Q4 FY2012 Earnings Call Transcript – May 16, 2012

CORPORATE PARTICIPANTS:

- Mr. Rajesh Subramaniam – Managing Director and Chief Executive Officer
- Mr. Dinesh Jain – Joint CFO – Financial Control
- Mr. Deep Babur – Joint CFO – Corporate Finance
- Mr. Yash Gadodia – Christensen Investor Relations

Firstsource Solutions Limited
Quarter Four Earnings Conference Call, Financial Year 2012
May 16, 2012

Moderator Ladies and gentlemen good day and welcome to the Firstsource Solutions Limited Q4 & Full Year ended March 31, 2012 Earnings Call. As a reminder, for the duration of this conference, all participants' lines will be in the listen-only mode, and 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 '*' followed by '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 Yash Gadodia from Christensen Investor Relations. Thank you and over to you.

Yash Gadodia 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 for the Q4 and full year ended March 31, 2012 earnings call for Firstsource. Please note the results, fact sheet and the presentation has been mailed to you and you can also view this on our website, www.firstsource.com. To take us through the results and to answer your questions we have with us today, Mr. Rajesh Subramaniam – our Managing Director and CEO

Yash Gadodia Rajesh Subramaniam, our Managing Director and CEO.

Rajesh Subramaniam Hi everybody

Yash Gadodia Our newly appointed Joint CFOs – Mr. Dinesh Jain, Joint CFO – Financial Control who will be responsible for Accounting, MIS, Financial Planning and Analysis, Pricing, Tax, Treasury Operations and Procurement

Dinesh Jain Hi everyone

Yash Gadodia Deep Babur, Joint CFO – Corporate Finance, responsible for Finance Strategy, Fund Raising, Liability Management, Investor Relations and Corporate Development.

Deep Babur Hi everyone

We will be starting this call with a brief presentation providing an overview of the company's performance followed by a Q&A session. I would like to remind you 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 uncertainties and the risks we face. These uncertainties and risks are included but not limited to what we have mentioned in our prospectus filed with SEBI and subsequent Annual Report which you can find on our website. With that said, I would now turn the call over to Rajesh Subramaniam, our Managing Director and CEO.

Rajesh Subramaniam Thank you. Hello, everybody. The first section I am going to be covering is our Q4 highlights for the period Jan to March 2012. Q4 revenues came in at about Rs. 6,218 million, reflecting a Q-o-Q growth of 7.8% in INR terms and 8.7% in constant currency terms. This has largely been on account of revenues from clients that went live in the latter part of Q3. We got the benefit of a full quarter earnings, especially from a couple of our T&M clients. Also, Q4 is seasonally our best quarter in our Collections business because it is the tax refund season in the US, so both the liquidation rates and the placement inventory is normally at its highest in Q4 and there is seasonality in our Healthcare Provider business which gives us some uplift in both revenues and margins. On a Y-o-Y basis, our revenues grew 13.8% in INR terms and 5.7% in constant currency terms.

Now, let me just touch upon our margins. In Q4, we had 150 basis points improvement in our operating margins from 3.5% in Q3 to 5% in Q4. The element of seasonality flow down to our bottom line, so that helps us in an uptick in our margins plus, in the past I have articulated that we have changed the structure of our business, we have realigned our business to the realities of what our business model should be to drive optimum efficiencies, both in terms of cost and delivery. So, this has resulted in significant cost savings that has helped us drive some margin expansion this quarter but the full benefit of those we will get to see in FY13 as the actions that were taken have a certain cost associated which has been earmarked in the financials, both in Q3 and Q4. We have also had some ramp downs in our international business, the effect of which we will feel over the next two quarters but volumes did come in lower and even in our domestic business we saw marketing budget freeze of some of our Telco clients which ensure that the volumes came in lower than what we thought it will be. But despite those setbacks we managed to improve our margins by 150 basis points. We have managed to build up our cash close to about $150 million, actually from levels of about $130 million in the previous quarter. So, it has been a strong cash flow accretive quarter for us. We have also generated cash from better working capital management and also we have availed a post-shipment credit.

As on 31st March, 2012, we had 30,086 employees. 21,601 are based in India and 8,485 employees are based outside of India. The net reduction of 35

employees compared to a net reduction of 255 employees in Q4FY11 and net addition of 830 in Q3FY12. Now, it is heartening that we have got a significant revenue increase which has been helped by seasonality but some of the productivity measures we have driven have managed to drive revenues without adding a linear number of employees in the business. So, that will give you a sense of some of the measures that we have taken to start driving margin expansion going forward. Attrition has spiked a little in both the offshore locations and in the domestic business. Offshore increased by close to 300 basis points from 56.4% to 59.4%. Domestic increased from 88.8% to 95.9%, while onshore reduced by about 370 basis points from 37.7% to 34%.

If I take you to Slide 6, it gives you a little bit of our capacity and utilization. Today, we have about 24,243 seats worldwide. We added 656 seats during the quarter. We delivered out of 48 delivery centers, which is the same as on December 31, 2011 because we added one center in the UK and we reduced one in India. Our seat fill factor which is defined as seat in production even if a seat is in production for an hour, it is counted as a seat which contributes to my seat fill. About 74% on 31st March compared to 75% on December 31st. The average seat fill factor for Q4 is at 75%.

On our hedges, outstanding FX hedges is at $33 million, £49 million and AUD15 million. For the next 12 months which basically would cover all of FY13, 93% coverage are with rates at about USD 51 approximately, the Pound is at about 80 levels, and the Australian dollar is at 50 levels. For the next 12 to 24 months which basically will cover FY14, we have an overall 51% coverage with the USD at about 54 levels, GBP at 87 and the Australian dollar at 52.

Some of the other elements in terms of how we derive our business from geography vertical and delivery perspective. By geography, US continue to be the largest geography. It contributes about 50% of our revenues. The UK follows, second at 30%. And India and Australia contribute about 20%, where India contributes predominantly the larger element.

