologies and services and will be a key component of our Europe strategy.

Coming on the heels of opening new centres in Mexico, Israel, and new locations in the US, this signals further global expansion for Persistent. We are looking forward to a major push on sales, marketing, and support in Europe as a result. Back to Anand.

Mritunjay Singh:

Thanks Anand. Services business in last quarter has seen almost 5% growth, just wanted to give a little bit colour on this growth. We were chasing couple of deals and some of them have closed last quarter, the significant ones, and one in India and two in the US. The India deal is very interesting; this is in the MP Vidhan Sabha. We had done similar work in UP last year; we wanted a validation of this in another state, so MP we closed last quarter. This is very interesting because we are using our IP and we are also using machine learning on top of that to make sure there is a lot more Intel built into what we had done already using search analytics, so very excited about this and it has a potential to expand into other states as we chase that.

The other deal is in US. We had talked about one particular life sciences company that we have been chosen as one of the partners, that deal has started to scale up last quarter and we will see scaling up of that because the nature of the deal is we will see lot of work starting in US, so initially there will be a lot of ramp up in the US and then eventually it will get into India as well. Another one which I would like to highlight is the deal that we have signed where we are rolling out an integration framework with 30 plus banks integrating with one of the product companies and this is a very interesting deal because this is like a global rollout and it will be done on Persistent paper, so will also end up acquiring fairly large number of banks as our customers. We are keeping focus in our business and there are small things and there is a lot of new technology work which is happening, so we are going after that and trying to build our business. Over to Sunil.

Sunil Sapre:

Thanks Mritunjay. You have heard from Anand, Sudhir, and Mritunjay about the business updates, I will take you through the margin movement and some financial data. The revenue for the quarter at USD 112.97 showed a quarter-on-quarter growth of 3.6% and 7.8% year-on-year growth. In rupee terms due to rupee appreciation, the revenue was INR 7,280 million with a growth of 0.1% QOQ and 3.7% YOY. The linear revenue grew by 4.1% QoQ mainly due to increase in volume by 1.8% and increase in billing rate by 2.2%. Onsite linear revenue grew faster at 11.2% driven by volume growth of 10.4%, an increase in billing rate of 0.8%. The offshore linear revenue actually had a small dip of 0.3% QoQ mainly due to decrease in billing rate of 0.8% although there was a volume growth of 0.4%.

Coming to the margins, you find EBITDA margins at 14.3% as against 16.3% in the previous quarter and I will explain the items that have impacted the margins. The first one being off course the currency appreciation in rupee by 3.4% impacted the margin by 120 basis points. The higher proportion of onsite revenue as I mentioned above coupled with investment that Sudhir talked about in some of the new partnerships we had announced last quarter, that is with USAA and Partners Healthcare, together impacted the margin by 90 basis points. The lower offshore utilization impacted margins by 40 basis points. During this quarter, we have one-time seasonal cost in terms of visa and certain acquisition related costs relating to PARX which impacted margins by 70 basis points. We have also done some investments in sales people which impacted the margin by 30 basis points and lastly the provision for certain debts that crossed 180 days impacted margin by 40 basis points. You will see that, last quarter we had a recovery against some of the earlier provided debts which had given a credit of 20 basis points whereas this quarter there is charge of 20 basis points. Certain IP revenue that is more during this quarter helped the margin to some extent. On the depreciation and amortization that came in at 5.4% of revenue same as in the previous quarter and the EBIT was 9% as against 10.9% in the preceding quarter, and at constant currency basis, EBIT was 10.2%. The Treasury income was INR 183 million as against INR 171 million in the previous quarter and the gain on foreign exchange was INR 184 million mainly due to the mark to market gain on hedges.

I would like to mention here that, the exchange gain which is largely on account of this mark to market gain on hedges has to be read along with the impact that the currency has at the EBITDA level, so what happens at the EBITDA level is that the revenue is reported at the average exchange rate for the quarter which was 64.44 vis-a-vis Rs. 66.69 for the previous quarter, and this is a direct impact with respect to

offshore revenue where the costs are in INR and hence the EBITDA gets impacted. We were adequately hedged to absorb this currency impact. The average rate on hedges was INR 70/USD during the quarter. However, the hedging gain gets accounted for in the 'other income'. So, this has resulted in sequential improvement in the PBT margin. The PBT was Rs. 1019 million at 14% of revenue as against 12.9% in the previous quarter. The ETR came in at 26.3% for the quarter and with this the PAT was Rs. 751 million at 10.3% as against 10% in the previous quarter and the growth in PAT was 3.2% QoQ and 2.5% YoY. On the CAPEX front, we had an operational CAPEX of INR 85 million, the cash and current investments amounted to INR 9,002 million as on June 30th vis-a-vis 9,411 as on March 31st. We hold hedges at the end of the quarter of USD 94 million with an average forward hedge rate of 69.40. Thanks all and I hand it back to Anand.

