# Infosys Technologies Limited

Transcript of Investor Earnings Call for the Quarter ended June 30, 2002
held on July 10, 2002 at 2.00 p.m. I.S.T., telecast direct by CNBC India

Lady presenter: Good afternoon and welcome to the first ever Earnings Call on air. Earnings Call, the venue where analysts put questions to a company management soon after results, is a closed-door affair. But CNBC India opens this door for you this afternoon by bringing you the Infosys Earnings Call direct. Well let us go across now to the Infosys management who are waiting there. Over to you Nandan.

Nandan Nilekani: Thank you Paromita. It is a great pleasure to be here on this live analyst call. We have had a quarter of robust growth. At the same time we are cautious about the future because of the challenging environment. We have added 23 new clients. We have had revenues of $153.6 million ***(Editor comment: $156.3 million)***. We have been successful in getting new customers like Bear Stearns, ZKB and others. We have added 744 employees ***(Editor comment: 772 gross employees)***, and we do believe that our utilization has gone up this quarter, the number of new projects this quarter has gone up, and therefore because of the new project starts we have had more onsite component to our business. We have also had an increase in sales and marketing expenses and hence our margins have been impacted by that. With this I throw it open for any questions.

Lady presenter: Right. Nandan of course we have got a line of analysts, lining up actually, to pose those questions. Well, we have got Sandeep Dhingra with us. Sandeep, good afternoon, go ahead with your question.

Sandeep: Yes I am here. Can you hear me?

Lady presenter: Yes Sandeep, we were waiting. Go ahead with your question.

Sandeep: Thanks. Congratulations to the Infosys team. You have had yet another strong quarter. Nandan, two questions. One is, the SG&A expenses which have gone up, can you tell us what exactly is behind this?

Nandan: There are two or three reasons for the SG&A going up. One is the bonus payment for sales bonuses which we have had to pay this quarter. The second is, we have additional people in both sales and in account management whom we have accounted for. The third thing is the increasing brand building expenses. For example, this quarter we had the Wharton Infosys Business Transformation Award, which is an increased brand awareness campaign to build a mind share among the executives. So, these are the kind of increased expenses on sales and marketing that we have had. I will request Mohan to add to that.

Mohandas Pai: The selling expenses have gone up to about 7.2%, an increase of nearly 2% compared to the previous quarter and they have been essentially on these three items as Nandan said. For the next quarter we do not think we will have an incremental increase as we had for Q1 over Q4. The growth will taper off, because once the bonuses start kicking in as per our methodology, the bonuses remain fairly constant, as they are linked to increase in people hire. Thank you Nandan.

Sandeep: Okay. Just one more question on the pricing front. Have we seen the worst of the pricing behind us?

Nandan: I will request Phaneesh to answer that.

Phaneesh: Hi Sandeep, how are you? In terms of the pricing, certainly the cut throat competitive intense pricing pressure which were there in 2001 are behind us. Whether we have seen a bottom? I don't know. I think really the Scott McNeil's statement comes so close to mind, which is only true bottom is my kid's when I am changing his daper kind of stuff. Right? But it is difficult to say, because we thought NASDAQ hit a bottom at some point, it hits further bottom and so on and so forth. So, it is difficult to say whether the bottom has been hit. But certainly, we are not facing any great pricing pressure right now. It is not that intense competitive stuff. Pricing still continues to be competitive, because of surplus capacity and because of overall challenging business environment, but it is not intense and cut throat like it was in 2001.

Sandeep: Thank you.

Lady presenter: Right Sandeep. Thanks for joining us. Next on line, we have got Sujit Sahgal with us, who is Director UBS Warburg. Sujit go ahead.

Sujit: Do you hear me?

Lady presenter: Yes Sujit, we can, loud and clear. Please go ahead.

Sujit: Yeah Hi. Congratulations to the management on a very good quarter this time to see the volume growth. I wanted to actually extend the questions on the margins. What I really wanted to understand was, we have all been all talking about the leverage that companies have with the increasing utilization rates and how that could set off some of the margin pressure. Surprisingly, in spite of 700 basis points improvement in net use rates, margins still have not been able to stay up. Any thoughts you can share with us on that?

Mohandas Pai: Sujit, the margins depend upon the right mix of onsite and offshore. Because the margins on offshore are higher in percentage terms than onsite, even though the per capita net income on both may be similar. So, on the incremental revenues, incremental revenues of approximately $16.5 million ***(Editor comment: $16.62 million)***, we have had 56% coming from onsite and 43.7% coming from offshore. And since the majority of the incremental income is coming from onsite, the margins are less. Now, this has been somewhat set off because of the increase in utilization, we have used up a part of our bench from 72.5% ***(Editor comment: 72.4%)*** to 78.9%. So, this increasing utilization offshore has reduced the impact of the sharp increase in onsite work due to very high projects starts. Projects starts in the quarter one have been the highest in our history and they have been very robust. And that is why you see the impact on the gross margin level, and even though the onsite is higher, at the gross margin level, the margin is impacted by only 1.9%.

Sujit: Okay thanks. The other question was on customer additions. I see that you have announced 23 new customers there, within that I have only seen may be one marqué name of Bear Stearns, can we have a few more quality names that you may have added in the last quarter?

Nandan: I think Sujit, we only give customer names where the customer has given us the permission to announce his name. To that extent, the 23 customers are of very high quality, only the names we give are those who give us permission to use that. So, we cannot really give the names of those who do not give us the permission.

Sujit: Okay, no problem. Thank you very much and once again congratulations to the team. Thanks.

Lady presenter: Right Sujit Sahagal of UBS Warburg. And our next analyst on line, we have got Dipankar Choudhury, Vice President, ICICI Securities. Dipankar good afternoon, go right ahead.

Supratim: Hi this is Supratim, can you hear me?

Lady presenter: Well, we have got Supratim Basu with us. Supratim, go ahead, pose your question to the Infosys management.

Supratim: Good afternoon gentlemen. Congratulations on an excellent quarter. My question actually relates more to the balance sheet side in terms of the cash that you have got on the books. Now, in view of the fact that your SG&A expenses are going up and hence net profits are not growing at the same rate as your top line is. Do you actually foresee a higher pay out in the near future which would actually allow you to keep your ROCE constant?

