

“Tech Mahindra Limited Q3FY20 Earnings Conference Call”

**January 31, 2020**

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**Moderator:** Good day, ladies and gentlemen, and a very warm welcome to the Tech Mahindra Limited Q2 FY '20 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 '\*' then '0' on your touchtone phone, Please note that this conference is being recorded. I am now glad to hand the conference over to Mr. CP Gurnani – Managing Director and CEO of Tech Mahindra. Thank you, and over to you, sir.

**Moderator:** Ladies and gentlemen, good day and welcome to the Tech Mahindra Limited Q3 FY'20 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 '\*' then '0' on your touchtone phone. I now hand the conference over to Mr. C.P. Gurnani – M.D. and CEO for Tech Mahindra. Thank you and over to you, sir.

**C.P. Gurnani:** Good morning, good evening, good afternoon, wherever you are. Thank you for joining the Q3 call. As most of you have seen the results, it has been a great quarter for growth, a marginal deceleration but overall a steady quarter for EBITDA and I am very happy with the results. The Communications sector has grown 8.9%, Enterprises also shown an all-round growth. Almost all the geographies and all the verticals have shown growth, particularly satisfying. Manufacturing, despite of the headwinds and aerospace and automobile sector has shown a good growth particularly from the process industry. We also announced the acquisition of VLSI, an embedded software company out of Bangalore. Again, my colleague, Manoj and Agarwal will share a lot more details on that acquisition. We have also seen that the deal pipeline is very robust, second continuous quarter where we are announcing approximately \$1.3 billion of deal wins, 900 million has come from BFSI client where we would be working together with our client on managing sales and digital transformation.

When I look back, I think the company is firing on all cylinders; #1, investment in R&D, whether it is 5G, Blockchain, AI or on Cloud, the company continues to invest and continues to focus on not only technology but industry solutions.

#2, Collaboration with the Academic World. We are expanding our footprint. We are setting up small centers of excellence.

#3, Collaboration with what we call our TechMNxt Program, which is a stronger alliance program.

**Manoj Bhat:** Sorry about that. I think C.P. was on the road. What I will do is I will pick it up from here and if C.P. can come back, I think we can have a few questions for him. So overall I think C.P. was saying, it has been a good quarter in terms of all-round growth across geographies. I think some of the things around some of the verticals where Manufacturing has stabilized, BFSI, we are back into growth territory, I think we are seeing some of signs in terms of healthcare deals, I think we are continuing to win them. So, I think a lot of positives from that side.

Coming to some of the numbers, I think clearly if we look at the EBITDA margin, I think there has been a dip of about 30 bps on the operating margins. If I look at the breakup of that, because of our efforts towards automation and AI, I think our utilization has climbed to an all-time high; it is about 84% today, an increase of 2%. That has contributed positively. Currency has helped us in terms of margin this quarter. I think the major headwinds were of course even last quarter we were saying that the normalized level of SG&A was about 13.5% to 14%. So because we had a one-time benefit in the last quarter and that has come about this quarter. The other thing is of course in terms of overall transition cost that continues to be a factor in terms of the margins. And to me I think overall that is slightly below where we thought it would be in terms of the quarter. I think as we look at going forward, the margin levers continue to remain and I will talk about that later.

The other thing I wanted to highlight is in terms of our operating cash flows. I think it has been a very strong quarter of cash flows with free cash flow being about 118% of PAT which is I think possibly the highest we have ever had in terms of percentages. And the DSO for the quarter decreased by two days. Our cash and cash equivalents were about 1.16 billion as of the quarter-end. And headcount marginally reduced on account of normal business operations, most of the reductions with the BPS side. I think hedging, we continue to follow the same policy and hedge book is about 1.9 billion. And that is something which we have consistently done.

So what I would now request is ask, Vivek to spend a few minutes on the acquisition we did on Cerium, and then throw the floor open for questions and discussions and we have our entire management team to answer these questions. Vivek?