Anand Deshpande:

Thanks Sunil, Mritunjay, and Sudhir. In terms of some of the questions that are likely to happen, let me share with you some more details specifically around the PARX acquisition. PARX is a Salesforce Platinum Partner, headquartered in Zürich, Switzerland. In the last calendar year, which ended on December 31, 2016, their annual revenues were 8 million Swiss Francs and they have a staff of approximately 80 people including contractors. The consideration that we paid for this was 8 million CHF upfront and there is a provision for CHF 7.5 million of additional earn out over the next three years depending on performance and the founders staying within the company. So that is really the highlight of that particular acquisition and as was mentioned by Sudhir it is critical for our European business and it aligns with Salesforce and some of the business consulting opportunities that we are looking out in the future. We expect to broaden the scope of this team and integrate it into overall Persistent's Digital business in the subsequent quarters.

Now regarding the overall numbers that you have seen, as I have mentioned in the last year or so on multiple calls, traditional business of effort-based billing is essentially under challenge because the effort required for the same work has been going down. Over the last couple of years and more so in the last one year and moving forward, we have been on a journey to transition our business from being entirely effort based to being based on IP and in many cases based on IP that we have built with solutions wrapped around it essentially trying to get away from pure effort based T&M projects, so that is the journey that we are on and I am happy to state that by and large we have continued to make forward progress in this journey and even some of the projects that we have had from the services business have now transitioned to being IP plus services or solutions as was explained by Mritunjay of the MP Vidhan Sabha project and some other projects that we are doing that he discussed as the new wins that we have had. Overall, I would recommend that to not get too crazy about just the quarterly numbers, but look at long-term trend of where these numbers are heading and we feel fairly confident about our ability to meet the yearly numbers and show growth rates in teens as we have said in the past, so I see us on good track for that. The pipeline is quite robust and we can share more on specifically the kind of trends that we see, but we are seeing very good activities around the Internet of Things where we have good story and our growth has been good and also in the healthcare space. I think some of you have questions around the IBM business and what is going on there. I am happy to note that by and large the business that we have been part of which is the Watson IoT business has been making steady growth quarter on

quarter and if you looked at this quarter's or this year's numbers in the first half as compared to the first half numbers of the last year, you will see reasonable growth that we have seen in the products.

In terms of the health of the products as well, we are seeing good performance on the products, the backlog on bugs and various other things down and overall, we are seeing an uptake where customers are engaging with us very actively for long-term business. This is going to be a keystone of our IoT business in the future and we are starting to get leads from customers in the IoT space. I do want to let people know that the IoT business that we are doing is not just staffing and we are dependent on few quarters of deployment of IoT sensors and technology before the monetization of that will happen, so the best way to look at it and we will give you more details in the subsequent quarters about the number of deals that gets signed in the IoT space.

Backed on the Partners Healthcare partnership and some of the work we have done with USAA and the launch of Neuro, we are starting to engage far more in terms of building out IP-centric deals which are starting to help in the way these projects are getting started. Now, some of the big questions that people have had regarding margins, so clearly there are certain factors that were unique for this quarter, but essentially the reason for compression in the margin in some way has to do with excess capacity in terms of additional hires that we had made in terms of both training people for projects for what we see as projects that are coming up and also additional investment in sales. These are all in line and as the revenue starts to go up, I expect the profit margins also start to improve as we go along. I am going to stop here and open it out for questions and we will take questions as we get along and answer any specific questions you might have on this.

Moderator:

Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. We will take the first question from the line of Sandeep Agarwal from Edelweiss. Please go ahead.

Sandeep Agarwal:

Anand, I have a couple of questions. If you see our numbers in this quarter, surprisingly the core engines which we are assuming like Accelerite and Digital, they have shown kind of quarter on quarter decline although I agree the year-over-year number is quite robust at 36% for Digital, so has some project got closed in this quarter, what has happened there, and secondly, the services business has shown a very, very strong number, is it kind of one-off or you think that we have bottomed out in last quarter and it is going to pick up, so that is question number one? Question number two is on the margins. Although I understand the currency and other things, but the admin and sales cost has also moved up by almost 100 basis points suddenly and the impact of 40 basis although Sunil explained, is that kind of just a provisioning and you think that it will reverse, so if you could help us on this information?

