Q1 FY2010 Earnings Call Transcript – July 29, 2009

CORPORATE PARTICIPANTS:

- Mr. Ananda Mukerji – Managing Director and Chief Executive Officer
- Mr. Carl Saldanha – Global CFO
- Mr. Mike Shea – President, Healthcare vertical
- Mr. Santanu Nandi – Executive Vice President, Telecom & Media vertical
- Mr. Sanjeev Sinha – Executive Vice President, BFSI
- Ms. Chandra Iyer – Executive Vice President, Asia Business Unit
- Mr. Dinesh Jain – Treasurer and Chief Commercial Officer
- Mr. Deep Babur – Vice President Finance
- Mr. Mahesh Pratap Singh – Head of Investor Relations

Moderator: Good morning ladies and gentlemen. I am Sandhya, the moderator for this conference. Welcome to the Firstsource Solutions Q1 FY2010 Earnings Call. For the duration of the presentation, all participants' lines will be in the listen-only mode. I will be standing by for the question and answer session. Now, I would like to hand over to Mr. Mahesh Pratap Singh, Head of Investor Relations. Thank you and over to you sir.

Mr. Mahesh Pratap Singh: Thank you Sandhya. Good morning to participants from India and Europe and good afternoon to participants from Singapore and Hong Kong. Welcome everyone and thank you for joining us on our earnings call for the first quarter ended June 30th 2009. Please note that the results, fact sheet, and press release are available on our website www.firstsource.com and have also been mailed across to you. The transcript of this call will also be made available on our website. To take us through the results and to answer your questions, we have with us today Ananda Mukerji, our Managing Director and CEO.

Mr. Ananda Mukerji: Good morning.

Mr. Mahesh Pratap Singh: Carl Saldanha, our global CFO.

Mr. Carl Saldanha: Good morning everybody.

Mr. Mahesh Pratap Singh: Mike Shea, President, Healthcare.

Mr. Mike Shea: Good morning.

Mr. Mahesh Pratap Singh: Santanu Nandi, Executive Vice President, Telecom and Media.

Mr. Santanu Nandi: Good morning everybody.

Mr. Mahesh Pratap Singh: Sanjeev Sinha, Executive Vice President, BFSI.

Mr. Sanjeev Sinha: Good morning.

Mr. Mahesh Pratap Singh: Chandra Iyer, Executive Vice President, Asia Business Unit.

Ms. Chandra Iyer: Good morning.

Mr. Mahesh Pratap Singh: We will be starting this call with a brief presentation providing an overview of the company's performance in this quarter followed by a Q&A session. Please note that everything said on this call that reflects any outlook for the future or which can be construed as a forward looking statement must be viewed in conjunction with the risks the company faces. The full statement of these risks and explanation is available in our prospectus filed with SEBI which can be found on www.sebi.gov.in. With that said, I would now turn the call over to Mr. Ananda Mukerji, our Managing Director and CEO.

Mr. Ananda Mukerji: Good morning again everyone and thank you for joining this earnings call. Let me begin by giving an overview of the financial performance for the quarter. We have had a strong quarter from both revenue as well as profitability perspective. To just go through the numbers, our revenue from operations has grown by 18.8% year on year and 2.6% quarter on quarter and is at 4,845 million rupees. The operating EBITDA has grown again 15% year on year and again 15% Q on Q and the operating EBIT has grown 22.9% year on year and 30.5% Q on Q. The operating margin has gone up from 7.6% to 9.7%. Below the operating EBIT line, there are a number of items out there. As you would recall, we had a large gain on FCCB buyback in the last quarter and as against that, we had some hedges which we had cancelled as also some extraordinary expenses which we had incurred during that quarter. In this quarter, we have had some FCCB buybacks, but the number is much less. As against roughly 50 million that we had bought back in the previous quarter, this quarter has been about 12 million. The gain on FCCB buyback is also lower and as against that, we have had one unusual extraordinary expense out there. So, I think the profit at the profit after tax level is strictly not comparable between Q4 and Q1 and so while we will be happy to answer questions on the line items there, I would focus for the purpose of performance on the operating EBIT line as we have consistently done in all the presentations we have made. So, if I look at the growth, as I mentioned, 2.6% in rupee terms Q on Q and 3.1% in terms of excluding cross-currency movements in terms of constant currency, the similar number in terms of year-on-year is 8.9%. You would recall, at the last earnings call we had expected that we will have a lower profitability in Q1 compared to Q4. The actual operating EBIT margins as I mentioned has come in higher by 210 basis points and that is on account of three or four factors. One is, we have had strong performance on the healthcare vertical during this quarter. Some of it is due to catch-up on payment delays which has impacted us in the last couple of quarters as also the larger approvals of high dollar value claims. We have seen higher contribution from telecom, media, and BFSI on the back of improvement in productivity and efficiency. The normal business seasonality in Q1 whereby we see a drop-off in both revenues and profits in the BFSI collections business, this year has not been as pronounced as in other years and also has been mitigated by improved productivity, and we have had a favorable exchange rate on the GBP. The extraordinary items which I mentioned, this 118 million of other income, this is largely on account of gains and cancellation of undesignated hedges. We had provided for cancellation of those hedges at the end of the last quarter. When we actually cancelled it, there was some gain and that is the 118 million which was reflected in other income. We also have a one-time expense of 84 million rupees which is related to the movement of an existing program from Argentina to Philippines. We run a program in Argentina for a large US customer of ours, for whom we actually operate out of three geographies, the Philippines, India, and Argentina. For various reasons, the customer would like to move this program from Argentina to Philippines and that is something which we also believe is going to be beneficial for us in the longer run as well, so we have decided to make that move and in the process of making the move, there are some upfront costs to be incurred and that is the 84 million rupees which is being provided for that. The other extraordinary item is a 74 million rupee gain on buyback of 12.9 million dollar face value of FCCB, net of the foreign exchange impact. As I mentioned, you would recall in the last quarter this number was 635 million rupees. At that time, we had bought back about 50 million dollars of bonds. So, outstanding FCCBs as of now is 212 million dollars compared to the original issue of 275 million dollars. In terms of clients, we see stable relationship with our existing clients. As you all are aware, most of our revenues in growth, particularly the growth comes from our top customers and I am happy that our volumes from the last top 10 customers have remained largely stable during this period. In terms of foreign exchange hedges, our outstanding FX hedges are at US dollar 41 million and 38 million GBP. Fiscal 10, we are 100% covered at the USD coverage at rupees 45 level and 85% GBP coverage at rupees 80 level and FY11, we have 100% dollar coverage at 46 rupee level and 35% GBP coverage at rupee 80 level. In terms of the employee strength, we had about 23,355 employees at the end of quarter, 18,416 of those in India and just under 5,000 of those based outside India. Net, we added just under 1,800 employees compared to the net reduction of 950 employees in Q4 and net addition of 984 employees in the first quarter of the previous year. Just want to reiterate something I have said several times in the past calls, our hiring is linked to specific customer demand, so we do not hire in advance or we do not keep a bench. So, really hiring pattern reflects whatever growth is taking in place in revenues and that is reflected in the headcount changes which take place. In terms of attrition, we are seeing significantly lower attrition, both in the offshore, that is India, Argentina, Philippines attrition compared to Q4 as also onshore which is the US and UK attrition. At the domestic, which is the Asia Business Unit, attrition has increased between Q4 and Q1, but that is really a function of the fact that a lot of these are early stage programs which are in the process of ramp, some of it is in the geographies or cities where we have entered where we are relatively new and this is really a space which is not yet stabilized and we expect these numbers to start stabilize and reduce and come down as the business starts to get into more of a steady state business as usual. Seat capacity and utilization, we are just under 20,000 seats worldwide. We added one new delivery center in Bhopal in India. Seat fill factor has shown some improvement over the last quarter by 3 percentage points and this is something as I have mentioned in the past, we are very focused on and we are looking at driving this up over the coming quarters. Significant awards, we are proud of the fact that we were considered among the top 100 companies in the world by the CIO magazine for innovative use of IT. Use of IT for improving the efficiency of our delivery and adding value to our customers is a core part of our value proposition and we are delighted that our capabilities there have been recognized by somebody as eminent as CIO magazine. In terms of other highlights, the next slide really talks about the mix of business across geography and verticals and not too much shift from the previous quarter as you would observe. In terms of geography, North America has come down by 1 percentage and UK has gone up by 1%. India remains stable. In terms of verticals, healthcare has remained stable from the last quarter and telecom has gone up by 1% and BFSI has come down by 1%. So, not a whole lot of movement, any movement in terms of mix of business, similarly in terms of delivery location. Client concentration also largely remains stable. Our general level at which we are, top clients at around 10-11% and the top five clients at around 30%. So, that is the kind of trend which we are seeing and I expect this would probably continue for the next few quarters. With that, what I will do is hand it over to the individual business units who will take you through what is happening in their specific verticals and then I will come back in terms of the overall business outlook going forward. So, with that, I will hand it over to Mike Shea who is President of our healthcare vertical. Mike, you want to take them through the healthcare vertical outlook.

