“MphasiS Q3 FY 2012 Earnings Conference Call”

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Moderator Ladies and gentlemen, good day and welcome to the MphasiS Q3 FY2012 Earnings Conference Call. As a reminder, all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Varun Divadkar from CDR India. Thank you and over to you, sir.

Varun Divadkar Good morning, everyone and thank you for joining us on the Q3 FY2012 results conference call of MphasiS Limited. We have with us today, Mr. Ganesh Ayyar – the CEO and Mr. Ganesh Murthy – the CFO. Before we begin, I would like to state that some of the statements in today's discussion maybe forward-looking in nature and may involve certain risks and uncertainties. A detailed statement in this regard is available on the Q3FY12 results announcement release that has been e-mailed to you earlier. This conference call will be archived and the transcript will be made available on the MphasiS corporate web site, www.mphasis.com. I now invite Mr. Ganesh Ayyar to begin the proceedings of the call.

Ganesh Ayyar: Good morning, everybody. We will discuss our operating and financial performance for the third quarter ended on July 31st 2012. I hope that you have had the time to go through the financial results and the overview release that we sent to all of you.

Q3 has been a reasonably good quarter. To call out the positives, our revenue saw a sequential growth of 2% to Rs. 13,551 million. The Direct business grew by 12.6% QoQ to Rs. 6,334 million and net of rupee depreciation it has reported a 5.8% QoQ growth. Direct business now has an annual run rate of about $450 million and comprises of 45% of our total revenue which a year back was just 33% of our total revenue. The quarter witnessed a healthy addition of 20 new logos in the Direct business and out of that seven were in our focused vertical of Banking and Capital Markets. The strong performance in the Direct business was partially offset by 2.3% QoQ decline in the HP channel. In constant currency terms, the decline was 6.2%. We continue to see some projects ramp down in our HP Enterprise Services business which declined 3.8% QoQ to Rs. 7,031 million. We expect this trend to persist in the next few quarters before we reach a steady state.

Moving to HP non-enterprise services part of the business, we have seen good traction and revenue growing at 16.2% QoQ to Rs. 688 million. HP non-ES contribution to our overall HP channel revenue has increased to 8.9% in Q3 from 7.5% in the second quarter.

As you are aware, profitability continues to be our focus and the highlight of our quarterly performance. We have seen a consistent increase in our margins in every quarter this year. Despite salary increments and promotions effective May 2012, we have been able to expand our gross margins by 70 basis points in Q3 to 26.3% while our EBIT margin has improved 50 basis points this quarter to 16.7%. Increase in utilization in Application Services and ITO Services and continued efforts towards cost rationalization have resulted in an incremental margin improvement. The net margins also saw a significant improvement of 110 basis points as compared to the previous quarter and rose to 15.4%.

It is credible to note that the effective tax rate this quarter was at 22.7% as against 24.2% which has also contributed to the overall improvement in profitability. In line with our assurance to all our investors at the beginning of the year our focus on profitability has seen results in the three quarters that we have announced this year. We also continue to see healthy cash generation with Rs. 2,366 million being added during the quarter.

Let me just switch a bit towards the market scenario. We see the market scenario having a good deal pipeline but a very choppy deal velocity. Deal decision cycles are getting elongated causing visibility and predictability to be poor. Our foundation of operational excellence is helping us on ongoing profit focus because when the deal velocity is choppy, operational excellence is key to our success.

On the other side, talking about Go-to-Market, we will further accelerate our focus on Go-to-Market combined with some focused offerings that we will bring to the market. Our focus would be to bring next generation business models and offerings which capitalize on the emerging trends that are appearing in the marketplace.

To sum up, this has been a satisfactory quarter. We have seen volume growth in our Direct business which is a testimony of our structured approach with focus on hyper specialization and customer centricity which has enabled us to cater to client needs, both the traditional needs as well as emerging needs. Our sustained focus on driving operational efficiencies has resulted in margin improvement and has improved our profitability. We continue to seek opportunities in these adverse times by building differentiation for our clients and providing them with innovative platforms and offerings.

