

# CYIENT

## “Cyient Limited Q3 FY2018 Earnings Conference Call”

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**CYIENT**



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**Moderator:** Good day, ladies and gentlemen, and a very warm welcome to the Q3 FY2018 Earnings Conference Call of Cyient Limited hosted by Edelweiss Securities Limited. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “\*” then “0” on your touchtone phone. I now hand the conference over to Mr. Sandip Agarwal from Edelweiss Securities Limited. Thank you and over to you Sir!

**Sandip Agarwal:** Thanks Ali. Good evening to everyone. On behalf of Edelweiss, let me welcome you to the Cyient Q3 FY2018 Earnings Call. We have with us the senior management of Cyient, headed by Mr. B.V.R. Mohan Reddy, along with other senior members of the management team. Without further ado, I will handover the call to Mr. Ajay Aggarwal to start the proceedings. Thanks.

**Ajay Agarwal:** Thank you, Sandip. This is Ajay Aggarwal here. Good evening, ladies and gentlemen, and good day to any people from outside of India. Welcome to Cyient Limited earnings call for the third quarter of financial year 2018 ended December 31, 2017. Present with me on this call are our Executive Chairman, Mr. Mohan Reddy; Managing Director and Chief Executive Officer, Mr. Krishna Bodanapu.

Before we begin, I would like to mention that some of the statements made in today's discussions may be forward-looking in nature and may involve risks and uncertainties. A detailed statement in this regard is available on our investor update, which has been e-mailed to you and is also posted in our corporate website.

Before I handover to Mr. Mohan Reddy to make his brief overview, I would just like to mention that we have slightly changed the process in terms of release of results. We are just trying to make sure that everybody has a good understanding of the results before the market starts reacting. So we take the results to the board, then we announce it by the time the markets close, we announce it. And then we provide at least one hour, one and a half hours for everybody to study and come prepared for the earnings call. So going forward, we will use this process because we have seen that earlier, looking at the summary without going into details, there have been some confusion in the past. So this is the practice we will follow.

Today, we have the consideration of interim dividend also. Because of that, I know you have got maybe less than one hour today to study the results. But going forward, we will make sure you get one and a half hours to study the numbers.

With that, I handover to Mr. Mohan Reddy to give you a brief overview of the company's performance for the quarter.

**BVR Mohan Reddy:** Thank you, Ajay. Good evening to all of you, ladies and gentlemen. I once again welcome you all to this conference call. Q3 Financial Year 2018 was in line with our expectations, both on revenue as well as margins. We saw the highest-ever quarterly revenue of US \$152 million with

a strong quarter-on-quarter growth of 1.3% and a year-on-year growth of 11.9% in US Dollar terms despite the lower working days.

For our services business, which is our core, the revenues stood at US \$139.9 million, which, again, the highest ever with a robust quarter-on-quarter growth of 4.2% in US Dollar terms and a 4.4% in constant currency terms and a year-on-year of 15.6% in US Dollar terms. The growth in our services business is more broad-based with six out of the eight business units, which grew at double digits year-on-year. Operating margins for the quarter sustained at 14.6% despite the headwinds of higher paydays. The expansion is 116 basis points year-on-year. Operating profit for the quarter stood at Indian Rupees Rs 1431 million or it is Rs.143.1 Crores, which is also the highest ever, with a quarter-on-quarter growth of 1.6% and a year-on-year growth of 16.5%.

Net profit for the quarter stood at Rs.878 million or it is Rs.87.8 Crores. There has been one-off event, the loss of IAS on two grounds. Two months of operating losses due to Hurricane in Puerto Rico, and some marginal loss on divestment that Ajay will explain in a moment. Adjusting for the one-off, the normalized profit for the quarter would stand at Rs.1088 million or Rs.108.8 Crores, implying a year-on-year growth of 15.5%.

Cash and cash equivalent stood at Rs.1,077 Crores or US Dollar \$168 million, which is again the highest ever. Free cash flow generation for the quarter stands at 67% of EBITDA, and that is at Rs.113.6 Crores. Adding the proceeds of IAS divestment, the free cash flow stands at Rs.174 Crores for the quarter.

Taking feedback from the investors, company declared a second interim dividend of Rs.4 per share, which is in line with our revised dividend policy of payout of 40% from the current payout of 30% barring unusual situations.

As a part of the ongoing CSR initiatives, we continue to support 25 government schools, supporting the education for the underprivileged children. As a part of our initiative to increase IT literacy, we have also added one more Cyient Digital Center, taking the total to 56.