Mr. Mike Shea: Good morning everyone. Thank you Ananda. The healthcare vertical, as you all know, the market geography is primarily in the United States and we serve two key segments, the payer and the provider segment and we comprise approximately 41 or just a little under 41% of the income Firstsource services is the healthcare vertical. We have as of June, 2,813 employees across the US and we have a seat capacity of 3,130 seats or 81% fill factor. We also do deliver some of our services offshore and our India location as well. As far as looking at some of the industry trends, I think you are all very well aware of the economic recession and increasing unemployment rate has been a catalyst for sustained change in the healthcare system. Currently, the congressional lawmakers are continuing to work towards finalizing the reform legislation, although it doesn't appear they are going to get this pass before the August recess and the latest is it appears it is going to take a shape is some time in the early fall towards maybe even as late as the end of the year. However, I think that we should be enthused that the Obama administration has certainly not backed away from this. As recent as this week, the Obama administration has had a major push and major new calls for enacting healthcare reform within 2009. With increased unemployment, more people rely on Federal and State programs for payment. Those programs we are speaking of are Medicare and Medicaid and this results in revenue shifts and protracted payment cycles for our clients. We are also seeing rising unemployment that continues to fuel an increase in the uninsured, for the hospitals. Some of these volume shifts are occurring as patients opt to defer immediate healthcare. Based on that, we expect the eligibility services and receivable management part of our business to be impacted favorably in the short and intermediate terms as increased enrollments and cash acceleration needs persist. However, reductions in employer-sponsored healthcare coverage results in lower claims processing volume in payer segment as the unemployment population continues to rise towards 10%. The provider margins, we are also seeing some pressure there and the increased complexities related to the response to reform suggest significant business opportunities may lie ahead. So, we believe we are positioned well to respond to the reform given our core competencies in the payer and provider segments and lastly, as you know, we had a good quarter and we experienced positive growth and performance that continued in spite of the challenging external environment. So, I will give it back to you Ananda.

Mr. Ananda Mukerji: Okay, thanks Mike. I will hand you to Santanu to take you through the telecoms and media outlook. Santanu.

Mr. Santanu Nandi: Thanks Ananda and good morning everybody. Just to give you a brief snapshot of our operation, the markets in terms of geographies that we service, essentially UK, US, and Australia and the key segments that we operate in essentially the satellite television, wireless and mobile, broadband, and ISP and the fixed line segment. We produce about 24% of the income from services for the overall company and employee about 5,500 employees across all the various geographies and the geographies from which we deliver are essentially India, Philippines, UK, and Argentina. Now, coming to some of the key trends and the business outlook, we see, particularly in the mobile and wireless segment, an increase in the Smart phone usage and a higher usage of mobile broadband. We also see a continued focus on consolidation and cost cutting. Arising from business trends, we see an increase in the technical support demand primarily because of higher end phones which are being used and we also see an increase need for commercial flexibility because of some of the cost pressures that the market is going through. In the broadband high-speed segment, we see some M&A activities in the UK market, particularly in the residential broadband segment and this has potential growth opportunities for us because some of those players essentially we are working with are the ones who are actually acquiring. In a fixed wire line segment, we see the effect of the economic situation in both the enterprise and residential market and this is one segment, as a result of this, we anticipate a marginal drop in the revenue. In terms of DTH and pay TV segment, you know, the players are moving towards bundle packages and triple play essentially to create stickiness of the customers and is gaining acceptance with the consumers as well. This essentially gives an outlook of increased volume for us, primarily because we already operate in all the various elements of triple play and as the brands continue to grow in the triple play area, they will find a natural ally in us in terms of providing those services. In terms of some of the other complex technologies, we see a growing usage in Triband for personal video recorder, video on demand, and HDTV (high-definition television), etc., and we operate with those players in this market segment who are essentially the innovators of these kinds of new technologies and therefore anticipate positive volume trend. So, overall if we look at it, based on the industry trends, we anticipate volume increases in segments like mobile, broadband, as well as pay TV and a marginal decline in the fixed wire line segment. So, overall there is a positive growth trend in FY10 in the telecom and media segment. Thank you. With that, I hand it back to Ananda.

