

**Cigniti Technologies Limited**  
**Q3 and 9 months FY19 results**  
**February 01, 2019**

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**Moderator:** Ladies and gentlemen, good day and welcome to the investor call of Cigniti Technologies Limited to discuss the Q3 and 9 months FY19 results. We have with us today from the management, Mr. Srikanth Chakkilam - Chief Executive Officer and non-Executive Director and Mr. Krishnan Venkatachary - Chief Financial Officer. 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, please signal an operator by entering "\*" then "0" on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Srikanth Chakkilam for the opening remarks. Thank you and over to you, sir.

**Srikanth Chakkilam:** Hello everyone, Srikanth here. Before we start, I would like to point out that certain statements made in today's call may be forward looking in nature and the disclaimer to this effect has been included in the earnings presentation shared with you earlier. The investor call may contain forward-looking statements based on the currently held beliefs and assumptions of the management of the company which are expressed in good faith and in their opinion reasonable. Forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, financial condition, performance or achievements of the company or industry results to differ materially from the results financial condition, performance or achievements expressed or implied by such forward-looking statement. The risks and uncertainties relating to these statements include but are not limited to risks and risks of expansion plans, benefits from there from fluctuations in our earnings, our ability to manage growth and implement strategies, competition in our business, including those factors which may affect our cost advantage, wage increases in India, our ability to attract and retain highly skilled professionals and our ability to win new contracts, changes in technology, availability of financing, our ability to successfully compete and integrate our expansion plans, liabilities, political instability and general economic conditions affecting our industry. Unless otherwise indicated, the information's contained herein is preliminary indicative and is based on the management information, current plans and estimates.

Welcome to the earnings call of Cigniti Technologies Limited for Q3FY19. Some key highlights for the quarter are; Revenues at Rs. 209.97 crores and EBITDA at Rs. 38.53 crores translating to an EBITDA margin of 18.4% and PAT at Rs. 28.02 crores. We have added 14 new clients in this quarter and there is no particular trend in terms of domain for the clients added. The

company continues to be vertical agonistic. The range of domains from which clients are added in this quarter include, travel, insurance and ISVs. North America continues to be our largest market and 80% of the clients added in Q3 are from North America. Automation is one of the key trends of the industry in quality engineering which continues to be flagship. Out of all the clients signed in this year 62% have test automation as the key requirement and within automation, queries on intelligent automation, which is the use of AI with an automatic and robotic process have been on the rise. We have successfully delivered and are delivering some of these projects. So, this gives rise to the second trend which is the change of skills in our industry. Expectation of multi-skilled professionals is on the rise especially software development engineers and test being a hot skill within the industry. There is a huge skill gap in this area and the company has been gearing up to tackle this problem since the last two quarters. We are continuously training, adding and up scaling people in this area and as a consequence of the two trends above, the third trend is the increasing adoption of digital transformation and increase in number of queries in the DevOps side. At least 20% of the clients are asking for digital transformation initiatives.

Another important trend is customer experience becoming the key outcome of quality engineering, which means that outcome based delivery in the quality engineering services, can be a key differentiator as we proceed. As we move ahead, adoption of cloud is almost main stream with main clients asking us about cloud related testing services as a key service area. Some key challenges that have arisen from the trends mentioned above is the skill gap and of course visa challenges which is not unique to Cigniti alone. For the skill gap part, the company is continuously focused on the resource management framework that we have and the incorporation of learning and development to train and up skill resources. On the second challenge we are exploring near shore facility options in Canada, specifically Toronto to be in the same time zone as US and with similar cultural minds that as the US. We continue to track and invest in some of the key trends to be ahead of the curve and come across as thought leaders in the world of quality engineering. I will now pass on the forum to the CFO.