With that I would like to thank you for all your support and for your participation. I would like to request the moderator to open this call for questions. Over to you, moderator.

Moderator Thank you. We will now begin the question-and-answer session.The first question is from Priya Rohira from Enam Securities. Please go ahead.

Priya Rohira Just a few questions. Could you give us an outlook on the non-HP (Direct) business and what sort of initiatives are you seeing to see this maintenance of net client additions being very strong - more so on the selling and marketing side. The second thing is if you could give us an update on the HP MSA renewal which comes up on October 31st?

Ganesh Ayyar **I**n the Direct space, we have been consistently investing in Go-to-Market new solutions which are based on, if I may, the emerging services model. Our pipeline is healthy, so that is a good sign. However, we are also seeing based on the current market conditions that the predictability in terms of closure of those deals is a bit choppy. So, if you look at our second quarter results we had a flat Direct channel growth. This quarter we have seen 12.6% Direct channel growth. It has nothing to do with the market demand, but more to do with the choppiness in the sales velocity. We do have good mid-size deals in our pipeline, we are seeing traction in the marketplace, and we are going to the market with these offerings. If you take an extended period view, let us say if you take a view of 9 to 12 months ahead, we believe that we will be able to deliver above market growth rate in the Direct space. So that is our prognosis and our pipeline analysis as we stand today.

Priya Rohira If I may chip in over here, in the non-HP deals are you seeing any pricing pressure from competition?

Ganesh Ayyar While the pricing pressure is not very obvious in the marketplace, at least I am not seeing that as a major trend. What we are seeing is that customers are beginning to be more open to newer models. So as a result, the traditional model in which this most of the industry has operated which is Time and Material (PxQ), that model has to give way to a newer business model. So that trend we have seen. We are not seeing a significant trend around pricing pressure.

Ganesh Murthy On the HP MSA, as you are aware it expires on 31st October this year. We have had several rounds of discussions with HP. HP has put forward their asks. We have also put forward our asks. We have not reached a conclusion yet. The question that you have uppermost in your mind is on pricing. We are quite firm in our stand that we will be led by industry pricing trends and that has been our message to HP. At this point of time it is still under progress. Obviously, I would not be able to provide further details.

Priya Rohira And in HP, out of the 55%, I think 24% is dominated by INR currency, right? So is there a thought process of converting it into USD?

Ganesh Murthy That is part of our negotiations and ongoing discussions with HP.

Priya Rohira And secondly, we had salary hikes this quarter, but the cost of revenues is not indicative, just a growth of 1% and a bulk of it coming because we have seen net reduction in employees in Application and in ITO. So if you could give us an outlook on one, what sort of employee additions you are looking in both these spaces? And second thing is in terms of the salary hikes impact on them which got absorbed this quarter?

Ganesh Murthy Let me talk about the salary hike. We gave an average hike of about 3% for onsite employees and about 8% for the India employees, and the total impact of that is around 2% on our margins. On the headcount additions, we are committed to hire based upon our forecasts of our demand position. If we feel that there are available opportunities for us in the market, based on our pipeline and based on our order conversion, we will be hiring. Given the decline in HP Enterprise Services it is important for us to keep a very close watch on our headcount and our bench. Even in this quarter we have further increased our utilization, sort of an all-time high, and we are committed to maintain that because if we take our eyes off that we will have a profit impact.

Priya Rohira But would this utilization be difficult to maintain? Would we say that there is a fair possibility of decline over there because it is almost at complete seat level?

Ganesh Murthy We are committed to maintain it. I do not say there would be any further increase but I think we are committed to maintain utilization at around the same levels.

Priya Rohira And what is the dollar denominated growth in the BFSI vertical?