Mr. Ananda Mukerji: Yeah. Sanjeev will take you through the BFSI segment.

Mr. Sanjeev Sinha: Thanks Ananda and good morning to everyone. BFSI segment services clients in the US and UK across the segments of credit cards, retail banking, mortgage, general and life insurance. In this quarter, we contributed 23% to the top line of the company. We have 3,310 employees working from 3,138 seats across delivery locations in India, the United States, and Philippines servicing our clients in the segments that I just mentioned. So, let me talk you through some of the industry trends and how do we see those trends impacting the business outlook. Across credit cards, what we have seen is that the liquidation rates have been stable and the volumes have increased and this has resulted in better than expected performance that we have seen from our collections business. There is the Credit Card Accountability, Responsibility, and Disclosures Act of 2009 which has been passed by the US Congress and we believe that this will create revenue and margin pressures on the industry. We are working with our clients to mitigate the impact of it and at the same time because these would create cost pressures, we are exploring opportunities to grow business with existing clients and looking at other opportunities in the market. On the retail banking side, there is large scale restructuring. There are a lot of clients of ours as well as large financial institutions that are under critical and regulatory pressure due to government ownership. We don't see large scale offshoring opportunities at this time, but there are potentials for innovative deals and that we are exploring at this time. On the mortgage side, overall the gross mortgage lending continues to remain low, but quarter on quarter we don't see it falling. We see origination and servicing volumes continue to be subdued as a result of the fact that mortgage lending continues to be low. On the general insurance side, we see that aggregators and price comparison sites are continuing to gain market share due to the tough economic environment that are being faced, especially in our key geographies of the US and UK. We work for a direct insurer which also has one of the top three UK price comparison sites, and we believe that Shields us better to these trends in the industry. Overall, BFSI continues to be a challenging segment and we expect to see a flat growth in the current year. Thanks Ananda.

Mr. Ananda Mukerji: Chandra will take you through the Asia Business Unit.

Ms. Chandra Iyer: Thanks Ananda. Good morning everyone. The Asia Business Unit particularly meets the requirement of the geography which is India and it is served also from the Indian market, here the delivery and the market both are in India. These key segments that we serve are the BFSI and the telecom and media verticals. Today, this unit contributes about 11% of the income and we have about 11,000 employees as at June. We operate this out of multiple centers across over 8,000 seats and we have a seat fill factor of growing business which as Ananda had earlier mentioned, we are increasingly improving the seat fill factor. So, in the industry trend, the two segments that we are operating, the telecom and media seems to be the more active of the two segments. There are lot of established players for whom the market is opening up into newer and wider circles into India and the existing players are getting licenses to operate in these new circles. There are new players who are also entering this market that is opening up. With the deepening of these players into the rural areas of India, the businesses are looking at lower ARPUs which is this subscriber base tend to make their businesses far lower in value and that we will be talking about how we propose to address in our outlook. The clients are therefore looking at, because they are spreading, they are looking at end-to-end solutions being offered by partners like ourselves and we see a lot of other trends in the industry which is new features like the 3G and number portability, etc., which is coming into the Indian market. On the BFSI sector, the private banks are largely operating in a captive environment and not many major decisions at this point in time towards movement to the non-captive setup. However, we see the insurance market beginning to open up. From a business outlook perspective, the telecom therefore becomes a primary growth driver for us and continues to be what will offer us growth in the coming periods. On the BFSI segment, there is some initial opening up and we do hope to see some traction there. The existing customer and new entrants in the telecom and media, you know, are allowing us therefore to spread into the pan-India where our regional presence is already there and we could leverage later on that basis. We are already looking at the number portability and the other new opportunities that are arriving from the market change to see what kind of solutions we can offer there and that we think will offer a business opportunity for us. In order to meet the cost pressures of the underlying business, we are looking at improving our delivery model which will enable us to support the growth with a low model operation. We overall expect the unit to continue to see a positive growth. With that, I will hand over to Ananda.

Mr. Ananda Mukerji: Thanks. Okay, to take you all to the business outlook overall, I think we are seeing in our key markets of US and UK that the conditions are showing signs of stabilization, but significant uncertainty still remains on the time of actual recovery on the ground when our customer starts seeing positive growth again and start taking, you know, more strategic outsourcing decisions. We maintain our outlook of overall positive revenue growth and improved profitability in fiscal 10 compared to fiscal 09. We expect some quarter on quarter volatility to continue because I think at this time volume fluctuations we get from our customers are higher than normal because of the economic environment that they are facing. As also we are growing in a number of segments of our business. So, there are ramp costs associated with that which we will continue to see during the year. Moving into Q2, we expect BFSI, healthcare, and Asia business unit will all have positive growth. We are expanding BFSI delivery in the US and Manila. There is ramp on the healthcare provider business taking place and there is some ramp in Asia Business Unit for our existing customers. We also expect that one of the factors this quarter which was a delayed payment catch-up in healthcare will not recur in Q2, so overall we expect to see flat to slightly negative revenue growth and lower profitability in Q2 on account of these factors. We remain optimistic on a medium term prospects of the BPO business and we believe we are directionally on track to achieve the steady state performance levels. As I said again that we would be maintaining our overall positive revenue growth and the fact that fiscal 10 will see better profitability than fiscal 09. With that, I would like to hand over back to the moderator and open it for questions

Moderator: Thank you very much sir. We will now begin the Q&A interactive session. Participants connected to the India Bridge, who wish to ask questions, please press *1 on your telephone keypad. Participants connected to the International Bridge may kindly press 01 on your telephone keypad. On pressing *1 and 01, participants will get a chance to present their questions on a first-in-line basis. Participants are requested to use only handsets while asking a question. To ask a question, please press *1 and 01 now. First in line, we have Ms. Mitali Ghosh from Merrill Lynch. Over to you ma'am.

Ms. Mitali Ghosh: Hi, good morning and congratulations on good numbers.

Mr. Ananda Mukerji: Hi Mitali.