Anand Deshpande:

Overall, the pipeline is quite robust and if you look at the Accelerite numbers, there is a minor dip in terms of the quarter-on-quarter numbers and also as we had mentioned earlier, we had had a settlement with one of the customers in the previous quarter which has a small impact that we will see in terms of revenues on that product going down a bit, but overall if you look at the Accelerite number and you convert it to real numbers, the dip is very marginal between quarter on quarter. The Digital business actually should have grown faster and that was clearly the plan and intention. There were certain

projects that completed, there was gap between one project ending and the second project starting out which constituted additional bench for some more time, so these are all basically operational issues that happened in the quarter. I do not want to read too much into long-term stuff because I see the pipeline and the pipeline is very robust. Sudhir, Mritunjay, and I, we have spent a lot of time with customers in the last quarter and I was there last week as well. We had some very good meetings and quality of discussion was very good. We are trying to avoid just staffing projects by putting bodies on projects, so that is really the key of what we need to do. I am very optimistic about the quality of business and nature of business happening and changes that are coming in, so I am not too concerned about the short numbers that you see on the Digital business.

On the services side some of the business that has come in as was mentioned, yes, there is some new kinds of business that has come in. So the point is that, yes, the challenges that we have had on certain business will have pressure in terms of the changes that are happening. That said, the sales team of the services business and they have been able to get good new business happening this quarter, which is the main reason for the growth on the services business, and some of the new business that we have closed on the services side is of the quality that we are looking for which means it is IP, it is next-generation business, and it is good quality work that we are doing in enterprises and other situation. So I read that as a very positive sign in general in terms of where the business could be going. It is an another engine that we have which is against the existing customers and all that stuff, but really it is generating better revenues.

If you look at the number of customers that are in the 3 million plus bucket, that number is also showing a healthy growth, so that is all a very positive number. Now, in terms of sales team utilization which has contributed to the downside on the margin, part of it is that at the beginning of the year we have started rolling our fairly ambitious plan for the year and you want to make sure you have the people to deliver it, you want to have the sales team and the capacity to sell more and more of these things and some of these decisions perhaps could have been made last quarter but got made this quarter, so the addition on the sales team which is also evident in the numbers that you will see contributes to a margin pressure, but again if we want to grow the business we have new things coming in, we have to invest in sales, so I do not want to read too much into it. You are right, finally the numbers that matter are the EBIT margin and the PAT margin and clearly we are fully aware of that and I am quite confident that if we see a little bit of uptake on the revenue which we should see because of the pipeline and the activities we see, 2 million plus will make all the difference that you want to see.

Moderator:

Thank you. We take the next question from the line of Nitin Padmanabhan from Investec Capital. Please go ahead.

Nitin Padmanabhan:

I wanted to specifically understand two things. One was if we look at the enterprise business which is our classification by industry, it has grown by around 9% and the Digital is actually flat, but services has grown by 5%. So I was just trying to understand the services business which has grown is driven by the enterprise customers within services, is that a fair understanding?

Anand Deshpande: This is one of those very tricky problems that you have when you disclose a lot of data like we have been disclosing for the last few years and we have a policy of disclosing what we are disclosing to you and what we have disclosed internally is identical, so we do not have like two sets of books on this one. The problem is we have four business units and the numbers that you show are less about services, Digital and all that stuff, it is about the performance of the four business units and every one of them is clearly exposed, so just want to keep that as a thing that you should consider at the back of your mind. That said, all the new business that we are trying to push on the services side on everything else that we are doing, we are focusing a lot on ensuring that the new quality of business comes in which has good quality business which to us is business that is not dependent on just pure body shopping. That is really the objective and the growth that we have seen in the services business this year is related to the fact that we are able to sell new kind of solutions like we have done in MP Vidhan Sabha and some of the Artificial Intelligence chat bot type solutions that we have sold to existing enterprise customers that we have within the network and some new customers which are very, I do not want to name them per se, but the new customers that we have opened are marquee names that we are very proud to have them, they are from the enterprise segment, they are not from the ISV side. All of those are all very positive signals in terms of what is going on, see if you look at the total Digital positioning that we have, perhaps that Digital number as such in the total business has gone up, but the Digital business unit which has some very specific things in it is where it is. I do not want to run the business just on a quarter-on-quarter basis or trying to give you some numbers, we are just exposing what the reality is.

Nitin Padmanabhan: I was just trying to understand from the perspective that when we changed the classification there was enterprise within services which got added...?

