"Cyient Limited Conference Call – Acquisition Update on Rangsons Electronics"

January 02, 2015

MANAGEMENT: **MR. KRISHNA BODANAPU – MANAGING DIRECTOR AND CHIEF EXECUTIVE OFFICER**
MR. AJAY AGGARWAL – CHIEF FINANCIAL OFFICER
MR. MANJUNATHA HEBBAR – HEAD OF PRODUCT REALIZATION
MR. SUJEET KUMAR – HEAD OF MERGER & ACQUISITIONS
MR. PAVAN RANGA – CHIEF EXECUTIVE OFFICER OF RANGSONS ELECTRONICS PRIVATE LIMITED

Moderator: Ladies and gentlemen, good day and welcome to the Cyient Limited Conference Call and Solution Update on Rangsons Electronics. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Krishna Bodanapu – Managing Director and CEO. Thank you and over to you sir.

Krishna Bodanapu: Thank you. Good morning ladies and Gentlemen. First let me start this off by wishing you a very happy new year and successful 2015. Welcome to the Cyient Limited analyst call. This is Krishna Bodanapu – Managing Director and Chief Executive Officer at Cyient. Also present with me on the call are Mr. Ajay Aggarwal, Chief Financial Officer; Mr. Manjunatha Hebbar, Head of Product Realization; Mr. Sujeet Kumar, Head of M&A and I also want to welcome Mr. Pavan Ranga who is the Chief Executive Officer of Rangsons Electronics Private Limited; and we will talk about the organization here in a moment.

Again, thank you very much for making the time on a short notice to be on this call this morning. We are really excited to announce the signing of definitive agreement to acquire 74% equity stake in Rangsons Electronics Private Limited. Rangsons Electronics is a leading electronics system design, system integration, and manufacturing services company headquartered in Mysore in India. This is an all cash transaction that we did and the reason why we did it is we believe this acquisition significantly strengthens our end-to-end capabilities in integrated engineering, design product lifecycle management production and so on and so forth.

What I will do is I will quickly take you through a presentation on the investment rational and why we are proposing to do this. We will have some time for Q&A in the end and will also request Pavan Ranga, the Chief Executive Officer of Rangsons Electronics to say a few words in the end.

But to begin with, what I want to do quickly is take you through the acquisition rational. If you look at some of the conversations that we previously had and that we communicated to our investors and analysts including during the Investor Day in May of last year. The intent of Cyient, the strategy of Cyient has been to move from being a simple services provider to being somebody who can become a provider of solutions which incorporate the entire lifecycle of various products. Just to recap, we call this the S3 strategy. To define, the first S was Services, services is when we provide discrete independent point offerings which are discreet technical solutions to technical problems. It is really about an industrialized service delivery model which is really built on efficiency and scale.

Systems is when we take the services and actually design and execute a system, a system typically has multiple elements of service to it, we actually execute various elements or various processes to actually design a system and give our customers a system design as the end product and that is really built on our domain centricity or domain capability and our ability to develop a solution or develop a system.

Now the third aspect which is Solutions is an integrated set of service that solves not just the technical problem but help us to address the business problem around managing the entire lifecycle of a product starting from the design of the product through to the prototyping, testing, certification, sourcing, producing and then all the aftermarket elements till the time product life cycle ends.

So really our stated strategy if you may recall is that we are moving from services to systems and then to solutions. Today, 80% of our businesses is in the services mode whereas 20% is in the systems mode, there is some solution related business that we do but that's a small number. And our strategy has been that by 2020, 30% will go to services, 50% will go to systems and 20% will go to solutions. To execute this strategy, it became quite important that we significantly strengthen certain aspects of the solution value chain especially around sourcing, prototyping, certification, testing, production, and then the aftermarket elements of it and I will explain that here in a second.

Really, our strategy has been to expand the core, we want to get into design led product lifecycle partnership so we are not just limited to the design phase but using our design competence and our design capabilities we can support the entire product lifecycle. Key to that is that you look at design as typically a three to seven year lifecycle, three is really in industries like heavy engineering, perhaps a little bit lower even in industries like medical and semiconductor and seven is really in industries like aerospace. But really what we believe by getting into the solutions space and by our ability to execute solutions, we then get into this lifecycle which is really a 10 to 30 years or even longer if you look at some of the aerospace and defense industries. So given that the intent is to get from just services to design led product lifecycle we believe that this partnership or this investment into Rangsons really provides us the capability to start doing that.

If you look at the 3x3 chart that is there, it articulates what our focus was, if you look at what is at the bottom, we tried to capture the engineering intensity in various industries. If you look at the left hand side, we tried to capture the competitive positioning and the growth. And industries like aerospace, transportation, medical are really where there is a lot of value that we can provide in design led lifecycle management, because if you look at what it say at the bottom left hand side which is more of your traditional manufacturing around plastics or sheet metals or fabricated goods that's really not the intent of where we want to do design led lifecycle management. It is really in these high-tech industries. Every component that gets created in the aerospace and defense sector for example is really a handcrafted part, there is a lot of design that goes into it, there is a lot of changes that have to be made through the design in the manufacturing process, there is a lot of intellectual capability that's required to conceive these products, design them, certify them, make them and then manage them through the lifecycle and that's really what we are trying to hit at in these industries specifically transportation, electronics, aerospace,

aerospace related electronics, defense, medical; these are the industries where the story actually becomes very-very compelling and very-very differentiated for us.