**Krishnan Venkatachary:**

Ladies and gentlemen, I am sure all of you have the investor presentation, shared with you little while ago. Taking in cue from what Srikanth spoke, our revenue on Dollar terms remains flat and the contribution of 200% growth has come on account of average rupee realization. EBITDA, PAT and resultant EPS has moved up reasonably, we have also given an analysis in terms of going trend as to how we have shaped up over the quarters in terms of EBITDA on an actual basis and also normalized EPS as to what the operations have contributed. In terms of the sector, North America continues to be the best of the sectors continuing to contribute about 80% to 81% of the revenue followed by UK at about 11% and rest of the world contributing the balance. The utilization, for both the regions as we see number of holidays and vacations has come down on a comparable basis to the previous quarters and hence we average at about 93% on onsite and off shore at about 81% at the billing rate of about \$69 and close to \$23 on offshore.

The revenue mix is slightly tilting; we are at about 43.2% towards off shore and 56.8% towards onsite. Revenue in terms of the Dollars could be seen in a way that, for a couple of projects start date has been pushed to about 10<sup>th</sup> or 15<sup>th</sup> January and we also have about close to 400K of revenues not recognized, which will be recognized in the subsequent quarters on account of the delay in signing off or the end milestone getting completed being slightly delayed on account of various other factors. For the quarter we anticipated that the Dollar would probably give about a percentage and Rupee would contribute the rest. In terms of the cost, we remain controlled on the cost as usual. This year we have seen sustainable growth and though we are not in the process of giving a guidance, we are trying to get; on a constant currency basis to inch up to close to about anywhere between 15.5% to 16% in terms of EBITDA.

We are on the right track as the quarter ahead looks definitely promising. The top 20 accounts contribute close to 48% of the revenues and the rest of the accounts contribute about 52%. The margins have been healthy, we have serviced about close to 203 clients during the quarter and the pipeline looks very healthy. We are moving ahead in terms of our business with great optimism. With these few remarks, I now leave the forum open for the questions.

**Moderator:** Thank you. Ladies and gentlemen, we will now begin the question and answer session. We have the first question from the line of Atul Shah from Siqueira Investments. Please go ahead.

**Atul Shah:** Sir, I understand that over the last couple of quarters we have reduced our number of cliental, we have come down from around 400 clients to about 200. I wanted to understand what is our strategy going forward in terms of taking clients on board and what kind of cliental are we looking at? Are we looking at high value clients? Can you just throw some light on that?

**Srikanth Chakkilam:** Within the organization we categorize clients into multiple sectors, not sectors multiple types rather. There is type 1, type 2, type 3, and type 4 clients within the company that usually we talk about. So, usually what happens is when we go after a client we look at their IT budget and subsequently we also look at their quality engineering budget, based on that we have certain criteria. Usually we would like to have the QA budget to be high. Typically this tends to be high in large, what you call, fortune 500 or global 2000 companies and we categorized them as type 3 and type 4 companies in our internal terminology. Those are the kind of accounts that we aim to go for. We reduced 400 down to 200 and we want to reduce further based on the IT budgets of some of these companies. Some of our strengths include travel and hospitality, ISVs, insurance and healthcare. Of course, banking is also another area but the top areas continue to be travel and hospitality, healthcare and insurance and ISVs. Secondly, we go after clients that have IT budgets and large QA budgets upwards of \$25 million.

**Atul Shah:** Accepted, but what is going to be your focus area in terms of the sectors?

**Srikanth Chakkilam:** We are sector agnostic. Sorry, you have question please complete.

**Atul Shah:** So, I just want to understand focus sectors. Yes, please go ahead, sir.

**Srikanth Chakkilam:** So, we are a sector/vertical agnostic company. While travel and hospitality contributes about 23.4%, ISVs contributes 17%, health care about 15%. We track that internally but that is not a guidance to give out to the market. These are just our areas of strength, but we will continue to be vertical agnostic until we reach a certain size. For our company it is not really relevant to go after sectors.

**Moderator:** Thank you. We have the next question from the line of Rohit Balakrishnan from Vrddhi Capital. Please go ahead.

**Rohit Balakrishnan:** So, I had a question sir. If I look at your historical numbers, there has been a lot of variability in your EBITDA margins. While typically IT services do not have such a big variability. I wanted to understand from you how do you look at your business and what do you think about your EBITDA margins, you think our receivables are normal in this business?

