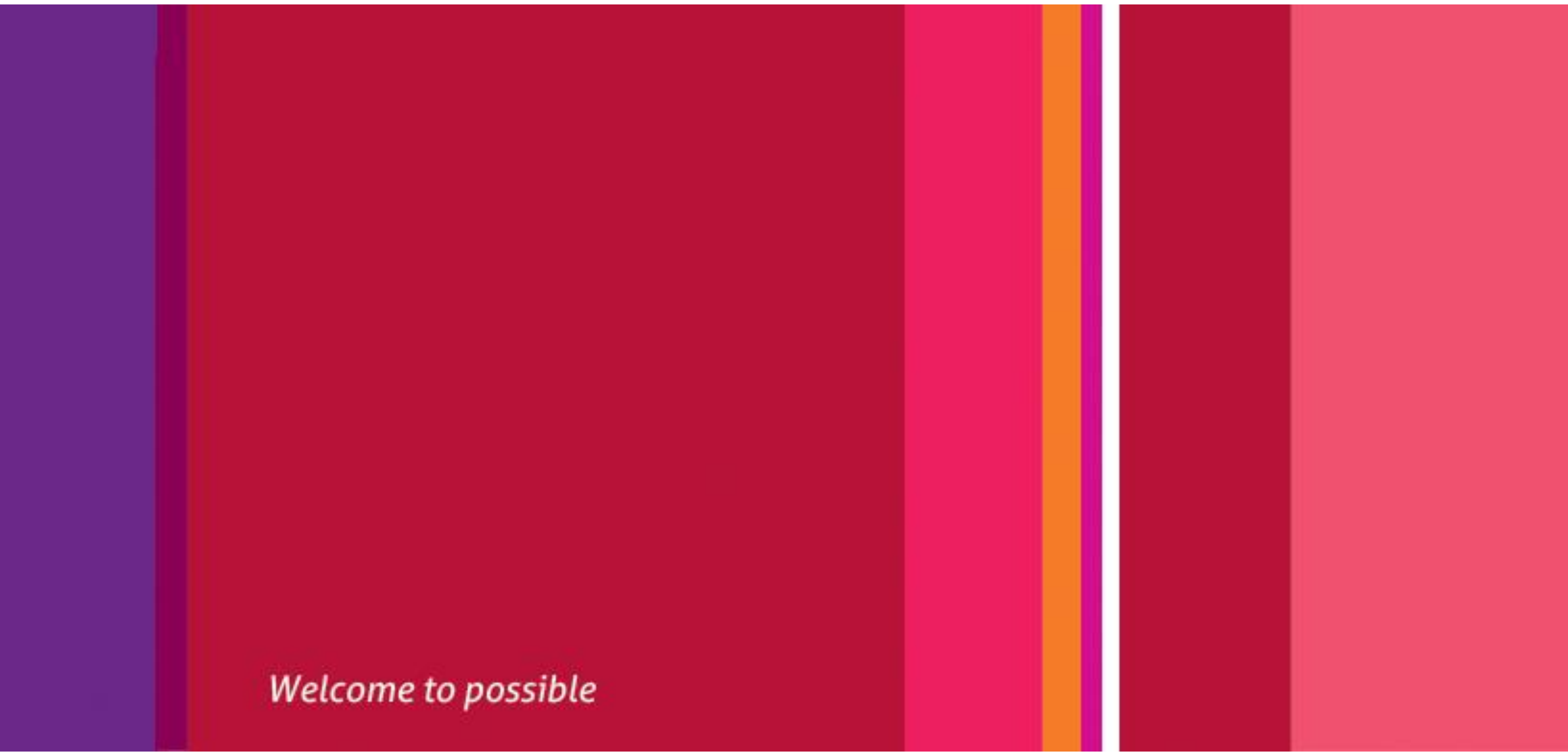
Mindtree Limited

(NSE: MINDTREE, BSE: 532819)

Transcript of analyst call

Third Quarter ended December 31, 2017

January 17, 2018



Moderator: Ladies and Gentlemen, Good Day and Welcome to the Mindtree Limited Q3 FY '18 Earnings Conference Call. 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 '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Sushanth Pai. Thank you and over to you, Sir.

Sushanth Pai: Thanks Stanford. Welcome to this Conference Call to discuss the Financial Results for Mindtree for the Third Quarter ended December 31, 2017. I am Sushanth, Head for Investor Relations. Before we start the proceedings, I would like to wish you all a very Happy and Prosperous 2018.

On this call, we have with us senior management team,

Krishnakumar Natarajan – Executive Chairman;

Rostow Ravanan – CEO and Managing Director;

Parthasarathy N. S. – Executive Vice Chairman and COO;

Jagannathan C N – CFO.

The agenda for the session is as follows. Rostow and Jagan will begin with a brief overview of the company's performance after which we will open the floor for the Q&A session. Since we have introduced an audio webcast, some of you may have joined the webcast. The webcast is a listen-only mode, but you can post questions. We will take the webcast questions once we complete the questions through the conference call mode.

Please note that this call is meant only for the analysts and investors. In case, there is anyone from media, I request you to please disconnect as we just concluded the media briefing before this call.