Mohandas Pai: Supratim, this is an issue which we discuss at every board meeting because we are conscious that we need to maintain or increase our earnings, our return on investment, return on invested capital. Let me assure you that we are seized of this very issue constantly and we keep it on our radar screen.

Supratim: Right thank you.

Lady presenter: Right Supratim, thanks for joining us. Let us move on. We have got Ajay Sharma with us, who has joined us on the line. Ajay Sharma of course joins us from Citigroup; he calls us on line from Singapore. Ajay, please go ahead with your question.

Ajay: Yeah Hi. I have actually two questions for Mohan. Mohan first, can you explain why there has been a sharp increase in unbilled revenues this quarter and whether you really accrue any profits at all on those revenues?

Mohandas Pai: Ajay, we have a sharp increase in unbilled revenues and in unearned revenues too. On both sides of the balance sheet, we have seen an increase. Unbilled revenues because, the percentage of work from fixed price has gone up compared to the previous quarter. There has been a sharp increase in the revenues, so they have been unbilled revenues. Unearned too, because we have billed ahead of the work being done and that has to be allocated to unearned. I think, it is a normal feature as we go along if there is a sharp increase, both sides will go up and the increase in each side obviously depends upon the level of revenues, the kind of billing we do.

Ajay: Right. And could it be one of the reasons for your margin drop, because typically on unbilled revenues you don't make any money right?

Mohandas Pai: No, on unbilled revenues too, as per the accounting standards that we use, particularly US GAAP, we recognize the margins on that part of the unbilled revenue which has taken credit of. So, I don't think you can attribute this to that.

Ajay: Right. And second question on, in terms of your margins, how do you see the next three quarters shaping up? Should we expect any improvement compared to the first quarter or should we expect almost flattish sort of margins?

Mohandas Pai: Ajay, let me explain this margin impact. First of all at the gross profit level, the margin has come down by 1.9%; because of the incremental revenue we have had more onsite work. Typically, we have onsite work in the ratio of 35% to 65%, may be 32% to 68%. But for the incremental revenue of $16.62 million, we have had 56.3% of onsite work because of higher projects starts on account of greater business. So, obviously when it comes back to normal, at the gross profit level you will find margins in the same range as earlier. As far the SG&A cost goes, there has been a hump this quarter basically because of the fact that we had to provide for bonuses to the sales staff, which bonus was not there in the last quarter because no bonus was due at that point of time, and we also spent $1 million more on brand building this quarter vis-a-vis the previous quarter. We do not see the SG&A increasing by 2% every quarter, QOQ, the growth will taper off, because the bonus is calculated on the expected value of the basic payments made, and it can only grow up in case we add on more people or the revenues grows up at a much much faster pace. So, I think going forward with a shift to a more normal onsite offshore ratio and with a greater revenue you will find that there is some scope for margin improvement.

Ajay: Okay, thank you very much.

Lady presenter: And moving on now from Singapore to Hong Kong, where we have got Mitali Ghosh calling in, Mitali is of course from Merrill Lynch. Mitali, good afternoon, go right ahead.

Mitali: yeah Hi. Congratulations on the strong volume growth that you have shown this quarter. Just going forward on this, you know the sales cost that you have had additionally this quarter. When you say brand building cost, just trying to understand what sort of cost were those involved?

Phaneesh: Mitali you know one of the big initiatives and campaigns which we did was this Wharton Infosys Business Transformation Award, which is a tie-up between the Wharton Business School and Infosys to recognize companies who have transformed themselves the most dramatically using technology. So that has given us a lot of awareness in the areas that we want to be known in, you know, CXO mind set, where we now associate us with business transformation using technology and stuff like that. So, that was the fairly large campaign, we spent a fair amount of money on that. Parallely, we continued to conduct various thought leadership initiatives. So, in the last quarter, for example, we did two major seminars on lead time optimization as a better earning strategy for retail companies than better forecasting. So, this was done with a Stanford Professor and so on and so forth. So, what we are trying to do is that we take these thought leadership kind of activities and we run seminars on these, and that is helping us get visibility in the right places, that is helping us connect with the business crowd.

Mitali: Right. And my second question is in terms of the new service lines which you have been focussing on, things like application outsourcing, systems integration, etc. Can you tell us a bit more about how things are shaping up there?

Nandan: I will request Shibulal, Head of Customer Delivery, to answer that.

Shibulal: In line with the philosophy of increasing the depth and breadth of our services, we have added a number of services over the last three years. Now in the last three years we had added consulting as a major services, high end testing, engineering service, as well as enterprise solutions. And today, in fact in this quarter we derived 19% of revenue from these new services, which we added in the last three years. Now the new services, which we have looked at in the last two quarters, IT outsourcing as well as the system integration, are in a pilot stage. If we look at the services, when we add a service, we go through a four stage service roll out, which starts with conceptualizing the service, going on to pilot, then redefining the service, and then rolling it out based on the inputs in the pilot. The services like IT outsourcing and system integration both are in the pilot stage.

Mitali: Right. And my last question is just on the impact of the Indo-Pak tensions that you have seen. How would you see that spanning out over the next, you know going forward over the next two-three quarters? And what cost can that involve in terms of business continuity plan?

Lady presenter: We have had a bit of a problem with our line there, with Bangalore. We have just lost connections for a bit. Mitali, are you still there with us on the line?

Mitali: Yes.

Lady presenter: Yes Mitali, what was your question that you would have liked to pose to the management?

Mitali: Yes. I wanted to know what is impact of the Indo-Pak tension that we had and how would they see that translating into cost over business continuity planning?

