Persistent Systems

Analyst Call

PERSISTENT

Persistent Systems Limited - Analyst Conference Call

Q3 FY18 Results

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MODERATORS

Dr. Anand Deshpande
Chairman & Managing Director

Mr. Sudhir Kulkarni
President - Digital

Mr. Jitendra Gokhale
President - Alliance

Mr. Atul Khadilkar
President – Corporate Operations

Mr. Sunil Sapre
Chief Financial Officer

Mr. Mukesh Agarwal
Chief Planning Officer

Mr. Amit Atre
Company Secretary

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Moderator: Ladies and Gentlemen, good day, and welcome to Persistent Systems Earnings Conference Call for the Third Quarter ended December 31st, 2017. 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); Mr. Jitendra Gokhale – President (Alliance); Mr. Atul Khadilkar – President (Corporate Operations); Mr. Sunil Sapre – Chief Financial Officer; Mr. Mukesh Agarwal – Chief Planning Officer; and Mr. Amit Atre – Company Secretary.

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. In case you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Dr. Anand Deshpande. Thank you, and over to you doctor.

Anand Deshpande: Thank you, Aman, and let me welcome you all on the Persistent call, the first one in 2018. And I'm really delighted to share with you the Financial Results for the Third Quarter that ended on December 31st.

The highlights of the financial numbers are that the revenue during the quarter Q3 FY18 in US dollar terms was 122.53 million, which is about 3.8% quarter-on-quarter growth and an yearly growth of 11.4%. Revenue during this quarter was Rs.7918.90 million, which was a 4% quarter-on-quarter growth. The profit after tax during this quarter was Rs.916.70 million, which constitutes a 10.9% quarter-on-quarter growth. As we have completed three quarters of this financial year, I would like to state that the revenue during the three quarters of this financial year totalled $353.60 million, which is a 10.5% year-on-year growth in dollar terms. The same amount in rupees is Rs.22,811.57 million, a growth of 6% year-on-year. The profit during this period has been Rs.2493.82 million, which is a 9.1% year-on-year growth over the three quarter period. I'm also delighted to share that the Board of Directors at its meeting declared an interim dividend of Rs.7 per share of a face value of Rs.10 per share for this financial year. I'm also delighted to share that the Board has decided to induct Mr. Sunil Sapre, our Chief Financial Officer, as an additional Director on the Board and henceforth his designation would be Executive Director and Chief Financial Officer with effect from Jan 27, 2018.

With these very high-level overview of the numbers, I'm going to invite Sudhir Kulkarni, who is visiting us from the US and he is currently at the airport to share a little bit about the Digital business and what he saw on the US side. I'm going to also invite after that Sunil Sapre to share the details of the financial performance, specifically around various accounting terms and activities that have happened, and after that I will take over again and share a little bit about some of the sales wins and some of the deal wins and other things and other points of interest that maybe followed through. And then we will open it up for questions very soon after that.

Thank you and let me invite Sudhir Kulkarni to share his point of view.

Sudhir Kulkarni: Thanks, Anand. I hope you can hear me. This was a quarter in which I think we consolidated our focus. We have been talking about co-creating models or co-creation models of digital solutions, especially in the areas of healthcare and financial services. This is important that one looks at the significant changes that are happening in the US healthcare industry, for example, for the long-term. I'd characterize the big changes as almost a tectonic shift taking place in healthcare. For example, the acquisition of healthcare insurance company, Aetna, by CVS, which is a $69 billion acquisition, so CVS is a pharmaceutical distributor or the acquisition of a $41 billion Hospital Corporation of America by an insurance company, UHG. These are all sort of massive changes that are happening. So all of these indicate to me that the lines of distinction between payer, provider and pharma and distributor, which were pretty clearly drawn in the past, are almost becoming like lines in the sand as the world of healthcare realigns.

Now, on a micro level, all that a patient, which is the consumer of healthcare, cares about is getting the best healthcare at the lowest cost, and there too, the focus is shifting at a micro level from curative to preventive care, from episodic to wellness monitoring, from in-room consultation to remote consultation and monitoring etc., from in-person treatments to robotic surgeries and so on. So I can go on and on.

But you get the point that there is a very different kind of a model that leverages state-of-the art technology, and in patient care, in operation of hospital operations as well as creating new models of care. Now that's where we play very significantly with our long-term bet. And in this context, I am pleased that our work with Partners HealthCare and a few other hospital systems in building digital platforms and clinical and operational applications is progressing well. And I had previously called it our co-creation models where we take risks along with our customers on their digital transformation journey.

Now, remember these are long-term bet and our investments will yield results over the long-term. So suffice it to say that in the short term, this will not show major movements on topline etc., but we continue to invest in these because we believe in them and these digital models are the ones for the long haul that will transform the healthcare industry for example.

Obviously, at our size, we could only take some of these bets and we decided to take those in the transformation of two major segments in the industry, healthcare, with mainly care management and providers and financial services mainly adoption of new technology from fintech into the digital banking space. Now, the unit as a whole, the digital operating unit as a whole grew to about 22%, which was a 3.7% growth organic and including Parx, the acquisition, it was about 8.6% Q-on-Q.