**Vivek Agarwal:**

Thanks, Manoj. I think what we have signed today is to acquire 70% of Cerium Systems. This is a Bangalore-based semiconductor and chip design firm. This is a continuation of our acquisition strategy of building capabilities or acquiring capabilities in white spaces and this creates a new capability for the organization as well as our belief in where the market is headed from a technology perspective. Silicon Engineering is becoming very important across the number of verticals when you start looking at use cases in automotive, consumer electronics, med devices, IoT. And this acquisition will help us strengthen our offerings to our clients in a number of verticals. And that is on top of the conventional semiconductor industry where we will be able to establish our footprint. We are buying 70% of the business upfront for \$24.5 million and then we would buy the balance 30% deferred over the next couple of years linked to the performance of the business.

**Manoj Bhat:**

With that we can throw the floor open for questions.

**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 Nitin Padmanabhan from Investec. Please go ahead.

**Nitin Padmanabhan:**

Just wanted to check, considering that we have had very solid deal wins and the transitions are likely to progress, do you think that margins could remain subdued in the near to medium-term before we see a pick up or we continue to hold on to achieving the 12.5%-13% for the year?

**Manoj Bhat:**

Nitin, the large deal win which we signed in Q3, there will be some impact in Q4. But I do not see much of an impact beyond that. So you will have to adjust those numbers for that. But other than that I think because of the faster transition on the communications large deal, I think we will be seeing some of the cost reductions also starting coming through probably later part of Q4 and going into Q1. So, it is a little bit of balanced, but

clearly, I think there will be some additional costs in Q4, which I do not think it will be a major impact but it will have some impact on the numbers.

**Nitin Padmanabhan:** Second is considering that we have had two big quarters in terms of deal wins, do you think it will sort of offset the seasonal weakness that we have seen in Q1 in the past?

**Manoj Bhat:** Nitin, we will have to see because there are multiple factors. It is probably too early to comment, but yes, they will help in reducing some of that volatility in Q1 because the current quarter deals will ramp up during the course of Q4 and Q1, and that will help in terms of mitigating some of the volatility. In terms of the Communications deal, during this quarter our transition has progressed much better than we expected. So, I think that deal is almost at full potential in terms of the revenue and of course this is the first phase of the deal, the second phase of the deal and the third phase of the deal will evolve over a period of time. So the immediate triggers in terms of that deal would not be there for Q1.

**Moderator:** Thank you. The next question is from the line of Sandeep Shah from CGS-CIMB. Please go ahead.

**Sandeep Shah:** Just a few things: In terms of Telecom, can you break down what is the deal win in this quarter?

**Manoj Bhat:** It is about \$150 million or so, Sandeep.

**Sandeep Shah:** What is the outlook in terms of deal pipeline especially in the Communications? Do you believe the deals which we have won in AT&T are sporadic or more such larger deals are shaping up in the pipeline and we continue to remain positive in terms of Communications growth over medium to longer-term?

**Manoj Bhat:** Sandeep, first of all, large deals of this magnitude are going to be sporadic. But the other way to answer this question is probably I will request Manish to step in, give a view of where we stand in the Communications business across multiple aspects including funnel, deal wins, how does he see geography that are telcos investing and so on and so forth. Manish?

**Manish Vyas:** Thank you, Manoj. Thank you, Sandeep for the question. I want to first echo a word Manoj said that large deals of that proportion and magnitude is not a pattern where you can do those deals every quarter. So, they would be at best sporadic but the overall question that you asked is even more important that the pipeline and the funnel, across the spectrum of our service offers and across the spectrum of our geography focus areas that we have decided to invest and remain invested in. That continues to remain healthy. Suffice to say that we are busy across our digital footprint or network or BPS as well as our engineering footprint and going forward as well that will continue to remain a very strong operational focus for us to continue to attack all pillars as we say and in the geographies that we are focused on. The important element is that the deals are triggered by essentially the need for service providers to drive more efficiency than what they have and to continue to modernize but on the network side or on the system side from a transformation standpoint. So the deal sizes vary depending on the size of a service provider, but the structure of the deal that we did in Q2, Q3 is likely to continue to be there, the sizes may vary as we go along.