Lady presenter: Right. Well, we would love to have posed that question to the Infosys management. Mitali, if you could just stay with us a bit. You know we have lost connection with Bangalore. We are having a bit of a trouble with the lines. Just stay with us a bit Mitali. Well, if we could just recap on the Infosys results for you once again, we got a net profit, which of course rose by over 14% to Rs. 217 crores, year on year, and of course sequentially we have an up movement of little over 3%. Let us get to those total income figures, which had surprised every one. Income from operations up nearly 25%, at Rs. 765 crore, and QOQ that translated into a growth of 12.5%, 765 that was a number which did surprise the street. Let us take a look at the guidance that Infosys had come out with, Q2 guidance. The company has given a revenue range of between Rs. 762 and Rs. 782 crore ***(Editor comment: Rs. 781 crore)***, which translates into a range of between either –0.39% or about 2.22%. Net profit, as you can see, Rs. 218 to Rs. 225 crores, that was the guidance for the Q2. And moving on from there, it also revised its guidance for the full year. Let us give you those numbers. Of course on the back of that strong volume growth that it has seen in the Q1, it says that it expects revenues to be in the range of Rs. 3108 crores to Rs. 3195 crores. As per net profit, over the full year, is now expected to lie between Rs. 940 and Rs. 966 crores. So, the question is, what does Infosys have to do to meet these numbers? Well, to meet its revenue estimates it needs revenues to grow by about 1.35% sequentially, that is across the third and the fourth quarters, provided it meets the second quarter guidance it is given out. Net profits though will have to grow by about 10% sequentially to meet its full year guidance. And of course the recent travel advisories, that was the question that Mitali had, Mitali Ghosh of DSP Merrill Lynch, for the management, and it did say the management's point of view was that things still looked cautious, they maintain the cautious outlook given the possibility of further events which is going to cause the overall economic situation, both in India as well as overseas especially.

Well, let us get back to Infosys, and tell you about the volume story there, which have gone up by 12.5% in the Q1, this is a substantial increase and the company says it is all thanks to a ramp up from existing clients. And of course, challenging market conditions has meant that Infosys has had to spend more on selling and marketing expenses, that is the point that a lot of people have been raising through the morning, that is in order to get those fresh order wins and that is expenditure incurred under this category has increased to more than Rs. 55 crore from Rs. 35 crore in the Q4, a trend that Infosys says will be maintained in the coming quarters. Of course, selling and marketing expenses that was one of the points. But let us tell you about the good news on pricing front, which of course has enthused a lot of people there. Prices, the Infosys management says, may have stabilized; in fact we have seen prices for the Q1 have fallen by just 0.6%. So, we have got a good volume growth story continuing and prices are showing signs of stabilization. Well, BPO or BPM rather, as Infosys calls it, their Progeon, that is their BPM unit. Well, it did see financial closure during the quarter with the funding of course coming in from Citicorp as well as Infosys. And Progeon did add two clients, with the latest win being Greenpoint Mortgage System; this will yield over $30 million over the next five years. And of course Progeon did record revenues of Rs. 21 lakhs, but the travel advisories, according to Infosys, have had a deeper impact on Progeon than the other sides of their business as they told us this morning. Well, despite the volume growth Infosys has seen a drop in the number of new client additions. While it continues to be cautious about fresh client wins, Infosys is optimistic about the ramp up from existing clients.

Gopalakrishnan: We see new clients added this quarter. It is lower than last quarter actually. So, we are cautious about it. The existing clients have been reassured. We had conference calls with them and we were able to reassure them.

Lady presenter: Of course getting back to prices. As we told you there is good news, there is good news on that front, which prices Infosys feels are stabilizing after those six turbulent quarters. In the Q1 alone prices fell by just 0.6%.

Phaneesh: Prices have stabilized and given the fact that we are competing more and more on the consulting led engagements, given the fact that we are competing more with the bigger players, the big 4 the big 5 etc. From our perspective, we do see a potential for, you know, the bias is more on the positive side for the revenue productivity growth on the pricing front.

Lady presenter: Well, we also asked Phaneesh Murthy this morning about Progeon as we were telling you it did see financial closure though, as Phaneesh told us, Progeon was harder hit from those travel advisories and this is exactly what he had to say on the matter.

Phaneesh: Progeon may have got impacted a little more because of the June travel advisory, because in business processing, I think is a little more sensitive to conditions around the world.

Lady presenter: But let us just tell you what happened during our board room direct this morning, when we had spoken to the whole management, which included Nandan, Kris, and Mohandas Pai. And of course Udayan began by asking where the volume growth was coming from.

Nandan: I think there is a lot of interest in offshore, and we have been seeing a number of metrics that show that the volume growth has been going up. New projects starts have gone up, utilization has gone up, the number of people going onsite has gone up to start these projects. So, I think there is definitely in this market where people want high quality, high value for money, reliable execution. I think the outsourcing story, and they are also looking at companies like Infosys, which are very strong, very stable, very financially strong and well-known brands. So, I think all this has contributed to the volume growth for this quarter.

Udayan: Has there been a ramp up from existing clients which has lead to this growth or is it the addition of new clients where you have got large orders which has lead to this?

Nandan: No, I would say the bulk of it is really from existing clients. Normally, in the Q1 we have existing business from the existing clients. So I would say that is the bulk of it.

Udayan: Kris, which segment of clients have really ramped up? Are these the ones which came in four to five quarters back, which are now ramped up or are these your top 5, top 10 big clients?

Gopalakrishnan: See, the clients would rotate within the top 5 also. So, as a percentage among the top 5, the percentages have not varied but there has been some changes in the top few clients. But the growth really has come from the clients which have been added over the last few quarters, and we have had a very good year last year about the number of clients which have been added and the growth has come from some of those clients actually really ramping up in this quarter.

Udayan: Mohan, the only disturbing point if one might point out from these results as such is, your top line has grown substantially, there has been pressure on margins, the SG&A expenses have gone up substantially. Are you worried about cost getting out of hand right now or is it a deliberate strategy that you need to spend….?

Lady presenter: Well, that was an earlier discussion with the Infosys management on Boardroom, but today we are giving you for the first time ever a look in to the Earnings Call. We had analysts waiting on the line, Mitali has been with us. Mitali Ghosh of DSP Merrill Lynch has been waiting for a while. Mitali why don't you go ahead and ask your question there to Infosys?

Mitali: My question was on business continuity plan and what sort of capital expenditure that could involve?

Nandan: I think, let me just explain some of implications of the plan of the what happened last month. We did not have any impact last month either on revenues or on costs. We only had an impact in terms of visitors from customers and prospects, and we feel the lingering impact of the lack of those visits will surface a little later, which is why we have been cautious in our outlook. So far there has been no capital expenditure on that front, but I will ask my colleague Kris to speak about specific plans for disaster recovery and the potential capital expenses related to that.