If I take a look at by verticals, the T&M vertical is my largest vertical. It contributes about 41% of my revenues because it includes a lot of my domestic clients won are also telecom and media clients, if I add that it comes to about 41%. My Healthcare contributes 34% and BFSI 25% and 1% contributed by other small work we do such as publishing and others.

By delivery location, onshore is about 65%, offshore is about 24% and domestic is 11% as on Q4FY11. For Q4FY12, 65% has increased to 67%, 24% is reduced to 22% and 11% has stayed flat.

From a client concentration perspective, my top client contributes 13% in Q4FY12 and top five clients 40% of our overall revenues.

So, in terms of the highlights for FY12, our FY12 revenues came in at about 2,255 crores, which is basically Rs. 22.5 billion. Y-o-Y growth of about close to 10% in INR terms and 5.8% in constant currency terms. The growth has been driven in the Telecom & Media and the Financial Services Customer Management segments of our business. We also had setbacks. We have had client losses and softness in some elements of our business both in the offshore businesses, domestic businesses and in our BFSI Collections business. So, overall operating EBIT margins at 4.2% are lower by 550 basis points compared to FY11. FY12 has been a bad year for us, at least the first three quarters, has seen profitability levels lot muted compared to where we were in the FY11 levels and to set the context of what are the corrective measures that we have taken to set this right and get the company back on track to a margin profile which has been at historical levels. To set the context, I believe that we verticalized too far to the right of center because we slipped both sales, marketing, solution design and service delivery aligned with verticals which I believe has resulted in a significant duplication of cost as the businesses that we have undertaken have become a lot more complex because we deliver from multiple geographies and we have customers in several geographies with different requirements. So, this causes to build excess capacity both people and in terms of technology cost which basically variable cost became very, very ungainly sunk cost. This is something which is in our control, which we should have controlled better but obviously, it did take a big erosion in our margins. And obviously, the Collections business has had a very challenging year. There has been significant erosion in profitability, especially because the macro-economic condition in the US suggests that the inventory of charged-off debt is shrinking, the economy is going through a process of deleveraging, and consumers are using cash, debit cards more than using credit cards. This has ensured that new card issuances and origination of new cards has completely taken a very different trajectory to what the US economy has been used to and if card issuances slacken, then inventory of charge-off debt takes about six to nine months to build up into inventory which then gets placed to a collection company like ours which also has seen a significant shrinkage. While we continue to support our clients, we believe when the turnaround occurs we will be ideally positioned to gain market share, we are driving certain cost disciplines which will ensure that if

the business environment gets harder, we are positioned to normalize cost rationalization to support a certain level of profitability that is required.

Also in FY12 a slight ramp down which occurred latter part of FY11 but went into FY12, exposed certain inefficiencies in our service delivery, governance structure, which again ensures that the cost rationalization aligning to a client ramp down was not at the speed as what it should have been which ensures that our margin erosions which were evident from Q1 became a reality. So, what did we do to fix it. The fix was in terms of verticalizing sales and marketing functions because it is relevant to build domain and capability in terms of what the market demand for services in the specific industries are. I cannot have generalist running sales functions, we need specialists with domain to go and talk the language of the clients, so we have segregated our sales teams in verticals and then we created a series of horizontals which then define the ability to build scale and economies of scale driven by geography, delivery in terms of horizontal. So, today, we have segregated horizontals into three lines. We have customer management; we have collections and transaction processing. The vertical effects are around T&M, BFSI and Healthcare. Healthcare truly remains a verticalised structure because a large part of our transaction processing engine sits in our Healthcare business, it is platform-based, completely transaction-based pricing model, and the business has a different rhythm to be at the customer management and collections business and the business which truly is for us defined as a vertical. The customer management business is segregated across Asia which includes, Philippines, Sri Lanka and India and UK and US, where we have customers for whom we do the entire customer lifecycle management and these businesses largely are centered around T&M and BFSI. So, now, I have a single point of accountability for Asia which is I have a president who manages that business and I have a single point of accountability for Europe and US, a gentleman by name of Sean Canning who manages that business for us. So, now, I think we have created the right governance structure in terms of driving accountability, both from a horizontal perspective and from a vertical markets perspective, which in turn has enabled us to rationalize significant elements of our G&A costs, significant element of our gross margin cost, including facility rationalization, span improvement, support cost rationalization, all of whose benefit we will start to see coming through in FY13, some benefits obviously we did see in Q4 but the larger benefits we will continue to see through margin expansion in FY13.

On our client side, we announced that we had signed about $160 million of TCVs with three significant Telecom & Media clients. One is an existing client that is likely to double its partnership with us over the next year. The other two

are new wins; one from Australia and the other one from Europe which will enable us to drive a certain level of growth over the next couple of years which we believe will be better than industry growth rate or at least the top end of the industry growth rate. So, these three year deals of a TCV about $160 million and more often than not we have seen that these clients from the baseline of where we start, the growth which they end up in those three years are normally much higher than the TCV that we signed up for. So, we are very excited about these three deals. And the other development in FY12 is the joint venture we signed with Dialog in Sri Lanka.

Coming to the favorite topic of our FCCB and elements of it. The outstanding FCCBs as of 31st March were close to 170 million. The accreted value of which is about 237 million. During the year we raised $180 million of foreign currency loans which helped us repay some of our existing ECBs and foreign loans and the rest of which we use to augment our cash to repay our FCCB payment in December. And in Q2 and Q3, we bought back $42 million of face values of bond for which cash was used at the RBI prescribed discount. Net of these activities, the outstanding accreted value of a bond is 237 million which is coming up for repayment in December. Currently, the company has built up cash of about $150 million and in the ensuing year free cash flows will add up to help us mitigate the gap between the March 31st closing and the accreted value of the repayment. But some in substance, the net gap we still see a gap of about 65 - 70 million, the same guidance that we gave last time on the previous quarter's analyst call and we have multiple strategies in place to evaluate how we will mitigate this, as time progresses over the next six months.

