Q3 FY2011 Earnings Call Transcript – February 10, 2011

CORPORATE PARTICIPANTS:

- Mr. Matthew Vallance– Managing Director and Chief Executive Officer
- Mr. Aashu Calapa – President, HR and Country Manager, India
- Mr. Carl Saldanha – Global CFO
- Mr. Tom Watters – President, Healthcare
- Mr. Santanu Nandi – Executive Vice President, Telecom & Media
- Mr. Sanjeev Sinha – Executive Vice President, BFSI
- Mr. Sanjay Venkataraman – Executive Vice President, Asia Business Unit
- Mr. Mahesh Pratap Singh – Head of Investor Relations

Firstsource Solutions Limited
Quarter Three Earnings Conference Call, Financial Year 2011
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Moderator: Ladies and gentlemen, good day and welcome to the Firstsource Solutions Limited Q3 FY2011 Earnings Conference Call. As a reminder, for the duration of this conference, all participants' lines will be in the listen-only mode. There will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, please signal an operator by pressing "*" and then "0" on your touchtone telephone. Please note that this conference is being recorded.

At this time, I would like to hand the conference over to Mr. Mahesh Pratap Singh, Head of Investor Relations at Firstsource Solutions. Thank you and over to you, Sir.

Mahesh Pratap Singh Thank you, Melissa. Good afternoon to participants from Asia and good morning to participants from Europe and US. Welcome everyone and thank you for joining us on our earnings call for the third quarter ended December 31, 2010. Please note that the results, fact sheet and presentation is available on our web site, www.firstsource.com and has also been mailed across to you. To take us through the results and to answer your questions, we have with us today, Matthew Vallance, our Managing Director and CEO.

Mahesh Pratap Singh Aashu Calapa, President, HR and Country Manager, India.

Aashu Calapa Hello.

Mahesh Pratap Singh Carl Saldanha, our Global CFO.

Carl Saldanha Good afternoon.

Mahesh Pratap Singh Tom Watters, President of our Healthcare Business Unit.

Tom Watters Good afternoon.

Mahesh Pratap Singh Santanu Nandi, Executive Vice President of our Telecom and Media Business Unit.

Santanu Nandi Hi, everyone.

Mahesh Pratap Singh Sanjeev Sinha, Executive Vice President of our BFSI Business Unit

Sanjeev Sinha Good afternoon.

Mahesh Pratap Singh And Sanjay Venkataraman, Executive Vice President, Asia Business Unit.

Sanjay Venkataraman Hello.

We will be starting this call with a brief presentation providing an overview of the company's performance followed by a Q&A session. Please note that everything said on this call that reflects any outlook for the future or which can be construed as a forward-looking statement, must be viewed in conjunction with the risk company faces. The detailed statement and explanation of these risks is available in our prospectus file with SEBI which can be found on www.sebi.gov.in.

With that said, I would now turn the call over to Matthew Valance, our Managing Director and CEO.

Matthew Valance Thank you, Mahesh. I will just start off by summarizing what we say is the main highlights of our third quarter this fiscal. And, if we turn on to Slide No. 4, in terms of our operating revenue we have seen Q3 has a strong performance in terms of our revenue growth and year-on-year in the corresponding period of the previous year, we grew by 4.8% in Rupee terms. And if you look at in constant currency terms, that was a 7.3% growth over the previous year. And in terms of our sequential quarter-on-quarter growth, we grew by 2.2% in Rupee terms and 5.1% in constant currency terms. In that sense, it is our strongest growth in the last seven quarters. So, in what is normally a seasonally weak quarter for us we are pleased with the quarter-on-quarter progression, in particular. And certainly, one of the main factors driving our growth on a sequential basis is the start of our engagement with Barclaycard which commenced on the 1st of November last year.

In terms of the operating EBIT from a percentage point of view, we are lower by 50 basis points over Q2 and the reasons for that being are three-fold. One is the lower realizations on our hedges, compared to Q2, where we booked GBP, the pound like Rs. 78 to the pound, so we got a little bit lower gains from that hedge. And in any case, the Q3, as I mentioned is typically a seasonally weak quarter for us, particularly, in our collections business and we also were affected by some slightly higher depreciation charges. These factors were partially offset by the starting of Barclaycard contract.

Another highlight of the quarter has been our cash generation and we continue to build momentum on that front. In fact, our cash balances over the quarter improved by about $24 million. There were some exceptional items in our normal run rate, our cash generation is somewhere between $8 million and $10 million. But we closed the quarter with cash balances of $80 million. As we mentioned, last time there were some temporary issues around invoice and receivables which resolved very quickly at the beginning of the quarter just gone, which allowed us to improve the cash balance for the quarter. Pipal divestment which concluded during the quarter, the proceeds for the same is to be received and when those proceeds are remitted, cash balance would move up to $85 million during the course of Q4.

One or two extraordinary items, a gain of Rs. 79 million on account of the Pipal divestment I just mentioned, which is accounted for in our other income. And there were some one-time expenses of 64 million mainly related to some restructuring of our operational centers in India. We had a growth in our employee base to just under 26,700 employees as of the end of the quarter. Of which, just under 20,000-odd India-based and 6,750 employees based outside of India, primarily in the US, the UK and the Philippines. Also, we have a small office that we opened up in Australia recently.

And in terms of the net additions we have added nearly 1,800 staff during the quarter which compares to the addition of 212 during Q2 and 876 in the same quarter the previous year, so fairly significant increase in headcount, of which about 700 staff transferred to us from Barclaycard during the quarter and the balance 1,000 mainly added in our India business.

