Datamatics Global Services Limited
Q1 FY21 Earnings Conference Call

September 14, 2020

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MODERATOR: **MS. ASHA GUPTA, CHRISTENSEN IR**

Moderator: Ladies and Gentlemen, Good Day and Welcome to Datamatics Global Services Limited Q1 FY21 Earnings Conference Call. As a reminder, all participants' 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 '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Ms. Asha Gupta from Christensen IR. Thank you and over to you, Madam.

Asha Gupta: Thank you, Aman. It gives me great pleasure to invite all of you for the Q1 FY21 Earnings Call for Datamatics Global Services Limited. The results and the investor presentation have been mailed to you and is also available on our website, www.datamatics.com. In case anyone does not have a copy of the press release, please do write to us, we will be happy to send the press release and presentation to you all.

To take us through the results today and to answer your questions, we have with us top management of the company represented by Rahul Kanodia, Vice Chairman and CEO; Sandeep Mantri, CFO; and Mitul Mehta, Senior VP and Head of Marketing and Communications. We will start the call with a brief overview of the quarter given by Rahul which will then be followed by financials given by Sandeep. We will then take the Q&A session.

The normal safe-harbor clause applies, with that said, I now hand over the call to Rahul. Over to you, Sir.

Rahul Kanodia: Thank you, Asha. Welcome and thank you everyone for joining our Q1FY2021 earnings call. This is our second earnings call and we are glad to have all of you on the call today. I hope that all of you and your families are safe in these challenging times.

The world has changed significantly since we last spoke. We pray for everyone who has been impacted by the COVID either they have lost a few loved ones or they have lost a livelihood. While the pandemic is posing significant medical and economic challenges, it is making the world united as well. We should be forever grateful to the medical professionals, which is delivering very well under the current crisis situation.

Most of the economies are not doing well. India has contracted almost 24% in Q1 and likely to contract more than 10% this year. The US has also contracted about 9% in Q1 and is likely to contract significantly for the full financial year. Almost all major and minor economies in the world are facing this problem except China, which for obvious reasons we cannot rely on their published data.

During this time, our key priorities remain at Datamatics:

- Ensuring the safety and well-being of our employees. Majority of our employees are working from home

- Retaining and servicing customers, having more meaningful engagements with clients during these difficult times
- Cyber security and data privacy for our customers
- Maintaining sufficient liquidity, focus on cash flows and cost reduction wherever possible.
- I would like to assure that every Datamatician is working relentlessly to deliver our services and commitments to all our stakeholders

As a socially responsible corporate, it has always been our endeavor to associate with causes that benefit the community. As part of this philosophy, we helped the BMC manage their migrant worker crisis setting up an emergency digital call centre and collaborate it with NGOs to provide food and supplies to over 6.5 lakh citizens. Additionally, we set up a data analytics cell that give real-time insight and updates on the ground situation to BMC officials. We also adopted a slum in Andheri, Mumbai, and that catered to the needs of almost 1000 families.

We announced our Q1 FY21 results on September 10th detailing out our operational performance. For those of you who have joined the earning calls for the first time, I would like to brief you as to what we do as a company before we go into the financial results.

We are a global information technology business process management and digital solutions company building intelligent solutions for data-driven businesses, to increase productivity and enhance customer experience. The two key areas for our focus are IT services and BPM services.

IT services constitutes 56% of our revenues and within that we have application management, enterprise document management, and digital solutions which of course includes robotics, enterprise, mobility and cloud. Under the cloud, we help customers migrate their businesses from legacy environment to the cloud. Here, we have partnered with Amazon Web Services and have also hosted several of our products such as TruFare, TruBot, and TruBI on the cloud. On the mobility front, we have built several applications for leading e-commerce companies and aggregators, artificial intelligence, which is focused on deploying AI within our products. Intelligent automation and robotics is growing at about 57% per annum globally and this is a very important focus area for Datamatics. We have recently launched TruBot 4, which is our own robotics product and we have built into this TruCap+ which is an integrated cognitive capture module. We are getting very good response on the market since the launch of this product and we will continue to invest in building our robotics product. One major focus area under IT services is automatic fare collection. We are the only Indian company with a very strong footprint in this space and have been in this space for the last 20 years. Here, we have our own product called TruFare that has given us significant advantage in the market. To-date we have done over 27 AFC projects globally and two projects are currently ongoing.