From an employee executive appointment perspective, two of my colleagues have been elevated as Joint Chief Financial Officers of the company. Dinesh Jain will be in charge of Financial Control, he will be responsible for Accounting, MIS, Financial Planning and Analysis, Pricing, Treasury, Tax, all the internal finance elements of a company and I have known Dinesh for the last ten years, he also having worked with me since the early days of this company. Deep Babur will be in charge of Corporate Finance, responsible for Finance Strategy, Fund Raising, Liability Management, IR and Corporate Development. Deep again is a ten-year old employee of the company and he joined the company in his very early years and I have known Deep for over now ten years, so I believe I now have the right structure of managing the whole finance functions and the complexity that are emerging in our businesses between the two gentlemen who have taken joint responsibility of the finance function.

As I flip you to the next section which is financial performance, I will hand it over to Deep to take you through the financial performance of the company.

Deep Babur

Thanks, Rajesh. Rajesh has walked us through the background and really the context of the numbers. This is just a table that is laying the numbers out. Our revenue from operations this quarter were at 622 crores, which is 7.8% higher than our previous quarter of 577 crores, about 13.8% higher than the same quarter the last year, of which we generated 546 crores. Our operating EBITDA has grown from 43 crores in Q3FY12 to 53 crores this quarter and in margin percentage terms that is a growth of 100 basis points from 7.5% to 8.5%. The corresponding number the previous year was 79 crores at 14.5%. At the operating EBIT levels, it is a 55% improvement from 20 crore we generated in the last quarter and 150 basis points improvement from 3.5% to 5% this quarter. Corresponding number the same quarter the previous year was 56 crores at 10.2%. Most of the line items between the operating EBIT and the profit before tax or rather all the way down to the PAT are fairly consistent with the last quarter with the exception of the loss on FCCB buyback which we have not done any further in the last quarter, hence, there is a gain/loss on account of that. Our PAT, we have generated 23 crores in Q4 as compared to 7 crores the previous quarter and 38 crores the same quarter the previous year. From an EPS standpoint, it is 54 paise on basic EPS and on a diluted basis 53 paise.

Moving on to the Slide 14, which lays out the full year performance, the revenue from operations has grown from 2,055 crores in FY11 to 2,255 crores in FY12, which is a growth of just under 10%. The operating EBITDA has fallen from 290 crores to 185 crores, a 36% drop and in margin terms 14.1% going down to 8.2%. EBIT was just slightly over 200 crores last year at 9.8%, which are now 96 crores at 4.2%. In terms of the line items between operating EBIT and profit before tax, we had an extraordinary expense of 6.4 crores which doesn't have a repeat this year. The other income has fallen from 14 crores last year to 6 crores this year. Interest expense has fallen from 21 crores last year to 7.6 crores this year. This is largely a function of the fact that we raised 180 million and essentially used that to refinance existing loans which were at higher rates of interest. The amortized cost on fair value of FCCB is largely flat from 13 to 14 crores. The slight exchange gain on the foreign currency loan which is under a crore last year is about 3 crores this year and the loss on the FCCB buyback which is 7 crores this year, there was not any buyback done last year, hence no entry against it. At a PAT level, it is 139 crores of last year has fallen to 62 crores in FY12, 6.7% falling to 2.7%. On an EPS basis Rs. 1.44 on both basic as well as the diluted level.

Rajesh, if I could request you to take everyone though business outlook. Thanks.

Rajesh Subramaniam In terms of an outlook segregated into revenue and margins, the full year impact of our recent wins will continue, will give us momentum. We are seeing existing clients' volume growth. We are also seeing existing clients' volume softness because that is a way of our business, ramp-ups and ramp-downs are a way of our life. So, net-net, we believe that the industry is expected to grow between 11 and 14%, we should be at the higher end and if lucky beat the higher end of the industry growth rate expected for FY13. The momentum from T&M is ably supported by Healthcare. We have a stable growth in our Provider segments and we are expecting significant growth in our Payor business on the back of the requirements driven by Healthcare reforms in the US. Our BFSI business will have a muted growth both from a vertical perspective and from a horizontal perspective, because horizontal is the largest footprint of our BFSI sits in collections and I have spoken about the issues about the reduced inventory of charge-off debt in the US which is continuing to impact the business. So, we are facing headwinds in that industry but between T&M and Healthcare we believe our growth rates will be robust as we look into the horizon of FY13. On the operating margin, the worst of our financial performance is over as on Q3. Q4, you have seen our margin expansion by 150 basis points. These margins as we go into the future will improve on the back of the measures that we have taken which I alluded to earlier in the call plus and the fact that with a higher revenue growth, there is a non-linearity in my margins because my fixed cost would not grow at the speed at which my revenue grows. So, that will see my margin expanding too. So, while we do not give any specific guidance on our margin, the only comfort I can give you is that we will see a significant uptick in our margins between FY12 and FY13 and as much as the depreciating rupee affects my loan book and repayment of my FCCB, it helps me in building my receivables book and covering my exchange rate at levels which will definitely help me in my margin expansion.

So, if I have to sum it up for FY13, it will be a much better year both in terms of revenue and profits. For Q1, despite the fall-off of seasonality, both on our revenues and profits, we expect a flat to positive revenue growth with marginal improvements at the operating margin level. So, that will signify the communication and the messages that we have been giving out for some time now and how they play themselves out into in our numbers.

Moderator Thank you. We will now begin with the question-and-answer session. The first question from the line of Kunal Tayal from Bank of America-Merrill Lynch. Please go ahead.

Kunal Tayal Rajesh, firstly, if you could just talk a little more about the deceleration in some portions of the international business that you mentioned. Was it essentially slower than expected seasonality in Collections or was it something else as well?