Gopalakrishnan: See, Infosys has a robust disaster recovery plan focused on India and to some extent moving people onsite at customer locations and our development centers in US, Canada and other parts of the world. Now, this has focussed our attention on looking at a location similar to India outside India, one or more locations. So, we are in the process of identifying which locations and if need be investing in setting up a facility, which will act as a back up for India. We hope to do this in the near future. There will be some investment from the capital investment side. Mostly these locations will be staffed only when a disaster occurs, so the revenue expenses will probably happen if a disaster indeed occurs.

Nandan: We do not have an exact budget for that, but as and when it unveils we will be able to share that with you.

Mitali: Sure thanks.

Lady presenter: Thanks Mitali for staying on the line. Let us go across now to Credit Suisse First Boston where we have got joining us on the line from there Ashis Kumar, Director and head of technology research. Ashis?

Ashis: Yeah Hi. Thank you so much. First of all heartiest congratulations to Infosys management. If you could explain my first question, in the past the muted sequential growth used to be because your large customers, some of them well known, were slowing down and you had new customer just about ramping. Now, the negative effect is almost getting over and you had a very strong quarter in terms of top-line QOQ growth. Why is it guidance muted? What is holding it back?

Nandan: I think, our guidance is cautious for two reasons. One is, we had complete cancellation of visits by both customers and prospects in the month of June and as you know yesterday's visitor is tomorrow's customer, and therefore we are anticipating that that will have some repercussions down the road on the subsequent quarters. The second is, we believe the economic environment continues to be challenging. People have not yet declared that the economy is out of the woods. These were the two reasons why we continued to be cautious and hence we have not revised our estimates for the year.

Ashis: And Sir, you are continuing on that as Mr. Mohandas Pai sort of suggested that that margin indeed could improve. So the buyers on even the guidance could be positive because you are assuming the economy remains weak and customers don't come, but usually your earlier customers contribute most of the growth. So, should it be taken as the typical Infosys approach that let us be conservative and let us beat numbers?

Nandan: No I think you know we have really taken a look at our business and we have looked at these external macro-economic and external conditions and having looked at all that we have come to the conclusion that this is not the time for us to revise our estimates.

Ashis: And Sir, continuing on that, you know you gave certain guidance for the June quarter and nicely beat the numbers very handsomely. What happened? What were the positive things that you did not perhaps see or were careful about and happened?

Nandan: I think, not withstanding the IT slowdown, it is very clear to us that offshore is becoming more and more mainstream. We have been saying that even in earlier conversations, and I think a lot of companies after a long time of not taking any decisions have now realized that they have to get on with it and take some decisions. So, I think the combination of more decision making at customer locations, our own infield investment in sales and marketing which has got us more and more projects, not just in new customers but also in existing customers, and the fact that outsourcing and offshoring has become mainstream. I think all these have contributed to the robust revenue growth for Q1.

Ashis: My last question to you Sir is, do you expect sales as a percentage of revenues, sales expenses as a percentage of revenue to stabilize at the current levels? So, in other words Infosys is accepting that as it becomes big, does more consulting, does more onsite work, it has to accept a lower margin though a higher top-line growth.

Nandan: Mohan explained that the margin is also a function of the onsite offshore mix, and this particular quarter the onsite content was much higher and therefore if that mix changes that also has implications on the net profits. Having said that, yes I think the sales and marketing expenses have to be more as we have done in this quarter and we expect it to stabilize around that level.

Ashis: Sure Sir. Thank you very much. That is all I have to ask. Thank you.

Nandan: Thank you.

Lady presenter: Well, from Singapore let us head right back to Mumbai. We have got a followup question coming in from ICICI Securities. You are online, please go ahead.

Supratim: I just want to go back to something that Phaneesh actually said in the morning call, which is that prices have stabilized and besides that he also said that they are facing competition from the big 5 and sometime you get pricing from the big 5 which is lower than what Infosys is quoting. Now, in such a situation if you say pricing is stabilizing, does that mean that we are seeing competition from the big 5 actually slackening because of the financial implications for their balance sheet or is it just that the demand-supply gap is becoming more favorable?

Phaneesh: See when I say the pricing intensity is stabilizing, really what I am talking about is with our base. So, see typically when we compete with the big 5, IBM, etc., the pricing base is a little different from the other India based competition that we compete within some customers. So, for us, even if we are competing aggressively on price with the big 5, we are still very comfortably placed on the price and we are really comfortably placed on the margins that we can make on that price. So, that is really what I was trying to say that. As more and more accounts come and as more and more projects we are competing with those players, it is better for us and it is more stable for us.

Supratim: Okay actually, if I could just expand on that what I meant to ask was that in the past Infosys has told us that the big 5 have started cross-subsidizing some of their assignments in which they compete with the Indian companies. Now, you are also saying that you are seeing, I mean, and that with your cost base per se. So, are you basically seeing a lessening in that sort of pricing competition from the big 5?

Phaneesh: Yeah. I think certainly with the fact that the markets have stabilized a little; we are not seeing very aggressive cross-subsidization. We are seeing very clearly that they are keen to build revenues. We are seeing very aggressive competition, you know two or three anecdotes, you know in one account like I said in the morning, they had gone and made a blanket offer that whatever Infosys quotes, mine is $250,000 for that project. Another account where we got news that they had quoted that…, you know, they knew that the customer was doing work with Infosys and they came and they said that we will do the work at 10% cheaper than Infosys regardless of what Infosys has quoted kind of stuff. There are some anecdotal evidences like that, which indicate that they are really trying to beef up their so called global delivery operations, but…, otherwise we are not seeing that the intense pricing pressure which was there in the January to December where customers were coming back and renegotiating contracts just based on their own positions and what they were making in terms of profits and what the pressures they were getting from their CEOs. We are not seeing that happening in 2002.

Supratim: Alright, I understand. One final question on the selling cost side, which is that are you actually hiring more expensive sales people, account management people with their own relationships now, compared to what you were doing say 6 months back and 12 months back?

Phaneesh: It is reasonable to say that we are trying to take the profile of everybody up in Infosys right time. As we compete in a more global economy, hiring of more global talent, hiring of people who come in with a *(audio blackout).*

Supratim: Hello. Can you hear me?

