Persistent Systems Limited

Analyst Conference Call

Q2 FY19 Results

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MODERATORS

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Chairman & Managing Director

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President Sales – Technology Services

Mr. Jitendra Gokhale
President Sales – Alliance Business

Mr. Atul Khadilkar
President Delivery Operations – Technology Services

Mr. Sunil Sapre
Executive Director & Chief Financial Officer

Mr. Mukesh Agarwal
Chief Planning Officer

Mr. Amit Atre
Company Secretary
Ladies and Gentlemen, Good Day and Welcome to Persistent Systems’ Earnings Conference Call for the Second Quarter of FY19 ended September 30, 2018. As a reminder, all participant lines will be in listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing ‘*’ and then ‘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 Sales, Technology Services, Mr. Jitendra Gokhale – President, Alliance Business, Mr. Atul Khadilkar – President Delivery Operations, Technology Services; Mr. Sunil Sapre – Chief Financial Officer; Mr. Mukesh Agarwal – Chief Planning Officer; and Mr. Amit Atre – Company Secretary.

I would now like to hand the conference over to Dr. Anand Deshpande. Thank you and over to you, sir.

Anand Deshpande:

Thank you, Aman. And thank you all for being part of this conference call. The way we will do this is I am going to read out some initial statements that are from the news that we shared yesterday. And then I am going to request Sudhir Kulkarni to share some of the details from the Digital and the US side of the business. And then I am going to request Sunil Sapre, our CFO, to give you the financial details. The intention being that we will answer many of the known questions that I am sure you have. After that we should open it out for Q&A and we will answer the questions as we get along.

Just to get started, in terms of the quarter ended September 30th, 2018, we clocked a revenue of US$118.23 million which was 4.3% negative Q-on-Q growth. Revenue in rupee terms was Rs. 8,355.57 million, which was a 0.2% Q-on-Q growth improvement. The profit before tax, PBT, was Rs. 1,268.79 million which was 7% growth over the previous quarter and the PAT was Rs. 881.41 million which was 0.9% over the previous quarter.

In terms of the highlights, we will talk about some of these again as we go to details in this one. One is that we announced last week that Partners HealthCare has launched a new center of excellence in collaboration with Persistent Systems, called Partners HealthCare Pivot Labs with an aim to disrupt the delivery of healthcare to enhance patient experience, improve clinical outcomes and control costs. And we will share a bit about this one, we are quite excited about this particular collaboration.

Second, Persistent Systems acquired Herald Health, a Boston based startup, that transforms healthcare data overload into clear actionable insights for care providers and patients. We also acquired during the quarter a small but important selected business and allied resources from Above Solutions India Pvt. Ltd. We were recognized in the Winner’s Circle by HFS Blueprint Report for Software Product Engineering Services. And we had a Trade Finance solution that won the Alconics Award for Best Application for AI and Financial Services.
In terms of the specific quote that I had in the press release which I am going to restate which I guess will be part of the questions that you might have, so while our Digital numbers are lower than expected, we see good growth opportunities across all segments of our business and multiple new projects started this quarter that will deliver long-term revenue growth. The shortfall in digital revenues can be attributed to short closure of one of our projects and shift in business mix as some projects moved offshore. We continue to invest in new technologies and enhancing domain and consulting skills in our customer’s geography, as can be seen with the acquisition of Herald Health and setting up of Partners HealthCare Pivot Labs.

I am going to hand it off to Sudhir first to give you a little bit of an overview of what is happening on the US side of the business, some of the opportunities we see and some of the business drivers. And then he will hand off to Sunil Sapre and then I will close out with some other open items. So, Sudhir, please.

Sudhir Kulkarni:

Thank you, Anand. Good morning, good evening, folks. I can tell you any number of success stories and how our customers are responding to our offerings, etc, and to our digital transformation point of view. But then it will appear like trying to cover up for a quarter that did not go well. So let me address that first.

We had a setback this quarter, with numbers coming in below expectation. However, when I look at the pipeline we have, the customers we have won and how CXOs of our existing customers are appreciating what we do, I think that there is a great growth potential for our business, as Anand mentioned in his comments.

Now, I fully expect the Digital business to bounce back from the 1.6% Q-on-Q decline to a healthy Q-on-Q growth and end the year ahead of our overall revenue growth. The revenue impact of an early closure of one of our major digital projects, and some customers’ projects moving offshore will be overcome with customers ramping up their digital spend with us in coming quarters. In the case of the closed project, there was a mismatch in client expectations and what we had set out in our big response. Since the mismatch was beyond an acceptable range, we decided that it was better to agree on a short closure in mutual interest. However, we continue to work with the client on other projects and, thus, have an ongoing relationship. The revenue impact of this short closure was about $800,000.

Our focused efforts in health care are starting to yield results, as we have seen from recent announcements. And we see continued progress in our relationship with Partners HealthCare, the largest hospital system in the state of Massachusetts. I am super proud as we partner with them on Partners HealthCare Pivot Labs for building transformational patient centered applications for digital health. We are also beefing up our set of offerings in health care with the acquisition of Herald Health, again, centered on data-driven transformation in that space.

