"R Systems International Limited Q1'FY24 Earnings Conference Call"

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Notes:

1. Please note that no unpublished price sensitive information was shared/ discussed during or in pursuance to this Earnings Call.
2. This transcript has been edited for readability purpose and may contain errors. The Company takes no responsibility of such errors, although an effort has been made to ensure high level of accuracy.

Moderator: Ladies and gentlemen, good day, and welcome to R Systems Q1 FY '24 Earnings Conference Call.

As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*"and then "0" on your touch-tone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Giriraj Maheshwari. Thank you, and over to you, sir.

Giriraj Maheshwari: Thank you, Ria. I welcome all participants to R Systems Q1 FY 2024 Earning Conference Call.

We have today with us Mr. Nitesh Bansal – Managing Director and CEO, R Systems; and Mr. Nand Sardana – CFO, R Systems.

We will start the Call with "Opening Remarks" on the performance of the Company by Mr. Nitesh, followed by a "Financial Overview" by Mr. Nand. Thereafter, we will have a closing statement by Mr. Nitesh. Subsequently, we will open for a Q&A session.

Before I hand over, let me read out the customary disclaimer statement on behalf of the Company:

"Investors are cautioned that this presentation contains certain forward-looking statements that involve risks and uncertainties. The Company undertakes no obligation publicly to update or revise any such statements. These statements may undertake revision because of new information, future events or otherwise. Actual results, performance, achievements could differ from those expressed or implied in such forward-looking statements."

With this, now I am handing over to Mr. Nitesh for his opening comments. Thank you and over to you, sir.

Nitesh Bansal: Thank you, Giri. Good morning. Welcome, everyone. Thanks for joining this call. For those of you who have access to the presentation, I will keep calling out the slide numbers as I refer to them. For those who don't, I will anyway be covering the content of the slides. I am on the agenda slide, and I will be covering some of the key highlights, trends and operating metrics, etc., as we go through. And then Nand will cover the financial details for the reported numbers for the quarter.

Coming to Slide #4, which is the "Key Highlights":

We reported a revenue of Rs. 4,166 million, which is about $50.2 million, which is a year-on-year revenue growth of 3.1% and a year-on-year adjusted EBITDA growth of 10.4%. The net profit stood at Rs. 275 million or $3.3 million. If you look from an adjusted EBITDA margin perspective, we have gone from 15.4% EBITDA to 14.4%, and we have provided a bridge for it, which I will just talk about. But on a year-on-year basis, gone from 13.5% EBITDA to 14.4% EBITDA, which is the improvement of 10.4% that we talked about.

It is adjusted for the share-based payment expense for RSUs that we have rolled out to all the key employees in the Company, the expense for which comes to about Rs. 65 million, which is recorded post this adjusted EBITDA. Adjusting for which, the EBITDA will come to Rs. 535 million or $6.4 million or 12.8% of the revenue.

The bridge between Q4 2023 to Q1 2024 EBITDA, we have further improved our utilization and got advantage of higher billing days resulting in Rs. 24 million and Rs. 16 million, so overall Rs. 40 million addition to the EBITDA in that sense. But we have also rolled out a salary hike to our employees in Q1, which cost us Rs. 26 million. And then there is a Rs. 57 million impact of standard operations, which covers stuff from ramp downs or project closures coming from the customers as well as certain additional provisions for gratuity, etc., or provision reversals for which we had advantage in Q4. Net-net, Rs. 600 million of EBITDA reported for the quarter.

Moving to the next slide. Looking at the trend, 8-quarter trend for the revenue and EBITDA starting Q2 ‘22 to now Q1 ‘24, across the 8 quarters, we have gone from Rs. 3,750 million to Rs. 4,166 million, which is a quarterly compounded growth rate of about 1.5%. In the same time, we have gone from 13.1% EBITDA to 14.4% adjusted EBITDA, which is again quarterly compounded growth rate of 2.9%, bringing our EBITDA to Rs. 600 million. Overall, the quality of revenue has improved with our focus on doing more with cloud, data and AI. Leading our value propositions with cloud data and AI has led to better quality of deals, which is reflected in the quality of revenue that we are reporting now.

Moving to the operations metrics, which is Slide #6:

There is no major change in revenue by geography, slight movement from 73.8% to 74.5% in North America, which is compensated by Southeast Asia and Europe going down from 13% to 12.2% and 10% to 9.8%, respectively. Our client concentration largely remains the same. Our top client contributes 6.2%. Overall top 10 clients contribute 22.7%, which has gone up from 22.3%. The mix has slightly changed over time, 2 or 3 clients which fell off the top 10 list and new clients have taken the place. But overall, on one hand, we enjoy the loyalty of some of our large clients. On the other hand, we remain largely diversified, which has helped us keep resilience during the last 4 to 5 quarters, as we have seen the market quite up and down. But because we are so spread out and have many clients to balance off, it has kept us very resilient.

On utilization, our numbers have significantly improved, and they have consistently improved over the last 3 to 4 quarters. We are now at a consolidated blended utilization of about 80%, which compared to 4 quarters ago was 75.8%. So, there is almost a 4% improvement in utilization.

On DSO, we have largely been in the range, quarterly up and down, we reported a DSO of 62 days for the quarter ending March ‘24. Coming to some of the qualitative commentary on Slide #7, building for the future. Like I said last time, we are continuing to build our go-to-market motion. Our sales and delivery organizations have been reorganized in vertical lines, which has created a sharper focus on target industries. And these are industries where we have developed differentiated capabilities over the years.

