Persistent Systems Limited Q2FY22 Earnings Conference Call

October 27, 2021

MANAGEMENT:

Dr. Anand Deshpande
Chairman and Managing Director

Mr. Sandeep Kalra
Executive Director and Chief Executive Officer

Mr. Sunil Sapre
Executive Director and Chief Financial Officer

Mr. Saurabh Dwivedi
Head, Investor Relations

Mr. Amit Atre
Company Secretary

Moderator: Ladies and gentlemen, good day and welcome to the Persistent Systems earnings conference call for the second quarter of FY22 ended September 30, 2021. We have with us today on the call Dr. Anand Deshpande - Chairman and Managing Director, Mr. Sandeep Kalra - Executive Director and Chief Executive Officer, Mr. Sunil Sapre – Executive Director and Chief Financial Officer, Mr. Saurabh Dwivedi – Head of Investor Relations and Mr. Amit Atre – Company Secretary. Please note, all participant's lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the management's opening remarks. Should you need assistance during the conference call, please raise hand from the participants tab on the screen. Please note, this conference is being recorded. I now hand the conference over to Mr. Sandeep Kalra. Thank you and over to you, Sir.

Sandeep Kalra: Good afternoon. Good morning. Good evening to all of you, depending on where you are joining. It is good to be with you once again and we hope all of you are doing well, staying safe and healthy. Before I go to the financial and business updates, I would like to thank you all, and our team members and customers for their continued trust in us. This quarter also marks the completion of one year for me as a CEO and about nine quarters as a part of Team Persistent. I am happy to report the continued progress through this time with yet another strong quarter across all major business metrics. I will begin with giving you a colour on the financial updates. The revenues for Q2 came in at US$ 182.32 million, giving us a growth rate of 9.3% quarter-on-quarter and 34% on year-on-year basis. In rupee terms, this translates into a growth of 9.9% Q-on-Q and 34.1% Y-on-Y basis respectively. This is the best Q-on-Q and Y-on-Y organic growth delivered by us as an organisation yet.

Our EBIT for Q2 came in at 13.9%. This translates into an EBIT growth of 12.5%, on sequential quarter basis and 53.8% on Y-on-Y basis.

Now, let me give you this quarter's performance from an industry segment perspective. On a sequential QoQ basis, this quarter's growth was broad-based. It was led by Healthcare Life Sciences industry vertical, which grew by 13.5% on a sequential Q-on-Q basis, followed by BFSI and Software and Hi-Tech segments, which grew by 8.6% and 8% respectively. On a Y-on-Y basis, all these three segments logged healthy growth rates with Healthcare Life Sciences going at 47.9%, Software and Hi-Tech at 31.9% and BFSI at 28.7%.

Now, coming to the order book details for the quarter, the total contract value for the quarter came in at US$ 282.5 million. The annual contract value component of Q2 is to the tune of US$ 201.1 million, in ACV terms. In terms of new bookings in the quarter, the new business TCV was US$ 149.3 million, of which the ACV component was US$ 108.8 million. As you may already be aware by now, these numbers both on TCV and ACV side include all bookings, small and large, renewals as well as new bookings across existing and new customers.

On the people front, we brought in 975 new colleagues, bringing our total employee base to 15,879 at the end of September 2021. The new addition was a healthy mix of lateral hires and fresh graduates and this should help us continue our growth in the coming quarters.

We are happy to report progress on the utilisation side, utilisation for the quarter came in at 82.8% a 2.7% improvement Q-on-Q backed by deployment of a number of our hires over the last few quarters.

Attrition for the quarter was at 23.6% compared to 16.6% in Q1 on a trailing twelve-month basis. As you would have observed, attrition has increased across the industry, given the shortage of digital skills, coupled with an overall increase in demand. This definitely is a focus area for our management team. We have taken many proactive measures with an aim to bring this under control. To give you some color on a few of the initiatives, we reverted to our normal wage cycle earlier this year in July, just about eight months after having our last pay hike, with the current quarter seeing the full impact of the hikes awarded to most of the eligible employees. We will give you more colour on the financial impact of this. Apart from this, we continue to undertake other measures including developing our own talent, both from fresher intake and lateral hiring, upscaling, helping our people with long-term career planning with active L&D, learning and development interventions. We also doubled down on enhancing engagement levels with our employees with a series of global employee events while respecting the social distancing norms, bringing back in-person employee engagement in a major way.

Another major highlight for us in the quarter, on the employee front was the launch of a broad-based employee stock option plan, covering 80% of our total employee base. This is unprecedented in the IT services industry and we are very proud of the support from our investors and our board of directors. Our employees have been foundational to the company's success and the significant shareholder returns that we have been able to deliver are on the back of contributions from each one of them. This ESOP will reward them for the resilience they have shown during the last two years and help them participate in the shareholder returns as stakeholders and partners in our growth journey over the next multiple years.

There are a few other highlights from this quarter that I would like to share with you.

First, on the acquisition side, we have been talking to you about our inorganic strategy over the past several quarters. We have been talking about how we want to go deeper in certain verticals, or in service lines, or expand in the geographies that we are focused on. I am happy to report the progress on the same with acquisitions of SCI Fusion360 and Shree Partners. We had organised an analyst call to discuss the relevant details post acquisitions, in late September and here we would just like to refresh everyone's memory on the same. SCI is a North Carolina-based company, with significant Payment domain consulting and implementation capabilities in North America, while Shree Partners is a New Jersey-based company with capabilities in cloud infrastructure and data. The acquisition of SCI deepens our client portfolio and relationships with 10 market-leading banks, with many of them categorised as among the top 20 banks in North America. The SCI acquisition will be foundational to the dedicated Payments Business Unit that we announced alongside the acquisition and the future expansion in core solutions and applications of a bank's technology architecture. With time, as we integrate SCI, we will look to see if we can do bolt-on acquisitions to further our foray into different streams in payments and associated areas.