Now, we had quite a few good wins this quarter, as Anand alluded to, including some in healthcare and in financial services. These included a transformative elder care experience platform, an analytics and visualization platform for a state government department in India, a US networking giant engaging us in
transforming their customer experience and a midsized bank initiating a major cloud and data driven transformation program using technologies such as RPA, AI/ML on AWS.

Now, on the Services front, we have been reviewing our margin profile and growth potential across several clients in the services portfolio. We have exited a few clients which had a revenue impact of about $300,000. Besides this, the shift from onsite to offshore covers some of the services’ clients as well. So we continue to strengthen our ability to deliver and staff projects both onsite in the US and in India. But it did impact us negatively through delays and some lost revenue in Q2. We have also embarked on some inorganic ways of enhancing this ability, as you have seen from the announcements.

One more area to enhance our digital offering has been to partner with two of the best-breed players in the market. I had spoken last time about OutSystems, a low-code application platform with whom we are now a global partner; and Mambu, a cloud-based core banking platform. We are engaged with these partners in building a strong pipeline of opportunities across the US and Europe.

In conclusion, with a clear set of steps taken already to fix our supply chain and a good set of pipeline of opportunities, I believe that the Technology Services business will bounce back to a growth rate which will be healthy at the end of the year.

Back to you, Anand.

Anand Deshpande: Let me hand off to Sunil to share some of the financial highlights.

Sunil Sapre: Hi, everyone. Thank you, Anand. And good evening to all. Anand and Sudhir have shared the market outlook and some of the revenue-related details. Let me explain the margin movement, liquidity and CAPEX for the quarter.

Revenue for the quarter came in at $118.23 million, 4.3% lower than the last quarter. One of the primary reasons for the dip in revenue in dollar terms was the fact that this was a seasonally soft quarter for IP. As you know, we had a large deal in Europe last quarter as part of the IBM reseller arrangement.

Looking at the linear and nonlinear mix of revenue, there was a decline of 2% in linear revenue due to shift of some business from onsite to offshore, and also a short closure of one project. The nonlinear revenue dropped by 10.4%, mainly due to seasonality of IP-led businesses I mentioned above. The revenue in INR terms grew by 0.2% because of the currency benefit on Q-on-Q basis, and 9.8% on YoY basis.

In respect of linear revenue, there was an increase in volume by 0.8%, and billing rate dipped by 2.8%. The onsite linear revenue declined by 8.7%, constituted by 5.4% decline in volume and 3.5% decline in billing rate. Some of this is attributable to the lower revenue impact, which has higher billing rates. The offshore linear revenue grew by 3%, comprised of a growth of 2% in volume, while billing rate increased by 0.9%.
As you are aware, we had a pay hike during this quarter, which took effect on 1st July. The sales and marketing expenses decreased by 3.8% as there were a few exits during the beginning of the quarter. There were some vacancies that got filled, people came in towards the end of Q2. So while on quarter-on-quarter basis we do not see a dip in sales headcount, the effective number of people were less during the quarter.

We could collect a good amount of money from the customers that we had provided for in the previous quarter, which resulted in benefit on the currency side, to the extent the collections were in excess of the hedges. The doubtful debt provision also came in at a lower level this quarter.

In terms of the currency depreciation, we had the benefit of 110 basis point benefit on the margins. EBIDTA margin for Q2 came in at 17.2% as against 16.8% in the previous quarter. And utilization improved to 81.9% as against 80.7% in the previous quarter. On depreciation and amortization, it was 4.7% as against 4.8% in the previous quarter, more or less flat in terms of absolute value. The EBIT was Rs. 1,038 million at 12.4% as against 12% in the preceding quarter.

The treasury income was Rs. 195 million against Rs. 166 million during the previous quarter, helped by the increase in treasury size and increase in short-term yields, net of some M2M loss on certain long-term mutual funds.

We have an exposure of Rs. 43 crores in the IL&FS group. This is in the form of inter-corporate deposits. These mature during the period Jan 2019 to June 2019. In terms of the developments that have happened over the last few weeks, with the Government of India taking control of IL&FS, and the systemic importance of this financial company, we believe that this will be a going concern going forward, and hence, there is no reason for immediate impairment of value in terms of our deposits. We have also not had any default in terms of interest till date. And we will continue to monitor the situation on a regular basis. We also have made disclosure in the financial statements with respect to this exposure.

The foreign exchange gain was Rs. 36 million as against Rs. 21 million. Given the sharp depreciation in rupee there was a mark-to-market loss on the hedges taken earlier. However, as I explained, the good collections during the quarter to the extent of unhedged portion got converted at higher USD-INR spot rate, which reduced the impact of M2M loss on hedges.

PBT was Rs. 1,269 million at a margin of 15.2% as against 14.2% in the previous quarter. So it is after quite a few quarters we have crossed 15% PBT kind of a number. ETR for the quarter came in higher at 30.5% as against 26.4% in the previous quarter. And for the half year it was 28.5%. We expect the full year ETR to be in the range of 27.5% to 28%. One of the reasons for increasing ETR is the fact that some of the mark-to-market losses which were higher this quarter due to the market volatility, both in currency and money markets, are not considered for tax purposes unless actually crystallized.
The other reason being that one of the SEZ units completed the tax holiday period, and there was a small charge also resulting from completion of business management of some of the previous years, which we have disclosed as a previous charge for previous period which is about Rs. 12 million.

