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Q2 & H1 FY2018 Earnings Conference Call Transcript

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

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Vipul Garg:

Vipul Garg: Thank you. Good afternoon, everyone. And welcome to Tata Communications Limited Conference Call. We are joined today by Vinod Kumar – MD and Group CEO; and Pratibha Advani – Chief Financial Officer.

Our results for the quarter and half year ended September 30, 2017, were announced yesterday, and the results fact sheet is available on our website. I hope you had an opportunity to browse through the highlights of the performance. We shall commence today's call with key thoughts from Vinod, who will provide you an update on the market environment and strategic direction of the company. He will be followed by Pratibha, who will share the financial highlights during the review period. At the end of the 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 the conference call today may be 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 is 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.

Vinod Kumar: Thanks, Vipul. Good afternoon, everyone. And a very warm welcome to all of you. I will start by giving you an overview of our performance, and then share my perspective on industry developments and our strategic direction.

The Indian telecom sector is going through a challenging time and the economic and market considerations are leading to industry consolidation. In the long-term we believe that this is good for the industry, but in the short-term this does cause some level of turbulence. At Tata Communications we are largely insulated from this since our business is more global and B2B in nature. Equally, we are well-expanded beyond the traditional services that most of our competition in India offers. Further, we actually see that their distractions are our blessings and we are seeing market share in India grow as a result.

As you all know that the Tata Teleservices announced to transfer its wireless operations to Bharti Airtel. They have been scaling down their operations for a few months and this has affected our business in TCTS this quarter. Well, there has been and will continue to be a top-line impact, the impact on margin is limited since we are mostly doing field operations work for them. We are working to recoup the lost revenue through other existing customer as well as by adding new logos. We have had recent wins in the international space for TCTS for higher margin services and so we believe that this shift will eventually prove to be even beneficial to us.

We are also in exploratory talks to acquire Tata Tele's enterprise business as we believe that Tata Tele has a strong asset base and enterprise customers with great synergistic benefits. The ability to consolidate our market leadership, strengthening our core network resilience and reach and the possibility to cross sell services across both our customer portfolios makes this opportunity worth pursuing.

Additionally, in a market where consolidation is taking place in other sectors within telecom, we need to do the same and gain size and create more avenues for growth. The industrial logic is very compelling, but rest assured that we will do the proper due diligence on the assets and the customers and of course pay extra heed to the need for doing this on a strictly arms length basis.

Coming to the financial results that we just announced, the performance delivered during H1 largely captures the impact of transformative initiatives that have been going on for the past few quarters. Other than for the impact from a handful of customer churn, I feel confident about the quarter and where we are headed. The voice revenue continues to decline in line with the industry trends and in line with what we have shared in the past. In this quarter we saw an improvement in the EBITDA margins of voice by 150 basis points as compared to the last quarter on account of recovery of outstanding from customers which was provided for as per policy.

The overall data business numbers look muted this quarter due to the Tata Tele impact and some softness in our traditional business. In traditional business we witnessed higher one-off customer churn this quarter and higher cost due to our business transformation which has lead to a decline in revenue and EBITDA. We have been ahead of this issue of churn for the past year and our programs to manage churn are being made more proactive. This increase in churn is temporary in nature and will normalize to previous levels in due course.

The question that I get asked is if traditional data is going the same way of voice? I believe that this is a fair question but this cannot be further from the truth. If you look within traditional data more closely we do have services like signaling which are slowing down. However, Ethernet is growing at 13%, VPN by 9%, ILL which is our internet access service in India by 10%, NPL which is our national private line service by 6% and so on. Each of these are significantly higher than market rates and actually in line with the 5% to 7% growth rates that I have provided before. There will be periods of churn due to customer contracting cycles. This is something we can anticipate up to an extent but not entirely. But we remained committed to the growth rates that we have provided for traditional services.

Moving on, our sales engine went through a large transformation as you know over the last year and we have decided to take an approach of having our teams focus on fewer accounts but go deeper into serving their full meals. This transformation exercise is beginning to settle down. Over the last quarter we added 96 new customers and our product penetration which is the number of products we sell to each of our customers has improved from 3.7 to 4.7 as on date.

Our growth services portfolio is driving strong and sustained expansion in the revenue profile of the business. Growth services witnessed a 40.5% year-on-year revenue growth and EBITDA losses are coming down steadily. The focus is clearly on driving solutions and platforms that can evolve, grow and serve enterprise customers.

I want to make a point here, in the growth services again is a basket of services. So, some of the reasons, why you see the gross revenue growing but net revenue not growing in line with the gross revenue growth, is because of the mix of services. We believe that the growth services portfolio are very complementary to each other within the products that make up that portfolio and as we sell one service we invariably open the door for conversations related to other services. And our sales and marketing teams are getting better at identifying these transitions from one service to the other and these are being fully leveraged. Therefore, I feel that the growth that we are seeing on gross revenue will also start flowing down the P&L as the quarters unfold.