Rajesh Subramaniam It is a great question, Kunal. The tax season has been very short this year. So, the tax season normally commences in Jan and ends pretty much in the early to mid part of March. This time a) the tax refunds came in late, so it did not come in the early part of Jan, it came in later part of Jan. Feb was a significant tax season month. We did really well in Feb but the tax season ended very quickly. So, if my tax season in Q4 of FY12 was in line with the tax season in Q4 of FY11, both my revenue and margin would have definitely been higher. So, there is a deceleration that we are seeing in the Collections business which is a function of the inventory.

Kunal Tayal So essentially it was the collections spill over from Q4 into maybe next quarter to some extent?

Rajesh Subramaniam No, the tax season is over. So, there is no spillover from collections into Q1. Now, in Q1, all the uptick I got in the shorter tax season that I have falls up completely in Q1.

Kunal Tayal Then just moving on to the ramps in a couple of deals that you had won in Q3. Was there a surprise either way in terms of speed of ramps?

Rajesh Subramaniam No, the speed of ramps were as anticipated because one is a lift out deal where we have taken over a customer's operations and then we manage going in and putting in our people, processes platforms, then drive a certain level of efficiencies that some of which we keep and some of which we transfer back to the client. So, one of the lift out deals have worked out very well for us. The transition was smooth, the processes were good in place, the base lining that we did, and everything came out just as on plan. So, normally, when it moves from an excel spreadsheet to actual, we normally see a deterioration but in this case I am happy to say that we came in very well in terms of how this transition happen and how the ramp happened. As far as the other ramp which we spoke about, one was from an existing client, so there was not much of a learning curve that we had to go through because we are already working for that client with significant scale both in India and in the

UK. So, the growth of the business was in addition to the existing lines. So we were able to manage it at the level of efficiency that we currently manage that business from. So, from a ramp perspective between what we took over and what we started in Q3 and in the benefit which I got in Q4, there have been no negative surprises.

Kunal Tayal Any pointers in terms of what your early stage pipeline looks like currently?

Rajesh Subramaniam Pipeline looks very good, Kunal. My Telecom and Media pipeline looks extremely robust. We are seeing an increased activity in Europe. The kind of deals that I am getting a seat of the table even across the Nordic countries is phenomenal and T&M as a vertical, I am extremely bullish on, again going into the next couple of years. Healthcare Payor side, thanks to the reforms, thanks to the standardization that the reform requires of Payors, be it in the disease codification or in terms of HIPAA compliance is seeing a huge amount of exception handling in the adjudication which is coming down our path and these are extremely high profitable businesses because the customer is going through significant elements of pain which is helping us drive growth and this is expected to continue over the next couple of years. For me the T&M business and the Payor business are my stars. Provider business has always been a stable business, in a good year it has grown at 10%, in a bad year it has grown at 5%. We expect that business to be stable and grow at those levels and that is the significant profit generating unit for me, given our relationship with our client and the impact we make for them. BFSI collections we are watching the environment, we have projected a muted growth in the collections business, but the macro environment directly affects us and the only thing that we can do is in case there is deviation to our stated forecasted goals for FY13, we just have a mechanism of adjusting the cost structure to ensure that at least from a percentage margin basis I remain whole and I cannot protect the dollar depletion of margin given the lower revenues that would come. So I hope that gives you a sense of how we see the pipeline in the three of our businesses.

Kunal Tayal Last question from my side, in terms of your margin trajectory for FY13, you did mention that Q1 should be maybe at Q4 levels, thereabouts because some headwind from seasonality coming off. But other than that it should be a secular improvement through the quarters of FY13?

Rajesh Subramaniam Absolutely, Kunal.

Moderator Thank you. The next question is from the line of Srivathsan Ramachandran from Spark Capital.

Srivathsan Just wanted your comments on the $160-odd million of deal flow that we have been winning. How would you comment on the margins of this deals that you have been winning, would you kind of on a steady state basis would this grow back, historical levels of 8, 9% EBIT margins or these reserves, substantially a lower margins business?

Rajesh Subramaniam The $160 million businesses, the EBIT margins are highly accretive to my FY12 EBIT margin of 4%.

Srivathsan That is possibly the lowest level I think I have seen compared to last six years?

Rajesh Subramaniam Exactly. It is hugely accretive to the levels that you have seen in FY12.

Srivathsan But below historical levels?

Rajesh Subramaniam Some of the deals are higher than the historical numbers, so if I take a look at a weighted average basket there might be about I would say at best 100 to 150 basis points lower than my historical highs of 10-10.5%.

Srivathsan In terms of the FCCBs just wanted to know what is the overall plan at this point of time, if the rupee behaves the way or stays where it is, just what kind of shortfall you will be having in terms of when you had to repay in December 2012?

Rajesh Subramaniam At the rupee level of 50, we are looking at a gap of 65 million. Every one dollar appreciation increases my loan book by $3 million.

Srivathsan So at 53 you would be more like 74 million?

Rajesh Subramaniam That is right.

Srivathsan And in terms of the hedges for FY14, I was just curious why are you hedging FY14 at all, given that you have far higher ECB and interest payments, I do not think you will have enough cash flows to hedge at. Just wanted to know what is your overall rationale for hedging?

Rajesh Subramaniam The dollar level is about 45%, the pound level is higher. So, we are working through the math of whatever is our interest, our interest repayments are service out of US cash flows, our principal repayments is where we need to find the dollars and remit to pay those money. So, to that extent, we are managing our liability in a way that I get an automatic hedge for the receivables book that I have in dollars. So, you should realize that a lot of my

receivables booked in dollars are a lot more muted compared to my pound book. And we do not do a cost like hedge between the pound and the dollar. We do a straight rupee dollar and the rupee pound. So, from a dollar perspective, absolutely, yes, what you stated is right, but as every analyst out there is giving a different range of the dollars, the dollar is a joker in the pack as we look at our redemption of our FCCB. Every rupee puts us out by $3 million. So, we are talking to our existing lenders and we are coming out with a clear strategy as to how we address this deficit and yeah, in between the accretion to our cash flows and the other conversations with our lenders, I am sure we will be able to overcome the $237 million liability on the 4th of December.