Shree Partners consolidates our position in a strategic account and is a part of a large vendor consolidation deal we won in Q2 with one of our existing customers. Furthermore, SCI helps us extend our footprint in Charlotte, one of the largest banking hubs in the US while Shree Partners adds a new point of presence for us in the National Capital Region in India. We continue to scout for and engage with potential targets in our focus areas. We will keep you posted as we make progress on these over the next few quarters.

Now coming to the IP side of the business, we are constantly working to optimise the margins. As a part of this exercise, we have optimized one of our long-standing IP contracts with conversion to a time-and-material contract. This should help us on the margin side as we go along.

Coming to ESG, we continue to make progress on the ESG front. We are working with a leading consulting company on defining our ESG strategy and by the end of FY22 will be releasing a comprehensive report on our ESG roadmap and the status of our current initiatives against industry standard frameworks. With this, I will turn the call to our CFO, Sunil Sapre to give detailed colour on the quarterly financials and related matters. I will come back after Sunil's comments to give you more details on key client wins, analyst awards and other recognitions for the quarter. Sunil, over to you.

Sunil Sapre: Yeah. Hi, thank you Sandeep and good evening, good morning to all of you. Hope you are all keeping safe and doing fine. Let me give you some details about the financial performance for the quarter. So, the revenue as you have seen at US$ 182.32 million with a Q-on-Q growth of 9.3% and Y-on-Y growth of 34.0%. In terms of INR revenue, it is INR 13,512 million, reflecting growth of 9.9%, Q-on-Q and 34.1% Y-on-Y. On the industry verticals, as Sandeep mentioned, just to refresh those numbers, Healthcare grew by 13.5%, BFSI grew by 8.6% and Technology companies grew by 8% on quarter-on-quarter basis. In respect of linear revenue, the offshore linear revenue grew by 12.4% primarily because of volume growth of 11.8% and growth in billing rate of 0.5%. Onsite linear revenue grew by 6% comprising of volume growth of 8.9% and reduction in billing rate by 2.7%. This drop in billing rate on site is due to lower revenue from Europe, essentially due to the seasonality and increase in revenue from Mexico, which has relatively lower billing rates. The number of customers in greater than US$ 5 million categories went up by 1 from 21 to 22, and the number of customers in greater than US$ 1 to 5 million category went up from 76 to 84. So far as the acquisitions that Sandeep mentioned about, these were announced at the end of Q2. So just to clarify, this quarter does not include any revenue or costs from these acquisitions except the costs relating to the due diligence on the companies.

As you are all aware, the annual pay hike was done with effect from July, and the impact of this on the margin is 230 basis points. However, the increase in revenue coupled with improved utilisation of 2.7% helped us to absorb the impact of pay hike, and yet have some small increment to the margin. The utilisation improved from 80.1% to 82.8%. And with that, the gross margin was same at 33.5%. With the additional hiring that continued during the quarter, as you would have seen last several quarters, we have added significant number of employees to our account. We have higher recruitment costs, and that's where you will find that so far as G&A expenses are concerned, they reflect higher recruitment costs, that is the main reason for G&A expenses, increasing almost similar to revenues. In terms of the overall SG&A, the growth in revenue allowed us to absorb the overall SG&A costs, which came in at 16.9% as against 17.2% in the last quarter. The EBITDA was 16.6% compared to 16.4%. Depreciation and amortisation has been in range of 2.7% as against 2.8% in the previous quarter, and with that EBIT was 13.9% as against 13.5% in the previous quarter. The treasury income for the quarter was INR 293 million as against INR 256 million in the last quarter and the Forex gain was INR 10 million versus INR 109 million in the previous quarter. In terms of profit before tax, it was 16.1% at INR 2,176 million, dropped from 16.5% in the previous quarter essentially because of the lower forex gain. The ETR for the quarter was in the range of 25.7% as against 25.5% in the previous quarter and with that PAT for the quarter was INR 1,618 million at 12.0% of revenue as against INR 1,512 million in the previous quarter at 12.3% of revenue. Elevated employee attrition rate, along with increased cost of new hires does pose a challenge on maintaining margins, but there are several margin improvement initiatives being undertaken. We have been working on utilisation improvement, pyramid improvement. We have been in conversation with customers on increasing billing rates and customers have been amenable to the discussions and we find that they are receptive to the discussion.

We hope to see the effect of all these initiatives coming through in the coming quarters. The ESOP scheme that we have launched to cover a larger, wider section of employees will have an impact of about 70 to 80 basis points, but we believe that the positive outcome it will create from broader participation and the sense of ownership will largely offset this impact over time. The operational Capex for the quarter was INR 1,431 million, which includes payment towards new office premises in Hinjewadi, Pune of INR 915 million. We have also provided a loan of INR 1,880 million, approximately US$ 25 million to our ESOP trust for purchase of shares from the secondary market. This is to meet the obligations under the ESOP-scheme. With this, cash and current investment on books was INR 18,704 million as of 30th September as compared to

INR 19,955 million as of 30th June. The DSO came in at 55 days as against 54 days in the previous quarter and the cash generation was quite handy. Forward contracts outstanding as on 30th September was about US$ 150 million at an average rate of INR 76.74. Thank you all, I wish you a Happy Diwali in advance and back to Sandeep.