Keeping in mind the investor feedback, we have segregated the innovation services from the growth portfolio to provide you a better understanding on the profitability mix and the shift that is taking place. Innovation services comprising of IoT, MOVE and NetFoundry are the new areas where we are investing for the future and they are in proof-of-concept stage, although in each of those cases we have several customers at various stages of implementation and billing. As the revenue scale up for these services, they will be gradually moved up in to the growth portfolio and we will keep it completely transparent for you to see those shifts.

In the payments solutions, EBITDA gap narrowed during this quarter on accounts of one-offs. The business has started to show some signs of improvement, the transaction is at almost 90% of pre-demonetization levels but cash handling continues to remain at 45% of pre-demonetization levels. We will continue with the exercise of ATM portfolio rebalancing and strict cost optimization to improve the profitability of TCPSL.

The product portfolio that we are focusing on today will ensure traction in both revenue and earnings performance, while at the same time underlying a strategic direction. Through digital transformation initiatives we are seeking to set a template for gains both in terms of business performance and enterprise productivity. The digital platforms that we are putting in place will help us to be more agile and will allow us to roll out managed services and solutions at an accelerated pace and at a lower cost.

We understand the company's pace of earnings delivery is going through a volatile period but we strongly believe that a portfolio shift is structural in nature and when we combine this with execution and operating leverage it will drive stronger EBITDA and return ratios in the future. We are committed to expanding earnings profile across the business, especially as growth services see some products attain significant scale.

One of the areas that we will be focused on is reducing staffing cost by tightening deployment of headcount in to the traditional areas of the business. We have had to add people during the transition period and while our new platforms are being created, but these additions have already stopped and going forward we will manage any increase that we need through the process of the natural attrition that takes place in the business. The headcount increase in H1 has largely been in the areas of IoT, mobility and security where our service portfolio is being created and where we are creating new avenues for growth.

Our new products and solutions are getting recognized on the global forums. We recently received recognition in the IoT space at the TechXLR8 Asia and Ovum Industry Congress. At the TechXLR8 Asia conference we won the award for the Best IoT Connectivity Solution, being voted the Best and Most Innovative Solution Provider for the MOVE proposition which we launched in October last year. At the Ovum Industry Congress, the company's IoT solutions emerged as the winner of the Internet of Things Award. This win was attributed to Tata Communications city wide deployment of the LoRa network as part of the smart city initiatives. Recently at the NetEvents' Global Press & Analyst Summit we won the Innovation Leader IoT Award for NetFoundry which offers technology for building application specific network.

Moving on, to give you a glimpse of what is happening within our sales organization with a particular view on the Americas region. During this quarter we appointed Bob Laskey as the regional head of our Americas business. This appointment forms part of the company's strategy of enabling its enterprise customers and cloud partners to drive their growth in the digital economy in both developed as well as emerging markets. We are seeing growing demand in the Americas for our cloud enablement services, including and especially IZO SDWAN and IZO Internet WAN solutions.

Tata Communications has made new investments in its infrastructure in the Americas. By connecting the recently launched Seabras-1 cable system to our Wall, New Jersey cable landing station and its global network, the company now offers US enterprises the most direct link between the financial centers of New York City and Sao Paolo. Additionally, the company has built three new points of presence in Jacksonville, Florida; Minneapolis, Minnesota and in San Louis, Missouri, growing the footprint of 48 pops across both major cities and emerging business hubs of the US. I should also add here that our sales team is focused on IZO WAN and IZO SDWAN capabilities has increased the funnel in both of these areas with very large US multinationals and we hope to be posting some wins in the coming quarters.

Globally, the world of communications has become challenging as widespread technology disruption over the past decade and beyond has lead a shift away from the traditional systems. What we know clearly is that the digital revolution is here and is here to stay. From my conversation with enterprises all over the world, everyone I meet wants to understand what digital transformation looks like and how it can enable them to capture borderless growth and boost productivity in both the short-term and long-term time frames.

A successful digital transformation hinges on having a global strategy which shows acute awareness of local implementation needs. Furthermore, you need to have a single transformation partner that will commit to deliver measurable objectives over the period of an agreed time. And this is exactly what Tata Communications has been doing and offers its customers. We have truly embraced being digital way of life, transforming data into new revenue and new sources of value and brings today an amalgamation of organizational culture and technology.

In summary, looking at the lead and lag indicators of our business in great detail, reviewing the execution status of our key projects and hearing about our product relevance through customer engagement I remain bullish about our transformation and our business.

Finally, on the surplus land issue, the matter is in its final leg and I see no hiccups whatsoever in our being able to file this scheme fairly soon. There are steps that have to be taken to complete the paperwork. These sometimes take longer than one anticipates but there are no issues of contention or dispute, it is really a matter of documentation and hence you will see movement on the long-pending issue fairly soon.

With that I would like to invite Pratibha to discuss the financial highlights of this last quarter. Thank you for your attention.

Pratibha Advani: Thank you, Vinod, for providing and sharing these perspectives. A very good afternoon to all of you on our call today. I will take you through the financial highlights of the quarter and will also share some updates regarding the progress of business and financial transformation journey that we have embarked upon.