Srivathsan My last question, 65 million gap funding, what are the options for if you look at maybe in ECB, your term loan go back to same lender, just wanted to know what are the options?

Rajesh Subramaniam All of the above.

Srivathsan Any thoughts on the tax treatment of the same given that we are going to pay, we have not had tax shield on this large sum, so just wanted to know what could a tax treatment be, what kind tax rate for FY13?

Rajesh Subramaniam There is no withholding tax…

Srivathsan Not for withholding tax, from an income tax shield point of view given that we have not taken benefit of this income tax, does not allow you to take benefit of zero coupon bond till you make the interest repayment. So, in FY13 we will make the interest payment. So just wanted to know whether it will be a far lower effective tax rate for us?

Rajesh Subramaniam Absolutely right.

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

Dinesh Kumar One is about domestic business. I just want to get a clarity on how this domestic business, ABU unit is performing especially when the Telecom sector is not doing well. My second query is a little more clarity on the FCCB outlook. Again, even though you mentioned about in the last call, out of 65 million, so are you looking for this ECB kind of, what exactly our plans?

Rajesh Subramaniam First question, on the domestic business, Q4 has not been a good quarter because Q4 we have seen a lot of the telcos basically cut back on their

marketing budgets which has a direct impact on the business that we handle for them. So, obviously we are looking at how we correct that in Q1. So despite all these setbacks the positives have helped us manage our margin profile to what we have exhibited. So, domestic business is growing top-line currently and the top two clients that we work for are profitable accounts for us. There are some clients where we do not make as much money that we can on a capital recovery basis. So, for those clients we are going back with price increase request and in a very disciplined manner we will have the ability of walking out of account if they do not make money for us this year. On the second question of 65 million, we have multiple options that we are evaluating in helping us fund the gap, I am not in a liberty to discuss what they are, but we are evaluating all options both from our existing lenders and from new lenders and also we are internally looking at how we can generate more cash which will be aided by a significant reduction in our net current assets and looking at other sale and lease back options for our assets. So we have multiple options that we are playing out with the intent of ensuring that we repay the $237 million in December this year.

Dinesh Kumar One more question on domestic business, actually last year Q2, we saw significant ramp-up happen in Indian business, right?

Rajesh Subramaniam That is right. We added about 3,000 people.

Dinesh Kumar So still that business is growing or you are saying some kind of ramp-up because most of the telecom companies are doing that much play?

Rajesh Subramaniam If you take a look at my Q3 numbers, my Asia Business Unit business did very well. The cost of ramp in Q2 translated into revenue and into profits in Q3. In Q4, given their own profit management requirements, they cut back on budgets, which basically meant they went low on their customer acquisition drive to manage their own financial situations which has a direct impact on our performance because volumes came down and contractually when volumes come down, I still need to roster people at a certain level because the expectation is that the volume will come back and I manage my fixed cost and my variable cost in a way that gives me a certain level of margin profile. But when the volumes come down, I am contractually bound to hold certain level of people for the volumes that I have committed to which has resulted in a margin compression for us in Q4. But this situation in Q1 is coming around with new budget allocations that our clients are coming back to the market with.

Dinesh Kumar One more confirmation, I think, TV was saying that our EBITDA margin will go to higher end of single digits. Is it, it will go to the level of which we saw in FY11?

Rajesh Subramaniam I said high single digit.

Dinesh Kumar So, can we take that as an FY11 kind of stuff?

Rajesh Subramaniam FY11 was 10 for full year. That was double digit, I am saying it is high single digit.

Moderator Thank you. The next question is from the line of Hardik Shah from KR Choksey. Please go ahead.

Hardik Shah Can you throw more light on specific areas where you are planning to have the cost cutting or expect the margins to spillover in FY13?

Rajesh Subramaniam You know, your question is what have we done, is that your question?

Hardik Shah No sir, which specific areas you are planning further cut, which areas you are saying cost cutting or cost saving which will support the margin improvement in FY13?

Rajesh Subramaniam Cost savings have already happened. What we did was, when we realigned the structure of the business which I explained in all of Q3, see we embarked on actions and given all these are people related business, and all actions have a certain lead time for it to translate in to margins. So we embarked on with the restructuring, we embarked on cleaning out the duplicity that was built in our business. So, we also started cleaning out some of the support organizations that were far ahead of the numbers required in managing the business plus the vertical structure saw the creation of multiple levels of capacity from a service delivery perspective. So once, we rationalize the service delivery with a single point of accountability, we realized we could cut down on significant elements of capacity by shutting down centers, increasing capacity on some of the other centers and rationalizing seat capacity which helps to save on rent, facilities cost, in terms of admin cost. See, ultimately in a business, there are a 100 line items of cost and elements that affect our profitability, and if I start analyzing each one and start taking bits and pieces and improving bits and pieces of each one of these line items, it will certainly adds up to a large number and that is exactly which we have done and which is translating into an uptick as we get into the Q1.

Hardik Shah Sir, like how much further benefit you will see in margins in Q1 and Q2 FY13?

Rajesh Subramaniam See, between my Q4 FY12 and Q1 FY13, there are significant elements of seasonality which will fall off. Seasonality falling off means my revenue loss is equivalent to my profit loss. But despite losing out on the seasonality in Q1, my margin profile will stay at the same levels or slightly better than what I exhibited in Q4, and from there, it will keep trending to a level which will get me to a high single digit level.

Hardik Shah How much seasonality revenue was there in Q4?

Rajesh Subramaniam Seasonality number we can't disclose.

Hardik Shah Sure sir, what is the Capex plan for the FY13. How much will be the CAPEX?