Continuing on the people theme, in terms of our attrition, something talked about in previous calls, we have made some encouraging progress during Q3, and in particular, in terms of our domestic operations, our Asia Business Unit, where the work we do in India for our Indian clients, attrition has come down dramatically to just under 77% which we acknowledge is still high than where we want it to be, but it is good to see that trending downwards.

And also, in terms of our onshore operations, where our attrition came down from 48% to 35% which is a fairly substantial reduction. In our offshore operations, the operations we run from India and Philippines servicing our international clients, our attrition went up from 50% to just under 55%.

In terms of the infrastructure, the seat capacity stood at 20,844 seats across the world and we are pretty much consistent with the previous quarter. We actually reduced 31 seats net. We actually removed two centers during the quarter through the sale of Pipal and we added an additional center in a location known as Thane, which is in Mumbai for servicing our domestic India market. And our seat fill factor is 75% similar to where we finished Q2 and had an average seat fill factor 76% for the quarter but yeah, we do intend over time to improve that seat fill factor.

Just finally before I pass on to Carl to talk through in a bit more detail on the financials, in terms of our foreign exchange hedging, in some sense, compared to others in the Indian headquartered outsourcing businesses we have natural hedging system built in by the fact that something like 70% of our revenues are costs in the same currency as we fell in. About 30% of our revenues are essentially cross-currency revenue streams which we hedge.

In terms of our outstanding hedges, we have $21 million hedges and about GBP 32 million hedged as well. Typically, we hedge for a year ahead, so the one remaining quarter of this fiscal year, we hedged at 95% of our revenues on the dollar at Rs. 47 level and we hedge 85% of our pound revenues at the 77 level and we have hedged also for the first three quarters of next fiscal year on the dollar at the 48 level and the pound at the 75 level.

I will just cover the segmentation of our revenues. Nothing too much to report there in terms of our revenue breakup by geography and North America accounting 55% of our revenues, UK being 33% of our revenues and Asia-Pacific business being 12% of our revenues.

In terms of our vertical segments, during the quarter, healthcare accounted for 34% of revenues, telecom, media including what we do in the Indian market accounted for 37% of our revenues, banking financial services and insurance which is largely cards and collections, 27% of revenues and others are 2%.

In terms of delivery location, , 62**%** of our revenues for the quarter came from onshore operations, 27% from offshore, essentially, the services which we deliver in India and Philippines for the international markets and 11% from the domestic market. And client concentration, our top client remains at 12% and our top five clients increased to 36% to our revenues.

With that I will hand over to Carl to talk to you in a bit more in detail about our financials.

Carl Saldanha Thank you, Matt. Good afternoon to everybody. We ended the quarter at a total revenue of Rs. 515 crores, which has increased from Rs. 490 crores last year at this point in time and from Rs. 503 crores last quarter. This represents an increase of 4.8% year-on-year and 2.2% quarter-on-quarter.

As Matt mentioned earlier, given the fact that seasonally a low quarter, it is a very good in increasing performance, also if you recall last year the rupee has strengthened in the last one year, therefore despite all that we have actually grown our revenues.

In terms of operating expenses, personnel and operating expenses, they have grown from Rs. 422 crores last year to Rs. 443 crores this last quarter. The main in this quarter was the fact that we added on roughly 1,800 people, of which 700 people were in the UK due to Barclay contract. Consequently, our

EBITDA has grown from Rs. 68 crores last year same quarter to Rs. 70 crores last quarter to Rs. 71.1 crores. It continues to increase quarter-on-quarter.

In terms of percentages gone down a little bit but that is because as I explained earlier, we added on lot of staff in this last quarter, the benefit of which we will see in subsequent quarters.

On an operating EBIT basis, we ended up with Rs. 47.9 crores compared to Rs. 46.7 crores in the last year's quarter. A slight drop from Rs. 49.4 crores in the previous quarter.

In terms of percentage, we have dropped from 9.5% last year to 9.3% and 9.8% last quarter to 9.3%. Below the EBIT line, there were a couple of unusual items. One is called we talked about the Pipal gain that we sold the Pipal. That is represented, the bigger part of Rs. 11.2 crores in other income is because of that item. The interest income has been more or less normal right through to Rs. 5.5 crores. The amortized cost on FCCB is really the options value which has been amortized every single quarter.

Extraordinary expenses of Rs. 6.4 crores is mainly because of rationalization of one of our sites, pretty close to Bombay, it was not used in the last six months, so we decided to take a charge on it. In terms of profit before tax, we ended up at Rs. 44.1 crores, compared to Rs. 39.7 crores last year and Rs. 41.5 crores last quarter.

Taxes were a little bit higher because one of our centers came out of STPI, but net-net on a PAT basis; we have grown from Rs. 33 crores last year to Rs. 35 crores for this quarter.

Moving on to next slide, we are showing the performance over the nine months period, our revenues for the first nine months was Rs. 1,509 crores compared to Rs. 1,464 crores last year, a growth of 3.1%.

In terms of EBITDA, we have slightly increased from Rs. 209 crores to Rs. 210 crores. In terms of percentage, 14.3% versus 13.9%. As I mentioned again, because of the expenses in the last quarter.

