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Q3 FY2019 Earnings Conference Call Transcript

MAIN SPEAKER:
Vinod Kumar, Managing Director and Group CEO
Pratibha K. Advani, Chief Financial Officer

Moderator: Ladies and gentlemen, good day and welcome to the Tata Communications Limited Q3 FY19 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Vipul Garg Head of Investor Relations at Tata Communications. Thank you and over to you, sir.

Vipul Garg: Thank you Stanford. Good afternoon everyone and welcome to Tata Communications Earnings Conference Call. We are being joined today by Mr. Vinod Kumar MD and group CEO and Pratibha K Advani Chief Financial Officer. The results for the quarter ended December 31st, 2018 were announced yesterday and the quarterly factsheet is available on our website. I believe you would have the opportunities to browse through the key highlights. We shall begin today's call with comments from Vinod Kumar who will share insights on business dynamics, market environment and business progress. We will be followed by Pratibha K Advani who will discuss the financials during the review period. At the end of management remarks, you will have an opportunity to get your queries addressed.

Before we get started, I would like to remind everyone that some of the statements made or discussed on conference call today maybe forward looking in nature and must be viewed in conjunction with the risks and uncertainties we face. A detailed statement and explanation of these risks are included in our annual filings which you can locate at our website www.tatacommunications.com. The company does not undertake to update these forward-looking statements publicly.

With that I would like to turn the call over to Vinod to share his views. Over to you Vinod.

Vinod Kumar: Thank you Vipul and good afternoon everyone and a very warm welcome to all of you. I would like to start by giving you a perspective on the industry and then discuss our performance in Q3 and close off with the few updates. A recent study called out at the most successful business model today in terms of customer value, in terms of revenue growth rates and market valuation in the digital platform business model. 70% of the world's top 10 most valuable companies and 70% of the 1 billion unicorn startups all operates using this model. Yet fewer than 2% of all other companies operate on the platform business models. This is forcing companies to dramatically change the way they look at themselves. Digital transformation that is internal and external lies at the center of every business strategy to transform itself into a platform and this frankly transcends size of companies, industries in its equally applicable in developing markets and in developed economies and there is no digital strategy without digital infrastructure.

Digital infrastructure that is borderless always on secure and that seamless connect humans and things. Digital infrastructure that allows seamless migration from one generation of technology to another especially for large enterprise that have to deal with many legacy decisions while also wanting to go rapidly into the future. Digital infrastructure that leverages customize solutions with the open and flexible world offered by both the cloud and the internet. Building such digital infrastructure has been at the core of our portfolio evolution, our investment strategy and our execution game plan for the past four years. This vision and steadfast focus is beginning to pay off in very tangible ways as I will discuss. It may not have always gone according to the timing that they envisioned, but there is ample evidence that what we are creating as a very large market.

Our strategy to drive convergence between the fixed and wireless world and in the internet of things and machines of things is compelling and is demonstrated through the following proof points. Our overall data revenue s grown by a CAGR of 8.8% over the last three years. This has been slower during the past one year due to the shakeup in the India service provider business and slower revenue ramp in our growth services portfolio. However, in comparison our large global competitors during the same period have grown from anywhere between minus 18.6% to 2.7% in the same period. During the past 9 months our growth services order book has grown by 85% over the same period last year. The issue we are contending with in growth services as I have explained before is a slower ramp or usage-based services and the longer gestation to implement our SD-WAN wins. We have been doing some very hard paddling for the revenue growth by creating such an order growth and this will translate into numbers in the coming quarters.

I want to talk a little bit about IoT India and then NetFoundry. Firstly, on IoT India we have chosen to focus on safety devices, smart lighting, smart metering and asset tracking solutions as priority tracks in India. I am happy to say that we are progressing well on each of these used cases with commercial pilots underway and sizable orders in the cards. As an example, we recently won a sizable contract from a reputed global manufacturing company offering safety solutions for their workers. Eventually we will be providing safety and tracking services for 50,000 workers under this contract. We have done many successful pilots for smart street lighting and for utilities and gas metering solutions across India and the use of LoRa is now being called for in many RFBs and hence the doors will open in the coming quarter.

NetFoundry there is a lot going on NetFoundry but I do want to mention one very salient data point and which can be verified in the public domain. NetFoundry is featured on both the AWS market place and in the Microsoft academy. This is no mean feat considering the elite names that we share this recognition with and it really validates the readiness and the need for application aware and internet based connectivity solutions.

Moving on, changing our internal process and making Tata Communications digital as you know has been the large preoccupation for us over the past 18 months. We are seeing clear evidence of this transformation with the end-to-end deployment of digitally enabled zero touch processes for fiber services. We have had nearly 35 customers ported to our Optimus platform and they are seeing dramatic improvements in turnaround times for everything from providing ports all the way through delivering our services. We probably have another year or so to go before this program get completed and we port all our customer with a majority of our customer to these platforms, but the evidence that what we are building is futuristic and comparatively differentiating is compelling and is already here.