Really, why are we going down this path because that's where the opportunity is. We believe that our customers are asking for this a lot more. If you look at our customers, Cyient's customers, they are just not asking us design things, they are asking us to manage them through the lifecycle. If you look at Rangsons customers they are not just giving them the design and asking them to produce it, they are also asking them to add the value around making the product better through design. So our customers are asking for it and we believe that our opportunity set really increases by 5 to 10 times in various industries because of this capability. We cannot just do the design but take the product through its lifecycle. We are seeing a lot more deals around risk reward, partnerships with customers who again want us to get involved in the lifecycle rather than just some discrete parts of their lifecycle. There is technology transfer option, India is becoming a very compelling location to do a lot of design, obviously there is some elements of manufacturing also which become very compelling and therefore it becomes a very interesting opportunity for us. And then I think what excites me about this, especially within the new macroeconomic situation in the country, is that there is a lot more focus now obviously in the Make in India program, defense offsets are becoming a little bit more of a reality.

Obviously, you may have heard that the Defense Minister on Saturday and the Finance Minister and Prime Minister on Monday, had some large meetings with some key influential and decision makers around how can we really get this started and how can we really make this is a reality and we believe with this, again, we had a very good story with design. I think this story becomes a lot more powerful and more importantly it becomes very-very differentiated and that's what makes this partnership, this acquisition of equity in Rangsons really compelling for us.

If I may just take a minute and introduce Rangsons to you. Rangsons is a privately held company incorporated in Mysore here in India. They have been in business since 1993, there are about thousand employees across the engineering value chain from design, to manufacturing, to systems level services, and obviously they also have employees on the production side of the business. The industry focus gels very well with our focus especially the areas that we believe are important for us in our growth journey that is aerospace and defense, medical, electronics in general. Rangsons has 95,000 square feet of space here in Mysore and in Bangalore where they do some of the product realization activities including the prototyping stuff, the testing, and certification and so on and so forth. They are focused on very similar markets as we are including, in Rangsons India also becomes a compelling market because offsets in Make in India is important.

In terms of financials, revenue will be roughly $66 million is what Rangsons' revenue was in financial year 2014. Going forward obviously we will provide a little bit more update as we do our quarterly updates and so on and so forth. And the EBITDA is between 10% and 12% is the typical EBITDA that Rangsons has been running at and which I think for some of us who understand manufacturing sector will agree is it is a pretty impressive number in that sector because they do some very high end work and they do some very value added work for our customers that's why they are able to deliver a very strong EBITDA and a very strong return on equity.

Just a quick breakdown and I apologies there is some problem with the chart and we will put and updated version on the website here very quickly but aerospace and defense constitutes about 70%, industrial is 18%, medical is 11%, there are some other businesses which are the rest. West Asia is the large for Rangsons, it is about 70% of their revenue, North America is about 27%, and the others have the smaller part. But what we think also, this complements us a little bit is because Israel is a big market for Rangsons, especially in the aerospace and defense sector, Israel is an opportunity that is waiting for us to really address because a lot of work gets done in some of these high-tech industries, aerospace and defense, medical, high-tech electronics and so on so forth. So I think that also gives us access to a very interesting new market where our services and our capabilities become quite important. Therefore what it really does is we now have the capability not just on the front end of the design cycle which is the design processes but it really helps us build and manage systems through the...

What I want to highlight here is that almost 80% of Rangsons current business is system integration box build what that means is, they take in complex systems, they are buying out a lot of these obviously the subsystems and assemblies but they are integrating it, they are testing, they are making sure that it works and then delivering it. So it is a very complex manufacturing because of the way the integration and the certification and the testing happens which is a big differentiator and a value proposition that they take to their clients. So there is about 20% which is sort of the lower end of manufacturing, if I may use that word around PCBs and so on, but really 80% is some very complex state of the art system integration work which is a big differentiator for Rangsons and really that's that our customers are looking for, especially in the industries where I talked about aerospace, medical and high-tech electronics.

So what this really does is it completes that continuum of where we will be, and I will talk about that here in a second but just quickly the key customers that Rangsons has. Like I said, some of the Israel companies are quite large for them be it Israel aerospace industry Elbit or Rafael. Good news is some of them are already our customers and there is a big buying from these customers that they would like to work with us in a larger way and then they also work with Thales who is also a Cyient customer, on the right hand side you have some of the other industries from the industrial side be it Honeywell ABB, etc. So my point is we both share a few interesting customers but we also have some very complementary customer which makes it very-very interesting to build up on our synergies.