- Sandeep Shah:** Manish, just the follow up to that is, it looks like are we in the initial phase of these kind of deals where client telcos are looking to optimize and modernize the spend, so where in terms of the penetration level for these kind of deals are there, so you believe still it is few clients who have started and more to follow as a whole?
- Manish Vyas:** There is never a global pattern as far as saving money and modernizing is concerned barring the fact that there will be one or two big trendy things. But overall it is always about what is specific to that one customer. I would not even say that it is a region-specific client. So hence the maturity of the deal funnel that we have is very mature to just about starting. It is a full range really.
- Sandeep Shah:** Manoj, just on the margin, even you believe that 12.5% as the lower end band of your targeted margin for FY'20, because of the deal transition cost may not be now achievable?
- Manoj Bhat:** There is only one quarter left. So I do not want to give a specific number. I think the question last time was 12.5-13% will we hit that number and I said there will be additional cost coming in. But obviously as you know Q4 is a better quarter also for some of our businesses. So I cannot be precise about 12.5, 12.4, 12.6. But that is something we will have to see, Sandeep.
- Sandeep Shah:** Just a related question, this quarter if we look at the gross margin, despite the deal transition cost, it has actually gone higher. So, it is largely due to currency and the utilization which more than offset the deal transition cost?
- Manoj Bhat:** In the construct of the deal, of course, that has helped but also I think since we are able to hit certain milestones in terms of the transition, I think that also helped on the revenue side. I think both of those impacts need to be taken when you look at that.
- Moderator:** Thank you. The next question is from the line of Rishi Jhunjhunwala from IIFL. Please go ahead.
- Rishi Jhunjhunwala:** Firstly, on the enterprise deal wins, so the one large deal that we have won in the insurance segment, just wanted to understand the nature of that, in the sense that, I mean, really insurance is not a very big part of our overall portfolio but this seems to be a landmark deal, it would have been a fairly competitive bid comparing with some of the other peers as well. So, what has gone into winning this deal, how is generally the pricing construct or is it something where we have promised savings over a period of time, how do we look at this large deal?
- Manoj Bhat:** I will request Vivek to answer that question because he is the architect of that deal. So Vivek, if you want to comment on?
- Vivek Agarwal:** I think there were two or three different parts to that question, and I will try and address as much as I can in terms of client-specific information. So firstly in terms of nature of work, so this is largely a horizontal deal around infrastructure services, clearly, there is no hard boundary, so there will be parts of domain but the basic offering is around infrastructure services, there is a run component and then there is a transform component in terms of taking the organization on a digital journey. So all the standard offering capabilities around Automation and AI are an integral part of what we will execute for the client. We will do a large scale cloud migration. That is part of the transformation journey. Similarly, on enterprise networks, that has been an area which we build capability over a period of time along with Manish coming from our heritage around telco networks. So there is work around network transformation. While domain is important, our need to understand

the customers' business is important and we do understand to that extent, we may not be very large in this sub-vertical. But our ability to execute on a number of the technology transformation initiatives is what I think stood us in good stead in terms of winning the deal. I think the next set of questions was more around the commercial constructs. I think clearly some of it is client-specific. So we would not go there. And Manoj has anyway guided on the overall margins which we manage as a company and in terms of controls and processes, how we do it on deals, we have adhered to a lot of those principles as we have gone about structuring the deal.

**Rishi Jhunjunwala:** Secondly, Manoj, if we really look at this year the subsidiary profitability, the EBITDA margin side has been fairly decent. But if we really look at minority losses, those have swelled significantly when we compare it with last year as well. So just wanted to understand what is happening there in terms of whether are there significant one-off charges that have happened on the non-operational side or what is the reason for minority losses to go substantially higher... consolidated level?