Cyient Foundation launched two smart classes. The first of such government school in the Telangana State. Cyient obtained the ICRA rating of CGR 2+ for corporate governance practices of the company. We won Pratt & Whitney, what they call it as the America Supplier Innovation Award for the fifth consecutive time; and Productivity Savings Award, second time in the last five years. Cyient won Golden Peacock Award 2017 for Risk Management recently in Singapore. Confederation of Indian Industries recognized Cyient as one of the most innovative organizations. On the infrastructure front, we established aerospace nearshore engineering center in Portishead, or it is called Portishead in the United Kingdom. We also inaugurated the Cyient Defense Services offices in West Palm Beach in Florida. We expanded the Center of Excellence for a key customer with additional capacity of 75 seats, strengthening our business relationship. We also inaugurated the Global Tower Operation Center, or TOC as it is called, in Hyderabad. It is the Tower Operations Center. This IoT-enabled TOC provides 24x7 surveillance and remotely monitors all passive assets in cell towers across multiple locations around the world.

On the infrastructure front, our Telstra delivery center in Blacktown, New South Wales got the coveted ISO 27001:2013 certification. We won our first grid analytics project in collaboration with the recently concluded partnership. With this, I would like to handover the call to Ajay, who will take you through the detailed financial performance for the quarter. Ajay!

**Ajay Agarwal:**

Thank you, Mohan. Before I go through the some of the numbers, I would just like to take a couple of minutes to explain one of the one-offs, which is there in quarter three. So as such, we have delivered a very robust profit growth. You can see, year-on-year, our profit growth is about 16%. We are giving for the first nine months a double-digit growth on profit. But if you look at the reported number, there is a one-off, and we have to read the reported numbers with this one-off.

So in the last quarter, we had already disclosed that we have this 49% joint venture with Pratt & Whitney, and we had already decided that we will be divesting this 49%. I think the transaction has been consummated in this quarter, exactly in line with what we have signed off. In terms of the financial returns, I think it has been a very handsome return. We got the IRR of more than 50% on this original investment that we made in 2003. And over a period of time, we got more than \$20 million from the original investment of \$250,000. In terms of how it impacts the quarter, we have got on a gross basis about \$11 million. On a net basis, net of tax, \$9 million, that is how you see we have the highest-ever cash of \$167 million. Obviously, there has been a handsome operating cash flow also that has been generated. In terms of the income statement, I think the overall impact is about \$3.5 million. There are two things before closing since there was a hurricane, as Chairman mentioned, the losses until that point of time were about \$3.15 million. And the loss on sale net of tax, I think more or less is at a neutral level. So when you look at this profit numbers, I would request you to please look at these details and they should be helpful in reading the statements.

So coming to the revenue, I think this has been a good quarter with \$152 million of growth. In constant currency, we have grown in services business 4.4%. All of us know we have a lot of headwinds that typically come in Q3. Despite that, I think 4.4% constant currency growth and 4.2% in dollar terms has been very good growth. If you look at year-on-year growth, all the businesses I think are growing positively in double-digits right from Aerospace, Transportation, Communication, IENR, Semiconductor, Transportation, U&G. DLM, where we had a push out of some of the revenue to the next year, is also on track, and Krishna will talk more about it. But I can assure you that with the growth in Q4, we are absolutely on track on DLM. If you look at the geography-wise, I think the growth is coming from all sites. America has grown 10%; Europe, 16% and Asia Pacific 10%.

In terms of the income statement, I would say the most gratifying factor as all of you know that because of the mismatch between the bill days and the payday, we do get a headwind on the operating margin in Q3 typically. So this time, we had a headwind of about 130 basis points but we had a lot of improvements in utilization and other operating parameters. Because of that, we have been able to sustain the margin at 14.6% level. In the services business, our margin is

moving in the right direction where we are looking at a number closer to 16% in the services business. For the Q3, I think that is one of the best performances. If you look at year-on-year also, our margin is improving. Most of it is coming from gross profit improvement, and the absorption of SG&A is also helping us.

In terms of profit after tax, there are two items. One is IASI impact and another is in terms of other income if you see both in terms of the treasury income as well as the income that we have made on the forward contracts, I think we are in positive. Only the restatement of the assets related items on last quarter, it was about - I think I will show you in the next slide about plus Rs.9 Crores, at this time, it is about minus Rs.5 Crores. So that swing of Rs.14 Crores makes a lot of impact. So overall, if you see on taking off the one-off, we have a 16% growth impact year-on-year and a degrowth of 2.4% quarter-on-quarter. This is all because of that Rs.14 Crore swing. If you take that out, the impact of that itself is about 12%. We would have delivered about 10%, had the rupee stayed at 64 and not moved to 63 between September 30, 2017 and December 31, 2017 just for the purpose of balance sheet restatement, it would have shown a quarter-on-quarter growth of about 10%.

ETR, you would see that the reported number is much better at 22.4%. But I would say, because of the tax adjustment on IASI and also the adjustment for the deferred tax because of the US, our like-to-like, excluding one-off number is 27.9. How to read the tax going forward? We are still studying the impact of the US tax rate. Our estimate is our ETR in SEZ stage should go down by about 1% but some of the further impacts are still being studied, and we continue to work on the SEZ ramp-ups, which could further reduce the tax rate in coming years.