PAT for the quarter was Rs. 881.41 million, which increased 0.9% on QoQ basis and 6.7% YoY basis, keeping the margin for Q2 at the same level as previous quarter at 10.5%.

Operational CAPEX for H1 was Rs. 147 million. Cash on the books, Rs. 13,266 million at 30th September as compared to Rs. 12,425 million as of 30th June. The forward contracts we have outstanding at the quarter-end is $120 million at an average rate of Rs. 69.49 per dollar.

Thank you all, and I hand it back to Anand.

Anand Deshpande: Thank you very much. Ladies & gentlemen, we will now begin the question-and-answer session. The first question is from the line of Nitin Padmanabhan from Investec. Please go ahead.

Nitin Padmanabhan: Anand, just wanted to understand your thoughts in terms of how do we see the market in terms of, let’s say, the underlying demand, do you think it is slowing down that is sort of driving the miss? Because if you look at last quarter, you had spoken about very strong pipelines and that is sort of translating to growth going forward. So, that was one. And the second question was, how do you see growth in the second half of the year for the services business, both Digital and the IP side of things?

Anand Deshpande: So in terms of the market demand, we definitely see growth in the market demand and the activities on the new project requirements have actually gone up quite high. Now you said, “Okay, you said this last quarter, what happened in this particular quarter?” So I think the biggest challenges, in some sense, has been not so much about the demand but about the ability to fulfil the demands of the right set of people at the right time. So, that has been the biggest reason why this quarter was slower than it should have been, it is not because of demand. We are also hiring a lot of people at the moment, as was seen in numbers that have gone up. Some staffing did happen towards the end of the quarter, which should start to help out in the last half of the quarter. But clearly there was a certain set of numbers that disappeared because of the short closure that we talked about. So, in some sense, what I would say is this has been a very volatile quarter, there has been very high entropy. But the activity is very high, the demand continues to be good. The opportunities are definitely there. And the conversations with customers are quite positive. The customers are definitely demanding next-generation technology and stuff. And moving people off existing projects to new projects and that whole transition has been the challenge to some extent. I do anticipate, if I look at the next half, second half of this year; I see a few things that, and again I do not want to go out on a limb to say numbers that would not be met, so let me be very careful about how I state this. But here is sort of what is going to happen. One, of course we see better numbers from the Alliance business in the next quarter, quarter three for sure, because that is
going to be the last quarter for the calendar year for our largest partner. So, we do see a much improved number there. We also have a reseller business that is tied into that part of the business where we have got some good number last quarter. I expect similar opportunities in the pipeline for numbers in the next two quarters on some of the resale business. On the digital and services business. Again, on the services business, we do see high demand. On the digital business as well, we are seeing a lot of activity. And again, we have been doubling down on the healthcare side where we are seeing a lot of action. We have seen a lot of activity around the partnerships that we have done. And some of the videos that we have released will give you a good sense on some of the works that is going on. Some of the other commentary that people have made, and I would also relate to that, is the fact that deal sizes, per se, are better today in these markets than they have been in the past, even for us. We are seeing good activity across the board in all of these opportunities in various places. This particular quarter, of course, we also had European holidays which contributed to the blip on the PARX side, and there were a bunch of things that are hard to explain, per se. But I am quite optimistic about the opportunity that we are in, as such. And I do not see there is a demand problem, as such. I think it is our execution problem rather than a demand problem, is how I see it. So I will let Sudhir comment a bit more, because he is sitting in the midst of the demand. And then we can take the next question.

Sudhir Kulkarni: I agree with you, Anand. I think there is no issue with demand, neither with the new customers that we have in our funnel and prospect list nor with existing customers upping their spend with our strategic accounts as well as our growth accounts. So I do not see that as a problem. And yes, I think if we execute better... on another note, I think one addition that I would like to say is that Sunil did mention about the sales attrition and rehiring, and some of it was stuff that we wanted to do because of performance and productivity reasons, which I think is the right kind of pruning. But at the end of the year, we do have a significant focus. And at the end of the quarter, last quarter, we had a significant focus in hiring a bunch of salespeople. And I think by the end of October or mid-November we will be able to do it fully and hopefully we should see these people come into full gear by the end of the quarter. So that might take some time to get them productive, but we are on the path of actually adding to our salespeople significantly.

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

Madhu Babu: Sir, could you give us a view on how are we looking to mine the existing enterprise accounts? Because I think we go with the solution-led approach, but after that how do we mine the account to reach a much larger revenue run rate?