We've maintained a 44% year-to-date growth over the last three quarters, if I look at the three quarter summation. And this quarter, we added several new enterprise customers and grew some existing digital programs at large existing customers. Some of the major new ones include a healthcare project, a large hospital system in the Midwest, a bank, an exchange, and a large retailer. We had decent traction in the DACH region, where we did the Parx acquisition, and in Australia where though our base is small, we're seeing some nice growth coming from that geography. And I expect that with some renewed focus on specific countries within these geographies, we will build some momentum over time.

Our investment in digital IP or IP assets including frameworks and accelerators, while not generating large license revenue yet, have begun to give us some leverage in building solutions and services around them. And one more thing, even as our focus continues on building innovative solutions and co-creation models, over the last couple of quarters, we also saw a small uptick in terms of margins in the digital business. And obviously, we are going to keep consciously building this business for the long-term, we are going to keep investing in this, but this uptick is nice to see this quarter as well.

So with that I'm going to hand over back to Anand for continuing the rest of the call.

Anand Deshpande: Let me now invite Sunil to share the details on the financials, please.

Sunil Sapre: Thank you, Anand, and good evening to all of you and let me wish you a very Happy New Year to all of you being the first call in 2018. I'm indeed thankful to Anand and the Board for my induction as a Board member. As you have already heard about some of the updates Anand gave and Sudhir mentioned about some flavor of the digital business, I will give you an update on the margin movement, the CAPEX and liquidity position of the Company. The revenue for the quarter was $122.53 million recording a growth of 3.8% quarter-on-quarter. The growth was comprised of growth of 2.7% in the services revenue while IP led revenue grew by 6.8% due to a seasonally strong quarter for the Alliance business. In Y-o-Y terms, the growth was 11.4% for this quarter. The revenue in rupee terms was Rs. 7,919 million with a growth of 4% quarter-on-quarter and 6.2% year-on-year. The YoY Rupee revenue growth was lower than the dollar revenue growth due to the currency movement. For the nine months, revenue was $353.60 million with a Y-o-Y growth of 10.5%.

On more details about the revenue, the 2.7% QoQ growth in linear revenue was mainly due to the increase in billing rate. The onsite linear revenue grew by 4.7% driven by volume growth of 2.9% and growth in billing rate by 1.8%. And the offshore linear revenue grew by 1.1% primarily due to increase in billing rate by 1.7%, while volume dipped by 0.6%.

On the EBITDA margins, the EBITDA margin improved to 17.4% this quarter as against 15.2% in the previous quarter. As you know, we had a wage hike during this quarter for the junior level staff, and this was primarily offset by improved utilization and other operational efficiencies. The utilization for the quarter was one of the highest in the recent quarters at 79.9% as against 78.6% in the previous quarter. You will find some movement in G&A expense, which is mainly because in the previous quarter, we had a credit of Rs. 41 million on account of insurance claim settlement, whereas in this quarter there were professional fees relating to Parx acquisition and certain other tax and advisory services, which amounted to Rs. 35 million. The growth in EBITDA was 10.9% quarter-on-quarter and 4.5% year-on-year.

In terms of depreciation and amortization, it came in at 5%, same as in the previous quarter, and EBIT was 12.4% as against 10.2% in the preceding quarter. So far as other income is concerned, it came in higher at Rs. 143 million as against Rs. 133 million in the previous quarter. As regards Forex, due to rupee appreciation of 2.2% during the quarter, foreign exchange gain was lower at Rs. 50 million as against Rs. 203 million in the previous quarter. You would observe that in the previous quarter rupee had depreciated significantly to 65.33 at quarter-end, whereas in Q3, rupee appreciated in two stages, first from a level of 65.33 to about 64.50 and then it closed at 63.87 as on 31st December and this is the main reason for the swing in foreign exchange gain. In absolute terms, PBT was Rs. 1,175 million at a margin of 14.8% as against 14.6% in the previous quarter. The tax provision came in lower due to reversal of tax liability in certain overseas jurisdictions on completion of assessments and tax benefits for R&D related work. As a result, the ETR was lower at 22% for the quarter as against 25.9% in the previous quarter. So the final result on the PAT for the quarter was Rs. 917 million at 11.6% as against 10.9% in the previous quarter. The growth in PAT was 10.9% quarter-on-quarter and 11.9% year-on-year. For the nine-month period, PAT was Rs. 2,494 million at 10.9% of revenue, registering growth of 9.1% over the same period last year.

The operational CAPEX for the quarter was Rs. 19 million, cash and current investments amounted to Rs. 11,117 million as on 31st December as compared to 9,992 million as on 30th September. The value of forward contracts outstanding at the end of the quarter was USD 85 million with an average forward rate of 67.10 per dollar.

Thank you all and I hand it back to Anand.