On an operating EBIT basis, again, we have grown from Rs. 142 crores to Rs. 144.6 crores, slightly lower in terms of percentage from 9.7% to 9.6%. Below the EBIT line, we have adjustment of similar explanation to what I just mentioned for the quarter, in the last year, we had similar adjustments in each of the categories, so net-net in terms of profit before tax, we have actually grown from Rs. 120 crores last year to Rs. 126 crores this period. PAT more or less flat at Rs. 100 crores.

I will now hand you over to Tom Watters, our Chief of Healthcare Business to take you through the Healthcare operations.

Tom Watters Thank you, Carl and hello again, everyone. For the quarter, Healthcare represented about 34% of total company revenues and was just over 2,900 employees with the capacity of just under 3,300 seats for the seat fill factor of 71%. Healthcare services are delivered from both India and in the United States.

In terms of industry trends, medical loss ratio provisions have been implemented at the beginning of January. The key administrative costs that have been identified and included in the medical loss ratios are claims adjudication, call center, fraud prevention initiatives and the coming ICD 10 coding implementations. As a result, any of the payers who fall short of the minimum medical loss ratios for each plan year will be required to issue pro rata rebates directly back to the claim members.

The Department of Health and Human Services will be awarding grant to each state that demonstrate leadership and delivery of Health Information Exchanges or HIE. California has been the first state to implement an HIE since reform mandates began and has essentially created a web-based insurance plan marketplace and then supported that with the toll free hot line to help the pension members understand the plan options.

Unemployment fell to 9.4% on December, that is down from 9.8% in the previous month and the estimates coming out of commerce are that they will remain high throughout calendar 2011 and in the year somewhere around about 9%.

We continue to see an increase in merger and acquisition activity by competitors within both segments of the vertical and these are primarily around integrating technology with BPO services. Focus in the marketplace has differed somewhat between the two segments in Healthcare, opportunities remain strong within the provider market, there has been some caution at the decision-making on revenue cycle project that is mainly due to distractions around implementing Electronic Health Records, EHRs were mandated to be in place by providers by 2014. The Federal government is funding a significant portion of hospital cost associated with the EHR implementation and that accounts for the strong interim focus on completing these initiatives.

With lower healthcare utilization experienced in the recent months, payers have realized relatively large increases in earnings which are driving immediate demand supported by the strong cash reserves for outsourcing to reduce administrative costs.

Moving on to the outlook for our business, as a result of the sustained high employment that I just talked about we continue to see increased interest in eligibility services on the provider side and the immediate demand for additional outsourcing within the payer segment is mitigating any volume fluctuations that we may see as a result of lower claims from decreased utilization and higher uninsured rolls. States are looking at ways to accommodate not only the ongoing increase in Medicaid rolls which will continue to build in the interim years, but the increase that we will see in 2014 and beyond we believe this will continue to be promising for both our eligibility services within provider as well as the significant coming increase in plan membership on the payer side.

Providers will continue I think to look for partners who can help restore pre-recession viability to their operations which will increase market opportunities for our revenue cycle management offerings, we did see some backlogs in the ways from payers that impacted our provider revenue realization in the current quarter but we anticipate the majority of those to rebound in Q4.

So in summary the outlook for Healthcare remains positive with stable growth and favorable financial performance.

With that I will hand it over to Santanu for telecom and media vertical.

Santanu Nandi Thank you, Tom. Hello every one. In terms of telecom and media vertical, as you are aware that we cater to three market geographies, namely US, UK and Australia and we cater to all the various different segments within the telecom market, namely cable & satellite television, the wireless and the mobile segment, ISP segment, also the fixed line enterprise segment.

The revenue contribution by this vertical has been about 26% with a total employee population of about 6,718 spread over an overall seat capacity of about 4,800, utilization of 77%. And as you are aware we deliver to these market geographies from India, UK and Philippines.

In terms of the various trends that we see in the industry and the corresponding outlook, what we find is that the theme of vendor consolidation which emerged few quarters back, that continues to hold, though we find that the vendor consolidation process across the various clients are moving with varying pace. We believe that we are well-positioned to gain from this vendor consolidation process, primarily on the back of a strong operational delivery domain knowledge and track record, however, we do face some protracted decision-making cycle as in some of our key clients and that situation persists.

In terms of new customers sign up, we see that in certain market segments, there has been slower than expected new customers sign up, as the clients are focusing more in terms of doing the right level of provisioning, servicing and higher focus in retention of customers. And that obviously has an impact in terms of lower volumes in the existing business. However, when you look at the overall environment it looks promising with respect to new business addition and we have built up a fairly strong business pipeline across all the various segments.

We find that the companies are continuously exploring alternative models of transforming their operational models and such transformation of clients' operational model does provide opportunity as well as pose challenges. While you find that most of them continue to focus on outsourcing few do challenge their own thinking to evaluate in-house or captive options.

We also find this is in terms of trend in the marketplace that clients are beginning to explore integrated and optimized multi-channel customer interaction with the focus on optimizing cost as well as customer satisfaction. And there is an increasing thrust on the business value and innovation in delivery.

We believe that with the emerging channels such as the web chat and social media, we are very well-positioned because of our proven capabilities in the service channels and we expect to gain from this trend. Overall, we find that we are well-positioned to gain from the market trends, as we go into the next quarter.

With that I hand you over to Sanjeev Sinha to take you through the BFSI market trends.

Sanjeev Sinha Thanks, Santanu, and good afternoon, everyone. The BFSI vertical at Firstsource as you know, our markets are the US and the UK, and we deliver to these markets from the US, from UK, from India and from Philippines. We play in four key segments; Credit Cards, Retail Banking, Mortgages and General Life Insurance. This quarter our contribution to the company's revenues was 27%. We have just under 4,800 employees working out of just over 3,600 seats, which is a seat fill factor of 81%.

