"Saksoft Limited Q2 and H1 FY21 Earnings Conference Call"

November 9, 2020

MANAGEMENT: MR. ADITYA KRISHNA, CHAIRMAN AND MANAGING DIRECTOR, SAKSOFT LIMITED
MR. NIRAJ GANERIWAL, CFO, SAKSOFT LIMITED

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Saksoft Limited Q2 and H1 FY21 Earnings Conference Call. This conference call may contain forward-looking statements about the company which are based on the beliefs, opinions, and expectations of the company as on date of this call. These statements are not guarantees of future performance and involve risk and uncertainties that are difficult to predict. As a reminder, all participants' lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Aditya Krishna – Chairman and Managing Director. Thank you and over to you, Sir.

Aditya Krishna: Hello and Good Afternoon everyone, Welcome and thank you for joining us today. First and foremost, I hope you are all keeping safe and healthy. On the call, I have with me Mr. Niraj Ganeriwal, CFO, from the team and SGA, our Investors Relations advisors.

I would like to begin by emphasizing that Saksoft is a digital transformation partner for its customers whereby we help our customers both run the business and also assist them in change the business aspirations.

The pandemic has underscored the need for greater efficiency, improved access, and enhanced customer experience across all verticals. Organizations are increasing their technology spends in the new age technologies like cloud, automation, and analytics. We believe that companies that are in existence to address a specific purpose like Saksoft in providing solutions and facilitate the digitalization of companies are better placed to seize this opportunity. Our existing clients are well placed in discretionary spends and with the organizations increasing their IT spends, we believe this is advantageous for us.

I am happy to announce that over the last six months, we have added two new clients in the US in $0.5 million to $1 million portfolio. We have added these clients in transport and logistics and healthcare verticals. Revenue contribution from top 10 clients has increased from 55% in FY20 to about 60% in H1FY21.

For the first half of this financial year, on the geographical front, our key markets of US and Europe are witnessing improvement. I am pleased that we have been able to maintain our margins in this competitive environment on the back of our dedicated Team model. We have been able to retain talent and generate superior people productivity to provide effective knowledge-based solutions that transform to business health of our customers.

We will continue to invest prudently in the sales and marketing teams across the foreseeable future with regard to balancing the need to grow top line on the one hand and the need to report presentable quarterly performance on the other. I am optimistic that given the company's long-term positioning in two of the most attractive markets and its verticals widening, we are at the cusp of generating outsized shareholder returns.

We have been witnessing reasonable demand from some of focused verticals of Fintech, Transportation and Logistics, and Healthcare and e-commerce, renewing our confidence of a poised growth opportunity ahead. Our expansion into the infrastructure managed space in 2019 was timely. With the pandemic, the relevance of cloud, remote working, virtual desktops have increased, and is an enabler for the growth at Saksoft.

I am pleased to announce that the company has declared an interim dividend of Rs. 2.5 per share, 25% on equity shares of Rs. 10 each for FY21. Now, I will request Mr. Niraj Ganeriwal, our CFO, to take you through the financial performance for Quarter-2 and for H1FY21.

Niraj Ganeriwal: Thank you, Aditya. We will now go over the financial performance for Q2 & H1FY21./////

On the revenue side, Q2FY21 revenues were at Rs. 97.19 crores versus Rs. 87.19 crores in Q2FY20, which registers a growth of 11.5% year-on-year and 3.7% on quarter-on-quarter basis. For H1FY21, revenue is at Rs. 190.94 crores versus Rs. 178.39 crores during H1FY20 registering a growth of 7%.

Looking at the EBITDA, the Q2FY21 EBITDA is at Rs. 16.5 crores versus 16.16 crores in Q2FY20 having a growth of 2.1% on year-on-year basis and 11.1% on a quarter-on-quarter basis. The Q2 FY21 EBITDA margins stood at 17% vis-a-vis 18.5% in Q2FY20 and 15.8% in Q1FY21. For H1FY21, the EBITDA stood at Rs. 31.35 crores versus Rs. 32.33 crores in H1FY20. Despite the challenging environment, the margins of the company have been stable as a result of strengthening of niche capabilities in selling industry verticals.