I want to wrap up this proof point section with the biggest proof of our strategy at work and this is the largest ever customer award that Tata Communications has received at least as far I remember, and this award was won in December 2018. Tata Communication was shortlisted against major global incumbent competitors and a won a five-year contract to provide connectivity in the IoT space using its MOVE platform through a large industry international industrial company. The five-year contract value is expected to be in the range of $250 million to $300 million with revenues expected to ramp from Q4 of the coming fiscal year, i.e., FY20.

This solution leverages many parts of our portfolio with MOVE in its core and with position as well of several other wins in this space. This win also moves us closer to the $150 million revenue goals we have set for ourselves for innovation services in FY21. I want to talk about sales now. One of the important metrics that we tract ourselves is on the total contract value sold during the period and these contracts can range anywhere from one to five years. For year to date FY19 a total contract value sold for data services has been $1.1 billion witnessing a 52% growth over the same period last year. I do not want to point out this is the gross contract value, but we also have price erosion and churn which will reduce the number as we look at it, but I am just giving indication of the overall size of business which we have been able to close and the level of market activity that we are going now.

The number of deals during this period also increased by 8% and we added 705 customers during this period. Within this the growth services total contract value sold for year to date FY19 is 619 million which is also an 85% increase over the same period. This TCV sold as explained in previous example of the large win of $253 to $300 million which is included in this is in various stages of execution and as we start to deliver, we will recognize the revenue in our books. Our strategy always has been to sell more products to existing customers and make the business stickier and reduce our pricing pressure considerably. The product penetration ratio for our top 300 customers is now 5.25. This is as of 31st December 2018 that is increase from 5.1 in December 2017. Again, I want to state that please note that all sales figures that I have provided on gross basis before taking into account any price erosion or churn from our existing base. Before I move on to quarterly performance, I want to give you quick update on the land demerger. The MCA approval for the land demerger has taken longer than expected due to the administrative control of Hemisphere Property is shifting from DOT to the ministry of urban affairs. The first motion at MCA has already been completed and the ministry of urban affairs and the process of appointing new director for HBIL. We expect the process to expedite once the new directors are in place and we are in continuous contact and following up with the concerned officials in the ministry of urban affairs.

Let me now touch upon the highlights of the quarterly performance:

Data business witnessed strong growth this quarter. The revenue grew 14.1% year-on-year and 8.4% quarter-on-quarter on the back of strong performance across all our portfolios. EBITDA for the quarter came in at 766.7 crores witnessing a growth of 35.2% year-on-year and 42.6% quarter-on-quarter. During the quarter ended December 31st, 2018 based on supreme court directives TRAI issued a notification stating new regulation on the access facilitation charges of cable landing station. These directives would be effective from November 28, 2018. Accordingly, a company has recorded one-time revenues as well as operating and maintenance expense recovery. This has led to a one-time EBITDA gain of 348 crore. This quarter we also had one-time expenses of 138 crore. All the adjustments were made on the data segment. Pratibha in a section will be providing more details about the financials and the one offs. Growth services portfolios witnessed strong momentum despite Q3 as I had mentioned earlier being a seasonally weak quarter. Revenue grew by 13.2% year-on-year and 4.6% quarter-on-quarter on the back of new deal wins. EBITDA for the quarter was marginally negative as we incurred an upfront cost for the large deals and usage-based revenue in Q3 is low due to the holiday season. We have a healthy pipeline as I mentioned earlier of orders under execution and this provides us confidence on the growth outlook. We continue to witness an uptake in growth service profitability, and we hope to end Q4 with positive EBITDA. The traditional services portfolio has started to stabilize and witness a revenue growth of 4.2% quarter-on-quarter. The operative consolidation in India as you know has affected this portfolio while the revenue impact from this is largely over were still affected by higher access cost. We expect these higher access cost we expect this high access cost to normalize by the end of this financial year. We witnessed strong growth in the transformational business on the back of new deal wins. Our international funnel is strong, and we expect strong growth in the coming quarter despite having to observe the TTSL impact. In payment solutions we have streamline operations to bring cost efficiencies and we started to see results for the steady uptake in EBITDA numbers. Consolidated PAT for the quarter came in at INR 173 crore compared to 1.6 crore in Q2 FY19.

To sum it up I want to say that we continue to deliver consistent results back by the strong performance in our data business. As a new year session, we are committed to bring in transformational change in 2019 by offering a plethora of services to enhance and support our customer experience and their evolving business model. We aspire to remain innovative and are geared up to bring the necessary synergies within our business. We realize that the pace of change may not be always be what one expects but the aspirations of our destination 21 goals remains alive in our hearts and forefronts in our minds. We are seeing evidence that what we are doing is making an impact to our customers. We are growing faster than our competition and most importantly we are making our business model future proof.

With that I would like to invite Pratibha K Advani to discuss the financial highlights for the last quarter.