Before I hand over, let me begin with the safe Harbor statement. During the course of the call, we could make forward-looking statements. These statements are considering the environment we see as of today, obviously carry a risk in terms of uncertainties because of which the actual results could be different. We do not undertake to update those statements periodically. I now pass it onto Rostow.

Rostow Ravanan: Thank you, Sushanth. Good evening to all of our friends from the investment community on this call. Let me also start by wishing all our friends in the investment community, a very Happy and Prosperous 2018.

Coming to our results for the quarter:

We are very happy to share that our Q3 revenues came in at $214.3 million, which represents a QOQ growth of 3.9% and 11.5% growth on a YOY basis. On a constant currency basis, our QOQ growth was marginally higher at 4%. This has been our best Q3 performance since 2011 in spite of the seasonality associated for this period. Our Execute Smart approach to delivery continues to bear fruit and contributed to a robust quarter on all fronts.

Breaking up our financial performance by verticals:

Most verticals showed good momentum and growth in this quarter. The Travel industry led the growth with 9.3% compared to the previous quarter, Retail, CPG and Manufacturing grew by 5.8%, and BFSI grew by 3.7%.

Looking at our results from a geography perspective:

US business showed a very good growth of 7.3% in this quarter. Digital grew 7.1% in this quarter and 24.2% YOY, which indicates our strong market positioning on digital. Amongst the other service lines, independent testing led the growth in this quarter with 8.4% on a QOQ basis and 11.7% on a YOY basis. At the end of the quarter, we have 344 active customers.

We added 28 new clients in Quarter-3. Our Top 10 clients have shown a good growth of 8.3% QOQ and 15% YOY. Trailing 12-month attrition has fallen to 12.6% compared to 13% last quarter. Quarterly annualized attrition is slightly higher at 13.2% compared to 12% in the previous quarter. At the end of the quarter, we have 17,200 people. During this quarter, we had a gross addition of 857 people at our lateral level and 473 campus graduates joined us in this quarter.

This quarter also saw some very strong multi-year, multi-million dollar wins in our sweet spot, some of the wins include providing digital transformation, quality assurance, and technology operation service for a leading industry association in the education sector in the US, providing managed services for a leading technology company.

We are also proud to be chosen as the anchor digital partner for an enterprise wide transformation initiative for a large beauty care company. We won an order to implement ShotClasses, Mindtree's employee training and micro-learning platform for a leading consumer goods company. We are also engaged to migrate SAP, ERP and BI solutions to SAP Hana for a large commercial vehicle retailer in the US.

Coming to the outlook:

We signed contracts worth $244 million in Q3 of which renewals were $187 million and new contracts were $57 million. Contracts to be executed within one year was $206 million and greater than one year was $38 million. Digital contracts during this quarter was $132 million. We continue to see strong contract closure and pipeline growth. For Q4, revenue growth is likely to be in the similar range of what we saw in Q2 and Q3 of this year, therefore, we continue to be on track for high single digit growth for FY '18 on a Mindtree consolidated basis.

With that, I am handing over to my colleague, Jagan, to share a few other financial highlights.

Jagannathan C N: Thank you, Rostow. Good evening to all. Wish you all a very Happy and Prosperous New Year 2018. In Q3, our fee revenue grew by 3.8%, volume dropped by 1.9% and price realization increased by 5.7%. Volume dropped mainly because of leave hours, without this impact, volume would have grown by 0.6%. Price realization increased mainly due to additional revenue generated with some projects moving from transition to steady state. Overall, pricing is stable. We have significant improvement on our EBITDA margin. On a consolidated basis, EBITDA margin are at 15.1% as compared to 11.6 % in Q2. The headwinds in this quarter were as follows: 50 basis points impact on account of salary increment, currency impact of 20 basis points. This was offset by tailwinds as follows: Operational improvement of 180 basis points mainly due to some of our projects moving to steady state from transition phase. Absence of one-time people restructuring cost of 90 basis points, SG&A leverage of 130 bps and absence of buyback cost of 20 basis points. For the quarter, we have a Forex loss of $1.3 million compared to Forex gain of $1.9 million in the previous quarter.

PAT for the quarter has improved to 10.3%, a QOQ improvement of 13.8 % and 44.1% YOY. EPS is at Rs. 8.61 with a quarter-on-quarter growth of 15.6% and 40.4% year-on-year. Our cash conversion has been strong with EBITDA to operating cash flow conversion at 83.3% and EBITDA to free cash flow at 72.1%. Return on capital employed was stable at 24.4 %.

The Board of Directors at its meeting held on January 17, 2018, has recommended an interim dividend of 20 %, Rs. 2 per equity share. Some points on margin outlook for Q4, we will have 385 Campus Mind joining us, we will continue our focus on operational efficiencies and we expect Quarter-4 margin to be stable.

With this, I conclude the updates.

Moderator: Thank you. Ladies and Gentlemen, we will now begin with the question and answer session. We take the first question from the line of Mukul Garg from Haitong Securities. Please go ahead.

Mukul Garg: Rostow, my first question or probably this is more relevant for Jagan was on the realization, you mentioned that there was a movement of projects from early to steady state, but can you give us a sense of effectively what was the size of the project and how much was the impact, because the realization change in reported numbers is quite significant, if you can throw some more color on this?