Anand Deshpande: The classification that we have, the same 100 is being distributed in three different ways, so the enterprise revenue generated by the Services unit will get counted there. If the Digital business generates an enterprise customer that will still get counted as enterprise but will be allocated to the Digital business unit.

Nitin Padmanabhan: The question was that on the services side that the underlying assumption that we have always had is that growth is going to be pretty low, does that change with the incremental business or the changes that have happened in that business is what I wanted to understand.

Anand Deshpande: There is a little bit of confusion that I think we have created partly but this is going to continue for some time because I do not want to change the metrics of how we are measuring all the stuff. The traditional business of T&M projects, staffing by headcount, linear business models is under a lot of pressure and we know that and we are trying to avoid going aggressively after that business. All the business units are now selling next-generation stuff and lot of the growth that you have seen in the services business and the turnaround is not because all of a sudden something has happened on the existing stuff, but sales teams are now empowered to sell everything that they want to sell.

Nitin Padmanabhan: Another one was on the margins. Within our consolidated financials that we report, we have a segment called cost of technical professionals, this number has sort of gone up by around 24 crores quarter on

quarter and like 340 bps as a percentage of revenues is increased, so I was just trying to understand what that pertains to because that seems to have eaten up all the margins for this quarter?

Anand Deshpande: Some of that had to do with the fact that there was additions on the onsite setup so some of the newer projects that we got required some special skills that were added on those projects, that is why the onsite number has gone up and that also has had an impact on the effective margins that you get because there are some new projects that we are starting out with some key customers and that has added to the extra cost on the project.

Nitin Padmanban: There is no one-time element there?

Anand Deshpande: No, there is no one-time element, but the margins will improve not because of the one-time stuff but they will improve when the top line grows up without additional incremental cost.

Moderator: Thank you. We will take the next question from the line of Mohit Jain from Anand Rathi. Please go ahead.

Mohit Jain: One is regarding the PARX acquisition, have you guys disclosed margins of PARX and whether it is dilutive or accretive?

Anand Deshpande: No, we do not have detailed margins on PARX right now, we have not disclosed it as well and there is no point disclosing it right now also because they do not have any India Centre, there are lot of things that need to be figured out before we can really tell you what the margins are, but it is small 8 million CHF which is almost 1 USD is almost 1.05, so it is almost the same.

Mohit Jain: But is it like directly loss-making profitable concern?

Anand Deshpande: It is not a loss-making concern, it is a growing company, they have been growing year-on-year and I think if you look at, we have a fairly detailed disclosure on PARX as part of the announcement that we made with SEBI and it gives you three-year numbers.

Mohit Jain: Revenue growth I know, so I read the BSE disclosure.

Anand Deshpande: Financial year 14 was 4.9 million, 15 it was 5.8 million, and 16 it is 8 million, so they have been growing concern, they are a good company and we are very excited to have them as part of it and I think they will be eventually margin accretive. I do not know exactly how much it will be in the first quarter, second quarter there is a bunch of issues with respect to working capital adjustments and all these things that has happened that will play out in the next two quarters, but again it is a small fraction of the total business that we do right now.

Mohit Jain: Sir, second your clients billed is falling on a QOQ basis?

Anand Deshpande: It is a marginal numbers, 302 as compared to the previous.

- Mohit Jain:** That is clearly a focus to go after the big guys?
- Anand Deshpande:** I think you should look at that in the context of the number of customers that have gone beyond 1 million, the number of customers that have gone beyond 3 million, so the number of customers above 3 million is now 18, the number of customers between one and three is 52 so together if you add the two it is about...
- Mohit Jain:** Three customers have moved up probably, but...
- Anand Deshpande:** Two down on the IP side and 10 customers less on services side.
- Mohit Jain:** Third is on the services margins like earlier we were hoping that services while the revenue growth may be slow, margins may be maintained. I am not referring to QOQ number here but if you see from the last three to four quarters perspective, the services business is down in terms of margin the way you report in this segment breakup?
- Anand Deshpande:** I do not have a specific comment on this right now, Mohit; it is all playing into each other.
- Mohit Jain:** This is not bench related right, this would be mostly pricing related?
- Anand Deshpande:** I think it is a combination of all those, see at the end of it, there are some factors there which are one-time as well. This MP Vidhan Sabha is an India business that will have some impact on the margin for short period, we have SI deal which includes hardware to be sold all these other things so contributing to that the eventual real profit part of this business is going to come in the second half of the year. So there is a whole bunch of things like this that have contributed, so it is not one single thing, it is a bunch of small factors and we can take this offline, so we can give you more details on exactly what the number is and what the gap is, but it is not one single thing, it is not one time, it is combination of various things, but these are early days where you spend more up front before you get the real pattern, so some of that has also contributed to this as the higher onsite percentage. There are about eight or 10 factors that are all kind of linked into each other to generate this number, but again once the revenue starts to pick up these things should take care of itself.
- Mohit Jain:** Last is on Digital, should we expect the Digital should have the highest margin given that it has been the latest service line etc. or do you think it can still remain low or below other segment margins?
- Anand Deshpande:** No, absolutely it should generate better margins than everyone else clearly, as you get past the investment phase, there are couple of investment going on but once you remove the investments, yes, absolutely it is generating better margins because rates are better.
- Mohit Jain:** What is the time frame for this investment phase?
- Anand Deshpande:** It is not that there is a, these are all like sliding things, we should start to push margins of even next quarter, it is not like we are waiting for the FY19 to happen, just wait for another quarter, see two-three