Now, switching to another focus area, which is business process management which accounts for 44% of our revenue. Here, we focus on content management and publishing, financial transaction processing, and customer management. We do content management for publishing and e-commerce companies and the next larger area for us is the back office of banks and insurance companies where we do a fair amount of data processing for these organizations.

In terms of our geographical footprint, the US comprises 54% of our business, Europe is 18%, India is about 20%, and the rest of the world is another 8%.

In terms of the industry footprint, the largest segment for us is BFSI, which comprises 29% of our revenue, publishing and e-retail which comprises 25% of our revenue and technology and consulting which is 22%, manufacturing 5%, and all the others put together are the balance 19%.

Our client concentration remains healthy, the top five clients contributing 25% of our revenue, the top 10 contributing 35%, and the top 20 contributing to 48% of our revenue. This is more or less similar to last year, so we have not seen any major shift.

The pandemic continues to add considerable uncertainty and headwind, however, our goal is to manage what is within our control, continue to invest and not lose sights on the long-term opportunities in digital automation, and I am delighted of the Datamaticians response into these difficult times and the commitment towards work. Our employees have come together to innovate and adjust global business opportunities and scenarios that we have never really experienced before.

Each area in which we operate is grappling with structural changes owing to the advancement in technologies, changes in consumer percentage, macroeconomic factors created due to the pandemic. We have built strong customer relationships and a solid foundation over the years. I believe that this provides us a competitive leverage to focus on customers, understand their business priorities, align strategies as per their business requirements, and help them navigate through the current situation. We have extended free use of three bots under the COVID-19 enterprise support program until September 30, 2020. I believe the pandemic will serve as a catalyst for growth for outsourcing businesses as the need for the cost reduction will be felt far more than ever before. We remain confident that the market will provide us opportunities for digital companies like us for exponential growth.

With this, I will now hand over the call to our CFO, Sandeep Mantri. Sandeep, over to you.

Sandeep Mantri: Thank you, Rahul for the business update. Good Evening to everybody on the call today and I thank you for joining our Q1 FY21 earning call and hope you are healthy and safe at your places.

Let me start with the key financial number for the quarter ended on June 30, 2020, so our net revenue came in at Rs. 277 crores, which is 4.5% drop from last year same quarter. The reason for the drop was twofold, one is we have a subsidiary which we have divested in last quarter, so about 1.8% drop in revenue was because of the subsidiary and the second one was the impact of COVID on our Quarter-1 revenues, which is approximately 7% on the top line. When we compare with the last quarter i.e. Q4FY20, we have a decline by 10.7%, but last quarter have a seasonable revenue of tax processing which is about 5%, so in reality we have declined by about 5.7%. Out of 5.7%, again 1.8% is because of the divestment in last quarter and remaining 7% is because of COVID on the top line, so this is all about revenue. on revenue segment from IT segment we have Rs 156 crores and from BPM segment we have Rs 121 crores in this quarter.

As far as our EBITDA margin is concerned, we are at 10.3% as compared to 9.1% in the last quarter and as compared to 12.2% in the previous year quarter, so despite decrease in the revenue, we were able to deliver a good EBITDA due to strict cost control measures, we have taken many measures to contain our cost, which I will come to later on.