Coming to the profit after tax, the Q2FY21 PAT before minority stood at Rs. 10.73 crores versus Rs. 9.76 crores in Q2FY20 registering a growth of 9.9% year-on-year basis and 5.9% on a quarter-on-quarter basis. H1FY21 PAT before minority is at Rs. 20.86 crores as compared to Rs. 19.27 crores during H1FY20 registering a growth of 8.3%, this resulted in the earnings per share being at Rs. 20.98 during H1FY21 versus Rs. 19.18 in H1FY20. The decrease in finance cost has also led to the improvement in the profitability.

The impact of currency movement on our revenues for H1 FY21 is about 3%. Based on the same, the pure volume driven growth in revenues is about 4% as compared to the previous year.

Looking at the revenue split by geography, America contributed 49% of our revenues, Europe contributed around 30% while the remaining 21% was from APAC and other regions.

The onsite and offshore revenue mix continue to be at 49:51 during the current half year. We expect the mix to be inclined towards the offshore in the subsequent quarters.

The revenue split across verticals is Fintech and Telecom contributed about 28% and 23% to the total revenues respectively, whilst Transport and Logistics, Retail and Healthcare and Public Sector contributed 9%, 10%, and 13%, respectively.

Saksoft has 6 customers of million dollar plus and 9 customers of USD 0.5 million plus. The total employee count stands at 1,225 out of which 1090 are technical and the remaining 135 are support staff. Utilization level of employees excluding trainee stands at 82% for H1FY21.

Now, moving onto the balance sheet, as of September 30th, our debt positions stood at Rs. 26.5 crores and cash position stood at Rs. 68.2 crores, which makes us a net cash company. We are a net cash company managing our growth from the annual surplus generations. Our renewed focus on collection of receivables has resulted in the debtor's collection period reducing from 67 days in FY20 to 59 days as on September 30, 2020. This has resulted in the improved cash balance as at the end of the current quarter.

For H1 FY21, ROE stood at 18.2% and ROCE stood at 22.7%.

That concludes the update on financials, and we will now open the discussion for Q&A.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Vaibhav Badjatya from HNI Investment. Please go ahead.

Vaibhav Badjatya: Sir, thanks for providing the opportunity, congratulations for steady set of numbers, I have two questions, firstly on the telecom vertical, we have seen growth continuing in telecom vertical, I understand that in 2019 it was due to vendor consolidation, but post that also the telecom vertical has continued to show healthy growth for us, so great if you can highlight actually what is driving this growth and what is the outlook for the same and what are the specific activity at clients end that drives our revenue?

Aditya Krishna: Our telecom focus is not on the typical B2C telecom companies that you can relate to like Reliance Jio or Airtel, our telecom customers are customers that provide cloud data center usage as well as data bandwidth, so the potential for these businesses is high and it continues to grow at a fast pace given the pandemic, so we are quite bullish about telecom in the coming years. Telecom is not B2C, it is more the B2B business.

Vaibhav Badjatya: So what kind of outsourcing work we are doing here for telecom, is it related to the demand for data activity and outsourcing activity to us and that drives our demand or what is the exact nature of activity that we are performing here for the client?

Aditya Krishna: I will give you an example, one of our telecom customers wants to digitize their approach to the market, so the way they deal with their customers, so the customer experience want to digitize, they want to make sure that their sales force uses digital products to prospect as well as acquire and onboard customers and for all that they need IT and that is where we come in and support them, so it is really digitalization of their entire business processes, which is where our specialty and focus is.

Vaibhav Badjatya: Okay, got it, and secondly on the subcontracting cost, there has been an increase in the first half as compared to first half of the last year, so just a bit of more details around what is driving the subcontracting cost, is it something that is there to, it will be at the same level going forward or it has to do with particular contract that we are currently executing?

Aditya Krishna: It is just a small abnormality which will get evened out in the coming quarters. We picked up some business, which required us to hire more subcontractors and this was typically unusual from what we typically do and we did not want to let go of this opportunity because we think that winning this customer or doing work for this customer will result in more business in the future, so that resulted in a little bit of a blip. In the coming quarters, this will get evened out.

Vaibhav Badjatya: So you mean to say in the coming quarters it will get evened out. Do you mean to say that portion of the work will be completed and that's why you will not need that subcontracting cost or you will convert that into in-house capability?

Aditya Krishna: I am assuming that you are referring to the fact that employee cost is a little higher as a percentage of sales, is that correct?

Vaibhav Badjatya: No, I am not referring practically I have not kind of given any emphasize to employee cost, I am just focusing on the subcontracting cost as you said that going forward that will normalize, so I mean to say whether that portion of the activity that requires subcontracting will get over going forward or you will develop in-house capability and what we have thought, we were originally subcontracting we will do it in-house and that is why it will reduce?