quarters and then we will make all these comments, right now I do not see any real major change in anything that we are doing.

Moderator: Thank you. We will take the next question from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria: Anand, where are we in the process of transforming the whole Digital business to solution-led business from a project-led business?

Anand Deshpande: I think it is going on track. There is a lot of activity around the healthcare side where we are trying to do far more solution-based business and also a lot of the work that is going on in the Salesforce plus Appian ecosystem is generating a long-term relationship business, so I think the progress has been pretty good. I can let Sudhir comment on it.

Sudhir Kulkarni: We are building some specific sort of solutions in the healthcare space as Anand mentioned and some of those we have also publicly talked about like Patient 360 and Care Coordination etc., and these are in addition to what we are doing with Partners e.g. so while we are moving towards a more solution led approach while selling to these customers, there is also a set of large marquee customers that we are acquiring and then we are going deeper into them in terms of doing their Digital programs that go beyond the solution that we have sold to them, that is been the plan I think it is going very well.

Anand Deshpande: Another thing I would like to point out to you Gaurav is the fact that here is the strategy that we will see more and more as we go along. We have a program where we will build out certain things which would be a solution plus deployment, but as part of the those programs we are also generating interesting IP solutions, specific point IP and the plan is to sell that to whoever buys it and some of the stuff that we have, for example, Engage 360, Neuro, and all these things, they are all not meant to be long-term relationships, but these are some very point solutions that the market needs that we can provide right now. There is a decent amount of money to get on those kinds of projects and if you sell enough of those that we plan to, they are fairly profitable because the work has already been done in some other projects.

Gaurav Rateria: On the Digital side do you think we can maintain the growth momentum what we saw last year?

Anand Deshpande: Absolutely, 100%.

Gaurav Rateria: Anand, you talked about the IoT business taking off really in a big manner maybe in the next 12-15 months after the sensors are deployed. If you look at the IBM Alliance growth right now, it looks like a big part of it is coming from the services or the traditional PE services business, would you be able to help us understand that the growth is being driven by IoT part, growth is driven by other IPs or it is driven by the services part?

Anand Deshpande: No, it is not driven by services; it is definitely driven by IoT, IP, and other things within the IBM ecosystem. Clearly services is not the fastest growing piece in that business, definitely and considering

what the challenges are that you can see with the market, it is clear that is not where the growth is going to happen, but that said we have enough IP joint solutions, go to market together, and the things where we are starting to see growth and that is what is helping the numbers stay where they are.

Moderator:

Thank you. We take the next question from the line of Ashish Chopra from Motilal Oswal Securities. Please go ahead.

Ashish Chopra:

Anand, firstly as far as the IBM deal is concerned you had mentioned about it probably breaking even and getting profitable in the couple of years' time, you expect that to happen through the course of FY18?

Anand Deshpande:

As we have said, we are seeing, there are two improvements that we had promised which we are starting to see already in the last two quarters and this will continue as we go along. A lot of it also depends on our Q4 calendar number because that is where the real number happens for IBM, so you have to wait for that for me to make any pronouncements, but that said if you look at the first two quarters that we have done, our numbers this quarter in terms of both revenues that we have generated on the Watson IoT deal as compared to the previous year are better. Second, the costs on that are also better managed this year than they were last year and the commitments that we had made about keeping certain extra people for those projects, we do not have those commitments to be made so we are seeing cost improvements on that by sort of increasing top line and reducing the costs, basically the profitability or the gap is getting reduced significantly and I think by the end of the quarter or rather at the end of the year that number should be relatively looking quite good.