Jagannathan C N: The projects were sizeable projects, but I do not have the number exactly on how much of the realization was due to this revenue moving from transition to the steady state, Mukul.

Mukul Garg: Okay, but in general because if we look at the onsite pricing and offshore both were up about 5% on average from last quarter, so are we expecting some reversion back to previous realization rate per hour or is this something which will remain stable going forward?

Jagannathan C N: The rates are in the stable environment at present. This quarter the transition was there on the revenue front as well the number of working days are lower compared to Q2, so all these have played a part on price realization improving by 5.8 %. You will not have similar amount of improvement next quarter, but it is in a stable situation at present.

Mukul Garg: Understood, and if I may ask one more question, the second was on the Top 2 to 5 clients, you have seen a very healthy growth this quarter, so should we assume that all the troubles which was there with your clients in Top 5 outside the top client are over now over and going forward these clients will resume a healthy growth?

Rostow Ravanan: Yes, broadly that is our expectation that the challenges we face with some of our large clients where we saw revenue decrease, I think are behind us and we have sort of turned around the corner now and expect to maintain a similar sort of growth rates like what we saw in Q2 and Q3 going forward. The clients that are now continuing as our Top 10 customers now have a lot of potential for us to mine and grow.

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

Madhu Babu: Sir, considering the strong exit rate, so next year can we look at 13% to 15% kind of dollar revenue growth for the company because the worst is behind?

Rostow Ravanan: Difficult to make any comment on it to be honest, one is because we do not give guidance and therefore we do not want to comment on a specific number or a range, but even otherwise I think it is too early, we have been just waiting for feedback from customers and next year's budget, our own plans for next year is not yet frozen etc., so difficult to comment on growth rate for next year at this stage.

Madhu Babu: But implied guidance for 4Q is around 4% quarter on quarter growth, right?

Rostow Ravanan: No, we said it is somewhere in the region of Q2 and Q3, so Q2 was 3%, Q3 was 3.9%, so it will be somewhere in that range.

Madhu Babu: Okay, and Sir I think once again the good momentum in the top account, so how is the market share there and we have potential for further growth because on year-on-year basis almost 30% growth in the top account?

Rostow Ravanan: Our largest customer has grown significantly even over the last three or four years. We continue to have great relationships and seamless delivery, so there is a lot of confidence about future growth potential in that account, however, I do not want to overly concentrate only on that. There is big effort to grow the top 2 to 10 customers and also the top 11 to 25 customers.

Madhu Babu: And Sir, just lastly on the digital side I think some of the larger peers have been showing larger deals in the digital side, so how are the deal size is increasing for us and just on the margins, are we confident that we will be sustaining 15-16% from here on, thanks

Rostow Ravanan: So on digital, yes, we are also seeing the same trend, in fact we probably called the trend ahead of the rest of the industry where digital projects are becoming larger, so we are seeing larger, longer, multi-year and multi-million dollar kind of programs in digital as a market trend, but what is more heartening and more exciting for us is customers are convinced that Mindtree is a great partner for them for those deals, so I think we have two advantages of Mindtree entry positioning resonating very well in a turning market, so as far as the digital question goes. As far as margin goes, we are reasonably confident that we will maintain the kind of revenue sort of margins that we showed in Q3 in to Q4 as well.

Madhu Babu: Okay Sir, thanks a lot.

Moderator: Thank you. We take the next question from the line of Sagar Lele from Motilal Oswal Securities. Please go ahead.

Sagar Lele: Thanks for the opportunity. Rostow, could you probably highlight how the performance in this quarter has been on the acquisitions front both Bluefin and Magnet 360 if you could just give us numbers in terms of both revenue and profitability, and if any of the overall profitability improvement that you have seen in the quarter has been attributed to things getting better here?

Rostow Ravanan: Bluefin was largely flat in this quarter I think maybe $300 or $400K decline over the previous quarter, but I would say largely flat over the previous quarter and I think at a bottom line level, Bluefin made a small loss, so revenue was like largely flat and a small loss at an EBITDA level for the Bluefin business. Magnet had a very good growth over the previous quarter, but still lower than their fixed cost, so the business made a loss at a Magnet level, however, you have to keep in mind that the Salesforce practice and both Mindtree and Magnet as legal entities, so some of our Salesforce revenue are also booked in Mindtree books, so I think it will probably be a breakeven or slightly profitable on a practice basis for Magnet business though from a reported basis, Magnet business reported a loss. At this point of time, I think we are confident that the worst is behind us and very positive on the future outlook for both of these businesses. Going forward, both of them will also get fully integrated into Mindtree, the Bluefin business now both legally and operationally is fully merged into Mindtree. As soon as we receive the necessary regulatory approvals, the Magnet360 business will also be fully integrated into Mindtree, so some of these legal entities based reporting distortions should also go away in one or two quarters.

Sagar Lele: Sure, just a follow up on that, in the last quarter there was 2.2% difference between your reported EBITDA and the EBITDA margin excluding acquisitions, would that gap have narrowed down now or is it still similar?

Jagannathan C N: Yes, it has narrowed down this quarter.

Moderator: Thank you. We take the next question from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria: Hi, Rostow, congratulations on good numbers. Firstly, on the quarter, did the revenue growth surprise positively to you guys and how much of it was led by very better macro or how much of it is led by better execution at the Mindtree level?