Our adjusted profit before tax for the quarter was Rs. 19.6 crores as compared to Rs 27.4 crores in the same quarter of previous year and Rs 25.8 crores in the last quarter. Our effective tax rate remains at 28.2% as compared to 23.6% in the last year quarter and 24% in the last quarter on adjusted profit. Our diluted earnings for the quarter was Rs. 2.29 per share in this quarter versus Rs 3.26 in the last year quarter and Rs. 1.96 in the last quarter.

As of June 30, 2020, our liquid position, our total cash and liquid investments stood at Rs 232.8 crores and we have a debt of around Rs 58.8 crores, so this results into a net cash of Rs 174 crores as compared to Rs 124 crores in the last quarter. This shows a significant increase of Rs 50 crores over March quarter, so in this quarter we have repaid a debt of about Rs 38 crores during the quarter and looking at our healthy liquidity now, we plan to repay most of our borrowings before the end of September ’20 and we will be largely a debt-free company. As far as our receivables are concerned, in March ’20 we were at 83 days in terms of DSO. In this quarter, we have significantly brought down the receivables and now we are 76 days DSO as at June 30, 2020, so we have a marked improvement in our days sales outstanding.

As mentioned by Rahul, from financial perspective we have three key priorities, one is liquidity, another one is cash flow, and third one is cost control. All these are remaining our top priorities, so if you see our cash flow from operations continues to be healthy. As against EBITDA of Rs 28.6 crores for the quarter, we have generated operational cash of Rs 51.2 crores during the quarter and that has resulted into a significant increase now in our liquidity position.

As far as cost control efforts are concerned, we have taken many measures. We have released two offices in India and one office in Philippines in last few months. The effect of those will be seen after Q2 once the notice period gets over for those offices. We are investing more on our IT capabilities, which enables us to execute efficient work from home wherever feasible and practical.

I am pleased to inform you that we have added 10 new channel partners during the quarter for our product business, so now we have 125 partners in total as compared to 115 partners as at the end of March quarter, and we will continue to strengthen our channel partner ecosystem as our long-term growth strategy.

As mentioned by Rahul, the pandemic continues to create uncertainty and thus we have decided not to give any annual guidance for the fiscal 2021.

I will now pass on the call to operate to open the floor for questions. Thank you very much for your patience and appreciate your continued interest in Datamatics.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. The first question is from the line of Rajendra Gupta as an Individual Investor. Please go ahead.

Rajendra Gupta: Good Evening Sir, we are the investors, our family is the investor in Datamatics since IPO days. We have higher respect for the Kanodia family and their expertise in the field, but we have a small regret since IPO days the shareholders did not get any return at all. Our employee strength have grown up four times, the sales have gone up several times…everything is fine Sir, but the returns for the shareholders is bit disappointing. On the last concall, you have promised us to tell us about buyback?

Rahul Kanodia: So we did discuss the options of buyback and then we decided that in the current situation it was very critical for the organization to contain and maintain its cash reserve, otherwise, it would put stress in the company, and therefore, we decided not to do a buyback. The buyback in itself is a fairly complicated process and it would take several months and with the uncertainties that presented itself, the Board decided that it may not be the wisest move to do from the point of view of maintaining sufficient liquidity in the organization because to compete in the market, we need to be fairly comfortable.

Rajendra Gupta: Because as you said in the last concall, taxation problem can be sorted out with buyback and another thing is the value , I mean numbers will improve but I am not saying for the full amount of liquidity and all of course Management would be having a reserve, I do not say no, however my request is to consider this?

Rahul Kanodia: Sure.

Rajendra Gupta: Second is recently China applications are banned in India like TikTok, Zoom, these kind of applications can we expect anything from, are you planning anything from Datamatics, Sir?

Rahul Kanodia: No, we are not planning anything from Datamatics because these are very consumer heavy applications and Datamatics focuses on business to business kind of applications and for consumer-heavy applications, the spend on marketing has to be very extremely high and Datamatics does not service that segment, so I do not think as a company we understand consumer marketing and we rather go to large corporate where each transaction is a few crores of rupees versus going through a mass scale consumer where each transaction maybe a few dollars, and also then for us to build such applications it will take at least a year or two by the time the market has moved, so we do not plan to focus on such a heavy consumer centric market.