Let us look at the industry trends. We are seeing increased interest in outsourcing from financial services organizations in US and UK, so there are lots of meaningful questions and conversations there. You would be aware that in the US last year, a Financial Services Regulation Act was passed known as the Dodd-Frank Act and as part of that legislation; a Consumer Financial Protection Bureau was created. Currently, in the US, many of the organizations are trying to see what are the new kinds of regulations that may come as a result of this new body that has been created, so there is a bit of a wait and watch mode in terms of understanding the regulatory impact.

On the Housing side what we have seen is that in the UK the new mortgages that have been approved by the major banks have fallen further in December. In the US the home values are poised to grow by more than 1.7 trillion this year. We see debit cards overtaking cash for the first time in the UK and also in the US more debit cards were issued than credit cards in the current financial year. We also see a number of financial services firms gearing up for investments in Social Media.

Moving towards the business outlook for ourselves:

We have just taken over the Barclaycard UK operations in Teesside site, 700 employees have become part of Firstsource and this quarter we had two months impact of that revenue and from now on we will have a full quarter impact going forward.

We see significant interest from prepaid card issuers in the US. We already work for a couple of them and we see more of them interested in our services and that we see as a potential growth area. We see lenders grow in their credit card, auto and commercial loan portfolios over the course of the year. This is a welcome change because we had seen a contraction in this area in the last about 18 months, so now we see these portfolios poised for growth. In the UK with the interest rates expected to rise, we also believe that there will be demand for re-mortgaging as customers would move to fix their rates.

Moving onto the collection side of the business, we see liquidation rates continuing to go up even though volumes are contracting a bit. Credit card originations are on the rise again and this again is happening after quite some time, so while the account delinquency rates continues to fall and the consumers are showing a bit more discipline in their borrowing are the fact that more cards are being originated and the liquidation rates have gone up, is a positive. We do see, however, some pressure on commission rates from our customers in collection. Overall, we believe that we are poised for good fourth quarter and then strong growth in BFSI. Thanks and I will pass you on to Sanjay Venkataraman, the Head of the ABU vertical.

Sanjay Venkataraman Thanks Sanjeev and hello everyone. As you are aware the Asia Business Unit primarily operates in India and services out of India. And our primary segments are telecoms and media and BFSI. We contributed about 11% of FSL overall revenues in Q3 through a shade under 12,000 employees, operating out of about 8,800 seats and we are operating a seat fill of 73% right now.

Moving on to industry trends, we believe that some stability and some growth are being seen in the telecom sector in India, which is positive. We have also seen new services around Mobile Number Portability and 3G being rolled out, both of which are admittedly just a few weeks old. We have also seen the regulator bring in some very stringent guidelines around telemarketing and associated outbound calling. We have also seen the regulator in the BFSI space, especially in the insurance space, start issuing draft guidelines on outsourcing; this has been something that has been under debate and discussion for some time now. I think IRDA has now come out with draft guidelines which classify what can be outsourced and what cannot be outsourced for insurance companies. We believe this brings a lot of clarity to this whole scenario right now. And as you all probably aware we are also seeing a number of large third-party and combined BPOs showing increasing focus on the domestic market.

As far as business outlook goes, we continue to see very high levels of traction with our existing customers both in expanding current service lines which we service for them and offer for them to also adding onto associated new service lines, so we continue to see very, very significant traction with our existing customers.

We have also seen that the launch of the MNP, though it just a weeks old has led to a modest increase in volumes. So MNP is having an impact, though for the detailed assessment I think we will have to wait for some more time.

We also see the launch of 3G. And as 3G roll out spreads across the country with increasing number of mobile operators rolling out their 3G services, we believe this offers an opportunity both in the area of platform support, tech support and application support so we see the roll out of 3G as a clear opportunity. And we continue to stay focused on significantly driving operational efficiency within the Asia Business Unit. Thank you.

I would now request Matt to come back to give a view on the business outlook

Matthew Valance Thanks, Sanjay. I will just conclude with Slide #16, in terms of the outlook for the last quarter of the fiscal and we are expecting a strong performance in Q4, both in terms of our revenues and our profitability, and the reasons for that as we mentioned most of these points already but the main factors in Q4 we get full quarter impact in terms of revenue from the Barclays contract. We will have the usual seasonal uplift in our collections business within BFSI. We have had some delays in payments in our Healthcare business and we will see some normalization of the payment cycle in that segment of our company and continue to improve profitability in the Asia Business Unit. So, with that I will conclude the presentation and invite you to ask us some questions.

Moderator Thank you. Ladies and gentlemen we will now begin with the Q&A session. We have the first question from the line of Srivathsan Ramachandran from Spark Capital. Please go ahead

Srivathsan I just wanted your thoughts on one clear cut trend we have been seeing for almost three quarters in a row that standalone BPOs have substantially underperformed BPOs with integrated idea offering for the BPO of large IT services companies. It is not specific to Firstsource alone; we are seeing it across standalone BPOs. In some form, just wanted to know what is causing this and what are your thoughts and how do you see this shaping up over maybe the next 12 to 18 months?