As we saw, we have the highest cash position of about Rs.1077 Crores or \$167 million. The cash conversion is tracking very nicely at 67%. Even if you look at the full year, we are at about 50%. The good thing is DLM also, there is a lot of focus on cash generation and while they have broken even on the operating profit, I think on cash also, we have generated positive free cash flows. All these have led to a cash generation of 1136 million INR. And you add the IASI, then the overall addition is Rs.1749 million or Rs.174 Crores and if you look at the bridge at the bottom, we are explaining where we have spent. The only takeaway is we have spent money on the dividends that were declared last quarter and we have spent another Rs.21 Crores on long-term investments, which includes some investments in IB.

In terms of the first, the other income as I explained, while on the face of it, you will see that our other income quarter-on-quarter has moved from 406 to 273. You can see that if you take off the impact of unrealized FX loss/gain that moment of 93 to minus 50, which is a swing of about Rs.14 Crores, then we are doing well on realized forward contract as well as on the treasury income and if there is no change in the FX policy. If you look at our total coverage, it is set at about \$123 million. We continue to have in the next quarter and coming period some advantage over the current spot rate, which translates at current spot rates to a gain of about \$5.24 million and you can see at the bottom, the arbitrage in the rate. So if you look at dollar rate, for example

our forward position is at about 67.5 whereas the current spot is at about 64. With this, I will handover to Krishna!

**Krishna Bodanapu:**

Thank you, Ajay. So like always we will start with the current investment pipeline and the focus areas. In terms of M&A, there are two active LOIs in place. One of which is a company called B&F that we have talked about previously. You may recall, we announced the acquisition of a specialist toolmaker in the US. It has taken some time to close because we needed something called the CFIUS approval, which is given by the Department of Treasury in the US because the company also does defense-related work. We got the CFIUS approval a few weeks ago, and we will close this very shortly and there are a few other things in terms of corporate investments, etc., which are going on. I will just lead the active pursuits. We have put that there to make sure that we are being transparent and articulating our requirements proactively. So nothing changes there, we are focusing on various businesses in various areas and we will continue to be focused on that going forward.

In terms of the industry outlook, I will spend a few minutes on this. The Aerospace & Defense industry is quite strong. While there are challenges, like I have been saying on the commercial aerospace, the defense is starting to pick up. We also like Chairman said, we inaugurated the office in West Palm Beach, Florida, which actually does a lot of work for defense-related projects. There are already about 150 people there, and we are seeing some very, very good growth over there.

We believe that the defense market is coming up, and we are well positioned both because of the organic investments and also once B&F comes into hold, we will see that being quite helpful to how our overall Aerospace & Defense business will grow. There are also areas like Avionics, which is essentially aerospace electronics, aftermarkets, manufacturing, engineering, which are all helping with this growth.

The Communication Industry obviously as you know cuts across a number of industries in the sense that it is an enabler for a lot of disruption that is happening across multiple industries. We are seeing some good opportunities around fiber deployment, which essentially helps high-speed broadband connections. If you look at the slide that Ajay presented, communications was one of our star performers and we see that momentum to be continuing.

The Utilities & Geospatial Industry also - there are some very good opportunities in this industry because there are new technologies like advanced metering, smart meters, etc., while the sort of the historic skills around transmission and distribution and network design are stable where we are seeing some very good growth opportunities in the areas like software and analytics, we are seeing grid management, things that really help collect data, collate data and then do analysis with the data.

On Rail Transportation, we are seeing strong growth both in Rolling Stock, which is the train itself and the signaling. The long-term outlook is quite positive. I want to say that we have also signed up with another new OEM, which is one of the largest OEMs in the world. And with this,

all the five large OEMs in rail are our customers and not just tactical customers, but quite strategic in terms of how we work with them.

The Industrial Energy and Natural Resources, that market still is under a little bit of stress. We are not seeing the spend in capital coming back. Capex still tends to be at a premium, but having said that though there are a lot of opportunities like U&G around electronics, telematics, IoE, analytics, etc. So while we do see muted growth for this year, which I have been talking about over the last couple of quarters. Next year, we are starting to see some good opportunities tee up again not in the traditional areas, but in areas like the design-led manufacturing, analytics, connected equipment, etc. We put together a strategy for connected equipment, how we can effectively connect things together and we are seeing some good traction because of that.

The semiconductor industry has had a fantastic run this year on top of what happened last year. Between the last two years, growth has almost been 25%, which is a significant pickup compared to what it was a few years ago. The demand for memory chips, analog chips are looking quite appealing at this point. There was a degrowth in this business in Q3, but that is just down to seasonality. The rest of the year outlook actually looks quite good.

