

“Zensar Technologies Limited Q3 FY-20 Earnings Conference Call”

January 24, 2020



Management: Mr. Sandeep Kishore - Managing Director & Chief Executive Officer
Mr. Ajay Bhandari - Head-Strategy & Corporate Development
Mr. Navneet Khandelwal - Chief Financial Officer
Mr. Vivek Ranjan - Chief Human Resources Officer
Mrs. Prameela Kalive - Chief Operating Officer
Mr. Harjott Atrii - Global Head-Cloud Infrastructure Business

Moderator: Mr. Mukul Garg - Haitong Securities Limited

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Moderator: Ladies and gentlemen, good day and welcome to the Q3 FY20 Earnings Conference Call of Zensar Technologies Limited hosted by Haitong Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing ‘*’ then ‘0’ on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Mukul Garg from Haitong Securities. Thank you and over to you.

Mukul Garg: Thanks everyone for being with us on the call today. On behalf of Haitong Securities I welcome you all to Zensar Technologies' 3Q FY20 earnings call. We have with us the senior management team of Zensar: Mr. Sandeep Kishore - MD & CEO; Mr. Navneet Khandelwal - CFO and other members of the management team.

I will now handover the call to Sandeep to start the proceedings. Thank you and over to you, Sandeep.

Sandeep Kishore: Hello and Good Afternoon everyone. Thank you for joining us today to discuss Zensar's financial results for the Third Quarter of Fiscal 20.

On the call, I have with me from the Zensar Management team – Ajay Bhandari, Head of Strategy and Corporate Development; Navneet Khandelwal, our Chief Financial Officer, Vivek Ranjan – our CHRO, Prameela Kalive, our COO and Harjott Atrii, Global Head of Cloud and Infrastructure Services Business

I will give you a brief overview on Q3 FY20 which will then be followed by an update on other financial metrics from Navneet. Post which we will open the call for questions.

I trust that all of you have had the chance to go through the detailed Q3 FY 20 financial results and fact sheet that we released yesterday. Let me take this opportunity to present some key pointers:

For Q3FY20 we reported revenue of USD 143.3m. This represented YoY \$ growth of 1.1% and a QoQ decline of 5.9%. The sequential revenue decline in Q3 was primarily on account of certain one-time and seasonal items. These one time or seasonal items include furloughs of USD -4M, specific year end discounts USD -1.5M for two of our top 20 clients, and ramp downs in retail USD -5M. Other verticals, especially Cloud and Infrastructure Services and Financial Services continue to show good revenue increase of USD 2.3M positive growth.

Our order booking was strong at USD 170M of TCV. We also have a strong pipeline of more than USD 1B, with a number of deals in final stages of closing.

By end of this fiscal, we expect growth to normalize and the business metrics to return to Q1FY20 levels. Our endeavor is to deliver industry level growth and margins in the coming quarters.

The digital revenues increased sequentially 1.6% QoQ and 20.2% YoY, the legacy business declined by 13.4% QoQ. Almost all the revenue de-growth is in legacy business.

The de-growth in revenue translated into a corresponding margin impact as well.

Reported EBITDA for the quarter was 6.8%, however after adjusting for the one time and seasonal items, Normalized EBIDTA was 11.2%. The 280bps drop from Q2 EBIDTA to normalized EBIDTA is explained by lower utilization of 210bps and higher G&A of 70bps.

We have been working on cost rationalization initiatives and better operating tracks to improve margins. We do expect to get to our target EBITDA of 15% over the coming quarters.

Q3 witnessed strong cash collections of \$33m on account of better receivables management (DSOs down from 102 days to 93 days). We will continue to focus on improving our free cash conversion and ROCEs metrics.

Our Cloud and Infrastructure business continues to see very good momentum with our clients. Apart from signing new deals, we have also grown CIS business in the existing accounts thru better mining. We have added 4 net new logos in FY20 in the last 3 quarters on the back of our Differentiated solution-centric CIS ecosystem with Digital Foundation Services. Both our next gen CIS business and our core CIS business registered growth of 5.4% and 19.6% QoQ respectively.

Relationship with our key and growth-oriented clients continues to remain strong and we continue to drive growth through digital and technology transformation maintaining Zensar's core values of customer centricity and continuous innovation and excellence. We have put focused efforts to scale up strategically into our top-tier high growth accounts and invest more in our spectrum of services in Applications, Digital and Cloud Infrastructure. Account mining focus has added 1 new client each in the 5M+ and the 10M+ category QoQ. As of Q3 FY20, we have 92 1M+ clients, 24 5M+ clients and 10 10M+ clients. 5+M and 10+M accounts have increased by 4 and 3 respectively on a YoY basis.

In terms of innovation and intellectual property, our total patents filings now have crossed the 100 mark, and now stands at 101 count with 11 patents having been granted.