Ms. Mitali Ghosh: Hi. That was quite a comprehensive presentation. I was just wondering Ananda, possibly if you could touch upon how you are seeing the competitive situation developing in the BPO industry because increasingly we are finding the integrated IT/BPO players, you know, focusing on this part of the market. So, you know, if you could comment on your, like I said, the competitive outlook and also your strategy in that regard?

Mr. Ananda Mukerji: Yeah, I think this industry has always faced, you know, strong competition from various kinds of players. We have had, you know, the IT, the IT integrated players being there right from the beginning. We have had the MNCs like, you know, IBM's of this world being active in this industry. So, I think it has always been competitive, but you are right. I think at this point in time this is the industry segment which is probably growing faster than some other alternative segments within the IT/BPO space. So, there is more interest from players out here. So, there is competitive pressure, but I think we have, you know, if you look at our strategy Mitali, we have focused on certain areas of the business where we believe we have competitive strength and can compete with anyone over there and in our business segments, I think we are fairly strong. If I look at the healthcare segment, we are probably the largest player amongst any of the players whom we compete with in that business segment. We probably have the more comprehensive set of offerings out there in the market place. So, I think we have a very strong competitive position out there. In the telecom space, I think we are one of the larger players in terms of the customers we have, the kind of work we do, the depth of what we provide on this. I think we have a strong competitive position. In BFSI, similarly in the areas where we specialize in, say credit card collections, I think we have a strong competitive position. So, I think we have chosen segments of work where we have the ability to compete, but having said that, clearly it is, you know, the competitive position as also the fact that the economic environment which is facing our customers does lead to, you know, some amount of pricing pressures and we have seen the pricing pressures impact us, you know, in terms of our numbers already and I suspect that some of that pressures are going to continue in the coming quarters. That is something sort of we are dealing with. There is enough room to improve our productivity and efficiency of our operation and that is something we will continue doing.

Ms. Mitali Ghosh: On pricing, last time I think you had mentioned that commission rates I think in collections had actually moved up in some cases and I think in the healthcare side you were seeing some possible pricing pressure. So, you know, could you elaborate a little bit more in terms of are there any differences in pricing trends in your different segments?

Mr. Ananda Mukerji: Yeah, that's right. I think on the collections side we have seen an increase in some of the commission rates and that has contributed to the fact that the collections performance in this quarter has been a little bit better than what we had planned. I think they also have done a far better job in terms of their productivity and improvement as well. On the healthcare side, yes, we are seeing continued pressure as our customers are facing a tough environment and that is something which continues. So, in different parts of our business, we are seeing different kind of pressures, but by and large customers are looking for obviously better value proposition from their customers and, you know, quite often are prepared to look at ways in which that can be delivered in terms of delivery models, you know, service levels, and they would visit service levels and look at whether those service levels are really needed or not. So, I think that kind of dynamics are going to continue.

Ms. Mitali Ghosh: Yeah. Then just finally one question on the margin outlook, I think you said that you should have better margins for FY10. You know; if we look at the last few years, I think the margins have come off from, you know, the 11-12% kind of levels, at least in let's say FY08 to about 8% kind of levels now. So, you know, what do you see your sort of long term margins stabilizing at?

Mr. Ananda Mukerji: See, I think at this point we are probably not in a steady state right now in terms of the business environment, so I don't think this year is the year when we are likely to reach our normal steady state margin levels, but I have said that I think this business should operate at a kind of a low teens kind of an operating margin level in a normal business environment, but I think this year is probably not normal and I think there continues to be uncertainties in our business, so which is why we believe we are going to see improvement, but it is probably a little premature for us to say that we are going to be reaching steady state any time soon.

Ms. Mitali Ghosh: And this, you know, when you are looking at this long-term margin, is this something that will driven more by scale or more by mix?

Mr. Ananda Mukerji: No, I think a combination, by scale, by efficiency, mix. If you look at our business Mitali, as I said, you know, at this point we are operating at, you know, 73% seat fill and that is the big drag on margins at this point in time. We have different business units which are, you know, some of which are significantly in an investment and a growth mode, so their margins are much lower than what it should be in a normal phase. We have segments of the business where there are, you know, sectoral challenges. So, I think once a lot of those things start to go away once the growth phase in our business which are growing start to stabilize, the economic environment start to get more normal, we will start to see the margins coming back to more normal levels, but I think even in this environment right now, I think because there is a focus on productivity and margin improvement, I think we will see, as I mentioned, we will see improvement in this year. We have seen a significant improvement in the last quarter to this quarter, but I think there are obviously some factors specific to this quarter out here, but overall I think we will continue to see improvement.

Ms. Mitali Ghosh: Thanks Ananda.

Mr. Ananda Mukerji: Thanks.

Moderator: Thank you very much sir. Next in line, we have Mr. Nimesh Mistry from MF Global. Over to you sir.

Mr. Nimesh Mistry: Yeah, hi everyone. I just wanted to understand the kind of deal wins during the quarter and also the ramps, I mean, the ramp-ups, in both telecom as well as BFSI vertical.

Mr. Ananda Mukerji: Yeah, we have had, you know, I think a number of deal wins and new business ramp-ups are taking place, but let me come back to you later with that in a little while. If there are any other questions, could you go on to that?

Mr. Nimesh Mistry: Yeah. My second question is on the grants, actually last year; you had said that you might not be receiving grants going ahead. So, was there an element of grants during the quarter and if that was, then how much it was?

Mr. Ananda Mukerji: Yeah, I don't remember what I exactly said, but I think the grants are as we add people in some of the geographies where we have government incentives; grants do come into the revenue stream. I think the point was that I think in the previous year, in fiscal 08, we have had significant grants because we had set up the operation in Northern Ireland and added a lot of people.

Mr. Nimesh Mistry: Okay.

Mr. Ananda Mukerji: That grant income has come in fiscal 08 and has fallen off in fiscal 09 comparatively. This year, we don't anticipate to see a lot of grant income, but there will be, you know, grant income coming in during the course of the year as business ramps.

Mr. Nimesh Mistry: Okay. How much was the amount in this quarter?

Mr. Ananda Mukerji: Sorry.

Mr. Nimesh Mistry: How much was the amount of grant during the quarter?

Mr. Ananda Mukerji: Yeah, 11 million rupees.

Mr. Nimesh Mistry: 11 million, okay. And how many people you wish to add in Ireland?