During Q2, core business revenues declined 2.1% Q-on-Q and 6.5% Y-on-Y. The decline in revenue is primarily due to de-growth in voice which de-grew by 6.5% Q-on-Q. We also saw de-growth in transformation services which Vinod mentioned earlier by 4.3% on account of lower revenue from Tata Teleservices. Core EBITDA this quarter came in at Rs. 565 crores, an increase of 1.1% Q-on-Q with an improvement in margins by 40 basis points over last quarter. This was primarily aided by higher margin in voice and one-off benefit that we received in the payments solutions business. On a Y-on-Y basis the EBITDA declined by 13.7%, the margins were down by 110 basis points due to payment solution services impact which had a 30-basis points impact on the margins, adverse FX impact of another 30 basis points and higher investment in innovation, transformation and the access facilitation charge impact together accounted for 60 basis points. You would recall last year in Q3 we had to take a 8 million provision on account of access facilitation charges.

Core depreciation was high this quarter by Rs. 39 crores due to one-time accelerated depreciation on some of the international assets. Core PAT was negative at Rs. 250 crores due to Rs. 186 crores of additional provisions on the contractual obligation to Tata Sons on Tata Teleservices investment and also due to one-time exceptional provision of Rs. 27 crores. Based on the recent developments in Tata Teleservices we have recognized a loss of Rs. 516 crores in other comprehensive income for the quarter. The value of Tata Teleservices investment in our books as on date stands at nil. This will result in net worth erosion of Rs. 927 crores including the dividend payout that we had made early on. This net worth erosion will be partially recouped during the course of the year as we make profit.

During Q2 data services revenue increased by 2.2% Y-on-Y and 0.2% on Q-on-Q basis. The growth was primarily lead by strong traction in growth services. In Q2 both revenue and EBITDA were affected by the Tata Tele impact and softness in traditional data business. As Vinod explained earlier we are working proactively to mitigate the impact of both these events. The data EBITDA for the quarter came in at Rs. 462 crores, a decline of 2% quarter-on-quarter and 14.6% Y-on-Y. On Y-on-Y basis the margins declined by 320 basis points due to higher investment in innovation transformation and ASA impact accounting for 150 basis points, higher manpower and backbone cost of 130 basis points and impact of the payment solution services business of 40 basis points. On Q-on-Q basis the margins declined by 40 basis points due to higher manpower cost. I would like to add, our data services portfolio excluding subsidiaries is growing at 1% Q-on-Q. The growth is 4.1% Y-on-Y and year-to-date the portfolio has grown by 5.1%. We are seeing a sequential growth for the last six quarters if we exclude the ASA impact, this converts to a quarterly CAGR growth of 2.2%. Please note that this CAGR growth includes one-time ASA reversal in Q3 last year of US$8 million that I mentioned earlier.

Moving to our traditional services portfolio, this witnessed a revenue growth of 1.7% year-on-year during Q2 with EBITDA of US$82 million. On a Q-on-Q basis the traditional revenues declined 2.6% due to higher one-off churn in H1. Traditional services grew by 4.4% year-on-year. The margins were affected by decline in revenue and increase in cost due to transformation initiatives. This decline in margins is temporary in nature and as the benefit of cost productivity on account of business transformation starts to flow through, the EBITDA margins will come back to the 29% - 30% range that you had witnessed earlier.

We continue to see strong Y-on-Y growth in few products like NPL, Ethernet and ILL. NPL is growing by 12%, Ethernet by 10% and ILL at 9% year-on-year. Growth services showed exceptional traction this quarter with a 40.5% revenue growth year-on-year. The momentum in the portfolio continues to build as we grow in scale and increase customer engagement. In H1 revenue grew by 33% year-on-year, this is third quarter in a row wherein the growth services have witnessed greater than 25% revenue growth. The EBITDA losses are steadily coming down and as Vinod mentioned we are hoping that a few products will turn EBITDA positive in near-term.

We are witnessing good traction in IZO which grew by 403% year-on-year, mobile new services grew by 192% year-on-year and video connect by 72% year-on-year. We have separated innovation services from the growth services portfolio. These services are the ones where we are still investing and are in the proof-of-concept stage. As these POCs start turning into revenue contract and achieve some scale these will be moved to growth portfolio - IOC, MOVE and NetFoundry are part of this portfolio. Year-to-date we have invested 14 million in this portfolio.

Coming to the subsidiaries, transformation services was affected by closure of Tata Tele as I mentioned earlier. We are working to recoup the lost revenues through new client wins and we are seeing a good funnel build up. We will also be optimizing the cost in coming quarters to enhance profitability. The payment solution business is taking longer to normalize than expected, though we are witnessing some signs of recovery. The focus remains to enhance profitability to efficient portfolio allocation and cost control. Our voice business saw a revenue decline of 6.5% quarter-on-quarter and 19.7% year-on-year. EBITDA saw an improvement by 17.5% Q-on-Q primarily due to recovery against provision for bad debt. Margins there are at 7.2%, an improvement of 140 basis points over the quarter. However, I would like to add that the normalized margins in the voice business will remain between 6% and 6.2%.