Zensar continued to get included across key industry analyst and advisor reports this quarter for our capabilities:

- Mentioned as a Challenger in the Avasant Blockchain RadarView™
- Innovator in Avasant's Hybrid Enterprise Cloud Services RadarView™ 2019
- Featured in Digital Workplace of the Future - ISG Provider Lens™ Study 2019
- Mentioned in the Competitive Landscape: Robotic Process Automation Service Providers 2019

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- Mentioned as disruptor in Avasant Intelligent Automation Services Radarview Report 2019
- Mentioned as Major Contender in Application Transformation Services PEAK Matrix™ Assessment 2020.
- Mentioned as an Aspirant in “Application and Digital Services in Banking –Services PEAK Matrix™ Assessment 2020
- Mentioned as an Aspirant in Blockchain Services PEAK Matrix™ Assessment 2020.
- Mentioned as an Aspirant in Advanced Analytics and Insights PEAK Matrix™ Assessment 2020
- Mentioned as an Aspirant in Cloud Enterprise Resource Planning (ERP) – PEAK Matrix™ Assessment 2020
- Mentioned as an Aspirant Talent Readiness for Next-generation IT Services PEAK Matrix™ Assessment 2020

Our global headcount is 9951 as of Q3 FY20 - a net decline of 268 associates on a QoQ basis on account of project ramp-downs as previously stated. Our voluntary attrition rate stands at 16%.

In the last call, we announced our commitment to shift to “Living AI” as a company, where we strive to make all our platforms driven by AI. We also started implementing these solutions for our associates, with various use cases from internal job recommendation and accelerated learning programs, opportunity readiness and infrastructure and space management. We continue to take these living AI enabled high-impact transformation solutions for our clients.

Before I invite Navneet, I want to take the opportunity to acknowledge and thank Ajay Bhandari, our CCDO for all his great work and wish him the best as he transitions out of Zensar, Navneet our CFO will henceforth be the SPOC for all IR tracks.

With that, I will now invite Navneet, our CFO to provide update on key finance data; after which we will open the floor for questions.

Navneet Khandelwal: Thank you, Sandeep. Good day, everyone. Welcome to Zensar’s Q3FY20 analyst call. In addition to Sandeep talking about the business, I will walk you through some of the details on financials.

In the third quarter of FY '20, we have reported revenue of \$143.3 million, reflecting a decline of 5.9% sequentially and a growth of 1.1% annually. In constant currency terms, this decline is 6.4% sequentially, while the growth is 0.8% on Y-o-Y basis.

In Indian rupees, we have reported Rs. 10,206 million as revenue, which reflects a sequential decline by 4.8% and a year-on-year decline by 0.1%. The U.S. dollar realization during the quarter have been Rs. 71.2 per dollar against Rs. 70.4 in the previous quarter. The year before, in the same quarter, it was Rs. 72.1.

Our gross margins for this quarter stood at 23.6% as against 29.1% in the previous quarter. Other income for the quarter includes a gain of \$3.6 million or Rs. 257 million on account of write-back of contingent consideration on business combinations being no longer payable.

The effective tax rate for the quarter is at 25.5% as against 28.5% in the previous quarter. The reduction in effective tax rate is a result of a proportion of other income not being chargeable to tax.

For the quarter ended December 31, 2019, billed DSO remain unchanged as compared with previous quarter and stood at 57 days. While DSO, including unbilled, reduced by 9 days to 93 days as against 102 days in the previous quarter.

Cash and cash equivalents, including investments in mutual funds, net of borrowings, increased from \$13.3 million in the previous quarter to \$46.7 million in the quarter ended December 31, 2019, representing a net increase of \$33.3 million.

The Board of Directors have approved an interim dividend of Rs. 1 per share. The total amount of outstanding hedges as of December 31, 2019, was equivalent to \$178.4 million against \$170.2 million in the previous quarter. As of end of this quarter, our cash and cash equivalent balance was \$92 million as against \$60.6 million in Q2 FY '20.

With that, I come to the end of my presentation and open the house for questions and answers.

Moderator: Thank you very much. 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: Sandeep, just wanted your thoughts in terms of how much of these one-timers are likely to come back into revenue next quarter? So, I think we have mentioned furloughs of \$4 million, year-end volume discounts of \$1.5 million and \$5 million drop in retail, so how much of this can we anticipate will come back next quarter? Any puts and takes that you can help us with?

Sandeep Kishore: Sure, thanks Nitin. I think all of furloughs and all of volume discounts will come back. And most part of the retail also will come back not through the same set of accounts because we have rationalized 8 accounts from retail sector, which were bottom of the pyramid accounts, but through the deal wins that we have talked about earlier and through the normal ramp-up into our existing accounts. We are quite confident that most of this will also come back.

Nitin Padmanabhan: So if I understand this, rationalization happened in the month of December. So would that mean that we have just had a 1-month impact and there is 2 months remaining?

Sandeep Kishore: So some part of the rationalization, you are right, will continue into quarter 4 also because these are client programs. But as explained earlier, these are strategic decisions that we took to get out of the customer. They were specifically into apparel retail, lower end of the spectrum. And we waited for the financials from the holiday seasons to actually start coming in before we took that decision. And these are live customer programs, so unfortunately, you cannot just pull the plug out. We do believe most of it is out. Some residual will go into quarter 4. But our existing pipeline and the deal win should be significant enough to overcome the softness in retail.

Nitin Padmanabhan: Sure. All these 3 elements would actually come back into revenue going into next quarter? So, then it appears, it should be a reasonably strong sort of growth for next quarter then? That is a fair assessment or inference to make?

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Sandeep Kishore: Yes. And as I made a statement earlier, we do expect by end of this fiscal, which is the end of quarter 4, we expect the growth to normalize and the business metrics to come back to the first quarter as we entered this fiscal. This quarter was a bit abnormal, there was very high seasonality and several of it actually came towards the end of first half to the second half of December.