Pratibha K Advani: Thank you Vinod. A very good afternoon to all of you and thank you for joining us on our earnings call today. I will take you through the progress we have made during the quarter and 9 month ended 31st December. Let me begin by giving a brief on our consolidated financials. Consolidated revenues during Q3 came in 4269 crore an increase of 4.9% Q-on-Q and 3% Y-on-Y. This was primarily led by strong performance in data services portfolio. Consolidated EBITDA for the quarter stood at 843 crore an increase of 33.7% Q-on-Q and 31% Y-on-Y. Margins have expanded by 420 basis points both sequentially as well as Y-on-Y largely due to one off benefits and strong performance in the data portfolio. Profit after tax on a consolidated basis came in at Rs. 173 crore as compared to 1.6 crore in the last quarter.

Before I move to segment performance let me call out the one off during the quarter. During the quarter ended 31st December based on supreme court directive TRAI issued a notification stating new regulations on the access facilitation charges for cable landing stations. These directives would be effective from November 28, 2018. Accordingly, the company has recorded one time revenue of 91 crore and operating and maintenance expense recovery of 257 crore. This has led to a one-time EBITDA gain of 348 crore for this quarter. You would recall that in Q3 of FY17 we have to take a provision against revenue and maintenance expense recovery write-back of 147 crore. This quarter we also had a onetime expense of 138 crore these expenses are on account of a one-off payment towards contractual prior period contractual employee obligation of 38 crore 14 crore was impairment of licenses which had become redundant due to the ongoing customer transformation program high access and core location cost due to operator consolidation has also impacted us this quarter. This contributes to 86 crore. You would recall that in my last quarter commentary I have specifically called out the expected impact on access cost. This cost I would like to add is temporary and we are investing in our owned last mile capability and optimizing our network architecture. We expect this cost to come down to 30 to 40 crore in Q4 and it will normalize or go away from Q1. All the one-off adjustments were made in data segment.

Consolidated normalize EBITDA for the quarter came in at 632 crore. During the quarter we acquired 100% stake in Teleena which is now consolidated line by line in our books. Teleena EBITDA loss run rate of INR 30 crore is part of our innovation portfolio. Talking about the segment performance data business revenue came in at 3326 crore and recorded a growth of 8.4% sequentially and 14.1% year-on-year. This growth was on the back of strong performance across all segments. Data services now contribute to 78% of overall revenues and increase of 7.6% as compared to same quarter last year. Data EBITDA for the quarter came in at 767 crore and grew by 42.6% sequentially and 35.2% Y-on-Y which was primarily led by one off benefit. Our performance in data portfolio is strong even if we exclude the one-off revenue gain of 91 crore on account of access facilitation charge. We witnessed a sequential growth of 5.4% after adjusting the AFA one off revenue.

Let me also remind you that seasonally this is a weak quarter for our usage-based services. Moving to our traditional services portfolio revenues for the quarter came in at $299.5 million and improvement of 4.2% quarter-on-quarter despite operator consolidation impact. On a constant currency basis this portfolio witnessed a growth of 5.8% quarter-on-quarter and 5% Y-on-Y. Traditional services had the benefit of AFA post adjustment of AFA our revenue grew by 1.2% sequentially compared to last quarter where we witnessed a decline of 1.3% and in Q1 this portfolio was down by 1.8%. As you can see from these data points this portfolio is rebounding to normal growth levels. The impact of operator consolidation on revenue has normalized but we are still affected on the cost side due to higher access cost. Growth services witnessed strong momentum. Revenue grew by 13.2% year-on-year and 4.6% sequentially coming in at $101.4 million. EBITDA was negative due to lower usage-based service in Q3 due to holiday season and higher upfront cost for the large deal wins that Vinod shared with you earlier on during this quarter that we have won and have end due to change in our product mix. The change in product mix has impacted the margin as we continue to invest in cloud, security and media services. We have expanded our foot print of our security operation in Dubai and London in current year.

On a year to date basis we witnessed strong growth of 137.6% year-on-year for ISO services. We have added over 40 customers in ISO between March and December of 2018. ISO brings a lot of stickiness to the business as a contract that typically for a five-year duration. Mobility services grew by 64.1% year-on-year. Media services grew by 39.2% year-on-year on the back of recent deal wins for some of the marquee sporting event. Our wallet share has been increasing due to our superior delivery in execution and we are getting more and more event from our existing customer. We have also added five new customers during current financial year.

Moving to innovation services this quarter innovation services have seen a significant growth revenue has grown from half a million in Q2 to 2.4 million in Q3 aided by MOVE. While these numbers are small but the movement is definitely significant. As we have graduated from POCs to commercial pilots as mentioned by Vinod earlier. Moving on to our subsidiaries transformation services revenue came in at 337 crore witnessing a growth of 14.7% year-on-year and 17.8% sequentially for the quarter. The growth was largely due to execution of deals in pipeline. EBITDA for Q3 stood at 35.1 crore witnessing a growth of 22.4% quarter-on-quarter. We will continue to see this strong momentum going forward.

