Mphasis
The Next Applied

27 January 2023

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Dear Sir/Madam,

**Sub: Transcript of the Investor(s)/Analyst(s) call**

Further to our intimation dated 20 January 2023, please find enclosed the transcript of the Investor(s)/Analyst(s) call which is hosted on the website of the Company at https://www.mphasis.com/content/dam/mphasis-com/global/en/investors/financial-results/2023/transcript-of-earnings-call-q3-2023.pdf

We request you to kindly take the above on record as required under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

Thanking you,

Yours faithfully,

**For Mphasis Limited**

NARAYAN SUBRAMANIAN

Digitally signed by NARAYAN SUBRAMANIAN
Date: 2023.01.27 15:51:52 +05'30'

Mphasis Limited BANGALORE

**Subramanian Narayan**
**Senior Vice President and Company Secretary**

Encl: As above

DS kk DS SN

Contact Us:
T : +91 080 67501000
F : +91 080 66959943
E : investor.relations@mphasis.com

www.mphasis.com

Mphasis Limited
Registered Office:
Bagmane World Technology Centre,
Marathahalli Outer Ring Road, Doddanakundi Village,
Mahadevapura, Bangalore 560 048, India
CIN: L30007KA1992PLC025294

# "Mphasis Limited
# Q3 FY 2023 Earnings Conference Call"
# January 20, 2023

**MANAGEMENT:** **MR. NITIN RAKESH – CHIEF EXECUTIVE OFFICER – MPHASIS LIMITED**
**MR. MANISH DUGAR – CHIEF FINANCIAL OFFICER – MPHASIS LIMITED**

**Moderator:** Good morning, ladies and gentlemen, and thanks for joining the Mphasis Q3 FY 2023 Earnings Conference Call. I am Aman, your moderator for the day. We have with us Mr. Nitin Rakesh, CEO of Mphasis, and Mr. Manish Dugar, CFO.

As a reminder, there is a webcast link in the call invite mail that the Mphasis management team would be referring to today. The same presentation is also available on the Mphasis website, www.mphasis.com, in the investor section under financial and filing as well as on both the BSE and NSE websites. Request you to please have the presentation handy.

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 star then zero on your touchtone telephone. Please note that this conference is being recorded.

Before we begin, I would like to state that some of the statements made in today's discussion may be forward-looking in nature and may involve certain risks and uncertainties. A detailed statement in this regard is available in the Q3 result release that has been sent out to all of you earlier.

I now hand over the floor to Mr. Nitin to begin the proceedings of this call. Thank you, and over to you, Nitin.

**Nitin Rakesh:** Thank you, Aman. And thanks, everyone, for joining us today. I know it's a busy day with multiple earnings calls and we appreciate your interest in Mphasis. I trust everybody has had a chance to review our earnings release documents, including the presentation. Though the macro environment has progressively gotten more challenging over the past few months, we continue to see interest in strategic areas of technology transformation. Enterprises continue to prioritize investments in areas such as cloud adoption, data engineering and strategic data assets, as well as areas like cyber security and customer experience and support transformation, as the latter also leads to a significant cost takeout opportunity given the high-cost base for customer support operations.

We see specific themes resonating across industries in 2023, including banking and insurance, themes that facilitate accelerated transformation and digitalization. Despite the resource environment easing up over the past couple of months, there is still scarcity of talent to address specific niches of segments in these areas. Our investment in Tribes that you heard me talk about previously are well aligned to play in these themes. On the other hand, vendors most exposed to offerings related to operating legacy tech architecture systems and data centers, mainframes and traditional support, etcetera, may find budget in such areas getting squeezed in 2023.

Our consistent performance in Apps and in anchor verticals such as BFS is thanks to our ability to profitably play such themes. Our Q3 FY '23 revenue represents a 5.7% Y-o-Y growth in constant currency terms. Direct revenue declined 2.8% sequentially and grew 6.4% year-over-year in constant currency terms. Our mortgage LOB, largely represented by Digital Risk experienced significant volume ramp down in this quarter, the magnitude of which was unanticipated and unprecedented. This business has experienced a perfect storm hammered by the trifecta of the trajectory of rates, consumer price inflation and sluggish home sales, even as leading banks prepare for a mild recession in 2023.

While mortgage rates have resumed their decline in the recent times, the market remains hypersensitive to rate movements with purchase demand experiencing large swings relative to minor changes in rate, leading to a freeze up in activity in residential real estate market in the US. The contribution of Digital Risk, our mortgage BPS subsidiary now stands at 8.8% of third quarter FY '23 revenue. Within Digital Risk, the contribution of the most vulnerable mortgage sub-segment, namely origination and refinancing, has declined to 20% of DR revenue and within 2% of our overall revenue.

That being said, DR is a valuable piece of the business portfolio for the synergies and cross-selling opportunities it provides us on IT and applications with these same clients, as well as providing a key connect to the business owners at large banks in addition to the CIOorg. It allows us to pursue integrated deals, which we believe is a source of our competitive advantage in that domain. Given the extreme volatility that our mortgage business has faced, the headwinds which we regard as cyclical, our overall direct performance may not give an accurate representation of the state of the other LOBs, particularly in our focus areas. Hence, we have provided performance cuts excluding DR wherever appropriate.

Excluding DR, our Direct business has grown sequentially as well as 15% year-over-year in constant currency terms. Managing this duality is akin to running on a two-speed track. One having speed breakers applied with greater force in short order and the other one, in which we try to sustain robust growth in the face of economic headwinds.

In keeping with the duality theme, we are providing some growth numbers here excluding Digital Risk. Our financial year-to-date FY '23 direct revenue growth is at 24.5% in constant currency terms and compares with the FYTD constant currency of overall revenue at 17.3% for Direct business. Our Direct business accounted for 94% of revenue in this quarter. DXC's contribution to our revenue is now less than 5%, at 4.8%, and given the low and declining contribution of this business to overall revenue, Direct business growth reflects more fully in the overall growth.