The voice business is important to us as it continues to generate healthy cash flow of Rs. 101 crores. In Q2 our CAPEX was US$75 million, this looks higher due to payment of US$20 million for the Seabras cable that Vinod mentioned earlier. This cable connects North America - Latin America and provides a vital connectivity link. Normal CAPEX for the quarter is $55 million which is very much in line with the guidance that we had given earlier. The free cash flow, EBITDA minus CAPEX for the quarter stands at Rs. 82 crores, lower by Rs. 148 crores as compared to last quarter due to increase in CAPEX of Rs. 154 crores during this quarter. The net debt at the end of the quarter is at US$1.209 billion, an increase of US$5 million over last quarter on account of the payment for Seabras cable.

The finance cost was marginally high this quarter due to reversal of capitalized interest as funding of projects happen through internal accruals. The cost of debt was marginally up to 3.3% from 3.24% earlier due to LIBOR moving up on USD borrowings. For us the objective remains to balance our free cash flow position with the transformational and growth initiatives that we have unleashed within the organization.

We are excited about the opportunity to increase our enterprise footprint through customized solutions and platforms which will boost both our top-line and our profitability. Our business transformation program is moving with the right momentum and we will be implementing robotics in some of our processes by the end of this calendar year. We are committed to drive cost productivity and you would have observed that Q-on-Q our operating costs are almost flat.

That brings me to the conclusion of my opening remarks. And I would now request the moderator to open up the forum for questions. Thank you.

Moderator: Thank you very much, ma'am. Ladies and Gentlemen, we will now begin with the question-and-answer session. We have the first question from the line of Riddhesh Gandhi from Discovery Capital. Please go ahead.

Riddhesh Gandhi: Just a question, so how large is the enterprise business acquisition that you guys are looking at in terms of EBITDA?

Pratibha Advani: Actually, we are currently going through the due diligence process, so it would not be appropriate for us to quantify. Hopefully, in the next call we will be able to add a little more color to that question.

Vinod Kumar: And there are different components to the enterprise business at TTSL which we are reviewing and we are also evaluating which ones are of interest to us. So it is a bit early to comment on the exact size of that.

Riddhesh Gandhi: Got it. And in terms of the recovery of the lost business of Tata Tele, how quickly do you think the recovery would be from the existing pipeline and like the new clients, you guys are expecting?

Vinod Kumar: It will probably take us, in terms of just replacing the top-line, around two to three quarters for us to make that recovery.

Riddhesh Gandhi: And at the EBITDA level?

Vinod Kumar: More or less the same, because when we acquire a new business there is also a ramp period, so it's tough to say. What I can say is over time the EBITDA profile will be stronger of the new business that we are acquiring because they tend to be more value-added services and are mostly international.

Riddhesh Gandhi: Got it. And in terms of the data traditional where we have had a small amount of de-growth which has happened, do you see that now up-ticking immediately or you see still actually another couple of quarters where you will have some incremental client churns?

Vinod Kumar: I think we will have a couple of incremental client churns, because keep in mind that we will also have to absorb the impact of the TTSL or services that Tata Communications sells to TTSL beginning to decline. So we have that too, we need to absorb going forward and replace it with new customers.

Moderator: Thank you. The next question is from Naveen Kulkarni from PhillipCapital. Please go ahead.

Naveen Kulkarni: First of all, a question related to Tata Teleservices. Could you quantify the exact impact of the loss of business from Tata Teleservices on the EBITDA number? That is my first question. Second question is on the data segment margins. So we have seen that of course there is some bit because of the new development, but we have seen that the margins are on a declining trend for a few quarters now. So how do we see this going ahead? Some time back we were looking at margins moving up in the 20% range. So, what kind of time frame do you see for that trajectory to come back? And thirdly on the traditional services, we are seeing some bit of pressure in that business. So, what exactly is leading to that pressure and how do we see revenue growth panning out in that segment? And if you could highlight some of the key areas of improvement in this segment or key business opportunities that can lead to growth?

Vinod Kumar: So the impact on EBITDA due to TTSL is about $1 million. And in data segment margins, I think we have to look at it within traditional and in growth. In growth, you can actually see what we have said beginning to unfold, which is the margins are trending in the right direction and I still believe that we will exit this year on the pure growth portfolio. In the month of March we should be close to EBITDA neutral. The traditional services is where we are having the challenge because of the churn. And some of that has been unexpected churn because of customers, mostly wholesale customers moving on to their own networks which they have deployed and not buying IPL services from us. And that is really the reason for it in terms of traditional service. I believe that some of it is seasonal and some of it is one-off. But while that will pass, we have to absorb this impact of the TTSL revenues from traditional services principally in India on ILL and some level of capacity that they buy on some networks from us beginning to wind down. So we will have to replace that in the coming quarters. So as I said in answer to the previous question that it will probably take us a couple of quarters to absorb that decline and while the rest of the growth begins to pick up. On growth services, the pace at which we are growing I believe is impressive, it is much more than anybody in the market. And we believe that that momentum will continue to maintain over the next few quarters also.