Ganesh Murthy I will come back to you on that. Let me give you overall impact. There are a couple of points that are important to keep in mind. One is as you mentioned 24% of our revenues with HP are in India rupee rate card which is not impacted by the rupee depreciation and then we have a significant amount of India business. If you notice in our MD&A, based on investor feedback and analyst feedback, we have shown India revenues separately. India revenues now account for about 13% of our total revenues. So you are talking about something like about 24% plus 13%, 37% of our revenues is actually unaffected by the rupee depreciation. The second factor is our hedging policy. We have been consistently following our long-term hedging policy, where we hedge 70% of our net exposures for one year in advance and that dilutes the impact of the rupee depreciation. So these two factors works to our advantage in an era where the rupee appreciates as we have seen last year. The whole idea is to contain the volatility. Coming to the specific question, we have given the details of our Direct Channel which is about 45% of our revenues which grew in volume terms, net of the rupee depreciation by 5.8% QoQ and HP Channel declined by 6.2% in volume terms. So if you take a weighted average, with HP Channel being 55% and Direct Channel being 45%, you will get a net volume reduction of 0.8% entirely driven because of the decline in HP channel.

Priya Rohira And more on BFSI because I think on INR numbers obviously, it should be with the growth just wanted to get a color is there a flat dollar number or is there a decline also over there?

Ganesh Murthy BCM - Direct Channel revenues grew by 10.8% QoQ, and if you take out the forex impact the actual volume growth was about 1.5%.

Moderator The next question is from Nitin Mohta from Macquarie. Please go ahead.

Nitin Mohta The first one was related to fungibility of people who are working on HP projects which are seeing ramp-downs. Are you actually facing any HR issues in terms of redeploying them on the business that you are winning on the Direct Channel side? The second one was just related to your thoughts on the shareholders return. I understand that acquisitions are your primary focus of using cash but at what point of time or are there any internal benchmarks that the Board has set which you want to share with the investors on when you would be looking at returning cash to the shareholders?

Ganesh Ayyar Let me start with the first question on our ability to handle the decline and move the balance from HP to Direct. Actually, there are no standard formulas. I wish we could have a standard formula that if you take 1% from there and 30% or 70% or 89% you are able to move. Depends on where you are winning the deal on the Direct side and where the decline is coming from on the HP side. But our focus is to be a responsible corporate and within that responsibility to ensure that we are balanced towards the employee as a stakeholder. So we need to be balanced. So far despite the decline you would see that we have managed it and we will continue to manage it along those lines. But I would not be able to give you a certain percentage on that question.

Nitin Mohta If I can just rephrase that, I just want to kind of understand qualitatively are you facing any HR issues in terms of redeploying the talent or just thoughts over there, is it a smooth process?

Ganesh Ayyar What do you mean by qualitative issues so that I can give you a precise answer?

Nitin Mohta My point was is there going to be an issue where obviously you have employees who have been taken off a project because there is a HP ramp-down and to that extent there is a risk for utilization to fall off because even though you are winning business on the Direct side you cannot really redeploy those resources which are already there with the Company?

Ganesh Ayyar Actually, there is a risk but that risk has existed for the last nine months and we have managed that risk so that gives us the confidence that we will be able to manage that risk, but yes, there is a risk. The second point is relating to cash and what are we planning to do with it. As we said, one of the things which we are working on as part of hyper-specialization is to see how we can accelerate our direct channel revenues. We are very, very strong in traditional services. Emerging services is another area where we have had good initial foray and we want to accelerate the pace of that and that is where we look for acquisitions which can help us accelerate that pace and that is why we are very, very choosy as to which Company we want. We are not looking to buy a company just to pluck the revenue. We are careful, it should help our strategic journey, and second, it should not create shareholder return issues in terms of profitability. So these are the two factors that will remain our focus. Have we set a deadline by which if we do not decide, we will go back to shareholder and return that cash in a different form, no that is not the case. Actually, what happens is we go through this discussion in every Board meeting and this is clearly a high priority item for us and it will remain as a high priority. We are again going to have a discussion in end of September when we are meeting for our annual strategy meeting of the Board. What we have not done is, we have not given an ultimatum to ourselves that if we do not decide by 23rd of September we will activate that because we need to keep a holistic point of view. But at the end of the day our commitment is towards total shareholder return.