Anand Deshpande: Thank you, Sunil. I'm delighted to share that for the first time in the history of the company, we have more than 10 billion rupees of cash on the balance sheet which is an achievement for us. The other thing I wanted to point out was that we have added Mike Kuklenko who joined us as Senior Vice President for Sales. He's based out of UK and will be driving our business growth in Europe.

Well, Mike used to be part of IBM and he was involved in working with us very closely on the CE/CLM products where he was running the sales team for the IBM CE/CLM product team. We are delighted to have him join our team, as we significantly strengthen our reseller business and go direct to customers in the CE/CLM portfolio. We are very confident that with him joining the portfolio, it strengthens our positioning in the market as we go direct into this market as a reseller.

Couple of other wins which were already mentioned by Sudhir, but in addition to that, we had a good opportunity of building out some next-generation solutions that leverage cognitive and artificial intelligence and machine learning in terms of building products solutions for some of our large customers, and these will help us in the long-term as we look at our growth.

I would also like to invite all of you to take a look at our website where we have some very interesting videos about some of the work we have done, including a very nice video with Pune Police about the Dial 100 Emergency Response Services that we have put up. We also announced the launch of the Accelerite's ShareInsights 2.0 product, which is a really nice self-service big data analytics platform and we hope that generates revenues for us in the data and analytics space in the next year.

I'm going to take a pause here, and I'm sure you have many questions. I will request the host to open up the lines for you to ask questions and we will answer your questions for the next 45 minutes. Thank you very much.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. First question is from the line of Sandeep Agarwal from Edelweiss. Please go ahead.

Sandeep Agarwal: So I have two questions, just wanted to get some qualitative input on that. So, Anand, if you see, since last year our ISV business contribution has gone down by 5%, still our nine-month YTD growth is like 10.5%. So does it clearly mean that the bottom of that growth for is definitely behind us and we can see a very significant jump in growth going forward? So that is question number one. And question number two, which is not related, but I would like to understand that we have not been able to do much other than US market in terms of revenue. The contributions have definitely moved up by 180, 200 basis point in last nine months, but why are we not going very aggressive in the European geography where we are hearing lot of deals are coming in, particularly digital arena, or you think that you know US itself is a very, very huge market and there is enough food for us in the US market alone?

Anand Deshpande: I think two very good questions, Sandeep. On the first part, when you mentioned the ISV stuff, actually I also believe in the ISV market. I think that's a market that has been good for us for the last 27 years. So we definitely want to continue to invest in that market. And we do see good signs in terms of business coming in, in that area. So, I hope we will see continued growth in that area. That said, I think our overall strategy at the moment is to stay focused on providing businesses to become software-driven businesses. So we are continuing to focus on the broader market in terms of helping companies to become software driven. So your observation that, yes, we are starting to see the bottom on many of our legacy businesses is actually true and we are definitely continuing to increase our growth in that market and hopefully you'll see in terms of absolute numbers growth happening, but when you compare that in terms of percentages, I don't want to comment a whole lot because it all depends on what other businesses do, which we hope also grow at a rapid or equally rapid pace. Now regarding your second question, regarding Europe, again your observation is very right. And two things that you should note in that context is one is of course we just announced this Parx acquisition about five months back, and that has started to just come online. We wanted to make sure that we got a consolidation on some of the basic stuff there. And you will see increased focus on European business. Also, you know Mike Kuklenko joining in Europe at the level of seniority that he brings in should help us in getting some more activities to happen in Europe. We have a plan on how to increase our reseller business on the CE/CLM part which has a very significant European presence and you should see some more activity on Europe. So definitely looking at non-US geographies is clearly the objective. And if you look at these numbers 12 months from now, I think they will look very different from what they are today. But when you're sort of looking at percentages, it's very hard to make up dramatic shift in the numbers as percentages, but you will see a steady increase for sure. On the quarter-on-quarter basis, you might observe that there was a dip on the European business, but I want to reassure you, it is because of one specific Accelerite deal that we had in the last quarter, meaning the previous quarter, which did not happen this quarter, which is why you might see a dip. But overall, the European business continues to be a stable growth business, again much smaller than US for us, but definitely growing. I just want to stop here on this question, but we'll take the next question. But before we take the next question, I just wanted to let people know that we are tracking on Twitter, and if you have a question, you should send a tweet on #Persistentresults and we will pick those questions up after every few questions depending on what comes up there. So that could be another channel for you to reach us in terms of if you have a question as well.

Let me now hand it back to Aman.

Moderator: Thank you. The next question is from the line of Nitin Jain from Credit Suisse. Please go ahead.

Nitin Jain: So I have two questions. So first on the margins. So how much of the expansion in margins in 3Q came from the IP business, which will eventually reverse in 4Q? And how much of it was from efficiencies and high utilization?

Sunil Sapre: So as you can see in terms of the utilization numbers, the increase in utilization was 1.3% and the increase in IP business essentially was of the order of about 3 million. So overall increase in this EBITDA percentage is contributed equally by both the parameters.