Regarding geographic growth, Direct business in America has recorded an overall growth of 6.2% in constant currency, weighed down by the mortgage LOB. Excluding Digital Risk, the

US grew at 17% Y-o-Y in constant currency. From a services perspective, our application service line has been a driver of our growth with 19% growth in Direct Apps this quarter, following on from a 34% growth in the second quarter of FY '23, driven by market share and wallet share growth. We believe that continued strong Apps growth is a testament to our continued investment in the right service areas using our unique Tribes and Squads-led competency development model as well as our ability to leverage the repeatability that comes with this highly efficient, go-to-market and delivery construct.

Our anchor vertical, BFS, continues to enjoy market share gains. While the overall numbers are impacted by the decline in the mortgage LOB, excluding DR, Direct BFS grew 2% sequentially and 17.6% year-over-year in constant currency terms. While we continue to find gains from our positioning of Specialization at Scale in banking, we are also seeing the contribution of other new engines of growth, especially our smaller verticals such as healthcare clubbed in the Others segment that grew faster, registering a 37% year-over-year growth within Direct.

This robust growth of smaller verticals reflects the success of the NCA strategy about which we've spoken to you in the past. The NCA basket has grown 30% year-over-year in this quarter. We've also been able to add some marquee new logos with large spend pools, giving us further growth visibility as well as reinforcing our differentiation in new segments besides BFS.

As mentioned earlier, we continue to consolidate our standing within our key clients, resulting in market share gains. DR has impacted the growth of key client buckets as well. Excluding DR, all our key customer segments grew strong double-digit year-over-year in constant currency. As you can see from the charts, Top 5 and Top 10 clients have grown consistently, registering 21% and 20%, respectively, in third quarter in constant currency terms on LTM basis. Excluding DR, LTM growth for Top 5 and Top 10 is significantly higher at 29% and 31%, respectively.

Our Top 3 clients contributed to $150 million or more each in LTM revenue with the top client's LTM revenue contribution at over $200 million. Revenue from this client is already at an all-time high, is set for further growth with strong wallet share gains as well as the expansion of TAM into newer spend pockets in the last few quarters.

The average LTM contribution of our Top 5 clients exceeds $150 million as well. Our Top 6 clients were greater than $75 million, which we continue to believe is unique for a company in our category. Our Top 6 to 10 clients, ex-Digital Risk grew at 40% constant currency on LTM basis. Our 11 to 20 client bucket ex-DR grew at 30% LTM on constant currency basis as well. As mentioned before, NCA continues to lead with 30% growth year-over-year and is now meaningful to overall growth strategy.

We recorded TCV of $401 million of net new deals won in Q3 of FY '23, the second highest ever. We're happy to note that this is well above our recent quarterly average of approximately $300 million per quarter. 74% of the TCV is in new gen areas. Last quarter, that is in second quarter of FY '23, we have noted that our pipeline was up 18% quarter-over-quarter. Converting some of that has resulted in strong TCV this quarter. Over half the TCV in this quarter accrues from BFS, our anchor vertical, offering visibility of continued growth in this vertical.

We have won 5 large deals in this quarter, matching the previous quarterly record with one deal over $100 million TCV. While we retain our market share with BFS clients, our large deals are increasingly coming from other smaller verticals outside of BFS, such as insurance and healthcare. We still continue to generate a high percentage of our TCV through proactive deal pursuits where win rates are materially higher than in competitive RFP situations.

As we report our TCV on a net new basis, excluding renewals, we find the correlation between our Direct TCV and revenue growth to be reasonably high at 0.85. This correlation, while has declined recently due to DR ramp downs, the conversion of TCV into revenue on a gross basis largely continues to be on expected lines. Behind our strong TCV track record is our evolved and continuously evolving Tribes & Squads model, driving the themes of Cloud-led transformation. This model, which has helped us scale our ability to service the growing pipeline and to close more deals, continues to mature.

The portfolio squads within each tribe continue to ensure that we constantly evolve our solutions, adopting newer tools and methodologies. Almost all our pipeline is tribe-driven and is up 6% sequentially and 27% year-over-year despite record conversion from pipeline to new sold TCV in the last four quarters. Our pipeline is very distributed across verticals as well. BFSI continues to generate the highest share of pipeline at 56%, despite large conversions in Q3. Pipeline in ex-BFSI verticals has grown at 86% year-over-year, suggesting that our aggressive hunting beyond anchor BFSI segment and strategic hunting with large deals to drive NCA expansion is working well.

Coming to our client metrics, our track record in migrating clients from one revenue bucket to the next continues to be healthy. In this quarter, we've sequentially added to our count of clients in US $5 million and $20 million revenue categories. As mentioned, we won five large deals in this quarter taking the total large deals in the last four quarters to 13 compared to eight in the previous period.

Coming to our financial metrics, our margin philosophy affords us the flexibility to manage our profitability in this volatile environment. EBIT margin at 15.3% is within the stated band. And in this quarter, we have substantially improved the pyramid with fresher billing at an all-time high in absolute and percentage terms.

We have taken some proactive actions in line with the performance norms and intent to improve developer productivity and efficiencies. These actions have helped manage margins despite the significant Digital Risk revenue drop. Operating profits stayed broadly flat sequentially and grew 13.8% year-over-year to INR 5,354 million in the third quarter of FY '23. Our EPS for the quarter at INR 21.9, declined 1.6% sequentially and grew 14.7% year-over-year. Cash conversion measured as operating cash including one-offs, as a percentage of profit after tax, stayed at 90%-plus.

To sum up, I'll leave you with the following three points. One, our Direct Growth year-over-year, ex-DR stood at a healthy 15% in constant currency terms in the third quarter. We faced significant headwinds from the mortgage LOBs. DR is now less than 9% of revenue. That being said, mortgage services remain a bigger part of the business portfolio for the strategic benefits it offers that I talked about for cross-selling and integrated large deal selling.