Lady presenter: Yes, Supratim, actually we can hear you very well, but we have once again lost Bangalore for a bit; actually we have not lost Bangalore, let us go right back. Supratim we will let Phaneesh continue with his answer. Phaneesh, please continue.

Phaneesh: As we become larger, we are becoming more global and you know our hiring is becoming more global and including hiring people who come with a rolodex of their own.

Dipankar Choudhury: Just one last question. What is the realistic level of utilization you can go far upto? When does it become difficult to operate?

Shibulal: Our goal for utilization is upper 70s low 80s. I mean in the last quarter we have seen considerable increase in the utilization. We have gone from about 72.2 ***(Editor comment: 72.4%)*** to about 78.9 utilization. But our goal is upper 70s and low 80s.

Dipankar Choudhury: Right. Thank you very much.

Lady presenter: Thank you Dipankar. And Supratim, well Saurabh from Alchemy joining us from Mumbai. Saurabh what is your question?

Saurabh: Yeah Hi. I mean in the past we have seen package implementation business showing decent growth, but this quarter there has been a 20% sequential decline. What were the main reasons and what is your view going forward?

Gopalakrishnan: See it is also a function of the type of projects we are doing, whether it is onsite offshore and things like that. In package implementation we have maintenance as a service also. So, it is a function of those things also. The service is actually growing.

Saurabh: Okay. But like going forward, if you are still bullish in package implementation, will it mean an increase in onsite component further because of it?

Gopalakrishnan: Package implementation services are more onsite oriented than let us say the development or maintenance service.

Saurabh: Right. So, this quarter itself we had high onsite business, then going forward you are expecting an expansion in margin mainly because of increase in offshore. So, would this package implementation a higher growth in it would be a bane to it?

Nandan: No I think, let us separate two things. There are certain services like consulting and package implementation, which have the likelihood of having higher onsite content and that is a attribute of the property of that service. However, the last quarter the increase in onsite content is really because over the last few months we have had a lot of new projects starts, and when we have these projects starts we have to send people onsite to meet with the customer, understand the requirements and then bring those requirements back for build and test in India. So, to some extent the onsite going up is not so much service mix, but because of the large number of projects starts that have happened this quarter.

Saurabh: Yeah, I mean because of the entire thing is that in terms of how would margin go forward. Because this quarter you had the benefit of improvement in utilization, which partially mitigated the expansion in onsite mix. I mean going forward, you would not have this but if even the other areas mitigate the expansion in onsite because of starts of projects, the margins will still be under pressure.

Mohandas Pai: I think, in the next quarters what we should see is the onsite ratio should go up the SG&A expenditure will not rise in the same manner that it has risen this quarter. For example, sequentially SG&A has gone up by about 30%, next quarter it is not going to go up sequentially by 30%, and that is for sure.

Saurabh: Okay, but like can we say this quarter was the worst margin? Because see next quarter you are expecting a flat 4% growth in EPS but subsequent year you are expecting 10% growth in EPS, where as your sales is growing by only 1% to 2% in the next three quarters, according to your guidance. So, can we say that this is the worst quarter in terms of the margins?

Mohandas Pai: Well, I cannot make a categorical statement whether this is the worst quarter in terms of margin going forward, because we cannot read the future with such a certainty.

Saurabh: Yeah, I am lining with what you are saying of your guidance.

Mohandas Pai: Based upon what we have worked out and our budgeting I could say that, one, we expect offshore to become more or the onsite offshore ratio to stabilize for the next two quarters, two the growth that we have seen in SG&A this quarter over the previous quarter will not be there in the subsequent quarters. The growth will be very much muted.

Lady presenter: Right Saurabh thanks so much for joining us this afternoon. Let us go across now to UTI Securities from Mumbai. We have got calling in Jaideep Goswami. Jaideep, good to hear from you, what is your question?

Jaideep: Hi, congrats for a great result. I just wanted to know; recently Infosys has announced a strategic tie-up with Concours, the management consulting firm. Just wanted to know what is the game plan, how this relationship is going to evolve over say next one year and what is the game plan about Infosys strengthening its position in the consulting space. How this tie-up will help?

Phaneesh: Concours is a boutique consulting company. They have extremely senior and experienced consultants with a high number of years of experience or whatever metric you want to take. We have actually been wanting to expand our consulting offering, in consulting presence to include a lot more of change management programs, strategic consulting, and executive relationships. Concours has all of these three. The objective of alliance with the Concours is to be able to use them in consulting projects that we can get from our existing customers so that we can offer more strategic consulting, to use them in change management programs and to use their executive relationships and to use the downstream and to get Infosys revenues from the downstream of the consulting engagements that they are doing with their customers. So, the alliance is actually intended to help both of us over the next 12 months or so or longer term.

Lady presenter: Well Jaideep thanks so much. Actually we are completely running out of time. We have got a lot of questions from analysts. Chetan, you have got about 10 seconds to ask your question. Go ahead. Quickly ask one question to Infosys management there.

Chetan: (audio blackout) of $7.7 million, does it include Autolay also?

Mohandas Pai: $7.7 million under US GAAP is a normal capital expenditure. If you go down the line in the cash flow you will find another item of about $2.9 million and that is for the IQ, but there is no item there for the Autolay because Autolay has not been paid. It will be payable over the next 10 years.

Chetan: Okay. And how does the I mean Infosys has presence in the banking products segment and the addition of the product in the engineering services side; I mean what is the game plan there?

Gopalakrishnan: Autolay is a product for composite design and things like that which can be used in the aeronautical as well as in the automobile sector. Infosys has an engineering service practice which is focussed on these services. So, we believe that this will help us gain more customers and more revenues from these sectors.

Chetan: Thank you Sir.

Nandan: We had Finacle™, which was very strong retail commercial corporate and internet banking product, and recently we added to that a CRM product, and the piece that was missing in our offering was a treasury product and that is what we got from the IQ trade purchase.

Lady presenter: Nandan, you have got another question coming in. This time Bhuvanesh from Credit Suisse First Boston called us from the lines in Mumbai. Bhuvanesh, what is your question?

Bhuvanesh: Hello.

Lady presenter: Yes Bhuvanesh, go right ahead.