Mr. Ananda Mukerji: See, we are currently at about 1,200 people in Northern Ireland and I think we are more or less full-up on the capacity we have created there in the two centers.

Mr. Nimesh Mistry: Okay.

Mr. Ananda Mukerji: We are seeing continued demand from both our existing customers and potentially new customers for services to be delivered onshore. I think at this point in time there is a need for a delivery proposition which is both onshore and offshore and I think that is one of the strength of Firstsource is that we have a delivery model which is doing that for a while now in delivering an integrated solution across the onshore and offshore. So, we are seeing demand from our services onshore and we would be looking at adding capacity there probably within the course of this year.

Mr. Nimesh Mistry: And finally on tax rate, actually if I were to strip the, you know, one time and the credit on MAT which we have taken, what will be the tax rate, you know, in this year actually?

Mr. Ananda Mukerji: Yeah, Dinesh, could you answer this?

Mr. Dinesh Jain: Current year, we are expecting I think at consolidated level we should be around 20% level the tax rate, which is what I think we are looking at. The MAT credit is mainly in the India side, but there are tax liabilities which are in the US and other geographies.

Mr. Nimesh Mistry: Right, okay. And Ananda, I am, you know, expecting answers for my first question.

Mr. Ananda Mukerji: Yeah, let me answer that right now. We had 38 new wins in the provider in the healthcare industry, 1 in BFSI, and we had 2 ramps in the telecom and media industry.

Mr. Nimesh Mistry: Okay. And can you also brief in terms of in telecom what area, was that a new win from a new client or it was from the existing client and second is, on the term of the win, is it a long-term win or it is a one-year kind of a thing?

Mr. Ananda Mukerji: Sorry, which one was the long term or one year did you say?

Mr. Nimesh Mistry: Telecom.

Mr. Ananda Mukerji: Okay. See, telecoms is really, you know, as Santanu mentioned in his presentation on the business outlook, what we are seeing is our customers are getting into, you know, different lines of businesses within the telecom vertical. The industry is getting redefined and we are seeing people…players who were earlier in DTH are getting into broadband and mobility, people who are in mobility are getting into broadband. So, we are seeing a lot of lateral movements from players in this industry. So, the two deals we have won are one is on account of growth of an existing customer in a line of business in which we are in as a result of an acquisition they have done. The other is a new line of work which has been provided by an existing customer, a kind of work which we were not doing earlier. Now, these are all long-term, you know, relationships we have and in normal course, we keep getting growth in business either from market share changes or from penetration of the customer with new segments of work. So, these are all part of the long-term relationship with the customers.

Mr. Nimesh Mistry: Alright. Thanks a lot.

Mr. Ananda Mukerji: Okay, thank you.

Moderator: Thank you very much sir. Next in line, we have Mr. Sujit Joshi from Crisil. Over to you sir.

Mr. Sujit Joshi: Hi. Just one question, what is your dollar revenue number for this quarter please.

Mr. Ananda Mukerji: I am sorry, say that again.

Mr. Sujit Joshi: The dollar revenue number, consolidated level.

Mr. Ananda Mukerji: Dollar revenue number?

Mr. Sujit Joshi: Yeah.

Mr. Ananda Mukerji: Just one sec. 98 million dollars.

Mr. Sujit Joshi: 98, okay. And could you break up the growth in terms of volume, pricing, could you just give…and currency fluctuations, how much did that impact your top line growth?

Mr. Ananda Mukerji: Can we come back to you and sort of address that separately with you. We don't have that analysis ready.

Mr. Sujit Joshi: Okay, sure, not a problem. That's it from my side.

Moderator: Thank you very much sir. Next in line, we have Mr. Ajay Nandanwar from India Capital. Over to you sir.

Mr. Ajay Nandanwar: Actually, I have a question about your balance sheet sir, what is the current debt and cash position as well as working capital position?

Mr. Ananda Mukerji: I am sorry, could you repeat that.

Mr. Ajay Nandanwar: Your current debt and cash positions?

Mr. Ananda Mukerji: Debt and cash position, just one sec.

Mr. Carl Saldanha: The total debt right now is 1,344 crores that basically consist of an FCCB outstanding and two external loans, one in the UK and one out of US.

Mr. Ajay Nandanwar: And could you please give us details of each of the loans, the two external loans?

Mr. Carl Saldanha: Well, the FCCB outstanding as of June 30th is 212 million dollars.

Mr. Ajay Nandanwar: Okay. This is after amortizing the interest cost or…

Mr. Carl Saldanha: This is basically after buyback. The original FCCB was 275 million dollars. As you know, we bought back roughly 62 million dollars, so the net amount now is 212 million dollars.

Mr. Ajay Nandanwar: Okay. Sir, this is including the amortization of the interest or…

Mr. Carl Saldanha: If you include the amortized interest year to date would be 225 million dollars.

Mr. Ajay Nandanwar: Okay.

Mr. Carl Saldanha: In addition to that, we have an ECB loan out of the UK which is 25 million dollars and we have another 20 million dollars in loans in the US.

Mr. Ajay Nandanwar: 20 million in US and 25 million UK. Both are dollar denomination sir?

Mr. Carl Saldanha: I am sorry…

Mr. Ajay Nandanwar: Both are dollar denominated?

Mr. Carl Saldanha: No, one is in sterling, the one in UK is sterling.

Mr. Ajay Nandanwar: Okay. And net cash at this point or cash at this point?

Mr. Carl Saldanha: Rs. 79 crores.

Mr. Ajay Nandanwar: Okay. Sir, what is the working capital position?

Mr. Carl Saldanha: I will just get back to you; I will get back to you during the call.

Mr. Ajay Nandanwar: Okay. Thanks. Thanks so much.

Moderator: Thank you very much sir. Next in line, we have Mr. Srivatsan from Spark Capital. Over to you sir.

Mr. Srivatsan: Yeah, hi. Just wanted the other income of about 12 crore rupees, it is mainly due to cancellation of hedges or due to write-back of mark-to-market provisions, just wanted to know that?

Mr. Ananda Mukerji: The gain of 12 crores?

Mr. Srivatsan: Yeah, in the other income.

Mr. Ananda Mukerji: That is due to cancellation of hedges.

Mr. Srivatsan: Okay. Sir, what is the tax rate outlook for the year?

Mr. Ananda Mukerji: Srivatsan, I can't hear you.