Rostow Ravanan: I do not think the revenue growth was a surprise, I think beginning to see a similar trend even at the end of the previous quarter and even if you remember the comments we made at the end of last quarter, we had indicated a high degree of confidence not just for Q3, but also over the next two or three quarters for Mindtree, so I do not think the revenue numbers caught us by surprise. I guess the performance was a result of some extent obviously the improvement in market sentiment perspective, but also a combination of a right strategy, investments behind the right strategy especially on areas like digital etc., so definitely some of those deliberate actions were Mindtree side including if you see this quarter, our independent testing business grew by 8.4% QOQ, which reflects strong deal momentum across both, run the business as well as grow the business kind of projects amongst our client base, so it is definitely a combination of both market sentiment plus also our own actions.

Gaurav Rateria: Sure, second question, how should we read the deal wins data because if you look at the trailing 12 months deal wins, it has declined by around 7% - 8% on a YOY basis and while revenues are growing, so should deal wins be looked as a leading indicator or not necessarily, how do you suggest one should look at the deal win data?

Rostow Ravanan: No, I think the deal win is a metrics that we started reporting based on some good practices that the financial community was sharing with us, so it is a reflection on the kind of business we are winning, so to that extent it will be an indication of growth especially since you are also breaking up and saying what is renewals and what is new contracts there, some of the deliberate actions we are taking is also like I said in 2011-12, we are one of the earliest to call digital as a trend and we are already starting thinking on what is beyond digital, thinking of newer offerings that we will take to clients in the newer model etc., so some of those are also conscious steps that we are taking on our business.

Gaurav Rateria: Sure. Rostow, last question from me, what gives the confidence that we have turned the corner on the portfolio entities, could you share some color on pipeline or any other metric which provides us this confidence, thank you?

Rostow Ravanan: Yes, the pipeline is building up for both our Salesforce and our SAP business not just in terms of Mindtree performance, but many of them are also becoming larger opportunities, so today for example, mid-sized like a $5 billion kind of revenue company that is looking for an end-to-end SAP transformation across our four verticals, we are being considered for like $30 million to $40 million kind of opportunities. We have not won any as of today, but beginning to see those kind of opportunities for example in our pipeline on the SAP business. Similarly, continuing to see larger pipeline increasing deal sizes etc. even for our Salesforce business, so all of those are the reasons why we are confident of the future. Apart from that, whatever steps that we needed to take in terms of integration, people management, systems integration etc., all of those are also proceeding on plan, so that is another reason we believe some of these issues are behind us and are confident about the future.

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

Rahul Jain: Hi Sir, firstly just a clarification, you said Q4 revenue outlook so the 3% to 4% range that you highlighted is it for volume growth or revenue growth?

Jagannathan C N: Revenue growth.

Rahul Jain: Okay, what was the volume growth on like-to-like basis as you said, the impact was for lower number of working days?

Jagannathan C N: Q3 volume was on decline of 1.9% compared to Q2.

Rahul Jain: Yes, but you said this is mostly because of lesser number of working days?

Jagannathan C N: Combination of employees taking leave, customers enforcing furloughs, and also lower working days.

Rahul Jain: Yes, so on a similar number of days basis what it should have been?

Jagannathan C N: 0.6%.

Rahul Jain: Positive.

Jagannathan C N: 1.9% decline would have been a 0.6% increase.

Rahul Jain: Okay, also if I see the revenue client buckets, the Top 10, the Top 25, not Top 10 but $10 million and $25 million, these client buckets are not showing any increase, rather it has come off and we are seeing a very spectacular growth in the Number one account and possibly Number two also which is driving the top 2 to 5 metrics as well, so is it that the growth is now coming from fewer clients much more faster versus total portfolio as a whole?

Rostow Ravanan: Not necessarily, if you look at our Top 10 clients as a whole have grown faster than Mindtree in this quarter and so more than one account has grown and you also have to keep in mind that the constituents of the Top 5 or Top 10 today are not the same of what we had one year ago or two years ago, so there is also a shift in the composition of the accounts, so that makes it difficult to compare like-for-like, but the underlying fact is those accounts which are in our top customers right now all have huge growth potential and all have shown good growth in this quarter.

Rahul Jain: Okay, and on the pricing you said this is because of some project moving from transition to steady state, is it something related to some seasonality because we see a similar pricing jump in last year same quarter, is it some way to do with that or specific for this year?

Jagannathan C N: No, this has got nothing to do with any previous year's performance, it is a reflection of how our business shaped up in this quarter.

Rahul Jain: Is it like there is some milestone payment that gets highlighted once it reaches certain stage?

Jagannathan C N: No, like we have explained in the past and like what is common in our industry, transition phases are built differently compared to steady state phases because during the transition time, the customer is paying to multiple vendors, so transition pricing is usually lower than the steady-state pricing so as the work gets picked up and it moves into steady state, revenues are higher.

Moderator: Thank you. We take the next question from the line of Ankit Pandey from Quant Capital. Please go ahead.