Ganesh Murthy I just want to add one more point to what Mr. Ganesh Ayyar has mentioned is when coming to acquisitions we are also cognizant of the fact that we do not want to leverage our balance sheet to a large extent and take in debt. So the size of acquisition will be sort of limited by the amount of cash that we have in our balance sheet.

Moderator The next question is from Ashwin Mehta from Nomura. Please go ahead.

Ashwin Mehta In terms of the decline in HP ES revenues in this quarter, was that a surprise because earlier indications were for less steeper declines in the HP Channel and what led to these declines?

Ganesh Ayyar I do not know whether it was a complete surprise, but there were elements, which were probably the size was bigger than what we anticipated but despite that as I said our operational focus has helped us to continue to deliver good results. Now, what led to this decline is a combination of factors from HP standpoint and one of the factors is at the stage of renewal whether they got the contract, whether they have other options for the same thing, so they are behaving like any other customer would based on the options that they have. It is not a single factor that as if they are taking the business away from us and giving it to someone else. It is not even a single factor that they are losing all the business. It is a combination of those and so they are making those choices based on their priority, and we are making our choices based on what is right for MphasiS shareholders.

Ashwin Mehta Do you see given the fact that second half of the calendar year has seen a lot of renegotiations come up in terms of deals where HP is one of the incumbents? Do you see risks there, given the fact that HP seems to be losing share to some of its competition in these deals, for the HP revenues to decline even further from hereon?

Ganesh Ayyar It is a great question but our focus is to see whether we will see decline from HP as our partner and customer. We are not necessarily completely privy to what deals they are working on and whether they are getting this renewal. As far as they are concerned, you know and this is based on publicly available data I am sharing with you, they are heavily focused on customer satisfaction and focused on cost optimization. So based on all those factors they will make their choices. Our job is to be ready for any eventuality, continue to grow our Direct business and continue to have a profitable book of business if I may.

Ashwin Mehta And secondly, we had indicated earlier that we would be looking at some of the businesses that HP possibly wants to get out because that might not be as remunerative for HP. So is there any movement in terms of that?

Ganesh Ayyar There is no specific movement. We continue to have discussions. At this point of time I have nothing to report which is specific and which says that this is the business that we have secured.

Ashwin Mehta And finally, one question for Mr. Murthy, what is the OCI balance currently in terms of the accumulated forex losses in the balance sheet?

Ganesh Murthy It is Rs. 176 crores debit balance.

Moderator The next question is from Prateesh Krishnan from Antique Finance. Please go ahead.

Pratish Krishnan My question is on the BPO side. If I see you have had fairly strong employee additions in the quarter and even the utilization numbers are more or less stable. But in terms of the revenue growth in specific segments, BPO has not done fairly well, growth is slightly muted. What is the reason for the disconnect?

Ganesh Murthy There is no reason for any disconnect here because what happens in the BPO is many of our customers adopt a model where it is linked to the forecasted volumes. So, unless you staff people and you get the volumes, you will not be able to take advantage of the volumes. We are growing in BPO. There has been ramp up but there is also a period when people have to undergo on-the-job training. So the actual results of this ramp up will be seen in Q4.

Pratish Krishnan Should we expect an accelerated growth in BPO segment going ahead?

Ganesh Murthy We are focused on BPO. It remains a very important aspect. It also has a good gross margin. So, we will be looking at growth in that area.

Pratish Krishnan Secondly, just to clarify in terms of the cost of revenues and you also provide this split, the 'others' segment in the cost of revenue has declined substantially. How sustainable and what was the reason for this decline?

Ganesh Murthy In the 'others' actually in Q2 there was a one-time accrual for service tax and TDS. We had accrued about Rs. 15 crore in the previous quarter and that is a one-time accrual. This did not happen again in this quarter. That is the main reason for the decrease in the 'others'.