Rajesh Subramaniam Between USD 10 to 15 million.

Hardik Shah And sir, what kind of steady state of cash flow from operations you see in the coming quarters?

Rajesh Subramaniam Roughly, we expect to add between a $2.5 to $3 million every month.

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

Amitabh Sonthalia So one is that you bought back FCCB's worth 42 odd million. What prevents you from buying further, right now since you are sitting on substantial cash to meet FCCB, is it the RBI regulation or what is it?

Rajesh Subramaniam: You are absolutely right. The RBI window has been shut on March 31. Once the window reopens and as and when the opportunity is present, we will definitely evaluate buying back bonds.

Amitabh Sonthalia Because what I can see on Bloomberg is your FCCBs are trading at YTM of 40%. So, you could save on that.

Rajesh Subramaniam Absolutely, this is the RBI window that needs to open up.

Amitabh Sonthalia Is the company is confident of meeting its liability as far as the FCCB redemption as well as the YTM is concerned?

Rajesh Subramaniam As I said, we have strategies in place and today am I across the line, the answer is, No. But am I confident that we will get there, as I said, we are working towards addressing that. The joker in the pack is the exchange rate.

Every one dollar appreciation increases my liability by $3 million, that is something which is not in our control.

Amitabh Sonthalia Why the money that you raised, the 180 million, not kept in the foreign currency?

Rajesh Subramaniam We brought that to India into rupee, we brought that in end of Q1.

Amitabh Sonthalia Why did you do that?

Rajesh Subramaniam At that point in time, we did not have the sense that the rupee was going to depreciate by the extent it has.

Amitabh Sonthalia Okay. My question is that since you have a big dollar liability coming up, if you raised dollar funds on that, would it not be prudent to leave it as foreign currency, so at least to the extent of 180 million, you are not taking the currency risk.

Rajesh Subramaniam That is fair enough. The view at that point in time suggested that the rupee will depreciate by 25%. And, if the rupee had appreciated by 25%-30%, the question would then have been why did you not bring the money into India?

Amitabh Sonthalia We could have debated on that, but the question is on one hand you are hedging your future receivables. Somebody also asked that you have a natural hedge on that, so ideally we do not need to hedge it as we have adequate liabilities in foreign exchange.

Rajesh Subramaniam See, the point is the money has been brought in and the decision to bring in the money has been taken by the board. The rupee had more chances of appreciating than the dollar appreciating against the rupee. This was the decision taken in that point in time.

Amitabh Sonthalia It is also an earning any positive carry?

Rajesh Subramaniam Yeah, it has got a positive carry of 3% over the cost of my funds.

Amitabh Sonthalia Okay, that was probably one of the motivations to bring it in to earn that carry?

Rajesh Subramaniam Yeah, in expectation of rupee appreciating and a positive carry, Yes.

Amitabh Sonthalia Okay, I am just wondering that the company has got still 6 months to go, rather than sit and keep watching the rupee go down. Would you look at

taking some mitigating steps on that, at current levels, you can at least cap your liability as far as the exchange is concerned?

Rajesh Subramaniam In February, we have evaluated it and the cost of covering was about Rs. 2.5 to Rs. 3 and the cost of covering it right now is about Rs. 1.5, closer to September where the 3 months premium will be far muted, that is the point at which we will evaluate whether we cover the liability because it is expensive to cover at this point in time.

Amitabh Sonthalia Okay, the other question is that from your FY12 balance sheet, I notice that your consolidated goodwill is greater than your net worth. So, which one way to look at it is your tangible net worth is actually negative. So, would that lead to any financial risk for the company in terms of fund raising in the future?

Rajesh Subramaniam No, goodwill is tested for impairment. As per the latest one, there has been an impairment because the business units on which the goodwill has been created has been performing to plan or sometimes exceeding plan. There is no risk of impairment which is going to see me take a charge on my goodwill which will impair my net worth.

Amitabh Sonthalia Okay, right, the second question was would it limit your ability to raise funds because you do not have collateralizable assets for the lenders?

Rajesh Subramaniam I think, any fund raising in the future is likely to be a combination of the cash flows. We believe in the buildup of cash flows as the company unfolds its next two years plans and from an asset perspective, we still do have headroom in providing cover and taking additional indebtedness.

Moderator Thank you. The next question is from the line of Ankit Bafna from Credit Suisse. Please go ahead.

Ankit Bafna First of all, I would like to know the nature of this increasing debt that you had in the fourth quarter, actually what exactly is the debt and who are the lenders, etc.?

Deep Babur So, the debt we really took on in this quarter was as we mentioned one part of it was post shipment credit that was taken from DBS. The other part was utilization of working capital facility from ICICI Bank. Really, what we are doing is essentially as we are building up cash towards the FCCB redemption, the idea really is that we start to use the working capital lines to fund our working capital requirements and keep the cash that we need for the FCCB's separate from it. That is the reason we are starting to tap into this working capital facility

although we do not see different cash wealth and really do not need to borrow at this point in time.

Ankit Bafna The first one is you said post shipment credit from whom?

Deep Babur: DBS.

Ankit Bafna Also, if you look at the cash flows for the fourth quarter. We see that the net interest expenses have increased by significantly compared to previous quarter. What has lead to this?

Deep Babur It is not significant. On a quarter-on-quarter basis it was about 1.4 crore in Q4 and is about 66 lakhs in Q3, it is really a 70 lakhs rise.

Ankit Bafna Sorry, I am talking about the net cash interest paid that you report in your cash flows. Which I believe was about 36, 29, and 95 millions for the first three quarters and for the full year you have reported a number, 373. So, for the fourth quarter it was almost at 21 crores. The cash flow number I am referring to.

