



“Kellton Tech Solutions Limited Q1 FY18 Earnings
Conference Call”

September 13, 2017



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MODERATOR: MR. DIWAKAR PINGLE, CHRISTENSEN IR



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Moderator: Good Day Ladies and Gentlemen, and a very warm Welcome to the Kellton Tech Solutions Limited Q1 FY18 Earnings Conference Call. 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 '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Diwakar Pingle from Christensen IR. Thank you and over to you, Sir.

Diwakar Pingle: Thanks Asad. Welcome to the investors who have logged into the Q1 FY18 earnings call of Kellton Tech Solutions Limited. We have mailed the results and the earnings presentation to you and the same is also available on the website of Kellton. In case, any of you have not received the same, you can write to us and we will be happy to send the same over.

To take us through the results and answer your questions today, we have with us Mr. Niranjan Chintam – Chairman and Whole-Time Director; Mr. Srinivas Potluri – Chief Executive Officer, USA; and Mr. Karanjit Singh – Chief Executive Officer, India at Kellton Tech.

We will start the call with a brief overview of the quarter gone past which will be given by Mr. Niranjan and then we will throw the floor open to Q&A.

I would like to remind you that everything that is said on this call which represents any outlook for the future or which can be construed as a forward-looking statement, must be viewed in conjunction with risks and uncertainties that we face. These risks are included and not limited to what we have mentioned in the prospectus filed with SEBI and subsequent annual reports which you can find on the website. With that said, I would now like to hand the call over to Mr. Niranjan Chintam. Over to you, Niranjan.

Niranjan Chintam: Thank you, Diwakar. Good evening everybody and thank you for taking the time to get on this call and listen to us. Just want to give you a quick highlight of the numbers first and I will talk about the business a little bit. We have total revenue of Rs 175 crores for this quarter, which is about 25% year-on-year growth and about 6% quarter on quarter growth. Our EBITDA stood at Rs 25.4 crores, which is about 33% growth year-on-year and 7% growth quarter-on-quarter. We have a PAT of Rs 14.4 crores, which is 20% year-on-year growth and about 2.5% growth quarter-on-quarter. Our EPS was at Rs. 3.10 for this quarter, which is 20% growth on year-on-year and 6.2% growth on quarter-on-quarter.

A quick highlights of the quarter that has passed. We have achieved a CMMi Level 5 for the company. I think you are all aware that this is a process and procedures and documentation that is required to do any software development, so this is the methodology that we are now certified the highest level that CMMi Level gives us. In addition to these, we have been featured in Forbes Asia's latest 'Best under Billion' list of the top 200 publicly traded companies in Asia-Pacific region, which is an achievement that was a pleasant surprise for us. We have also won an early

digital learning program project from the Republic of Mauritius. These are the main highlights of the quarter that has gone past. With this I will open up the floor for questions that you might have about the results and/or the operations of the company.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. We will take the first question from the line of Augustya Dave from CAO Capital. Please go ahead.

Augustya Dave: My usual question Sir, how is the business looking forward for the next two to three quarters and how is it looking for two to three years from now, any disruption in pricing which is happening because of Forex or competition and the third question is you have mentioned some of your client wins and I also remember from previous calls that you were talking about rationalizing the client list as such, reducing some of the not-so-lucrative account, so how successful have you been in that?

Niranjan Chintam: We will talk about first the foreign exchange effect, yes, there is a foreign exchange effect compared the last quarter to this quarter about 3% rupee has appreciated, so that has an impact on both the top line and the bottom line. Coming to the business point of view, since we are in the digital transformation space, we do not see much of an impact that rest of the industry is facing especially today the IT industry is facing headwinds. We do not see that because we are in the digital transformation space, 60% of our revenue is coming from digital transformation which has also seen a growth compared to what it was last year. From that perspective, yes, we are in the right space at the right time, so we are able to leverage that. The margin pressure like I said earlier since we have the digital transformation space, we do not see much margin pressure since this is not a commodity yet.

Coming to your question on two to three year growth, we have ambitions to grow which we have already announced. I do not want to give any targets now, but we believe that we will be on an organic growth of about close to 20% organic growth that we will be doing and in addition to that, we will also be doing some inorganic growth also.

Augustya Dave: Basically, whether I look at two to three quarters from now or two to three years from now, short-term and medium-term outlook are basically unchanged?

Niranjan Chintam: That is correct, there is no change.

Moderator: Thank you. We will take the next question from the line of Diwakar Pingle. Please go ahead.

Diwakar Pingle: My question to you Niranjan and possibly Srinivas is, obviously the performance has been good in the phase of what we have seen among the other Mid Cap companies, so my question to you guys is what part of your business is actually driving growth and why do you think you are getting those wins that possibly we are not getting the commentary from some of the other people, maybe you could just give me some kind of color on that?