Nitin Jain: Okay sir, half of that is sustainable, you mean.

Anand Deshpande: Yes, see when we are moving into the fourth quarter, the operational efficiencies of course need to hold and so far as the business is concerned, the substitution of business with the seasonality of IBM business, if it happens through the IP route, then it has a possibility to hold if you have the substitution of business happening from the services business, it has an associated cost. So that's the only way to look at it.

Nitin Jain: Okay, thank you. And the second question is for Sudhir on Digital. So are you satisfied with this 30% to 35% organic Y-o-Y growth in this digital business. Given your smaller base, can this business grow at a faster rate?

Sudhir Kulkarni: I mean, nobody can be satisfied with whatever they have, right? I think we are, as I said, consciously putting some efforts in there in terms of the programs that we are launching with some customers. Now some of these are producing results in short-term, some of these will produce results in the long-term. So, we can go for bigger, better growth. We certainly can. We are putting a lot of effort in certain specific areas, but I don't want to just hold out a thing out there saying that we can go multiple times with what we have, certainly we are making all the efforts that we can.

Moderator: Thank you. The next question is from the line of Apurva Prasad from HDFC Securities. Please go ahead.

Apurva Prasad: Anand, couple of quick ones, I think you mentioned earlier, but if you can probably highlight about the Accelerite part of our business, now there is a steep decline this quarter and what's the outlook on that piece? And my second one is on the margins. So, Sunil, if you can help me with the wage impact on margins?

Anand Deshpande: Let me ask Sunil to answer the margin related question and then I'll give you the answer on the Accelerite related question.

Sunil Sapre: Yes, so on the wage hike, we effected the wage hike for the junior staff and the impact was about 85 basis points.

Anand Deshpande: So let me comment a bit on what's happening on the Accelerite' side. As you would be aware, one of our premise in Accelerite was to take on end-of-life and potentially declining product line. These products have generated the revenues that we thought they would and they were overall are a fairly profitable businesses for us. We haven't done any more Accelerite acquisitions in the last couple of years and that's just because we haven't found the right ones as such and we ended up doing some of those as part of the Alliance business in some form or the other where we had a similar effort required in terms of any rebadging employees and all the other work that we did, which could have been part of the Accelerite business, but that actually ended up as part of the Alliance business. So we have continued to be on this lookout for acquiring assets and acquiring teams and all of those things. So that part of the business continues to be there. More than last one year, we have tried to also make sure that the assets and the customer base that we have in Accelerite can be used for launching new sets of products. So we have three lines of products which are completely based on the Accelerite portfolio and then ShareInsights. So the three lines of products that we are selling as part of the Accelerite line, one of them is related to cloud and cloud-related stuff, we have re-branded that as Rovius. That is starting to hit some traction, but we should see more action on it in the next 12 months. The second one was the Radia endpoint client management product that we have. We are continuing to support Radia and maintain Radia, but the growth on that part is going to come out of Sentient which is the next-generation product, which will allow you to do real-time monitoring and it becomes very relevant in the security context especially when you look at the kinds of challenges where machines get infected and trying to disable machines and getting them going is becoming a big issue. So we are very confident that Sentient as a product will do well in that market. And the third line of business that we are focusing on is around the IoT and Concert stuff. So we have taken the assets that we have acquired from Aepona and trying to extend those to the IoT market. So that's really our strategy for doing what we are doing in that area. And then we have a new product that we have built around ShareInsights. So, as I've pointed out to you in the past, in general, we are on a journey to migrate our business which has been purely effort based for ISVs, which was the traditional business, which was the OPD business that Persistent did well in, to a model where we have IP, IP driven revenues, which are value based, and going to customers that are broader than just ISVs, so that we can provide them help on their journey to become a software-driven business. And this is the journey that we are on. So while we want to share with you all the details, I think one has to look at our rather holistic view of the company. And some of the Accelerite IP will be sold as IP, but it comes with IP packaged with a bunch of services that are being counted as part of the services and other business. And all of these are helping us transform us from being effort-based company to being a value-based company. And this is going to be a journey that's going to be our path for the next few years.

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

Nitin Padmanabhan: So this quarter specifically from an Accelerite perspective, I think we have seen margins come off quite sharply, any specific reason for that, and is that a one-off, and do you see that coming back?

Anand Deshpande: No, the margins have dropped predominantly because the revenue has dropped, okay. So it's a small base with a fixed cost of engineering and that's the reason why that has happened. And the part of the revenues that dropped was also because of a few deals. There are two things actually worth pointing out here. One particular thing is regarding a trend that we are going to see in these kinds of businesses as we look at newer businesses that there was a particular deal that we have done, which is reasonable size deal, which would have helped in making the margins happen. But instead of selling that as a one-off license deal, we were able to convert that to a revenue share agreement over a period of time. So it's a five-year deal now instead of a one-year deal. And we believe that that's really what people are looking for. We will see some of that and those will give better returns and long-term stability in the business. So we had one of that happen. And the second reason why, there were a couple of other deals that should have been closed, but we didn't want to discount this quarter, and we hope we will get them later.