Equally importantly is the industry specific certifications that Rangsons already have be it either for rail or AS9100C for aerospace and so on so forth. And what we believe is very important is these certifications come because of long well documented repetitive process that produces some very consistent quality. So the fact that this is already there gives you the big advantage because if we were to work with any aerospace company on avionics or any critical electronics they will insist on having AS9100C, we actually have AS9100 for design, now we also have AS9100 for manufacturing. Put together, it is a compelling value proposition and I will capture that in the next slide where we talk about what this does, it takes serious design capability, adds Rangsons prototyping system integration, production, combines that again with our aftermarket and ability to manage aftermarket engineering and that really completes the entire chain and that's really where we want to be per our articulated strategy.

Just to give you a little bit feel on the financial aspects of the deal, like I said we have acquired 74% equity of Rangsons, we have a structure on how the other 26% or how the ownership group which is the Ranga family of Mysore and Cyient can transact the other 26%, we have a structure that's agreed upon and that's quite robust over the next two to four years depending on various things. But we will run this as a separate legal entity, it functionally aligns with our solutions and systems business. Obviously, like again I had spoken to some of you previously, we want to leave our services business to function the way it is because it is obviously a business that our clients count on, we deliver a lot of value to our clients, where it is something which expands the services business so we are going to treat it or we are going to manage it a little bit separately. At a customer level we are going to integrate the offerings, obviously Manjunatha Hebbar whom some of you have also already met will be responsible for the integration and to make sure that we have a complete offering not just a bunch of discrete offerings and both the teams are working on putting that in place.

We are not going to disclose the financials because of non-disclosure and confidentiality but I can tell you that the acquisitions will be EPS accretive immediately, it will also improve our return on capital by about 0.5% on a consolidated basis in FY16 because of full year impact. Integration will take about four to six weeks as we have estimated and then full year integration will be from next year but we believe that in the current state ROE will increase by about 0.5%, all else being equal. And as you know we also have about Rs. 750 crores of cash so we are looking at various avenues of funding this acquisition but the cash is obviously already there, any funding that we put in place is really to optimize our capital structure a little bit, but outside of that the resources to do this are very much there in the organization.

So with that I once again thank you for taking the time to be on the call. At this point before we open it up for Q&A, what I would like to do is request Mr. Pavan Ranga who is the CEO of Rangsons Electronics Private Limited, a part of the Ranga family who ultimately own this business. So I will request Pavan to say a few words on Rangsons deal.

Pavan Ranga: Thank you Krishna. Good afternoon ladies and Gentlemen, I wish you all a very happy and prosperous 2015. I am Pavan Ranga, CEO Rangsons Electronics.

Very brief overview of Rangsons, we are about 20 year old company, a part of NR group, manufacturers of Cycle Agarbattis. We are India's leading electronics system integration house, we have grown consistently over the last decade with about US$66 million in annual revenue. We have a visibility to continue a robust growth and we were strategically also looking to expand our offering, our customers continue to treasure that from system integration they would want us to graduate to a product lifecycle management kind of an engagement model and I think the partnership with Cyient here would accomplish that to a great deal. And going forward we look at significant amount of opportunities for product realization in aerospace, defense, medical electronics and industrial electronics. We have a very strong competence in RF microwave, digital electronics, and analog. Apart from that we have some very strong capabilities in critical manufacturing technology areas in speciality materials. So we are looking forward to this association with Cyient and the integration. The structure is very robust and I think it is well strategized to realize the benefit to market and customers. Thank you.

Krishna Bodanapu: Thank you Pavan. And with that we will open it up for some questions.

Moderator: Thank you very much sir. Ladies and Gentlemen, we will now begin the question-and-answer session. We have first question from the line of Srinivasan Ramachandran from Spark Capital. Please go ahead.

Srinivasan Ramachandran: Just wanted couple of broad thought process on the Rangsons business model per say. So what is the business model here, is it do we have a multi-year agreement in some of clients to manufacture some of these boxes as a systems integration or as a spare parts player or as a manufacturing entity or is it that it is more three six month kind of an order book. Just wanted to understand what is the typical revenue model structure and what is the sales process involved?

Krishna Bodanapu: Srinivasan I will ask Pavan to answer that because he knows the best obviously.

Pavan Ranga: Yes. Well, there are two kinds of engagements we have with customers. One is purchase orders based on their end markets which would for example in the aerospace and defense field if the Ministry of Defense of any country gives them an order for a certain number of systems they will flow that order through to us. Now this can vary a purchase order from a timeline standpoint, it can vary from 12 months up to five years and sometimes it can extend even beyond that, which is the purchase order based engagement. The other engagement is in an environment where there is a repeat requirement for products which are consumed on a regular basis, here we work on a forecast model, and engagement here generally lasts up to the lifecycle of the product. Now like Krishna said, if you are only involved in the engineering in the production side then the slide cycle may last between three and five years or three and seven years. But if we are at a product lifecycle engagement level it can extend between 10 and 30 years. So very long-term engagements.

Srinivasan Ramachandran: Okay. And in terms of the stage at which Rangsons participates, is it typically post design is when you kind of enter into the overall scheme of things from a client point, if you have to take – Thales aerospace as an example, at what stage does Rangsons intervene and start taking over, that's one. Second is, is there any product warranty that we typically end up taking for the products you ship to your customers?