Aditya Krishna: Always whenever we do subcontracting, it is for that moment because we do not have that capability or that same level of quality capability that is in-house versus outsourced, so the idea always is that either we in source this capability or we build, we hire these people internally, so this will go away, you are right when you say that this level of outsourcing will disappear.

Moderator: Thank you. The next question is from the line of Ankit Agarwal from ARC Capital. Please go ahead.

Ankit Agarwal: Thank you for the opportunity, Sir I have couple of questions, the first one being do you see that the current digitization trend will benefit us in terms of increased order book for us over the next couple of years?

Aditya Krishna: Absolutely, that is where our growth is coming from, Ankit.

Ankit Agarwal: I mean can you quantify something or like some outlook on the same?

Aditya Krishna: As a rule, we do not give guidance, so focus is growth and this growth is coming from increased transformation in the digital space, which will continue I do not see any change or any decline there.

Ankit Agarwal: Okay Sir that is great, and second question, there is a small amount of debt on your balance sheet of about Rs. 27 crores and you did say that you are a net cash company, so any plans on repaying this debt?

Aditya Krishna: We can repay this debt very easily though, the only issue is that being a global company with 100% subsidiaries in different countries where we operate, very often the cash gets locked in these geographies, so you might have cash in the UK company, we might have cash in the US company. Now, the debt is in the Indian books, so now to move the cash from overseas to India, we need to do it through dividends sometimes that might not be the most prudent, so we are looking at it. It is not a priority right now for us because we rather conserve the cash given what is happening in the world and the uncertainty that the pandemic is presenting to everybody.

Moderator: Thank you. The next question is from the line of Arush Oberoi from Victor Deltor Securities. Please go ahead.

Arush Oberoi: Good Evening Sir, thank you for giving me the opportunity, couple of questions, first one is that as you mentioned the employee cost has been increased as a percentage of sale, so are we adding any professionals on the sales side or any other details you can throw?

Aditya Krishna: I will just repeat what I have said earlier, we will continue to invest in sales and marketing, but it will be based so that we do not have a blip which will result in reduced EBITDA margins, so the focus is invest in sales marketing, grow the top line, but at the same time report decent quarterly numbers, so the employee cost that you are referring to is a temporary thing quarter-on-quarter and it will happen, but it will get evened out in the coming quarters.

Arush Oberoi: Sir, the second question is that, the public sector vertical performance given the pandemic situation, how is the public sector vertical performance, are we seeing any traction over there?

Aditya Krishna: We focus on public sector only in the UK geography and given what has happened in the UK in terms of the economy, the Government has increased public sector spending. Now, there is a lot more opportunity in public sector, but we are deliberately ring fencing our growth in public sector because it is a business which is not relationship driven, it is a business which is driven by tender business, so what tends to happen is you win a contract for 3 million or 4 million, it is for three years, after three years chances are you will lose that contract because it gets re-tendered, so there is no because it is not a relationship driven business, the stickiness of revenue is much less than if it was relationship driven, so yes, there is opportunity in public sector, but we are not pushing aggressively on it, we rather grow in the private enterprise space than the public sector.

Moderator: Thank you. The next question is from the line of Amit Shah from SS Securities. Please go ahead.

Amit Shah: Good Afternoon Sir, I have two questions, one is can you highlight some of our niche capabilities on the healthcare side as this is very demanding vertical given the current environment, are we seeing any demand traction on this segment?

Aditya Krishna: Lots of demand coming up on this Amit, but to give you an idea of what is our capabilities, our capabilities are in the telemedicine space predominantly. We work more with the provider space, we do not work with the payer space, so there is a lot of opportunities for small healthcare ISVs, which reduce insurance cost, which reduce time to market. One of the examples I will give you is there is a law in the US that every language needs to be translated in a hospital, so we work with a company that specializes in providing translation services for patients and doctors when they visit the hospital, big business and gives you an idea of where the opportunity resides today.

Amit Shah: Okay Sir, are we witnessing further increase in EBITDA margin on the back of dedicated team model?

Aditya Krishna: Our EBITDA margins this quarter was 17% that is quite healthy, I would say that EBITDA margins will be at the same level, maybe little lower as we push for higher top line because as we push for higher top line, sometimes you will compromise on margins in the short-term and medium-term to grow the business, but I do not see EBITDA margins going much higher than 18%.