Sandeep Kalra: Thank you, Sunil. So, now let me give you a colour on the movement of our customer segments, and key client wins from this quarter. So, we saw healthy growth across our top account categories, top 1 customer grew by 8.6%, top 2 to 5 by 5.9%, top 6 to 10 by 3.1% and top 11 to 20 customers by 8.1% on a sequential quarterly basis. All of this growth, as you would have noticed is on basis of organic growth and the acquisitions as Sunil pointed out, will start contributing to the growth from this quarter onwards. Our press release for the quarterly results carries a number of our deal wins across industry segments. Just to highlight a few of these, in the Banking, Financial Services and Insurance segment, we were chosen by a leading global third-party insurance administrator to establish a Global Technology Center to deliver enterprise digital transformation. This is an existing customer, and one of the largest proactive deal wins in our recent history, including vendor consolidation as a part of the deal. The TCV of this exceeds US$ 50 million over five years. We were chosen by a US government and health savings facilitator to build an enhanced government savings platform to provide competitive advantage and accelerate revenue growth.

On the Healthcare Life Sciences, let me highlight two of the wins. The first one is with a contract research organisation to aggregate clinical data sources in Microsoft Azure-based data lake and the second win is with a leading US healthcare provider to develop a patient engagement platform using leading no-code, low-code, platform-based solution. Software, Hi-Tech and Emerging Technologies segment as well saw some good deal wins. We were chosen by a leading provider of employee engagement solutions to migrate its product from legacy platform to AWS and enhance the product roadmap. Similarly, we were chosen by a leading tax preparation and financial technology provider to transform and modernise its cloud-based product.

Now moving to the awards and recognitions for the quarter, Q2 saw us get continued recognition from industry leading analysts, firms and associations. To mention a few, Forbes Asia named us on its ‘Best under a Billion’ list, which highlights 200 Asia-Pacific public companies under a billion dollars in revenue with consistent top line and bottom line growth. This is the first time we have been included in this list and we are very proud of the recognition. For the seventh consecutive quarter, we were named a top 15 sourcing standout for managed services in Q3 2021 Global ISG index, Booming 15 category. ISG also named us as a Leader in Traditional Archetype of Outsourcing for Hybrid Cloud Deployments and Private Cloud in the Archetypal Report 2021 for ISG Provider Lens Next Generation Private/Hybrid Cloud Services and Solutions.

In summary, we delivered yet another strong quarter, we continue to see good traction for our services in the markets we serve and we remain confident of our growth journey going ahead. With this, I would like to conclude the prepared comments and would like to request the operator to open the floor for questions and answers. Operator, over to you.

Moderator: Thank you very much, sir. We will now begin the question and answer session. Anyone who wishes to ask a question may raise your hand from the participants tab on your screen. Participants are requested to use headphone or earphone while asking a question. Ladies and gentlemen, we will wait for a moment while the question queue assembles. First question is from Mr. Mohit Jain.

Mohit Jain: Yes, sir, first of all on account of onsite billing rates, while you mentioned in the opening remark that it is probably on account of Mexico. But what I wanted to check was if you look at last four or five quarters, onsite billing rate is more or less steady, some quarters it is up, some quarters it is down. So, how should we read it like clients are really willing to give you a higher rate and we should expect it to trend up over the next three, four quarters or do you think it will more or less remain stable with some delivery moving to Mexico was the basic strategy included in it?

Sandeep Kalra: Sunil, you want to go ahead?

Sunil Sapre: Yeah, I'll give my perspective on that and you can add. You know, Mohit, what is happening in this situation is that we are also as we have talked earlier looking at this near-shore delivery. So, so far as onsite billing rates are concerned, earlier they used to be only concentrated in US as our footprint in Europe has been small, but over a period of time, we have been working on Europe business. So now you can say US, Europe is the more critical mass of that onsite footprint. Now, over the last few quarters say three or four quarters, we have been working on adding Mexico, Canada as the near-shore delivery and few other pockets where we already have footprint like Malaysia and so on. So, I would not read too much into this, we will only ensure that there is not too much of volatility and this time the main reason for this as you know, the Europe business contribution has been slightly lower and the main reason for that being the vacation period in Europe and post-COVID there has been a bit of opening you know globally and this is a time when people have been able to take vacations after longer periods. So, we have lost certain billing days over there because of which the Europe billing rates being higher, it has put further pressure on the onsite billing rates as a number that you see going down.

Sandeep Kalra: With the time and at an Uber level, if you look at it, there is no pressure on the US billing rates downwards or Mexico billing rates downwards etc. The mix is changing and as we go ahead as the US travel opens up next month and similarly the other regions like Canada, Mexico, etc. open up. We do have plans to go bigger in terms of our presence in Canada, in US, in Mexico, and we are seeing a good receptiveness for near-shore Canada and Mexico from our US customers; perspective. So, you will see those numbers go up over a period of time in terms of volume, in terms of value as I said before, the mix may change. So, your average dollar value may change, but there is no negative pricing pressure on that.

Mohit Jain: Sir, second was on the TCV where there's reported, you mentioned US$ 50 million deal is probably included in the TCV reported for the quarter, but there are also some companies reporting higher ACV and lower TCV type of scenario. So, are you also observing such a trend where larger deals are drying up and smaller deals are sort of picking up?

Sandeep Kalra: Look, the nature of business for us versus some of our bigger peers may be slightly different. If we were to you know be in the infrastructure business or application support business, the number of deals in three to five years is much higher. The kind of business that we do, it is more digital in nature and where the number of those deals are lesser and the deals may happen in the one to three years period, more three to five years maybe lesser and then they may get renewed with different scope and so on so forth. So, we are seeing a very healthy demand, demand-wise we are not worried but TCV may be slightly different for us given the nature of our business.