Also, as we discussed last time, we have, during the quarter, rolled out focused account management for some of our key accounts, and this has been done under the leadership of our new Chief Customer Officer, Arun, who joined us in January of this year.

On offerings and positioning, which is a direct result of go-to-market, our new offerings and solutions have been rolled out on cloud platforms, which are both related to generative AI as well as smart manufacturing or AI for automation. So, of course, data, cloud, AI have been our areas of focus, and we have been rolling out newer offerings and solutions in that area.

We have also been rated as major contender in the Everest PEAK Matrix for Software Product Engineering Services. I’ve got a slide for that later. So, I will talk a little more about it, but this was the first ever Everest PEAK Matrix we participated in, and we have been put in the Company of a lot of notable peers. On the partnership front, we have increased our focus on the ecosystem play on partnering with the other tech providers or tech product companies whose products we use and we implement. So, we are participating in events organized by those tech companies. We are showcasing our expertise in AI-powered intelligent integration and automation. And both with the 2 large hyperscalers, Microsoft and AWS, we have increased that traction. We now have 4 solutions registered on the AWS marketplace. And we are also jointly pursuing opportunities with Microsoft in the APAC region. On the leadership front, while this is post closure of Q1, but we have had our Chief Marketing Officer, Sanjay Saha, who joined us in April. And he will be bringing in a lot of marketing focus, both to focus on and elevate our brand. And of course, that would have impact on our overall demand generation.

Moving on to Slide #8, some of the key wins that I would like to highlight, which also denote the nature of or the shift of business as it takes place. So, we have been entrusted by U.S. behavioral healthcare solution provider to set up a center of excellence for their product engineering and digital transformation needs. This includes data science and analytics to augment operational efficiency and value-based care.

One of the leading fire safety solution providers in Canada has engaged us to develop a mobility app using .NET and other multiple platforms app UI. It is to help digitize their operations and enhance business efficiency. A U.S.-based digital marketing solution provider has engaged us to upgrade their content management product. And this is actually not just upgrade, but also cloud enabled. So, this includes cloud migration, assisting in consolidating their engineering teams for product engineering and modern data platform/ AI needs.

One of the largest privately-owned general insurance companies have engaged us to provide product engineering services to digitize their in-house products. And one of the leading distributors of live and frozen seafood in Singapore has engaged us to implement Microsoft Dynamics-based Business Central and CRM to optimize their end-to-end business processes, yielding financial visibility and operational excellence for the enterprise.

So, all in all, a decent set of wins and good quality of revenue, which obviously is a leading indicator for sustainable revenue base that we are building up for the future. And these are all accounts which will definitely give us opportunities to mine them further and grow with them.

At this point, I would like to hand it over to Nand for financial performance and contribution analysis. Over to you.

Nand Sardana: Thank you, Nitesh. Good morning to all. Thank you, everybody, for attending the call. I will cover the financial performance, those who are having the presentation, it is in the last slide.

Revenue for the quarter was Rs. 416.6 crores or $50.2 million as against Rs. 416.3 crores or $50 million in last quarter and Rs. 404 crores, i.e. $49.2 million in the same quarter last year. This is a growth of 3.1% year-on-year in dollar terms, almost flat quarter-on-quarter. Just to let you know that we are a calendar year Company, and this is our first quarter. The gross margin was 33.7% compared to 34% last quarter and 33.6% same quarter last year. This is mainly due to the increase in average salary due to the increments kicked in this quarter as offset by higher utilization and billing days. SG&A expenses have increased by Rs. 3.4 crores from Rs. 77.1 crores in Q4 to Rs. 80.4 crores in this quarter. The adjusted EBITDA was 14.4% compared to 15.4% last quarter and 13.5% in the same quarter last year. The Company is able to expand its sustainable operating margin through improved utilization.

We have granted 53.5 lakh RSUs to the identified employees pursuant to the Management Incentive Plan 2023, as approved by the shareholders. As per Accounting Standards, we have booked an expense of Rs. 6.5 crores on these RSUs. EBITDA post the cost of RSUs is 12.8%. We are committed for profitable growth and continued our investment in sales engine, new technologies and innovation to deliver long-term sustainable growth.

Getting down to depreciation and amortization, the total expense was Rs. 16.6 crores compared to Rs. 16.9 crores last quarter. This includes Rs. 6.2 crores approximate for intangible capitalized on account of Velotio and ScaleWorx acquisitions. Interest expense is Rs. 2.8 crores compared to Rs. 2.9 crores last quarter.

Other income was Rs. 2.3 crores compared to Rs. 1.5 crores last quarter. This quarter, we had an exchange gain of Rs. 99 lakhs compared to an exchange loss of Rs. 58 lakhs last quarter. Further, the other income comprised of interest income of Rs. 84 lakhs this quarter compared to Rs. 1.46 crores last quarter. This is primarily due to reduction in corpus post dividend payment.

During the quarter, the average rate for USD and Euro was Rs. 83.04 and Rs. 90.14, respectively, as against last quarter average of USD and Euro of Rs. 83.24 and Rs. 89.59, respectively. These are the 2 main currencies for R Systems. As at the quarter end, we have a total forward cover of $35.9 million with an average rate of Rs. 84.21 and euro cover of EUR 2.2 million with average rate of Rs. 93.57, which we have already mark-to-market at closing rate of March 31.