Matthew Vallance I guess in terms of benefit that the integrated companies are getting from a sales point of view, perhaps getting some traction to effectively a sales channel perspective the leverage of existing relationships they have on the IT side. I still see that the service lines, IT and BPO service lines is quite separate and distinct and in that sense standalone BPO offering is still very attractive, and in some cases we are seeing ourselves getting invited into client situations where the client has a tradition of using IT companies who also provide BPO services, because I think that they are surprised to see the focus that independent standalone BPO business can provide in terms of company specialized purely on BPO, as I mentioned service lines are quite a distinct and there is not a great overlap unless you have a business proposition which is essentially driven of an IT platform and through platform base BPO offerings, relatively where in the marketplace I think if you look at the integrated IT and BPO companies, they are providing IT services, they are providing BPO services, there are pretty distinct service offerings. As I mentioned they are perhaps getting some benefits of synergy through effectively having a captive sales channel.

Srivathsan Because increasingly even if we have to see what Gartner or some of the larger research houses are seeing, even we have seen they expect platform-based players to go maybe double the rate of what is typical customer management BPOs growing. So the other thing that we are seeing is there is almost inability of standalone BPOs to grow beyond customer management, customer contact and to transaction processing in the B2B environment, just wanted to know what has your experience been?

Matthew Vallance We have a whole range of services that we offer beyond customer management essentially we focus the business predominantly along vertical lines, so we target segments in terms of the Telecoms, Healthcare, Financial Services on the vertical line. In terms of our horizontal service offering, we specialize in what you mentioned customer management, yes, we are strong in that area, we are also very strong in the receivables management and collections area in particular, I guess in response to your question we have a lot of strength and capability in workflow base document processing, so we have service lines that extend well beyond customer management although we think that customer management is inherently an attractive space to operate as a BPO company, on a global basis it is a very large base and it is growing. So we see customer management as a very viable space to operate in. But in addition to that we do have other service offerings and if we specialize in terms of our horizontal, in terms of the customer management, the receivables management, workflow base document and transaction processing and apply that to industry verticals that we understand well to telecom, healthcare, financial services, yeah, we believe that is a pretty powerful combination.

Srivathsan Sure. My last question is I just wanted to know in terms of your offerings in the respective end market, just wanted to know what are the new offerings that you are thinking that would expand your reach within existing customers and what kind of investments are going in some of these newer offerings.

Matthew Vallance Yeah, I think I guess it depends according to the segment, but for example, in the customer management space, that space is developing pretty rapidly in a number of ways and to be particular, that I have mentioned that we are quite successfully adopting, one is the increased use of multiple channels in customer management. And so essentially, customer management has moved way beyond call center environments. Its increased adoption of other channels, in particular, the web chat channel and so essentially using text based messenger type chat sessions, the companies to both sell to customer bases and deliver customer service to them and we are pretty well entrenched now. We have our own technology platform for delivering just that service, we have partnerships with external companies, where we partner to deliver chat services to our clients and that has been pretty successful. In addition to that, we have an expanding capability in the area of social media, so, we are seeing consumer-based corporations in particular, transforming the way they interact with that customer base by using social media and essentially not just listening to what is happening in the social media space they can react to customers and develop their products. But they are also using social media to communicate with customers. That's an area where we are developing new offerings. In the Asia Business Unit, another example would be in the area of

3G. We are adopting our service offering to be able to support the adoption of 3G services in India. We are doing some work in healthcare enrollment space as well.

Srivathsan Sure, thanks a lot.

Moderator Thank you. The next question is from the line of Lori Woodland from Ferox Capital. Please go ahead.

Lori Woodland How much is the total debt at this point?

Carl Saldanha We got an outstanding of FCCBs of $212 million which including accrued interest would be around $254 million and addition to that we have other ECB and term loans of $61 million. There is small component of about $8 million of other working capital related debt. So roughly 323 million gross debt altogether. We have cash balance of $80 million and hence net debt will be around $243 million.

Lori Woodland Okay. There has been a very large increase in the amount of cash over the quarter and as far as I can tell the change in receivables is about $15 million. Could you walk me through more specifically what some of the other drivers were that increased cash balance so much?

Carl Saldanha Actually what happened, if you look at the previous quarter, typically, in a quarter, we generate something between $8 million and $10 million of cash. What happened in the previous quarter there was a huge amount of receivables that we had not collected. So, in fact, in the last quarter, our cash actually dipped and it did not go up. So, a lot of that was the overhang of the previous quarter. So, overall, we added on $24 million of cash in the last quarter. Some of it was the overhang from the previous quarter, some are normal cash generation. And we added about $5 million of what we call a pre post shipment credit. So, there was a working capital loan of $5 million in there.

Lori Woodland Okay. That is fine. Those are all my questions. Thank you.

Moderator Thank you. The next question is from the line of Dinesh Kumar from Aditya Birla Money. Please go ahead.

Dinesh Kumar I have got few queries. First one this is the seasonally weak quarter or how many billing hours we lost in this quarter?

Dinesh Kumar Second question is regarding this Axis Bank deal, how much incremental revenue can we expect from this Axis bank deal going forward? And can you give a split up of revenue growth, that is in terms of how much is from volume growth, and how much is from pricing, if there is any pricing pressure and how much is from revenue conversion?

Matthew Vallance Okay, I will start you with that last question. All of the growth has come from effectively either new contracts or volume growth, but there has been no price compression has led to our revenues in this quarter. And in fact, for Axis revenues, we don't split our revenues by clients. And in terms of the billing hours it is not something we measure as such, but in Q3 as we come up to the holiday period in the US, in particular, there are less number of working days, so that is a factor that affected us essentially we are paying staff a monthly salary is actually less work time delivered, so that is the one of the seasonal factors we typically see in Q3.