Two, our KPIs are moving in the right direction, namely, our consistently improving track record in winning large deals with five large deal wins this quarter, including $100 million-plus deal. Over half the TCV originated from BFS vertical. Improving client metrics across the revenue bucket continues to strengthen our diversifying growth. As I previously stated, our average Top 5 client LTM contribution has crossed $150 million. Six to 10 clients continue to grow well above our Direct revenue growth with 30% LTM growth, while 11 to 20 clients have also grown in strong double-digits.

Our pipeline has grown 6% sequentially and 27% year-over-year. Further, while BFSI continues to be the bedrock of the pipeline and TCV gains, our non-BFSI pipeline has grown at 86% year-over-year, as the new engines of growth kick in. Our talent strategy and pyramid optimization is on course as well. Fresher deployment in percentage and absolute numbers is at an all-time high.

Three, operating within stated target operating margin band, we believe that the margin stance ensures margin stability in a volatile environment, especially in a seasonally weak quarter with significant ramp downs in one part of the business. Our EBIT margin of 15.3% lies within the stated band and our adjusted EBIT margin of 15.8% is stable sequentially and year-over-year. 2023 will likely see increasing vendor consolidation and we believe we are well positioned to be net gainers from this theme as demonstrated by our superior client mining and increasingly sharper strategic hunting.

To be sure, we are operating in an environment of increasing macro uncertainty, which potentially impacts certain decision-making of clients, thus affecting the pace of translation of pipeline in TCV and TCV into revenue, potentially requiring clients to repurpose their spends and reprioritizing spends across segments of tech investment, all of which can alter the complexion of near-term growth. We continue to believe that pipeline and TCV will be the lead indicators of outlook going forward.

Coming to our fourth quarter '23 outlook, it is about focusing on the micro in an uncertain macro. We believe that some of the pipeline that we have built up over the vendor consolidation theme should start to translate into TCV, beginning in the current quarter. We also expect to grow several of our top accounts sequentially, sustaining our market share gains, thus, despite being at an all-time quarterly high revenue, they continue to scale.

We will support our investments in farming and strategic hunting. Uncertain macro may well weigh on the market business in the near term. There are some pockets of discretionary spending weakness and growth trends here are subjected to tech budget swings. We are confident in maintaining our EBIT margin in stated bands. And given our actions and operational efficiency and productivity, we also intend to continue to invest in growth across the chosen business and technology segments.

With that, we can open the call for Q&A. Operator?

**Moderator:** First question is from the line of Mukul Garg from Motilal Oswal Financial Services.

**Mukul Garg:** Let me start with the mortgage part of the business, how should we see this in the near term? I know the visibility is fairly low right now. But obviously, and you have in earlier quarters also indicated that this is bottoming out before the shock, which we saw this quarter with the environment which is there in US. How should we see this business beyond maybe next one to two quarters? Is this something which is now coming close to stabilizing, or again, visibility is low here?

**Nitin Rakesh:** So Mukul, I think, first, let me explain to you the structure of our mortgage business as well as the State of the Union when it comes to the residential real estate market in the US. If you look at our current business, it's primarily made up of three buckets of services. First bucket is originations that used to be the only business we were in a few years ago. Just to give you a sense, we've seen a volume drop between refinance and new purchases of about 80% in the last four quarters.

And that is because the market for new purchases is completely seized up in the US given where the mortgage rates climbed to in the last quarter. Not only are home prices still at elevated levels coming out of the pandemic, but because interest rates spiked, buyers are basically finding these rates and these home prices unaffordable. It was still okay when the interest rates were low because that kind of gave them some leverage, but I think that's one part of the story.

To bring diversification into the business, as we stated many quarters ago, and we continue to talk about it, we actually added a home equity line to the business over the last few quarters. And that line of business has a negative correlation because as home prices were up and new purchases were down, you still had a lot of homeowners cashing in on the equity as the economic environment changed.

That correlation worked well for the last three or four quarters. But given just the total freeze in the market right now, we are also seeing a decline in volumes in the home equity business. And that's what we saw playing out in the third quarter. And the reason for that is, at some part of the economic cycle, home prices start declining as well and higher interest rates with lower home prices means the equity value start disappearing also.

The third line of the business that we have in the mortgage servicing side is servicing, which is a little bit more project-based because that involves diligencing loans that are bought and sold either between the government institutions, Freddie and Fannie, or between secondary buyers, from one bank to another or one capital market firm to another. I think the current environment in the market is, as I mentioned, is fairly frozen.

Activity volumes are very low, but this cannot sustain because if the market stays frozen and the delinquencies go up, which is what the banks are expecting, then the loans will start getting traded and the servicing line will pick up, which is the reason by design we had that line because we think that provides a certain hedge even if the interest rate cycle doesn't change.

We expect that to come to a head at some point between this quarter and next quarter. And hopefully gives us a little more visibility to volume pick up in the servicing side of the house. And eventually, of course, as the interest cycle peaks, the rest of the market will peak as well. So, I gave you a little bit more color. I think I wanted you guys to understand what is made up of that 8.8% of revenue across these three segments. We've seen big brunt of the origination decline already happen. I think the unknown variable really is the timing of cycle turning. So, it's very hard to hazard a guess. But the known variable is that at least in the short to medium term, we will see some parts of the market start unlocking and activity will start which will lead to opportunities and projects. We are very closely aligned with all our customers and we're using this opportunity to also gain more wallet share. And in fact, in many cases, they're using this opportunity to also make up for services that traditionally were not considered for us on the tech side. So, that's the second motion we continue to play with.

So, to kind of just summarize, I think the very short-term outlook is uncertain, but we think that as the market comes out of the freeze we will see opportunities on servicing and eventually, as well on the interest rate cycle.

**Mukul Garg:** The other question which was there was your TCV number continue to increase. Are you seeing increasing instances of longer duration deals forming part of your overall TCV? How should we think about TCV or deal duration perspective? How much of this can convert into revenue over the next four quarters?