We have been consistently following this conservative accounting instead of parking such non cash items in balance sheet through hedge accounting. Our tax expense was Rs. 8.9 crore this quarter as against tax of negative Rs. 1.4 crore last quarter. Tax expense was negative in last quarter due to reversal of the tax provision of Rs. 11.4 crores against dividend received from subsidiary company post dividend declaration by the Company. Effective consolidated tax percentage is approximately 25%.

Net profit after tax was Rs. 27.5 crores or $3.3 million, compared to Rs. 45.9 crores or $5.5 million last quarter. Basic EPS for the quarter was Rs. 2.32 compared to Rs. 3.88 last quarter. With this, let me hand over to Nitesh for summing up.

Nitesh Bansal: Thank you, Nand ji. So, summing up and looking ahead, Slide #9, I am referring to. Our focused account management approach, is beginning to see some results from it in the form of increased client traction and there is a proactive deal pipeline that is getting generated through that. This is obviously leading to more meaningful relationships with those clients. We have also signed a strategic partnership with IIT Delhi. This is something we did in January or rather, February this year to create a joint COE for research towards applied AI and sustainable solutions.

IIT Delhi, as we all know, is a premier institute in India, and they have a dedicated artificial intelligence department. And being close to us from Noida, it makes a lot of sense for us to collaborate with them. And this is a joint center of excellence, where we get access to their latest research as well as most of the PhD students as well as their faculty members to work together with us on joint projects of interest.

Trends that are shaping 2024. And as we know, '23 has been quite an interesting year, lots of things happening around the world, both on geopolitical as well as on business front. As we have gone into 2024, we are seeing that there is still an increased focus on India as an offshoring destination, where clients are choosing options like setting up captives or partnering with service providers and quite often both, because lot of clients do not want to have a complete fixed cost base even if it is in a low-cost geography.

While it creates some competition, it opens up new avenues of opportunities for us as well. Generative AI, from being obviously the fascination and talk of the town, is also getting embedded into the software life cycle, changing the ways that we develop software. We ourselves at R Systems have rolled out co-pilot trainings and licenses to our workforce to stay both in touch and ahead of the trend to the extent possible.

While there are sectoral nuances with some evergreen sectors like tech, media, telecom, health, etc., or BFS sometimes being slow, but we have a very balanced portfolio across multiple verticals, and that has helped us keep resilient through those times when some sectors have slowed down, other sectors have picked up. And hence, we stay resilient. And we are optimistic on the market sentiment improving in the second half of this calendar year. In fact, from the deal activity as we see, we have seen green shoots of things picking up both in terms of the deal sizes as well as the duration that customers are taking for the decision-making.

And I will come to the last slide on the Everest PEAK Matrix. As we talked about, this is the Everest Group's PEAK Matrix Software Product Engineering Services Assessment of 2024, where we have been placed amongst the major contenders, which is, if you are referring to the slide, it has a green box over there to show where R Systems is.

The assessment, obviously, is a fairly rigorous assessment done by the Everest Group. And according to them, they have highlighted some of the key strengths that we need to obviously honed-in and continue to stay focused on. So, what Everest has also highlighted is we have a balanced portfolio across buyer sizes and geographies, that we have a strong partner ecosystem comprising hyperscalers, data engineering partners and enterprise technology providers, that we are amongst a few firms who have a dedicated service for private equity firms, and we have the willingness to engage in emerging deal constructs. And in their own research and talking to our customers, they have heard client appreciation and feedback for our technical expertise, effective project management practices and proactiveness and pitching innovative solutions. So, I think it's a good reaffirmation of what we believe our core strengths are, what we stand on, and we stay committed to building on these and deepening our relationship with the clients for the future.

That's really what I had in the form of presentation. We would be open for questions now.

Moderator: We will now begin the question-and-answer session. The first question is from the line of Harsh Chaurasia from Vallum Capital Advisors. Please go ahead.

Harsh Chaurasia: Good Morning Sir, thank you for giving me opportunity. So, I have two questions. From last 5 quarters, we have seen decline in on-site employees. But in the current quarter, there was on-site employee addition. And at the same time, the North American region grew both on a Q-on-Q and a Y-on-Y basis. So, are we seeing some green shoots in the region from both direct channel as well as the private equity channel?

And my second question would be, in the last quarter, in the call, you mentioned we have built up a strong sales funnel. And even in this quarter press release, you have mentioned like the sales funnel is quite strong. So, where are we in terms of the stages, like the early stage, mid stage or the later stage where our sales funnel is getting converted into the dealings. So, these are my two questions.

Nitesh Bansal: Thank you, Harsh. Thanks for those questions. So, I think your observation is right. Last 5 quarters, we have seen decline in the North America onshore, which is also very directly, I think, a reflection of the tech landscape in North America with significant layoffs across tech companies, etc., who happened to be our customers in many cases because we serve the tech ecosystem.

The increase in North America this quarter largely is from the direct sales channel because we did win a significant deal with the California state government. We have also won a few more deals where the projects are being done on an on-site and offshore mix mode, which required some more onshore presence. So, those are good green shoots. Like you said, yes, they are green shoots of both emergence in terms of new demand as well as a little bit of opening of spending in the North American tech sector or largely in the North American region. I would wait another quarter before calling it a secular trend, but the green shoots are definitely positive, and we are excited about it.