Moderator: Thank you. The next question is a follow from the line of Vaibhav Badjatya from HNI Investment. Please go ahead.

Vaibhav Badjatya: Thanks for providing the follow up, so I just wanted to understand the ESOP trust that we have and I think they have about 4% holding sitting there, so how does it actually work and how ESOP trust gets the share and from where the money comes to ESOP trust to subscribe to our shares and if there are losses in the ESOP trust, how are they treated in consolidation, great if you can just help me understand on this dynamic?

Niraj Ganeriwal: Just to answer your question that the ESOP trust is not buying any new shares currently. The shares were the ones which were already allotted at the time of the IPO, so a percentage of the shares were reserved for the employee stock option scheme and these are continuing from the IPO times, so they have not been any subsequent secondary market purchases in the trust. Accordingly, there is no loss also, there is only income which comes from the dividend, which is declared by the company, so that is the situation with the trust.

Vaibhav Badjatya: So as of now ESOP trust basically have the shares or currently has the right to get the shares whenever the trustees decides to get the shares, what is the current status?

Niraj Ganeriwal: The shares are in the trust, so the 5 lakh plus shares are a part of the trust, these are already allotted and they are listed, so it is not an option, it is a share which is already in existence and it is held by the trust.

Vaibhav Badjatya: Okay got it, so whenever basically then it will be just the transfer from the employee trust to the employees whenever that gets due to an employee, it will just get transferred from ESOP trust to that particular employee, right?

Niraj Ganeriwal: Correct, so if anyone is having options under this particular scheme which was through the trust, at that time it would just be a transfer from the trust. There is another scheme also which is like issue of primary shares in which case there would be new allotment happening, but if anyone is under the trust scheme then it would be just a transfer of share from the trust to that particular employee.

Vaibhav Badjatya: Okay and this trust as of now or going forward will not be doing any open market purchase activity like some of the other companies do?

Niraj Ganeriwal: Currently looking at the situation, we do not envisage because it is having a good number of shares depending on the other remuneration policy of the company and others if more options are granted it may, but in the near term we do not expect it to do a secondary market purchase.

Vaibhav Badjatya: Got it, that is on ESOP, and lastly, from a longer term growth perspective, it is quite encouraging that company wants to have the predictability in the business and wants to get a business which is sustainable over long term, but given the kind of opportunities that are throwing up in UK, public sector business, it is quite encouraging, some of the other companies are getting very good big contracts, maybe I do not know what you are thinking about it, but maybe it is a good idea to get those probably one-time contracts, invest that money into growing other business alternately in form of sales and some other activity, so that you know our annual numbers does not look very fluctuating, but we will build the capability by using that money, I do not know what is your thoughts on that because otherwise it would be very slow process to slowly win the scale up slowly there will be pickup in sales activity from us and then the engine will start, but if we get something like this, one time boost somewhere and can invest that one-time money into sales and marketing maybe that can accelerate the pace of our growth?

Aditya Krishna: It is a valid point, but please keep in mind that the public sector business in the UK is a tender business like I said earlier and the margin on this business typically is around 15% versus on average 30%-32%, so it is half of the normal margin, number one. Number two, it is not sticky, so you will lose it after two or three years, so both things are adverse. One, you will have a dip in revenue, second, margin is not so good, so that is the reason why we have deliberately decided to ring fence growth in public sector because if revenues come down then that becomes a difficult proposition to counter with more growth.

Vaibhav Badjatya: I understand that, but the interim cash that will get generated -maybe we can use that to drive long term sustainable growth, that is what my point is but I will leave it to you guys, you are still in a better position to decide on the strategy, and best of luck for the next quarter.

Aditya Krishna: Thank you.

Moderator: Thank you. As there are no further questions, I now hand the conference over to the Management for closing comments.

Aditya Krishna: Thank you for the questions. We would like to assure all our stakeholders that at Saksoft we are leaving no stone unturned and with a mix of verticals we are present in like the cloud, healthcare, and retail, we believe that we are in a sweet spot to leverage the opportunity and also de-risk our portfolio. I hope we have been able to answer all your queries. In case you require any further details, you may please contact us or our Investor Relations advisors, Strategic Growth Advisors. Thank you everyone for joining us, take care.

Moderator: Thank you. Ladies and Gentlemen, on behalf of Saksoft Limited, that concludes this conference. Thank you all for joining us and you may now disconnect your lines.