Furloughs, for example, normally, we have seen furloughs coming into the United States customer. This time, in South Africa, we had pretty much a shutdown for the last 2 weeks, which, of course, is a first-timer, never before has it happened. It is about close to 11% of our business. In U.K. also, several of our large clients had a 1-week off.

So it was a reasonably unusual quarter, and hence, we have provided quite a detailed walk from the last quarter to this quarter. We feel quite confident that we should get back in the same zone as that of quarter 1 of this fiscal, as we exit the year.

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

Madhu Babu: Sir, retail has declined substantially as a percentage of revenues, so what portion do you think is still vulnerable or have we bottomed out? Is it like 13.5% of the total revenues that would be the new normal? Or are there any pieces of business where you see further risk?

Sandeep Kishore: So Madhu Babu, it is a question that has come many, many times before as well. And if I just draw the context of going several quarters prior, if you look at 8 quarters before, on a smaller base, retail used to be close to 27%, 28% of our business, and that sector has seen significant challenge because of the category of our customers. And hence, we had no choice but to moderate it down to a level where these kind of high seasonalities are not there and they do not impact the business. So we are down to about 13%.

Have we bottomed out? I still think it will take maybe 1 quarter, 2 quarter to bottom out. But our endeavor is actually to drive more financial services and high-tech and manufacturing business growth, and relook at retail and broaden it into more of a consumer services rather than just retail.

So there are categories like CPG, new age media, retail tech and specialty niche retailers rather than just apparel retailers, which is the category of clients that we are in today.

So it should bottom out. I do not think it has bottomed out yet. It will bottom out probably by end of next quarter, it will bottom out. So by then, we will add new categories.

Madhu Babu: So some of the acquisitions we have done, especially on the digital side, like Foolproof or a Keystone, so how easy for us it would be to build something like a travel or hospitality vertical where there could be some of digital work and maybe then get into the traditional services in such kind of new verticals?

Sandeep Kishore: Yes. I mean it is not a slam dunk, but those are the areas we are considering because we do have phenomenal capabilities through those acquisitions that we've built.

Also through the retail specific acquisition that we had, Keystone, in this particular case, that we acquired close to 3 years ago now, I mean, it came in with digital supply chain and omnichannel competencies built on Manhattan platform. And we have pivoted that now and have started taking it into other companies which implement supply chain, CPG, for example, is a travel and hospitality company. So there are implications of that. And that is exactly the direction that we are walking to broad-base retail into consumer sector as a strategic choice.

We had a difficult decision to take this quarter. A lot of it was unknown. We did not know the South Africa shutdown would happen. Also the onetime volume discount, which I called out earlier. In a way, it is a positive news because we hit the execution top end of the goal that the client had set. A lot of SOWs were in progress at the beginning of the quarter, which were converted and closed. The client's fiscal year ended at the calendar year. So of course, the client wanted the discount to be given at the close of the fiscal for them as well. The quarter had a lot of one-timer come in. On the retail side, we are very focused on bringing the growth back into consumer category, not just into retail.

Madhu Babu: Sir, and the last one on the TCV, how much are multiservice deals where you have good annuity stream? Because currently, it appears that we have a lot of exposure to project-based work?

Sandeep Kishore: So, on the TCV \$170 million, as I mentioned, \$75 million of that is incremental, 5-year TCV. Of the \$75 million, roughly about 40% is annuity and 60% is project.

Moderator: Thank you. The next question is from the line of Mukul Garg from Haitong Securities. Please go ahead.

Mukul Garg: Sandeep, I just wanted to go a little bit longer term. If you look at how the business has progressed over last 2-2.5 years, earlier there was a lot of focus on the retail vertical, where our view used to be that since we are mostly exposed to new retail. Now it seems like that philosophy has probably has not worked, and we are kind of pivoting to a broader area of operation. So if you can just help us what are the learnings, which are there from this? And what is our kind of backup plan in case there is any issues which happens in the wider area of retail as well?

Sandeep Kishore: Yes Mukul, I think it is a great question. Strategically, you always have to fine-tune your strategy and align to where we see the growth happening. Where we see the growth happening, as we stand today, is in our cloud infrastructure business, is in our financial services business, is in our high-tech manufacturing business. If I actually remove the furlough and the year-end volume discount, which is significant, it is \$5.5 million for a quarter. For, \$150 million, it is a significant number. Even high-tech manufacturing actually has grown, if I add that back.

So, we have competencies, we have pivots and we have differentiated offerings into each of these verticals and CIS as a global horizontal. That is where our focus is. Retail, 3-4 years ago, when we looked at it, of course, the sector was behaving differently. And at that time, we were largely an ATG commerce-led shop. And most of the commerce implementations are done, one. Two, Oracle Cloud, which obviously took and converted everything of ATG into cloud, the services business around that has come down.

Application services. It is now more on cloud infrastructure, orchestration, DevOps, managed services. So, you have to pivot and look and take your bets. Our bet over the next 2 to 3 years is clearly going to be experience plus data on the application stack and the middleware level, then the back-end is either bespoke or Oracle stack customs, largely custom because of financial services need. And then the whole next-gen cloud infrastructure stack. We are anywhere not there in the legacy cloud because our cloud business is a very new business.