The medical devices industry also continues to do well. We expect a CAGR of about 5% going forward and the major drivers of these are increasing healthcare expenditure, awareness, aging population, application of technology, etc. So there is a lot of impact on the medical device market, starting from design to manufacturing to servicing, etc. Therefore, we are quite well positioned over there. Again, there was a small de-growth because of seasonality, but we have started a number of relationships and some quite strategic with the top 10 medtech players. So we believe that is growing. And also, medical is an interesting business because there is a lot of new companies and start-ups. So we are also seeing some good opportunities there.

DLM continues to be positive and I will talk about what happened this quarter. But because of a push out of one order this quarter, which we are very confident will happen in Q4. Q3 was a little bit tepid in the DLM business. But again from a longer-term perspective, communications, defense, transport are all doing well and the outlook for Q4 is actually quite strong in that business, which I will talk about here in a second. So net-net putting it all together, the services business, we said double-digit growth that will absolutely be there. It will be obviously a little bit better than just being double digit. It will be higher than that. It will be closer to 11%, 12% in that range is what we are looking at.

Now DLM business, I said 20% growth at the beginning of the year. I just want to caveat that a little bit. From a volume perspective, the 20% growth is going to happen. There is just one small oversight from my part and that is last year, we were adding excise duty to the revenue whereas this year we would not just because of the new GST regulations and so on and so forth. So the reported revenue will look a little bit smaller. It will be more like 16% or so because that 4% will be excise duty that we were adding last year, but not this year and I apologize for that maybe that was an oversight, but keeping that caveat aside right, the volume growth is still going to be 20%; that is the first point over there. The second point is before you pull out your calculators, it will

be 80%, 90% growth, is what we have to do in Q4 over Q3 and one I want to assure you that is in the pipeline, the orders are there. The material has come in. We have double checked with our production schedule. The manufacturing capability that we have in Mysore can deliver about \$25 million to \$28 million of product in any given quarter. So all that adding up together, between 80% and 90% quarter-on-quarter growth is what we will deliver 20% volume growth is what we will deliver. It is just that from a reported perspective, it looks a little bit lower, so please bear with me on that one.

The margin will expand by about 50 basis points or I will say at least 50 basis points. It will be a little bit better than 50. But anyway at this point, it is really semantics. It will be very close to 50 let me say, but operational improvements gave us 350 BPs, utilization mix, better onsite margin and actually that was a very important aspect because a significant portion of our business is onsite. We got some good margins because of that. The wage hike took away 150. We made about 100 basis points of investments and obviously these are quite strategic in nature be it through the new business accelerator or intellectual property investments, etc. There has also been a little bit of pricing pressure in various spaces, but that took away about 50 basis points, and that is where DLM will also end up with a low single-digit number for the year. So net-net I want to say from where we started off the year, we are going to end up pretty close to where we started off the year. Earnings growth will be double digits, putting all this together and before I close, I will say while it is too early to comment on FY2019 numbers with still going through the budgeting and the forecasting process. As things stand, we do not see things to be very different in FY2019 compared to FY2018. There will be the usual ups. There will be the usual downs but net-net where I still feel very confident about where the business is headed.

Specifically, in DLM, some of the projects that we have been talking about that are really the long-term strategic projects are getting teed up into the pipeline and we are quite confident that through the year, some of these will come up. Obviously at the end of April, I will give you a much better peg on where that stands. With that, I will end here and once again, thank you very much for your support. It has been a good quarter especially in terms of the services business. The forecast also looks quite good for the DLM business. So net-net, we will have a good Q4 as things stand.

**Moderator:** Thank you very much. We will take the first question from the line of Ravi Menon from Elara Securities.

**Ravi Menon:** Thank you for the opportunity and congratulations on a good quarter. So I have a couple of questions. First is on the DLM side, we have seen a decline in the communications, so I wanted to understand if that is what helped us post slightly better margins because I see that the material manufacturing cost has come off and should we expect that this vertical mix change in DLM will continue?

**Krishna Bodanapu:** Broadly yes, the communications business is, at least as it stands we believe that that is not really strategic to us. So that was part of the plan. The dependence on communications will further come down next year and we believe that because of this, we will get some better margins again



there are some mix issues, etc., and say consciously we are reducing the current mix of communications. It is just that there are some really good opportunities that are coming up, which help us make much better margins, which is the current customers want and we want to moderate that. I do not want to say we are not going to do that, but we are going to moderate that.

**Ravi Menon:** Great and in Aerospace saw that you posted nice growth on the services side despite top five clients not really contributing to the bulk of that, so is it really new customer or a set of customers where you got the growth from?

**Krishna Bodanapu:** So it is a new set of customers, I think in some of the top five, Q3 for example hit us quite hard in UTC because there is a lot of US dependency on UTC. The US has obviously fewer working days, etc.