Pratish Krishnan The steady-state cost would be something similar that you reported this quarter or?

Ganesh Murthy Yes, it is more or less around this quarter figures subject to exchange, because in the 'others' also, all the license costs and the software cost, etc., which are foreign currency denominated will be there. So, if the rupee continues to depreciate that will slightly go up.

Moderator The next question is from Manik Taneja from Emkay Global. Please go ahead.

Manik Taneja First of all on the HP non-ES segment where our target was close to $55 million to $60 million in revenues in financial year October '12, could you talk about what is the outlook over there as well as the outlook heading into next year? And secondly, in terms of the cost of revenues, there is a non-salary cost element which has declined sharply. Could you explain that in greater detail and what kind of a steady-state cost we would build over there?

Ganesh Ayyar On the non-ES front, the types of project are smaller apart from one business which we do which is with the R&D side of HP. So it has been growing quarter-over-quarter, and right now we are kind of upon target to deliver whatever $50 million to $60 million of revenue on an overall basis for the year. And going forward, we expect that business to be just like our Direct to be part of our focus to grow that business.

Ganesh Murthy Manik, your question was on manpower cost?

Manik Taneja Non-manpower cost within cost of revenues, that number essentially has declined sharply in the current quarter.

Ganesh Murthy As I mentioned this was the others, bulk of the decline is in the others item. And that was because in Q2, we had a one-time accrual for service tax and TDS of Rs. 15 crores.

Manik Taneja So one should look at something like Rs. 160 crore kind of a run rate provided currency does not play at constant currency one should look at a similar number going ahead?

Ganesh Murthy That is correct.

Manik Taneja How much juice is left in terms of our cost containment, rationalization exercise given the fact that we have been consolidating our delivery facilities?

Ganesh Murthy The delivery facility consolidation is an ongoing exercise. Because of our ramp down in HP channel, there is a volume decline and there are seats that are released and usually what happens is there is a time lag between headcount reduction and the seat reduction. So as soon as we are ready with consolidating our seats and we have a bulk of vacant seats available we tend to give it up if there is no demand from that facility. Moreover, especially if it is an STP, since there are no tax breaks available for STPs we try to give it up and focus on growth only on SEZ. So, there is still scope on the facility consolidation effort. I would not say there is any further headroom on the utilization. I think we are fairly maxed out there.

Ganesh Ayyar I do not know whether you are alluding to our focus on profitability and cost being one lever, the other one is the type of portfolio that you take to market and portfolio profitability at the point of sale. So, what you are seeing is probably, you got the answer on the cost side and Ganesh Murthy shared with you what our plans are and how we manage it. The other aspect is we are also focused on what we take to market and portfolio profitability and you heard about that in the BPO comments as well. So, there are two levers based on which one can say that you have to maintain profitability and we have got ambidextrous focus on both.

Moderator The next question is from Vimal Gohil from Asit C Mehta. Please go ahead.

Vimal Gohil Gentlemen, what is the effective tax rate that you are expecting in the coming quarters?

Ganesh Murthy Tax rate has been a very good area where we have seen a lot of improvement. In this quarter we had some savings in the US taxes because we were able to file consolidated returns and take advantage of some carry forward losses of one of our subsidiaries. Going forward, we anticipate the effective tax rates to be around the same levels. So, I would say around 23%.

Vimal Gohil Coming to non-HP business, which we have got 12%-odd, just wanted you to add some more color on the sustainability of the growth rate over here. Do you think that this growth rate is sustainable given the pipeline that we have in the non-HP business particularly?

Ganesh Ayyar When you say sustainable, your question is based on if you are expecting this to happen every quarter?

Vimal Gohil Could we see similar growth rates in the coming quarters as well?