Sunil Sapre: So the margins will come up for the numbers on Accelerite for sure. Once the revenue goes up, it automatically hits the bottom-line, because the cost is fixed.

Nitin Padmanabhan: Sure. And just one last one on Digital. Digital, during this quarter, if I exclude Parx, it appears to be quite weak. So, again, is this just a quarter specific thing or there is enough in the pipeline to bring it back to normal growth that we've seen in the past?

Anand Deshpande: Sudhir is there, I'll let him answer

Sudhir Kulkarni: Sure. So, yes, I think we were expecting a few things to close this quarter, but it didn't happen. I think the pipeline is fairly good. We should see growth in the business, and obviously Parx has added a little bit of a bump there. But Yes, I mean, we will continue to execute on the path that we've set out. It is something that is a weak quarter I would say. I was quite clear that we would have probably done a little bit better than what we did.

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

Mohit Jain: I've three questions. One is on the volume growth for the quarter, like, we saw there was a marginal decline if we remove the Parx numbers on a Q-o-Q basis. So last few years we've seen some growth in linear business as well in the third quarter. So any specific reason on client ramp-down that you would have noticed this quarter?

Anand Deshpande: No, one of the things I would point out is that I had mentioned this in the last couple of quarters as well. See, overall, I'm starting to see good traction and good quality business for us. So we are saying 'No' to bad quality business. Now I'm not chasing bad business anymore. I was last year, but not anymore, this year. We have stopped just doing staffing projects. So this will have some impact on the linear business. But I think, overall improvement of quality of business is very crucial right now and that's really the plan. So that's what I would say is the reason why you would see a slight negative on the services business.

Mohit Jain: So saying 'No' also means closure of certain projects or you're not taking new assignments?

Anand Deshpande: No, it's not like we shut down any accounts, but we did not follow through on some of the accounts where people were expecting stuff. See, one of the things that's starting to happen and then it's a trend that we are trying to avoid is, see the captives in India are starting to ask for a lot of headcount resources staffed in their offices. We had some business in that category, but we have now sort of consciously started to turn ourselves away from those kinds of businesses. So you'll see some of that happening, but again, we'll manage this as it comes along.

Mohit Jain: Okay. Second is on Parx like when will it start contributing to your margins like next year or next quarter?

Anand Deshpande: No, I think you'll start to see improvements on margins already and you'll start to see that it's generating profits on margins from next quarter, next financial year meaning next quarter onwards, we'll start to see some numbers and again on from first quarter of the year. I think it's a good asset, they are doing quite well, and I think there are opportunities of extending the work that they're doing in DACH region with fulfillment from our Indian team. So that's sort of where the improvement on margin is going to happen.

Mohit Jain: But they remain profitable?

Anand Deshpande: Yes, meaning it's not as profitable as the rest of our business, but I'm sure we'll get there pretty soon.

Mohit Jain: Okay. And lastly sir, for Sunil sir, any outlook on margins for next year and tax rate?

Sunil Sapre: You know, we don't have an answer to your question, right?

Mohit Jain: Tax rate?

Sunil Sapre: Tax rate, we'll give you the idea, but we don't know what Trump is going to do. And we have the budget next week, right?

Anand Deshpande: So I mean just to answer you Mohit, as you see, we still have certain levers to improve, you know areas like onsite utilization, the traction on the IP deals. So these are basically the areas which contribute to margins more than proportionately. So the whole idea will be to concentrate on that and hold the improvement in utilization that we already achieved. So rest of it will be played by the business mix that we are able to achieve.

Mohit Jain: Do you still find some scope for expansion and utilization in it?

Anand Deshpande: See, I think the profit margin improvement will happen by changing the mix of the business, okay, meaning that is utilization, Yes, you can get a few percent point here and there, but it's not going to be dramatic. There is not a whole lot of room in it. I'm quite pleased that the point where we are in terms of the quality of new deals that we are seeing in the market. The new quality deals actually generate better revenues, better margins and long-term sustainability with key partnerships where we get a seat on the table, that's really our objective and we are starting to see more of those. And that's what's going to generate growth and that's what's going to generate the margin.

Mohit Jain: So that is more on revenue per employee side that we will see some changes happening?

Anand Deshpande: Yes, meaning finally we've got to beat this out through revenue growth. There is only so much you can squeeze on the costs.

Mohit Jain: Right. Lastly on the tax rate, any benefit that you guys because you have a large business in US?

Anand Deshpande: Yes, it's all not worked out Mohit, we'll get back to you on that one in a while, I think next quarter we will be in a better position to answer that question. We believe that there will be an improvement because tax rates are coming down, but it's more complicated than that unfortunately.