**Manoj Bhat:** I will have to get back to you, Sandeep. Off hand, I cannot think of a big reason but if during the call it comes back, I will answer that question.

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

**Mukul Garg:** Two related questions; first, on the deal wins, last two quarters really impressive. While telecom capabilities is probably well-known but again I think the total deal value compared to what you guys have won historically has gone up materially. So, is this something which you guys are doing differently versus earlier both on enterprise and telecom side which is helping you win large deals and should we expect this to continue? And second, basically given that Q3, potentially Q4 will benefit from them, are you looking at both segments grow a little bit differently than what you are expecting around the analyst meet time?

**Manoj Bhat:** So let me pick the second question first, right. The way to look at it is of course whatever we mentioned during the analyst meet in terms of enterprise and coms, some of these wins gave it a very solid footing in terms of visibility. Of course, as visibility keeps improving, we will come back to you, but at this point, I do not think we are changing our view. And keep in mind this is a fairly early days of both these deals if you look at it. It has actually been only 3.5-months or so, 4-months into transition on the first one and about probably 15-days to 1-month on the other one. So, on that we will reserve our comments in terms of whether we should look at thinking about that kind of reference point differently. But on the Enterprise side, I wanted to get in Jagdish in terms of what are the key initiatives which are driving funnel growth across verticals and across some of the competency areas and I think Vivek did mention that how competency and strong capability demonstration is also leading to be a differentiator in some of the deals. So, Jagdish, do you want to comment?

**Jagdish Mitra:** Sure-sure. Thanks Manoj. I think a couple of things we started taking a few steps about two, three quarters back for the overall for the company and definitely for the enterprise side of it, if you recollect, we said, we are going to bring an initiative or driving through based on our "Run, Change and Grow" strategy to look at the change aspect of what each of our customers are looking which is really digital transformation and therefore the role of the competency in modernizing the organization in change. So we have always reported good digital numbers that I think we were always talking about saying how do we use those digital numbers to lead the discussion. Now, it is starting to have this competency and vertical play in defining what could transform these guys. So that is probably proactively setting up with the competencies that we talked about, whether it is cloud

or different aspects of digital, enabling us to drive a better growth pipeline. And the other initiative is we are leading with a little more business-driven initiative. We had started an initiative called 25/25 for our initiatives on business. And that is starting to at least create the good momentum in terms of proactive conversations with our customers. So that I would say two of the initiatives that are driving I think good pipeline. I hope that answers your question.

**Mukul Garg:** I think it did help a lot but I also wanted to understand specifically in the context that given that historically on the enterprise side specifically you guys were meaningfully smaller than your peer group. So, a) have you started kind of getting the same perception level as the larger IT vendors in enterprise side and b) are you seeing a significantly more number of large deal wins, multi hundred million dollars coming out in the market which you guys can compete in?

**Jagdish Mitra:** So, a couple of things: I guess the journeys do not happen overnight, it started a while back, we did state very clearly that we are going to invest in creating and developing our enterprise business which was a conscious step, knowing that we are sort of falling short of some of our larger peers in the industry. And we picked up a few areas to focus on. So our strengths in Manufacturing, Digital Transformation around BFSI, driving BPS growth into enterprise segment, driving 25/25 initiatives as I just talked about. So yes, I would say that we are approaching these verticals from a completely digital transformation type play, rather than trying to compete on the same grounds that our peers are. And it's starting to show results across the verticals. Some of the verticals, so for example, we will talk about it later. But for example, our synergy in HLS is starting to play out very well. So, the seeds that one sort of put together four to six quarters back is starting to play out well now.

**Moderator:** Thank you. The next question is from the line of Sudheer Guntupalli from Motilal Oswal Financial Services. Please go ahead.