Mr. Srivatsan: The tax rate outlook for the year.

Mr. Ananda Mukerji: The tax rate, we are expecting about 20%.

Mr. Srivatsan: Okay. Thanks, great. I will come back later.

Moderator: Thank you very much sir. Next in line, we have Mr. Madhu Babu from Systematix Shares. Over to you sir.

Mr. Madhu Babu: Yeah, hi sir.

Mr. Ananda Mukerji: Hi.

Mr. Madhu Babu: Sir, regarding the ramp-ups in Q2 you are talking of, whether these ramp-ups will happen in US delivery centers or in India?

Mr. Ananda Mukerji: I am sorry, I couldn't hear clear, can you repeat that please.

Mr. Madhu Babu: These ramp-ups you are talking of in Q2, there were some costs associated with the ramp-ups in Q2 you said

Mr. Ananda Mukerji: Right, right, right.

Mr. Madhu Babu: So, whether these ramp-ups will happen in onsite or in India?

Mr. Ananda Mukerji: Both. We are seeing increase in India as also in the US. In US, our collections business is expanding, we had one site in the US, and we are expanding in a second site right now. Our healthcare business, provider business is expanding as we are adding clients, we are adding people there. We are adding people in the Philippines as we speak and there is growth in the Asia Business Unit as ramp-ups with customers take place. So, across the board, there is people being added.

Mr. Madhu Babu: Okay. And sir, despite the challenging economic environment, the attrition is at 33%. So, do we understand that this would be the long-term attrition rate in the company?

Mr. Ananda Mukerji: No, if you look at the attrition rates, you know, if you look at, there are three attrition rates which you need to look at. The offshore attrition rate, the onshore attrition rate, both have come down quite significantly from Q4. One which is high is the domestic attrition rate and that is really a function of, as I mentioned in my initial remarks on function of the fact that the business is in a ramp mode and has not yet reached steady state and typically at this point in time you tend to add more people than you need and then you allow that to come down and that reflects in the attrition numbers. As also, it needs to reach stabilization before attrition stabilizes. So, I think those numbers will certainly come down when it stabilizes.

Mr. Madhu Babu: Okay sir, thank you.

Moderator: Thank you very much sir. Next in line, we have Mr. Ranjit Shinde from Economic Times. Over to you sir.

Mr. Ranjit Shinde: Yeah, hi there. My question is about receivables, I mean, during the quarter, I think the DSO has increased by about three days. So, I wanted to know how it is panning out across various verticals and which verticals are facing, I mean, is there any problem with collectibles and how the outlook appears there?

Mr. Ananda Mukerji: Yeah, I mean, I think it is fair to say that, you know, receivables management is obviously more challenging in tougher economic environment than it is in easier economic environment. So, yes, it is a focus for us and, you know, customers tend to take a little longer to pay at this point in time. There is really no specific customer which are of any concern to us. These are all customers with whom we have worked with for a long time, so we really don't have so much concern around it. It is not anything specific to any geography, but, you know, the DSOs were higher in the end of the quarter and have subsequently come down.

Mr. Ranjit Shinde: Okay. And about capacity fill factor, this quarter it was about 73%, what is the general trend for your kind of business and where is the, what would be your target for that?

Mr. Ananda Mukerji: Yeah, you know, historically we have been, you know, as high as 90% in terms of seat fill factor and we definitely want to see it incrementally moving up, up from this 73% level certainly into the 80s and that is something we are driving towards and hopefully we will still continue to show in a steady improvement. We recognize it is a big drag on numbers, but unfortunately it is somewhat inherent to our business is that, you know, capacity has to be created a little bit ahead of time and when we are trying to create delivery models, you know, as aggressively we have in the last couple of years, we will end up with surplus capacity in different pockets of our business and we will have to work towards bringing that into a more normal level when that phase gets completed. So, yes, we are focused on getting it up and we expect we should be able to get it up into the 80s over time.

Mr. Ranjit Shinde: In what way Firstsource will be benefited or is it already getting benefited due to the entry of new telecom operators in India, like some of the operators have already started ramping up very quickly, they are adding good number of subscriber base, so what is Firstsource's outlook about it?

Mr. Ananda Mukerji: Yeah, I think the telecom industry is one industry where we see a lot of growth potential. It is clearly an industry which is booming in India and, you know, we are fortunate that we have already established a strong presence in this industry. We work for three of the top five telecom companies in India and, you know, I think there is a lot of growth coming from just those companies expanding their business, getting new segments of the telecom industry and, you know, with new areas like 3G licensing and all coming in, I am sure there is going to be even more opportunities from these players. Obviously, there are a lot of new players coming in as well and that also is an opportunity for expanding our business, so overall we are positive about the prospects of growth in the telecoms industry.

Mr. Ranjit Shinde: Thanks so much.

Moderator: Thank you very much sir. Next in line, we have Mr. Sunil from Credit Suisse. Over to you sir.

Mr. Sunil: Hi. Thank you very much for taking my questions. Sir, I had just a couple of questions. Firstly, on the Credit Card Act that you mentioned that is coming about in the US, what exactly is that about and how does it impact you?

Mr. Ananda Mukerji: Sanjeev, can you take that question?

Mr. Sanjeev Sinha: Yeah. There are a number of different developments that we believe can happen. Firstly, the overall credit card financing will come down, so the size of the market will shrink to some extent. Secondly, the interest rates on cards will be capped. So, banks cannot raise rates. So, putting them under some pressure on the top line and therefore, they will have incentives to lower the cost and that we see as, you know, a positive for us. We also believe that the top three card issuers would expect about, you know, up to 10 billion dollars in revenues. So, overall there will be shrinkage in terms of credit availability. There will be pressures on these companies to reduce cost which we see as a positive and the size of the market would shrink a bit. So, broadly these are key impacts that we see.

Mr. Sunil: Okay, thank you. And the second question is, can I get a sense of how many seats you have in the tier II cities in India, like you mentioned about the new center in Bhopal, so similar to that, how many seats would you have in tier II cities?

Mr. Ananda Mukerji: Yeah, why don't we come back to you a little later. Somebody will just compute that and come back to you.

Mr. Sunil: Okay sir, thanks for that. Just my last question, the Asia Business Unit has, if I am right, around 11,000 employees, but still contributes just 10-12% of revenues. How is the profitability of that business?