And financial service is built on our Guidewire competency and is largely P&C. And that is where the investment, Mukul, is being built for the company, both in terms of go-to-market as well as our operational capability.

Mukul Garg: And Sandeep, sorry to push on the retail side, again, while I understand that there were a couple of clients which were not core for you and I think you wanted to reduce exposure, but given that Q3 is a seasonally weak quarter and you were already seeing some weakness in other clients during the quarter, what was the urgency to kind of cut and see a meaningfully high reduction in top line during Q3?

Sandeep Kishore: Yes, not at all to push on this, I am happy to answer this question because this question has come up earlier as well. When you decide to walk out of a client, you just cannot do this at the last minute. So there was a well thought out plan that if their numbers do not hit their own goals because you, of course, track it at the beginning of the holiday season, right at the end of Thanksgiving, you are going to walk out, and you have to let the client know. And at that time, when we did decide that, there was no excruciatingly painful furlough impact that we were aware of in the South Africa and in the U.K. market.

Also, the volume discount was not there because the SOWs were not signed in the early part of the quarter. So it was a difficult choice that now that you have already committed to the customer, you really cannot go back because the transition plans are in place. We moved, you will see in our headcount data, close to 160 of our folks on-site to offshore. And all of these needs to be planned.

So once you set the ball in motion, it is very difficult to roll back in because there are client streams involved, there are live projects involved. And it actually hit us all together, and that is why, in a very transparent manner, we are calling out each one of them, category-by-category.

Mukul Garg: And then one final question from my side. While you mentioned in on top line, you will revert to start of FY '20 by Q4. On margin side, when do you think you would be able to revert back to the 14% margin profile in Q2? Because as we progress through the calendar year, in the fiscal second quarter, we will also have wage hikes, so should we assume that, that will be towards the second half of FY '21?

Sandeep Kishore: Yes, I think that is a fair assumption. We are working on our cost rationalization initiative to improve margin. We were at 14% operating margin in quarter 2. Quarter 1 also in the same zone. Yes, wage hike will come. So, as we exit the year fiscal '21, we do want to be 14%-15%. We have a commitment to get to 15%. And as management team, we are very focused and committed to get to 15%, certainly in fiscal '21.

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Moderator: Thank you. The next question is from the line of Namit Arora from IndGrowth Capital. Please go ahead.

Namit Arora: Sandeep, over the last few quarters, every quarter, you've had various sort of one-offs. What is your confidence level that we will not see that recurring in the coming quarters to come? And what steps are you taking to change a few things if some changes are required?

Sandeep Kishore: So I think, Namit, it is a fair question. If I just go back and exclude the last 2 quarters, particularly, quarter 3, of course, we have talked about it, quarter 2 was soft as well. But the previous 10, 12 quarters, every single quarter, we have delivered between 2.5% to 3.5% sequential growth consistently. Yes, none of us in the management team are happy, in my team of what has happened into quarter 3, but it has happened.

Strategic choices need to be made; we made those choices. As I look ahead with the pipeline and the wins that we have had, we feel actually quite confident that the softness into retail sector, we must be able to mitigate through CIS, cloud infrastructure, our financial services business and our high-tech and manufacturing as a sector.

And the reason I feel pretty positive about it is because the deal pipelines have started to move quite well. Our focus on existing account mining has been working very well. And I called out some data. If you look at 8 quarters ago, we have more than double \$5-plus million and \$10-plus million deal, and that we have stated that all along. We actually want to work with fewer customers, multi-services rather than a long list of customers.

So where I stand today, our endeavor is to deliver industry level growth and margins in the coming quarters. And our immediate priority is to actually by end of this fiscal, get back to the normal business metrics of quarter 1. We want to get in that zone, which we have consistently delivered.

Namit Arora: Just a quick follow-up. As the pipeline flows into the business, what is your confidence level that the gross margin levels will hold sort of steady as compared to the past average levels?

Sandeep Kishore: Yes. So gross margin level, of course, in quarter 3 was pretty bad because of all the revenue drift, which full off all of that almost flowed straight into the gross margin. But otherwise, we have been operating between 28.5% to closer to 30% or so. And we want to get back to that level and manage our fixed costs better. We had our increase in Opex even in quarter 3, and that also added and there is a 70 basis point impact on increased G&A.

So we are focused on EBITDA, that 15% commit that we have given, and we are all working towards making that happen as we get through into fiscal '21.

I just want to maybe take a minute and call Harjott who heads our global cloud infrastructure business. And the reason I am calling him to give a little more color on our margin expansion, particularly that we have done in our cloud infrastructure business, and we have reported in our sector reporting. And as that business scales, you will see better margins, which also we have talked in many of the analyst commentary before. Harjott, do you want to just give a quick color on the broader commentary on margin expansion of the business?

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Harjott Atrii: Sure, Sandeep. Thank you. The margin expansion is courtesy to the fact that we are signing, we are winning the deals at a healthy margin. We have also applied autonomies and the other aspects of operations optimization to drive margin expansion.

We have also built internal capabilities to drive shared services. So a lot of our engagements are moving to shared services and the utilization rates have gone up as well.

And also, finally, the pressure track in terms of how we do the span of control and the pyramid optimization, including pressure track is also effective and operational in most of the new engagements. So all these factors combined are contributing to the margin expansion, which you are seeing in Q3.

Moderator: We move to the next question from the line of Shekhar Mundra, an individual investor. Please go ahead.