**Sudheer Guntupalli:** Your growth in BFSI and retail seem to be very strong, the trend looks like a bit of divergence from the industry trends and concerns around the slowdown in these two verticals. So, any qualitative color on this will be helpful. And how sustainable is this going into the quarters ahead?

**Manoj Bhat:** So I think we have said this many times in the past that from a BFSI perspective I think our growth approach is slightly different from some of the larger peers who are, obviously, different history and a different coverage. So I think our commentary and our behavior is probably not necessarily true across the sector. And that's something we have always maintained. So to me, I think, as we stand here today, I think it looks like that going into next year I think BFSI will be a growth vertical for us. And it is something which I think if I look at the last few quarters, I think we had a bit of slowness. And I have spoken about this that a lot of our business is transformation, and there will be transformation cycles, and then there will be sustenance cycles. And that's in line with that. So that's my view and I won't mean it as a commentary on the broader BFSI segment, but it's a commentary on our BFSI segment.

**Sudheer Guntupalli:** Sure. And if you look at the growth across client buckets, there seems to be a strong growth in the revenue from top-five accounts. We understand this might be because of the ramp up for the large telecom deal. But the clients below that, top six to ten and below, there seems to be a sharp revenue decline, indicating growth was very much concentrated and driven by top-five accounts. But if you look at the geography growth rates, on the other hand,

it has been fairly broad based. So, just trying to reconcile how the invoicing is done for these top accounts or these invoices across geographies, including rest of the world?

**Manoj Bhat:** So many of our clients would be multi-geography, firstly. Secondly, I think we report top-20 for the quarter, so there might be some differences coming through because of that. Because you must remember, for example, some of our businesses go up and down in terms of quarters. And specifically, I think some parts of our healthcare business, some parts of our mobility business. So I think it's probably a combination of that, but I don't detect the pattern otherwise from what you are saying. So it's not a structural thing.

**Moderator:** Thank you. The next question is from the line of Abhishek S from Elara Capital. Please go ahead.

**Abhishek S:** Just the first is a clarification regarding the large insurance deal that was mentioned earlier. Now, it seems that the deal was predominantly APAC dominated, so would it have any different impact on the constant currency business that we do?

**Manoj Bhat:** I think we have clarified on this deal. I don't want this to be like a discussion around that. But yes, it has components across multiple geographies, including APAC, and that that's where I would like to leave it, and the US.

**Abhishek S:** Okay. That's helpful. And secondly, would like to understand the capability of the acquisition that we announced today. From a per employee metric basis the revenue profile seems to be substantially inferior to what we have. So, could you just elaborate on to what capability is kind of getting integrated into the business? Thank you.

**Manoj Bhat:** Sorry, could you repeat that question, I lost you in between.

**Abhishek S:** So, from a revenue per employee metric basis, the acquisition revenue per employees is substantially inferior to the company average. So, if you can just help us understand what capability build up happened because of this acquisition? That would be helpful.

**Manoj Bhat:** And you are calculating it how? So that just we can follow the logic.

**Abhishek S:** So, from your filing it seems the revenue was around \$115 million and the employee number is given along with the filing. It's Rs. 105 crores as the revenue.

**Manoj Bhat:** And 850 employees. But 850 is the current employees and Rs. 105 crores is almost a year back data, right?

**Abhishek S:** Yes, so even if I apply the growth rate for the past two years has been like on an average 70%, which translates to a \$25,000 per year kind of a business. I am just curious to understand, from a capability standpoint.

**Vivek Agarwal:** So, I think two things. One, it's a largely offshore business and it's in a growth phase. So there will be that differential what Manoj said about historical revenue numbers versus where the business is now and what we see as the growth prospects of the business. And I think from a capability perspective, that is really our driver for the acquisition. So in some ways, the size of it is secondary. What I said right in the beginning, I mean, apart from the opportunity we see in the semiconductor industry itself, it's a large addressable market, and we didn't have



any historical capabilities in that space. That's one reason. And secondly, we see silicon engineering becoming a very important and integral part going forward as you start looking at autonomous driving, IoT, electronic devices, med devices. So, this will help us across a number of verticals to be able to offer a more comprehensive offering for our clients.