Naveen Kulkarni: So just if I get it correct, sir, the impact of Tata Teleservices is $1 million on a quarterly basis, right? So that would be around $4 million on an annual basis. That's right?

Pratibha Advani: It is $1 million only this quarter.

Naveen Kulkarni: So this $1 million, is it going to increase in the forthcoming quarters or it is going to remain at roundabout this level only?

Pratibha Advani: It could change, it depends on how the structuring happens with Airtel. As you know, a part of that is going to Airtel. We currently do not have visibility on the structuring.

Naveen Kulkarni: But Airtel would also have a parallel structure, a service structure that you guys would be providing. Is that understanding correct or?

Vinod Kumar: I would not jump to any conclusions there. We will have to wait and see. That is why we are not able to give a precise answer on that because those things are being worked out.

Moderator: Thank you very much. The next question is from Naval Seth from Emkay Global. Please go ahead.

Naval Seth: As you stated that some part of growth services will be EBITDA breakeven by end of this fiscal. So, what kind of run rate we should see in next financial year? So, will there be more services which will be EBITDA breakeven or there will be a slew of new product launches which might accelerate the losses?

Vinod Kumar: So, within the growth portfolio what we currently, I do not want to start moving things from innovation into the growth portfolio, that will be too confusing. So, I believe into next year we will continue to maintain the same classification or categorization under growth and innovation which we just introduced this quarter. So we do not want to confuse you any more than required. So within that I believe, at an aggregate the growth services portfolio will continue showing an improvement in its EBITDA margin. We have not called out yet right now which services are EBITDA positive and which ones are not, so I do not want to get into it. But overall the trend of EBITDA for growth services will keep improving.

Naval Seth: And in terms of the guidance what you had given last quarter for $90 million to $100 million spend will be done over the next five years for transformation of internal processes, so how much of that would be done this year or how much of that is done already in H1? And if you can break up between OPEX and CAPEX within that?

Pratibha Advani: So actually our quarterly run rate on transformation is about $5 million a quarter and this is OPEX.

Naval Seth: And this will continue in the ensuing quarters as well?

Pratibha Advani: That is right.

Naval Seth: Okay. And last question is on the EBITDA margin, so continuing from the last caller's question. So, what kind of margin now we should look at for FY19 because there has been lot of one-offs in this year? So are we trending towards 23% - 24% margins or we should get restricted to a 20%? Any thought over there?

Pratibha Advani: What I would say is that while we will start to see margin expansion, and this will come on the back of improvement that we will see in growth services as we gain scale and due to some of the productivity measures that we are putting in place for our traditional services portfolio, there would be definitely a margin expansion. But currently it will be difficult for us to commit a number, because they are just too many moving parts happening with the change in the Tata Tele business revenue and the fact that we are currently also looking and having exploratory talks and acquisition of the enterprise business. So, there could be some one-off costs also coming to us. So at this point it will be very difficult to provide you a guidance.

Moderator: Thank you very much. The next question is from Amruta Pabalkar from Morgan Stanley. Please go ahead.

Amruta Pabalkar: Firstly, on the Tata Teleservices, could you give us some sense on what is the overall revenue exposure in the TCTSL segment towards Tata Teleservices?

Pratibha Advani: The total exposure would be close to about $50 million - $55 million.

Amruta Pabalkar: $50 million to $55 million on an annual basis?

Pratibha Advani: That is right.

Amruta Pabalkar: US dollars?

Pratibha Advani: That is right. But mind you, this is on the whole basket of services that they offer. And I would just reiterate that we are looking at some of those services moving within TCL fold.

Amruta Pabalkar: Okay. Now when we are looking at the impact of Tata Teleservices, would that be largely restricted to TCTSL segment or it would flow down even to the traditional ex-datacenter to some extent?

Pratibha Advani: The bulk of the impact would sit in TCTSL, the transformation services business. But mind you, having quantified that number on revenue, Vinod had also alluded earlier that the EBITDA impact would be far lesser.

Amruta Pabalkar: We can assume that margins would be marginally compressed and there would not be a significant cost allocated or increase in the costs?

Pratibha Advani: That is right. You are right there, Amruta, but one of the challenge before us is also we would need to reorganize that business once we have better visibility of the commercial relationship we may have with Airtel and really drive some cost productivity in terms of restructuring.

Vinod Kumar: So there are two parts of the services, or you can think of it as two kinds of services we offer TTSL. One is what we do through TCTS and the other is our network services that we provide. And both of these, it is tough to determine right now exactly what will continue and what would not. We know for certainty that they will be impacted and there will be a reduction, but we have not factored yet how much, what the quantified impact will be at this point because there will be a transition period to Airtel for the consumer business, the wireless consumer business of TTSL. And also the whole project of evaluating the TTSL enterprise business acquisition is underway as well. So there are a few moving parts here that make it difficult to give a precise number on what the impact will be.

Amruta Pabalkar: On the traditional bit, there has been softness over last two quarters. Do you revise your guidance for fiscal 2018 in terms of YoY growth of 5% to 7% or you still believe that that could be achievable? And what is your sense over next two years, 5% to 7%, do you maintain that guidance?