Payment solution as part of our strategy we have optimized our ATM portfolio and this quarter we have closed over 1500 less profitable ATM this has led to increase in profitability and we recorded an EBITDA of 6.4 crore against 0.4 crore in Q2. EBITDA margin expanded by 680 basis points as compared in last quarter coming in at 7.2%. Our average transaction per day per ATM has gone up from 85 in Q2 to 92 in Q3. This is also seasonally one of our stronger quarter. Invoice business it continued to witness a decline. Revenue for the quarter stood at 943 crore translating to a decline of 5.6% Q-on-Q and 23.3% Y-on-Y due to continued decline in volume. Year to date our volumes have decline by 7 billion minutes. EBITDA stood at INR 75.9 crore witnessing a decline of 18.1% Q-on-Q but flat on Y-on-Y basis. We would recall that we had one-time gain in voice business in last quarter. EBITDA margin for the quarter was at 8%. We continue to focus on cost efficiencies and our aim is to generate as much as free cash flow as possible from the invoice business.

Year to date we have generated free cash flow of 235 crore. CAPEX for Q3 was at $69.3 million. Year to date we have incurred a CAPEX of 206.7 million. This is very much in line with a broad guidance that we had given at the start of the year. Free cash flow that is EBITDA less CAPEX for the quarter came in at 343 crore and increase of 99% over last quarter even after deducting finance cost and taxes we have delivered a free cash flow of 172 crore this quarter.

Consolidated net debt stands at $1.287 billion, an increase of 36 million compared to last quarter due to working capital gap as voice business is declining and also on account of acquisition of 100% stake in Teleena during the quarter. Our average net debt for the quarter was at same level as last quarter with spike at quarter end. Average cost of borrowing is at 3.76%, this has increased by 9 basis points quarter-on-quarter due to increase in average LIBOR movement from 2.11% in Q2 to 2.35% in Q3. We have seen a steady ramp up in our financial performance as the year gone by and delivered strong numbers across all parameters. Data business continuous to be strong and growth of services have been instrumental in our overall revenue growth.

We are confident that we are moving in the right direction and our product portfolio and solutions are geared towards the future as we gain scale in our growth and innovation portfolio. We will see stronger momentum in our top line growth as well as profitability.

This brings us end to our commentary and would now like to request the moderator to open the forum for question and answer.

Moderator: Ladies and gentlemen we will now begin the question and answer session. The first question is from the line of Girish Raj from Quest Investments. Please go ahead.

Girish Raj: Just want to confirm that TCV that we have mentioned of $619 million, this is net new or there is a renewal part also?

Vinod Kumar: The 619 million is 85% increase over the last year is gross so to that there has to be some in the case of growth services it is mostly going to be new because these are the portfolio, but these are gross numbers that I shared.

Girish Raj: This would include innovation also, right?

Vinod Kumar: Yes, this is growth and innovation.

Girish Raj: So can you break it up?

Vinod Kumar: I do not have it handy we will have to provide that later I do not have that number.

Girish Raj: And order book can you please this is the TCV so we would have order book for growth and innovation also if you can share that?

Vinod Kumar: Yes, we can there is 1.1 billion and we are saying 619 is for the growth service.

Girish Raj: I thought it was TCV, but we would have some other order in hand which was booked otherwise.

Vinod Kumar: When you say this is the contract value, so it can be anywhere from 1 to 5 year generally. There may be some exception but by and large that is what it would be that is what I am referring to contract value and order book I do not know how you are seeing it differently maybe you can take that with Vipul. It can be various term I just wanted to be clear it is not one-year contract, but it can be some of it can be 1, 2, 3 to 5.

Girish Raj: And the typical deal size in innovation would be Vinod in what range?

Vinod Kumar: It is very tough to call that out and also keep in mind that this time in the growth services we have won $300 million deal that skews things up.

Girish Raj: You noted that ramp up will start fourth quarter can you also tell us meaningful revenue for innovation services on a quarterly run rate basis when can we see that?

Vinod Kumar: To the growth services level you know remember we said that we expect in FY21 to be about 150 million from innovation services so if you are waiting for growth services level you will have to wait till then.

Girish Raj: And what kind of net revenue margin can we expect in innovation?

Vinod Kumar: In the innovation services in the 30% range.

Girish Raj: 30% range lower than what we do in growth services.

Vinod Kumar: It will take some time for them to reach steady state right that is giving like an FY22.

Girish Raj: So when we do $150 million I am assuming that is steady state?

Vinod Kumar: Not really if you look at growth services on an annual basis it is more than that right. So I would say steady state will be in FY22 onwards so FY21 I would still think that it is parts of the portfolio will still be growing.

Girish Raj: One question on growth services it has grown very well but operating expenses run rate is only $49 million to $50 million per quarter despite the growth how do you see these operating expenses trending because we have good pipeline of orders.