**Krishnan Venkatachary:** I do agree in terms of comparison with the previous year, but I think we have evolved over a period in terms of what is the right kind of the business, what we are doing and what we are trying to focus on. We are focusing on client concentration, have brought it down from 400 to 200 clients and things like that. Over the last seven quarters if you look through in terms of our publication, I think we are more or less stable on our EBITDA. And more so, if you look at in terms of the cash EBITDA I think I am averaging somewhere around 18% in terms of the consistent part of it. On a Dollar part as well basically, I think the whole year more or less has remained at about 16%. If you look at it optimistically, though there is a scope for improvement by about 100 basis points, I think the couple of basis points in terms of reaching it from 16% to 18% on a constant currency basis are possible over the next couple of years. It is not just that possible in a year because we need to factor in the growth and we need to come back. So, if you look at the industry as a trend for our size what we feel that it is achievable for us to get revenue with a consistent baseline of about 20%. But with the timeline caveat in mind, we are focusing a coupled growth and not trying to maintain 16%-17% EBITDA.

**Rohit Balakrishnan:** The other question that I had is that in general, if you look at the QA market or the testing market, last few years the growth has been slower. So, I just wanted to understand from you what would be the overall growth of the industry that you are in? And what are the trends that you are seeing over the next 1-2 years maybe?

**Krishnan Venkatachary:** So, I mentioned the trends earlier, Rohit. But QA not in the company's opinion has become a board room discussion, meaning many clients QA has become more important than ever with all the digital proliferation that we are seeing with so many mobiles, so many applications, with so many devices in the market. And independent testing as a market has been growing about 7% CAGR that is the number I have from NelsonHall. And within that 15% year-on-year growth is coming from the digital testing. And that is a trend that is no different for the company as well, so we are seeing similar trends. And the overall independent testing market is set to be at about \$50 billion.

**Rohit Balakrishnan:** And sorry, I am actually new to your company. So, I have just looked at the presentation that you have posted on your website. So, I mean typically IT companies do not have a lot of debt but you have had historically and that is reducing. And maybe this is a question that is quite live and very basic. I am sorry for that, but just wanted to understand what is the reason for the debt to be there in the balance sheet around 100 crores as of FY19?

**Krishnan Venkatachary:** It is about 93 crores to be very precise as of 31<sup>st</sup> December, which is nothing but factoring account backed by receivables which also currently we are probably in a weeks' time we will be converting that there is an optimization coming up to our commercial line of credit in US at about 5% as against what we are currently paying at about 12.5%. So, that is nothing but except working capital limit of 93 crores. But I think that is backed by our cash and cash equivalents if you look through in terms of the balance sheet which is to the tune of about 47 crores. So, netting that off, we are confident that the balance portion of approximately 45 crores to 50 crores as I start moving the couple of quarters optimism is that, that should get eliminated. And traditionally, we have moved ahead and we have invested heavily into tools and into marketing, we have invested into product development across and we did an optimization from November 2016 and March 2017, that is a culmination which will you have seen. And subsequently, so the cash flows where needed at that point of time, so different kinds of borrowings have taken out and then with all the tightening of purse and putting our focus on a systematic basis, I think with the cash generation, last year we generated about 30 plus crores, this year we have generated in the 9 months about close to 95 crores. We cleared all the long-term debts and the corporate loans everything across and we have also reduced the working capital usage and cycle and accumulated some cash which is a balancing act because I negative of about 5% I think, I will like to use it for my business expansion in terms of the working capital. I have brought down my receivables to 60 days and trying to bring it down to 55 days. So that, that can support me further and I will be able to knock that in the next couple of quarters.

**Rohit Balakrishnan:** And sir, just last question to you mentioned that while the overall QA market, testing market is going at about 7%, there are levers which are growing at 15% which are more digital in new age. But if I look at your revenue you have been growing at 15%-20% over the last few quarters. So, just wanted to understand what is enabling you to grow like that and what is your strategy?