Dinesh Kumar Okay, fine. Can you compare with Q2 and Q3, how much working hours we have in Q2 and Q3, how much we lost in terms of days or number of hours?

Mahesh Pratap Singh Dinesh, we follow various billing models, there are parts of services which are billed on time and material basis, there are parts of services which are billed on output transaction basis, there are parts of services which are billed on outcome or contingency basis, so we haven't tracked it in the way you are articulating, we don't have a number like-to-like because of the various mix of billing models being there.

Dinesh Kumar Okay, fine. Actually, can you give me an overall view of how US and Indian market is looking because in Indian market we are seeing a lot of new developments happening in telecom, on the Axis Bank deal also, we have signed two quarters before, so how much incremental revenue can we see from India domestic business?

Matthew Vallance Yeah, we are not going to go specifics, but I am going to ask, Sanjay to give his perspectives on how he sees the opportunities looking at a general level within the Asia Business Unit. Sanjay, do you comment on that?

Sanjay Venkataraman Sure, Dinesh, a couple of things are happening in this market. One, as I mentioned earlier is that we are seeing significant traction and winning new businesses from our existing customers. That's something which we are seeing having a very positive impact on the overall domestic business. Just to throw some light on your earlier question around Axis. We completed the ramps on Axis. So while we would not like to state exact revenues, this quarter we will probably see a complete contribution from the Axis Bank account coming through as revenue.

Dinesh Kumar That is Q4, you are saying?

Sanjay Venkataraman Q4 right. And as I mentioned we are also seeing at an overall level how these significant trends in telecom in terms of its MNP or 3G just opening up opportunities for us to increase our footprints or wallet share with our existing customers.

Dinesh Kumar Okay. Let it put it, say for another two or three quarters, this will have a severe positive impact on our Indian domestic business you are saying, this 3G and Mobile Number Portability, which happened in the first month of this year?

Sanjay Venkataraman Yes, it certainly will. All the new businesses booked and all these trends we are seeing will continue to have an impact over the next few quarters.

Dinesh Kumar Okay, what about margin split, margin side from domestic business; actually, it is breakeven, right, from this quarter?

Sanjay Venkataraman Dinesh, that is again something we are very committed to, very focused on. We made very encouraging progress in our path to improving margins in the ABU; we continue to forecast that we will be at or very close to breakeven in this Q4.

Dinesh Kumar In terms of PAT?

Matthew Vallance In terms of operating EBIT.

Sanjay Venkataraman We have been cash positive for some time now within this business.

Dinesh Kumar Okay, fine. And another query is about this Pipal research deal, the total amount is 12.8 million, right?

Carl Saldanha 12.75 is the sale price.

Dinesh Kumar So the actual amount is 580 million in terms of rupee, so we have 51% stake in that?

Carl Saldanha: There is amount of tax we have to pay after receiving that amount. Net of the tax and then you take 51%, and net of capital gain was $1.7 million. And also it is net of what we paid for it, five years ago.

Dinesh Kumar Okay, okay fine. That is all from my side. Thanks a lot.

Moderator Thank you. The next question is from the line of Dipesh Mehta from SBI Cap Securities. Please go ahead

Dipesh Mehta We have generated close to 24 million cash during the quarter and you provided some breakup like overhang of last quarter and Pipal and other things. So is the current DSO sustainable, DSO days? Second is, in results note we have mentioned Twin Lake Properties LLC, 80% is consolidated, so does this have any meaningful impact on numbers?

Carl Saldanha In terms of the DSO, I think we are right now at 58 days. We are actually trying to improve that, we are hoping to get down to 55 days or lower, so, yes we are trying to get our receivables lower.

Dipesh Mehta This Twin Lake Properties LLC has been consolidated 80% ownership with effect from April, so does that have any meaningful impact on this quarter's number?

Deep Babur No, no, that has no meaningful impact because that was essentially an option that we had just extended for $100 so there is no meaningful impact on the numbers at all.

Dipesh Mehta Okay, thank you.

Moderator Thank you. The next question is from the line of Subhankar Ohja from SKS Capital and Research. Please go ahead

Subhankar Ohja I just want to check a couple of things, one is, are you planning to pay back any of your debts with the cash that you have on hand?

Carl Saldanha We are not really going to be paying back any debts. The big outstanding is the FCCB as you know, and we are building up cash to payoff debt which is due in December 2012.

Subhankar Ohja That's almost two years down the line?

Carl Saldanha Yeah.

Subhankar Ohja I am sorry, I joined the call late but can you give the breakup of your total debt between FCCB and domestic, again?

Carl Saldanha The FCCB principal outstanding is 212 million. If you add on the accrued interest as of today it comes to 254 million exactly and in addition to that we have other debt from banks of 69 million so the total gross debts is 323 million altogether.

Subhankar Ohja 323 million?

Carl Saldanha Let me say that again, the outstanding FCCB is 254 million

Subhankar Ohja Including YTM?

Carl Saldanha Yeah, that's right, $61 million is other term debt, we have about $8 million in working capital loan and the total is 323 million.

Subhankar Ohja Okay, that is total debt in foreign currency and domestic and rupee?

Carl Saldanha We do not have any domestic loans.

Subhankar Ohja Okay, so it is all foreign currency loans?

Carl Saldanha Yeah, all foreign currency loans, yes.