Mohit Jain: So, in our case TCV reflects or it is a fair representation of revenue growth ahead?

Sandeep Kalra: Yeah, it is. And we are confident, if you look at it, if we were in the project business, we have now delivered I think six plus quarters of sequential healthy growth that if it was project-based it would wobble so we are fairly confident what we are doing is a longer-term play, and it's a good mix of short to medium to longer-term deals. So, we are happy with the deal profile.

Mohit Jain: Perfect Sir. Thank you and all the best.

Sandeep Kalra: Thank you.

Moderator: Thank you. Next question is from Mr. Sandeep Shah.

Sandeep Shah: Yeah, can you hear me?

Moderator: Yes.

Sandeep Shah: Yeah, congrats on a stellar performance quarter after quarter. Sandeep, just wanted to understand in this demand scenario, which is high, also as a benefit of some bit of the pent-up demand. So, do you believe that your TCV wins, which is consistent now between US$ 250-US $300 million a quarter can continue even beyond FY22 where we may see some amount of normalisation of IT spend or you don't believe in this trend of pent-up demand been there? It's largely a transformation demand, which is driving the growth across sector.

Sandeep Kalra: So, Sandeep, good question. So, let's go a little deeper into this. The segments we play in you know, on one side, we have the enterprise side, whether it is Healthcare, Life Sciences, whether it's Banking, Financial Services, so, there are those enterprise transformation programs, and a number of those are long-range programs. On the other side, we are also significantly playing in the product development side, where we are playing in the ISV/Tech company ecosystem. Now, a number of those are also impacted by people like private equity players, if you look at the dry powder, the committed money to private equity, which is not yet put to use is at an all-time high right now. Similarly, the VC funding is you know, the amount of money available is at an all-time high right now, a number of that will be called over the next two to three years if not more. So, what we are seeing is a structural demand, whether it is enterprise, whether it is product companies that you know, provide the tools for the enterprise transformation. So, as far as we are concerned for the segments we service whether industry segments or the technology segments, we believe this is a multi-year segment, multi-year play, and they should continue for the next at least two to three years, if not more. So, from a demand perspective, we are confident that this demand is here to last for the next 20 years.

Sandeep Shah: Okay, great. And second, just in terms of the restructuring, which you said in your opening remarks related to IP, will it be effective starting from 3Q or it may be slightly ahead of that and one can assume this will have a positive impact in the gross margin and when you say converted to time and material, is it fair to say from an IT classification, it may be classified now as a services business?

Sandeep Kalra: Yes. So, the answer to most of what you said is yes. So, the timing is basically from 4Q for us, first calendar quarter of next year. And as far as we are concerned, now, it will move from IP bucket to time-and-material, the revenue may be slightly lesser, but the gross margins may be much better. So, that is the overall impact there and it should be positive in the medium to longer term, both revenue and, you know, the gross margins because we have enough demand to be able to redeploy any people that may be impacted or whatever else.

Sandeep Shah: Okay. And just the last question, to Sunil Sir, so, if you look at the headwinds, this, starting from Q3-Q4, we may have the inorganic pressure on the margins plus additional ESOP cost, but you still believe there are tailwinds. So, is it fair to say Q2 margins can be maintained on a going forward basis and 2Q, is there any non-recurring expense or any non-recurring reversals in the P&L?

Sunil Sapre: Yeah, Sandeep, so, there is no one off in Q2 except, you know, for the small M&A-related expense, but that's very small amount in terms of the overall transaction that we have. The headwinds and levers that we are working on, the whole idea is to ensure that we are able to attract best talent, right, engage with them as you know, so far as attrition is concerned, it is not just one time pay hike that impacts the P&L, it is also the replenishment cost which comes in at higher costs because of the situation we have in the industry. So, as a company and all our peers, you would find I've been working on balancing this with significant addition of freshers to the system. This about a year ago nobody would have thought, demand scenario is going to be so good and people could have actually onboarded much more freshers earlier but that didn't happen. So, as an industry kind of a situation when more freshers get deployed, I'm sure over the next say, two-three quarters which is a time that is required to make those people you know, you can deploy them on projects. This should help, but one or two quarters more stress will be there and that's the time when we have to put all the levers to use to ensure that at least margins don't go south, right, the improvement in margin will take a little while to come because of this scenario we are in. And we are also growing very fast. So, we do need to carry the capacity for growth. While we have worked on the utilisation from 80.1%, to 82.8%, we feel that 83-84% in near-term is what we would target, not something at much higher level because of the growth that we are looking for. I hope that answers.

Sandeep Shah: So, directionally, we can maintain the margins at Q2 level?

Sandeep Kalra: Yeah, so directionally, we will say, we will be in the 16% to 17% band, that is our attempt, while you know continuing to grow very well. So that is the band you should expect, and growth is our focus.

Sandeep Shah: Okay, thanks and all the best.

Sandeep Kalra: Thank you so much.

Sunil Sapre: Thank you.

Moderator: Thank you. Next question is from Mr. Nitin Padmanabhan.