**Moderator:** Thank you. The next question is from the line of Sandeep Agarwal from Edelweiss. Please go ahead.

**Sandeep Agarwal:** So, Manoj, I have one question on the margin front. Our margin journey started and we have done extremely well in last few quarters, this quarter probably we were not able to expand much. Can you give us some sense that given the huge amount of deal wins which are happening, is the margin trajectory still on the northern side where we can see significant improvement? Or you would say that it may take a little pause for the time being? Number one.

Number two, on the growth front, are you seeing a very big change on the telecom side, which is driving such huge growth or is that something else?

**Manoj Bhat:** So. Sandeep, if I look at margins, and I really don't want to concentrate on Q4 and talk more about next year, right. So, we have said that we will improve margins, which still remains to be the case. So I don't think anything we have done this quarter changes that.

Number two, as I mentioned, probably Q4 we might have some additional cost because of the large deal. But going back into Q1, etc., I think some of the leavers around margin improvement will start to kick in.

Then the third thing we had said even last quarter was, aspirationally I think we have a goal in mind in terms of the margins for FY21. Now, of course, every such large deal which comes in, of course, it becomes a bit more of a stretch that much I think I have to say. But clearly, we will have to find ways and means to get to a margin improvement. But definitely I think margin improvement will happen. The extent of margin improvement, I think that's something we will have to look at.

**Sandeep Agarwal:** There was a question on the large deal on the telecom side also.

**Manoj Bhat:** Sorry, what was the question? I think you had said, is there any fundamental change in the market which is causing this, was that the question?

**Sandeep Agarwal:** Yes.

**Manoj Bhat:** And Manish, you want to pick that up? I think you covered it in your first answer, but please.

**Manish Vyas:** Yes. I will probably paraphrase that slightly differently, Sandeep. So the question is, are there any new trends? No, but the same trends continue. Broadly speaking, the need for the service providers to reshape their operations across IT, network, back office is going to be a continual journey and a trend, because they have to be ready as their products and services evolve from beyond voice and data. Part one.

Part two, I think the overall CAPEX cycles are largely driven around both architectural change, as well as the expansion that they will do on their network. And while that may be a non-uniform pattern, but that will continue to remain a pattern for a period of time. So our drivers for, broadly speaking, across the world are deal funnel today, irrespective of which competency and pillar we are talking about, is indeed falling into these two big criteria or these artists chasing these two trends, if I may. I hope that answers your question, Sandeep.

- Moderator:** Thank you. The next question is from the line of Rahul Jain from Dolat Capital. Please go ahead.
- Rahul Jain:** Congratulations on strong quarter and deal wins. Firstly, in light of our improved deal win performance, can we say that we are set well to deliver higher than industry level growth, or at par with larger peer in the next fiscal or CY20?
- Manoj Bhat:** I did answer the question a little while back. So I think with every passing quarter, I think our fundamental... and what we have said is our ambition is to grow ahead of industry in enterprise. And on the comms, we want to be steady in terms of the growth. And so that's something which is being made more concrete and more profitable. And I also said that any comments on increasing that visibility is something which we will comment as and when the quarters progress.
- Rahul Jain:** Okay. And secondly, in terms of the acquisition, the growth in this business has been very significant, at least on the data that we have shared. And considering the growth and valuation that we have paid, is it safe to assume that the current profitability in this business is quite low?
- Manoj Bhat:** I think it is running at a decent profitability, it's not very low. But again, I think, to me, I think we are spending a fair bit of time on an acquisition which is essentially a capability acquisition. And in the overall context, I think, from a revenue accretion, it is not probably a very significant one, right? So, I think in terms of multiples it is in line with what we have paid for some of our other acquisitions.
- Vivek Agarwal:** And I think it's a timing issue of historical versus where the business is now relative to what I would say.
- Rahul Jain:** Right. And if I can speak one more, to the earlier comment about that telecom prospects are looking promising from a funnel perspective, but not necessarily from a specific brand perspective. How we see this as a unique or superior fortunately for us? Is it more about our historical strength in the vertical or is it a general statement and it will all be a function of our win ratio going forward?
- Manish Vyas:** Rahul, if I am getting your question right, you are saying, what is going to be our right to win in the telecom space?
- Rahul Jain:** So, what I am trying to say, if we just look at last couple of years performance in this particular vertical to put together, the past growth has not been that significant. If we look at three, four years as together. So what gives us confidence that this general optimism that we see in terms of funnel will materialize into a superior growth for us? Or it is just more of a relative versus what we did now and what we see into future?
- Manish Vyas:** Got it. Absolutely. Great question. I think the last two or three years, as you would recall, has also been a function of more than normal slowdown in some of our businesses. It also was a result of some of the voluntary retirement