Anand Deshpande: So, I think there are different things that we are trying to do across various parts. So, again, let me go back a step what we did at the beginning of the year. So prior to this we were doing all the digital and enterprise digital transformation work as one broad horizontal area where we think everything is digital and anything would be either customer facing or employee facing. At the beginning of the year we started to say that, okay, digital is starting to get a little bit more specialized in some areas, and we have been looking at healthcare, life sciences and industrial areas to focus on. So if you see the activity level, you can look up our website and other places, we have done specific partnerships where we are now not
just putting our toe in but going deeper into some of these partnerships because we have created
domain expertise and knowledge about the account and operational improvements that we can
generate. So, these are all techniques that we are using to dig deeper into accounts so that we have
more things that we can sell in limited areas of expertise. So, instead of saying that we will grow every
opportunity that we get out of Salesforce into a large deal, we are saying in the healthcare area, in the
financial services and industrial, if we see an opportunity where we are already embedded, we want to
find a way to grow that business. So, this strategy is clearly defined by trying to build expertise in these
areas and going after them. So, yes, we all understand that we need to convert some projects to long-
term relationships. And to build long-term relationships we need to have domain expertise and
customers facing relationships that need to be in place. Some of these acquisitions that we have done
give us access to that, and that is really what we are trying to see. And in specific accounts, we are seeing
improvements on the healthcare side or on the other sides where we have seen deeper relationships not
just in terms of volumes of revenues, but health of partnership; meaning, the relationship at what level
are we speaking to them and what level of engagements are they willing to make with us. And it is hard
to share all of this stuff. See, the problem is when you are sitting on a down quarter, anything I say is
better with things that we are going to pull up something, but I will just have to wait out for another
quarter to show you some of these things, but that is really the way it is.

Madhu Babu: And just one more, sir. In terms of capital allocation, I think the cash position has been very strong, so
would we look at a buyback? Or would we look to acquire a company under traditional IP or enterprise
services to boost our portfolio?

Anand Deshpande: So, like we have pointed out, there are two vectors on which we think we need to focus on in terms of
the acquisition related areas. So, ones that has been around technology related areas, and we have
outlined the fact that, see we have been a data, AI, machine learning-centric company for many years,
and that is an area that we need to augment and extend. So, we are looking for opportunities in that
area. And the second area is to get to customers and the interaction related stuff, and that has been, to
start with, in the healthcare area because we see an opportunity there where we have some good entry
points. But yes, that is really the strategy in terms of what we are trying to acquire. Now we are starting
to do some of these, and we will do more of them. And again, that does not mean we have enough in the
pipeline to acquire with all the money that is sitting in there. So, we have to figure that out. Regarding
the buybacks, they were discussed in some sense but we do not have a clear plan on exactly doing this,
this quarter. We will definitely look at it again in January when the dividends are due. So, I will let the
board decide on some of these ideas because the financial guys are in that room, and I am going with
their call.

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

Gaurav Rateria: Just two questions. Firstly, Anand, you have made certain interventions in the last two quarters in the
form of merging the digital and services unit. You had made some changes on sales incentive structure,
how has that manifested? And do you expect to see some results going forward? And second question is
that on the digital business what should be the normalized level of growth? Two years back we were
growing at 50%, this quarter we grew at 5% because of multiple other factors. But what should be the normalized level of growth? Thank you.

Anand Deshpande:  
Okay, so I think two good questions. So, Gaurav, your question was regarding the changes that we made, so just wanted to outline for the completeness of this discussion some of the specific changes that we talked about. First specific change was the fact that we merged the technology services group which was a merger of the services and their digital business, and the reason we did that was to avoid internal conflicts that we were seeing because of various reasons. That particular thing did address that problem and we have now certain growth that is happening in those areas. The second major change we had done was we changed the sales comp from being quota driven to being percentage commission. The consequence of that was that yes we lost some people who resigned because they realized they were not going to make the numbers, and we have very good understanding of who is going to make the numbers and who is not, and there is no place to hide. So, in a sense, it is good to get the right people who are hunters, hunting new business has been the objective. So, short-term consequence has been that, yes, we have had a depleted sales team to some extent. The long-term consequence is that, yes, that is exactly what we wanted, we do not want people who are sitting around and collecting on existing accounts. So that is the change that has been made. So it did have an impact this quarter, but I think it is a good thing to do.

The third thing that we made, which was different, was that we created a sales velocity team, which was a common team that we created to help the sales team to deliver sales numbers. So, that part has been moving slowly but steadily. We now have a machine which we have implemented, which uses machine learning and other things. That allows us to understand what we should sell to which customer at what time. And that is starting to kick in and hopefully that should generate better productivity with salespeople as we look at the next quarter. And another thing that we did, which is starting to kick in, is the stuff that we created around what we call growth and solutions team. And we are focusing on 2 + 4 + 3, is how I would say areas of interest where we want to focus on. The three verticals I called out were healthcare and life sciences, financial services and industrial vertical. And all of these three things we have people who are looking at what growth should be done, what acquisitions, partnerships should be done. So, if you look at the videos, you will see some of the activity that has come from here.

In terms of the 4 technology segments that we are focusing on, we are focusing a lot on cloud. We upgraded our partnership at Amazon and AWS and also with Azure to get to the next level. We have been doing better with partnerships. And we are doing a lot more work in data, ML and AI. Then security, again, we had some change in the personnel there, but we are starting to see some more activity, this week is the Oracle World and we should see some more announcements that we are working together with them.