Shekhar Mundra: Yes. So I have been invested in this company for long. So for the past 4-5 years, I have been tracking it. I understand, like, digital has become a significant percentage of revenues, and even we are having a higher concentration of bigger clients. But as a company, if you see, I just see the bottom line, it is not showing in the numbers. So are we actually moving ahead as a company? I just wanted some color on that.

Sandeep Kishore: Yes. Thank you, Shekhar, for your investment and your support and commitment. Digital, when we started the change journey, we were probably under 17%-18%, I remember. And it has now crossed 53%-54%, actually, now. Right, so beyond a point of time, actually, digital, most of the people in the industry have also started talking about it. It is becoming a part of the business itself.

The reason for our business softness in quarter 3 has not been attributed to digital at all. Actually, our digital business continued to do quite well. It is all those furloughs and one-timers and retail specific things that have come.

What you also heard, Shekhar, from Harjott on our cloud infrastructure is all next-generation digital stack business that we deliver. The 2 companies that we had acquired, Foolproof in U.K. and Indigo Slate in the U.S., they are all experienced and creative content company, which is the need of the hour. Based on that, we have won 4 new logos outside of the CIS, actually just last quarter. So, you will see it has not shown into margins for a different reason. I do believe it is strategically important.

If we have to be relevant to our customers, I do not think you have a choice but to align to where the clients are investing. Over a period of time, it will start to show the margin. Unfortunately, it has not showed up yet.

Shekhar Mundra: Right. So what I meant was, this quarter, I can understand, there are some reasons for it, but as I see, like earlier, our margins used to be in the range of 15%-16%. So now the new normal has somewhat becomes like 12% to 13%. So are we hopeful of getting back to those levels or even higher?

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- Sandeep Kishore:** If you meant the operating margin, EBITDA?
- Shekhar Mundra:** Yes. EBITDA margins, yes.
- Sandeep Kishore:** Yes, absolutely. I have made a statement, Shekhar, earlier it can get back to 15%.
- Moderator:** Thank you. The next question is from the line of Sudheer Guntupalli from Motilal Oswal Securities Limited. Please go ahead.
- Sudheer Guntupalli:** When you are talking about the tail account rationalization, and especially when we are saying it was planned well in advance, the usual expectation is that it is planned in such a way not to disrupt the utilization metric or margins much. However, your utilization seemed to have shown a sharp drop on a sequential basis. And if we look at the previous quarter, on a gross basis, we have added almost 1,000 employees, even on a net basis, the offshore technical headcount addition was strong in the previous quarter. So with the benefit of hindsight, can we say this rationalization could have been done with lesser disruption on the utilization and margin front than what it created now?
- Sandeep Kishore:** So Sudheer, hindsight, could we have done it differently? Maybe we would have moderated it if we knew that all of these, that is furloughs into South Africa, U.K., this volume discount and the planned ramps down that we had, all of that would hit together. We could have certainly moderated it better. I totally hear you.
- Moderator:** Thank you. The next question is from the line of Amit Chandra from HDFC Securities. Please go ahead.
- Amit Chandra:** Sir, as we mentioned that we have a TCV of \$170 million and 45% of that is net new wins, so can you quantify the number that was there in the last quarter? And as we see that the pipeline remains strong at, like, \$1 billion, so are we investing into SG&A and to just build the pipeline? And how has been the conversion there?
- Sandeep Kishore:** So Amit, there are multiple parts of your question, the last question first, yes, we are investing into SG&A. If you look at our factsheet, in our sales and marketing headcount, we have added actually year-on-year, probably 14 additional associates, even sequentially, about 5. Plus, it is not just headcount, we have increased significantly into adviser analyst track, and that is the reason why you see Zensar now getting featured and captured into multiple reports, which was never the case before. We have created a customer advisory board where we are meeting with our customers, engaging with them much more meaningfully. That helps us mine account better. That is the reason why you see \$5-plus million and \$10-plus million account category go up. So it is a strategic choice to invest into sales and marketing.
- We are very focused in those 3 countries, South Africa, now crossed 10%, U.K. and U.S. It is a very focused strategy to build competency at scale into 3 countries and largely, 3 verticals, which are FS, consumer, as we go forward in fiscal '21, it will be called consumer services and, of course, technology and manufacturing.

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Amit Chandra: Okay. And the 45% number that you have mentioned in this quarter, what was the number for the last quarter?

Sandeep Kishore: Yes. So we actually, in our all analyst calls, I think we have called it out. It is normally in the range of 50-50. So if you look at quarter 2, we had \$120 million of win; quarter 1, we had \$160 million; and the previous fiscal year, the total wins were about \$750 million, but that included the 2 acquisitions. This year, we have had no acquisitions. So actually, on an apples-to-apples basis, it is in the same zone.

Amit Chandra: Okay. And sir, as you mentioned that the furlough impact was higher-than-expected in the South African geography, so can you please quantify the nature of the furlough? Was it planned? Or was it a surprise for you? And can we see the extended impact of furloughs the next quarter also?

Sandeep Kishore: So normal furloughs are always planned because of the U.S. furloughs, we have worked with the customers for long term and we know the furloughs. South Africa till now has had no furloughs for our clients. Actually, this is the first time. And there was virtually very little notice even given to us.