Bhuvanesh: Sir, my query basically comes from the decrease in the margins. I think, Ashis also asked it. What I want to understand this increase in sales as a percentage of revenues by about 2%, should we take it as constant that sales expenses would remain as that high or should we take that they would go back to the previous level of say previous quarters?

Mohandas Pai: I think you could say with some amount of certainty that in case revenues were to go up let us say $5 million, the total SG&A on that incremental $5 million could be within 15%. Please remember, this quarter under Indian GAAP we have seen a 29.7% sequential increase, a large part of it will be sort of one time because of the fact that bonus kicked in this quarter, last quarter there is no bonus. In future, we are going to be in steady state. So, you are not going to have a 29% increase in SG&A next quarter too, what you will have is an incremental revenue, may be a 15% of it will go towards SG&A.

Lady presenter: Right Bhuvanesh. Thanks so much for joining us. And we would just like to inform all of you watching that to make up for the time we lost, when we lost the signal to Bangalore, we are extending Earnings Call by another 15 minutes, so it is now going to end at 03:15 and not at 3 o'clock as earlier. So, we are extending it by another 15 minutes. Let us continue with our Earnings Call. Our next analyst on line, still in Mumbai, is Nikunj Doshi from REFCO-Sify. Nikunj, good afternoon, go right ahead.

Nikunj: Yeah, good afternoon everyone. I just wanted to know this; we have been saying that telecom business is facing slowdown, but if we look at the percentage of revenue from telecom sector I believe it is stabilizing around 15.2% to 15.3%. And as well as in absolute term, telecom revenue has gone up during this quarter on sequential basis. So, what is your call on telecom sector going forward?

Phaneesh: You know if you look at the telecom sector, it is really made up for us of three components, the large equipment manufacturers, which are like the Nortel, Lucent, Cisco, Ericson, Nokia, etc. The smaller companies who were venture funded who wanted to come out with new products and cutting edge products either on the software or on the switch up router side. And in the third is the service providers, you know the people likeVerizon, AT&T, Telestra, Belgacom etc., who need services. On the equipment manufacturer's side, I think with all of the ravaging that they went through in 2001, we think that with the capital expenditure still coming down, overall in the market place, there will be still some shake out left. But from our perspective we have kind of stabilized there. So, we are not seeing too much movement either way. On the small company side, that came down to almost zero or very close to zero over the last year anyway, because the venture funding got cut off. The service provider side on the other hand is going through some dramatic restructuring, rationalizations, and they want to change their cost structure more dramatically. They also have to offer much better customer service, automated auto provisioning and so on and so forth. So, for those a whole of host of new services and investments have to be gone through, which are helping them reduce their cost of operations and we have been getting a lot of wins in that space. So, when you look at the telecom it is not really one segment, it is a composition of these three and within the three different segments make up at the time when the other segments are slower.

Nikunj: Okay. And, on the currency front, have you assumed any currency rupee depreciation vis-à-vis dollar in our projections in guidance? Or we have assumed the current rate of rupee-dollar?

Mohandas Pai: Current rate of rupee-dollar for the rupee figures, and that is why you find a increase in rupee figures. The increase in the rupee figures is not because of any increase in revenues, but because of the currency issue. If you look at the dollar figure, the dollar figures for guidance remain the same.

Nikunj: So that means you have assumed some kind of a depreciation of rupee!

Mohandas Pai: No, we have not assumed any kind of depreciation in rupee. We have taken the rupee rate as on 30$^{th}$ of June.

Nikunj: Okay. But in case it appreciates, which is likely to happen, we may see a kind of negative.

Mohandas Pai: Well, in case it appreciates, we do have some forward cover and we are looking at this issue on a regular basis. To the extent of the forward cover any appreciation will be muted, but if it continues after that, we certainly will see some impact on the P&L.

Nikunj: Okay. And can we get billing rates in absolute numbers for onsite as well as offshore?

Mohandas Pai: Well, let me give you the billing rates for…, revenue productivity. In this quarter, the billing rate has been for onsite, revenue productivity has been for onsite, $10,864 and offshore $4,721 per month. In terms of annual figures, it is about $130,400 onsite per year and offshore is $56,700.

Nikunj: Okay, thank you very much.

Lady presenter: We do indeed have Mahesh Vaze of Motilal Oswal Securities. Mahesh are you there?

Mahesh: Yeah, could you hear me?

Lady presenter: Great! Yes, please go ahead.

Mahesh: I just wanted to understand whether Infosys is planning some kind of salary rise, because some of the competition has given salary raise recently and the recruitment seems to have picked up. So, is Infosys is also contemplating some salary rise?

Nandan: I will request Dinesh to answer that.

Dinesh: We are planning to increase the compensation for the employees and this increase will be variable and it will be linked to the performance of the company as well as to the performance of the individual. So, once again we want to reinforce the high performance work culture that we are trying to build and as part of this we are going to increase the salaries only as a variable part.

Mahesh: And that would happen this quarter Sir? Hello.

Lady presenter: Yes Sir. Dinesh could you please go ahead?

Dinesh: yeah, it will be planned this quarter.

Mahesh: See the second thing I wanted to know was, one of the things you have said is that gross margins are down because of higher onsite component. But according to my numbers, onsite as proportion of revenue has gone up from something like 52.2% to 52.7%. Are the numbers correct?

Gopalakrishnan: The onsite has gone from 52.2% to 52.7% from last quarter to this quarter.

Nandan: I think the key is to look at the incremental effort man-months. The typical ratio is 2:1. That is for every one man-month of effort done onsite we have 2 man-months of effort offshore, but if you look at the incremental man-months of this quarter, the ratio is 1:1.2, that is for every one month of effort onsite there is only 1.2 man-months of effort offshore. And hence the incremental man-months this quarter has been skewed more towards onsite.

Mahesh: My last question is what is the kind of capex that Infosys plans to have for FY03? Thanks a lot.

Mohandas Pai: We have said that we will spend about $45 million on capex, excluding any acquisition that we make of any intangible property. We have spent about Rs. 39.7 crores in the first quarter of this year, as against a total budget of about $45 million.

Mahesh: Okay, thanks.

Lady presenter: Trideep are you there with us?

Trideep: Hello, can you hear me?

Lady presenter: Great Trideep, go ahead, ask your question.