And finally, the fourth one was around IoT where, again, market has been slow, but we are starting to see some increased traction at smaller numbers though. And then there are two others that we have focused on, one was relating to product engineering services and the second one was partnerships. Again, in both of those we are starting to make some move. So, in terms of long-term things, I think...
these are the right things to do for us, and I am pretty pleased at where we are at the moment. It did cause certain grief in the first two quarters which would have caused some numbers to go down. But when you are looking at it on a longer-term basis, you have to make some of these decisions. So, that is really what I wanted to mention on that.

In terms of the norms for digital growth, clearly, we need to do double digit every quarter. That is clearly the number growth that Sudhir has as his target to exceed. And I do realize that we have not been meeting those numbers. But then there is no real excuse for not growing at that level for small numbers. So that is the target we have for us internally, but we have not met it.

**Moderator:** Thank you. The next question is from the line of Mayur Parkeria from Wealth Managers. Please go ahead.

**Mayur Parkeria:** Sir, first, a little operational question. When we acquired Citrix and Aepona together, they were around a run rate of $20 million, right? $8 million and $12 million approximately. And we understand that Aepona has been into the Sentient part, but it is going little weaker, I know it has since we have launched. So where are we on that in terms of Accelerite run rate for these two? And if you can just also add on overall Accelerite products, some color on the different products in terms of Concert, Sentient, Neuro, how they are going.

**Anand Deshpande:** Yes. So, let me give you a quick overview on that. So right now, we have the product that came from Citrix is now Rovius, which is a cloud platform. We have some good deals in this quarter on that product and we have been selected to partner on a fairly large project, which is still early on. But the way this product works, the license revenues that we get will come over a period of time. So, it does not have immediate short-term impact in terms of the revenues that you might get. A lot of this is paid for as a service, so that takes a while. The second set of products were all the Radia products, which were all the ones that we picked from HP, and that is the endpoint client management product. We have added to that the Sentient product set. Again, there is a slow but steady progress, we had a few new customers there, absolutely new ones in new product areas, mainly around the ATM related areas. The third set of products that we have are around the Aepona one where we have sort of migrated that to Concert. We have moved that; we have a few customers on which we are working on that. But overall Concert and the IoT business has been slow for doing new deals in it, a lot of them have been very small project related activities going on. So, selling that product has been pretty hard. And then the new product that we have which we have built out has been ShareInsights, which is also in the market. And we have made some good partnerships in this last quarter with AWS and others. So hopefully, in the next two weeks, three weeks there is a launch there, we should be able to see how well that goes. In terms of the revenues, we shut down our cloud business which was our backup business for a bunch of things, we had a Location business which had a time line that ended. So that has been shut down. So I think we are maintaining steady to flat revenues on the existing products. The growth will depend on how ShareInsights and Neuro, which are the two new products, start to deliver numbers. That is sort of where it is.

**Moderator:** Thank you. The next question is from the line of Ruchi Burde from Bank of Baroda. Please go ahead.
Ruchi Burde: Anand, I wanted to ask you regarding your top client performance. If you look at revenues from top two to 10 clients, there was a sharp decline. Was it driven by a systematic offshore move or there is something else to it?

Anand Deshpande: No, I think the biggest reason why that happens is because our largest customer, the top one, has very high seasonality in some sense. So that has to do with that. Our second customer and the third customer is where we are seeing some offshore pressure as well, so some of that might come in one of those areas. But in general, the top one customer has had an impact on this one. The other thing is that we had one specific customer where we did a license agreement in the last quarter, which was a fairly large reselling agreement that came into the top 10. This was not there this quarter. So again, it is all related to the seasonality of numbers in our top one customer.

Ruchi Burde: So, would it be fair to assume that off-shoring or seasonality related issues are behind that and growth should resume in our top accounts from next quarter?

Anand Deshpande: Well, see, it is like this, our top customer, you will see odd and even quarter phenomenon in there, so you will see good growth next quarter. But you will see a dip on that particular account in the next quarter. So, you will see sort of a see-saw or up and down number on the top one customer because of the way the business is set up.

Moderator: Thank you. The next question is from the line of Deepesh Mehta from SBICAP Securities. Please go ahead.

Deepesh Mehta: Two questions. First is about the top client. Now if I look top client YoY it seems to be now showing some moderation in growth. So, do we expect now top client reach to almost peak kind of thing? Seasonality, I understand, but if I look YoY, I think it is relatively better comparison, and H1 is showing relative performance. So, if you can help us understand how one should look growth trajectory in top client. Second question is about the employee addition. We have seen around 400 additions this quarter, and it seems to be largely fresher kind of hiring. So, can you help us understand how we are building talent pool? And when we are seeing good demand opportunity, why it is not getting reflected in the lateral side. So, if you can provide how you are managing talent pool and opportunity?