So, it was literally told that we will have furloughs of 2 weeks, and we have large financial services clients in South Africa. So it did come as a surprise to us. So, 70% of the furloughs impact came from U.S., because 70% of our business is in the U.S., the other 30% or so actually was a surprise.

Amit Chandra: Okay. And sir, in terms of the margins, can you quantify the near-term levers that you have for margin expansion? And what we have in plan to improve our margin in the long term? So the near-term and the long-term margin levers?

Sandeep Kishore: Let me actually ask Prameela, our COO, and she also runs the entire application digital business to just give a little more color on the margin levers.

Prameela Kalive: Yes. So in terms of the near-term levers, the 2 important things that we are doing is in terms of correcting our resource key pyramid, and that is why you see in the last couple of quarters, we have been investing in onboarding sessions. They are all going through training, they have all moved into our delivery teams. So, over the next quarter or 2, we will see all of them get into billing roles, helping us flatten the pyramid and reduce the average cost of operation.

In the medium to long-term, again, as an investment, in this year, we have started to implement all the lean and automation levers in all our managed services and fixed price projects. We have created a lot of reusable assets, which are going in into the project. They will take 6 to 8 months for us to really impact the margin because that is when we apply the levers, we slowly release the people, we correct the pyramid. So, we see that as a medium-term and a sustainable impact for us on the margins part.

The sub-contractor part has been a focus area that we started in the beginning of the year, and if you see now, both, not just the subcontractor headcount, but also the subcontractor margin is something we are focusing on. We see that heading in the right direction for us.

And the on-site mix. Reducing the dependence on on-site revenue, improving the offshore mix is another area we are very focused on because the more offshore we do, the higher will be the leverage for us to apply all our margin expansion levers.

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

Madhu Babu: Sir, just on the portfolio, we used to be earlier higher on the Oracle side, so currently can we give within Oracle, Salesforce, Pega, which are the areas? And how was the team sizes within each of these? And Oracle as such has been not doing that great because of the competitive pressures from others. So how is that portfolio shaping up on that? Can you give some view?

Prameela Kalive: Yes. So the Oracle in the last 1.5 years, we completely rehashed our offering. There was a traditional Oracle business that Zensar always had a few years back. But now if you see the Oracle pipeline is building up very well for us. This is the new age, the Cloud Oracle business. We have very significant deals in the pipeline that we are working on, specifically in the U.S. on the Oracle side. So we see the mix of the traditional Oracle business versus the new age Cloud Oracle business shifting in the right direction. So we see that will be very different in the coming quarters.

Madhu Babu: So the other areas like Salesforce, Pega, because in the website, we have shown some team sizes, but how big are they currently?

Prameela Kalive: Yes. So the Pega practice for us is something that we began to incubate in one of the large U.S. customers. And now that practice is scaling back to become a global practice for us, while we led from the U.S. SFDC has been significant one of our very prominent centers of excellence that we have invested on. And SFDC in the new age, which Einstein and Lightning, which is a new technology that SFDC itself is pushing into the market.

Both are areas where, in fact, what we have done in the last few quarters, is to take a bet on some of these fast-moving technologies from building proactive capacity and capability through our technology transformation group. So these are fast-growing few areas for us, and we see significant growth coming from these in our top accounts, specifically in the U.S. and the U.K. markets. Both are high investment area for us, where we are building capacity as well as SME leadership in the region.

Madhu Babu: Okay. And just one more. So now that retail has been on the back foot, so insurance for us is around 20% and, of course, Cynosure has helped us in the Guidewire implementation. So how are we able to get into some of the new accounts in insurance, mining and the traditional services? Because let us say we do a Guidewire implementation and then cross sell.

Sandeep Kishore: So P&C focus in the United States is built around Guidewire competency. And I think we have done very well in terms of not just opening new logos. Actually, Guidewire has elevated the partnership with us. We are now a higher level advantage with Guidewire than what we were even before. So our business has scaled up. We have opened new logos. We now have 27 active clients on P&C Insurance, largely built around Guidewire.

And our strategy there is that we want to be a full-service provider, multi services. We are bringing, as we talked earlier, the whole creative content front-end technology work, which our experience and data analytics team does and then cloud infrastructure. So you go in with Guidewire, you do the transformation on any of the platforms: billing, claims and account and data, and then bring other services as well, policy billing claims, data and then bring cloud infrastructure on one track and experience and content on the other track.

And we have started to see the traction. I mean I feel very good. There are very, very good discussions happening. We are of the \$1 billion pipeline; our U.S. financial services pipeline is probably over 25% of that.

Madhu Babu: And one question for Navneet. What is the payout remaining for the earlier acquisitions? And now that the cash flow has improved, around the Rs. 330 crores of net cash and the stock is at a very reasonable valuation, would you look to do some open-market buyback or something like that?

Navneet Khandelwal: So answering your first question, in this fiscal, we still have about \$1.3 million of payout remaining from the earlier acquisitions, which is expected to happen in Q4. With respect to the cash that we have got, we have always stated that we will always continue to look for opportunities for any future acquisitions. And so we are going to conserve the cash for further expansion opportunities. And at this moment, we do not have any particular plan of a buyback to be put in place.

Madhu Babu: But this earn out, this is the last or do we have anything for '21?

Navneet Khandelwal: No. We do have further earn outs going on into FY '21 also. It will go until FY '22.

Madhu Babu: Yes, but how much is that tentative approximate number?