Ankit Pandey: Thanks for taking my question and a very Happy New Year to everyone on the call. My question would be on the sustainability of the growth momentum, we have seen some of the headwinds as you have indicated just now, just sort of tied over for a little bit and you did mention in the middle of the conference call or in the middle of the Q&A session that you expect a Q2, Q3 like 3 to 4 percentage sequential like momentum going forward, that would indicate well above single digit growth year-on-year basis, so on one hand I want you to confirm that whether you meant it that way, but on the other hand what gives us the clarity and a clear vision, is some of our pipeline conversion and things like that, could you speak on some of those lines, please?

Rostow Ravanan: I think most of these issues were covered in previous question where essentially we did indicate growth in Q4 to be similar to the kind of growth rates we saw in Q2 and Q3 and that confidence is on the back of larger pipeline, faster conversion, improved win ratios for Mindtree all of which is reflected in the good wins that we have announced over the last two or three quarters, so that is what gives us the confidence of growth for Q4.

Ankit Pandey: Okay, Sir, comment was restricted to Q4, is that correct?

Rostow Ravanan: Correct, but like I said the trend will continue even into the future as well except that I am not commenting on the growth rates beyond Q4, so the estimate of growth was more limited to Q4, but the underlying trend should obviously support us even going forward beyond Q4.

Moderator: Thank you. Next question is from the line of Vaibhav Badjatya from HNI Investment. Please go ahead.

Vaibhav Badjatya: Hi Sir, thanks for providing me this opportunity, so recently we have seen that Google researchers have found some design problems in AMD and Intel Chips the solution of which is going to have impact on processing speed, so I want to ask the question regarding, so in places where we manage the infrastructure on client's behalf, does this likely to have an impact of say, we have to provide for more processing speed to clients and there perhaps some impact on the profitability in some of the divisions?

Rostow Ravanan: I am not sure if I understood your question right, but I think you are referring to some of the announcements from companies like Apple and other chip companies where there were some vulnerabilities in chips etc. that has no correlation or no implication to our business.

Moderator: Thank you. We will take the next question from the line of Sandeep Shah from CIMB India. Please go ahead.

Sandeep Shah: Thanks for the opportunity, congrats on very good execution and Happy New Year to the management. Rostow, I think the question is in terms of the conversion of the pipeline into the deal awards, as you have kept saying for the last two to three quarters that the pipeline is at the historic high, but when we look into the new business wins in this year as a whole or a nine-month, it looks like that it is likely to lag versus what we had in FY 2017, I do agree in FY '17 you had couple of large deal wins, so I just want to understand whether you still believe the large deal wins are sporadic or there is a concentrated efforts for you to say that the large deal wins will continue going forward which gives the new business TCV also growing on a YOY which also gives us a confidence in terms of a growth visibility beyond Q4 entering into FY 2019, so just your comments on the same?

Rostow Ravanan: The pipeline of large deals is growing, for example, this quarter we won seven deals each of which was more than $5 million, so I think the pipeline of large deals is growing for multiple reasons including the fact that digital is becoming mainstream and customers are investing a larger digital project and extremely confident of Mindtree delivering those kind of transformative projects for them. Even this quarter, for example, I pointed out a new customer who is embarking on an enterprise wide transformative digital kind of a program and has chosen Mindtree as the anchor partner for that. Even if you look at the run the business kind of work is still leading to a large progress, so I do not think the pipeline is a problem. Closure will be by definition sporadic, last quarter maybe I did not close anything, maybe last year we closed one and maybe next quarter if all goes well, we can close one etc., so closure of large deals you know will obviously depend on which quarter they get closed, but pipeline is continuously building up.

Sandeep Shah: Second question is in terms of the margin, so I think this quarter's margin is at a seven-quarter high and you are also saying it would be maintained in the Q4, but just a long-term vision on the margin, you believe still there is a potential to increase it to the historic high at a EBIT level of 15-16% which we used to have which touched even 17% in FY '15 and what can lead to that kind of margins?

Rostow Ravanan: I do not want to comment on a particular range whether it is 15% or 16% or anything higher or lower, but more as a directional statement, I think we are completely conscious of the fact that our profitability is below our own comfort levels right now, all of which is logical and explainable because we made investments, sometimes for example, one or two quarters our acquired entities did not do well etc., so notwithstanding the fact that you know we have good reasons, there is still a deep desire to improve our profitability, so there is going to be a continuous focus both in terms of cost reduction, operational efficiency improvement, and also better management of clients, better realization of prices etc., so multiple factors are being worked upon to improve margins. Once we get to our own sort of mental comfort level, we will then reassess and say what is the future plan beyond that, but at this moment, I think the focus is on trying to improve profitability from where we are and like we have shown even if you look at Q1 this year or Q2 this year in spite of the one off of visa cost in Q1 or the employee restructuring cost in Q2 even in those kind of tough quarters, we still grew profitability, so it is beginning to sort of fall into place now.

Sandeep Shah: Just last thing on the BEAT, the US tax reforms and the Base Erosion Anti-Abuse Tax, any comment where it will affect you positively, negatively or it will help us, and on the wage side is there any balance wage inflation which is pending which may come in the fourth quarter as a whole and last thing I think you have also exposure to insurance clients and in the US I think Hurricane has led to a lot of financial impact for most of the US insurance companies, so will that be a bit of a near-term concern for you?