Vinod Kumar: I think there will be some pressure because of this, but we maintain the 5% to 7% range. But if I had to pick a number, I would say on the lower end of that range at this point because we also have to absorb this TTSL impact. Let us assume the worst-case scenario there. So we will have to absorb that.

Amruta Pabalkar: And coming on the margin bit when you had earlier said about 30% margin for this segment, in the current scheme of things how do you see that, how soon do you think you will be able to achieve this 30% margin and what gives you that confidence?

Vinod Kumar: You are talking about the data services, right?

Amruta Pabalkar: Traditional ex-datacenter, that's right.

Vinod Kumar: We continue to maintain that because we believe that there will be significant gains once our transformation and digital platform's programs are completed and our digital platforms are in place. We really are looking at radically changing the way we build, deliver and support services to our customers. So directionally, I still hold on to that and I am confident we will get there. Timeline, some of these impacts we will have to absorb, so there will be some impact by a couple of quarters, but it will not be, it is still definitely within our sight.

Amruta Pabalkar: It is fair to say that by end of fiscal 2019 you will be at 30% EBITDA margins on, any rough estimate there?

Vinod Kumar: No, I do not want to commit to that yet till I know the quantified impact. We are also taking, absorbing a hit due to RCom also being wound down. So we have some big players just exiting the market who use our services. We can take all these shocks. There is no impact to our business or direction. But these are big wholesale customers that we have to realize will impact our top-line.

Amruta Pabalkar: So, if I may just chip in one last question. On the growth services now you are seeing higher mid-teens growth over last couple of quarters and you expect this to continue over next couple of quarters. So, that clearly puts an upside risk to your overall revenue growth over next couple of quarters. In terms of margins of the growth basket, what do you see the steady state margin for this segment once you breakeven over next two, three quarters?

Vinod Kumar: For growth services I do not think we will be at steady state in two to three quarters, we have never said that. We believe that the margin will improve steadily, and I think we will get to the single-digit by middle of next year.

Amruta Pabalkar: And what would be the steady state margin once you achieve a scale for this segment?

Vinod Kumar: For growth to achieve scale, because you are talking about a portfolio of services, you are talking between four to six quarters, it will take us that long to start declaring it as a steady state and it is a blend. So, Pratibha, do we have a number that we can safely pick?

Pratibha Advani: Actually, in the current portfolio, I would think we should be able to hit mid single-digit margins. But then again in this portfolio we would start to add some of the innovation products.

Vinod Kumar: Just in this portfolio, I think that is a number for next year, but if you had to look beyond that. It will probably get to the low-teens in the following year.

Vinod Kumar: But IoT and MOVE I'm keeping outside, those are in the Innovation, right? She wants just the growth.

Moderator: Thank you. The next question is from Srinivas Rao from Deutsche Bank. Please go ahead.

Srinivas Rao: First, a slightly prosaic question here. You have shown SIP trunking as part of your bouquet of actually growth services. That's a fairly traditional product, shouldn't that be a part of your traditional services or are you seeing like massive…

Vinod Kumar: We do not see it that way, because SIP is being sold as part of our cloud solutions for hosted Skype for business and Cisco deployment. So, the way it is reported may sound traditional but by no means is it traditional in the way it is being consumed and for the services that customers or the bundles of service that customers are buying.

Srinivas Rao: Just a couple of more questions. I know people have already touched upon Tata Teleservices. The enterprise business purchase the deal is confirmed, right? It is just the contours is what you are kind of looking at? Am I correct in that assumption?

Vinod Kumar: No, the deal is not confirmed, we have just been approved by our board to enter into due diligence and to study the business based on the industrial logic of acquiring those assets and those customers. But obviously a deal is only agreed if you really know fully what you are buying, and you have to agree on value as well.

Srinivas Rao: So essentially you would evaluate, and you will make an offer price which has to be accepted by the TTSL board. Is that what you are looking at right now?

Vinod Kumar: That is right. And the deal is not be approved till the shareholders approve it also.

Srinivas Rao: And I do not know, do you have a exclusivity period to make an offer or TTSL can solicit from even other parties, including I don't know maybe Vodafone or Airtel itself making an offer for that part of the business?

Vinod Kumar: Well, right now there is no formal exclusivity.

Srinivas Rao: Okay, understood. And on the related part of the enterprise, because still that as a fairly large proportion of your revenue and I am including all enterprise services as you report, India being almost 45% - 47%. I mean, players like Vodafone and even Airtel and probably going forward even Reliance Jio have indicated or at least signaled an aspiration in that space, which has been historically underserved in India. Do you see that becoming much more competitive or the market growth will be such that you should be relatively less impacted going forward? And I am talking of a more two, three-year view here, not like for a year.