Anand Deshpande: Okay. So, let’s go to first customer. See, the thing is, yes, we will see moderate growth directly on top one customer, but it will not be phenomenally great, so we have to grow faster than the first customer, that is clear. That said, we have created a partnership opportunity where, as I have mentioned to you before, we have set up a team in Europe that is selling through the top one customer’s ecosystem. And when we do that we will see new customers that come in which will not reflect as numbers as part of the top one. This is what happened in the previous quarter as well. So, we will see new deals. They will not come into the top one’s count, but they are sort of in that ecosystem. So that is how you need to look at that. And the growth rate on that would be modest. But, again, we are also aware that we do not want to go and increase, we need to get other business and reduce the risk on the top one customer as well. So that is one of the factors there.
The second question that you have regarding the hiring and the new staff. So yes, we did take 400 new fresh graduates this quarter. But if you look at the net addition, all of it is not because of fresh graduates because there is a significant attrition that you would see, and a lot of that has come in through lateral hires. We have actually significantly increased the hiring across the board in India and in the US. We have doubled our recruitment teams, and a lot of those will take sort of the offers and the mix, which mean people who have been made offers but not joined, that number is quite significant, which you will not see visibly in the number as you see the snapshot on 30th of September. But if you sort of look at the next few months, I think those numbers should start to add on. So, we are recruiting quite aggressively right now, both laterals and fresh hires.

Deepesh Mehta: So, Anand, just question was, whether the fresher was campus, because demand, if let’s say you are seeing a healthy demand, you require lateral to fulfill it now, right? And fresher will require some training time and all those things. That’s why I just want to understand your preference lateral versus fresher to cater to near-term demand.

Anand Deshpande: No, so the freshers are already in place and that is already taken care of. They will start to contribute, as you have pointed out, after four to six months, and they are in process. So, we will see some of them being deployed on projects during this quarter, and more of them will get deployed in the next quarter. So, a lot of the immediate demand has to be met by lateral hires, which are in the process. So, last quarter we did make the largest number of lateral hires, recruitments in the last quarter, which are in the pipeline in the sense they have accepted offers but not joined us yet. They take 60 to 90 days for people to join after you have made offers, so we should start to see more laterals coming in this quarter.

I am going to be brief now because I think we do have still quite a few people in the question queue, so I am trying to get through them. But I can answer any further questions you have, Dipesh, on email, but we are hiring laterals as well, yes.

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

Mohit Jain: So, first is on digital, because given our sharp deceleration in growth, and we had this background that we signed a lot of small value deals. So, the thesis was that our dependence on a few cancellations would be less. So, I just wanted your comments on how that has moved in the last two quarters, first half versus first half last year?

Sudhir Kulkarni: So, I think you are right in the expectation that some of these customers that came in through the digital channel, we would have deeper roots in them by now. And that was kind of borne out during this last quarter and the previous one as well. But as we have been talking about, there have been just specific reasons why we could not really materialize as much revenue as we would have if cancellation of some project that we talked about had not happened, and a few other things that we talked about. So, I think these are all temporary moment in time things for the last couple of quarters. I think that the change is happening the way you described, certain customers that we have entered through digital last year have
grown, and they are part of our strategic list of accounts now. And we are doing more things with them than what we were doing before, which was just some digital project.

**Mohit Jain:** Sir, any number that you can share in terms of deal pipeline, up, down YoY, what has happened there?

**Sudhir Kulkarni:** Yes, I mean the deal pipeline has gone up significantly. And I do not know that I can share specific numbers here. But I see almost 25%, 30% uptake on the pipeline. And Anand mentioned that the market is there, customers want to buy from us, there is a pipeline. It is about executing both on the sales as well as on the delivery side and supply side.

**Moderator:** Thank you. The next question is from the line of Aman Agarwal from Multi-Act. Please go ahead.

**Aman Agarwal:** So, I have been participating in the calls in the last three to four con-calls. I have noticed, yes, there have been a lot of reorg, and what we also noticed is that a lot of the large IT players have been seeing a lot of strong digital growth. And somewhere Persistent was always known to be quite strong out there. What I wanted to understand is that, firstly, I mean of course you have tried and explained where the shortcomings have been on the digital front. But what I would like to understand is that with all the changes that you have made, which are the verticals where you believe that you are satisfied with all what’s happening and which are the verticals where you believe otherwise? Because somewhere, I am just not able to connect the dots that we continue to have strong pipeline, which does not mean anything because they do not even convert. So, I just wanted some input out there for us to understand going forward.

**Sudhir Kulkarni:** So, it is not about converting the pipeline. In fact, like we mentioned before, there have been some challenges on our supply side even for projects that we have already won. And we are addressing those very aggressively, as Anand mentioned. But at the same time, continuing to build a healthy pipeline is absolutely necessary. Conversion improvements are also continuing to go on with new sales velocity initiative that we have initiated last couple of quarters. We are starting to see more qualifying leads sort of coming into the funnel as well, and we will see more ramping up of that in the next couple of quarters. So, that would be how I would look at it. I forgot what the second part of your question was.