Vinod Kumar: But let me explain that the manpower cost in platform cost associated with growth services will largely remain flat and we will show operational leverage or economies of scale in that portfolio that is the general comment and specific number let me just quickly look at or Pratibha can answer.

Pratibha K Advani: As revenue ramps up there is going to be a bit of scale effect while it is not going to be directly proportional to growth, but there will be slab increase as the revenues increase.

Girish Raj: No Pratibha where I am coming from is we started with $88 million quarterly run rate and we have done 101 still the operating expenses in dollar terms has remain more or less flat at $50 million just to understand how we should build our numbers?

Pratibha K Advani: As Vinod said that they would remain flat at these levels, but there is a step-up impact that happens as revenue grow but more or less at least for the next year they should be at these levels.

Girish Raj: We also had a expectation on neutral EBITDA in FY19 do we still maintain that for the growth service.

Pratibha K Advani: We would be marginally maybe negative and the only reason for that is the fact that we have had this upfront cost for some of the large deal wins that we have had, but we will close Q4 on a positive note.

Girish Raj: So largely what will be the size of these large deals?

Pratibha K Advani: Vinod just share that some of this like one of the deals that we won for unified communication portfolio is close $30, $35 million.

Girish Raj: Excluding this one off in the traditional services what kind of operating expenses run rate can we see because this is more of a stable business and it has been in the range of $140, $145 range this quarter it came in at 125 million.

Pratibha K Advani: This quarter while we did get the benefit on account of ASA there was also the incremental cost that we incurred close to 86 odd crore on account of access. We expect this access cost to be in the range of 30, 40 crore in Q4 and thereafter it would normalize.

Vinod Kumar: Overall for traditional services you will see fairly cost going into next year, but as Pratibha said we are doing a lot of accessory engineering in this cost associated with it. Accessory engineering on account of the India market shake up and our options have decreased in terms of third-party access over the course of this year and we had to redesign our network and how we provide access those are the costs that Pratibha was referring to but we hope that we will be over that hump by once this quarter did get in closes.

Girish Raj: If I may just ask margin more or less in the transformation services remain flat despite good growth in revenue what kind of business are we handling and the pipeline growth outlook and margin on this particular business?

Vinod Kumar: For transformation services the margin contraction has been on account of some of the fiber maintenance contract and field work for India related contract, but we have a healthy pipeline of close deals as well as healthy funnel of international activity that is gives us comfort that the margin profile will change in the coming quarter.

Moderator: The next question is from the line of Aliasgar Shakir from Motilal Oswal. Please go ahead.

Aliasgar Shakir: First question on this traditional business to be done even if I exclude all the cost and one off I think close to about 31% odd EBIDTA margin I think historically we have sort of given a trend of about 29%, 30% of thereabout, do you think there is a step up in this EBITDA margin which is a steady state number which is sustainable?

Pratibha K Advani: Ali we would still go with 29%, 30% range.

Aliasgar Shakir: So in that context are you suggesting that we should see downward trend in the traditional EBITDA number going forward/

Pratibha K Advani: I would say you would see stability of margin at 29%, 30%.

Aliasgar Shakir: And on the growth services you mentioned that you will be slightly negative on the overall base in FY19 but we have done cumulatively about 93 crore of loss in EBITDA for growth services and related question is that given that Vinod mentioned that we have a very strong deal pipeline and there are cost associated with them so even if we do turn profitable in fourth quarter, do you see this concern that I mean although we will remain EBITDA positive if you exclude that related cost, but if you add that there will be a substantial impact on EBITDA and therefore we may not probably kind of EBIDTA number that we have been suggesting?

Pratibha K Advani: Ali the way to look at is that if this one-off deal cost had not come, we would have ended the marginal loss or EBITDA neutral this quarter of course the impact as I mentioned in my commentary has been on account of three reasons one is the fact it is a seasonally weak quarter. Secondly the product mix has undergone a change and the numbers that I shared you thought that our media services portfolios and the other portfolios have grown. Now these are portfolio that we are still continuing to invest and of course the one-off impact because of the large deals that we have won.

Vinod Kumar: To add to there I just want to say that yes there are one off cost if your concern is at future revenue and we will also have this one-off cost. We believe that they will start getting offset by the usage revenues growing on some of our sole deals and on contracts which are being implemented reaching completion stage and then we can deliver them to customer and bill they will offset it. So we can say that going from Q4 will be positive on growth services for EBITDA and we believe that it will stay positive going forward after that if that is what you are trying to let out.

Aliasgar Shakir: This quarter I think can you just suggest the number that we spent towards this growth services for the deal related cost?

Pratibha K Advani: This would be close to $2 million.

Aliasgar Shakir: So that kind of cost should one build in our numbers going forward consistently for the kind of growth that we are building in this segment?

Pratibha K Advani: No Ali. Vinod just explain that you do not need to build that the cost because it will get offset with the revenue scale up that we are seeing.