Anand Deshpande: I want to take a question that we have on Twitter right now from Ankit Pandey saying, what's the update on IoT Business profitability on the IBM IoT stuff that we have, right? So let me give you a quick answer on that. So for those of you who track all these numbers at the level of granularity that you do, we had a 5% growth this year and I'm talking calendar year. And we got about $49 million in terms of our revenue, we counted about $15 million this quarter, that's really the bare bone number that I'm giving you. In terms of the profitability for this quarter, this year for the IBM business, the profits were better this year than last year, but they were still not at the level where they are usually profitable, but the subsidiary and ancillary business and other things have happened along those lines have been really good. We have really gotten many other smaller deals which you don't see in this one, but direct relationships with some of the large order companies and other things have been really the benefit of this. Next year, we hope and we believe that we should have a similar rise in the revenue numbers for the topline and the fact that we have managed to reduce costs for the next release that we are submitting and proposing should give us improved margins for next year in this particular business on its own. See, as I said, there is business happening, we were not able to make it partly because we were not reselling directly reaching the customers. With Mike joining the team, I think we can change that. And he was the one who was running the entire business anyways, so he knows all the customers, he knows exactly what they have bought, and now with him working for us, we should see some growth there. Let me go back to Aman and get going and I'm going to start giving you shorter answers now, because we have several people who have questions on their list.

Moderator: Sure. Thank you. The next question is from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria: Anand, just a question on where are we in the journey of transitioning from just doing project-related work to more solution-based work, which will be more longer-term in nature and give us more sustainability of revenues as far as digital is concerned, if you could throw some metrics around that will be very helpful. Thank you.

Anand Deshpande: I think absolutely, we are on that journey. I think, as I said, with this quarter I can very confidently say that we believe that our story is working. We have been trying out this in various different formats, but I think we have a pretty good idea on what needs to happen. I do expect that, next year, we should double down on sales side efforts to make sure that we can replicate the wins that we have had across a broader and wider portfolio. So I would say we are on track in terms of the kinds of deals we have closed. As Sudhir pointed out, the focus is a lot more on the healthcare side where we think there are lots of very interesting opportunities. Some of the work we have done in the financial sector also is around digital opportunities. And then with Mike and others joining on our push on the industrial stuff also we have done some really good work in the last few quarters and it should start to show results next year.

Gaurav Rateria: Sure. Thank you. And second question, do we have any big investment planned for the next year either with respect to IBM CE/CLM product or with respect to Digital or do you think it's going to be an investment as usual we do in the business?

Anand Deshpande: See, it's very hard to, so let me say the following. We have $175 million on our book. And clearly, we are looking for acquisitions of different kinds. We definitely want to make sure that these acquisitions are accretive and also are taking us in the right direction, rather than just adding revenues and volumes. So we will look for IP and other domain-centric acquisitions that help us either growing regions outside of North America or give us access to IP and technology in the newer things. So those two things we are continuously looking for. On the IBM side, again it all depends on what gets offered, but I'm not trying to acquire a whole amount of legacy business at this moment because we really need to get the transition to move faster than it is and acquiring legacy would not be the right thing to do at this moment.

Moderator: Thank you. The next question is from the line of Mayank Babla from Dalal & Broacha. Please go ahead.

Mayank Babla: My first question was more on SG&A expenses. I have noticed that year-on-year it's come down from 14.6% of sales to 12.4% of sales. So how sustainable is this and what can we expect going ahead?

Anand Deshpande: So it's again, some of these things are little bit plus or minus depends on how the deals get closed, but I do expect that we will invest in sales next year. But I'm also confident that revenue should go up to the extent that the sales numbers would be in line with the SG&A expense.

Mayank Babla: Okay. And my next question was, sir, in this transition from the effort-based business to a more non-linear kind of a business, I've seen that the services contribution has reduced from 48% odd to 42% as of Q3 FY'18. Sir, what is your aim or target mix, over the next five years, what can we expect?

Anand Deshpande: Five years is too long man, but in the next two to three years, I do expect that the services business also will transform to being non-linear, because every time we go to a customer, the customers are also asking us, show me value, don't just show me effort, this aligns with where we want to go. So I think the services business will grow, we still continue to be a services-driven company. But I think the effort-based business in the next two years, I would like to see that in the sub 30% range, where 70% of our business is coming from value that we are providing to customers rather than just effort, and we'll see how it goes after that.

Mayank Babla: And sir, just last, if I could squeeze in one more question. Sir, could you just throw some light on this co-creation model that you've been talking about?

Anand Deshpande: Right. So let me explain little bit about how these go and everyone is unique and different, but what we try to do with the customers is that, we convince the customers or they convince us, however, we agree that we should build something that can have long-term value. And the idea is to see if we can get some revenue share out of that rather than just we billing it out one time on effort. So some of it has, and so now then the issue becomes, who spends when and when do you actually monetize it and who shares the risk. So depending on the situation and the customer context and our ability to see how aligned it is to various areas, we have been trying to get in many cases. So there is a little bit of that happening across the board, but we have to manage this within range, is what our goal is. So we are not doing this unconstrained. But I think these things will give you long-term returns and long-term margins in some sense. But I think it's important that we do some of this because this whole linear effort-based business, it has an expiry date in some sense, we can't continue with this forever.