Rajendra Gupta: Okay, and one more question Sir, regarding investors and shareholders, Sir, there was a detailed report on Datamatics by Dr. Vijay Malik, I have gone through the report particularly there I have noticed one point that is regarding the purchase of Datamatics Staffing Services Limited which was bought at a valuation of Rs 15 crores at 51% which made hardly a profit of Rs 7 lakhs plus here, and this was bought from the family-owned business this was the concern and this kind of reports being circulated Datamatics to coming with any positive points about Datamatics I know that the company has to attract the investor side, I am sure you must be knowing about that report?

Rahul Kanodia: No, I am not familiar with the report that you are referring to, nevertheless, I shall try to get my hands on it and read it, having said that Datamatics Staffing Services does IT what is called professional services and that is the focus area, they have got some good marquee customers. The reason the valuation was so high is that and if you notice in the same report, I am assuming the report would have done an analysis, we have not acquired the entire company, we only acquired about 51% of the company. The reason is that the company has some surplus real estate which is not required, so as the real estate gets divested from the company, the balance money would be paid out, so our intent was to acquire the business and not the real estate, and therefore, we did not acquire the entire company.

Rajendra Gupta: My question was about the valuation and profitable income?

Sandeep Mantri: The valuation of this equity comprises of two parts, one is business valuation and another one is the property which company owns, so there is some portion of value which goes into this real estate which Rahul is referring and there is some portion of valuation which goes into the business. Having said that, during this unfortunate time and after March, businesses are down because of covid, so this may be one of the reasons whatever report you are referring maybe highlighting this, I can only say that valuation is fair and valued by a competent registered valuer .

Moderator: Thank you. We have the next question from the line of Amar Maurya from Alpha Accurate Advisors. Please go ahead.

Amar Maurya: Sir, my question is not specific to this particular quarter and I am new to this company, so probably pardon if I am asking some basic questions also, Sir wanted to understand that I think there were some divestment we did of the subsidiary, so now how the business is divided into the services and the product business, and secondly, like you know which part of the pie is going to grow from here on in terms of the accelerator for the growth, and third Sir, if I see the overall profitability of the company and relative to the peers or relative to the overall IT universe, we are relatively at the very lower level of margin, so now since you know we talked about cost efficiencies, we also talked about the turnaround in business, so if you can give me the road ahead for the profitability and for growth and how the business will look going forward?

Rahul Kanodia: I will answer both the questions, first one is about the subsidiary. We have not divested the subsidiary, we have created a subsidiary which is a 100% subsidiary for the product business, particularly in robotics. The reason it is created separately is that the whole functioning of that organization has to be slightly different when you sell licenses and things like that and focus on marketing. The services company profile is again very different, so we have created a subsidiary, it is a 100% subsidiary and we plan to do our robotics business from that subsidiary. The services arm will continue to be in Datamatics, which is the parent. Now, in terms of profitability, couple of things, so once the products really starts taking off, we will have non-linear growth because in the product business it is not headcount dependent, so therefore that will contribute substantially to the profitability and improving the profitability. Second is that we have started implementing a lot of these robotics in our own internal operations, and therefore, getting operational efficiencies, unfortunately this covid has hit us, but nevertheless we will see that the operational efficiency coming in very soon. The third is that we started weeding out select low margin projects where if the margins are low, we are choosing not to continue servicing those customers, so in a very steady way we are eliminating or not renewing those contracts, and therefore, you should see profitability improvement in the next two quarters.

Amar Maurya: Okay, so Sir like any let us say, I am not asking for the immediate, but any long-term target like in ’2022 or ’2023 for reaching a certain ROCE level?