Mr. Ananda Mukerji: Yeah, I think that business is, as I was mentioning while I was addressing another question earlier, that business is in a ramp and growth phase right now, so the profitability of that business is obviously not where it should be, or will be in a steady state. So, it is really at this point in a growth and investment phase. So, it is not at a level where we expect it to be.

Mr. Sunil: But can it become, when it reaches a steady state, can it become, can at least the margins or the EBITDA become comparable to or be proportional to the number of employees that the segment has?

Mr. Ananda Mukerji: I don't think we would look at it in terms of employees as the basis for measurement and the reason is because, you know, employee cost also varies quite significantly depending on where you are delivering it from. For example, an employee in Bombay costs very different from an employee in say Hubli as does an employee in Bombay compared to an employee in Buffalo, NY. So, we don't really look at, you know, productivity or revenues per employee in that sense because our business has many different components and that would that would be probably simplistic for us to gauge it on that basis. The way we would look at is in terms of are we expecting to generate the same amount of, you know, operating profit or EBITDA percentage out of that business as other business and I think our expectation is that, you know, over time this business should be able to get the same level of profitability as other businesses.

Mr. Sunil: Sure. Thank you very much.

Mr. Ananda Mukerji: Yeah. Okay, I think the other question you asked was, yeah, tier II cities we have about 6,000 seats, the answer to your question.

Mr. Sunil: Okay, that was very useful. Thank you sir.

Mr. Ananda Mukerji: Okay. Before we get to the next question, I think there was a previous question on the working capital. Carl, will you just answer that.

Mr. Carl Saldanha: The working capital, the current assets as of June 30th is 533 crores. The current liabilities is 240 crores. So, the net current asset is 293 crores at the end of the quarter. From the previous quarter, we have actually grown by 40 crores, but since then, we have recovered from the receivables, we have come down a bit, so that's why our receivable position is actually much better right now.

Mr. Ananda Mukerji: Okay, back to the moderator.

Moderator: Thank you very much sir. Next in line, we have Ms. Priya from Inspire Capital Management. Over to you ma'am.

Ms. Priya: Hi everyone. I just have one question, how much portion of revenue is voiced based?

Mr. Ananda Mukerji: Sorry, say that again.

Ms. Priya: How much portion of the revenue is voiced based, I mean, can I have segregation between voice based revenue and nonvoice based?

Mr. Ananda Mukerji: Yeah, I mean, I think our amount of revenues which comes from, you know, customer service or call center activities is about 30%.

Ms. Priya: 30%, okay. Alright, that's it from my side. Thank you.

Moderator: Thank you very much ma'am. Next in line, we have Mr. Dipesh Mehta from Khandwala Securities. Over to you sir.

Mr. Dipesh Mehta: Yes sir, I have only one question, can you explain the movement in reserves from last quarter to this quarter?

Mr. Ananda Mukerji: Movement in?

Mr. Dipesh Mehta: Reverse and surplus on the balance sheet side?

Mr. Ananda Mukerji: Yeah. Dinesh or Carl.

Mr. Dinesh Jain: I think our reserves have moved down from 9,512 to 9,290 million. It is basically on account of translation of our integral subsidy where the dollar rate has moved down from 50.50 to 48.75. So, that is the main impact because when you do the AS30 accounting, that is the treatment that takes place, we have also added during the quarter the profits which have increased the reserve as well as one more major component is the FCCB where we provide for the accretion of the interest through their fair premium account, which account for around 139 million. I think these are the three main components which have changed the reserve from Rs. 9,512 to 9,290 million.

Mr. Dipesh Mehta: The FCCB you said is positive or negative?

Mr. Dinesh Jain: It is negative; it reduces because your liabilities get reduced.

Mr. Dipesh Mehta: Yeah.

Mr. Dinesh Jain: It is basically the hedging reserves have reduced the liability.

Mr. Dipesh Mehta: And it is around 14 crore you said?

Mr. Dinesh Jain: Yeah.

Mr. Dipesh Mehta: Okay.

Mr. Dinesh: Premium is 14 crores.

Mr. Dipesh Mehta: Okay, thanks.

Moderator: Thank you very much sir. Next, we have a followup question from Mr. Ajay Nandanwar from India Capital. Over to you sir.

Mr. Ajay Nandanwar: Good afternoon sir. Thanks for the information on working capital. Sir, I have just a follow-on question on the Asia Business Unit. What is the capital invested in this business?

Mr. Ananda Mukerji: I am sorry, your line is not very clear, can you say that again.

Mr. Ajay Nandanwar: Thanks for the information on working capital.

Mr. Ananda Mukerji: Yeah.

Mr. Ajay Nandanwar: A follow-on question about the Asia Business Unit, what is the capital invested in this business?

Mr. Ananda Mukerji: We don't allocate capital by businesses in a sense that because capacity is in a sense utilized by other businesses and we don't track it on that basis?

Mr. Ajay Nandanwar: Sir, I guess let me ask you the question differently, the 8,500 seats roughly in this business, what is the Capex per seat?

Mr. Ananda Mukerji: What is the Capex?

Mr. Deep Babur: The Capex per seat would be roughly about 3,000 dollars.

Mr. Ajay Nandanwar: Of?

Mr. Deep Babur: 3,000 US dollars roughly, so about 150,000 Indian rupees.

Mr. Ajay Nandanwar: 3,000 US dollars even for the Asia Business Unit?

Mr. Deep Babur: That's right, for the Asia Business Unit, but again just to clarify, the seats that we mentioned are very indicative and as Ananda mentioned, we don't really, we can't specifically allocate it to each business unit or each vertical, but if you want to take a higher level, you can use the number of seats and multiply by 150,000, then set the capital invested.

Mr. Ajay Nandanwar: Okay. And sir, would this unit be running at similar EBITDA margins as your remaining business?

Mr. Ananda Mukerji: I think I mentioned that, you know, the business is currently in a growing and ramping, so we are adding capacity, adding people, so clearly will not be at the same level as other business.

Mr. Ajay Nandanwar: Got it. Sir, you know, it seems like since your Capex per seat is not too different than that of international business, but the revenues are much lower, so how do you look at the return on capital from this business?

Mr. Deep Babur: I think just a comment here. In fact, the capital, Capex will be significantly lower than in the international business. International will be at least 6,000 dollars if not more, 6,000 to 8,000 dollars is what it could cost in the, you know, for an offshore delivery center located in India or for that matter in Philippines as well. So, the Capex is about half than that what we see in an international environment.