On your second question on strong sales funnel, I still stand by that Q4, when we presented, we talked about our strong sales funnel. We have executed on that. Our result may look like flat from Q4 to Q1, but that's a net flat, which contains some effect of whatever ramp-downs were already known, etc., versus all the business that we have won. From a decision-making cycle perspective, I think we were expecting a much faster decision-making cycle in Q1. We did not exactly get that. So, the funnel has stayed strong. It is a mid to late-stage funnel, but the decisions have taken longer. So, we have not lost deals, just that the deals which could have started off in January, maybe started off in March or maybe starting off in April. So, we are seeing some delay, but that funnel is building up. It is both in terms of average deal size, I am positively enthused by it, and also from the perspective that these are good quality revenue type of deals that we are looking at.

Harsh Chaurasia: So, if I may ask, so have we made the addressable market for Blackstone private equity channel? Like what are we looking at like where we can provide our capabilities? What are the number of clients we are looking to pitch? And what would be the addressable market for Blackstone channel?

Nitesh Bansal: So, Harsh, Blackstone has been in a fairly good channel or active hunting ground for us. We have been part of that portfolio now for 3 quarters or 9 months. And during this time, we have already started working with or getting revenues from over basically a double-digit number of clients, I would say. From a prospecting or reaching out perspective, I think there is 40 to 50 clients within Blackstone portfolio that we have access to. But again, individual Blackstone companies will make their own decisions based on their own spend cycles, etc. So, we are definitely getting that traction. We are taking advantage of that access, and it is a very active channel for hunting for us and it has been quite positive for us so far.

Harsh Chaurasia: Thanks you. Just last question, if I squeeze in. So, basically, it's of data regarding question. Earlier, we used to provide repeat business. Now we have stopped providing the data points. So, what would be the repeat business for this quarter? Same data point for last quarter and the year before?

Nitesh Bansal: So, at least in the last 2, 3 investor calls that I've been part of, we haven't focused on repeat business. But having said that, and right now, I don't have the direct numbers or exact numbers in front of me. But given my sense of the business, on a rough order of magnitude basis, we still get close to 88% to 90% of our business from repeat customers. Because we are dependent on or because we do a lot of discretionary work, we open quite a good number of new clients each year. So, about 10% to 12% of our revenue does come from new customers, but 88% to 90% would definitely be repeat business consistently.

Moderator: Next question is from the line of Yash from Awriga Capital Advisors. Please go ahead.

Yash: You have been adding team members in the top and upper middle management level. Where are you in that journey? Are these investments or gaps in this space filled? Or there is more to go?

Nitesh Bansal: So, yes. So, far, we have added basically 2 team members in the upper management level, the Chief Customer Officer and Chief Marketing Officer, which basically have been a Q1 and a Q2 addition for this year. We did not make any major addition or change to the senior team. Actually, there, we have not made any changes. These are only additions, but we did not do anything last year of that kind. These are gaps that we have identified as a result of our strategy exercise that we did in Q4 last year, where we identified certain gaps. Not having a Chief Marketing Officer was a clear gap. Not having anybody running the account management or farming function was a clear gap. So, we filled those.

We will continue to invest in bringing some focused talent around sales and marketing because we had promised we will continue to invest in sales and marketing as we develop our go-to-market motion. So, those would be more middle tier talent, not at leadership level. So, it will continue. You will see some additions happen as we go across during this year because clearly, it takes time to identify talent, bring them on board and by the time they join. It is an ongoing exercise. I think your question was, are we going to see more during the coming quarters? The answer is, yes. We will see a few more coming during the quarter.

Yash: So, as you are in the investment phase currently and with the demand remaining subdued for the next 6 months. So, how do you see the movement in the margin for the medium and long term?

Nitesh Bansal: So, I think last quarter also, I had addressed this question. We are phasing out this investment in a manner that we can keep pace with the growth of the business, so that we continue to deliver margins. Pretty much in that, we have been managing. So, whatever margin expansion we are able to do may get offset by some of the investments we make. There might be again, seasonality across quarters, which may be a few basis points here or there, but we are not indicating any massive margin dilution because of the investment, because we are phasing out the investment along with the business growth.

Yash: So, you cannot give a number, right?

Nitesh Bansal: Well, like I am saying, I mean, we will continue to report or continue to maintain our margins at current levels. We will expand on margins through operational efficiencies. We will invest them into the investments that we are making. So, we are currently at around 14 point levels. Our endeavor is that we continue at those levels.

Yash: Okay. And can you speak about the organic growth for CY '23 and Q1? That's all.

Nitesh Bansal: Did you mean CY '23?

Yash: CY '23, and yes, this current quarter.

Nitesh Bansal: So, CY '23, we saw our numbers largely remain flat, okay? And this was a combination of we did acquire Velotio Technologies middle of the year. And then at the same time, the market has also kind of taken a turn. But overall, we combined Velotio Technologies with our business. And as a result, as a whole, we have continued to stay moving in the positive territory.