Pavan Ranga: See, what happens is because we are an engineering led integration company, we engage with customers at a fairly early level. What do I mean by that? Customers would have generally solidified their intellectual property meaning their core technology would have been in place, we start to engage with them at a manufacturing engineering level which means the designs are generally ready but they are not yet tested for manufacturing so we provide what is called design for manufacturability, design for testability and then the prototyping which is the validation process and then take it through to the productionization phase till the end of the lifecycle.

Srinivasan Ramachandran: Okay. My last question is, Krishna, just in terms of the ROE or the EPS accretive, I presume those numbers are assuming there is no debt to optimize capital structure that's being shared with us?

Krishna Bodanapu: That's why then that can subsequently assume that we use this out of our cash, which is a bare minimum. Further, we are working to look at alternate options where we can get further arbitrage on the cost of capital by using some other means. But this whatever we have mentioned is assuming the use of our cash.

Srinivasan Ramachandran: Sure. And I think so Ranga you missed on the warranty, is there any warranty that we undertake in terms of, say a product does not deliver as per expectation or on the risks from a product lifecycle point of view?

Pavan Ranga: Yes. Generally we do not take warranties from a product standpoint but what we do provide is a warranty on our workmanship. So it is a limited warranty but something we provide.

Krishna Bodanapu: If I may just add Srinivasan, as a due diligence we had also seen the track record of the company, we did find that the total amount on this, normally what is done is a rework in the company and I think this is less than 0.001% or something of the revenue in terms of what is the financial impact of those warranties in the history of the company. Very fair comment Pavan?

Pavan Ranga: Yes, that's right.

Moderator: Thank you. We have the next question from the line of Sandeep Muthangi from IIFL. Please go ahead.

Sandeep Muthangi: I had a couple of questions about the exposure; can you let us know what is the exposure to the end markets? I understand, let us say for instance the Israeli customers or West Asia customers account for 70%, but those customers would also be supplying to say Indian government etc, so what is the net exposure to the end markets?

Krishna Bodanapu: Well, Sandeep it is difficult to say in the sense that if you look at it, the Israelis might be supplying to the Indian MoD or they might be supplying to the different MoD. So we still look at Israel as the end market because that's where the OEM really is. So one way of looking at it is most of the business, almost 100% of the business goes to OEMs, it does not go to another system player who then does some more value add and sends it off to the OEMs. Almost 100% goes to the OEMs really. Now the OEMs can supply it wherever they need to supply it.

Sandeep Muthangi: Right. I guess my question was that because the Make in India and the India story was mentioned so prominently in the presentation, while the exposure is very minimal I wanted to see if this acquisition actually gives you a descent exposure to the domestic market as such.

Krishna Bodanapu: So, Sandeep it does, but what we want to do is, if you look at the best case scenario it is based on the current business. And if you look at why we actually started talking to Rangsons for example and the strategy, it was really on what else can we do for our customers and how can we become more strategic to them. Now the make in India story is really the add on to it, I mean I would assume that the best case Make in India would be a great booster when it happens but the best case is still the fact that we can do a lot more for our existing global customers.

Sandeep Muthangi: Right, makes sense.

Krishna Bodanapu: And Hebbar has a quick comment to it.

Manjunatha Hebbar: Also Sandeep I think just to clarify on the Make in India, government wants Make in India as the country which wants to implement it as more like Make in India for everybody including the domestic as well as the world. So all our OEMs and other customers are also looking at a way to really work with their partner who actually can qualify and support that initiative and are actually looking for themselves as well. So that is the premise with which it actually will have significance.

Sandeep Muthangi: Right, makes sense. And can you give us some idea about the client concentration with Rangsons, do top five accounts or is there any major client that dominates the revenues?

Pavan Ranga: What happens in our kind of industry is that we have generally large engagements as we grow and today we have fairly significant engagements with Israeli aerospace industry who also happens to be a key partner to the Indian MoD while there are also strong player globally. We have very strong engagements with ABB and GE in several of their locations and businesses.

Sandeep Muthangi: Okay. Just one last question. Can you give us also an idea of what kind of growth rates and the margin profile has been there in the past three to five years?

Pavan Ranga: Yes, in the last three to five years we have had a compounded growth of about 30% - 35% as a company. And we continue to see such robust growths happening, of course we'll stabilize now at about 15% - 20% going forward.

Sandeep Muthangi: And this we are talking of dollar revenue growth, is it?

Pavan Ranga: Yes, that's right.

Krishna Bodanapu: And just Sandeep, top five approximately are 85% of the revenue.

Pavan Ranga: But the top five may be changing.

Manjunatha Hebbar: Yes, the top five may be changing depending on how programs come and go but I think there is also something that we honestly liked because fits in with our whole strategy, let's focus on few customers and do a lot more for them rather than go after just a wide set of customers.

Krishna Bodanapu: And I think also just to add on to that quickly, the 80% concentration comes mostly from the Fortune500, the large customers.

Moderator: Thank you. We have next question from the line of Omkar Hadkar from Edelweiss. Please go ahead.