There is also lot of growth that we have seen from the IoT business that is generating us the third part of the business that we have said which are very important for the whole IBM arrangement that we have, so as we said this is summarized. We are going to keep doing better on the percentage revenue that we get for the costs that we have, second is we do more LAB services in the services business and that is also growing and some of the people who are part of the product team have been moved to services that thing has happened this year and we are starting to see better revenues, and third is there is generation of leads that we are getting from IBM that is helping us setup initial engagements that are going to take two to four quarters to really generate major profits, but these are important engagements for the IoT business. The IoT business that we want to be in is going to involve people setting up sensors and technologies to get started and over a period monetizing that and we want to be part of the monetization of the business and not just providing headcount on those projects, so that is really the goal that we have and you will see the impact of this as we go along. We have moved to people who are very key members from the IoT product business to Munich to be part of the Watson IoT centre right there. With this engagement that we are in, we are starting to see lot more activities in the IoT business especially on the industrial side in Europe and this is all aligning very nicely with what we are trying to do. So we have I guess a step-by-step plans which we are executing and all I can say is that something will go up and down, but by and large we are tracking on the plan we have.

- Ashish Chopra:** Secondly from my side, the sales and BV team did see some healthy addition in this quarter like you mentioned you are building, you are getting kind of ready on that front, so how do you think about the size of this team in a sense that, I mean I am sure you need to keep adding, but do you think you started off with a fairly healthy addition to ensure that the revenue growth will probably exceed the growth of your sales team or do you think that there is still a lot more to be done on the frontend capacity building etc.?
- Anand Deshpande:** As we have said this in the past, once we start to see traction in some of these cases where non-linear revenue is starting to show better number such as in healthcare, IoT, some of the IP sales, we will keep adding more and more sales. That is part of the reason why we have added large number of people that we added in Q1 is because we think we are optimistic about what we can generate by the end of the year and this is going to be a daily activity that we are going to track as we start to see that, hey, this particular product is really selling well because of our lack of sales capacity we are holding back, we are going to keep adding more and more sales people, but irrespective of all of this stuff, at the end of it the way you have to look at it is that are we improving our profit, are we improving better yield per person and all of those standard things that need to happen and you will see the benefits around right now, whether this S&M as a percentage of sales will that go up, maybe it will, but if the business shift is happening, the S&M needs to be higher than what it was for just pure services business. Ratios will change, we do not know what the right ratios are and we will evolve as we got along. Finally, all of this is being done so that we can improve the margins overall.
- Moderator:** Thank you. We will take the next question from the line of Akshen Thakkar from Fidelity. Please go ahead.
- Akshen Thakkar:** Just a couple of, one housekeeping question in just trying to understand the margin picture maybe slightly more nuanced, so the housekeeping question really is that if we look into this year what is the level of rate inflation that you are likely to see onsite and offshore, so that is question one? I am just trying generally to understand from a margin point of view, you started the year at single digit EBITDA margins with the amount of work that you are doing, it is sort of understandable that there will be quarterly volatility in margins but just if you look at the whole year how comfortable are you to get to let us say double-digit margins or may be expanding on margins that you had last year and just from where we are sitting we may or may not understand the math, but just what are the key drivers to get from 9% EBITDA margins to double digits because I am presuming you still have inflation hitting you next quarter?
- Anand Deshpande:** Let me explain the way this inflation stuff, we have deferred a little bit on the salary increments this year, we have moved some people's salary increments that were supposed to happen in July to October and for some other people, we have moved them to January, so there is no additional wage pressure in this quarter, so that is one important thing. The second point I would like to point out is, see here is the challenge that we have and this is sort of universal problem and we have to solve this problem and I am sort of explaining to you what we are trying to do and how it looks. In general if you base it on effort-based billing, the market is the way it is, the effort required is going down, the number of people

available has gone up, the rates are not going to go up, you are going to have margin pressures on existing business.

The only way to get around this problem is to find something else to sell and sell solutions where you are selling IP and selling the same thing multiple times and to do that you need to have more sales people who are little different and different kinds of sales members, but effectively if you sell the same thing eight times, 10 times, you will start to see benefit of that incremental sales generating direct margins to your bottom line and that is the model that we will have to evolve as we go along, so clearly we think we are on a path till that is going to happen and yes absolutely we think that by the end of the year or even next quarter and the quarter after that, we should see improvement in margins. We are aware that we cannot be operating at margins of single digit EBIT and we have to get this to pretty healthy numbers even better than what we had last year and that is clearly the goal and everyone is completely aware of that.