that we had done of an acquisition that we did three, four years ago, where we took specific steps to right size our focus areas from a portfolio and from the market standpoint. The reason I say that is also to add that it is not that we have, at any point in time, stagnated our ability to win, our investments in our offerings, or more importantly, our relationships with the market leaders in almost every major geographies of ours. We have continued to win market share with almost all the major service providers. That said, that indeed was a little slow down in spend from some of the major ones that we do business with.

The other little factor, of course, is, I think we have said before, that the categorization of our telecom business is pure play telecom, it doesn't add a lot of the other sectors that some of our eminent fears do include as part of their business. But that's beside the point. That said, going forward, I think we are well positioned based on a combination of two or three things. One, our access rights, our relationship with the leading service providers are better than ever before. We continue to be in discussions with them for either the run change or the grow opportunity. Two, the investment that we have made in recent times, including having built some very specific IPs and some specific partnerships across BFS, OSS and the related areas where the CAPEX cycle is likely to happen, I think it will also probably put us in good stead as we go along.

And third, if anything, we continue to believe that we may have done a lot of our optimization, it is maybe behind us most of it. And hence, it's about trying to take a march forward and continue to put one step forward every other quarter. But we've always maintained this is a journey, telecom industry is not exactly at a point where their growth rates are highest across all industry sectors. So there will always be a little churn that will continue to happen. But our worldwide presence with almost every single major service provider, I think is a good position to be in. I would any day take that position than anybody else.

**Moderator:** Thank you. The next question is from the line of Vibhor Singhal from Phillip Capital. Please go ahead.

**Vibhor Singhal:** Congrats on a great set of numbers. Manoj, is it fair to assume that the AT&T deal contributed for the full period in this quarter?

**Manoj Bhat:** Yeah, that's a right assumption, Vibhor.

**Vibhor Singhal:** Sir, just two more questions on my side. One on the subcontracting cost, as we have seen, and you mentioned in your opening remarks also that probably we will discuss that in more detail. So as we have seen the subcontracting cost rise in this quarter around 15% of revenues. So what is the kind of comfortable level of target that we are looking at? Or if not a target or at least a number that we would be comfortable with? Considering that we are getting these large deals which would require some subcontracting as well. So what is the number that you believe as a company you would be comfortable with?

And secondly, on the manufacturing business. In the Analyst Meet we had mentioned that the auto business of the manufacturing vertical, is probably facing some of the headwinds because of the weakness in the global auto segment. So, does the coverage remain the same or have you seen any changes in the few weeks or period has elapsed between the Analysts Meet and now?