Omkar Hatkar: You have mentioned that the integration will be at customer level, so do we have two separate teams coming in or we'll have a single team that will approach the customers? And secondly, you just mentioned that it will be a separate legal entity, so are there any scope for cost synergies because if it is a separate legal entity…?

Krishna Bodanapu: Okay. We are working on the integration plan but to the customer it will be a one face, we are very clear about that because that's really how we drive synergy and we drive collaborator benefit, so to the customer it will be one face. Obviously there will be a single point of contact, there will be a single interface or you will see within that interface various people with various skills go in and that's how we've been selling our businesses, if it is a complex project there will be some mechanical people who will be involved, there will be some electronics, manufacturing engineering guys. So we will continue to do that, but to the customer it will be one face as Cyient Systems and Solutions as the framework. In terms of the separate legal entity, like I said it is also right now it is in a joint venture mode because the Ranga family still owns 26% and we have obviously two to four year plan on that. Therefore it will continue as a separate legal entity. Long-term also we believe that there are certain aspects of this business that make it better to leave it as such but obviously we are already working on integration wherever we can especially if we can drive some shared services, some synergies around our purchases and so on so forth. So we will definitely do that, I think there are some opportunities to learn from both organizations, for example Rangsons does sourcing very well because for them material is relatively higher part than what it is for us. So there are both areas in which organizations can collaborate and we are working on that at this point.

Moderator: Thank you. The next question is from the line of Madhu Babu from HDFC Securities. Please go ahead.

Madhu Babu: Sir, what would be the cost structure be for this kind of a company? Is it like material cost is substantial, or what is the percentage of cost from employees, etc.?

Manjunatha Hebbar: Yes, Ajay will take this.

Ajay Aggarwal: So typically I think it depends on nature of projects being recorded from year-to-year but typically you will find we have 65% to 80% could be the raw material cost depending on the projects being executed in various years. Typical people cost will be much lower, for the last year it would be something like 3% - 4% of the total revenue. So I think that's the correct assessment. So predominant cost will be the raw material cost, the components which go in to the boxes and which is low on the people cost.

Madhu Babu: Sir and would there be any scope for margin expansion because it looks more like a manufacturing entity and what would be the cross-sell opportunities to the other large aerospace clients in this business?

Krishna Bodanapu: So we will have some margin improvement opportunities and we have a plan on how we are going to do it because we believe that once we truly execute solutions of the projects the margin profile will look a little bit different. But I will differ the comment to maybe a few months, perhaps the next update because we need to understand exactly how that works before we make the commitment on what that could be. But the more important thing, the second part of your question around synergies, there are a lot of synergies both with Rangsons customers for Cyient services and the other way around. Because if you look at it, to put it very bluntly, we design something, the customer takes it back, does his value-add and then gives it to Rangsons to manufacture it. Whereas now, what we are saying is, for the same customer we can go from design to managing it all the way through the end of its lifecycle. So that is the synergy that we are really after.

Moderator: Thank you. We have the next question from the line of Vinay Rohit from ICICI Prudential. Please go ahead.

Vinay Rohit: Sir, if you could help me in terms of the extent of manufacturing you are saying 80% is system integration, so do we have significant manufacturing facility and fixed asset base?

Krishna Bodanapu: No, it is actually interesting, there is a pretty sophisticated manufacturing setup in Bangalore and Mysore but the asset base is quite limited just for the simple reason that it is a complicated manufacturing so it is really how people are able to manipulate the machinery or the tools that are available, that's really where the differentiator comes from. So it's not a typical manufacturing company where you have some big factories with large machinery, that's not the intent of Rangsons and why we are collaborating here. It is really some sophisticated manufacturing which is really driven by design and also driven by the people who are ultimately executing the projects. So it is really at that system level where they bring things together, where they prototype, test, certify and make sure that it passes and make everything work rather than just sort of what I would consider a typical mechanical manufacturing set up which basically has some large machines and some complex materials and so on so forth.

Pavan Ranga: I think in terms of the investment involved also it doesn't really involve very high investment outlays like a typical manufacturing setup, it is quite low. If you look at the revenue to the asset base, the ratios are quite low for this kind of business because it is all high precision kind of work.

Vinay Rohit: And since you specifically mentioned the defense offset, so the clients we have, they have significant exposure to Indian defense sector, is it?

Krishna Bodanapu: Our aerospace clients look at Indian defense as a very important market. It is no secret that we work with people like Boeing and Airbus and UTC, etc., for all of them Indian defense is a pretty significant market.

Moderator: Thank you. The next question is from the line of Ravi Menon from Centrum Broking. Please go ahead.

Ravi Menon: I just had a question about, what would be the percentage between the product qualification and the initial prototyping kind of work versus more, if I may put it, mass manufacturing.

Krishna Bodanapu: At this point roughly 80% would be the lifecycle manufacturing so more during the life of the product and about 20% to 30% will be in the upfront product certification prototyping and those areas.