Ganesh Ayyar Predicting such growth quarter-over-quarter with the current deal velocity is a challenge. We definitely see that over an extended period of time as I mentioned earlier between 9 to 12 months that we will continue to deliver above market growth rate. But would we be able to do it every quarter and that adds up to the above market growth rate, that is a tough ask and as of now I am not in a position to answer that question.

Ganesh Murthy Let me also add some perspective here. You need to really look at it with a one year perspective. If you look at last year and compare it to this year you will see YoY basis our Direct Channel revenues have grown by 48.3%. That is in rupee terms. Even if you take out the exchange impact, we still have grown by something like 30%+ YoY. So that provides you the perspective. I think a lot of us are looking at one quarter, say each quarter, maybe 3%, 5% and things like that and instead I think you should look at it from an overall yearly perspective whether we are on track of growing on the Direct channel.

Vimal Gohil One more question, I do acknowledge the fact that 37% of your revenues are rupee-denominated. But is it possible for you to give me the total dollar revenues in this quarter if you could convert your entire revenue into dollars or so, what was that figure in million?

Ganesh Murthy We do not provide dollar revenues because 37% is in Rupees, so that depends on the exchange rate. This quarter if I converted at Rs. 55, last quarter if I converted at Rs. 50, then there would be a sudden decrease or an increase. We provide constant currency growth rates which are there in our MD&A.

Moderator The next question is from Dipesh Mehta from SBI Cap Securities. Please go ahead.

Dipesh Mehta First is about HP non-ES side. Can you tell us how much was the revenue in first nine months? Second is about capex. What was the capex in the first nine months? The reason for asking is depreciation and amortization declined this quarter. Just getting some sense how much capex we are running at? And last is about how many freshers added during the third quarter and the first nine months?

Ganesh Murthy Let me talk about the HP non-ES first, your first question, over the last three quarters, we have done around $37 million. We are looking at somewhere around $50 million to $55 million for the whole year. On the capex, our capex spend has been very minimal. The reduction in the depreciation that you see is primarily because a lot of assets have been fully depreciated and so there is no further depreciation added to that. That is the primary reason for the decline. As I mentioned clearly, the increase in our gross fixed assets is quite marginal, the gross fixed assets addition stood at about Rs. 12 crore in this quarter.

Dipesh Mehta And first nine months how much increase would be there?

Ganesh Murthy I will just work it out and let you know.

Dipesh Mehta And last part about fresher addition?

Ganesh Murthy Last year we added around 1,300 freshers and this was part of our strategy to get a good work-force pyramid. This year because of the decline in HP we are going slow on the freshers strategy. We are still committed to that but our intake will be much lower, probably below 1,000 freshers.

Dipesh Mehta Can you provide specific number for the first nine months?

Ganesh Murthy We have added about 250 to 300 freshers.

Dipesh Mehta Do you intend to take around 700-odd in Q4?

Ganesh Murthy No, not really. I do not think we will take 700 freshers in Q4. We will take probably about 200, 300 freshers in Q4.

Dipesh Mehta And just last part on HP non-ES. Non-HP ES side INR billing and dollar billing mix would be materially different than the company average?

Ganesh Murthy Most of the billing is actually dollar billing.

Moderator The next question is from Rahul Jain from Dolat Capital. Please go ahead.

Rahul Jain What kind of an outlook do we have on the Enterprise Services side because earlier we had a certain anticipation and we have moved little off from that kind of a run rate. What would we see on a long term basis?

Ganesh Ayyar We do not have a specific outlook because fundamentally we do not give specific outlook on an overall business anyway, but our prognosis is that it will be in a decline mode for the next few quarters. At least we are planning based on decline mode for the next few quarters. Of course, we are hoping that it will turn positive but we are preparing ourselves based on decline as a scenario.

Moderator The next question is from Hardik Shah from K R Choksey. Please go ahead.

Hardik Shah Your DSO in the past has came down from 91 days to almost 80 days but in this quarter it has increased from 80 to 85 days. So this is one-off or do you expect in the coming quarters the DSO to increase again into 90 days level?