Moderator: Thank you. We have the next question from the line of Neerav Dalal from Maybank. Please go ahead.

Neerav Dalal: I just had a question on the IBM IoT deal, you just said that you did 5% growth this year. Are you happy with the growth and what number would it have been if not for that?

Anand Deshpande: No, I think 5% to 7% in this kind of a market for a stable product with IBM selling it, they'll say that they are happy with it. I'm never happy with anything I get. That said, I think if you look at our premise of where we are short, the plan we had was to say that, okay, this will continue to grow at single-digits, but we will try to go after the IoT business as such where we will go and do some more end-to-end solutions in the IoT space along the customer lines. On that account, I would admit that we have not been as successful as we would have thought and that is for various reasons. But I think the fact is that the customers that we work with are pretty much the marquee customers. They are all trying to do IoT and we were short on our ability to sell to them. And with Mike and some more things that we are likely to do in this quarter, you will see our direct access to customers going up and I believe that there's also been a change of strategy on how IBM is looking at partners. We are a re-seller now. They have decided to hand off rather than say hand off, but they're trying to focus themselves on larger deals and let partners do more. That should all help us in increasing the IoT Presence.

Neerav Dalal: Very quickly, wage hike impact in 4Q if any?

Anand Deshpande: Yes, I mean, some of it is already factored in. There'll be a little bit of wage hike in terms of the senior level people, but also at the end of the year lot of the provisions that were made for bonuses on sales and other teams will get converted to actual numbers. So we'll see where that ends up.

Moderator: Thank you. The next question is from the line of Shivam Gupta from CWC Advisors. Please go ahead.

Shivam Gupta: So Sudhir, just to peel this digital growth a little better. So from the last few quarters we do understand that given the nature of this work some deals move from one quarter to another and at the same time some deferments take place. So there should be some interplay of offsetting of this input in often number of deals and given where your funnel stands, do you think that this 4%, 5% is something which is comfortable for the next few quarters in terms of Q-o-Q growth we have to do?

Sudhir Kulkarni: I think we've set out to grow this business as our growth engine for the company. And I think we're kind of betting a lot on investing in this business. So yes, I mean we're looking to grow this business, what volume it generates from the big bet that we're taking in this business. Only time will tell. Some of these things are taking time, So that's what you're seeing right now that there is a longer sort of horizon for some of these initiatives.

Shivam Gupta: So Sudhir, just a small follow-up there. So, if I recollect this, you were like, definitely tracking much higher than where we were for this quarter. So is there something in the environment which has changed for the number to come down and when you're saying that these investments are made for long-term, is there some kind of timeframe you have in mind before you could start tracking any kind of revenue or quantitative milestones on these investments?

Sudhir Kulkarni: Yes, I mean, look at some stuff that we're doing in the healthcare systems for example, right. I mean, a large hospital system doesn't move backwards, and it being right now is something that is going to impact their future in a pretty significant way when they engage with patients or when they engage with different physicians, the kind of clinical applications that they have that are rising on the platform they've been building. So, these investments will need at least year, year and a half to generate meaningful traction. We've already announced that we have built the congestive heart failure application. How much this generates for us right now in the next quarter or two, only time will tell.

Shivam Gupta: So but when these investments do come to monetize, I mean even after, let's say, two, two-and-a-half years or one-and-a-half years later, these should be materially higher in terms of the run rate that they will produce currently compared to what we're seeing today in your digital BU?

Anand Deshpande: No, I think, Shivam, your point is valid, let me move on because we have only 10 minutes to go on this. I would like to take your question offline.

Moderator: Thank you. We've the next question from the line of Dipesh Mehta from SBICAP Securities. Please go ahead.

Dipesh Mehta: I just want to get update about IP, if I look at the portfolio related thing, if I look investment, what we saw is mainly one kind of thing is flattish for last few quarters. If you can help us how we are looking, whether there is any change in strategy about IP portfolio and the investment which we intend to make in creation of IPs. And M&A also we have not seen much activity, I think partly you touched upon, but if you can provide overall strategy considering the investment seeing flattish kind of movement over last eight quarters or so. Second question is, any update if you can provide on the Partners of USA and Partners HealthCare? Thank you.

Anand Deshpande: Okay. The first point regarding investment being flat, clearly IP we need to push the sales rather than the engineering costs. So that is really the plan. And as you are aware when lot of the IP was from acquired places that we had taken on and our motivation was to squeeze the costs on it by improving the efficiency by reducing the number of people. On the other question regarding what acquisitions, Yes, see we are looking around for acquisitions and you'll see some as they go along. I don't know exactly what's happening in the pipeline. That said, I don't want to put our target to the acquisition team to just acquire for the sake of acquiring as well.

Moderator: Thank you. The next question is from the line of Madhu Babu from Prabhudas Lilladher. Please go ahead.