Niranjan Chintam: Last year is when we started seeing digital transformation becoming mainstream. Earlier to that, digital transmission was in what we are calling the digital companies or the start-up companies. Today, we are seeing lot of digital transformation getting adopted by the enterprises, so that is what is driving our revenues, the digital being adopted. Gartner has said by FY2020, 70% of the companies or enterprises would either have to think about digital or have some plans of digital. Since we are in that space, we are able to exploit and we are also an early mover when it comes to digital transformation, before anybody else was talking about digital transformation we were doing it, so for us we have a lot of wins, we have a lot of logos that is also giving us the market share when we go to a customer, we are able to tell them, we have done this which is similar to what you are looking for and we are able to win those contracts. I do not want to speak about why others are not able to do similar stuff, but this is what we have seen the success and this is what is helping us to grow.

Diwakar Pingle: When you say that my question is, are you seeing more business happening in US or is it happening in India, or is it a mixture of both?

Niranjan Chintam: It is a mixture of both, let Srinivas talk about the US side, so he will be able to talk to you firsthand about his experiences there while he is meeting the customers, what it is that he is hearing.

Srinivas Potluri: Thanks Niranjan and thanks Diwakar. Yes, to extend Niranjan's thought process as well as the facts here in the US. Last year we had seen the growth of a lot of these born-digital companies and as a result of our participation in their growth, we are at this time poised very well to work with our enterprise clients and help them understand the disrupting changes in the environment, so effectively all of our enterprise clients are looking for services from us. We are uniquely poised at this time. We have all the technology capabilities to take to digitally transform our enterprise clients. From a US perspective, we see a strong growth in the digital transformation area and since we have deliberately poised ourselves to move into the digital transformation space for the last two years, and our case studies and our work experience with the digitally-born company is helping us to help our clients be digitally transformed, so from a perspective of two to three years, we see strong growth, we do not see any downside. The general IT sentiment in the industry seems to be average, it is not very positive, but within IT the digital transformation area seems rock solid and that is where we see the potential to grow.

Diwakar Pingle: My last question is on the SAP enterprise part of the business, what is happening there and are we getting any new deal wins given our capabilities in SAP S/4HANA and things like that, maybe some highlights on that would be helpful?

Srinivas Potluri: On the enterprise side, obviously the disruptions in the market have impacted the big software vendors as well namely SAP, Oracle etc., and they are reshaping themselves to meet the demands of the market. Like you rightly pointed out, Diwakar, S/4HANA is on the prime, large enterprises have begun implementing S/4HANA this year, the Exxons of the world and the Coca-Colas of the world, and we see a lot of middle and small enterprises following suite towards the end of the year



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early next year, so that is our sweet spot with respect to clients and our existing enterprise clients. We see a potential growth within the system of records going into the digital transformation phase, S/4HANA being prime, S/4HANA being implemented on the cloud, being a focus point, and over and beyond that, Leonardo is the new technology push from SAP to integrate IoT with SAP, and at this point, there are workshops going on with SAP and there is technology exchange going on, and we are at the forefront and we have been selected as one of the channel partners to lead the efforts and bring Leonardo into the market.

Moderator: Thank you. We will take the next question from the line of Augustya Dave from CAO Capital. Please go ahead.

Augustya Dave: How is the competition shaping up now, are you seeing more, let us say \$100 to \$200 million companies standing up to you, more specialized firms coming up, you mentioned that it has still not commoditized and the segmental breakup that you have given this time that kind of validates your point, but in terms of competition is there any acquisitions happening, smaller firms, larger firms, anything you are seeing on competition side?

Niranjan Chintam: When it comes to competition, we are seeing competition from everybody, from a small vendor to a large company, when I mean the large companies, I am talking about all the way up to Accenture and IBM level, but why we are winning most of the deals is because of our technical capability. We have done multiple times whereas the others are talking about it, so when we go to the customer and tell them, for this pick any industry, in this industry we have done this, this and this, and we have done a holistic one. It is not just building a small app and giving it, it is the whole gamut of the digital transformation, not many have done that. Coming to the smaller player, there will be always these what we call the mom-and-pop shop where they are specialists niche areas, like they are good at mobile app development or they are good at analytics, but ask them to do a complete digital transformation, they will not be able to do, so if some specific customer wants just an analytics or an app, then we say, you might as well go to some specialists.

Augustya Dave: Just another question, I would understand if you are not comfortable on saying this publicly, when you get into a new client do you win it because of one of your capabilities or you win because you have the entire portfolio and suppose that, let us say you start with \$100,000, what is your strategy in terms of ramping it up to a million dollars over a period of time, how is that shaping up, I just want to understand how the existing, some of your last quarter you won a pretty large bank as one of your clients, I was just wondering how much can we mine that particular client, how much will your wallet share go up and how much of your incremental revenues will be coming from your existing client growing much bigger?