Nitin Padmanabhan: Yeah, Hi, good evening, everyone. Great quarter. Couple of quick questions. One is, I think there was an impairment of INR 74 million, and we saw a similar kind of number last quarter as well. Is this likely to continue in the next quarter or this, we have already had two quarters so is it likely to end? The second question was on the IP business. So obviously, there are a lot of end-of-life products in there. Do you think this will be over the years it'll be a gradual sort of decline there or do you think that there is scope for step drops, if you think take a longer-term view on that? And in relation to that, I think we have seen the effort in the IP business sort of improve over the last two quarters, after multiple quarter of declines that we have had. So how should we actually think about it? And finally, on the new ESOP plan, how are you actually thinking about this one, philosophically, is it over and above, is it part of potential salary increases that you're thinking about as total comp or this is over and above in terms of philosophically sort of sharing wealth? And is there any impact in the current quarter? And do you see further impact going forward? Thanks.

Sandeep Kalra: Sunil, if you can talk about the impairment, I'll take the rest.

Sunil Sapre: Yeah, sure Sandeep. So, Nitin, this impairment is kind of done with now, there is no further impact that you need to expect.

Sandeep Kalra: Right, on the other side to IP business, I think it will be stable to you know, maybe a slight growth for some time and then maybe decline over the long run. So, whatever decline had to happen in a bigger way, I think it is behind us, we have you know, seen stability in that and we are also repurposing the IP through derivatives etc. and so on. So, we are relatively confident with the flat marginal increase in the shorter run, decline gradually in the long run. So, no worries on that. As far as the ESOP plan is concerned, look, here's what has happened and why we did the ESOP. So, we have grown very well over the last six, seven quarters as all of you who follow us very closely, would have observed. Now, with that, we have seen a significant amount of shareholder value creation that has happened. Now, our employees who are the people behind the shareholder value creation, in all our employee townhalls have been requesting participation in this and it is only fair that we take them along as we create value for our stakeholders because of the efforts of all our employees. So, that is where we took our investors' approval, we took our board of directors' approval, and we did this, you know, fairly encompassing 80% of our employees are covered or will get covered in the next few months as they get eligible under this ESOP.

So, this is to make sure, we are basically creating an environment in which we are sharing wealth that our employees create for our stakeholders with them. It also helps us on the other side, make our employee value proposition much stronger. So far, Persistent employee value proposition has been good brand, good work culture, good employee orientation, good content of work. So, if you want to work on the latest technology in a very friendly environment, which is very employee friendly, come to Persistent, and we are the, you know, best tech services company from a niche service provider perspective. Now, with this, it is not basically this, that it is a part of our core compensation. So, core compensation will still remain very competitive. All the other things that I talked about will remain there and this ESOP plan will be a small, thank you wealth generation, for the effort that they do and they help us create wealth for our shareholders. So overall, we believe they should also help us in retention over a period of time, manage, you know, attrition over a period of time, and so it will be beneficial for our employees, our investors, our customers and nine yards of our stakeholders. So, that was the philosophy behind the entire ESOP, and we are pretty sure in the shorter run, it may cost us a bit. But in the medium to longer term, it'd be value accretive for our investors. So, that is the story behind the ESOP, that we have.

Nitin Padmanabhan: Great, helpful. This one sort of clarification to Sunil sir, over the last two quarters, our stock-comp has been roughly 1.4% of revenues. Do you think as this kicks in, we'll replace some of that to a certain degree, and that number should have come off? That's the last from my side. Thank you.

Sunil Sapre: You're right. Actually, the stock-comp expense would stay in that range of 1.5%.

Nitin Padmanabhan: Great, thank you so much, and all the very best.

Sunil Sapre: Sure.

Sandeep Kalra: Thank you.

Moderator: Thank you. Next question is from Mr. Manik Taneja.

Manik Taneja: Hi, thank you for the opportunity. Sandeep, you made a statement about the restructuring of large IP contract into T&M billing going forward, if you could elaborate on that front, and how that helps in terms of profitability improvement? That's question number one. The second was a much broader question which is true, not just for Persistent, but for broad industry as well while over the last 18 months, we've seen a significant rise in offshore delivery of revenues. And typically, what one used to see was that as offshore proportion of business used to increase, our utilisation rates used to essentially moderate. But in the current environment, what one has seen is that the utilisation has continued to record new highs. So, what's driving that, is this the underlying demand momentum because of which utilisation continues to be very sticky and high? That's, that's the second part of the question. And also, are you seeing customers looking at more innovative engagement models as they get used to greater work being delivered offshore? Thank you.

Sandeep Kalra: Okay, I'll try and keep this brief, because we have 25 minutes left. So, on the IP side, look, here is where it is we, one of the largest contracts that we had, you know, it was basically to be renewed in five years. So, and since we had seen depressed margins that we requested, understanding from our customer, we have converted that to a T&M, what that means is, it'll become a services contract rather than a revenue share contract. And in a revenue share, contract, our margins were getting depressed, because the revenue on that product was not necessarily growing that heavily. Now, in terms of the revenue impact, and so on, without going into too many details, it will basically take our revenue down to maybe about 40-45%, of what it was. And at the same time, the margins will become equal to the company gross margins for whatever business it is. So, on a margin perspective, it will definitely be more accretive. On the growth perspective, the revenue profile, we don't expect an impact on this.

Because today, honestly, we are hurting on the people side, if we had 1,000 more people today, and anyone who's listening to this call and wants to be an acqui-hire, we are happy to do that. So, any people that come off of this contract, we can easily redeploy them without missing a heartbeat. So, from a revenue perspective, not going to impact, margin perspective, going to be accretive. So, it's good for us, good for the customer, good for our employees. So, from that perspective, that is the story on the IP contract restructuring. Now, you talked about the offshore utilisation, look, we have been traditionally in the range of 78 to 80% offshore utilisation, we have cranked up the lever a little bit higher, because obviously, we are also in the same industry facing the same headwinds, where we have issues, whether it is attrition, whether it is salary increases, etc. and a lot of our investors and people like you want us to maintain a healthy margin profile. So, in order to make sure that we are doing that, prudently, we have cranked the engine, we had hired a number of people, roughly, we have hired 5,000 people over the last four quarters.