Aliasgar Shakir: And just on this TTSL deal should one assume that given that Bharti deal with TTSL has got slightly delayed I mean any deal with TTSL linked to when Bharti gets DOT approval from TTSL and in case I mean now the elections are coming if it gets delayed our deal with TTSL should probably also be linked to that?

Vinod Kumar: I do not know whether it is linked to general election or not. I will take this opportunity to make a commentary on the TTSL so we continue to remain interested in the asset and the business we believe is complimentary and it will also help us in the access side. However, it can be seen transaction with Bharti has to be concluded and that is taking than was expected. Though once that happens then the clock will start on our transaction. So just by the nature of these things if you take the closure of the Bharti transaction on TTSL related mobile as time zero it will probably take anywhere from 2 to 4 quarters, after that to go through our own process to consummate a deal. So if you are thinking of timeframes how you should think about it but we have bridges to cross before get to that day zero milestone. We are not involved in ourselves I am going to be clear about that.

Aliasgar Shakir: Just one clarification over there so TTSL some of the liabilities that Bharti is not going to take do they remain with Tata Sons or there is a possibility of….

Vinod Kumar: I cannot comment on that. That has nothing to do with us?

Aliasgar Shakir: And just if I can slip in last question on the land sale part that you mentioned again over there given that general election are coming, should one assume that I mean now the ball will be in the next regime to sort of clear the deal given that now it is sitting with the cabinet or is just procedural and this not really require any ministerial approval, can you just throw some light on that?

Vinod Kumar: My personal view on this is that this is now procedural. Ministry of Urban Affairs, they are in the process of appointing directors it is not with the cabinet, it is just the process of clearing the MCA procedure and we believe it will happen largely mechanically and it does not require any further executive review or approval.

Moderator; The next question is from the line of Sanjesh Jain from ICICI Securities. Please go ahead.

Sanjesh Jain: On the TCV side which you mentioned we have an order of $1.1 billion on the data side and this we mentioned is gross right, so what kind of price erosion generally we see in these kind of deals over the period of execution?

Vinod Jain: Sanjesh that is a good question, but too broad a one for me to give you a simple answer. The price erosion on a blended basis across our base of service can be in the high single digit. We really have to look at service by service and comment, but you can take high single-digit.

Sanjesh Jain: On the other side if I look at the way our GDS revenue has grown over the years the robustness which we are seeing in the order book is still not getting reflected in the revenue is there still time for us to show this kind of growth as in 52% growth in order book and 10% growth in revenue still does not match a lot, what are we missing here?

Vinod Kumar: I think there are so many things happening right which we have to look at. One is we lost a big chunk of our India service provider business on account of the market consolidation. So this year therefore dampened our good traditional services growth within our data portfolio considerably on the back of that. The second as I said is on the growth services part of GDS is a longer duration to ramp revenues order is in hand partly in the case of SD-WAN services because of the complexity of the implementation and in the case of a UC portfolio to turn up usage and to drive adoption within the customer. So, this year we have seen both playing out and hence you see the lag and hence you see although we have had a CAGR of 8.8% over the last three years, we are in low single-digits for the year that we are in right now.

Sanjesh Jain: So when can we expect this convergence happening wherein our revenue growth also dragged the kind of order book which is showing a fall. I agree over a period of time.

Vinod Jain: So over a period of time and if you take for example an IoT deal the volume will build up even for the customer and it will peak maybe in this third year and then go and those are the kind of services we are dealing with now, but I would say that going into the next year you will see revenue begin to pick up speed which is why I have been able to say that in the innovation portfolio we still feel that we have a good chance to get to the $150 million number that we have in our FY 21 goals which we have shared.

Sanjesh Jain: On the growth services I was saying last three years our revenue on a quarterly basis has gone up by 124% and our losses have also increased in the same proportion with 164%. So despite such a strong growth still profitable growth is missing in the growth services, so how is it going to change probably from here when we are looking to double the revenue from here on the cost side and on the margin side?

Vinod Kumar: We have alluded to this in earlier answer that in both services the operating expenses will still flattening out of the growth rate will decrease because we have the critical mass of people, system, capability, sales force and so on. Yes we have to add we cannot create double digit growth without any investment but it would not be at the same time as we have had in the past and this has been the key metric that we have been tracking and all of you have been tracking which is how is the growth services is turning profitable and there is come through yes increased but now increased to previous periods slower ramp and expenses and the revenue is beginning to pick up. We believe that going into next year the gap between the two, i.e., between revenue growth rate and cost growth rate will widen and hence, my remark that we believe that one is turning EBITDA positive in Q4 we will remain that way and grow the quantum?

Sanjesh Jain: And in the innovative services when we will turn around as in at a what revenue do we think we will turn around because that again will keep adding to the drag on the profitability on the GDS side? So what kind of mass you are looking in wherein the losses at least on the innovative side.

Vinod Kumar: I will just give a rough timeframe in FY21-22 period we should start seeing innovation services portfolio turn positive.