There has been some churn in the business. There has been some impact to our traditional business, which went down. So, organically, in Q4 CY '23, we did see a slight amount of degrowth, which was offset through our acquisition of Velotio. Q1 trend has sort of flattened out, and we are seeing a positive impact coming towards the future. We are seeing positive organic growth. Hopefully in the next 2 quarters, we will start seeing both quarter-on-quarter, year-on-year positive organic growth impact as well. It will be difficult to make out because Velotio has been fully integrated. So, the numbers won't be available separately. But I am sure since you do a lot of analysis, you will have a sense of how it is coming through in the numbers.

Moderator: Next question is from the line of Abdul Kadir Raja from Ratnabali Investments Private Limited. Please go ahead.

Abdul Kadir Raja: Thank you for the opportunity, sir. Just a couple of questions. In the last few calls, you had mentioned that the Velotio has a quarterly run rate of roughly $2.3 million. So, just wanted to understand like is this run rate being maintained with a 30% EBITDA margin?

Nitesh Bansal: So, Abdul, I don't think we have given a quarterly run rate for Velotio in any of the calls. And so, I wouldn't go into the exact number of what is Velotio's quarterly run rate. But having said that, what I have definitely said, and I will repeat and reiterate now is that Velotio has been both growth and margin accretive for us. So, that the business is integrated with ours, we have seen that bring positive growth momentum to our overall business and to the portion of business which we execute out of Pune. We have actually managed to extract better margins. So, it has been margin accretive as well.

So, since we are not reporting separately, it will be very difficult to put a finger at saying exactly how much is Velotio. But from a people utilization and growth of the center and growth of the services perspective, I have absolutely no doubt in saying it has positively grown and been both growth and margin accretive for us.

Abdul Kadir Raja: Sir, the next would be like we have a sales target of roughly $1 billion to achieve in, say, the next 4, 5, 6 years. So, I just wanted to know if you have narrowed down any acquisition target. So, I don't want any details, but are we on track? Or like have we found out the target Company, which you can acquire? Just any thoughts on that?

Nitesh Bansal: Abdul, we are very active players in the market from an acquisition perspective. Every month, we probably do at least a couple, if not 4 or 5, due diligences. Due diligence is probably much later, but at least the initial discussions with potential targets. And being part of a Blackstone portfolio Company, we have the advantage of having an extremely large ecosystem of acquisitions that kind of acts on our behalf to have access to a lot of bankers and other players in the industry.

So, our funnel for potential acquisition targets is extremely rich. We are, of course, being conscious and cautious in terms of where we spend our bandwidth, how many we are able to kind of look at in detail and what suits our kind of growth thesis. So, that way, yes, we are constantly looking. They are in various stages. It's both the meeting of the objectives, the growth thesis, the value it offers and the right price to acquire, then we will be in a position to probably make an announcement whenever it happens.

Moderator: Next question is from the line of Pravin from LIC. Please go ahead.

Pravin: Sir, I would like to know how the telecom sector is helping the Company's growth especially after the Vodafone public issue?

Nitesh Bansal: I am sorry, I was hearing a ring tone. But Pravin, thank you for the question. Telecom has been a core sector for us, and it has been something that differentiates us in the market because product engineering for telecom requires both specialized skills and deep programming knowledge, which thankfully we are able to demonstrate and do.

The customers that we work for, Pravin, are mostly the technology providers for telecom companies and the core OEMs who the telecom companies use to build their tech stack, right? So, we are not so much exposed to the service providers themselves, the likes of Vodafone, etc. But we are working with the technology providers, who actually provide the core stack on which their telecom works.

Again, there are merger situations happening between telco operators around the world. We are less impacted by that. But we are more impacted by the general spend by those operators on technology, right. And which, if you look at in the last 4, 5 quarters after the 5G spectrum, a lot of operators have spent a lot of money on 5G spectrum. They are struggling to monetize. And that has resulted in some amount of expense squeeze of what these operators spend on technology or refreshing their technology, etc., which has some impact on us.

But because we are working on core products, it's also a fairly resilient spend. So, we have not grown significantly in telecom space, because that's how the market is. But our business is very sticky, and we are continuing to kind of stay with our customers because we are core to them. And telecom is not a stand-alone market. We work with telecom, media and entertainment companies. Some amount of media and entertainment spend is something that we have taken advantage of, and that's also something that was one of the reasons for acquiring Velotio, because they also have a strong media offering. So, that has helped us in overall keeping the market rounded up and taking advantage of it.

Pravin: Sir, 1 more question. You have been giving good dividends for the past 2 years. Can we expect a bonus issue?

Nitesh Bansal: Pravin, this is something that is obviously a Board decision on how we appropriate, and this is part of our capital appropriation policy. We stay committed to returning back our reserves and the shareholders' profit back to the shareholders in one form or the other. Whether it goes in form of dividend, bonus issue or anything of that sort is a decision that's probably taken at that point of time. I do not know if there has been any precedence. Nand, do you want to comment on that?

Nand Sardana: We have never issued bonus in the past since the IPO. Currently, there is no such plan. Whenever there is any such thing, we will inform the stock exchanges.

Moderator: Next question is from the line of Nikhil from SnP Family Office. Please go ahead.

Nikhil: So, my first question is like we are trying to cap the larger clients. So, are you planning to under bid to grab them? And my second set of question is like what is the growth rate in ACV and TCV? And what is the contribution of Blackstone portfolio companies in ACV and TCV?