**Anand Deshpande:** No, so let me comment on this a little bit further, Aman. So, one specifically right, so we made a lot of changes, I guess, good, bad that I think they were necessary. So, we have to make them, so we made them. That said, yes, our numbers should have been a lot better than they are right now because we have been early in this game, we have been anticipating some other changes. And some of the calls that we have made in terms of sharing what we think have been on spot, and other people have executed better than us on some of these points, no doubt about it. That said, we are seeing good activity on the health care side, for example, some of the bets we have made, and on the financial services side as well. So, both of these areas we are seeing very good growth. In terms of what we are trying to do on the Industrial side, it has been much slower than that we had anticipated, we had anticipated that we will be able to grow that part significantly. We are starting to see better reselling opportunities and good growth in terms of the numbers that will come up. But in terms of digital transformation projects in industrial
markets they been very slow to come by and the numbers have not been as good as we would have liked to see. Some of the other partnerships, again, I think the opportunities are quite significant, but we could grow a lot better in both Salesforce, Appian and some of the other partnerships that we have. We have good entry situations, but I think we need to double down much more aggressively on these partnerships because they can give much better revenues. And this is a question that Mohit also brought up. I think the conversion of small deals to large deals is again, theoretically, it is much easier to say that it should be done, but when you complete a phase one to phase two and the whole how do you manage that part, has been definitely a weakness that has contributed to slower growth on these items. So, there is a whole bunch of issues that we can see and we are measuring and tracking, and we are going to make these changes as we go along. And we have been making many changes as you would have seen. Unfortunately, it takes some time to get these changes to make results and when you measure it on a 90-day quarter-on-quarter number, some of these do not look as visible as they look inside. So, no, I just do not want to keep churning this particular point. Yes, we have not delivered where we needed to, that is the reality, but we have some analysis and we will try to see and make some changes. That is all I can say right now.

**Moderator:** Thank you. The next question is from the line of Nirav Dalal from Maybank. Please go ahead.

**Nirav Dalal:** If you could guide in terms of what would be the people intake this year? Or corollary to this is that if you could just share some details in terms of what was the order intake in the quarter or just to improve the visibility for us to work on something.

**Anand Deshpande:** See, next addition we are expecting at least, we want to get to 400, 500 additional people that we will add in the next 30 days, not 30 days, sorry, in this quarter. And we have many of these in pipeline. Okay, so we will see how that comes out. But the real revenue growth that you will see in this quarter or the next quarter is going to come from some of the IP revenues that we have in the pipeline. And as you all know, a lot of that has a Q4 effect for calendar year; and also we have reselling going on in that market. So, you will see significant numbers, which are not related to people as such. So, if you are trying to extrapolate the numbers, yes, this number will help you in identifying how the services and the TSU business looks like, but it will not give you an indication on how to resell a business. Now, if you say, "Why do not you give me numbers on that?" Well, if I knew specific numbers, I would give them to you. Unfortunately, the way this thing works, I am dependent on another partner. But from what indications I have, they say that they feel like they are looking at a strong number for the Q4. And I am quite confident that we will make that strong numbers on that part of the business. So, again, if you segment pieces and add them up, you should get a good sense on what the second half looks like. And we think it will be a lot in components, it should be better than these two quarters so.

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

**Girish Pai:** I just want to go back to that short closure of one project. And you mentioned there was a difference between client’s expectations and what you could deliver. Can you just throw a little bit more color on this? And is this a one-off or is this a structural problem that you see in your company?
Anand Deshpande: So Sudhir, you want to take that first?

Sudhir Kulkarni: Yes, sure. I do not think that it is a structural problem of any kind. I think it is just execution, and some of these things I kind of outlined in detail.

Anand Deshpande: Yes, so just to add to that, the way it happens is that there were changes on the customer side as well. There were personnel changes there and some other changes on our side that caused a disconnect in terms of what we had bid for the project versus what they thought we should be doing. And I do not think it is any, we run about 800 projects at the same time, so there will always be a few. Sometimes they are larger than what we would like to see. Sometimes when you have good growth, some of these things do not become very visible.

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

Rahul Jain: My question is more long-term in nature. I understand that we have been facing these some quarterly specific challenges. But if I have to draw a longer chart in terms of where we can go and some of this digital specific strategy where you are working on domain, any other thing or alliance or partnership and stuff? So, what do you think takes you from the current 500 odd run rate to the next level? What would drive that?

Anand Deshpande: So, I think just executing. I do not think it is a strategy problem as you would observe as such. What we are doing is some basic stuff, and I think we just have to do more selling and better delivering. I think you can easily take this to the next level by just doing that. And I just think we should just push harder, that is all. And more specifically, yes, meaning, we are looking at other partnerships. We would like to see how to get deeper on the domain side as well, and that will have to be done from strategically key acquisitions that will have to be made to get expertise on the front-end side in the customer context. And that will help in better deliveries as well.

Rahul Jain: So, you mean to say this has more to do with sustainable growth; is the reason we choose three areas versus more? Or this has more to do with accelerated growth one would see because you have more domain expertise than your peers?

Anand Deshpande: Well, some of both, right? Meaning, you do not want to be in every single area. You want to make some focused bets, and be the expert in that area, work with the people who are leaders in that market and deliver high-quality software. And that is really what we are trying to do. So, you cannot do this in every single area. So, we have picked three because we already had some connects there and we have already doubled down on them rather than try to be spread all over the place.