Sanjesh Jain: On the enterprise side for the last three years the enterprise contribution has somewhere remained in a range bound of 56% to 59% earlier that we used to expand quarter after quarter and this again is on the background that our growth services have grown much stronger way which is mostly on the enterprise side so what is happening. there why is this contribution is not growing?

Vinod Kumar: Firstly, I would just say that we should look at what is profitable revenue and over worry about enterprise or service provider in one way at a very macro level. The reason why we want to pivot more towards enterprises we believe that there is potential to sell more services to enterprise customers, i.e., increase our PPR and that creates stickiness and reduces price erosion. So, our strategy continuous to remain that we will be double barreled in our market approach to go after service provider and enterprise to leverage this scale at which we can sell and service provider business to achieve unit cost and reach that will help us in the enterprise space and then keep that virtual cycle going. I think it is important to track that number but not get to alarmed if it does not change dramatically as in by large percentages on a quarter-to-quarter basis, but the general trend in our business over the last five years has been enterprise is growing and that will continue to be the case. But we are equally focused on leveraging our reach and sweating our scale to grow in the service provider business as well.

Sanjesh Jain: How this mix is in your order book as in incrementally if I look at order book are we inching up from these level in the enterprise side?

Vinod Kumar: The very fact that growth services is a big part of our order book it is largely from enterprise.

Pratibha K Advani: Also I can I just add Sanjesh to what Vinod has already said that if you look at the share of enterprise even between last year to September it had gone up by 2%. This quarter it has fallen only because of the AFA impact coming in our service provider revenue.

Sanjesh Jain: This is also on a background that we have lost lot of India service provider revenue in that sense I thought 200 basis point is slightly low and if you look at two years back we have reached up to 59% and again come back to like 57%, 58%.

Pratibha K Advani: Last quarter we were at 59%, we are stable at that number.

Sanjesh Jain: Just on the CAPEX side can you give a little more breakup on the data side where are we spending between traditional growth and subsidiaries because this number remains quite sticky for us and even if you look at order book predominantly it is coming up from growth side so how should we see it in the view that our order book is more towards side is there a probability that can the CAPEX can come down from the levels we are now today?

Vinod Kumar: I would keep CAPEX in your models that we are today we still have to refresh network we have to increase our access. Keep in mind that we sell more growth services once we have customer on our network. Yes, we are moving to internet-based solutions and so on, but especially in India access is an important competitive advantage. We have been very prudent with our CAPEX spent the ratio is lower than any of our competitors globally but there is an entry ticket level of CAPEX that we have to invest in to be in this game. So, I would it that main kind of the current level.

Sanjesh Jain: Can you break it between the segment and the data which is traditional growth and subsidiary?

Vinod Kumar: In the interest of time why do not we move forward as soon as Pratibha has that data point we will share that on the call.

Sanjesh Jain: Just one last question here. Given that Reliance Jio is looking to share its fiber and they look having a very sizable piece will that help in reducing your CAPEX of converting CAPEX into OPEX?

Vinod Kumar: I do not know the answer to that we have not have any discussion with them.

Moderator: The next question is from the line of Bharat Sheth from Quest Investment. Please go ahead.

Bharat Sheth: On innovation side this quarter is our operating expense run rate has increased which was 11.4 in Q1 then 12.1 this quarter it is 15.6 I believe this is largely on account of Teleena merger correct?

Vinod Kumar: 3 odd million increase is on account of Teleena merger, yes.

Bharat Sheth: So how do we see now from here on this run rate.

Vinod Kumar: I would not call it Teleena separately I would just say that

Bharat Sheth: Including Teleena this is 15.6.

Vinod Kumar: We will even maintain and even grown our expenses on the innovation side, but we expect to start seeing some revenue growth as evidence by the order book that I said that we have from MOVE and IoT so we will start seeing that off set, but we are not calling for a positive EBITDA on the innovation category for the coming three to four quarters.

Bharat Sheth: In current quarter 9 months we have done a revenue of around 3.34 million and we are looking for 150 million in FY21 so what in your guess will be approximately in FY20 and so will that I mean bring down the loss percentage?

Vinod Kumar: We have not modeled that fully to share a figure. I would say that we will see revenues in the order of 25 million to 30 million next year.

Bharat Sheth: That is net revenue or gross?

Vinod Kumar: Gross.

Bharat Sheth: So, net will be somewhere around 7, 8 million.

Vinod Kumar: Depending on the mix yes you can take that 8 million to 9 million.

Bharat Sheth: So further I mean there could be increase in the overall expense so loss may remain at this level?

Vinod Kumar: So, loss could be at this level or slightly greater if you look only at innovation services.

Bharat Sheth: It will not be targeted say our EBITDA of data business I mean 23% to 25% in FY21 which was say 17.2 in FY18 so where do we stand in this whole journey?