Navneet Khandelwal: Specific number for FY '21 would be about \$5 million. For FY '22, would be roughly about \$10 million.

Moderator: Thank you. The next question is from the line of Akshay Ramnani from Axis Capital. Please go ahead.

Akshay Ramnani: I just have one question on our deal TCV number. While bookings in this quarter have been strong, what I really would like to know is that, has this portfolio restructuring exercise in the retail has had any impact on our previous deal booking? So if you can reiterate our deal TCV number for FY '19 and 9-month FY '20, that would be helpful.

Sandeep Kishore: So Akshay, broadly, no. Our deal wins traditionally have been in the high-tech manufacturing, it is 54% of our business and largely financial services. That is why you are seeing both of those sectors growing. We did win a few projects into retail, but no, I do not think retail, long tail account rationalization has had much of an impact. It has been a softer sector, per se. So I do not think so.

The third category is, as I mentioned, cloud infrastructure business has had a very, very robust pipeline and a very good deal momentum. So that is horizontal, right? So I do not think retail has had much impact into any of those leakages.

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

Rahul Jain: Yes. So my question is more regarding the discounts that we offer during the quarter. So if you could bit elaborate a bit more? I know you have spent some time on this, but in terms of understanding what kind of factors are driving this kind of thing? Do we see this kind of things possibly occurring more across the spectrum and not just for offline but beyond this? Any kind of flavor you could share on this would be very helpful.

Navneet Khandelwal: Yes, sure. See, this discount is specifically happened in 2 of our top 20 customers. Typically, the contract years with these customers are calendar years, and these discounts are linked to the threshold of invoicing, which is done to them. And based on the year-end invoicing that we have done for them, we have hit these thresholds. And these were unanticipated from a perspective that you can see that our unbilled also has moved very significantly from the previous quarter to the current quarter. It has also resulted in a significant positive cash flow. And that is the reason that these thresholds have been hit, and we ended up paying these discounts as a onetime thing. So these discounts will not continue in the subsequent quarter because it has got completely paid out at this moment.

Rahul Jain: Okay. So this has nothing to do with the demand environment it is more than like it is?

Navneet Khandelwal: No, there is no element of demand environment related issues nor any pricing pressure-related issue in this.

Rahul Jain: So my question was on the other income side, is it why there has been this move from Q2 being soft and Q3 being this? Is there something related to reporting which we could not do previous quarter and which is coming in this quarter?

Navneet Khandelwal: No. Actually, as we have called out both in our notes to accounts and in my opening commentary as well, there is a onetime element in the other income, which is related to a write-back which has come into as a result of a contingent consideration on an acquisition no longer being payable. And we have quantified that to be about \$3.6 million, which is featuring in our other income line item. It is a onetime event.

Rahul Jain: And any specific reason why our attrition on a quarterly annualized basis have jumped significantly in this quarter?

Sandeep Kishore: Vivek, do you want to give a quick answer?

Vivek Ranjan: Yes. Thanks, Rahul. So, Rahul, our voluntary attrition is 16%, which is as per the industry standard. So is that what you are referring to? Because the attrition is as per the industry standard, better than industry standard.

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- Rahul Jain:** So actually, I was more talking about current quarter numbers. If we annualize, this looks pretty sharp.
- Vivek Ranjan:** Yes. So it is 16%, the attrition percentage.
- Rahul Jain:** Is this 16% on a trailing 12-month basis?
- Vivek Ranjan:** Yes, YTD. Annualized.
- Rahul Jain:** Yes, so I was more talking about this particular quarter. Nevertheless, I will take this off-line.
- Moderator:** Thank you. The next question is from the line of Mukul Garg from Haitong Securities. Please go ahead.
- Mukul Garg:** Sandeep, just wanted to understand this discount issue a bit more. When you say that 2 of your top customers' invoicing thresholds got hit and you were not expecting that to kind of happen this quarter. Was there a material pickup in business with these 2 clients, which led to this threshold coming in Q3 instead of, I think, expected probably in Q4? And is that something, which you expect to continue?
- Sandeep Kishore:** So Mukul, the last question first. I do not think it is going to continue for a very long time. And I am not saying it will not continue perpetually because these are large clients and the volume threshold is in steps of next \$10 million per annum kind of revenue. You do not hit that, that often. So I do not think in any near-term is going to come and hit us, certainly not in next several quarters.
- Second is, were we expecting it at the beginning of the quarter, several SOWs were in play. So actually, the good news with this is, we signed the SOW, we executed on them, we ramped up, we hit the threshold discount. And one of these customers is our top most client. Their calendar year, fiscal year, everything ends there, and they actually insisted that we provide for that into the quarter itself. And it is our top most customer. So we, of course, made sure that we continue our growth momentum with them. And the next threshold is at a much higher level with them. So we do not see that happening any time in the near future.
- Mukul Garg:** But what I was kind of referring to was, so SOWs were mainly applicable for the quarter or was that an increase in share at the client which will help us our growth over the coming quarters?
- Sandeep Kishore:** Actually, both. So some of these are projects and some are annuity. I think probably 70% in these cases are projects. These are all digital analytics, cloud kind of projects. And 30% are the support maintenance work.
- Mukul Garg:** The other question was again a bit more hypothetical in nature. If you look at last 3 to 4 years, there are a couple of quarters. I think this is the third one where we had unexpected material impact either on growth or on margins, which was unexpected, even for the company. So (a) do you expect to build in any mechanism internally to kind of prevent these kind of sharp hits;

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and (b) what do you see right now as the key areas which will, to probably use the word, keep you awake at night?