Subhankar Ohja And what would be the average cost on this that you are expensing every year?

Carl Saldanha The FCCB is at 6.75% per annum, that is the interest rate on it, we do not actually expense that as you know, that will be happening later on. And on the other debt is currently around 8%, but we are working to reduce that

Subhankar Ohja So you are paying 8% cost on your dollar-denominated loans?

Carl Saldanha That is right.

Subhankar Ohja Okay. And are you hoping to get back on the dividend paying list anytime soon?

Carl Saldanha We have never paid dividend actually.

Matthew Vallance I think our priority clearly is to make sure that we put ourselves in a position to pay down the bond as and when it becomes due in December 2012, so that's our priority which is why we are accumulating cash reserves and in addition sizing that debt we are sitting on $80 million of cash and we expect some more to continue to accumulate that cash so that we remain in an comfortable position with regard to refinancing the FCCB when it is due.

Subhankar Ohja So the cash that you hold currently which may accumulate let us say $100 million in a quarter, what would the cash be yielding, are you keeping that in rupees or are you keeping that overseas in dollars?

Carl Saldanha No, no, the bulk of it is in rupees, we are investing in the local market, where currently we can get over 8% on term deposit.

Subhankar Ohja Okay, so you are parking it in money market and liquid?

Carl Saldanha Especially, bank deposits and mutual funds.

Subhankar Ohja Right, right. So you are trying to neutralize the cost of your debt overseas versus what you are earning yield on your cash balances here?

Carl Saldanha That's correct, that's correct.

Subhankar Ohja Okay, and would you be expensing the FCCB YTM next year in lines with the IFRS?

Carl Saldanha Yes, if IFRS do come into effect. We will have to, yes.

Subhankar Ohja So, what would be the likely impact on your reported earnings of that in the next year?

Carl Saldanha Basically 6.75% into $212 million, which is roughly $13 million.

Subhankar Ohja Okay.

Carl Saldanha So net of tax will be lower than that. The absolute interest rate will be 6.75% into $212 million

Subhankar Ohja Right.

Carl Saldanha So the absolute effect will be $13 million, but we will get a tax break

Subhankar Ohja Post tax will be lower?

Carl Saldanha So that the actual amount will be lower.

Subhankar Ohja Okay, okay. Have you given any kind of guidance for the next quarter or year or anything like that?

Matthew Vallance We are not giving guidance but we have indicated that we expect Q4 to be a strong quarter for us, some good fundamental momentum, we have, for example full quarter of the work that we do on the new Barclays contract we signed, we normally find seasonal benefits in Q4, we will get some uplift from our collections business that normally has a strong Q4 and we have some delays in revenues and in our Healthcare business that we expect to normalize, primarily for those reasons, we expect to see a strong Q4.

Subhankar Ohja Okay, all right, thanks very much.

Moderator Thank you. The next question is from the line of Mohit Jain from Alchemy. Please go ahead

Mohit Jain Just one question on your seat capacity. Does this include 700 seats being transferred on Barclays account?

Matthew Vallance No, it doesn't, that's excluded.

Mohit Jain So it should be 20,844 plus 700, is it correct? I am on Slide #6.

Mahesh Pratap Singh Mohit, right now, we have assumed operations "as is" from Barclaycard's existing center. We don't own those seats. As we start to transition those programs in our premises, those seats will come in consideration, and a big part of that is already in the number that you are seeing 20,844.

Mohit Jain So it includes a large part of 700 employees?

Mahesh Pratap Singh Yeah, employees are included in the employee count we have reported, but the seats are technically owned by Barclays, so there is no seat count on that account in 20,844.

Mohit Jain Okay, got it, so your employees are over seated, in a sense it includes 700 Barclays employees being transferred to Firstsource.

Matthew Vallance The Barclays staff is on our payroll but the seats are not counted, because the seats we are using at the moment are the Barclays seats, but they will transfer over on to our seats over the next two quarters.

Mohit Jain You will be taking on those seats in the coming quarter?

Matthew Vallance Yeah, we will be taking on some more seats. We already have some of the facilities created for that, but we will need to create some additional within the existing centers that we already have.

Mohit Jain And second is again on seats, you reduced 31 seats during the quarter, however, your revenue growth looks stronger, good enough, so what was the reason why we had to cut number of seats in the quarter?

Matthew Vallance No, no, what happened was that two centers went away on account of divestment of Pipal, and we added one center to accommodate expansion in our Asia business, so net effect of those two things is a reduction of 31 seats.

Mohit Jain So Pipal was also counted in terms of seats?

Matthew Vallance That is right. Yeah, exactly.

Mahesh Pratap Singh But that is not there in the closing number you are seeing now as Pipal deal was concluded during the quarter.

Mohit Jain I am sorry, that is not there in the closing number?

Mahesh Pratap Singh That's right, Pipal seats are not in the closing number. But when you see reported previous quarter seat capacity, Pipal seats were considered in those numbers.

Mohit Jain Okay and can you give me the number of seats which you reported in the last quarter on account of Pipal?

Mahesh Pratap Singh That would have been roughly about 300 seats, somewhere there about.

Mohit Jain So if I have to compare Q2, I should exclude 300 from last quarter's number?

Mahesh Pratap Singh Yes.

Mohit Jain Okay, thank you, that is it from my side.

Moderator Thank you. The next question is from the line of Rakesh Tarway from Motilal Oswal. Please go ahead

Rakesh Tarway Just wanted to know what are the employee's onsite, basically in UK and US not Manila?