Akshen Thakkar: Last question from my side Anand if I may is on the acquisition, would it be fair to assume that current margins may not be as high as what you have given that all of it is onsite, but two, three, four quarters down the line as you move work offshore and given that the Salesforce or billing ratio is to be decent, margins over there can be company equivalent or slightly better than company?

Anand Deshpande: You have already answered all the questions, but...

Akshay Thakkar: That is my understanding, I just wanted to confirm.

Anand Deshpande: Absolutely your understanding is quite good, there is no question about it but the point I am trying to make again and again is that it is time we sort of moved off of this, how many people, what rates all that stuff, to saying, okay if I am building out and if you look at the PARX website there are many solutions that they are building out, they have some very cool IP technologies that they have not necessarily leveraged. We think we have a much better ecosystem to deliver the numbers out of Salesforce's IP that they have and we are not going to just sell it in Europe, we are going to sell it all across the world. So there is a certain new skill set we have acquired and we are going to integrate that very aggressively in the business. There is, in the whole context of this 80 people in Europe generating numbers is a good way for us to expand our European presence. I do not want you to super analyse on headcount on a per person basis, just have some faith, we will share the numbers going up in this particular business. This is actually an excellent acquisition in many ways. You should go look at their website and see what they have delivered, the number of senior people, the quality of projects that they have done. I think it is a phenomenal acquisition. I am very excited about what we see in this thing and we have had a challenge on our European business, our European business is less than 6%. It is time to grow it and the best way to do it is to do this acquisition. We will look at more such acquisitions in the future.

Moderator: Thank you. We will take the next question from the line of Basant Choksi, an Individual Investor. Please go ahead.

Basant Choksi: I am not sure if this has been discussed earlier, but my question pertains to be BFSI sector, are there any developments or growth happening in the sector?

Anand Deshpande: The answer is yes.

Basant Choksi: If it is possible for you, can you discuss what type of developments are you currently doing on Blockchain?

Anand Deshpande: Actually, I would take this question offline, please. We just stay focused on this quarter numbers for the 10-15 people I have on the queue right now. I will come back to you with a very detailed answer, you look at our website we have enough on Blockchain, it is a huge area for us and do not judge me, I love talking about all the stuff, so we will get all over the place if we get there.

Basant Choksi: Just one last question, last con call you mentioned some deals did not happen because in the March quarter, so you are expecting it to happen this quarter, so are all the deals on record?

Anand Deshpande: Yes, some of those happened, some new ones should have happened that moved to the next quarter, it is a pipeline.

Moderator: Thank you. We will take the next question from the line of Madhu Babu from Prabhudas Lilladher. Please go ahead.

Madhu Babu: Sir, is there a risk of onsite increase drastically because that is what is being reflected in the numbers on a directional basis and what would that mean for margins?

Anand Deshpande: Onsite might go up but not drastically. Finally the assumption that onsite necessarily will reduce the margin is a function of how the billing happens. I want to just sort of correlate that right away, just say that yes, there is some risk that the onsite numbers could go up, all the same we understand the need for improving the margins, yes, we will have to deal with that but we think we can charge better rates onsite as well. Unfortunately, all these things are rather complex in some ways and it is not that straightforward anymore. The business is quite different from what it was one year back or two years back, so it is not that straightforward about headcount, people, rates, and numbers anymore.

Madhu Babu: Last year we had the IBM which was again onsite and now we have done one acquisition in Europe which is again an onsite. Would we able to absorb these costs or it is kind of a long-term investment which we are looking at, because that is how the trajectory of margin has been falling because of these investments?

Anand Deshpande: No, but I think this PARX acquisition is very different from the IBM acquisition and I am very sure that the margins that you will see on this after we clean out the first set of working capital basic numbers, we are halfway in the quarter and all that, so we should get two to three quarters and we will see a margin improvement in this one. I do not see this to be reducing our margins in anyway. It is a straightforward

Salesforce business, there is enough opportunity in the market, there is a lot of growth happening. We do a lot of Salesforce work offshore, we have 600 people right now working on Salesforce-related stuff.

Moderator: Thank you. We take the next question from the line of Mayur Parkeria from Wealth Managers India Pvt. Ltd. Please go ahead.

Mayur Parkeria: Last quarter, we discussed about the reseller agreement that we have with IBM, so if you could little expand on that?