Pavan Ranga: So due to the nature of systems that we produce here, even the production volumes are like prototype volumes, so it is highly engineering driven. Every unit needs to be built in a particular way and tested in a certain way. You will see batch quantities going all the way down to 5 numbers and 10 numbers, These are highly complex systems and is not commodity mass manufacturing.

Moderator: Thank you. We have the next question from the line of Ashish Agarwal from Antique Stock Broking. Please go ahead.

Ashish Agarwal: Most of my questions have been answered, just need couple of clarification. First of all, Rangsons also has a JV with an Israeli company, is it a part of this company and does it stay? And my second question is that Rangsons have around 1,000 odd employees, just wanted to understand what are the education qualifications of most of these employees?

Krishna Bodanapu: The JV is part of another company that they have, we have a process of how we will work with that JV, so I think we've talked about it in great detail and the way that it is structured and the way that that works it makes more sense for us to work with that JV rather than make it a part of this transaction or this initiative.

Moderator: Thank you. We have the next question from the line of Shivam Gupta from Equirus securities. Please go ahead.

Shivam Gupta: I just have one question, given that there will be a single face which is going to be selling the combined offering to the client so in that particular scenarios wouldn't some kind of a performance guide or warranty clause will ultimately come to rest with you guys?

Krishna Bodanapu: It depends on what we are doing and how we are doing and how we are pricing and so on so forth. So it really depends from case-to-case because if you look at even some of the works that we currently do around the engineering where we take the responsibility for the whole lifecycle we will have some elements of a performances guaranteed that we involved. So obviously it depends, we have to be careful about it in the sense that we have to be careful about what we take as liability, and what we give as warranty, etc., but some of it can be managed. Even in our current business we run up against that and we manage that through various initiatives including insurance or testing to the level that our liability can stand in any court of law and various things. So we will continue to do that.

Shivam Gupta: Okay. So in that case let's say going forward once your solutions pie in your revenue increase, would it be a fair assumption to make that, you would be using higher discount rates to assess the profitability of those kind of contracts and if yes then could you give a color like maybe how much higher are those current compare to your current cost of capital?

Pavan Ranga: So when we do any project that has a risk-reward, what we do is we actually estimate how much sale or what is the end outcome and what are the various scenarios, we then assign a probability to each scenario. So if the end outcome is based on product sales then we assign a probability of what those sales would be to determine if we can make money or we can't make money on a project, and it depends which industry, how we are doing things but typically our weighted average cost of capital or discount rate is 15% is what we typically take for a normal project. Whereas if it is anything where we will have to take risk, we quantify the risk and the discount rate is typically 25% to double, it is 30%. That's how we have been trying to do it, again, it depends on the situation and the scenario, but when there is risk we quantify the risk and assign a weightage to it.

Shivam Gupta: Okay. And the last question from my side is that since there is some level of overlap between your customers and Rangsons so are there instances where you have already spoken with these customers and what has been the feedback from their end towards the joint entity?

Krishna Bodanapu: It's been very-very good, obviously we have spoken to customers, in some cases very specifically and directly but in some cases where we have had disclosure issues maybe indirectly but this gives me an immense confidence that our customers really are going to like this proposition, I mean we already have a couple of opportunities where we have put in bids together and that's already started to happen. We have even formed the paper JV with Rangsons before we could announce this deal because there were opportunities where we had to bid together on some very complex lifecycle related projects. So basically I am a very strong believer that our customers are going to like this value proposition because we have talked to them, they have agreed that this is the case, they want us to do more, they want Rangsons to do more, and I think this provides that opportunity.

Moderator: Thank you. We have the next question from the line of Ankit Sancheti from Kotak Singapore. Please go ahead.

Ankit Sancheti: Couple of questions from my side. First of all, whom do you compete with? In the sense when you bid for any project who are the typical competitors for you and on what basis you are being selected?

Krishna Bodanapu: You mean in the joint entity or in the individual entities?

Ankit Sancheti: I am saying from a Rangson perspective, when you bid for any project with say ABB or whichever of your clients, which are the typical competitors you see? And second, on what basis are you given the orders, is it just the cost or is it the capabilities? Can you throw some light on that?

Pavan Ranga: Sure. See, as I said most of the products we integrate are fairly complex systems so price is always a point everywhere but that is not the primary selection criteria. Our typically projects competitor will be in the home country so if you look at a US customer most of the time either they are manufacturing it in the US already or they are manufacturing it somewhere near-source like Mexico or if it's Europe it's Eastern Europe. Because typically our kind of products don't come to Far East Asia so to speak. So these are system integration projects where either they are doing in house or they are having a near-source player for it.

Ankit Sancheti: Okay. Second thing is, in terms of you mentioned that we are buying 74% stake and the rest will be acquired in next couple of years, two to four years. Is it dependent on subject to some financial parameters being met or it's just an agreement that we will buy in next two-three years, can you throw some light on it whether there are any set parameters that EBITDA should go to X level or sales should go to Y level, something like that?

Krishna Bodanapu: No, it is an option on both sides. In the first couple of years it is an option on the seller's side and fourth year onwards it is an option on our side based on how the performance happens. Now there is certainty that we will acquire the rest of the entity in four years but when it happens it depends on sort of what the EBITDA numbers are and what the revenue is. So based on that the groups can exercise their option.