**Nitin Rakesh:** Good question. In general, it is unusual to see very large banks  do very large tenure deals. So, I think that, that portion of the TCV continue to be a little bit more relatively shorter duration, but there are deals that do stretch out into multiyear as well. I think we talked about a deal that we signed -- that was a 10-year deal early last year. I think in the current quarter, the makeup is, I wouldn't say very unusual, we don't have very long-term deals, but we also don't have just short-term deals. So, it's a fairly good mix.

I think the reason we give the correlation metric is so you can actually see how they are going to convert to revenue. And while the caution had crept in over the last quarter or 2, I think for strategic deals, we are still continuing to see conversion being steady. But this definitely, it takes harder work for us to convert a deal and then convert that to revenue compared to this time last year. So, I think correlation  is pretty strong and that should give you a good visibility into the next four quarters.

**Moderator:** The next question is from the line of Kawaljeet Saluja from Kotak Securities.

**Kawaljeet Saluja:** Happy New Year, Nitin. A couple of questions. First, Nitin, is that when you look at our performance in the last three quarters, it has been fairly muted. Is it entirely due to mortgage exposure, or were there any areas in which Mphasis could have done better?

**Nitin Rakesh:** I think Kawaljeet, we've broken out the whole mortgage segment in granularity this quarter because I thought that was the right thing to do for you to get an understanding of what level of extent of decline that's provided. I think there are a couple of other pockets of weaknesses. None of them are not unknown to you.

So, they're all well understood. We called out the weakness in some segments in Hi-Tech last quarter. I think we had an unexpected furlough in Q2 and that continued in Q3 in that segment. We've also seen one or two of our larger relationships go through a short-term turbulence in their business, looking for short-term cost takeout opportunities. I think we've gained wallet share in those engagements in the very short term itself. And I think we're now looking at getting back on the growth path including in Q3, and of course, visibility for Q4 is pretty strong as well.

Answering your question of what we could have done differently. If we had a crystal ball, we could have figured out if there was something else we could have done to hedge against the interest rate cycle and I think the only thing we could have done was gone and look for projects on the servicing side, which typically are lumpier, but barring that, I think at a micro level, at an account level, we still have a majority of our Top 5 accounts at record revenue run rate in the fourth quarter.

We still have robust growth in Top 10. New clients have grown quite robustly. The new sectors we added, especially healthcare has actually done really well over the last four quarters as well. But I think the price we are paying for the portfolio is something that is visible to all including us and the only way to summarize it is that we cannot control what we cannot control. What we can control is the micro bottom-up account-by-account strategy that has worked very well for us and that's what we are focused on.

**Kawaljeet Saluja:** The second question that I had is on banking spends. In the last few days, a lot of the banks have reported, and it's a mixed picture out there, with Citi, BofA, Wells Fargo talking about an increase, Goldman talking about a cut and a lot of other banks talking about continuing of strategic priorities. I just thought I'll basically pick your point of view on how to read this myriad of data points on banking spending, what your assessment is? And where does Mphasis fit in in the overall scheme of things? Do you think that you'll end up being a significant gainer this year in the process?

**Nitin Rakesh:** Great question, Kawaljeet, I think the way to think about banking is to actually look at sub segments of banking in an environment like this because as you mentioned, you've talked about some clients that are increasing spend and you talk about some clients that are reducing spend. And I think the simplest way to think about it is that anybody who has a strong capital market linkage, anybody who has a strong linkage to deal volumes, M&A, IPOs, definitely that business is kind of locked up as well, and they are looking for ways to balance their costs compared to the declines they're seeing in that business.

But well diversified, large banks, that have a retail franchise, I think they're looking to use this opportunity to invest in getting to know their customers better and actually gaining a higher share of their wallet. And we've seen a lot of the deals in the last quarter or two that align towards the themes of, I want to modernize my customer experience, I want to modernize my core systems because we are not being able to respond to clients and the time trend we need to respond to. And that's leading to some significant opportunities in that segment.

And I think on a BFS ex-DR basis, we probably still have best-in-class growth sequentially and Y-o-Y. And I think that should tell you that we still think there is a large opportunity to gain wallet share and market share with the customers in this segment. And I think that's reflecting in the TCV numbers because if you look at the pipeline, we have 56% of the pipeline is still BFSI driven and if you look at current quarter TCV, almost 60% came from that segment. So, I think at least in segments that are not only exposed to capital markets, but we are also finding a very good set of willing buyers that are very focused on the themes of cloud, data, cyber, customer and modernization.

**Kawaljeet Saluja:** Just a final question to Manish. Manish, you have flexed every possible lever. Your utilization is up. You have utilized your sales and marketing leverage as well. That seems to be down as a percentage of revenues. Yet your margins refuse to budge from 15.3%. When does one see the much-awaited improvement?

**Manish Dugar:** Well, Kawal, we have stated earlier that the objective will be to invest for growth while maintaining margin in a stable narrow range. If you look at this quarter, you are right that we got the utilization improvement, although there is still opportunity to improve that. The fresher mix billability has gone up, at its highest ever and we also saw offshore mix improve. All of that does give us some wiggle room to make investments.

A large part of that kind of goes in managing the decline in the mortgage revenue and while we have an ability to manage the supply chain and the costs along with revenue decline, but this sudden decline led to a little bit erosion in the margins. As we go forward, I guess, our expectation is utilization should improve further because the fresher engine has started kicking in. And that, along with the revenue growth, we should certainly see an ability to report expanded margins.

**Kawaljeet Saluja:** Manish, I'm going to push it a little bit further. Let's say, what is required for you to take your margins up to 16%. And actually, let's not even talk about 17% because that seems to be outside the realm of possibility right now. But what is required for you to take the margin up to that 16% number?

**Manish Dugar:** The supply chain, if you remember, Kawal, when we guided that 15.3% to 17%, we were expecting the supply chain situation to become much better. It has improved over the last few weeks. Attrition has reduced, we're seeing lesser pressure on compensation. But we are still not at the place where we would like it to be. And this revenue decline was unexpected, with the significant tightening of the volumes because of interest rate movement was unexpected, and coupled that with the HELOC business as well, getting affected.