Madhu Babu: Sir, within our enterprise clients in digital, so what has been the revenue run rate, annual run rate for large clients, what does it reach now?

Anand Deshpande: I don't know what specifically to tell you, but if you look at the top one, top five, top ten, you should see an indication of what's happening on them. The other indicators which we are sharing right now are this in a fact sheet we do show you how many customers we have which are larger than 3 million and between three and one. And if you look at them, all of them are trending in the right direction. So definitely our ability to grow an existing account has gone up far more and those are all good signs.

Madhu Babu: Okay. So sir, would we have an enterprise account with say 15 million over one, two-year period or already we are having?

Anand Deshpande: No, we have several right, meaning actually, let me say the following, we have at least five accounts, which are more than 10 million.

Moderator: Thank you. The next question is from the line of Girish Pai from Nirmal Bang. Please go ahead.

Girish Pai: Anand, in an interview today on one of the channels, you mentioned about double-digit growth for FY19, did I hear you right?

Anand Deshpande: Yes, that is right.

Girish Pai: Okay, the second question is regarding the IBM CE/CLM deal. 2017, did you break-even or where exactly was the margin for the CE/CLM business?

Anand Deshpande: No, we were more negative in calendar year 2016, we were lot less negative in 2017 and we will be profitable in 2018.

Moderator: Thank you. The next question is from the line of Ashish Chopra from Motilal Oswal Securities Limited. Please go ahead.

Ashish Chopra: Anand, my question once again was around Accelerite. So the three to four lines of products that you mentioned over here, what I wanted to understand was on the scale of the business from current levels of 32 million to 35 million, do you think that given that this gets sold a lot with other services and packages and hence this grows kind of linearly from this level or should we expect, could there be a tipping point to these solutions whereby this can scale significantly in the foreseeable future? Just your thoughts on that. Thanks.

Anand Deshpande: Okay, no. Clearly, our intention on these products is to see a hockey stick and see a growth rate. Now, unfortunately, because these are all products and the way they need to be sold and all of those things, we can't predict exactly when that will happen, but clearly, that is the goal, right? And if that doesn't happen, and we are not seeing, we are going to see slow linear growth, then we are going to be brutal about shutting them down as well or selling them off or doing something about it, but clearly having a slow linear growth on a product business is a bad idea.

Moderator: Thank you. The next question is from the line of Ankit Pande from Quant Capital. Please go ahead.

Ankit Pande: My question to Dr. Deshpande would be, you did mention that end-of-life we've been inactive in the market for a couple of years. So could you just give us a brief overview of the market and where we're looking to participate?

Anand Deshpande: Right. So, see actually few things happened in the last few years which are all trends that came in from different points of view, and when we started this end-of-life products, we felt that we had a stable growth on our existing business. Unfortunately, the market changed faster than we thought, and by and large, we found that the effort-based business was under a lot of threat, so we did not want to continue on a situation where we're just growing revenue rather than growing good quality revenue. So that was the main reason why we decided to sort of slowdown on some of those and focus a lot more on newer and better revenue.

Ankit Pande: If I can just interrupt you, so my reading is correct that there is a big overlap between end of life and what you have just said that you would look to sort of move away from the linear activity or just staffing activity. So if I have to look at inorganic activity for you for Persistent in the IP space, what are the spaces will you target more actively to make up for this area where you have lot of space?

Anand Deshpande: So let me finish what I was trying to tell you on this side. So clearly if you look at opportunity side of the business, we think that there is a lot of action in data, IoT, digital, areas that we are focusing on. We see a lot of action in machine learning, block chain and some of the new technologies that we are working on. Some of these we showcase to people at the Investor Day. We are starting to see action in those, some of them have reflected into actual deals that have come to us during this quarter and some are in the pipeline. So we are looking for acquisitions that will help us in broadly in a few areas, let me say the three areas that would be of interest. One is to look at increasing our footprint outside of North America and US like Parx and other things we're looking at where we can go to other regions. Second, to go after IP, which is going to generate us capabilities and strengths in these newer areas like say machine learning or block chain and there is chatbot, there's a whole bunch of things. Again, these will be smaller acquisitions, small team acquisitions, not very large companies, but companies that are helping us in terms of either building out an IP capability or building out a domain capability. So those are sort of where we are trying to go on some of these and some of them could come out of existing customers, selling those pieces to us or whatever, but really our focus is to go on a trend where we are selling next-generation stuff to customers who want to become software-driven business.

Ankit Pande: Great. So if I have to just factor in for next year, double-digit growth, would you say that there is a meaningful component of inorganic there?

Anand Deshpande: Without knowing much I would say, yes, right, but I don't know the answer to that question. These things are unfortunately very unpredictable. We are interested if there is any product that suits our requirements. I know we are sort of past the time that we want to be now. So I'm going to stop this thing here, hand it back. Finally, I'd like to thank all of you for being on this call. Really appreciate the support. And if you have any questions, by all means, send them to us and we'd be very happy to answer them for you by e-mail. Thank you very much.

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