**Srikanth Chakkilam:** Just to focus on the large ticket clients that I was talking about earlier. So, we have cut down from 400 clients to 200 clients. We changed our focus to the clients that can potentially give high value and of course we are driving some of the revenue through IP. So, that is a differentiator for us and we are investing in some of our strengths which is some of the sectors that we believe that we are strong in. That is what is driving the growth.

**Rohit Balakrishnan:** And in case I would like to do more work and may be do a meeting, whom should I get in touch with from the company?

**Krishnan Venkatachary:** You are always free to get in touch with me; my coordinates are there in the investor page in the investor presentation available.

**Moderator:** Thank you. We have the next question from the line of Ashish Agarwal from Principal Mutual Fund. Please go ahead.

**Ashish Agarwal:** So, just wanted to understand how is your deal pipeline looking like and any indication of what kind of a growth we are looking in for next year?

**Srikanth Chakkilam:** So, I cannot give you the exact pipeline value but all I can say is the pipeline when we entered Q4 is more than what we had in Q3. Again there is no particular trend in the division of this pipeline. Some of the deals that we are supposed to start in Q3 and did not have started in Q4. So that possibly will give you some indication of what is going on in terms of growth.

**Ashish Agarwal:** Because the reason I was asking about the last 2 quarter in terms of Dollars growth has been slightly muted. So, do we believe that Q4 and going forward the growth rate should return back?

**Krishnan Venkatachary:** Yes, confidently yes. Q4 and moving forward, I think we will be going at geometric progression in the years ahead because we will be galloping. It is just that we are not in the business of providing any kind of guidance but I think the optimism and the confidence I would say more than optimism as there is confidence based on the data backed, based on the pipeline on the order book, we are very confident that in the next couple of years I think we are on a very strong wicket and we do not see any kind of hurdle.

**Ashish Agarwal:** And last 2 things question on the data point side, so the export incentive income did we book 2.5 crores this quarter?

**Krishnan Venkatachary:** Yes, we have booked 2.5 crores and that is netted off with the exchange loss. And that has been detailed out in the PAT slide basically at about, when you look at the exchange loss at about 5.87 and the export incentive is 2.63 crores that is netted off to about close to 3.2 crores of loss which has been priced.

**Ashish Agarwal:** So, how should we take that income going forward?

**Krishnan Venkatachary:** We expect for this, next quarter to be at about 2.6 and for the next year probably slightly higher at about 10% comparing to what it is.

**Ashish Agarwal:** And lastly on the tax rate, right last 2 quarters tax rate has been low because I think there is some losses. So, what should be the tax rate going into the next year?

**Management:** I expect for the next 6 quarters it will be at a MAT in India at about 4% MAT about in US. And I expect the tax rates should be more or less stable for the next 6 quarters from April. The next quarter is going to be repetitive same. But, from April it is going to be for the next 6 quarters at a stable rate which will be in line with the current year consistency. If you remove the one-time reversals of the taxes which has been done in Q1 net debt off and that is probably gross debt off and then the total taxation which comes as a percentage will remain stable for the next 6 quarters commencing April.

**Ashish Agarwal:** So, blended should be around 15%, right?

**Krishnan Venkatachary:** More or less I would say, yes. Marginally it can come up bit lower but I think we will not be exceeding it.

**Moderator:** Thank you. We have the next question from the line of Sandeep D from NS and Associates. Please go ahead.

**Sandeep D:** Sir, I just want to specify actually our carry forward losses which we have been carrying from US operations. Has it been completely written-out or if there is any?