**Krishna Bodanapu:** So that always happens in Q3 that was expected and happened. In general, there was also a little bit of a lower Q2 there and that just continued, but we are also seeing a lot of new customers that are coming in. It is not just one customer who has skewed those numbers, there are multiple. We put in a lot of effort in aerospace over the last few years to continue to develop that pipeline and new customers, and I think that is paying off quite nicely.

**Moderator:** Thank you. We have the next question from Mohit Jain from Anand Rathi. Please go ahead.

**Mohit Jain:** First is on the theme, which Ravi asked on the topline concentration. How should we read it going forward like do you expect this ratio to keep coming off and growth will come from new clients, few years ago, I think we had this correlation we are between topline and company growth, so do you think that can change a little bit in FY2019?

**Krishna Bodanapu:** I think it will change, also given our size at this point and given the growth. We will have to concentrate across the value chain. The growth will be quite broad based, it just would not be in the top customers. Also having said that there is always going to be a bit of seasonality because if I look at even on the top of my head if I think of the top 20 there is nobody where there is a crisis or revenues coming off. It is just that the others are doing better and again it is a seasonality thing. I would not read too much into it.

**Ajay Agarwal:** Typically we have seen that our growth in the top 20 customers, not top 10. I think it is plus or minus 3% and that trend is continuing. I think aerospace is a typical case where we have got it a lot from non-top customers including the new customers what Krishna said, but I think overall if you look at the top customers, they continue to have good traction.

**Krishna Bodanapu:** Yes, absolutely.

**Mohit Jain:** Second one on utilization like where do you see this number settling down?

- Krishna Bodanapu:** I think Q3 was a good number, Q4 it will come down a little bit because we are all just pushing the limits of how we can effectively manage, but it would not change very significantly. I think it will be around this number. I think this quarter, which was the highest ever in terms of utilization or at least once the complexity of the business came in, but it would not change significantly I mean plus or minus 200 BPS is what I believe at least will happen for the foreseeable future.
- Moderator:** Thank you. We will take the next question from the line of Pankaj Kapoor from JM Financial. Please go ahead.
- Pankaj Kapoor:** Thanks and good quarter congratulations. Just a question on the reported revenue growth, was it a surprise because as you mentioned Q3 typically seasonally weak for us, so how the quarter shaped up, was it a surprise to you?
- Krishna Bodanapu:** Not really. I mean it is just that I say if we looked at the beginning of the year it would have been a surprise because typically Q3 is like that, but during the course of the year as the pipeline started building up as what basis our conversations with customers, etc., I say even at the end of Q2 what we thought internally in terms of where we would be we were about there. Actually we were slightly better than that, but it was not anything where we, on January 1, 2018 we all did not run to the office and sit in front of a computer and analyzed it. We pretty much knew where it was going to be plus or minus. At the beginning of the year, maybe not, but through the year, yes.
- Pankaj Kapoor:** Right and the order book addition also has been quite good, so any colour you can give in terms of how this stacks up across different verticals?
- Krishna Bodanapu:** I think the order book has been quite robust across all the verticals. Aerospace would be the biggest part in that because typically aerospace has the seasonality that Q3 has lost orders, but DLM orders were low, but we are not really worried about that because there is a lot of backlog there and we are set there, so it has been quite consistent across various businesses.
- Pankaj Kapoor:** With that kind of order book and the pipeline that you are seeing, you mentioned that while it is too early, but FY2019 is likely to shape up very similar to what FY2018 could be. Just wanted to understand what could be one or two or three things, which could possibly drag that down, any client-specific challenges that you foresee where you might be hitting a glass ceiling or the client might be looking at their spending portfolio, anything which we should keep in mind while we try to extrapolate the order book into the future revenues?
- Krishna Bodanapu:** I think it might be a little bit too premature to talk about that because we have not gone through a scrub down by customer, by industry, etc., but again just the fact that there is a reasonably good order book, there is a reasonably good pipeline, there is obviously macroeconomic crisis, etc., can always happen, but otherwise in our business I think things are looking okay at this point to be in line with what it is last year. The usual risks are always there. There is always while order book might be there, there can be cancellations, there can be regulations, where the order book might come from might create a challenge from workload, attrition, all those are there, but I do not see anything specific to derail this.

**Moderator:** Thank you. We will take the next question from the line of Urmil Shah from IDBI Capital. Please go ahead.

**Urmil Shah:** Congrats on a strong quarter. Krishna, my question was again, on the DLM business. One was a very strong growth in Q4, which are the segments you think that could drive growth and moreover FY2019 and FY2020 our target of increasing the design part of the business based on the order pipeline, how does that look?