Jagannathan C N: I will first take the US tax impact, Sandeep. The US tax impact will not substantially impact us, but there will be an benefit from taking a tax credit in India to that extent there will be some amount of benefit flowing to us in future, otherwise on the tax rate front, there will not be any substantial impact for us because we work on branch model. On BEAT provision, it does not have any major impact for us.

Sandeep Shah: What could be the effective tax rate we can actually model, the second question was on wage and third question was on the insurance impact in the US because of the Hurricane?

Jagannathan C N: There is no wage increment due for this quarter other than very, very small amount may be there for some new joinees, but there is nothing there for this quarter.

Sandeep Shah: Effective tax rate, if you can give us some color for years after FY '18 I do agree, just a range will help us?

Jagannathan C N: Yes, it will be between 24 to 26%.

Sandeep Shah: Last question on the insurance, which I asked?

Rostow Ravanan: Currently, like I said we have one large insurance client for whom we are like massive amount of disruption given some of their business priorities there, but other than that for the rest of our clients, we currently not seeing any changes to their priorities etc. because of any of the weather-related impact of the US has seen over the last year, so not seeing that as a specific trend on a broader basis.

Sandeep Shah: Thanks and all the best to the management.

Rostow Ravanan: Thanks, Sandeep.

Moderator: Thank you. Next question is from the line of Dipesh Mehta from SBICAP Securities. Please go ahead.

Dipesh Mehta: Just want to get sense about how we look Calendar '18, whether we find Calendar '18 to be much better than what we have seen in terms of overall demand traction at the beginning of Calendar '17? Second question is about the employee cost, if we look it seems to be more or less flat quarter on quarter despite salary hike given during the quarter, so can you help us first quantify the impact and despite employee addition why it seems to be flattish, if you can answer these two?

Rostow Ravanan: The employee cost over the last two or three quarters has been a combination of like you said some inflows, promotions, wage hikes etc., that is a lot of effort to mitigate cost in terms of rationalization of the pyramid and so on and so forth so both factors work. I think probably we begin to see some amount of benefit also as some of the large digital programs have a larger offshore component, so that will also help us get growth without having to increase our wage costs there, so that is the outlook that we have on wages.

Jagannathan Chakravarthi: Last quarter, there was a one-time restructuring people cost, that is not there this quarter so that is also sort of decreased the employee cost this quarter.

Dipesh Mehta: Can you quantify the salary hike given this quarter in terms of percentage, how much we have given, because it seems to be very low impact only, 50 basis points what we quantify?

Rostow Ravanan: Very small selection of people was covered in this quarter.

Jagannathan C N: That is why it is only 50 basis points impact, the majority of the hike happened in the previous quarter.

Dipesh Mehta: And how we look Calendar '18?

Rostow Ravanan: Overall, like I said our impressions in terms of talking to customers, analysts etc. beginning to see like I said a strong demand environment and improved ability of Mindtree to convert that demand into business for Mindtree, which is our four verticals.

Dipesh Mehta: Last thing about the pricing, I think broadly we are suggesting relatively stable pricing, but if I look our offshore pricing, it is now almost YOY growing at double-digit kind of thing and even if onsite I think both the things, eight to 10 quarters back we used to see pressure on pricing in terms of onsite, offshore, but for last few quarters it is steady uptick kind of thing, can you help us understand what is going on in this, I understand about this quarter specific you mentioned from transition to steady state kind of thing, but broadly if you can help us understand how one should look pricing?

Rostow Ravanan: I think broadly pricing is remaining stable, part of it moved in this quarter was like Jagan explained a few large programs that we were running for clients, they completed the transition phase and moved into steady state phase, and therefore, the realization improved because of it, small amount was also because this quarter had lower working days, on your fixed price and on our fixed price and fixed monthly kind of contracts, you have a higher realization of lower working days to that, so some of those seasonal factors also played in, but I would say broadly the realized rates will remain constant going forward.

Dipesh Mehta: Even if let us say we exclude Q3 kind of number even I go to Q2, our offshore pricing is showing mid-single digit kind of growth trajectory?

Rostow Ravanan: The same trend, all of those transition did not end on single day, right, so it is a beginning of a momentum that we are seeing and to some extent it is also a function of the fact that our offshore price has fell significantly and we got a lot of concerns from the investment community on that fall, and now we are beginning to build that back.

Dipesh Mehta: Whether automation or any other way it impacts your reported pricing?

Rostow Ravanan: No, because if we have done automation etc., it will reflect in improved margins because the pricing is a function of revenue divided by the effort, so automation will help improve margins, will not help improve revenues.

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

Apurva Prasad: Hi, thanks for taking my question and congratulations on strong quarter, so Rostow just to prod further on the margin side, you said fourth quarter to be flattish, how should we really look at it from a slightly medium to long-term perspective?

Rostow Ravanan: I think effort will be to increase it from where we are like I explained to a previous question, we believe we are below our own comfort level and we believe we need to do a lot to improve margins, so I think from a medium-term perspective, the effort will continue to improve margins except that nothing is available for us to increase between Q3 and Q4, but going forward basis we will work on all the levers available to us to improve margins.

Apurva Prasad: Sure, and also within the client metrics in the Top 10, was the growth largely secular or were they driven by fewer pockets, so top account obviously it is very well, but beyond that?