**Krishnan Venkatachary:** No, it is not yet completely written-out.

**Sandeep D:** So, what is the figures are it actually as on December?

**Krishnan Venkatachary:** it is approximately about 90 crores.

**Sandeep D:** And there is another query which I just want to ask Mr. Srikanth. I hope that you would answer this question not in a diplomatic way. Since last years if we going to the promoter holdings, the promoter holdings have been substantially down from the highs of 60s to something around 35%-36%, right now. And there have been reasons for this, I think one of the promoters Mr. Sudhakar, I suppose has almost sold his stake and then they are two ex-promoters were gone public. My query is sir, why is not the other promoter's trying to buy our stake? The reason being is they are just selling out in the open market as and there is no tomorrow. And then it is just hurting the investor sentiment. And suppose if the promoters are not keen to add into it then we have been seeing that they have been investors meet and then they have been road shows. If I am not wrong, sir according to my calculation I think Cigniti right now is under PE 9 or 10 whereas; the industrial average is 22-23. It is a mouthwatering level if we looking to this. So, I am just not able to figure out why there is no

big investor coming into the company? Or are there any surprises in the cover which I am not taking into consideration, sir?

**Srikanth Chakkilam:** So, first thing as promoters we would love to add more of us stake into the company. But we really cannot control to whom they want to sell and if they want to sell in the market that is something that really we cannot control.

**Krishnan Venkatachary:** Yes, I will just take up this question, gentleman. I wanted to tell you very clearly is that promoter holding over a period of time. The history of why the promoter share has come down systematically is also on account of the ESOP issued to employees about 5 years back and this has been close to 10% of the equity at that point of time and which is got vested over a period of time. So, ultimately the total outstanding equity for the promoters which is an erstwhile acquired from Cigniti which is Sudhakar and Kumar as a family together. Kumar and family, Sudhakar and family and Mr. Subramanyam and Srikanth as a family, they were splitting at about 24%-24%. Mr. Kumar and family regrouped themselves out as a non-promoter sand so the holding came down to 37% which currently holds at about 36% or so still held by Sudhakar's spouses name clearly. If you look through, we are in definitely in dialogues with them, asking them to really come out and speak to the market in terms of trying to get the deal done. But I think sometimes it so happens that on some emergency or at their need probably they are trying to get through and liquidate. But I did not see any big quantity is coming though into the market. Previously they have negotiated some deals and they have done some bulk deals to that you are up about 2% of the equity which has gone into some institutions hand. There is a consistent effort from our side but as far as I am talking on behalf of the current set of promoters in terms of acquiring the shares. A wishful thinking is there over the next 24 months in terms of whatever possible but I think it all depends on their personal finances as well because they have put their energy and money completely on this company and they are moving ahead clearly. So, as and when the right occasion arises for them I think, they will be dealing with this definitely. But I do understand your concern, we are also definitely making efforts in terms of speaking to them and making them understand that what the business is all about and how it is.

**Sandeep D:** The reason why I am pin pointing is because we have been posting very good results in class IV quarters, wherein as an investor we are not getting the returns as far as the results going through. So, I just wanted to figure it out how much times will it take?

**Management:** So, that is really not in our control. We cannot estimate any time.

**Sandeep D:** Another query is sir, it is regarding Mr. Phaneesh Murthy sir. Sir, role is Mr. Phaneesh Murthy has been assigned to?

**Srikanth Chakkilam:** Phaneesh Murthy is an independent Director and he is also an advisor for the company.



**Sandeep D:** So, he is not into getting orders, sir?

**Srikanth Chakkilam:** No, he is just an advisor and an independent director.

**Moderator:** Thank you. We have the next question from the line of Tejpal Jain from Suruchi Investments. Please go ahead.

**Tejpal Jain:** So, I have only one question here, is the company looking for a normally growth in FY20?

**Srikanth Chakkilam:** This is something that I answered in the previous quarter also. So, we usually have a year to the ground and this is something nobody can commit to.

**Moderator:** Thank you. As there are no further questions, I would like to hand the conference over to Mr. Srikanth Chakkilam for closing comments. Please go ahead.

**Srikanth Chakkilam:** Thank you everyone for participating in the call. I look forward to a wonderful Q4 and meeting you all next time in the next earnings call, thank you.

**Moderator:** Thank you, gentlemen. Ladies and gentlemen, on behalf of Cigniti Technologies Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.