Deep Babur No, I understand, I think, if you really look at it on an annual basis, maybe in Q4 there is a significant interest that is paid out other than the regular interest payment that is due on the $180 million loan. There is really nothing over and above that. Maybe, Ankit and I could circle back to you with that number. If we really look at the annual cash flows, I think, what you are saying is that you deriving it by annual cash flow and deducting by three quarters and seeing the number, but I think what has happened is that there is a set of re-class that does happen when you prepare the annual cash flow and you cannot just derive the fourth quarter cash flow, that may be the reason, but there are no extraordinary essentially the payments that are made are ordinary in Q4.

Ankit Bafna Okay, got it, we can circle on that later. The next question that I had was if you could just provide me the breakdown of your other current liabilities and that you classify on the current liability and that is a significant amount, does that also include the FCCB payment coming up?

Deep Babur Yeah, that is correct. The 1,249 crores is debt under the other current liability, bulk of that is really the FCCB's, so 1,142 crores of that is FCCB. That will hopefully explain, this is barely 100 crore outside of that.

Ankit Bafna So, if you take the balance and add that to the current liability number that you have on the balance sheet, the total current liabilities have actually declined

by almost 25% to 30% compared to the previous quarter. Is there something that you want to comment on?

Deep Babur It is interesting what has happened is that there is a new Schedule-6 that has come about and that is completely different way of classifying things. But to really answer your question quarter-on-quarter the current liability has not come down. If you noticed, Rajesh earlier mentioned that, we have generated significant cash flows this quarter and management of the working capital cycle operates a part of it and is also managing our creditors, so we are not really seen our current liabilities fall on a quarter-on-quarter basis. It will be difficult for you to compare this number because what we have put out here is under the new Schedule-6 where the last quarter numbers were reported under the old Schedule-6. If you really look at the re-class to explain that better to you may be that we can do offline but that is the cash that has been generated from the net current assets where the current liability has gone up marginally.

Ankit Bafna Would you like to comment on the some of the changes that are happening quite frequently in the top management in the last one year, I mean, change in CFO, etc., if you can please comment on that and some reason for that?

Rajesh Subramaniam: Well, the change in CFO, when I left the company in 2008, Carl Saldanha came in as a CFO, and his contract expired in December. Prior to that the board has decided that they were not going to extend his contract and they were trying to hire a new CFO / try and get me back into the business. So, I did come back to the business and took the mantle of the CFO and Deputy Managing Directory. Apart from that, Matthew Vallance who decided to leave the company and to pursue other interests, it was his idea, I guess at some level, to get me back in as his deputy and create an orderly transition so that he can pursue other interests. I guess, that is the limited point I can make at this point.

Harsh Hi guys, this is Harsh. I work with Ankit, couple of more questions, very quickly, how much is the minimum cash balance you guys think you need to run the company, I think you have $150 million right now, you are saying a lot of that would go towards paying down the FCCB's. In a base case scenario, how much cash you need post that redemption to run the business?

Deep Babur We probably need in the region of about $15 maximum $20 million and all of it really, as I was explaining earlier, use working capital facilities for these purposes, really all of that can be easily funded by working capital lines that we have available today.

Harsh Okay, how easy or difficult it will be to take cash out from India given what is happening with the rupee and RBI regulations and what have you done to pay out the FCCBs in December. You said, the cash balance currently sits in India, basically, right?

Deep Babur Bulk of the cash balance is in India.

Harsh I was just wondering that would it be easy to convert the rupees into dollars and take the money out to pay the FCCB's off.

Deep Babur When you say take some money out, I have some FCCB obligation due December 4

Harsh Would it would be easy to get the dollar basically, seeing what is happening with the rupee?

Deep Babur That is the function the way it is, there is no lack availability of dollar. It is a question of at what price I will get those dollars?

Harsh Okay, my understanding was RBI is trying to tightly control a lot of these ECB maturities in India and they do not want the dollar to sort of leave the country or you know what have you basically? So, just trying to see what sort of impediment you see on that ground?

Deep Babur No, absolutely, no. As far as any ECB maturity or FCCB maturity is there, we are authorized to buy the dollars from our authorized dealer, we need not even go to RBI. We do not need RBI approval to buy dollars to redeem our FCCB.

Harsh Okay, got it, the last thing guys is, I remember, when we met few months back you mentioned the reasons for not buying back FCCB so the fact that your book value of FCCB was sort of higher than the 8% to 10% discount, what the RBI requires you to buy back the FCCBs was. The reason you just came up with the call was completely different from what you mentioned last time. Has something changed or am I missing something out here?

Deep Babur No, nothing has really changed. I think, at this point in time, there is really no window available today. So, from our standpoint we really do not have that but having said that after the window does open, if and when if it does open, we need to evaluate and at that point in time, clearly the point you mention will hold, but what has probably changed over the last few weeks is that some of the YTM has widened on the bond and we have not really done the calculation, may be as it has widened, if at some stage the discount of the

YTM is wide enough for us to be able to buy back without incurring a loss in our books then it is something we certainly will look at. So, it is still something under evaluation. We cannot even go down the path evaluating it because the window is not open.

Harsh That is fair, what is the book value of FCCB right now?

Deep Babur Book value is 1,142 crores.

Harsh I am sorry, easy to give a sort of per FCCB number like dollar price number.

Deep Babur If you work that back into dollars, that will be about $224.5 million.

Moderator Thank you. The next question is from the line of Jeff Chan from BNP Paribas. Please go ahead.

Jeff Chan I just have two questions. One is also related to FCCB. Currently, you still have around USD 65 million deficit to redeem that and how would you make up this gap and if you are going to do an additional borrowing, may I ask what is the progress of it and secondly, you mentioned also the margins would continue to improve, can you have a rough number, because in the fourth quarter you have 8.5% EBITDA and 5% EBIT, would the EBITDA margin come back above 10%?