Rahul Kanodia: That is a good question and I will have to come back to you with an answer. For this year, we put a pause on some of these things because we were focused only on this year because of the covid situation and now that we have that pretty much under our belt, we know where it is, there is some sense of stability that is come in again, we will now look at the planning. We have to revise the numbers, we could not go with last year’s numbers because that was pre-covid, so we will look at these numbers and come back to you.

Amar Maurya: Sure, Sir my last question was on the growth part, because what I understand here is that product business obviously it is a profitable business and it is a non-linear business, but it is also a slightly high gestation period kind of a business model that basically it takes time to enter into the clients kitty to prove the credentials, so how do we see that the growth in the overall business including the product as well as the services business in a longer term, I am not asking about the guidance part, but how the overall pie to look let us say today it is at and down the line three years or two years, the product business will be this percentage of revenue?

Rahul Kanodia: Today, for practical purposes one can imagine that Datamatics would be 100% services although we do have a small footprint in products, but it would be largely all services. I think in the next three years or so we should see anywhere in the range of 20% to 30% revenues coming out of products. Having said that, both services and production both will grow, so it is not that the services is not growing, so we will have a healthy growth in that space as well.

Amar Maurya: Okay, but is it fair to assume that the product business you are at verge of where the product business will grow exponentially versus the services business because if I say 20% kind of, so basically we are talking about at least Rs 250 to 300 crores kind of a revenue coming from the product business in the next three years?

Rahul Kanodia: We have, in the last couple of years, invested in building these products. These products have also been featured by several analysts in their reports, so I think we have come a long way and now we will be sort of converging several of these opportunities that we have in the business, so you are right and the last three or four years of investment will now start paying off.

Amar Maurya: Okay, this would be like largely the BFSI, if I see the product mix, it would be catering to like if you can give me some industry this kind of thing?

Rahul Kanodia: We have multiple products, many of them are horizontal, so they service multiple industries, so robotics goes into logistics, hospitality, BFSI also, manufacturing, several of those. Our products in fare collection which is very vertical focused is around automatic fare collection with tickets, so that was into the Metro business, the monorails and the Metros that are coming up. The other one is around BI and analytics, again that is industry agnostic and it goes to multiple industries, but Datamatics footprint is the largest in BFSI, so it would be natural to imagine that a lot of these products would be sold into the BFSI segment.

Moderator: Thank you. The next question is from the line of Rahul Singh as an Individual Investor. Please go ahead.

Rahul Singh: Sir, my question pertains to the current environment, so in the current challenging environment, are we seeing any kind of nudge from the clients in terms of pricing etc. which may going forward that will impact our margins, so do we see any such kind of threat going forward if this kind of situation persists?

Rahul Kanodia: We have not seen too many clients come back with pricing pressures there have been some, some clients have come back saying we need reduced prices, but most of the clients have not done that. However, more clients have scaled down their operations because they were also impacted and because they were impacted, they had to reduce the business that they were outsourcing to us, so we saw more of clients reducing the business and few clients reducing price, so pricing pressure we did not see too much, there is some of it, but not too much.

Rahul Singh: With respect to your presentation, you talked about net cash in your books, so are there any plans to use this net cash in terms of special dividend or may be thinking of some kind of M&A or anything else acquisitions or as you told earlier will be only used to tide over this current crisis?

Rahul Kanodia: We keep looking at M&A opportunities and we tend to be opportunistic and select M&As that are sweet deals, so we have used cash for all the M&As that we have done in the past. We continue looking at that, having said that there is no M&A deal that is on the table right now In terms of dividend declaration, a lot of this money as we mentioned in the last call as well is in subsidiaries and many of them are overseas and bringing those monies into India would mean declaring layers of dividends and that would be very tax inefficient, so having done that we are seeing how to simplify the structure, but yes but we will conserve the cash and we keep looking at M&A as the opportunities present itself.

Moderator: Thank you. We have follow-up question from the line of Amar Maurya from Alpha Accurate Advisors. Please go ahead.