**Krishna Bodanapu:** I think the Q4 growth will primarily come from aerospace and defence that is why the order backlog is. In terms of how it stacks up for the future years I think there is a lot of design that is starting off in the pipeline. Obviously, it takes some time to get the design through to manufacturers. So that is why I said these things that will tee off in DLM will happen during the year, but most likely towards the second half of the year that is when the strategic projects will really start to kick in. But having said that I will say our first product that we designed has gotten EASA, which is the European design authority or certification authority for aerospace. We got our first EASA approval a few weeks ago. The second EASA approval will also happen imminently, I think it is going through the process. The volume in design is starting to build up.

**Urmil Shah:** My last question was you talked about the opportunity in the defence part. Does that look like it can make aerospace and defence overtake grow at the company growth over FY2019 and FY2020?

**Krishna Bodanapu:** I think it is a little too early to comment on that. I mean the problem with the aerospace and defence is its binary either it happens or it does not, honestly if it does not is one thing, if it happens it will be significantly higher than even the company average. So I would just say at part that aside I mean I would look at that more as an upside as things happen.

**Moderator:** Thank you. We will take the next question from the line of Prakash Chellam from JM Financial. Please go ahead.

**Prakash Chellam:** Congratulations on a good quarter. Just wanted to check on the DLM business, you are indicated earlier that you would be free cash flow positive, I noticed that this quarter the DLM business is free cash flow positive. Is that something, which you kind of see continuing to happen over the next few quarters going ahead?

**Krishna Bodanapu:** Yes, so if you see the challenge, I think the free cash flow had two elements. One is we had to break even at the operating profit level, which we have achieved this quarter and I think we will continue that and second I think we have been working on the working capital and we have got a good handle on that. So I think going forward we will - so of course next quarter if the volumes go up just because of mathematics of it, there could be some working capital because we were looking at very good growth, but in general I think we do look at both at operating profit level as well as cash flow level, we are going to be positive going forward.

**Prakash Chellam:** Second question, which I had was on the Australian telecom business. Do you foresee any challenges, any political uncertainties around spending in that area or are you aware of anything, which might impact your potential growth of that part of the business, please? Thank you.

**Krishna Bodanapu:** Prakash we do not see anything is derailing it, but it is not going to grow at the same pace as what it has grown. The telecom business still has a lot of potentials, but we are also seeing that happened in various parts of the world, growth will be a little bit more broad based going forward not just in Australia. Also I think some parts of that business that are still ramping up, some parts, which are ramping down because the work has done. So net-net I will say nothing will derail us at least where we stand or where we fall in the value chain because from a sort of broader political aspects a number of other things that are out of our control, but from where we stand we believe nothing will derail us, it is just the growth margin a little bit lower, but there are enough opportunities there elsewhere to make up for that.

**Prakash Chellam:** Thank you for taking my question.

**Moderator:** Thank you. We will take the next question from the line of Rishi Maheshwari from Aksa Capital. Please go ahead.

**Rishi Maheshwari:** Thanks for taking my question. Congratulations guys, good quarter. Just to understand in your conversations that you have recently had with the winds that you have had, is there any conversations on pricing increased that you have engaged or I understand that when you go into the future, are we also looking at because of the change in the mix of the business we would naturally look at the change in pricing for the positive trajectory?

**Krishna Bodanapu:** From a pure pricing increase perspective from a hourly rate type of pricing increase that is just not going to happen. I do not really see that is happening in general I mean there is always going to be places where that will happen. The smart way that we can get our price increases is really by packaging it as a project where we have end-to-end responsibility or more comprehensive responsibility. There we will see some better luck where we can package it as an outcome based or a risk reward kind of a project that is where we are seeing some better opportunities to get better price in, but purely from a hourly rate perspective I would be very surprised that we see price increases. We have seen it in some places having said that like especially some of the onsite business, etc., where we were delivering some good value, but we would not get in the price increases we were not seeing it, but the opportunities to clever things at this point that is risk reward and outcome based pricing are significantly higher especially if you have the competence and the confidence.

**Rishi Maheshwari:** The second question was to understand the Make in India opportunity, the size of that or anything that you can share with us on the offset opportunity now that the first airlines also launched so there will be clear spending in the avionics within India as well. We seemed to be rightly placed for benefiting out of that trend. If we can have your views in the same?

**Krishna Bodanapu:** I think it is one of those things where the opportunity is huge, but we would not counter shake hands before the rooster hatch and nothing has hatched so far honestly so I think the opportunity is there. We will invest into the opportunity, but we are pragmatically investing in those things, we are being very careful on how much we invest at the same time we are not expecting some huge numbers to come in immediately. So if it happens it happens it is icing on the cake, but at this point I would still look at that as the bluebird or the icing on the cake or whatever the sort of the right way of putting at it. I would not take that into the business plan. We have operating team on it although the expenses have been written off, etc., so it is really a bonus hopefully Diwali bonus, but it is a bonus.