I guess the macro like Nitin mentioned, is not in our control. So, we can't say when the interest rate reversal will happen. But even without that, we should start seeing the revenue coming back on track. So, when the revenue comes back on track and we start seeing the supply chain becoming even more eased, there should be an expansion in margins. When we get to 16% is something that's difficult to say, but we should certainly be able to get to that not too long from now.

**Nitin Rakesh:** And Kawaljeet if I can just add to what Manish said, actually, firstly I'm very-very pleased with the fact that we've optimized a lot of these levers, whether it was lateral bench reduction, fresher reduction, off-shore increase. All of those have been efforts that we've been undertaking for the last few quarters.

I think the sudden disruption in the mortgage service line has obviously meant that we weren't able to keep cost in the same line as we would have wanted to. I think as this gets fixed, you will see margin expansion opportunities in the short to medium term as well.

**Kawaljeet Saluja:** I wish you a great year ahead.

**Nitin Rakesh:** Thank you.

**Moderator:** The next question is from the line of Abhishek Bhandari from Nomura.

**Abhishek Bhandari:** Nitin, I just had a question on your employee count and the hiring outlook. So this quarter, we have seen some bit of reduction on your employee headcount by almost 1,200 people, both on-site and offshore. Is it mostly to do with the continued attrition? Or there has been some involuntary attrition as well, keeping in mind what kind of demand outlook we have at least for the next few quarters? And if you could also highlight what are your hiring plans going forward?

**Nitin Rakesh:** So, I think firstly, Abhishek the headcount reduction obviously is in line with the optimization that we talked about. The biggest metric that I want you to focus on is record fresher adoption, both in absolute and percentage terms, given our track record since we have been tracking it.

What that means is that we have the ability to then optimize our lateral bench, both onshore and offshore because that gives us the ability to actually do upward movement from within the company and do a lot more fulfillment from within the company and hence our aging of bench has reduced, and our percentage of bench has reduced leading to high utilization as well.

Now that we've gone on this journey, we are not going to pause because remember, a fresher is only a fresher for one year. And a year later, you still have to then continue to stay on that treadmill, so you don't lose that pyramid shape. So, we have a significant number of freshers that are in Q4 on-boarding based on when we need them.

And we also have a pretty clear idea of their skill sets as well as the time required to actually absorb them into the billable workforce. So, I think that gives us the confidence that we can operate at a slightly optimized or a more optimized point of view. And hiring plans will continue to be optimized based on the demand forecast that we run for a rolling two quarter basis.

So, I wouldn't read the bench optimization as a view on demand forecast. But I would definitely read that as the restructured supply chain that we've been focused on over the last few quarters.

What percentage of hiring we will do, it all depends on the segment growth, what kind of productivity gains can we get and what kind of projects we are winning between managed services, fixed price and managed T&M and some of these transformation projects actually start heavier onshore and migrate offshore, which also means that some of those actions will continue to be applied as they move offshore.

I think I can't give you a number because we typically don't disclose what our hiring plans are on a going-forward basis. What I can tell you that the supply chain transformation work is work-in-progress, but we're pleased with the progress we've made and that's what's reflecting in the headcount metrics.

**Abhishek Bhandari:** Nitin, my second and last question is on your top clients and Top 2 to 10. So, do you see the furlough situation in your top client ending soon? And what is the outlook over there? And if you could also clarify the growth pattern of Top 2 to 10, because it looks like even Top 10 accounts growth rate seems to be moderating. It may be to do with the top line, but if you could clarify the Top 2 to 10 as well?

**Nitin Rakesh:** I didn't get your question on the top clients. I thought I actually addressed it.

**Manish Dugar:** The question was on Top 2 to 10. It seems to be moderating.

**Nitin Rakesh:** I think that's the reason we broke out the Top 5 and Top 10 metrics ex-DR business because that's what's muddying the overall growth of the Top 10 because there are DR customers in there as well. So, I think if you look at the number ex-DR that I called out, that will give you a little bit clear picture of what that other metric is, and I will repeat that for you.

If I look at the overall client metrics, if I look at clients in the six to 10 category, ex-DR, they grew 40%, CC LTM, 11 to 20 grew 30% LTM CC and one to five, excluding DR, Top 5 grew 29% and Top 10 grew 31% ex-DR.

So, I think that should give you a little bit of sense of what that overall number looks like as you strip that out. Having said that, I think we talked about select pockets of weakness that are also reflected in TMT and some of the other clients more attuned to the e-commerce volumes. There, that's behind us and those businesses are on track. I think we'll continue to watch the post-furlough impact on the Hi-Tech side as well, but at least to me, it looks like that’s behind us.

**Moderator:** The next question is from the line of Nitin Jain from FairView Advisory.

**Nitin Jain:** So, post the Q1 earnings call, the guidance was that revenue growth should pick up as the year progresses. But on the contrary, we have seen that the gap between TCV and revenue growth have widened with every quarter. And this is despite the TCV ramping up from the average $250 million that we used to do last year to almost $400 million now. So I mean, the numbers are kind of speaking for themselves. So, how bad do we think it can get in the short term before things actually start to look up?

My second question is on the margins. So, in like in the last three calls, the management has guided that there is an upward bias to the margin. And as the attrition cools down, there should be a significant pick-up in the margin. However, we continue to be right at the bottom of the guided band. So, are these margins net of the blink adjustment? Or it's not included in the 15.3%?

**Manish Dugar:** So Nitin, let me take the second part first, Manish here. The margins are reported margins after adjustment of dilution because of M&A. We did say that there is northward bias to the margins. And we have had events which has happened post those discussions leading to the expansion not happening.

For example, the Fed increasing the interest rate twice by 0.75% is completely unprecedented, which had an impact on the mortgage business as Nitin was explaining, leading to a significant decline in revenue. And while we had not just one, but multiple levers firing from an operating margin improvement perspective, a lot of those kind of got absorbed by the revenue decline.