Mr. Ajay Nandanwar: But sir, the asset, the revenues from international are to the tune of 15,000 dollars or so and here they are coming to roughly 3,500 to 4,000 dollars per employee per seat.

Mr. Ananda Mukerji: Yeah.

Mr. Ajay Nandanwar: So, we need significantly higher margins to attain similar return on capital in that business.

Mr. Ananda Mukerji: Yeah, I think the point is that clearly it is an area of business which we believe is going to be a significant driver of growth. We believe that the Asia market is an important market both from a perspective of growth as also creation of capabilities and getting into new market. So, we think it is an important market from an investment perspective. I think the return on capital is also got to be seen in the context of what is the growth expectation from those markets and what we can expect to see over time. I think we expect to see margins comparable with other businesses in this area as well and I think the capital requirement is somewhat higher than other business, we expect that the growth which we get from those businesses over time will make it a business which is going to be valuable.

Mr. Ajay Nandanwar: So, sir, what is the hurdle rate in that case from the Asia business from, you know

Mr. Ananda Mukerji: I am sorry, say that again.

Mr. Ajay Nandanwar: What kind of a…given that I would imagine that the Capex required, you know, depreciates fairly fast…

Mr. Ananda Mukerji: Right.

Mr. Ajay Nandanwar: What is your internal hurdle rate, you know, for 3,000 dollars Capex per seat.

Mr. Ananda Mukerji: No, I think we have to….

Mr. Ajay Nandanwar: I am trying to see, you know, how 4,000 dollars revenue per seat with 15% EBITDA margins is coming to, you know, 1,200 dollars EBITDA on a 3000 dollar CAPEX, how that would, you know, on a fast depreciating asset, how that creates value, I am trying to understand how that creates value?

Mr. Ananda Mukerji: No, I think it creates value because over time you are able to both grow the revenues and the margins in the kind of business you are doing. You also depreciate your assets, but typically economic life of the assets are significant larger than the actual depreciating period of the asset. So, I think if I look at the economic value of the business over time, the business will generate a positive return on capital.

Mr. Ajay Nandanwar: Sir, one last question sir, what are you Capex plans for the next two years?

Mr. Ananda Mukerji: I think our Capex plan for this year is about…

Mr. Carl Saldanha: 15 million dollars.

Mr. Ananda Mukerji: 15 million dollars is the plan for the year.

Mr. Ajay Nandanwar: And how would the next year look in comparison to?

Mr. Ananda Mukerji: I mean we haven't forecast for Capex requirement for the fiscal year 11. I think, as I have mentioned, we have a fair amount of capacity which we have created, so I expect that we will be, in terms of addition of capacity, it would be more moderate in this year and the next year compared to, you know, what kind of capacity we have set in right now, but I think the capacity we will create depending on what kind of business we see, so I think it is a little premature to try to predict fiscal 11 Capex requirement.

Moderator: Thank you very much sir. Next in line, we have Mr. Srivatsan from Spark Capital. Over to you sir.

Mr. Srivatsan: Yeah, hi. Just wanted to get an update on MedAssist mainly because when we acquired, we were about 100 million dollars with 20% profitability, but looking at the overall margins, it seems to be, the profitability seems to have plummeted even in the MedAssist business. What is driving this low profitability on this business?

Mr. Ananda Mukerji: Yeah, I think, as I have mentioned, the profitability in the healthcare business is... There is a lot of background noise, can you please mute your line?

Mr. Srivatsan: Just a second.

Mr. Ananda Mukerji: Yeah. Okay, so, as I mentioned, there is some pressure in the healthcare industry right now because of the unemployment issue. So, that's why margin has been affected to some extent. I will let Mike, you know, explain what the margin trends are and what are the factors we expect to see by which margins will move. Mike…

Mr. Mike Shea: Yes Ananda, I think it is, as we look at our margins, we have had significant ramp, number one, we invested heavily in our sales organization and infrastructure as well in order to get to the growth targets that we have set for that quarter. So, that is probably the largest secular area. We have seen some pressures on price and that would be another one of the drivers, but those are the primary two.

Moderator: Thank you very much sir. Next, we have a question from Ms. Mitali Ghosh from Merrill Lynch. Over to you ma'am.

Ms. Mitali Ghosh: Yeah, thanks. Just two quick questions. One is if you could update as on any discussions you had with Fidelity post the Metavante acquisition, you know, both as a shareholder and as business partner?

Mr. Ananda Mukerji: Yeah, we have spoken to Fidelity, but as you might be aware, their merger is still not completed and they are still in the process right now. So, I think they are quite busy right now with getting that process completed. In our conversation with them, what they have told us is they don't intend to make any immediate change in the way we are operating, so I don't anticipate any change in the short run from that. We will have to wait and see once their merger is completed and, you know, at that point we will have a better sense of what we want to do with them in the future.

Ms. Mitali Ghosh: Any timeline in terms of when they might expect to complete it that they may have shared?

Mr. Ananda Mukerji: No, I mean, I think right now they are in the process of getting Antitrust Approval. It would probably not be appropriate for me to predict a timeline.

Ms. Mitali Ghosh: Right. And secondly, just on the tax I wanted to check post the extension by one year, what should one expect for next year tax rate?

Mr. Dinesh Jain: I think the next year tax rate, again that component one year extension is I don't think going to be hugely beneficial because I think combination of other than India taxes, plus the domestic business is going to play a role because the domestic businesses are taxable. I think up to the time the change on a domestic BPO industry tax structure, I don't see it is going to come down by one year extension. We will probably be at the similar levels of tax rate.

Ms. Mitali Ghosh: Okay. Thank you.

Moderator: Thank you very much ma'am. At this moment, I would like to hand over the floor back to Mr. Ananda Mukerji for final remarks.

Mr. Ananda Mukerji: Okay, thank you everyone. I think, as I mentioned, we have had a quarter and good start to the year. While I see business outlook continues to have uncertainties ahead, we are positive that the overall proposition which we have continues to be very strong. I think the delivery model we have which is the ability to deliver both onshore and offshore, the verticals we are in, all of them are going to stand us in good stead in the coming quarter, so we feel that we will be able to see positive growth and profitability improvement in this current year. Thank you.

Moderator: Thank you very much sir. Ladies and gentlemen, thank you for choosing WebEx's conferencing service. That concludes this conference call. Thank you for your participation. You may now disconnect your lines. Thank you and have a great day.