Deep Babur First let me take the first one regarding the FCCB. Really, you know, Rajesh has spoken about the funding gap, we have as you speak of a number just 100 millions, it is actually $87 million, if you said around March 31, 2012, and we do expect that number to contract to 65 million based on the cash flow that we generate between now, when I say now, I mean between April 1 and December 4, as Rajesh mentioned one of the joker in the pack is the exchange rate and we do expect at Rs. 50 exchange rate, our estimate of the gap is $65 million and then you add the basically $3 million for each rupee that essentially at which level, we will sign up to buy dollars. The gap probably will come up to $65 to 70 million range, we have got a number of avenues that we are evaluating and really I am sure that you will appreciate and we don't quite have the liberty to discuss that on the call, especially, right now, but everything from, you know, a lot people came back to me saying are you guys looking at an external commercial borrowing which is foreign currency borrowing in India, absolutely that is something we are evaluating. Are we talking to our existing lenders? Yes, we are. Are there other options, we are evaluating outside of this? Absolutely. So, there are a number of things that we are evaluating and like I said we really won't be able to share all that with

you at this point in time, but we are confident that we will be able to cross over the line on the 4th December.

Jeff Chan If you are going to have such funding in place, what would be the timeline as an investor would be hearing from you on the progress, like you have some kind of sanction?

Deep Babur I would suppose that it would probably be about 3 to 4 months from today. Which will be also 3 months which is also prior to when it is due.

Jeff Chan Right, you mentioned, once the purchase window opens, you consider to purchase, and do you have any clue from RBI yet on what will be timeline of that window to open?

Deep Babur Unfortunately, we specifically as a company do not but if you have been following the Indian business press, you will see that there have been a number of articles which seem to suggest that the RBI is looking at not just reopening the window but really allowing other flexibilities to companies that have redemption due this year on FCCB. But, that is as much as we know.

Jeff Chan Right, okay, and you have Rs. 3.5 billion receivables sitting in your book. May I know, would this be as presented sales wise, would it be normal because it seems to be a big jump from the last year. In the coming few quarters you may get back some.

Deep Babur: You know, I think, receiving will be clearly essentially working our net current assets will also be a key part of generating cash over the next few months as we near the redemption. I think, if you look at it, our DSOs are not out of line, we are not extremely high, we are not in a situation where receivables are really extraordinarily high. Our Rs. 3.5 billion that you mentioned that really represents by itself, a DSO of about 51 days which is not very high. Yes, certainly, we would like to see it going down to 40 to 45 days level and we are working towards that.

Jeff Chan On the margin question?

Rajesh Subramaniam On the margin question, our EBIT would be a high single digit and the delta between our EBIT and EBITDA is about 200 to 300 basis points. For FY13, we expect our EBITDA to be north of 10% to 10.5%.

Moderator Thank you. The next question is from the line of Rosita D'Souza from Elara Capital. Please go ahead.

Rosita D'Souza I have one question on your attrition rate. I mean, there seem to be an increase in the attrition rate, and is there anything to worry? Is the management actually doing something to try and stem that rate?

Rajesh Subramaniam Attrition rate has spiked in Q4. Because the Q4, typically is the season where the people are preparing for their exams and so sometimes, we do see a spike in Q4. It normalizes in Q1 with post the exam season where there is supply of students who finish their graduation or whatever professional exams they take, they come back. So, I am not too worried, the attrition has been lower onshore, actually it has fallen by about 300 basis points. Attrition in our domestic business has increased by 10% points and I cannot tell you that these positions will reverse because it is too early in the quarter, but it has not had adversely affected our performance. That is the heads up that I can give you.

Rosita D'Souza Okay, the other question I have for you is, apart from the FCCB that is payable you have loans worth about 107 crores that is repayable in the year. Is all of these repayable before the FCCB is due or how much is actually due before the FCCB repayment?

Deep Babur You know, actually, when you say loans due prior to FCCB, so some of the working capital lines that we have tapped into. Technically, these are repayable on demand. They will show as an essentially short term borrowings or current borrowings. That is the one element. The other elements would be essentially the current component of the some of the finance leases that we have taken. The working capital lines like you mentioned earlier while they are due the fact is that we are going to be using those lines, those are the amounts that are not strictly speaking repayable so they will be redrawn. Then I guess, the smaller element is within the limit of the amounts due on the financial ECB, which is not particularly significant.

Rosita D'Souza Okay, on the FCCBs, we had a lot of discussions on that. I have just one more question on it. Is rollover an option that the company would essentially look at because you know right now we are looking at as you mentioned about $65 million gap, but you know, if the rupee were to move or even stay the way it is right now, obviously your liability increases. So, given the current environment where refinancing is becoming increasingly difficult, is rollover an option that the company is potentially exploring?

Rajesh Subramaniam At this point in time, No. In 3 to 4 months, we will know which conclusions we will derive and we will communicate appropriately. At this point in time, we are evaluating all options and roll over as an option is not considered right now

because we believe we can get across the line. But, if the macro-environment deteriorates further and which is the beyond the control of the company at that point in time, we will take guidance from the board and share with you.

Moderator Thank you ladies and gentlemen. That was the last question. I would now like to hand the floor back to the management for closing comments. Please go ahead.

Rajesh Subramaniam Thank you everybody, very insightful questions, and we have had a bad 2012, but we have had the first signs of recovery in Q4. We expect FY13 to restore us back to resemblance in profit margin levels, albeit, not entirely at FY11 level but definitely significantly better than what we saw in FY12. Our core elements of business continue to do well, especially, in telecom and media and healthcare. The big event for the year for the company is repaying its FCCB liability and we are trying our level best to make sure that we have resources in place to get us across the line. With that closing statement, I will hand it back to our investor relations member, Yash.

Yash Gadodia Thanks Rajesh, and thank you once again everyone for joining the call, if any of your questions have been unanswered you could write to us or call us at investor relations - either Ankit or me.

Moderator Thank you. Thank you gentlemen of the management. Ladies and gentlemen, on behalf of Firstsource Solutions Limited that concludes this conference.