So far as the growth is concerned, I think answer is really the same, with mortgage was not projected at that point in time. I would say that if you look at ex-mortgage, we are doing reasonably okay. And then outside of the mortgage business, the other businesses have had softness because of the macro effect, whether it is geopolitical situation or whether it is the inflation or recession, the conversations in the US. So, it's difficult to give a reconciliation between what we said in Q1 versus where we are today, but I think most of what has changed has been unexpected events and not necessarily something that we would have predicted at that point in time.

**Nitin Rakesh:** But just to put in context, this time last year, the consensus was four 25 bps rate hikes by the Fed in 2022 in a year, and we both know how that played out. So I think, again, the reason we broke out numbers ex DR is so you get a better sense of what that breakup of growth is and the breakdown of segments and sources of growth are. So, I'd hope that will give you, as you absorb the data we gave out in the earnings deck that will give you a little bit more color on how to think about it going forward.

**Moderator:** Mr. Jain, does this answer your question.

**Nitin Rakesh:** I don’t know, we lost him. Why don't we move to the next question.

**Moderator:** That is from the line of Nitin Padmanabhan from Investec.

**Nitin Padmanabhan:** So a couple of questions, actually. The first is, do you think the pace of decline that we saw this time, do you think the worst is in terms of the pace is sort of over and things should incrementally moderate? So, that's the first one. And maybe on an overall basis, do you think the overall impact on the portfolio wherein we saw a decline on a sequential basis, you think things should start gradually improving on a sequential basis from here on?

The second bit is, if you look at the mortgage business, you spoke about how the origination piece has anyway dropped 80% in volumes. And then the home equity is also seeing some decline. So, I was just wondering, do you believe that the home equity, is there risk within that business that could sort of see another bout of sort of headwinds for the overall revenue, was the second question.

And the third was in terms of new client additions, do you think that the pace at which we're adding new clients is strong enough, considering, I think we've done very well in terms of mining and growing and having a large proportion of large customers compared to anyone else of this size.

But in terms of new client additions, are you happy with that? And do you think that new clients as a proportion of revenue in terms of contribution over the last three years, how would that sort of change? Any context you could give there? And finally, do you think that Mphasis should really look at some kind of an acquisition to really offset or sort of improve the portfolio on an overall basis? So, those were the four questions.

**Nitin Rakesh:** Let me take the DR question first. I think, yes, the decline in originations at 80% seems to have taken a large beating. I think there definitely is some residual risk in the current book of business because we can't forecast what we control, which is the environment.

But as I said, the counter to that is that the market cannot stay ceased up for a very long time because this is the key part of the US economy. So, that will give us opportunities that will continue to provide some cushion to the decline. But the reason we broke out contribution of revenue is because we want you to get a sense of what that quantum can look like.

What we don't want to happen is the tail wagging the dog. So, that's the why the 8.8% contribution of revenue in third quarter revenue from DR will give you a sense of what the residual risk is and you can assume the rates and the quantum cannot sustain at this rate, of course, for a very long period of time.

We do believe that given the fact that a very large portion of the revenue in Direct is outside of that, we are only focused on accelerating growth in that given the positioning with large clients as well as the TCV wins that we have seen. The other question that you asked around NCA, if you look at the metrics, the NCA growth at 30% Y-o-Y, consistently been in that segment. It actually hasn't moderated in the last few quarters either.

We do believe that we have focused on a strategic hunting mindset where we're trying to bring in some marquee logos. While we announced a certain number of new client additions that meet our thresholds every quarter, I think it was four this quarter and five the previous quarter, we have another 20-plus customers that have been signed on just in FY '23 and many of those are large marquee logos in industries that we operate in, that we still think haven't met the revenue thresholds for us to announce them as new additions.

I'm giving that additional color because we track that separately. In our industry, some people call them hunting licenses, where we've actually become a strategic provider, we have an MSA in place, and we are now looking for opportunities in those accounts. And I'm talking marquee logos in healthcare, in travel and coordination, in retail, in banking, in insurance.

So, I think that should give you a sense that the hunting engine definitely has -- we operate with a phasing approach. Think about it, think of this as accounts signed up, accounts start generating revenue, accounts get the investments needed to do the mining and then they continue to grow. And that's the reason why we published the client pyramid and you can see that even in the 1 million and above customers, we've actually added clients almost every quarter, but that's only on the reported basis as well. So, there is another tale of clients that have been brought on and that will continue to contribute to growth.

And just to give you some more color, I think that number, I'm very pleased with, and it's a very-very healthy list of names that we managed to bring onboard. To remind you, this was not an easy job to do for any company in our industry until a few years ago.

The opportunity that has come up in the last two or three years is as every enterprise looking at the digital pivot and applying transformation, they're now looking for a new set of providers who actually have the ability to do that. And that opens up a crack in the door and that's what we've been leveraging on the last couple of years, including as recently as actually even the current quarter post Q3 as well. So, I think that should give you a little bit more color.

**Manish Dugar:** Just to add, Nitin, I think if you look at the pipeline growth year-over-year, while at an overall level, the pipeline has grown 27%, non-BFSI segment, which largely represents the new accounts added by the NCA channel, that pipeline has actually grown 86% and which kind of suggest that, like Nitin mentioned, we have more customers added, which are yet to scale, but even those that are scaling are actually firing on all cylinders.

**Nitin Padmanabhan:** I think two questions you missed was, one on the home equity side. Because the way I read it, I think home inventories in the US are around 8.5 months. The equity holdings of people are around $300,000, the highest ever. And their residual mortgages, whatever they have on those houses are 30 years fixed mortgage rate. So, do you see risk to that business on a going forward basis?

So that's one. And just one clarification, if I got this right, is the mortgage business sub $10 million at this point in time? Is that a fair assumption based on the data that you gave? And thereby, that shouldn't be -- maybe that's still rest of it, whatever goes away. And yes, so those are two things. And I think the last question was on the acquisition that I asked in terms of are you thinking of anything?