Niranjan Chintam: Today 80% of our revenue is repeat business, so we are mindful of this account mining, so we have started hiring more and more account managers, so when we look into a deal or when we win a deal, we look at the potential and not the immediate win or the size of the project that we get, so some places we started like you said \$100 K initially, but if you look at what would be the ultimate

potential, after investigation if we see the potential growing to a million dollar plus is when we try to enter those, sometimes we might do certain things for strategic reasons, but those strategic reasons are going to be very small compared to our other larger things that we look at where we say okay we want to get into this space and we see that, we are going to get only 100 K and we are not going to get any more, we might take it, but whereas the larger part of it if you look at what is the potential of mining that account to a million dollar or a multimillion dollar. To answer your question on the bank, yes, it initially was a few \$100,000 worth of deal, but we see potential to go to multimillion dollars. Like I was saying earlier, 80% of the revenue is coming from repeat business, so we do not lose...

Augustya Dave:

Sorry to interrupt you, just out of curiosity I remember when sales force was much, much smaller, they used to have this slide in their presentation where there was one particular unnamed client when they started the business it was \$100K and I think in five years' time, they had grown it to over \$5 million, so is that kind of scalability in one single client possible for you?

Niranjan Chintam:

Yes, it is possible. Initially for this digital transformation project is always going to be a few hundred thousand or maybe a million dollar, you start off with the project. There are projects like what we won with the Mauritius Government, it is a \$10 million project we won immediately. They have larger deals coming down the pipe. Earlier it used to be, can you try this initiative for us or can you do this for this particular business unit, now we are going across all business units and saying they want to do it for the whole company, so we have started seeing deals like that. To answer your question, absolutely, we see where we can get multimillion dollar contracts from the existing customers itself.

Moderator:

Thank you. The next question is from the line of Mudit Minocha from M3 Investments. Please go ahead.

Mudit Minocha:

Congrats for the CMMi 5 eligibility, my question is with the CMMi 5 certification, do you get access to some projects which you were not getting initially?

Niranjan Chintam:

The answer to your question is yes, in certain cases there is an eligibility criteria where they prefer CMMi Level 5 company or what we call the maturity, what large enterprises would be looking at is the maturity of our process, our methodology when it comes to software development, so specifically since we are now focused more and more of the enterprises and not these digital company which are maybe start-ups to mid-size that is where this CMMi Level 5 would help.

Mudit Minocha:

My second question is regarding the goodwill that is accumulated in our balance sheet, so how do you see amortizing that over the time because our strategy has always been acquisitive in nature, thus do you feel the need to amortize the goodwill?

Niranjan Chintam:

At this time, we do not feel the need because the goodwill is coming at consolidation level, yes, the number maybe huge, but in an IT company when you do acquisitions you know that the

tangible asset there is very small and negligible, right, 1% to 2% of whatever revenue or whatever we pay is going to be the physical asset that we purchase. Many of the cases or most of the cases what we see is the asset that we are purchasing is the contract from the people, so that it becomes intangible, that is why this goodwill is getting added. Every year our auditor does an assessment to see if there is an impairment and every year they come back say there is no impairment of goodwill, why do you want to amortize or write it off, so that is what reason why we are not amortizing that.

Mudit Minocha: What would be our long-term debt strategy, how much would be our long-term debt and where do you see growing three to five years?

Niranjan Chintam: I do not have a fixed number in mind as such, today debt is around 0.6% of the debt-to-equity ratio, which is very small to the size of the company that we are. I do not believe it is going to go anywhere above that. We have been consistent with that for the last one year where we are hovering around 0.5 to 0.6, I do not believe we are going to go anything above that.

Mudit Minocha: My last question is, pardon me for my ignorance, I have seen that the ticket size of the projects are going down because of more and more use of open source technology, so I was in touch with one of the regulators in India and they were saying that they got the entire UPI payment gateway setup in less than million dollar, so are you seeing that in your existing portfolio or going forward the ticket sizes because of open source is going down?

Niranjan Chintam: The ticket size is not because of open source, the ticket size is because there is no software sale, where previously they were just selling a software and then services on top of, today everybody is selling services, that is what is happening, but with that in mind, let us look at what enterprises, enterprises are still insisting on or large enterprises. I will give you an example, Amazon, Amazon is completely built on open source. Now go to Exxon that Srinivas was talking about, Exxon would never go with open source. They might tinker with open source, but they will still rely on SAP , Oracle, or IBM and build upon it than relying on open source, so there is always going to be these born-digital companies where everything is open source and then you have this enterprises where they are used to a software product and they are comfortable, they do not want to go with open source or there will be a mix, so to answer your question where there is a software sales in a digital company, they will not be many software sales whereas enterprises there are always going to be software sales, so the ticket size if you minus the software sales or the products sale we call it is going to be still the same. For us, the software sale is very minimal.

Moderator: Thank you. As there are no further questions from the participants, I now hand the conference over to the management for their closing comments.

Niranjan Chintam: Thank you very much for taking the time to get on the call. We have an AGM on the 27th of this month, I would request all of you to make time to attend to that where you can have one-on interaction with us and where I can answer many more questions that you probably are feeling shy



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to ask me on the call, so thank you again and we look forward to seeing you at the AGM, if not then on the next earnings call.

Moderator:

Thank you. Ladies and Gentlemen, on behalf of Kellton Tech Solutions Limited, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.