Ganesh Murthy No, absolutely not. We are looking at decreasing the DSO. If you look at our focus, part of our focus also has been to grow the India market and if you see over a one year period our contribution from 9% has shifted to about 13%. The India market definitely has higher DSOs than the international business and that is the reason for the increase in DSOs but we do not expect any further deterioration in DSOs. In fact, we are working towards an improvement in our DSOs.

Ganesh Ayyar Just to add, I mean, that is an area which we could have done better in Q3 to put it simply.

Hardik Shah Going forward we can expect 80 day levels to continue on an average on TTM basis?

Ganesh Ayyar Yes, that is what we are working towards, that is the model based on which we have worked.

Hardik Shah And your cash flow from operations were roughly like Rs. 250-260 crore in the last three, four quarters. So do you expect that kind of trend to continue in the coming quarters or do you expect some deterioration there?

Ganesh Murthy We do not expect any deterioration. Very consistently over the last 12 quarters and in fact, every quarter we have been adding a minimum of about $12 to $15 million every month and we expect that to continue.

Hardik Shah Last question, can you give the breakup in terms of constant currency terms growth between HP ES and HP non-ES in Q3?

Ganesh Murthy Constant currency growth in HP non-ES was about 11% and ES was negative of about 7%.

Moderator The next question is from Ritesh Rathod from UTI Mutual Fund. Please go ahead.

Ritesh Rathod Just want to know, have we changed some estimations or the basis on which we provide for receivables, especially for the aged-receivables and what has been the change?

Ganesh Murthy This change was done last year from November 2011. The estimate is based to align ourselves with the new Schedule VI requirement. The Schedule VI states overdue invoices and we changed our basis to align to that. The India receivables, which I mentioned has a higher credit period, because of the change in estimation which we did last year, there is an impact.

Ritesh Rathod So that was effective post October, right?

Ganesh Murthy November 2011 onwards.

Ritesh Rathod So has there been any major change in this quarter in case of provision for receivables? Like had it been the earlier estimations your provisions would have been higher and had it been not like the provisions are lower?

Ganesh Murthy This impact was there right from the beginning, right from November onwards. In this quarter we have reported it because Accounting Standard V says that if the estimate becomes a material amount, if it crosses 5 to 10% of our profits, then we need to report it separately. So that is the reason why we have reported it. The change was always there, right from the beginning of the year.

Moderator The next question is from Madhu Babu from HDFC Securities. Please go ahead.

Madhu Babu What is the kind of deals in the Direct Channel, I mean in terms of TCV if you can?

Ganesh Ayyar It is a range, so I do not know how to give you a precise number. But one of the things, because we have stayed invested in Go-to-market, the TCV size that we have, at least the median, is moving towards a slightly bigger number than what we used to have over the last 12 months. So that is one way of answering your question but to give a precise number it varies so much that we may not be able to derive much out of it because there is nothing called a precise number there. But we do have slightly larger deals in our pipeline and we are pursuing that.

Madhu Babu Are these project base or would we have a lot of annuity streams? I just want to understand that.

Ganesh Ayyar That pattern has not changed to be honest. The pattern between annuity and project-based remains fairly similar and in fact it is based on newer business models the chances of that becoming annuity-based is higher than based on the older model.

Madhu Babu And which are the verticals which are doing well in Direct Channel and service lines also if you can?

Ganesh Ayyar You want a quarterly view or….?

Madhu Babu Generally, on a business perspective.

Ganesh Ayyar There is a lot of chatter in the market about Banking Capital Markets and Insurance completely getting tanked because of the economic climate. We have not seen that in our pipeline. In fact, in many ways that pipeline has become healthier. But what we are clearly seeing is that deal velocity is getting longer and longer and in some case some deals get pulled out of the pipeline. So these are the two factors which are making visibility slightly tougher. So that is the trend we are seeing. We are not seeing any weakness specifically in these verticals. At the same time we are also seeing that certain horizontals are playing up in terms of market demand. So, that is part of our ongoing strategy to see what horizontals we should be going after.