Ankit Sancheti: Okay. Can you share why the promoter family wants to cash in out when specifically "Make in India" and the defense initiative, though it has been a dream for last six-seven years but right now it looks more closure to the reality than it has been ever in the past. So given the size of opportunity why sell it out right now, why not encash it later? It's good from a Cyient perspective but I am saying from a promoter perspective who is selling it out, what's the need to sell it out?

Krishna Bodanapu: Sir, I will say through our diligence process obviously, we have also asked some of these questions because very honestly what you articulated also went through my mind. But really what we came to the conclusion is together there is a much bigger opportunity, at this point for example in "Make in India" also they are not just saying it is low-end manufacturing or it is straightforward system integration, they are saying that "Make in India" will constitute a pretty significant elements of design, of innovation, of IC that will go into making some sophisticated products. So together we have a much better value proposition and I think with all due credit to Pavan and the Ranga family, the compelling need at this point that you can't just have one way of servicing a client, it has to be a comprehensive service that comes to them. If you look at how this conversation started that they were really looking at a financial investment from various people at some point and I think when we started talking and when we started working together and more importantly when we started looking at some projects that were coming our way what became apparent is we'll have to have an integrated service offering, it can't just be an isolated service offering. At that point is when we really started talking about why we should take a stake that is quite significant rather than just a financial investment which could have still let us transition customers and so on and so forth and that's how the conversation really started. Obviously the other equity, the 26% that they will retain and that they will contribute and be on the board is because they do see a pretty significant upside going forward but I think with a lot of credit to them they see that together we will have a much better and more compelling value proposition and that's how I got convinced that why they wanted to possibly at this point look at the structure rather than just continue and that gave me a lot of confidence that it's a great company and that together we can do a lot adding our client capability.

Ankit Sancheti: Okay sir, sure, appreciate that. One or two things, one is, someone in the call mentioned that there is one more JV and subsequently you mentioned that that JV is not part of the current deal and you will work out something on that. I am just wondering from the perspective of selling promoter, the Ranga family, do they have similar businesses, one or two or three more entities which we are not aware of? This JV was told by someone else so I am not aware if you guys have something else in the similar domain.

Krishna Bodanapu: So the Ranga family has obviously a lot of other business interest especially in consumer products and some other businesses in the agriculture space and so on and so forth. But we have a pretty solid non-compete with them, even this JV that exists there is a very specific purpose that it exists for and that's why it does not make sense to bring it into this equation but it exists for a very specific purpose. Therefore we have a very clear understanding of non-compete with them and therefore we are fairly confident that it is something that we can work with them with the non-competed place and also having the insights into what they want to do next and what their plans are going forward.

Ankit Sancheti: Okay. Typically in this I think somewhere it was mentioned that projects can be for one, two, three year, five year, do we work for some kind of order backlog kind of thing that say for example ABB has given you an order to manufacture an x thing and that order is say 50-60 odd crores executable over five years, is that the typical kind of structure and if that is the case can you share what can be the order visibility which we have at this point of time?

Pavan Ranga: See there are two models as I said, one is the order backlog model where we do have some order backlogs, these orders can range from Rs. 20 crores to Rs. 300 crores as of now and they can range from one year back log to a five year backlog but the business itself comprises of two models, about 50% - 60% of the business comes from this kind of a model where there is an order book built up and the rest of the business like the ABB and the medical electronics like I was telling you is more of a long-term contract and a rolling forecast, usually contracts range between five and eight years.

Ankit Sancheti: Okay. And just last one or two things, you mentioned that everything will be bought out in cash, is that right, and is my understanding right?

Krishna Bodanapu: Yes, that is correct.

Ankit Sancheti: Entire 74% stake. And I don't know how much you can share, in this presentation we have FY14 numbers of $66 million and practically to be honest FY15 is nearing end, I am not asking for any specific numbers, I am not saying give me a specific nine months number but if you can just give me a trend how has been last eight-nine months or how do you see FY15 going ahead either in terms of qualitatively, in terms of revenues and EBITDA?

Krishna Bodanapu: No, I think last couple of months have also gone quite well for them and obviously we have a little bit more insight but they will at least grow in the double-digits, 10% - 12% is at least what will be in FY15. But again, it is a little bit early to comment on that.

Ankit Sancheti: No sure, I am just asking for a trend. So you are saying 10% to 12% at least growth would have been there in FY15 as I look at FY14 revenues, is that right?

Krishna Bodanapu: Yes, absolutely.

Ankit Sancheti: And EBITDA would have been either in this range or improved because high rate of…

Krishna Bodanapu: It would at least be in this range, yes.

Ankit Sancheti: Okay. Is it a full taxpaying company or there are some tax exemptions, do they enjoy some tax exemptions?

Ajay Aggarwal: As far as corporate tax is concerned, it is full taxpaying company.

Ankit Sancheti: 33% whatever, 30-33%?

Ajay Aggarwal: That's right.

Ankit Sancheti: And have you shared that this company does not have any debt, sorry if I might have missed in the con call.