Nitesh Bansal: So, getting for larger value clients, are we underbidding or are we taking margin impact to win those customers, the current answer is no. But again, just to be completely honest, Nikhil, depending on the nature of the business, we might take those calls from time to time. So, far we haven't, because the nature of work that we are still winning either in premium, digital, skills and services, cloud, data, AI, etc., and customers who are investing in those areas, our experience so far has been there has not been any pinching. They are building something which is strategic to them. So, we are able to get the rates we normally command, and we deserve. But tomorrow, if we do get larger, long-term sustainable revenue, we will obviously try to stay competitive to the market to win such business, but that's for future to tell.

On growth rate on ACV and TCV wins, I don't think we track it in terms of growth rate of TCV wins on a quarter-over-quarter basis. But having said that, since we did put a new go-to-market motion in place, we are tracking the number of deals over a certain size that we win. And there, like I said, we have seen a very positive movement, where our deals which are above $1 million in ACV or above $2 million or $3 million in ACV or beyond, have continued to grow consistently quarter-on-quarter.

Contribution of Blackstone portfolio, again, that's a split we don't report as a percentage. But like I mentioned to another question, I think Harsh had asked earlier was we are already working with double-digit number of Blackstone clients. And we have made significant headway with those customers, with some of those customers actually crossing a $1 million revenue with us already. And we have significant runway in terms of where we have in the pipeline over 30 to 40 other Blackstone portfolio companies that we are prospecting with.

Nikhil: So, my next question is like margins in the IT services business has improved drastically, like it's a good improvement in the margin. So, are these sustainable margins? And what are the margins there going to be sustainable margins going ahead?

Nitesh Bansal: So, we believe that the margins that we are currently operating at are sustainable. And, we are quite confident that we will be able to continue to report these margins even after some of the investments that we are embarking upon that we are making both in sales and marketing improvement and our go-to-market motions. So, yes, the short answer is these are sustainable margins. Nand ji, do you want to add anything to that?

Nand Sardana: Sure. Nitesh has already answered, we feel that these are sustainable margins and by growth, operating leverage will play in. Also, there is lot of thrust on improving utilization. So, we are confident of not only maintaining, but slight improvement in margin as well.

Moderator: Next question is from the line of Vinay Menon from Monarch Capital. Please go ahead.

Vinay Menon: So, I have a few questions. One is, sir, over the last few quarters, you've been talking about the funding issues for especially U.S. tech companies and start-ups. So, what is the update over there? And if you can just provide like you used to provide a breakup between tech, BFSI, telecom. So, if you can provide that number, that would be great.

Nitesh Bansal: So, the funding issues for U.S. tech companies, start-ups, etc., is quite a public knowledge. I mean if you look at any of the reports published, the total funding for the tech sector in general, and I am not going to single out startups in there because some of these fundings are for larger enterprises as well, who are dependent on external borrowings or private equity investments, but the net funding has gone down significantly.

And still there are lots of companies who are seeing their funds dry up. And it's not just in U.S. alone, I think we have seen that phenomenon across the world. Though we are exposed more to U.S. because our 74%- 75% of our business comes from U.S., that's why we see it in our reports but it's true across the world that most companies that the venture capitalist or private equities have started asking their investment companies to focus on fundamentals to report a real annual revenue run rates as well as margins versus what was a very buoyant market up to 2021, 2022, where funding was, i.e. the funds were available for cheap and funding was being provided for investment in technology and growth of subscription rather than the real revenue and margins.

So, that situation, I think, is still true. At least so far there is no immediate sign that situation is reversed or reversal is happening. But we hope that with stabilization of the interest rates and hopefully reduction on interest rates in a few quarters from now, maybe the situation could change. Nand ji, you want to talk about any split? Because again, I do not think we were reporting the split across sectors. But if you have some comments to make on that.

Nand Sardana: Yes. So, broadly, tech and telecom put together comprise of close to 50% of our revenue and BFSI around 11%-12% as the broad breakup. I think we report in our annual report, so you can refer. But broadly, the category is the same.

Vinay Menon: And just one more question. Nand ji, if you can answer. So, you have mentioned that about, I think, in the last call, you had said that Rs. 12 crores will come as a tax write-back because of the funds which you got from your U.S. subsidiary, which you had used for the Velotio acquisition. So, that is the same Rs. 12 crores which you've mentioned for Q4 2023?

Nand Sardana: Yes. I've explained that, the tax impact is because of that Rs. 12 crore benefit which we got. Yes, that's right, we have given in the form of a note in the press release.

Vinay Menon: And one last question, if you just answer. Nitesh sir, what kind of revenue growth are we targeting for R Systems over the next few years? If you could possibly give any guidance, that would be great, sir.

Nitesh Bansal: Vinay, we don't provide guidance. But we have consistently mentioned that we are tracking ourselves closely with the industry and industry peers. And our ambition, our goal is to grow at least faster than the industry average and hopefully, at par with some of the best performing players in the industry. But this has been a very dynamic cycle. So, getting that predictability is very important for us. But we certainly will continue to track ourselves with industry averages, and we will grow faster than industry average is something that I am very confident of saying.

Vinay Menon: Sir, if there is any way to reach you all because we just wanted to know a bit more. So, if you can let us know that if there is any way I can contact you after this, that will be based on some offline questions.

Nitesh Bansal: Sure. our Investor Relations contacts are provided with this. So, please do feel free to reach our investor contact team.