Mahesh Pratap Singh That number would be 5,922.

Rakesh Tarway That includes the Barclays. Guys on the Barclays project?

Matthew Vallance Yes, it does.

Rakesh Tarway Okay, 5922 right sir?

Matthew Vallance That's right.

Rakesh Tarway Thanks a lot, sir.

Moderator Thank you the next question is from the line of Shweta Malik from Marwadi Shares and Finance Limited. Please go ahead.

Shweta Malik My first question is to the Barclays seats. Now that you have mentioned that the seat capacity is not added in the current BFSI vertical, so going forward will there be any transitioning cost that you will be incurring on the same?

Sanjeev Sinha There would be some transition cost but those were factored into the deal at the beginning itself.

Shweta Malik No more transitioning cost would be incurred thereafter?

Sanjeev Sinha No, the transition will continue on for several months and therefore, cost would be incurred; it is just that those costs have been factored into the overall economics of the deal.

Shweta Malik Okay, my second question is the Indian domestic business, on an absolute basis, if you see the business has grown, I mean it has slacked, it is 56 crores in this quarter compared to the last quarter, so despite the initiation of the Axis Bank deal, are we facing pressure on the telecom volume side?

Sanjay Venkataraman If you notice, also we have added on employees last quarter, on the back of visibility from our existing customers. We also completed the Axis Bank ramp last quarter in Q3. You will begin to see the impact of all these additions in Q4. So we are forecasting revenue growth for the vertical in Q4.

Shweta Malik Okay, and now that you have given that industry trends in the Indian business of the regulations and all. After closing in the Axis Bank deal as well, how are the new deals, are we seeing any kind of deal traction in the BFSI segment for the domestic business?

Sanjay Venkataraman More than restructuring, I think especially if you look at the insurance sector I think with the publication of the IRDA guidelines which are draft right now, measure of certainty will probably come in as to what can be outsourced and what cannot be outsourced. And if you look at the draft guidelines today, customer service and all voice-related activities of servicing customers are classified as non-core, which means insurance organizations can potentially outsource those, so we believe with some certainty coming into what can and cannot be outsourced. And with the whole industry increasingly beginning to embrace the efficiencies and effectiveness of outsourcing, the outlook for the sector is very, very bright. So we continue to stay engaged in the sector, we continue to scout around for opportunities in this sector and we are beginning to see the impact of that on our pipeline.

Shweta Malik Okay, thank you, sir.

Moderator Thank you. The next question is a follow up from the line of Srivathsan Ramachandran from Spark Capital. Please go ahead

Srivathsan Just wanted to get your comments on two specific things, almost two months down, how do you see the collections business doing this quarter? It has been a seasonally strong quarter, just wanted your thoughts on whether we could see some amount of positive seasonality coming in this quarter?

Sanjeev Sinha Yes, Q4 is the tax season in the US and traditionally it has been a strong quarter, we expect the same this year as well.

Srivathsan Sure. And just wanted to get some idea as to the kind of order bookings we have had, maybe over the last six months, how do you kind of look at that vis-à-vis maybe six months back or on a year basis and what kind of growth we see in an absolute bookings?

Matthew Vallance Yeah, I do not have any specifics for you but what I can say is that our pipeline as we exit the Q3 was quite robust in most places so that gives us some confidence as we start to move into the next fiscal year.

Srivathsan Okay, and just wanted your comments on margins at this point of time, this year we have anticipated some amount of margin expansion whereas if you have to see YTD financial year '11 versus '10, we are flat, so just wanted to know whether we would be in line to achieve or maybe slightly below the targeted margins we are looking for FY11 and what is your outlook for FY12 margins?

Matthew Vallance In terms of our margins, we are relatively steady compared to last fiscal. Yeah we do see some opportunities for margin uplift through a number of reasons. One is, operating efficiencies, see some potential to up margins as our Asia Business Unit turns around from the negative operating profit, and as we see enhanced profitability in other areas including our BFSI business, there are certainly opportunities that we see for margin expansion as we move into next year. I mean there is notwithstanding that there are headwinds around the currency that may amount to some pressure, but on the whole we expect margins to expand.

Srivathsan Sure, thank you.

Moderator Thank you. Ladies and gentlemen, that is the last question. I would now like to hand the floor back to Mr. Matthew Vallance for closing comments. Please go ahead

Matthew Vallance Yeah, thank you for joining the call. Thank you for your questions. Just to reiterate I think we have had a solid progress over Q3. We have grown by 2.3% quarter-on-quarter over Q2 and in constant currency terms, posted a 5.1% growth, our profitability has declined slightly, but it has been relatively stable on EBIT basis and we expanded on our profit after tax basis. We generated cash strongly and added $24 million in terms of cash balances. We have seen the reduction in our attrition in most parts of the business, so our staff retention has improved quite significantly, and we have seen addition to our employee strength, which is a signal for further growth. We expect Q4 to be robust and the growth will continue into the Q4 because it is seasonally a strong quarter for us in any case, plus we have additional business coming in from new contracts, in particular Barclays, so we had a good quarter, it has been on a constant currency basis been the best quarter's growth in seven quarters and we expect to see that continuing into the next quarter. Thanks very much for joining us. I would like to thank my colleagues as well.

Moderator Thank you gentlemen of the management. Ladies and gentleman on behalf of Firstsource Solutions that concludes this conference call. Thank you for joining us and you may now disconnect your lines.