Moderator: Thank you. Next question is from the line of Ravi Menon from Elara Securities. Please go ahead.

Ravi Menon: Just wanted to understand what caused the billing rate decline for onsite linear business, what should probably be a good quarter with more working days? And should we expect this to come down a little further next quarter?
Anand Deshpande: Actually, the billing rate is not really recent. People read it as billing rate, but it is really yield per person, and that has to do with utilization as well. So, this quarter some of our onsite utilization was lower than what we had anticipated, and that caused the billing rate to look like it is lower. But it is not the rate, it is actually the yield per person. It is very hard for us to give an average billing rate because billing rate is very complicated to calculate on a per project basis. It’s a lot of variability there. So, what we are sharing with you is total revenue divided by total hours that have been there. And which is why you see that of the number of hours that were available goes up, then the yield looks good. The rates are not going down.

Moderator: Thank you. The next question is from the line of Raghav Kapoor from ActiveAlpha. Please go ahead.

Raghav Kapoor: I had a question on your foreign exchange gains. If you look at the numbers for first half of 2017, you gained about Rs. 387 million. But in 2018 the corresponding period is Rs. 56 million. Would you explain that, given that the currency depreciation in 2018 was much more significant than that in 2017?

Sunil Sapre: Yes, sure. So, the way this plays out is actually your hedge rate versus the spot rate. So, when you have a situation, if you look at FY17 or FY18, it had a situation where the hedge rate was much higher than the spot rate consistently throughout the year. So, any hedges that are maturing, you are booking gains. And when you are restating at the end of every quarter, you are booking mark-to-market gain on those hedges. Whereas, in this year, what has happened is in the month of April, May, in that period, the spot rate actually pierced through the hedge rate. So today we are sitting at a situation that the spot rate is higher than the hedge rate for the hedges that we have taken about a year ago. So, we have been hedging one year forward on an ongoing basis. On a rolling basis we hedge one year forward. So just to give you the perspective, today we are hedging for October 2019 at a rate of about Rs. 77, Rs. 77.25. There is a prediction HSBC has put out that by 2019 the rate will be Rs. 79. Now, if this reality plays out, that same hedge which will be otherwise in the money in October - December 2019 quarter, will be out of the money. And that is what actually happens is that in reported financials the gain flows up to EBITDA or EBIT level and gets reversed to that extent of your hedge, and that is where the foreign exchange gain is lower in this period. Whereas in the earlier year, you would have spot rate, which hasn’t gone up, and that is where it flows to EBITDA, EBIT in a moderated manner, whereas, your booked hedges where the gain comes in at the exchange gain level. That is how this needs to be read actually.

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

Shivam Gupta: Yes, just one question on the digital piece. So 800k is what you have mentioned as the impact of the foreclosure of the project. But on your base for that 10% growth you need around $2 million to $3 million to come in. So, the remaining $2 million is entirely attributed to the sales transformation we are doing?

Sudhir Kulkarni: So, there are three parts to what happened during this quarter. I mentioned about the project closure. I talked about some of the fulfilment that we couldn’t make of projects that we already had in the bag, and some of it is related to the sales transformation. So, I think there are these combinations of factors.
do not know exactly that we could quantify each one of them specifically, but those are the three things that really happened during this quarter.

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

Apurva Prasad: Anand, based on the pipeline and the deal wins that you talked about, do you think for the year FY19 you can deliver growth in the services segment? And also, the double-digit sequential growth that you talked about in digital, do you see that coming from next quarter onwards? I am actually trying to understand in terms of revenue visibility how that has moved over the last two quarters?

Anand Deshpande: Well, you have asked a loaded question at 6:00 p.m. So, let me try to reassure you that we do have a pipeline, we do have opportunities. If we can staff all work we have and we are able to get that to work out in right timing, we should be able to see that 10% quarter-on-quarter growth that we want to anticipate next quarter and the quarter after that. So, I do not see any reason why that should not happen. That is really the target that Sudhir has. And actually, we should be doing a lot more, because the whole idea is that I think we can grow at the half year too. If you already looked at last full year versus next year there is a number that he needs to make, and this is all going to be relating to that. So, yes, I think there is no shortage of opportunities, it is just a question of making sure that those opportunities get fulfilled and a lot of different things happen. So, yes, we screwed up this quarter, no doubt about it, but I think we can do better next quarter. So on this note, I think I am going to end this call because we are at the top of the hour here, and we want to complete this on time because other people will have other appointments as well.

So, I just want to close by thanking all of you for being on the call and for your patience and your support so far. I want to wish you all a very happy festive season and Diwali and for the next few weeks. And we should have another Investor Day that we are trying to schedule sometime in December, and we are trying to work out something that would be meaningful. Currently, our plan is to explore doing this in Mumbai, which would make it easier for all of you to attend. So we will meet again somewhere in December before the next quarter’s numbers. So, we should have much more details at that time.

With this, I would like to thank you all again and hand it back to Aman, please.

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 disconnect your lines.