So, we have taken the utilisation a little higher as we have been able to train and deploy the people, we are not cranking the utilisation to the levels of 88-89% that some of our biggest peers are doing. We are happy as Sunil said, maybe doing another percentage or two at max and we will be in this range so that we are able to bring in the kind of technical people that we need as additional team members as we go along with time and have a healthy pipeline to back up the growth that we intend to. So, that's the thing on off-shore utilisation.

On the customers' innovative engagement models, look, there are definitely discussions that happen with customers on different models, whether it is fixed bid programs, whether it is taking over support for many years in different business models, but again, one has to be prudent in doing those business models as we have seen some of these IP contracts can be, or revenue sharing contracts and innovative business models can be tricky. So, where it makes prudent sense, we will definitely engage and we are seeing those discussions. So, I will stop with that and happy to answer any questions you know, offline on this.

Manik Taneja: Thank you for those inputs. Thank you, and all the best for the future.

Sandeep Kalra: Thank you.

Moderator: Thank you. Next question is from Mr. Rahul Paliwal.

Rahul Paliwal: Congratulations to the management, first of all, for taking this industry-leading initiative to share the wealth with the most important stakeholders, which is their employees, I'm sure it will have a boomerang impact in terms of profitability and stickiness to the organisation. So, congrats to Anand and then the team and Sandeep to you. So, my question is, around when I compare with the peers, the margin front, we are lagging almost since 2015. Why this is the gap since so long, and when the demand scenario is such high, how soon we can catch up with the peers? That's the question, sir.

Sandeep Kalra: So, look on the margin front, yes, when you compare us with the bigger peers, there's a delta. But if you were to compare with our competitors, who's the competitor for Persistent, let's look at it, we are competing with the EPAM, Globant, Endava and the likes. So, if you look at that profile of companies that we compete with, and then maybe in some places, we compete with niche providers, some places we may compete with the larger tier-1s. Now, if that is the competition, if you look at our margins versus that set of cohorts, we are pretty much in-line, if you were to study any of these competitors. Now, do we desire to go up from here? Absolutely. Our answer to you would be give us next six to eight quarters, as we build the company to scale, there is a number of things that will not proportionately scale from a cost perspective, there'll be bigger leverage of SG&A, there will be bigger leverage of many other fixed costs or the proportion in which they will increase will not necessarily be in the proportion that our revenue will increase. And with that our aspirations definitely are over the next 6, 8, 10 quarters to go up by 100-150 basis points on the margins but it'll take us time to go there. So, definitely we have the eyes on the ball. Growth comes first, with the growth, margin will kind of follow. So, have some patience, we'll get there sooner or later.

Moderator: Thank you. Next question is from Mr. Dipesh Mehta.

Dipesh Mehta: Thanks for the opportunity. Couple of questions. First of all, the margin, earlier, I think, Sunil made a comment about 16 to 17%, EBITDA margin which I just want to get sense about it is after considering both the kind of retention related, amortisation plus ESOP, and on EBIT there will be only incremental impact what it is how, right from margin perspective for next couple of quarters. The second question is about overall hiring and related things. How is the fresher intake plan for the next few quarters if you can share some number about, how we look at fresher intake and whether it can be a margin lever for FY23, considering pyramid rationalisation is limited.

Sunil Sapre: Yeah, Dipesh. So, in terms of your question, I'll answer in two parts. One is with respect to the immediate near future and then as we go along in the next financial year. So, if you see the acquisitions that we have announced, when we had announced the acquisitions, we had mentioned about the fact that both the acquisitions are actually accretive at gross margin level. And so far as the retention payouts and the money that gets amortised, that we'll have, you can say some impact happening at the EBITDA and EBIT level.

But overall, this will not have a huge impact. I would say in the next two quarters, it could have an impact of 30 to 40 basis points which we have to manage on various other levers. Over the longer term, yes, we have to work on these acquisitions, integrate them well, create synergy revenues and do a whole lot of those things to ensure that this is really not a worry for us to manage the amortisation charge, which comes out of intangibles. And in terms of the ESOP thing, it will happen as we go along. I don't think as I mentioned earlier, the overall expense will not be much different percentage to revenue, it will remain in that 1.5%, kind of that.

Sandeep Kalra: On the fresher intake, we will target somewhere between 2,500 to 3,000 freshers over the next one year. So, if I look one year from now that is the number that we are looking at and obviously we have to execute on that and then train and deploy.

Moderator: Thank you. Next question is from Mr. Hardik Sangani. Hardik, please unmute and ask your question. Okay. Next question is from Mr. Nagendra Moriya.

Nagendra Moriya: So, good evening, and congratulation on great quarter. I have a small question regarding the employee costs. If you see there was a hike in salary in July itself. And if you see the ratio of the cost to revenue is more or less similar about 60% kind of ratio. So, do you think from the next upcoming quarter, with the normalisation of attrition, the revenue, with this cost ratio about 60% would go up or it will be remained in the same level? That is one question. And second thing, second question on the revenue goal or the new vision you shared about US$ 1 billion goal or target. What is the timeline of this revenue goal and what additional things is company doing to achieve this goal? Thank you.

Sandeep Kalra: Sunil, if you can take the first, I'll take the second.