Amar Maurya: Sir, thanks a lot for the opportunity again, so as you indicated that growth is going to come from both services as well as from the product business, what I am trying to understand here probably not from the quarter perspective but from the overall strategic perspective, if I see the overall growth for the company from FY'15 to FY'19, I mean you were at Rs 800 odd crores top line at that point of time and in FY'19 also we are at Rs 1000 or 1100 crores top line and barring Rs 1200 crores top line, so if I see this growth relative to the overall peers or even the mid cap IT, probably we have missed somewhere something, so exactly what we are now realigning and is this now in the new 'Avtaar' that Datamatics is going to become more aggressive, fully growing company than relative to what we had seen in the history, so where we are changing if you can help us understand?

Rahul Kanodia: Three things, one is that you rightly pointed out that the growth has not been as aggressive with the recent past in the last four or five years and that is because some of our subsidiaries where we had invested and where we did not have 100% equity, they were sort of not delivering up to par, in fact they were struggling and we struggled with them for a while, so we have sort of taken a decision by and large to have any subsidiary that will be a 100% subsidiary and there will not be so to speak joint-ventures, so our joint ventures have not really delivered and they have not grown at the same level, and therefore, you see the growth being subdued, so that is in the last four or five years. Going forward, we are trying to sort of clean that structure up. The second thing is that we in the last three or four years have focused on building these products, so as we take these products to the market, I think we will see growth coming. In fact that should come with the higher profitability, so that is on the product side and the third thing that we have done is also focused heavily on the new emerging trends, which is around cloud and mobility and robotics what is called digital, so we have spent a fair amount of effort and we have got a very good practice in that space, and these are the hottest things in the market, so I think we are now well positioned to capture the opportunities of the market presents to us, so given these three or four things, I have felt bullish that we will have a good growth going forward.

Sandeep Mantri: Adding to Rahul, we are actually creating an ecosystem for this product distribution as well which is called channel partner which will also drive to some extent our growth in the business, so that is a part of our core strategy for selling the products in the market.

Amar Maurya: Got that, then this product ideally, we will be targeting in the international market or also it will be sold domestically?

Rahul Kanodia: Both.

Amar Maurya: Okay, but our larger mix would be international, right?

Rahul Kanodia: Yes.

Moderator: Thank you. The next question is from the line of Rahul Singh as an Individual Investor. Please go ahead.

Rahul Singh: Thank you for providing the opportunity once again, just one more question in my mind regarding the Cignex business, what is happening on this Cignex thing, could you please provide some kind of update, the timeline of the presentation so whatever is happening in that particular line?

Rahul Kanodia: Sure, so if you go back into history, there was a SPA that was signed and then the Board had approved this and shareholders voted against it because the shareholders felt they would prefer to have a very different kind of a structure versus a share swap deal, so since then we have been in dialogue and we are trying to talk to different entities to see whether we could divest it or we roll it into the company and make it a 100% subsidiary, so one of those two options is happening, we are currently evaluating all these options, so right now it is not quite clear as to which way it will go.

Moderator: Thank you. Ladies and Gentlemen, that was the last question for today. I now hand the conference over to the Management for their closing comments. Thank you and over to you.

Rahul Kanodia: Thank you everyone for being on this call. We really appreciate the time that you spent with us and asking us questions. If you have any further questions, we will be happy to get into more detailed answers. Overall, we are very bullish about the opportunities that present themselves and the prospects for Datamatics and I am fairly confident that the next year or so, we will see those results coming out once we tide over the current covid crisis, which I expect another six months we should be over it, not completely but at least we will have come out of the major lockdown that we have had and start seeing a good growth going forward, so thank you again for being on the call.

Moderator: Thank you very much. Ladies and Gentlemen, on behalf of Datamatics Global Services Limited, that concludes today's call. Thank you all for joining us and you may now disconnect your lines.