**Rishi Maheshwari:** Thanks. My next set of questions would be on understanding your margins. In the last concall you have elaborated in terms of the various levers that you have had SG&A being very high. There has been also utilization, which you had a chance to improve, which you have done and onsite offshore. You have stepped on the pedal, it seems that there is just one thing, which I think is extremely important is that you have got a really long deal of less than a million dollar client, which could be operationally heavy and therefore would not be as remunerative as possible. Do you think that is an area of opportunity where pruning down some of those, which are not remunerative could also give you a margin kicker while at the same point concentrating your energies on some of the key clients?

**Krishna Bodanapu:** Absolutely. There is something that we have been doing actually, we have cut down a number of clients in the long tail especially we do an XY on what is the size of the client and what is the margin that we get out of them especially low margin, low small accounts or most of them have been pruned. Obviously when we start getting into trouble our low margin, but large customers that is when we get into trouble because the weightage is quite significant, we have started to prune some of those, but the size means that usually there is some dependency on it. So we are looking at that and we will continue to do that actually that is a metric that we review every month in terms of how many low margin customers and how long if it is. From a pure margin take I am not sure how much we cannot comment on it at this point.

**Moderator:** Thank you. The next question is from the line of Ashi Anand from Allegro Capital Advisors. Please go ahead.

**Ashi Anand:** Congratulations on a good set of numbers. The first question was on the aerospace, you made a comment on challenges we are facing on commercial aerospace, could you just highlight what is this?

**Krishna Bodanapu:** The design in commercial aerospace has come down quite a bit because a lot of programs that have been designed over the last 10 years, be it the 787, the 350, the 320neo, the 737 MAX, all those programs, the C Series from Bombardier, the ERJ from Embraer, etc., those programs the design is done we are going into manufacturing. So from a commercial aerospace perspective, design in commercial aerospace has been coming down for the last few years and it is stabilized, but it would not increase at least for the foreseeable future where the opportunity is though if you look at this sort of continuum the design is done, now things are going into manufacturing. This

is the actual physical manufacturing, but there is a number of tasks that have to be performed, which are engineering related, which I need to support manufacturing that is why there is a huge opportunity. Similarly, once they have been manufactured they start flying there is a lot of things that have to be done to support the after markets, the repairs and MRO, all that good stuff. Again there is a lot of engineering task. So my point was the new design and new products in commercial aerospace is come down, which is happened over the last few years and that is sort of something, which just have to deal with over the last few years, but the support are of manufacturing and after markets has gone up significantly.

**Ashi Anand:** You also mentioned that there is some interesting opportunity around defence. What proportion of aerospace revenues would currently come from defence?

**Krishna Bodanapu:** Right now it is quite small I think there is some let us say 5% is what difference at this point. At this point where we are looking at is there were interesting opportunities we have competence, we will focus on them, but we will consider with bonus.

**Ashi Anand:** Just lastly in terms of DLM. If I look at see DLMS margins are two or three years down the line what level of margins could we still be targeting from slightly medium to longer term perspective?

**Krishna Bodanapu:** I mean 10% is what we have stated as the steady state margin and that would happen in the next two to three years at an operating level, but very quickly while that in isolation is 10% there is a big dependency on design because the whole idea of DLM has design led manufacturing, so the design margins would be much better, so once you start adding the design margins, which will be more in the 20% range to the manufacturing margins now you are starting to come more to the 12%-13% operating margin level, but what is the interesting part is the volume will be significantly higher, so that is a play that we are going after design is a better margin, it has to be designed in manufacturing and volume and the market share will be significantly higher.

**Moderator:** Thank you. We will take the next question from the line of Sagar Lele from Motilal Oswal Securities. Please go ahead.

**Sagar Lele:** Thanks for the opportunity. Krishna just wanted to understand the DLM business are you getting any material orders yet from Cyient's key customers you are initially targeting them in order to cross sell lot of the Rangsons' service offerings. I understand the sale cycle is a little long, but anything materializing on that front?

**Krishna Bodanapu:** Yes absolutely. I think we have got some really good orders. It just takes time to materialize also from the perspective of you have to do the design first, it is basically design qualification, new product introduction, prototype certification, volume production. So we are in the early stage for some really good opportunities. Again in 2019 we should start seeing this move to that value chain in FY2019.