Sunil Sapre: Yeah, sure Sandeep. So, what you mentioned about the employee cost as percentage to revenue that's a very important direct costs that all of us always, I want to ensure that we are optimising to the best extent impossible. So, as you would have seen over the last several quarters, like Sandeep talked about we added significant number of employees and when we add such a significant growth from ten and a half thousand to fifteen thousand eight hundred today, along with managing the attrition part of it, there is a significant investment that we have done to build the learning and development and the deployment kind of a framework to ensure that we get the best talent available to our customers. Having said that, the percentage of cost to revenue is a dynamic, you can say mix of three things. One is the onsite-offshore ratio of the business, the second is the utilisation and third is within the utilisation, whether you are able to have a fair mix of lateral versus freshers. So, directionally, yes, the whole idea about improving overall EBITDA margin in the earlier question that we talked about comes out of improvement in gross margin, and also improvement by spreading the SG&A over a wider revenue base. So, it is hard to predict these things because attrition is something that is evolving and how much attrition gives additional costs for the same capacity to be replenished, is a factor that is not in our control. But you can be rest assured that all of us are working very closely to ensure that this is optimised to the best extent.

Sandeep Kalra: So, on the billion-dollar plan, our eyes are absolutely set on that it is line of sight for us. And if you look at it at US$ 182.3 million, that gives us a run rate of roughly about US$ 730 million. Over the past five to six quarters, we have been going 6%-plus in CQGR terms. And if we look at it, next six to eight quarters is where our ambition would be to hit the billion-dollar mark. Now, this would come from mostly organic growth, there will be some inorganic part to it. Like we announced the acquisition of SCI and Shree Partners. We are looking at multiple different acquisitions as well, but these are more capability acquisitions, whether it is in the cloud space or security or data or Salesforce, and we are confident of the combination of organic initiatives, the larger deals that we have been doing going deeper into service lines, going deeper into partnerships etc. and number of these things are panning out well for us as you would have seen over the last, you know sequential quarters that we have. So, we are reasonably confident next six to eight quarters, we should be able to reach our vision and then obviously it is an evolving vision when we are at one, we will target three, we are at three, maybe we will target five or ten. So, it's an evolving thing and we are confident of delivering it.

Nagendra Moriya: Thank you for the answer. Just one quick question on the travel cost side, it was in the likelihood 2-3% of the revenue earlier, but current COVID time has gone down. So, how do you see in the upcoming quarter travel costs will pick up?

Sunil Sapre: See, the travel has started opening up it is already some small amount of 10-15 basis points impact has already happened in Q2. We expect that trend to be like that. So, if you take about two to three quarters from now, if nothing materially changes, then it will have an incremental impact of about 15, 20, 25 basis points per quarter, it may move in that range but today it is little hard to predict, but you're right over a period of next three, four quarters, we should be seeing travel coming to about two thirds of where it used to be.

Nagendra Moriya: Okay, thank you for the answer.

Moderator: Thank you. Next question is from Abhishek Shindadkar.

Abhishek Shindadkar: Hi. Thanks for the opportunity and congrats on a solid execution. Couple of questions. The first thing is conversion of that IP contract into time and material would that end the seasonality that we have generally in Q3, I am sure you said it will happen from next year. So, we'll have this seasonality probably in this time. The second is more on the mix of geography, you know, India is almost now at a higher mix then Europe. So, what is driving this business and what is probably not working in Europe, if you can just elaborate that, that could be helpful and just a follow up to that is India Business historically, the hypothesis is the DSOs are a little higher, anything that we should be aware of from a DSO stand-point, thank you for taking my questions.

Sandeep Kalra: Sure. So, let me try and answer that. So, the conversion of the IP contract to T&M the seasonality look, the seasonality-wise October, November, December quarter is the highest in that particular contract or overall IP business and January, February, March which happens to be Q4 is the lower side. So, every alternate quarter is the pattern that we see. So, from that perspective, this quarter, it is continuing the way it is in October, November, December, the restructuring is effective in January. So, from that perspective, you should look to not have the major ups and downs beyond that. And we had more or less as a company if you look at it last Q4, we had overcome that any which ways. So, that should answer your question on seasonality. And it is all positive for us. The other side of it the India Business being higher mix than Europe. So, in India, what has happened for us is this, our capabilities on certain service lines, including Salesforce, our engagement with financial services customers, that's what is driving the revenue and it's a healthy revenue that we are seeing in the BFSI segment that I talked about.

And again, some of the other customers, which are multinationals, their Indian arms and so on. So, that is the positive side of it. Now, DSOs I don't think it is impacting us. If you look at it, our DSO, we have been able to thankfully manage it because of our team's efforts very well. I think we are at a very healthy clip in terms of DSOs, they are at 55 if we were to not look at the unbilled part and even with unbilled part its fairly healthy. Now, what is not working in Europe, I would not say what is not working in Europe, the last quarter, as Sunil pointed out, it was impacted because of vacations etc. Otherwise, we would have seen a lot of good growth there as well. Now, can we do better in Europe? That is the question. I will not say what is not working, I would say how do we work better in Europe and we have stated very clearly as we look to our billion-dollar goal, we want it to be 12 to 15% instead of the 8.5 to 10%. So, in that we see and we are at it both organically and inorganically, the team is focused and over a period of next several quarters, we hope to have that situation change in a positive manner and we'll keep reporting on that. So, that is the thing about Europe.

Abhishek Shindadkar: Perfect. Thank you for taking my questions.

Sandeep Kalra: Thanks Abhishek.

Moderator: Thank you. Next question is from Madhu Babu.