**Manoj Bhat:** So, let me pick the first one first. So, if I look at subcontracting cost, I think it's largely because of the deal transition. So, I do expect that going into Q4 and Q1 it will start to come off to probably some of our historical

levels I think was about anywhere between 12.5% to 14%, so something which we do expect will happen over a period of time. Having said that, I mean, I think, obviously, we have always thought of subcontracting as an integral part of our resourcing mix. And that's something which we continue to do. I think in terms of your second question on the auto segment from the Analyst Day to now, I don't think there's any incremental difference. But I think if we look at our commentary even that it has bottomed out, that's what we feel and that's what's happened this quarter in terms of, if you look at manufacturing also, that's kind of consistent with what we thought would happen.

**Vibhor Singhal:** So, basically, I just wanted to check, if, from any of the client's perspective or overall have we seen any kind of weakness or postponement of deal flows, or do we expect the same because of it being an election year in the US this year?

**Manoj Bhat:** So, I think same is probably a wrong word to use, because we have had two record quarters. But if the question is have we seen bill postponement? I don't think we are seeing any deal postponement. I think a lot of engagement, a lot of charts around what can we do together and a lot of protocols are in place. So I think the short answer is, no.

**Moderator:** Thank you. The next question is from the line of Sumeet Jain from Goldman Sachs. Please go ahead.

**Sumeet Jain:** Sir, a couple of questions. So firstly, wanted to understand, are you planning to increase your local hiring levels in US just to ensure in future whenever we are winning such large deals, the subcontracting cost doesn't go up?

**Manoj Bhat:** So, Sumeet, most of these large deals, I think it is kind of now probably a combination of local plus global, plus, I would say, subcontractor. I think it's a mix. And in some cases there will be non-manpower costs in some form or fashion, right? Because I think as with most of these, I would say, mega deals, you would take end-to-end responsibility across multiple buckets. So, having said that, from a localization perspective, I think we are seeing increased localization and that's something which is an effort which we are putting in also. And I would request Harsh to talk a bit about some of our localization efforts.

**Harshvendra Soni:** Thanks, Manoj. I think you put it aptly, that as part of our strategy, we are doing localization across, so for example, from engineering to business schools. Because as a strategy, we believe that it gets us closer to the lay of the land. And also, we would like to hire people from the same country or region we are in. So nothing changes because of any deal, but as part of our strategy we are, obviously, putting efforts to make sure that that is on the rise.

**Sumeet Jain:** Got it. Thanks for that clarity. And just one more question. I think, Manoj, you have mentioned in the past that portfolio companies' profitability, increasing that is one of the key levers you will be focusing on. So can you highlight some of the key portfolio companies you are focusing on to improve profitability next year?

**Manoj Bhat:** I think from a perspective of portfolio companies, I think there are two elements here. So one is, if we think about revenue synergies and how do we take the operating leverage of the business. So, because I think a lot of these portfolio companies, I think we have a front end investment already, and it's a question of how do we adequately lever it up by actually winning more. And I think that journey is well and truly started. And I think I would say,

overall, I would say the healthcare side has been the most traction there. But we are pretty positive that it will kind of move to some of the other areas also.

The second area is in terms of thinking about how do we leverage our combined synergy on the cost side, whether it is in terms of facilities, in terms of procurement and so on and so forth. So that's the second big initiative. This is also all across portfolio companies. To me, I think this this is a margin lever from both perspective. And I think that will play out in the coming year across all of our portfolio companies. I don't know whether you are looking for anything else, but that's broadly how we are approaching it today.

**Moderator:** Thank you. Ladies and gentlemen, due to time constraint, that would be the last question for today. I now hand the conference over to Mr. Manoj Bhat for closing comments. Thank you. And over to you, sir.

**Manoj Bhat:** Thank you all for joining the call. And as usual, if you have any questions, please do feel free to reach out to Kaustubh or me, and we will be happy to answer any questions offline. And Sandeep, I owe you an answer on that one, I will come back to you. Thank you.

**Moderator:** Thank you very much. Ladies and gentlemen, on behalf of Tech Mahindra Limited, that concludes this conference. Thank you all for joining us. And you may now disconnect your lines.

*Note: The above transcript has been edited for better readability*

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