Anand Deshpande: We have made some deals on reseller agreement this quarter and this will take some time, but it is something that is going to be beneficial in the long run. By the end of the year, we should have some reasonable revenues in reseller opportunity and we are engaged right now with customers every minute. In Q1 we have added some more sales people in that team and you will see numbers that will help in that reseller part.

Mayur Parkeria: Lastly, Sir on the new product that we have launched in the last quarter, so how is the traction for those products in the market and what is the response from the market?

Anand Deshpande: The response is very good, the product is not a new product. The product that we launched called Neuro is based on a license agreement that we have with USAA. So if you look at some of the press releases and other activities not just press release, news releases, you will find that USAA is coming with us to customer calls and telling people about how important their product is and how well we have done the whole thing together, so it is a fairly safe product in the sense that this is a proven technology, it is being used already, it is well-known and we are reselling it in a sense.

Mayur Tarkeia: Apart from that Neuro, I was talking about Concert and ShareInsights the product that we launched in the last couple of months?

Anand Deshpande: Right, both of those are doing quite well, actually we had some sales on ShareInsights this quarter, we had some sales on Concert as well this quarter, so all of those are playing along quite well, and they are all integrated well into the accelerate portfolio right now.

Moderator: Thank you. We will take the next question from the line of Rahul Jain from Emkay Global. Please go ahead.

Rahul Jain: Firstly on the IoT thing, we won this award, congratulations for that but is this more in terms of the capability that we have showcased or it is function of the kind of project we would have done in that market?

Anand Deshpande: This one has to do with an award that we won for the work we did on the Watson platform. If you really think through it, there is an another one that explains the Robot Concierge that we built using IBM Watson to engage customers in real estate showrooms and such things, that is really what got the award, this is actually fairly cool work.

- Rahul Jain:** On the PARX, one motivation probably the existing owners could be in terms of that this practice goes global and not just stays with German-speaking market, so does Silvio take a bigger role in the organization or he still looks the PARX portfolio at the moment?
- Anand Deshpande:** He takes a bigger role. He will start to help significantly. There are three-four key individuals there, who have been running a much smaller organization than their capacity. Within the context of Persistent, they are expected to play a much bigger role in our European business across the board and they are going to sell not just Salesforce, but Digital transformation and services across Europe and some of the IoT work that we are doing in Munich will align well with some of the work that is happening with them in the DACH region, so it is to be thought of as a holistic acquisition and not just a Salesforce team addition.
- Rahul Jain:** If we see the number of projects they have done and versus the revenue they have, does that which translate like maybe 10 K, 20 K kind of deal on average basis, is this the usual size or they are more focused on SME right now?
- Anand Deshpande:** They are not focused on SMEs per se. They are doing some of these projects across and you can actually look them up, if you go to the Salesforce partner portfolio, you will see a lot of details about their business. In general, if you have a very small company like 60 to 80 people right now, you end up being on many projects as a small partner, much harder to take full ownership on large projects.
- Moderator:** Thank you. We will take the next question from the line of Sandeep Agarwal from Edelweiss. Please go ahead.
- Sandeep Agarwal:** Anand, I was saying that if I remember correctly we were kind of indicating a mid-teen kind of growth numbers or early teen kind of growth number for this year in terms of revenue and slight improvement in margins at least, so do you still, I know it is just first quarter and...?
- Anand Deshpande:** I have no reason to believe that will not happen. I am quite confident we will make those numbers.
- Moderator:** Thank you. We will take the next question from the line of Shashi Bhushan from IDFC Securities. Please go ahead.
- Shashi Bhushan:** How far we from the stability of growth in the ISV business? Do we see muted performance for quite some time now?
- Anand Deshpande:** We are going to live in a world where there will be a chaotic stability.
- Shashi Bhushan:** Stability is good if it is not declining, it is still better than, are we expecting any growth there?
- Anand Deshpande:** We are selling in the market, yes, there will be growth, there will be some deceleration, so it is a volatile market you will see some of this going up and down all the time. As I said to you before, in the overall long-term trend that we are trying to focus on, we are trying to really go after markets and businesses

where we are not charging effort based. A lot of ISV business will shift in some sense from being just driven by us working by putting bodies on those projects to working very closely with the ISVs to sell to enterprises whoever buys and wants to become a software driven business. The business will shift quite a bit, but we are part of the shift and I am quite excited at the moment that we have seen in general in terms of where, how our conversations have changed, what we are talking to customers and all of those things, and it just takes some time, that is all I can say. I would like to thank all of you for being on this call and really appreciate your support and you will all of course hear from us as the quarter progresses.

Moderator:

Thank you ladies and gentlemen. On behalf of Persistent Systems, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.