**Nitin Rakesh:** I think what I said was that the contribution of DR to quarterly revenue is 8.8%. So, you can do the math on that one. Addressing the question around home equity lines. I think, by the way, that business has more than doubled in the last four quarter for us on absolute dollar basis. Of course, that's one of the reasons why we were able to protect the contribution from DR over the last two or three quarters despite origination starting to decline quite rapidly at the beginning of last year. Is there a residual risk in that business in the very short term? The answer is yes, because even though there is home equity, getting a home equity loan at such high rates also is a deterrent for many homeowners.

So, we definitely think there is a definite residual risk in the very short run. We don't know what that will look like because we are obviously monitoring on a daily basis given that we run the business on a per transaction or on volume basis. But as I said that the servicing side of the house is where we think there is activity that will start picking up in the very short run as well. So, I think the 8.8% of revenue, you can assume what the breakdown of that will be and I'll be happy to give some more color on that if need be.

Finally, on the question M&A, I think, very important question....

**Nitin Padmanabhan:** Nitin, you had mentioned mortgage is 22% of DR, am I right?

**Nitin Rakesh:** Sorry, you mean originations?

**Nitin Padmanabhan:** Yes, originations is 22% of DR?

**Nitin Rakesh:** What I said was it has declined 80% year-over-year.

**Nitin Padmanabhan:** You didn't give a number on that. Okay, fine.

**Nitin Rakesh:** I don't think we break out, yes. We didn't give a number on that. Last question is on M&A. And I think the right way to think about it, is the question is very pertinent. I mean, if you noticed, we announced a new leadership position. We hired a new head of M&A that reports in to me because the intent is for us to look at not only tuck-in but also some strategic deals given the intent and the desire to grow faster in our chosen areas. There are multiple dimensions to that besides technology-led dimensions like we are looking for new tech capabilities. They could be tuck-ins or they could be at scale. We are looking for vertical-led capabilities, and we're also looking for geographical capabilities.

When we will do a deal, I mean, it's very hard for me to say given that the variance of valuations in public versus private markets is only now starting to fall in line. I think this year, 2023 will be conducive year for us to do some deal making. And at least that's our intent, and we're working hard at continuing to work on what we have in the pipeline as well as originating new deals in the pipeline aligned to these three or four things that I talked about.

**Moderator:** The next question is from the line of Mohit Jain from Anand Rathi.

**Mohit Jain:** Sir, one question outside BCM vertical and more related to service line breakup also. So, on the Application service side, what is your outlook if you exclude this whole BPM piece? And the second part, which is related is, if I adjust for BCM, in other verticals, how do you see growth panning out, say, over the next few quarters, given your TCV pipeline, etcetera?

**Manish Dugar:** Mohit, we looked at the pipeline data by vertical, if you look at it this time. And that talks about most TCV wins as well as pipeline growing at an overall level, plus growing for the non-BFSI segment at a faster clip. We have had some large deal wins which are outside of the BFSI segment as well. And specifically, healthcare and insurance, we see the TCV conversions to be very healthy. So, as we go forward, the growth by the BFSI segment should continue to see growth. The non-BFSI segment also has reasonable wins and the pipeline to kind of give us comfort on the growth going forward.

**Mohit Jain:** So, this is because 3Q appeared relatively flattish outside BCM also and also on the Application side. So, that's why I was trying to see if there is some incremental furlough or something else which you would have experienced in third quarter, which we should not expect to repeat in the fourth quarter?

**Manish Dugar:** Nitin talked about the fact that in one of the verticals, Tech vertical, we did see furlough starting Q2 and an incremental furlough in Q3 as well. And seasonally, Q3 is the weaker or a seasonally low quarter because of fewer working days and furlough. So, if you are talking specifically about Q3, yes, those are factors that has impacted each of those businesses. And some of that will go away in Q4, whether it is the furlough or the less number of working days, although the number of working days will not fully get recovered in Q4, it will really come back in Q1. But yes, if the observation is Q3 specific, yes, then it is driven by the seasonality and not necessarily any reflection on the business momentum.

**Moderator:** The next question is from the line of Abhinav Ganeshan from SBI Pension Funds.

**Abhinav Ganeshan:** I just had two very broad questions. First one is, what is our book-to-bill right now?

**Nitin Rakesh:** I think, traditionally, book-to-bill includes the renewals in the overall TCV number. We only report net new TCV numbers, and hence we report the correlation. So, I think you can make a...

**Abhinav Ganeshan:** Okay, got that. So, if I invert that broadly, that will either the book-to-bill?

**Nitin Rakesh:** **..**number based on those. Yes.

**Abhinav Ganeshan:** Sure. And a couple of other broad questions is what would be our aspirational utilization level over the medium term? And this correlation number since we are speaking about that, we've been at 90-plus previously, so, can we assume that, that would be our aspiration in the medium term?

**Nitin Rakesh:** I think we still think there is some room for upside in the utilization number because we are still, while we are no longer at the historic lows that we had two quarters ago, I think we are still at a point where we can see a 3% to 4% increase in utilization in the near term. It also depends on demand outlook, skill set match and the ability to redeploy internally trained talent. So I think there is upward bias in the utilization. On the correlation, I think, a big DR ramp down, obviously, takes the correlation down. As that ramp down goes behind us, the correlation will increase. And I think we had a previous high of 0.93. So, that's definitely something that we will continue to look in through above the 0.9 mark.

**Moderator:** The next question is from the line of Ruchi Burde Mukhija from Elara Capital.

**Ruchi Mukhija:** I have two quick questions. First, do you see any deviation in deal ramp-up compared to planned one, particularly given the macro environment?

**Nitin Rakesh:** So, I think we addressed that briefly. In select cases, yes, we are seeing that clients are taking longer to ramp up a deal given the scrutiny and the internal processes that they have to go through in some cases. I think the year-end budgeting cycle also sometimes interferes with that. We're still early in the New Year, we are still seeing some clients take a very cautious approach. There are instances, kind of one-off, but there are instances where clients have asked for a couple more months before they engage in a longer-term renewal and I think we are continuing to kind of work through those as well.