Ajay Aggarwal: They have the normal working capital arrangements which are typical for these kinds of setups.

Moderator: Thank you. We have the next question from the line of Sagar Lele from Antique Stock Broking.

Sagar Lele: I had this one question on how much would be the import component in the total materials that you procure?

Management: It would be 70% to 75%.

Sagar Lele: So would there be scope for more localization in the materials?

Pavan Ranga: There would definitely be overtime. See, electronic component manufacturing in India, the government is giving a huge push and that would be the key driver for more and more localization.

Sagar Lele: So would it be alright to say that your EBITDA margin range probably of the 10% to 12% is quite variable and dependent on currency fluctuations as well?

Pavan Ranga: It would not be as impacted, thought there would be some impact because we are heavily export driven but if you look at exports and imports are more or less kind of balancing off. So there would be some impact but it would not be so to speak drastic.

Sagar Lele: Right. And just one more question, so basically you are involved in a very high mix and low volume kind of a play, so this obviously involves a lot of knowledge transfer and process transfers or say training requirements and production line set ups after a particular contract has been received. So does it take a lot of time in terms of setting up and in terms of commencing manufacturing after order has been received?

Pavan Ranga: Yes, you are right in your observation. Actually these kind of products take a long time to kind of transition into and stabilize and you usually typically have teams from Rangsons stationed in different parts of the world where there is a robust knowledge transition happening, knowledge transfer happening. Now the good part about such transitions is once they come in here they are very solid for a long period of time because it’s very expensive to move such programs around.

Moderator: Thank you. Next question is from the line of Srinivasan Ramachandran from Spark Capital. Please go ahead.

Srinivasan Ramachandran: Hi. Just wanted to understand in terms of the retention of the senior management at Rangsons level what are the thought process there from Cyient point of view to ensure that there is not much of senior management attrition and what are the incentive structures that are being thought off?

Krishna Bodanapu: Mr. Srinivasan, obviously one is at Pavan's level, Pavan will remain on the board and represent them or represent the ownership for as long as they own stake, so we have some continuity from that perspective. From the others perspective, just like in any transaction we are working with the current management to put together retention plan, obviously it's all about the people and we want to keep people happy and keep people around. So I mean that's as you know we have done this a lot and we typically have a retention plan for the top 10 to 20 key employees and we are working on similar thing here.

Srinivasan Ramachandran: Sure. And in terms of the broader opportunity, you said it substantially opens up opportunity on a combined level. Just wanted your thoughts in terms of which sub-segments do you think maximum opportunity would open up, would it be more with some of the original large equipment manufacturers or would it be more like airframe manufacturers, where do you see this opportunity playing up and are there any large competition who can be both an integrative engineering and manufacturing entities that are out there?

Krishna Bodanapu: So in terms of the segments that we are excited about or are really focused on is aerospace and defense, rail transportation, medical electronics and basically anywhere where it's electronics heavy. So more than airframe manufacturers it's really the avionics guys for example because avionics is really what, again I want to reiterate that we are not trying to get into large mechanical manufacturing which is what the airframe guys would be looking for, we are really trying to get into sophisticated electronics. So it would be people like the avionics guys like Honeywell, Rockwell Collins or obviously IAIs or Elbit and so on so forth is one set. Similarly medical equipment manufacturers, medical device manufacturers like rail for example, Thales that we talked about as well a lot of rail electronics and sophisticated rail electronics and each box is pretty customized because each station has different requirements and so on so forth. So that is really what we are after is the guys who have a large electronic continent and who have much sophisticated electronic content.

Srinivasan Ramachandran: And in terms of the competition that's potential out there from an integrated manufacturing/engineering design capabilities point of view?

Krishna Bodanapu: There are some good companies along those lines, I mean there is a company in Canada for example called Esterline. They do a lot of this work but they really take ownership of the product, they are not just doing either or, either design or manufacturing. So there are some good companies out there that we are looking at as you know, because we also don't want to create a market as you know, we want to play in a market where there is an opportunity and where we believe we have a differentiator we want to play it and we believe this is a market where somebody like this comes in, we can create a pretty significant disruption and a differentiator.

Moderator: Thank you. As there are no further questions from the participants, I would now like to hand over the conference back to Mr. Krishna Bodanapu for his closing remarks. Over to you sir.

Krishna Bodanapu: Thank you very much and I again want to thank everybody for participating on a relatively short notice. To us and Cyient and now in Rangsons this is a big game changer, we believe that this is a differentiated strategy and we are really focused on executing it well and executing it to plan. So as always, thank you for your support, we count on it, we value it and I want to assure you that this is a very important aspect of our strategy that we have talked through in great detail. We really-really are proud to be associated with Rangsons Electronics and the Ranga Group because not just the business but more importantly the value system and the ethos of the organization is very similar. So we believe we have a really solid partner and we have a really clever plan and now it really comes down to the execution and we believe we have a great team in place that will execute this strategy. So once again thank you for the support and we look forward to being in touch.

Moderator: Thank you very much sir. Ladies and Gentlemen, on behalf of Cyient Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.