Nand Sardana: My e-mail address is in the press release, do write to me and we will answer your questions.

Moderator: Next question is from the line of Ravi Anand from InCred Asset Management. Please go ahead.

Ravi Anand: I have few questions. The first question is on growth. Sir, this quarter has been kind of a flattish quarter. Last quarter was obviously seasonally weak. And prior to that, we had one-off under Velotio acquisition. And prior to that, 3 quarters were kind of 1% CAGR kind of stuff. So, we understand that the industry is going through some headwinds. And so are we guiding that our growth will be kind of in line with, looking at the past 5, 6 quarters and our growth in the next few quarters will be in line with the industry because that is what the data is suggesting. And if I just want to add to it, you mentioned that this quarter, there is some impact on both because of rationalization of certain accounts. So, I would just want to understand had this rationalization not being there, what would have been the normalized growth? And where that growth be coming from? Would it come from mining of existing clients or like the new clients may be added by that?

Nitesh Bansal: Sorry, Ravi, what was the question around rationalization? I lost your voice a little bit over there.

Ravi Anand: So, you mentioned that the growth during the quarter was muted. One of the reasons was that we had to cut down the smaller accounts, if my understanding is correct or may be rationalization.

Nitesh Bansal: No, we haven't deliberately cut down on any smaller accounts or rationalized. What I had mentioned was that there has been continued churn of some customers, which like I think the earlier question that Vinay had asked about that in our business because of discretionary spend, there is a certain amount of business that will naturally come to an end because the project gets over, right?

And then there are the longer-term R&D investments which we are part of because we develop products for our customers, which are dependent on the R&D budgets of the customers. And in the last 2 or 3 quarters due to some of those funding issues, etc., that we talked about earlier, we have seen some of our customers shut down on those initiatives, which creates ramp-downs for us, right? So, those have been the ramp-downs or churn that we have seen.

On the other hand, we have continued to win new business to compensate for that ramp-down and churn and kind of build up both revenue base for the quarter and pipeline for the future to kind of continue to grow upon it. So, yes, I mean, there was no rationalization of customers deliberately done from our side, but that's a natural churn that we have seen. But go ahead with your question. I mean there was some other part to the question, I guess.

Ravi Anand: Yes. Sir, just in continuation with this, so this will be a natural phenomenon every quarter. So, in context of this, actually given that the industry is going through headwinds, I am not asking for a explicit guidance, but a range of growth guidance maybe between 10% to 15%, something like that.

Nitesh Bansal: So, Ravi, your first question was, is our growth largely tracking the industry? And at any point, are we going to break away from it? Are we going to grow much faster than it, right? So, currently, yes, we are largely tracking the industry, in fact, depending on which statistics you see across some of our larger peers, mid-cap peers or small-sized companies like us, we are probably slightly better off with most of the companies having somewhere given muted results, negative growth trajectories, etc. But yes, we are still largely subject to the kind of industry trends currently.

With the investments we are making in account management, in mining function, etc., we believe, first, it will help us solidify our positions with the accounts, which means bring more predictability in our revenue. And then eventually may contribute and will, I mean I am confident it will, but I am just projecting in the future whether it will happen in 3 quarters or 4 quarters or it will take longer, when it can start giving us that additional growth trajectory where we can break away from the industry trend.

Our new account acquisition engine has been one of the strengths, we will continue to leverage that. We will continue to acquire new accounts so the growth will come from a combination of new accounts and existing. We would like to see to increase our predictability if the dependence or if the contribution of the new accounts could come to 10% or below, that would just improve our productivity and efficiency.

But we are happy with the new accounts coming in because it gives us exposure to new customers. And being in product engineering and R&D, we do need that fresh infusion so that we are constantly working on the latest products and the newer technologies, right? So, that combination will continue. Right now, we are tracking the industry and we are staying above the average, but we will break free at some point of time.

And yes, churn will remain a natural phenomenon. But industry has a role to play because the churn was not that high 3 or 4 quarters ago. We have seen it become very high. We hope it stabilizes. Typically, our business is more sticky business than generic IT services because R&D investments are made for several years, products continue to stay in development and new features keep getting added over and over time. And that's how we have maintained a very long-term relationship with our clients. If that churn reduces and the R&D investments become more stable, we will definitely see that translate into positive growth for us.

Ravi Anand: My second question was on margins. So, as we build the team, the RSU costs will be there, maybe it's not even phenomenon. But we will continue to invest in SG&A as well. So, as you mentioned that the margins are sustainable, and it might improve going ahead. But if I look at the segmental table, the information technology services business is generating EBITDA less than 10%. Most of the margin is coming from the business process outsourcing services. And obviously, utilization is one of the levers. But how do we see this margin on a more longest-term sustainable basis?

Nitesh Bansal: So, I will definitely ask Nand ji to also comment on top of what I said. But broadly speaking, Ravi, our business mix, at least for the foreseeable future and we haven't forecasted for 5 years. We are forecasting only 1 year or 18 months. We see our business mix remaining largely similar. And with a similar business mix, we should be able to deliver a similar margin. When we are making more investments in sales and marketing, like I've answered earlier, we will be compensating that through our both business growth as well as some amount of efficiency levers that we will bring in so that we don't dilute our operating margin from that significantly.