I think it's all a reflection of the fact that this zone of uncertainty where people are really forecasting what the recession will look like between soft landing, hard landing and deep recession, I think all of that is creating that uncertainty. But I think our job is, as I mentioned to worry less about the macro because we can't control it, but instead continue to work account by account in converting those deals and then converting those deals to revenue.

**Ruchi Mukhija:** Secondly, I mean this has been discussed in the call, but can you summarize what you meant for Q4? Do you see Q4 as a growth quarter or not?

**Manish Dugar:** So we talked about, the lead indicators for growth are, as you know, TCV and the pipeline and $400 million is one of the largest, second highest TCV conversion that we have had. And the pipeline has grown again over the previous quarter by 5%. Both of this does add to the confidence on the growth, kind of countered partly by the uncertainty that continues to exist on the mortgage business. So, it's difficult to give a number for the quarter. However, we should have a northward bias, Q4 should look better than Q3 for sure.

**Moderator:** Will take the last two questions. The next question is from the line of Ashwin Mehta from Ambit Capital.

**Ashwin Mehta:** So Nitin, you talked about the consolidation possibilities as you go forward. So, by when do you see the revenue impact of those consolidation possibilities and which segments are where you are seeing those consolidation opportunities? And my second question was to Manish. Manish, we had around INR 294 million loss because of hedges, which was taken to the revenue line this quarter. So, when do we start to see participation in terms of rupee depreciation on margins because that seems to be also depressing your margins?

**Manish Dugar:** So Ashwin, Manish here, I'll take the second question first. As you know, our treasury policy has been to assure us of certainty of currency rather than operate on a profit center basis and the stated policy was coverage of 80% for the next four quarters, maybe 100% for the next four quarters. And then on a gradual scale, reducing for the next four quarters. Three quarters back, we started seeing the exchange rate significantly strengthening, dollar strengthening. And we were already covered for four quarters.

And the gap between the hedge and the spot, became very high this quarter when we ended the quarter at 82.73, leading to a INR 29 crore impact of the hedge on revenue as well as on the bottom line. We have, for the last three quarters, started reducing our coverage keeping in line with our policy and towards the bottom end. So as we go forward, this coverage is reducing and we should be able to exploit the spot rate more and more.

However, there is still 1.5 quarters to go for us to become closer to 40%-50% cover and hence, unfortunately, if the exchange rate remains at these levels, we will see that opportunity loss in the P&L. And that's the cost of certainty over the risk that you would like to take.

And going forward, depending on how the dollar performs, if we kind of get a view that it will remain stable, we will start taking the cover, but we will be taking the cover at a higher exchange rate. So hopefully, we will either reduce this loss or get to a profitability on hedge again once we have kind of consumed the covers that we already have.

**Ashwin Mehta:** First question on consolidation?

**Nitin Rakesh:** Yes. Thanks. It's been a long day. Ashwin, the good news is that we are already seeing consolidation deals in the pipeline. As you can expect, the very first set of accounts where you will see opportunity in consolidation will be your large accounts, which definitely are right in the mix because we have a very strong positioning, strong account plans, strong track record and the likes.

Having said that, we are also seeing that given the dynamics I talked about, which is the fact that certain enterprises continue to look for new age providers, that can accelerate their transformation agenda, especially in banking and insurance, that is playing out really well because there is a lot of credibility and specialization that they're looking for, to impact that change very quickly.

But in terms of just in Q3 TCV, we actually have a large deal from a health care customer, and that is a new customer and the first deal itself is a large deal for us. So, I think we are even seeing, as we are looking for these new partners, as they want to move over from their legacy provider, you can call it consolidation or you can call it opening up of the tap for new providers. We are seeing opportunities open up there as well.

**Ashwin Mehta:** Just one follow-up, Nitin, in terms of our concentration, we have around 59% of revenues coming in from Top 10. So, any risks that we want to call out in terms of that?

**Nitin Rakesh:** Ashwin, I think at this point, nothing to call out, but much as much as large accounts are a concentration risk they're actually, equally a source of strength because they give referenceability, and the ability to actually not only be a reference customer for a new client, but also capability and competency pools can be reused and leadership is actually well attuned to how to scale the account.

So, I think to me, having a number of large relationships, I mean if it was one client above 30% of revenue I would have been done in a different mode from a risk standpoint. But given that Top five on an average are over $150 million, I think gives us -- one of them is over $200 million and still is within 11%, 12% range, I think it gives us a big source of strength when it comes to that mix.

Also, the reason I broke out the fact that majority of our Top five clients were actually at record ARRs, which means their quarterly revenue is at a new record in Q3, despite being a seasonally weak quarter, should set us up nicely for us to continue to mine these accounts and find additional growth because I do believe that even at these levels, whether it's 200 million or 175 million or 150 million, we are still at a wallet share position where we can continue to find growth because spend pools are in billions in these clients. The largest deal we announced this quarter is actually from a Top 10 customer.

**Moderator:** As there are no further questions from the participants, I now hand the conference over to Mr. Nitin Rakesh for closing comments. Thank you, and over to you, Nitin.

**Nitin Rakesh:** Thank you, all. In a way, we're still living through some interesting times. Despite the headwinds we are seeing in some parts of the business, we continue to have operating leverage needed to invest in the business for growth, which means we have to continue to make strategic investments, both in farming and in hunting. I think we'll continue to focus intensely on executing our strategies and supporting our clients in this complex environment, we're planning conservatively and are prepared for all environments and I thank you for continued interest in Mphasis and your sustained investments and time and efforts. We look forward to speaking to you after the next quarter.

**Moderator:** Thank you. Ladies and gentlemen, on behalf of Mphasis Limited, that concludes this conference. If you have any further questions, please reach out to the Mphasis Investor Relations at investor.relations@mphasis.com. Thank you for joining us, and you may now disconnect your lines.