- Sagar Lele:** Great. Also in the European business you have been seeing some really good growth there. Which verticals would this really overlap with, is it more the transportation overlap that is causing this growth?
- Krishna Bodanapu:** Transportation, aerospace and defence. There should be also some utilities and geospatial. These are three businesses that we will do.
- Sagar Lele:** Thanks a lot.
- Moderator:** Thank you. We will take the next question from the line of Mayank Bable from Dalal & Broacha. Please go ahead.
- Mayank Bable:** Congratulations on a great set of numbers. I just wanted to understand from you as far as the Geospatial segment is concerned, with google maps coming in aggressively and top client being TomTom in Geospatial what kind of threat do we see or any challenges that we can expect in the forthcoming future?
- Krishna Bodanapu:** It is a great question because I think that something that is on the top of a lot of people's mind, but what I want to say is, if you look at where and we have also had this conversation with TomTom multiple times, obviously we have a great relationship there and we have a transparent conversation with them on their business and we tie into their strategy. Two things are happening while google maps does provide a consumer option. From a commercial perspective the TomTom algorithm and the data is significantly more accurate than google maps. So for example TomTom I think their largest customer is either FedEx or UPS. For FedEx or UPS whether the business depends on the quality of data it is quite a value add that TomTom provides to them that is the accuracy of data, the accuracy of traffic and the algorithm to get from point A to point B including driver scheduling, how did they go up from address A to B to C all that, so that is one aspect. So they do not have a significant value proposition. Again as a consumer your five minutes to say that you can still live with it. FedEx and UPS in those five minutes keeps adding up and it goes into the hundreds of millions of dollars that there is an impact, so that is one aspect. The second aspect is if you look at maps historically happen two dimensional relatively accurate information whereas today with things like autonomous driving, highly automated driving, all those things coming in they cannot just be two dimensional they have to be three dimensional. We also have to be not just relatively accurate but even in an absolute sense of technicality, but it is quite important on creating a database that shows absolute location of things rather than just relative location. Also look at the quality of data that is you just do not need to earlier as long as you knew that there was a road it was okay then as long as you knew that they were three lanes it was okay, today you need to know exactly how wide the lane is at each point because for automated driving that becomes quite important. So actually if you look at it all of a sudden TomTom's business has come back very strongly because of the second aspect. The first aspect is what let them survive that is commercially they had an absolutely fantastic product that let them survive, but now would be new technologies that required not just XY also Z and even W I think fourth dimension on within so on so forth that has created the huge opportunity for them.

**Moderator:** Thank you. We will take the next question from the line of Moiz Tambawala from Florintree Advisors. Please go ahead.

**Moiz Tambawala:** Couple of questions. One on the newly opened tower operation center, speak a little bit about revenue model what exactly is it that we do and whether this would be substantial base business and the next question is on the sub-contracting that we do we have mentioned that this is lot of large data collection people that we have there and now that we have the Elpis, IP solutions that mostly on the automate a lot of it so is there going to any structural change in this sort of work that we do?

**Krishna Bodanapu:** On the first one the tower operation center the model is really outcome based model that is we helped our customers manage towers and bases the outcome of how they have been managed we get paid. It is an interesting model because it is not anymore just sort of how many bodies you are going to put in front of a center. It is quite interesting because it has many elements to it obviously there is Softential element because there is operation center that needs to be managed, but also there is DLM element to it because the towers per se today are dump construction sites, there is just a tower, so we are also rechecking these towers with sensors with an ability to communicate with all the stuffs, so you put these sensors in various electronic kits there to capture the data. Then the IOT let you transmit the data and then ultimately the analytic speed, which is our analytic business helps analyze the data. So one of the interesting thing on the TOC is that it brings a lot of elements for business and a lot of the acquisitions together to come up with the solution, which can also be monetized in a very unique manner. In the second question on Elpis, it does change some of the dynamics, but I would say sometimes we jump in front of ourselves in terms of how quickly a technology will be adopted, Elpis can help that with a collection of data over a period of time and one of the deals that we won is going to help us to do that, but some of the subcontracting work that we do is even more elementary today, it is really around the physical asset around the network rather than the network itself. So it will happen, but I would not write off the current business model at least for a few years. I think the great thing for us at least is that we are doing these things that are really give the large volumes two, three or four years down the line, but at the same time the current business would not go away in a hurry.

**Moiz Tambawala:** Great and lastly if you can sort of indicate what are sort of revenues that you are expecting from the tower operation center and margin if at all you can?

**Krishna Bodanapu:** It is too early for that I think the operation center has been created so we are now in the business cycle I would take some time to answer that.

**Moiz Tambawala:** Sure. Thank you.

**Moderator:** Thank you very much. That was the last question. I now hand the conference over to Mr. Sandip Agarwal for closing comments.

**Sandip Agarwal:** Thanks to everyone for participating in the call. I will handover the call now to Ajay. Over to Ajay thanks.



**Ajay Aggarwal:** Thank you very much. As Krishna said we have delivered a very strong year financial year 2018 and we all look forward to a very strong year financial year 2019 and thanks for all your support. Thank you very much.

**Moderator:** Thank you. Ladies and gentlemen on behalf of Edelweiss Securities that concludes this conference call for today. Thank you for joining us. You may now disconnect your lines.