Madhu Babu: Yeah. Hi sir. Sir, at least the perceived premium of the sector has increased in the last two years, the perceived importance. So, what is stopping us on the price hikes? I mean, because even the inflation has been substantial for us, even not this sector, across other industries also input costs are increasing even in other sectors as well. So, what is stopping on the price hikes, when you're you know, all-time, high demand as well as most, the perceived importance is reached a new high for IT Services. Thanks.

Sandeep Kalra: So, Madhu Babu, the, there's nothing stopping us from pricing hikes. See, it is like this, the customers today understand, they're very empathetic, but in the customers' organisation is an organisation called procurement whose job is to make sure that they are controlling the costs and nobody likes to pay more, even though they may be empathetic to you, nobody likes to pay more and you know, these things have to be done when the contracts are up for renewal. So, one is the sequencing issue, you just can't go arbitrarily and ask for pricing increases, customers, some customers will not like it, some customers may still work with you. So, we are as we have the contracts coming up for renewal, we are working with them. And we are hopeful of as you rightly said, demand is high. Whatever issues we are facing in India is global issues. I don't think it is relegated only to India only to services companies. So, I'm pretty hopeful as we go along, this will happen and we are seeing pricing related positivity in newer contracts and even in renewals. So, it may take a little bit of time, but it will you know, happen it will happen in the right direction.

Moderator: Thank you. We will take one question per participant as we have less minutes in hand now. Next question is from Girish Pai.

Girish Pai: Yeah, Sandeep, I had a question on the margin guidance in the media interview you gave in the morning, you kind of meant said that you're looking at 100 basis point improvement in margins over the next two to three years, it seemed fairly conservative to me, because sitting 12 months back, you were saying that EBIT margins would be in that 12.5% kind of region and today, you're sitting at 13.9%. So, are you being ultra conservative on the margin front? You see, could this be going up significantly, as you see serious traction in your revenues?

Sandeep Kalra: So, there are two things. Number one, look, we are building the company for the longer run, we are hunkered down, if we can do the margin improvement next quarter, rest assured, we will do it. But the point is, if you ask us for a forward-looking guidance, we have to give you a guidance that is practically doable, while we will give it our effort to do it in the shorter term. So, the fact that, we said whatever we said on the EBIT, and we are delivering much better than that should give you, the confidence that we are focused on growth, we are focused on operational improvement our profitability has so far if you look at the operational improvement, it has outpaced our revenue improvement that we have done. So, rest assured, if we can do it better, faster, we will do it. But from a guidance perspective, look, we don't want to guide something that we can't live up. So, we are at it, if we can do it faster. Despite the challenges that are there in the industry, we will do it. There's nothing stopping us from doing it but if you ask us to commit to something, it will take us that much more of time.

Girish Pai: Okay, Sandeep, just one question more, if I can squeeze it in. And what I see is two sets of tier two companies like yours, which are giving a TCV number and there is a growth coming through and there are companies, which are not giving a TCV number but showing very strong growth. So, I'm just trying to understand the nature of business coming your way. Are these like really, really small contracts which do not appear in the TCV, which are strung together, so to speak and therefore, you see this growth in those companies where the TCV numbers not being given, what are you seeing on the ground? Why are those companies not giving those TCV numbers?

Sandeep Kalra: Look, I don't control those companies so, I can't say why they give, they don't give. We try to give you as much transparency into our system as we can and it's practically possible and as far as we are concerned, our contracts are with reasonable size companies, with the companies that we want to work with the contracts are increasing in size. So, we are happy with the kind of contracts that we have and the proof of the pudding is nobody can grow sequentially for six quarters, if you're doing shorter contracts, and they finish and then you are digging newer ways to find, newer sources of revenue. So, there are some, which are shorter term, some medium term, some long-term contracts, a healthy mix of all of this and that's where we have been able to sequentially give that growth that we have. And if you look at year-on-year growth, 34% growth doesn't come on back of smaller contracts. It definitely needs a lot of good work to be done to get sequentially from last quarter was 27%, this quarter is 34%. So, we are happy with the kind of contracts we have made good progress, if we can keep on this progress, I think as a company and as a team will be very happy for this.

Girish Pai: Thank you very much.

Moderator: Thank you. Next question is from Ruchi Burde.

Ruchi Burde: Congratulations on excellent execution. My question is on pricing again. In the prepared remarks, Sunil mentioned that clients today are more receptive for pricing discussions. So, are these conversations of equal ease for fixed pay contract and T&M engagement? And if not, is it fair to imply that the margin pressure is relatively more in the fixed pay engagement versus T&M?

Sandeep Kalra: So, so I'll keep it short. We have one-minute left in the call. So, look, a significant amount of our work is on the T&M side and customers are willing to look at that. As far as the fixed pay is concerned, it's more of the IP business and that's any which ways we control…

Ruchi Burde: My question is specifically for IT services.

Sandeep Kalra: Yeah. So, for IT services, if you look at it, we have a fairly healthy margin on IT except for a few contracts, which we have basically said we are optimising, so, no concerns there. The margins, there are more than the company average. So, moderator I think let me get to the final comments, and then we will close the call because we are at the end of the call. So, we sincerely appreciate all of you taking time and joining us for the call today. We would like to thank our 15,500-plus team members, customers, partners and investors for their support in our growth journey. We are bullish about our prospects for the future. We look forward to connecting back with you in the next three months to provide an update on our ongoing progress and we wish you all good health and Very Happy Diwali and Season's Greetings. Thank you, moderator, you may close the call.

Moderator: Thank you very much to the Persistent Management. Ladies and gentlemen, on behalf of Persistent System Limited, that concludes today's conference. Thank you for joining us and you may now disconnect your lines and exit the webinar.

Sandeep Kalra: Thank you.

Sunil Sapre: Thank you.

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