Vinod Kumar: Two things I will point to. One is we believe that the enterprise market has growth in India. Level of IT penetration or network services spend is lower than in other countries. So we believe the market is growing. Second is, and one of the reasons we are interested in the TTSL business is also enterprise businesses, the SMB segment we are seeing growth and that will be an opportunity for us to expand our addressable market further. But I think the biggest thing that goes in our favor is, while these guys may enter the space, we are redrawing the lines of what we do for customers so dramatically that while they are thinking of moving from consumer services to traditional connectivity services to enterprise, that was our game before, we offer that but we moved on to security hosting, UCC services, mobility, IoT. It is a different ballgame altogether. So we have redrawn the lines of what they are interested in well beyond traditional telecom. So that is why we feel both buoyant and confident about the addressable market as well as the ability to take on competition. It does not mean we would not face threats or pressure but we feel that we are ahead in terms of planning for the fight.

Moderator: Thank you. The next question is from Rajiv Sharma from HSBC. Please go ahead.

Rajiv Sharma: Just a couple of questions from my side. Given this TTSL acquisition which is under consideration, what is the kind of net debt to EBITDA you will be comfortable with say in next 12 to 15 months from now? Second question is, while RCom is trying to shut down the wireless business, they are still there in enterprise. But is there a time for you to take market share from them in the enterprise segment given low moral or any other thing you can think off? Third is, termination has been revised to Rs. 0.06, what kind of impact it may have on voice business? And is there an opportunity with the new voice over internet recommendations, internet telephony recommendations TRAI is suggesting? And lastly, do you want to take your IoT business to more retail or some kind of consumer, direct to consumer in nature or you'll still be industrial safety and B2B? I will stop here.

Vinod Kumar: You asked me five completely different questions there, and I think I got four of them, not the fifth one, but you can ask me again. Okay, so with the TTSL acquisition, we will have to see what the contours of the deal are to precisely answer you on what debt or how it will be structured from a financing perspective. But I would like to operate the business ideally between 3.5% to 3.7% debt when absorbing something like this. But obviously from a longer-term perspective what we have said is if we can get it to less than 3% that is where we want to be. But I do not want to also set the expectation that when we are doing an acquisition, whether it's TTSL or any other significant one, that you would not have period of going outside that ideal state of 3% or less. Keep in mind, though, that even at 3.5% - 3.7% we will still be significantly lower than other players in India or abroad. And we will never put the business at any risk in terms of debt to EBITDA ratio or interest cover ratios. Our board is very disciplined about that and so are we on the leadership team. And I have my treasurer looking at me with very sharp eyes as I make that statement saying that he is watching me as well and I am scared of him.

The termination cost reversal in India, we will have to come back to you. Frankly, the market is operating at such low margin. We are growing our business for maintaining what we are doing in voice based on the rest of world traffic in a way, and therefore, I do not see any upside or significant downside due to that. The policy change which is expected around voice over IP I believe will be beneficial for us, we are in support of it and we will come on the good side of that equation.

The question on IoT, we are not looking at IoT retail. We are singularly focused on B2B applications. And frankly, in India we are not even general B2B. We are looking at three or four key areas and those are smart metering, smart lighting, industrial safety and asset tracking and logistics and also smart cities, which brings all of that together. So, those are the five areas of focus for our IoT business in India. And we believe that that is where the ROI can be proven to our customers and also where we can actually make decent returns on our investments. So a short answer is, we focus on B2B and industrial IoT more and not on retail. And what was your other question?

Rajiv Sharma: RCom market share on the enterprise, can you take some from them?

Vinod Kumar: Yes, definitely. RCom, I will have to be careful about saying that because RCom has not been such a big player that we compete with in the enterprise space. So, we will have to look at the kind of customers they are serving, we would not blindly go after their customers. We need customers where we can make both margin and collection.

Rajiv Sharma: And lastly on that VoIP thing, if there is a 8% revenue share, if you will have to pay termination and some minimum network fee to any MVNO or underlying network, even in that case it will be a beneficial business for you?

Vinod Kumar: I think so, we will look at it in the context of expanded business and new revenues. And so if there is a license fee payable, then so be it.

Moderator: Thank you. The next question is from Bharat Sheth from Quest Investments. Please go ahead.

Bharat Sheth: If it is not too confidential, can we share TTSL FY17 enterprise business size and EBITDA?

Vinod Kumar: No, we cannot Bharat, I wish I could. One is, we are still in the process of due diligence, it would be unfair of me to disclose any numbers at this stage.

Bharat Sheth: And in this digital transformation, where OPEX run rate which is around $5 million per quarter, where do we see that in next year?

Vinod Kumar: We will continue to spend that during the course of next year. And there could be some marginal increase as well because the vendor contracts will be fully activated during the course of next year.

Bharat Sheth: And you said that we are selling these SIP services to Cisco for their cloud services. So now recently I understand that Cisco has tied up with the Google for their cloud's business. So how do we see that opportunity?

Vinod Kumar: Well, I think they are two different things. The announcement that came out last night we will have to study that more. But we are not selling this to Cisco alone. We are selling it to Cisco's customers jointly with Cisco as we are with Microsoft, and we are selling it to other players as well on the SIP trunking. So, we see this as a growth market and we see it as being able to continue maintain the growth rates that we have had. What they announced from my understanding is more on the compute side and storage side and we are not really serving that market today through Cisco.