Moderator The next question is from the line of Ashwin Mehta from Nomura. Please go ahead.

Ashwin Mehta This is just a follow-up on our hedging strategy. We had a forex loss of around Rs. 50 crore in this quarter because of hedging on our revenue lines. Do you see that progressively reducing as the hedge rates become much more favorable, any indications in terms of the distribution of our OCI losses in the future quarters would be helpful?

Ganesh Murthy Yes, you are right. There will be a decrease in this losses going forward and it is difficult to give a precise figure on this but I think our average hedge rate for the next one year would be somewhere around Rs. 51-52. So that will give you a good indication.

Moderator The next question is from Vimal Gohil from Asit C Mehta. Please go ahead.

Vimal Gohil I wanted to know about your adjustment in hedging reserve figure. You just spoke about that, is it the same thing, the Rs. 50 crore figure that is there in the adjustment in hedging reserve?

Ganesh Murthy Yeah that is netted off against revenue but are you talking about the OCI, OCI balance is what is there in the balance sheet.

Vimal Gohil The Rs. 50 crores figure that is there in the P&L could you just add more detail to that? Could you throw some detail because the number is bigger than probably your previous quarter if I compare it that way?

Ganesh Murthy The previous quarter, our average exchange rate was Rs. 50.9 and in this quarter the average exchange rate was Rs. 55.78. So obviously, when the exchange has depreciated by 9.6% over one quarter, you will see at least a 9.6% increase in the hedging reserve.

Moderator The next question is from Soumitra Chatterjee from Espirito Santo. Please go ahead.

Soumitra Chatterjee I have two questions. First one is on attrition. What is the current attrition rate and what is the rate of involuntary attrition? And second question is on the HP side. If I am not wrong, there are four deals which are coming up for renewal, where HP is the current vendor in infrastructure management segment. If I am not wrong, there were some talks going around that probably you will try and work with HP in the segment and convince them to reduce the mark-up or go solo in that. Just wanted to know what is the status on that, have you communicated this to HP, what is HP's outlook on this and importantly, from the client side, if say HP agrees to work on this sort of model will the client actually agree to work with MphasiS as a direct vendor?

Ganesh Murthy On the attrition, we are around 20% for the Apps offshore.

Ganesh Ayyar First of all, we cannot disclose our discussions with any customer at this stage because whatever we are discussing here on the line is publicly available data. Nobody is going to discuss what strategy and where is the deal with any customer. So unfortunately, I will not be able to comment. One thing which I want to reemphasize, the proposal that we went with for a certain part of portfolio which was the question earlier, as of now, we do not have anything to report. But on these four deals or two deals or what is the customers' point of view I will not be able to comment.

Somitra Chatterje Okay, so if I could just ask in a different way that because some of the deals last year HP actually lost to one Indian vendor because their cost base is a bit higher. Now there could be an option where probably you can go solo. I am not saying to comment on specific deals but is there an option with them where probably you can convince them that whatever the mark-up they are doing on an overall basis can that be reduced by allowing you to directly bid?

Ganesh Murthy This is part of our Go-to-Market strategy. That is all we can say. It is definitely part of our discussions with HP. We would not be able to give any further details specifically.

Moderator The next question is from Rahul Jain from Dolat Capital. Please go ahead.

Rahul Jain Just a follow-up on the capex if you could give some clue on what we incurred this quarter and what we expect for next as well as for the coming year?

Ganesh Murthy Our capex requirement as I mentioned earlier is very, very limited especially since we do not own any real estate. I would say nothing beyond Rs. 20-30 crore for the whole year.

Rahul Jain For next year

Ganesh Murthy Yes.

Ganesh Ayyar On that note, I want to thank all of you for your interest and participation and certainly, we will stay connected and look forward to interact with all of you either prior to announcing results or after we announce the results.

Moderator Thank you very much. On behalf of MphasiS that concludes this conference call.