Trideep: Yeah thanks, finally we made it. First of all, congratulations to the management. My question is regarding the existing client ramp ups. Now, if I look at two external variables, one is Indo-Pak war issue, and other is status of the US economy. Since, existing clients have been working for, I mean, have been working with you for the last more than one year, so I believe that the customer visit issue should not impact too much of that. Having said that, then the volume growth that you have experienced this quarter of 12.5%, how do you see this sustaining over a period of.., over the next three quarters in the light of the external variables, and what could impact that?

Phaneesh: Let me take a shot at it. The first part, in terms of, you know, existing clients, in the last 6 to 12 months we have added very marqué names. These marqué names actually in 2001 just took options on the future I think in terms of how to, you know, do strategic sourcing from India. How to include India in the strategic arsenal and stuff like that. They did small pilot projects. What has happened is that, these accounts and of course, you know, the other accounts that we have had in the past, once the budget seasons have cleared, most companies in the US budget on January to December cycle. Europe and Asia, is more on April to March cycle. So, if you take bulk of our revenue, which comes from the US, on a January cycle, the budgets are released. People have started getting used to the environment. They have started making the decisions. February and March, you start getting the decisions, and then you basically start doing the initial scoping and then you do the bigger requirements projects, which hopefully will go out into more downstream as we go down. So, the concern on the Indo-Pak side, you are right. With existing customers, it is significantly less, primarily because they are already engaged with us and they are in touch with us, and they already have a record of the fact that we are doing a great job with them. The impact of prospects, impact of you know the June, whatever happened in June, if at all, will actually be felt down the line. That is one of the reasons why we said, you know, in terms of…, although the volume growth has been very robust, you know, it has been 5 or 6 quarters since we saw a double digit volume growth of this kind. While the volume growth has been very robust, because we cannot predict how long this June sentiment is going to last, how long the travel advisory is going to last, and because of the overall general weakness in the economy around the world, we have thought it prudent to retain our guidance as what we had done in April. We have not changed that estimate.

Trideep: Okay. Could you give the price and the volume split for the September quarter guidance that you have provided us Sir?

Mohandas Pai: Well I think the September quarter guidance is relatively flat, $156 to 160 million as against $156 achieved. So I think, you know, for the purpose of the guidance we assume the same kind of a mix for the September guidance.

Trideep: Okay. Thanks a lot.

Lady presenter: Thanks Trideep for being on the line with us. Next on line is Amit Khurana of Birla Sunlife. He calls us from Mumbai. Amit, hi, go ahead with your question.

Amit: Phaneesh, just one thing to start off with. We have seen the development work picking up in the current quarter; I think this is about four quarters, after 5 odd quarters, when we are seeing development work picking up. Is there some signal, which indicates that we are probably on an up trend and, you know, one could take a call that there is a reversal in sort of the trend as such?

Phaneesh: I think it is, you are right. You know, the development work is a direct function of IT spending and decisions being made. So if the initiatives are being funded, essentially if you are doing a supply chain initiative, you have SI and development work which goes with that, a new supply chain. If you are doing a new CRM program in terms of revenue enhancement, then effectively you have package selection, package implementation and development work which goes along with that and integration work. So, it is certainly a function of the fact, I think, that people are starting to make decisions. That has been the biggest turnaround. The decisions are being made. Right now, people have got used to this economy. People have got used to these conditions, and the fact that development work has been going up is really a function of that, of the decisions being made.

Amit: Okay. Which brings me to the second issue, would you say that the muted guidance that we are putting out for Q2, kind of, had certain amount of preponement of such development work, or any such engagement which has got reflected in Q1 numbers and that is why you are trying to be muted for Q2 numbers.

Phaneesh: No, nothing like that.

Amit: Okay. The second issue was in terms of the opportunities that we see especially on healthcare, and we had kind of discussed HIPAA earlier, and certain plans on Western government or the US government talking about spending on technology, do you foresee some opportunities there, let us say another three or four quarters down the line?

Phaneesh: We have, recently, I think, one of the things that we have done is that we have beefed up our healthcare group. We have had a new VP, who is an Ex-CIO from a health plan. So, he is putting together a new business plan for healthcare. So, hopefully, we will be able to get more visibility into the kind of services that we will be able to offer in the healthcare and consequently better revenue visibility. We of course have one or two very large customers in healthcare already as you probably know.

Lady presenter: Amit, unfortunately we will have to leave it at that. We have got a lot of callers waiting on line. Thanks so much for joining us. Lakshmikanth Reddy from ABN Amro joins us next. Lakshmikanth, we have got time for one question, please go ahead.

Lakshmikanth: Well hi. Thanks a lot. Just one question. Could I have the break up of your revenues in terms of your various denominations and currencies, I know, we have the geographic break up, but if you have to give us the breakup in terms of, you know, dollars, euros, yens, etc.., what would that look like?

Mohandas Pai: Lakshmikanth, I don't have the exact figures, but let me give you what we could have for the last 12 months, 90% will be in dollars, about 3.5% will be in euros, about 3.5% will be in British pounds, and may be about 1.5% will be in yen.

Lakshmikanth: Okay. Thanks a lot.

Lady presenter: Thanks Lakshmikanth. We have got Shyam Bhat on the line. Shyam Bhat from Tata Mutual Fund. Shyam go ahead, we have got time for one question.

Shyam Bhat: Yeah. Good afternoon to all. Could you please elaborate on the plans that you have for Progeon in terms of Capex that you have lined up for Progeon over the next two years, and whether you see breaking even in this year, and also if you could elaborate on the opportunities in the BPO space, particularly in the aftermath of the border tensions.

Phaneesh: Progeon, the good news about Progeon, it is being privately held, hopefully, we don't have to give all this information out to everybody, right? So, we want to take a little bit of.., we want to just reflect in that for a few quarters. But, you know, on a more serious note, we are increasing the space. We have taken capacity now for almost a 1000 plus seats in Bangalore. We have already implemented a number of the workstations, you know, the switches and so on and so forth, which have already been put in place.

Shyam Bhat: Could you elaborate on the general opportunities in the BPO space as far as India is concerned.