Bharat Sheth: Okay. And recently since last year we have enhanced our effort in U.S. market and we have put the sales team as well as recently we have appointed also sales, marketing person there. So, how do we see this enterprise business' size currently in US and how do we see a plan to grow?

Vinod Kumar: So the US market is clearly the world's largest market when it comes to enterprise, and hence we are putting more emphasis there in terms of deploying resources to sell directly to enterprise customers, but also we have expanded our partner program in the US quite considerably. The funnel we are seeing in the US is strong and we hope that we can start tapping into the US market more than we have in the past. We have been selling to US customers, it is not like we are entering the US for the first time, we are just putting more emphasis on it.

Bharat Sheth: How is the traction in the first six months that you have started?

Vinod Kumar: The traction has been good from a funnel perspective. In the second half of this year we should start seeing some closures. And to the extent that customers permit us, we will be making public announcements on the wins.

Bharat Sheth: And this growth service, are we looking only Indian markets or are we looking also other market, I mean like IoT and cyber security?

Vinod Kumar: For the growth services, we are looking around the world. It is not only in Indian market. In fact a lot of the growth has been outside India and the funnel for us outside India in the second half of the year is also strong.

Bharat Sheth: And some of PoC that you have established, so are we getting I mean commercial realization happening? I mean what time frame?

Vinod Kumar: The PoCs I referred to were in the innovation bucket and some of those are already converting into build revenue, but they obviously take time to ramp-up, which is why the revenue numbers from innovation category, if you look at our fact sheet, are quite small. But you will see those beginning to grow in the coming two quarters. But again, they will be relatively small numbers compared to our overall portfolio. But they will start showing up and you will be able to track the progress.

Moderator: Thank you very much. The next question is from Pranav Kshatriya from Edelweiss. Please go ahead.

Pranav Kshatriya: I just got two quick questions. Firstly, we are seeing a lot of, so Reliance Communication has decided to shut down their consumer business. It is likely that Aircel may also follow the suit. What kind of impact do you see on the voice business, specifically if these kind of things happen with TTSL and Aircel, their revenue goes down? Will that be in the single-digit voice revenue decline what we see or there could be sharper decline in that? That is my first question. Secondly, on Tata Teleservices, are you having any kind of a bank guarantees or any contingent liabilities outstanding for Tata Teleservices? That is it from my side.

Vinod Kumar: So, there will be some impact. I do not want to like send people to their death before it actually happens. It would not be fair to them. But we will have to absorb the impact that will be on the data side as well as the voice side. On the voice side, frankly, on termination the impact can be absorbed because the traffic will still come into the country and the subscribers are not going to go away. It will just be one provider or another. You could make an argument that it may even reduce comparative intensity a little bit and may help stabilize prices. But these things have to play out before we start celebrating anything. There will be an impact on traditional services' revenues if all these players begin to shut down and there will be some rebalancing of traffic. So we will have to wait and see how it plays out. We have anticipated in a way on traditional services that some of these players will start slowing down. And if you see what we are doing in terms of selling ILL to other ISPs, the regional players, the cable companies and so on, that has been increasing over a period of time. So there will be traffic shifts as these things happen and we will have to see how they play out, it is tough to put numbers out.

Pranav Kshatriya: But would it be a significant impact or it would not really, I mean will it move the needle meaningfully? Because 10% to 12% kind of a decline what we are seeing in the voice business is very natural, it will be significantly higher, that is what I am trying to understand.

Vinod Kumar: Okay, on the voice business, see, as I said, it's not driven by who the players are as much as who are the subscribers there and the volume.

Pranav Kshatriya: At least my point is at least on the India outbound side, because the top three players do have their own their pipe for India outbound.

Vinod Kumar: We do not do much outbound traffic out of India, so it will have very little impact on us.

Pranav Kshatriya: And contingent liability for Tata Teleservices, anything outstanding?

Pratibha Advani: No. We have actually mentioned, I also mentioned, that all the investments have been written down.

Pranav Kshatriya: So no contingent. So bank guarantee, etc., is also not outstanding from that basis?

Pratibha Advani: No. We would have routine debtors and payables, but nothing else.

Moderator: Thank you. Ladies and Gentlemen, that was our last question. I now hand the conference over to Mr. Vinod Kumar for closing comments. Over to you, sir.

Vinod Kumar: Thank you all for your questions. We look forward to your participation in our next meeting, hopefully on the matter of TTSL. We will have a lot more clarity by then. And in the interim if there are any updates to share, we will be providing those to all investors at the same time. So there are things which are in flight now and it is difficult for us to answer them specifically without breaching any confidentiality, so I hope you will realize that the position that we are in makes us difficult to put specific numbers out. But we will share them as soon as we can.

Thank you for your patience as we go through this process. Thank you and have a nice day.

Moderator: Thank you very much members of management. Ladies and Gentlemen, on behalf of Tata Communications, that concludes today's conference call. Thank you all for joining us and you may now disconnect your lines.

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