Like I said earlier also, there might be a few 10, 20 basis points dilution seasonality that may happen because sometimes when you hire someone, when you bring someone on board, it may be a step ahead of when the growth came in or margin expansion happened or later. So, that may create some seasonality. But broadly speaking, we are in that sustainable range.

And you had some point about RSU cost. This RSU cost is for the bulk of the people or that have already been covered. If we do hire some more people, that will be 1 or 2 people coming in who might then be given RSUs at the time of joining. The total cost impact of that spread over the 7 years duration, as it is spread over, will not be significant on any quarter from a cost of RSUs perspective. At least that's my sense of it. Nand ji can maybe throw more color at it.

Nand Sardana: Sure. I think you have answered it correctly. So, because most of the employees are already covered in that. And just to answer your question on the split between IT service and business versus outsourcing, 91% of our business comes from IT services. So, whatever the margins are, are more a reflection of our IT services. The balance 9% comes from businesses process outsourcing services, where the margins are a bit higher because the kind of work we do. But again, the 91% business is IT services. So, most of the profit is coming from that services only.

Moderator: Next question is from the line of Gokul Maheshwari from Awriga Capital Advisors. Please go ahead.

Gokul Maheshwari: Sir, technology is changing very rapidly with AI coming in. In that context, any parts of the business where you feel worried that is grown to some level of disruption or would you be on the right side of the disruption, if you could comment on that?

Nitesh Bansal: Thank you for that question, Gokul. I think I had covered in my presentation that AI, obviously, is a very large opportunity for us, but it also poses some amount of threat to those who are not ready, right? And the threat is not in terms of loss of jobs or loss of positions or anything. It is just that the customer expectation will shift over time. They will expect that the work is done in the most efficient manner, leveraging technology to the extent possible.

Since large part of our work is product R&D related to where we are developing products of the other companies who are product companies, they actually do not want their products to be developed using AI technologies because they are writing code for high efficiency and specialized code and functions to deliver that special functionality. So, quite often, our customers do not want that to be included. But then there are functions in the software development life cycle when it comes to testing, automation testing, when it comes to doing a certain amount of data simulation and all those things, where AI can be very useful.

So, what we have done is we have already rolled out co-pilot trainings to our staff. We have also rolled out licenses to our people to the workforce where they can start experimenting and using in their day-to-day work, they become used to working together with copilot and start looking at what kind of suggestions can come from AI, which can actually provide them efficiency and better mode of working.

So, one, our business as compared to, let's say, some other businesses which might be more in terms of support maintenance or testing or some of the other generic IT services oriented, is actually less impacted because of being core R&D. But even though it is the case, we are being proactive and we have identified the need and we have already taken steps to get our workforce up to speed on the latest technologies, including generative AI for software development.

Gokul Maheshwari: When you mentioned about the fact that the industry is going through some amount of a challenging time because of the macros. But over a 3- to 5-year basis in your core segments, what would be the expectation for the industry growth?

Nitesh Bansal: You obviously have been watching the market more than I have. For the last 4 quarters, everybody in industry has been talking 2 quarters, right? And that 2 quarters has been kind of moving forward every quarter. So, the honest truth is, this is very difficult to say. Also, this is an election year in half of the world, basically. All the major democracies are going for elections. And there is elections in European Union this year. So, in my own little world, I am seeing optimism in terms of people beginning to spend, budgets are beginning to open up. Some decisions, which was stuck for some time are beginning to come through.

Now this is as of last month. If this trend continues, I will feel a lot more positive and optimistic about this, which I am, honestly. But to be able to say how fast the industry will grow, what the growth trend would look like over the course of the next 3 to 4 years is anybody's guess. My hope is that industry will get back towards growth trajectory next year. The second half of this year will be the uptick. Next year, it will be back to its growth trajectory. And I think the consumption need of the industry is so high that expecting a 10% to 15% growth from thereon should be possible because that's what the world needs to consume. But again, going by the last 3 or 4 quarters or 10, I would not put it in very definite terms, I mean, I will keep my fingers crossed, and I wish that could happen.

Gokul Maheshwari: Last question on the employee front. What are you looking to add in terms of number of people? You have around 4,100-odd employees.

Nitesh Bansal: So, you mean where in which areas?

Gokul Maheshwari: So, in terms of which areas? And the quantum, if there are any plans which you have put in place on a net basis?

Nitesh Bansal: So, our plan to hire would be in line with as we look at our quarterly growth projections because we don't hire freshers, right? So, we don't have a college intake where we would make advanced plans to say this year we are going to hire whatever, 500 freshers or something, who we will train for the 6 next months to make them ready for the workforce. We mostly use talent who are with us when they come for on projects or we hire ready talent from the market in the 2-plus years, 3-plus years experienced categories, all the way up to 10-15 years experienced people. So, our hiring plans are in line with as we see the forecast for the quarter. Areas that we are definitely investing in and we are actively hiring and because that's where we are also seeing demand, like I said earlier, is data AI, cloud, plus Salesforce, and those have been areas of consistent demand and consistent growth. So, those will continue to remain our focus to hire.

Moderator: Ladies and gentlemen, that was the last question of the day. I now hand the conference over to Mr. Nitesh Bansal for closing comments. Over to you, sir.

Nand Sardana: Sure. If anybody has questions, one can write to me, my phone number and e-mail address are at the end of the press release. Thank you, everybody. Thank you for attending the call.

Moderator: On behalf of R Systems, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.