Phaneesh: Yeah. I think, this whole globalization of services, which is happening today, you know, is a fantastic trend. If you look at what happened to manufacturing, hi-tech manufacturing etc over the last 20-30 years, that is exactly what is happening today in services. Services are getting globalized so dramatically that it is, you know, it is really a huge opportunity for multiple countries to pick up their economies, and certainly we hope that India is one such country which will pick up its economy based on the amount of servicing which will get outsourced globally. We are finding that there will be multiple back office kind of hubs or services kind of hubs around the world, and India is well placed to be one of those servicing hubs for the rest of the world. So, I would say that, you know, from multiple perspectives, the earlier BPO work, as it was called, you know, used to be just primarily low-end call center work. I think, with the movement of more credible players and stronger players, we are looking at really business process management which is more business process re-engineering, business process optimization, and back office shared service centers, common platform based outsourcing and so on. Much, much more sophisticated in the way things have to be done. So, I think, there are huge opportunities, we are only scratching the surface.

Lady presenter: Shyam, thanks so much for joining us. Let's get a quick question in from Dipan Mehta of Dipan Mehta Shares and Brokers. Dipan, go ahead.

Dipan Mehta: Yeah, thanks. Congratulations on the excellent results. Just a short question, has there been any change in the composition of the top 5 clients and the top 10 clients, any new entrance this quarter compared to last quarter.

Gopalakrishnan: We always have some movement between these clients.

Dipan Mehta: Can you tell me any new in the top 5 club Sir.

Gopalakrishnan: No we cannot give you any names of these clients.

Dipan Mehta: Not name Sir, number? Whether one new client has come in the top 5 in place of another and same for the top 10.

Gopalakrishnan: No, not at this point.

Dipan Mehta: Right Sir. Thank you.

Lady presenter: Bye Dipan, thanks. Time now for Shekar Singh to ask his question. Shekar Singh from DSP Merrill Lynch. Go ahead.

Vijay Bhayani: Hi. This is Vijay Bhayani from DSP Merrill Lynch. I have a question on this travel advisory, based on our interaction with a couple of industry sources, we are getting signals that probably the US government is consciously delaying the decision, considering that any slower offshore shift could help them stagger the layoff situation in the US. I would like to have your views on, you know, why the travel advisory has not been removed so far.

Nandan: I think we can speculate on why they are not being removed. All we can say is that the travel advisory has had an impact on us, and now since they are being lifted, we are seeing a trickle of visitors, but we really can't speculate on the motives behind the travel advisory.

Vijay Bhayani: No, industry participants are admitting that in case the situation continues for long time for some more, couple of months, then it can have a severe impact on the long term growth prospects for the Indian sector, so that is the main concern we have.

Nandan: I think there are two things, one is of course, you know, as a country we will have to project why we are a very safe place to work, and also as companies like Infosys we have to have a comprehensive global business continuity plan to give comfort to our customers that we can continue to service them even in the event of any dislocation in India, which is what we are trying to do. But I do believe that India will continue to be a very attractive place for software services and for BPO, and we hope that things will continue as usual.

Lady presenter: Vijay Bhayani thanks so much for joining us this afternoon. Anantha Narayan from Morgan Stanley, are you there with us? Do you have a question?

Anantha Narayan: Yes I do. Thank you. Good afternoon everyone. I have two questions actually for Mohan, and Mohan sorry to just keep on hopping on this margin issue. My first question was, is it possible to get a feel of how offshore and on-site gross margins have moved individually this quarter versus last quarter.

Mohandas Pai: Yes, I think, Anantha you can know this by just looking at the mix and looking at the incremental revenue. For example, in the fourth quarter, we had on-site effort of 31.2%, offshore 68.8%, and revenues of 52.2 and 47.8. For the incremental business, we had on-site effort of 45.1 and offshore of 54.9. And in terms of revenue, on-site has been 56.3 and offshore has been 43.7. And you will appreciate that on-site revenues per capita has come down by 2.6% and offshore has gone up, and the difference between the on-site and offshore is really, is slightly, is about 2.3:1. If you factor all that in, you will be able to work out the impact.

Anantha Narayan: Okay. I will try that out. My second question was, when you last spoke after the March quarter results, the general idea was that margins will be more or less stable, and you gave, you know, three reasons why there has been some pressure on margins. Now, I would have thought that all the three reasons would have been visible at that point of time, has anything changed significantly since the last quarter.

Mohandas Pai: Well Anantha we also said that growth will be 141 to 143 at that point of time, right?

Anantha Narayan: Right.

Mohandas Pai: Now, we had estimated the growth will come may be in the second or third quarter, we are seeing growth in the first quarter itself, and the growth has come in the month of May and June. So, at the time of the April meeting, we did not anticipate so much of growth in the first quarter itself, and we are very happy about it, and when the growth did come, we found that it came more from project starts. Project starts have really gone up to more than 400 from something like 260 or 270 the previous quarter. So, the increased project start has been more on-site driven, and that is why you see this kind of decline in margin.

Lady presenter: Right. We have got our last call from our last analyst on the line; Chellappa from Pioneer ITI calls us from Chennai. Chellappa, go ahead.

Chellappa: Good afternoon. This is Chellappa from Pioneer ITI. Could you tell us whether the new product acquisitions, do you have access to the existing customers of these products.

Nandan: In the case of the IQ trade, yes. They have clients in Japan, in USA, and in UK and Europe, and all those clients have been acquired as part of the acquisition. But actually there are two parts, you know, the total acquisition value was about $3.88 million, we have paid about $2.9 million and $1 million is an escrow pending one of those clients coming on board. But, yes, the acquisition comes with their customers.

Chellappa: Could you tell us the number of customers acquired.

Nandan: We cannot publish that.

Gopalakrishnan: In the case of Autolay also some of the relationships have been transferred to Infosys.

Lady presenter: Bye Chellappa. Thanks so much for joining us this afternoon. In fact, this brings us to the end of this earnings call session. I would like to go across to Nandan for closing comments at the end of this call.

Nandan: I would like to thank CNBC for giving us this first opportunity to create live analyst call on television, and we hope we have been able to answer all your questions, and please feel free to ask more questions in the call we have later or call each of us individually. Thank you.

Lady presenter: In fact, it is our turn to thank everyone at Infosys. Thank you gentlemen so much for being so patient and of course helping us to host this first ever earnings call. Many thanks from all of us here at CNBC.