Sandeep Kishore: So in the last 15, 16 quarters, you are right, it is probably second or third time. So these things do not happen that often. And yes, as a core management team, we do want to ensure that we prepare ourselves well, so that if there are some softness in some sectors, growth in the other sector must be able to balance it.

Unfortunately, the retail track has been rather softer than normal. Otherwise, we should not have been and then this project got hit by all the furloughs and the volume discount here.

But our focus, Mukul, is, as I have maintained in this call throughout the day, is we expect most of these are behind us, we expect the growth to normalize and get back to our quarter 1 level. And the reason it is important is so that when we get into fiscal '21, we get in on a strong footing and deliver to our 15% number on operating margin as we get through fiscal '21.

Moderator: Ladies and gentlemen, due to time constraint, we will take the last question from the line of Amar Mourya from AlfAccurate Advisors.

Amar Mourya: Firstly, sir, I wanted to understand a little bit on this 15% margin guidance, which we are talking about. Is this we are talking about the full year margin guidance of 15%?

Navneet Khandelwal: Yes. So this 15% margin guidance we are talking of, we should be able to hit on a run rate basis in the coming fiscal year. So it will still take a couple of quarters to get there.

Amar Mourya: So meaning, are you saying that your 15% would be the exit margin run rate? That is fair to assume.

Navneet Khandelwal: Yes, that is fair, for FY '21.

Amar Mourya: Yes, for FY '20 so full year FY '21, 15% margin. Are you saying that or you are saying that 15% would be my Q4 exit margin?

Navneet Khandelwal: No. I am saying that in FY '21, we will get into the run rate of 15%.

Amar Mourya: So basically, you will report 15% kind of a margin rather than the 11%, which is current?

Navneet Khandelwal: Yes. But not for the full fiscal, is what I am saying. We will get into that run rate in FY '21, in one of the quarters in FY '21.

Amar Mourya: Okay. So Q3, Q4 would be the case?

Navneet Khandelwal: Yes, absolutely.

Amar Mourya: Okay. And secondly, sir, if I look your 20 quarters now, I mean, probably 19 quarters, I mean, on a CAGR basis on a yearly CAGR basis, you had done a kind of a 10% kind of top line growth, but only 1% kind of EBITDA growth? And now when we are saying, after, I think after 4 years or 5 years, we are going to reach to again the 15% kind of a margin, so what gives us

this kind of a confidence that again we will be back after 4 years to this kind of a margin trajectory?

Navneet Khandelwal: So there are 2 aspects to it. Number one is when you are looking at a 19-quarter CAGR, about 19 quarters back, we were not reporting as per Ind AS. From the time Ind AS has come in, you have to start taking amortization of intangible assets in your P&L. So that amortization impact itself is about 2 percentage on the EBITDA because of the accounting standard changes. And we, as indicated in the call earlier, by Prameela, we have identified the levers that we need to work on. We believe the levers are reasonable to be able to achieve and that gives us the confidence that we should be able to get back to the margin trajectory.

Amar Mourya: Okay. So basically, then you are talking about on a like-to-like basis, you are talking about not 15%, but basically a 17% margin on a like-to-like basis. Because you said that 200 basis point was basically the Ind AS impact, if I compare a 4 years view?

Navneet Khandelwal: So basically, 4 years back, our EBITDA were 15%. If I were to apply the current accounting standards, those EBITDA would get restated to 13%.

Amar Mourya: Okay. Got it. And sir, lastly, if I can? I mean now even on the growth trajectory part, if I see, barring '19, I think there was a 3%, 1% kind of a top line growth, and I believe in '19, there were a lot of I mean, there were acquisitions also. So now given that in '20, there will be no acquisitions, and I believe in '21, we do not plan to anything. So how I mean, how we should we look a growth trajectory going forward? I mean you had obviously indicated that TCV looks healthy. But what kind of growth we should look? I mean, is it like a single-digit or high double-digit kind of a growth?

Sandeep Kishore: So Amar, Sandeep, here. As I have stated earlier, we definitely plan to get to the industry level, mid-cap sector industry level growth in the coming quarters. I also want to call out that if you look at fiscal '19, that you called, we grew about 17%, year-on-year. If you do just organic, that number is also publicly available, the organic growth was roughly about 8.5% to 9%.

Now this year, in spite of one-timers that we talked about all through the call, in quarter 3, we are still tracking to make sure that we get to high single-digits even in this quarter, even in this fiscal, and that is going to be all organic. So being in the same mode of course, as we get into fiscal '21, we are still an acquisitive company. You heard it from Navneet. I mean we are generating cash; we are conserving it, we are looking for acquisitions. But on an organic basis, pure apples-to-apples, you should expect us to get to the industry level growth in fiscal '21.

Amar Mourya: Okay. So basically, a high single-digit kind of a growth or double-digit?

Sandeep Kishore: Yes. We will be in the zone.

Moderator: Thank you. I now hand the conference over to the management for closing comments.

Sandeep Kishore: Well, thank you for being with us today on the call in quarter 3 and look forward to talking to all of you again next quarter. Thank you.