Rostow Ravanan: If you look at our Top 10, many of our accounts in the Top 10 grew, just anecdotally one customer dropped out of the Top 10 from Q2 to Q3 but all the accounts that we ended in Q3 largely many of them had very good growth.

Moderator: Thank you. We will take the next question from the line of Pankaj Kapoor from JM Financial. Please go ahead.

Pankaj Kapoor: Hi, good quarter, Rostow, just a small question again on the realization jump, you mentioned that this was because of the projects moving to a steady phase; normally these kind of things happen in infrastructure or application outsourcing contracts, but if I see your numbers IMS and as well as maintenance seems to be flattish, in fact maintenance is down QOQ, so I am just trying to reconcile these two things with what we saw on the pricing and the comment that you made?

Rostow Ravanan: Pankaj, thank you for your wishes, that is absolutely logical. It is because you are delivering the same revenue with lower efforts that is why the realized rates have gone up.

Pankaj Kapoor: No, you are right, but normally as I said like these would be for contracts on the infrastructure management side or on the application maintenance side, but on those service lines, the revenues have been flattish quarter on quarter or have shown a very marginal increase, so I mean I am just trying to reconcile how the revenue recognition would have happened, so that these two things can match?

Jagannathan C N: Pankaj, I think I will take your question off-line and give you an update on that.

Pankaj Kapoor: Sure, that is okay, second thing is again on this part only that are most of these projects which had this transition phase are they now done or all of them have achieved a steady state?

Jagannathan C N: Sorry Pankaj your question got, your voice was not clear, could you repeat your question again?

Pankaj Kapoor: Yes, what I was asking is most of these projects which are transitioning, are we over with them or are some projects still in the transition phase which can go into steady phase in the coming quarters?

Rostow Ravanan: I think it is largely over, a small percentage will complete transition during the course of Q4.

Moderator: Thank you. We take the next question from the line of Shashi Bhushan from Axis Capital. Please go ahead.

Shashi Bhushan: Thanks for taking my question, congrats, good quarter, Sir. Our one-year executable is still weak, how one should interpret this, some smaller deals that gets closed during the quarter and executed during the quarter do not get captured in this, also what else do not get captured in this number?

Rostow Ravanan: Everything is captured in the number, so whatever contracts we sign in the quarter are aggregated and then reported as per the breakup that we disclose, so nothing is left out. I am not sure if I would call my less than one year to be weak, if you look at this quarter for example out of the 200 + million, larger portion of contract is less than one year, contracts larger than one year was $40 million, so therefore, we are reasonably confident about the contracts less than one year in this quarter, last quarter and even over the last one or two quarters, for our size I think that is a reasonable number of what we have.

Shashi Bhushan: No, if I look at on a trailing 12-month and year-on-year change, it has actually came down, my problem is how to interpret this data?

Rostow Ravanan: I am saying reasonably they are simple interpretation, if you look at last year Q3 for example, we announced a single larger deal in the history of Mindtree, so let us assume it was $100 contract. Now the $100 had a certain portion and let us say that contract is $100 over five years, so it is $20 of one-year contract that got included in less than one-year contract correspondingly we announced last year numbers, so if I do not have the contract this quarter, it will be different. Now next quarter or a quarter down the line, it will win more such business and it will obviously reflect, but if you look at overall, it is difficult to compare like how you are comparing, probably not the right way of comparing as well. Look at how much we are winning continuously and how quickly that is being reflected in the actual pickup in terms of reported quarterly numbers as well, so we announced these last year Q3 and we are starting to reflect in revenues from Q2 to Q3 of this year, so that is the trend that makes sense.

Shashi Bhushan: Sir, very helpful. Another thing on deal pipe and perspective, which are the verticals that are seeing better traction or dominating the deal pipeline?

Rostow Ravanan: At this point of time, Technology Media and Services and Travel and Hospitality have the strongest pipeline. Banking and Retail, CPG and Manufacturing both have I would say medium kind of pipeline, it could be across also, but Technology and Travel are slightly higher.

Moderator: Thank you. We take the next question from the line of Nitin Padmanabhan from Investec. Please go ahead.

Nitin Padmanabhan: Hi, thanks for taking my question, a very Happy New Year. Sir, if you look at the margins, the cost of revenues are lower by 200 basis points quarter on quarter. I understand that 100 basis points is because of non-recurrence of the restructuring cost, but this quarter if I look at it, there is gratuity and compensated absences, these two items put together is a decline of INR14 odd crores which is close to 100 basis points on the margin, I just want to understand these compensated absences, the decline that has been there, is it a sustainable number and should that be something that will eat into margins going forward or is it a sustainable number?

Jagannathan C N: The margin will be at similar level, that is what we have confirmed but between this number, there will be some changes because there are some seasonal impact coming into the numbers also and also like our financial year, calendar year closures as per our policy, there may be some changes happening in that.

Nitin Padmanabhan: So the incremental leverage on margins, if you could just give some color on what are the drivers that could actually sort of move the needle on margins to sustain it if this were to be a headwind going forward?