Vinod Kumar: The aspirational goal that we shared of the 25% EBITDA still remain. It will have to come from the growth services. Innovation services is really building a future proof business but to also I will come to the valuation remarks separately, but the growth services is where we will have to deliver significant economies of scale. We also hope that some of the large wins that we have in the innovation services, we can multiply and therefore we will be able to deliver positive and meaningfully EBITDA contribution from FY21 onwards to the data services. The point that I want to make on this is the innovation service is that the three areas we have identified the three larger ones are all getting significant traction in the market place and we do not want to think short-term and pull back on investing to create the inflection for the future and we are not living a pipe dream here. It is real services, real customers who were doing pilots and many of them are increasing the size of the pilots and the application and we will not over-spend in this area, but at the same time we do not want to just squeeze it out of necessary investment that will lead to bigger ramp in the future.

Bharat Sheth: Still at FY21 150 million we are expecting from innovation still at that level do you think will be EBITDA positive or still it will be a breakeven?

Vinod Kumar: I do not have that information right now. I have spoken only at a portfolio level so we still we believe that our aspiration is at 25% that is the number we called out for EBITDA for data services on a blended basis that continuous to be our aspiration. Is it a walk in the park? The answer is no because that is the industry-leading level especially since we have to contain the CAPEX and deliver a high ROCE which is better than industry also. And all parts of our portfolio will have to play a role to achieve that number that is much as I could comment.

Bharat Sheth: And growth service I mean this is your 9 months we have already clocked in I mean 287 so roughly we will be closing the year around 400 million level, so how do we see this in FY20 and then FY21 what kind of growth do we envisage?

Vinod Kumar; We will maintain or beat this growth rate.

Bharat Sheth: 9-month in your dollar term you have grown around 15% so do we expect I mean to beat this growth?

Vinod Kumar: Yes.

Bharat Sheth: So that will I mean give you a substantial positive EBITDA next year onwards correct?

Vinod Kumar: That is the plan.

Bharat Sheth: And traditional data I mean again I mean after all this one-off so Pratibha can you just say I mean operating expenses which was around 148 million so after all this thing whatever adjustment and closing so next year onward would it be I mean at lower level than 148 million run rate for the quarter?

Pratibha K Advani: These should be at lower levels. Hopefully, we would not get these 136-odd crores of one-off expenses hitting us.

Bharat Sheth: So that data is traditional data I would like to put I mean again at 29%, 30% kind of EBITDA margin or there will be some increase because the transformation service that which we are spending I mean earlier we were investing substantial amount in that so OPEX side also, so how that is happening?

Vinod Kumar: So that is going but frankly Mr. Sheth we are doing it at much lower both CAPEX and OPEX cost then what we shared two years ago, the digital transformation project. Pratibha keep me honest we said between 20 million to 25 million a year we would spend only on that right.

Pratibha K Advani: That is right.

Vinod Kumar: And we are not spending anywhere near that and we are achieving similar kind of outcomes that is a longer conversation on how we are doing it but we are doing it at much lower levels. We have even managed to do it largely within the previous IT spends level that we had.

Bharat Sheth: What kind of revenue target are we looking for this transformation service and EBITDA margins from next year onwards.

Pratibha K Advani: We should look at the range of about 16% to 17% Vinod.

Bharat Sheth: From this 10.5% level.

Pratibha K Advani: Transformational services is doing a 12%, 13% margin. I think you are looking at the standalone financials which is correct that standalone EBITDA margin will move up to about 13%-odd.

Bharat Sheth: As transformation standalone I mean I am not getting what you are saying because this is what we have reported in our factsheet.

Pratibha K Advani: Yes, that is correct because that is a subsidiary so we have reported the standalone margin, but when we look at the consolidated, we net if off at the company level some of the expenses get netted-off at the company level.

Bharat Sheth: And how do we see the scenario of working capital I mean in this whole year working capital is increasing with Voice revenue is coming down?

Pratibha K Advani: You rightly pointed out that the working capital gap is primarily because of the steep decline that we are seeing in voice. We hope to augment this gap by monetization of some our real estate assets, and that is really will help us reach this gap.

Bharat Sheth: Are we talking of this land parcel or other assets that we have in our book?

Pratibha K Advani: Yes, I am talking about both land and buildings that we have.

Moderator: Ladies and gentlemen that was the last question. I now hand the conference over to the management for closing comments.

Pratibha K Advani: Just response to Sanjesh's question our CAPEX breakup between traditional growth and subsidiary so growth and innovation together would be around 60 odd million. Our traditional we spent about $100 million and subsidiaries is 5 million.

Vinod Kumar: Thank you everyone for joining. I think we had great question and we have given a commentary on where we stand with the business. We expect to see the momentum in growth services continuing and we are also emboldened by the wins that we have had in the innovation category of our services and we remain committed to our FY21 goals and the aspirations that we have shared with you. I look forward to reporting good numbers in the next call that we will have in about three months or so. Thank you so much.

Moderator: Thank you so much. Ladies and gentlemen on behalf of Tata Communications that concludes this conference. Thank you for joining us and you may now disconnect your lines.

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