Rostow Ravanan: I think the compensated absence and gratuity, etc., are quarter-to-quarter kind of an accounting estimate and for example the compensated absence is an actuarial calculation, so the actuary calculation charges, etc., so next quarter there may be a higher number, maybe a lower number, it is difficult to make a prediction on one single line item like that. Going forward, I think multiple sort of factors are giving us confidence on margins. One clearly revenue growth is the biggest driver like we explained in the past, for example, where more of the revenue start coming in as programs move out of transition into steady state, therefore similar cost structure is going to get higher revenues, so that is a big margin lever as one angle, but even otherwise, larger deal wins and digital more profitability on digital deals etc. are all of which will also contribute to improvement in profitability. Finally, as our two acquired entities, Bluefin and Magnet, starts becoming breakeven, more stable growth etc., so that is also a margin lever. Thirdly, the operational efficiency improvement, cost reduction program etc. that we have is a continuous amount of focus on those as well, so that is also a margin lever, so overall I think we are doing multiple things to get margins back into our comfort zone.

Nitin Padmanabhan: Sure, that is quite helpful. The other thing I wanted to check was this quarter almost 90% of the incremental revenues came from the top 10 clients, I was just wondering going forward do you expect a more broader sort of spread of the incremental revenues that would come through and second is that the transition related gain on pricing or on the revenue growth, is there a lot of that yet to come going into the next quarter and so on and so forth?

Rostow Ravanan: I think transition related benefit will be lesser in Q4 because a large portion of those programs are completed with this quarter there, but overall like I said confidence on revenue momentum continues to be strong both because of market traction and also our own experience with customers, increasing win rates, etc.

Nitin Padmanabhan: Sir, just one last one, if you look at your US based clients and your European clients, versus same time last year where are you seeing a significant sort of change in momentum with reference to the demand environment?

Rostow Ravanan: I think there is an improvement in the demand environment overall between say geographies of US and Europe, between verticals etc., I think there is a lot more improvement in customer sentiment, willingness to make investments, taking larger bets in programs like digital, I think it is a broad- based kind of improvement that we are seeing amongst our customers.

Moderator: Thank you. We take the next question from the line of Rumit Dugar from IDFC. Please go ahead.

Rumit Dugar: Hi, thanks for taking my question, my margin question has been partly answered, but I just wanted to get some color specifically on the BFSI and Retail vertical, what are the kind of trends that you are seeing there in terms of spending and particularly spending in new tech, thanks?

Rostow Ravanan: Okay, let me take BFSI first. Our experience has been that we had one large customer that went through a lot of turmoil and in a way had like a big challenge with that vertical last year, but it has made a very smart turnaround, great wins. If you look at Q3 last year, we announced a large win from a US insurance company, Q2 this year, we announced a large win from another large credit reporting kind of a company, so many of our recent wins especially in the run the business kind of programs have been in banking, so this year that vertical has done quite well. This quarter also that vertical grew approximately the same rate as the rest of Mindtree growth, so overall I think our BFSI business has grown quite well. With one, I would say little bit of interesting trend, we are seeing our BFSI clients being late adopters on digital, so more of our pipeline, most of our wins, most of our work has been more of a traditional services kind of opportunities at the moment. Our Retail, CPG Manufacturing vertical has probably been a leader for us in terms of pushing the boundaries on innovation and doing some of the most cutting-edge kind of work in digital is happening in the Retail, CPG vertical for us at the moment, so that is the broad trends we are seeing in both these verticals.

Moderator: Thank you. Ladies and Gentlemen, I would now like to hand the conference over to Mr. Sushanth Pai for further questions.

Sushanth Pai: Yes, we will just take a few webcast questions, so one question has come on why receivables days are going up over the last three quarters?

A: Actually as per the data I think receivables days have gone up slightly up in this quarter alone from 64 to 71 days, but if you see the trend for the last few quarters, it has actually gained very stable or improved, like if you see in Quarter-2 of the previous quarter, it has actually been 64, the previous quarter was 57, before that it was 65, and then it was 71, so I think I do not think it has increased, but it has been stable and some quarters we have improved and some quarters that has been stable, I do not think it has gone steadily up over the last three quarters.

Q: The next question is there any one time in depreciation for the quarter?

A: There is no one time in depreciation for the quarter.

Q: The tax rate outlook for the next year?

A: I think Jagan just mentioned it is about 24 to 26% for the next year is what we think.

Q: Loss of a $10 million bucket client?

A: Yes, there has been one client which has come down because of a slight ramp down in one of our clients, the $10 million bucket has come down.

Q: Did any decline in expenses?

A: I think they explained margin walk, so in this quarter we have had an operational improvement of about mainly 180 basis point because of some projects moving from steady state to transition phase, so that is one of the main impact and we also had some SG&A leverage because of the growth of the 130 basis points, I think these two were key reasons for the decline in expenses or improvements in margin.

Q: The last question is, why new deal wins seems to get little soft?

Rostow Ravanan: The main reason for that is Q3 typically tends to be a seasonally weak quarter for new wins.

Moderator: Thank you, Sir. Ladies and Gentlemen, that was the last question. I would now like to hand the conference over to Mr. Sushanth Pai for closing comments.

Sushanth Pai: Thanks, Stanford. Thank you all for joining this call. If you have any further questions, please do write to us and we can get back to you. Thank you once again.

Moderator: Thank you very much members of the management. Ladies and Gentlemen, on behalf of Mindtree Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.