



“Teamlease Services Q2 FY2017
Earnings Conference Call”

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Moderator: Good day Ladies and gentlemen, and welcome to the Q2 FY17 earnings Conference Call of TeamLease Services hosted by IDFC Securities Limited. As a reminder, all participant lines will be in listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “*” then “0” on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Abhishek Gupta from IDFC Securities. Thank you and over to you Sir!

Abhishek Gupta: Thanks. Good morning everyone and welcome to the Q2 FY2017 conference call for TeamLease Services. Today we have with us Mr. Ashok Reddy, Managing Director of TeamLease Services along with Mr. Ravi Vishwanath, the Chief Financial Officer. We would have the usual format of Ashok starting the call with his opening remarks and then we can have the question and answer session. Over to you Ashok!

Ashok Reddy: Thanks Abhishek. I think we have been driving on three elements, one is growth in revenue, the second element is the margin improvement keeping our costs as linear as possible in line with the last year’s headcount and the third element is the M&A for the organization.

I think on the M&A’s front the ASAP Technologies and Nichepro acquisitions have been completed. The comprehensive impact of the two organizations from a topline and the bottom line will come in to TeamLease effective Q3 and Q4. I think the HR integration and other integration aspects have been taken care of and we will effectively look to operational consolidation in these two quarters and kind of buildup growth as we go forward on the IT acquisitions front.

From a business growth perspective, I think we have broadly in line with the traction that we have shown in the previous years to some extent Q2 looks softer than normal purely from a number’s play perspective but that also is the function of the fact that we had a one time bonus revenue that we had to book in the previous September quarter. We do not have any of those one time revenue in this quarter in that sense, so if we do par-to-par comparison it is about a 20% plus quarter-on-quarter growth, but effectively I think the key variable is also that with clients that we have today and element of client additions that we have had we have a good projection coming out for Q3, Q4.

As it is we had earlier also stated that Q3, Q4 accounts for about 60% of the business and Q1, Q2 accounts are about 40% of the business and I think with the demand that we are seeing we still believe that we will be heading towards that element of traction as we go forward.

On the margin improvement front I think as we mentioned one of the key variables that we had put was that we would not be hiring any additional headcounts this year. Worked element of the growth both on the NETAP front and on the associate's front with the existing headcounts because a lot of investments that we had made in technology last year have started getting implemented and the enforcement and adoption is improving on that front. So effectively the continued focus on cost control and not increasing the element of expensive continues.

The increased focus also to kind of drive on the portal and app has been a project that we have taken up, they have gone live, we have got about 55% of the associates who have downloaded the app client adoption is a little lower, but I think what we are also trying to drive on is a lot of digitization and paperless transactions with the customers, which potentially could bring down the costs further as we go forward.

I think largely at an organizational level we are on track with the performance with the element of continued growth and margin improvement. The Q3 will be a strong quarter from a perspective of the seasonality that exists and the acquisition play will come through in Q3, Q4.

We continue to look for additional opportunities in the market at this point in time in the IT vertical and other verticals as things come to a more structured decision level we will communicate on that front, but continued lookout is there at this point in time. So that is it from me Abhishek. If there are any questions, we can take.

Abhishek Gupta

Margaret we can open up for the Q&A.

Moderator:

Thank you very much. Ladies and gentlemen we will now begin with a question and answer session. The first question is from the line of Anil Tulsiram from ContrarianValue Edge. Please go ahead.

Anil Tulsiram:

Thanks for taking my question. My question is on your EBITDA per associates. Your EBITDA per associates for general staffing has increased from 2000 to around 3000 currently and if I compared the same with your another listed peer, only general staffing including the IT staffing is around 8000 per annum per associate, so just want to know why your EBITDA is far lower as compared to your peers what is that your peer is doing whatever there you can explain?

Ashok Reddy:

We primarily are into the general staffing space. Historically if you look at our numbers we do not have IT staffing, which is the higher margin business or other vertical managed service space and I think that is clearly where we said that we would work to bringing those

verticals into the organization for effective improvement in realization per associate per month or per annum. Currently our associate base of near 120,000 is purely into the general staffing space where the margin play is very low and that is comparable across all industry players and the element of economies of scale are what are creating the improvement in the margin play. As we go forward as we look at the IT vertical coming in and so on the average realization per associate will go up.

Anil Tulsiram: Sir the 8000 number, which I am talking about your listed peer is excluding the IT staffing because I have taken the numbers from their IPO document where they have clearly segregated general and IT staffing, so this 8000 per associate is excluding the IT staffing?

Ashok Reddy: Yes and understanding is that there are some managed services aspect in that, which is what we tend to call value added services with the same customer, so when we are talking about sales force deployment today we only do the element of employment contract and the HR administration. We do not do the reporting on the sales front and everything else, so these are value added services, which my competitor provides to the customers and charges them for it. Those are also again variables that we are building into our app that we look at providing over a period of time.

Ravi Vishwanath: The logistic services also part of the services that our competitor provides and that are part of the P&A segment that they actually report their numbers and all.

Anil Tulsiram: Thank you. That is it from mine.

Ashok Reddy: Just again to reiterate on a par for par general staffing front, I think largely the revenue realization for all players in the market is more or less the same. It is really the cost play thereon that leads the margin.

Anil Tulsiram: Exactly revenue per associate is very much similar that is what I also note.

Ashok Reddy: The differential in the EBITDA level comes from the other services that are provided and the revenue stack up from that.

Anil Tulsiram: Thanks a lot Sir. Very helpful.

Moderator: The next question is from the line of Binoy Jariwala from Sunidhi Securities. Please go ahead.

Binoy Jariwala: Good morning and thank you for the opportunity to ask questions. My question is GST is on its way, if you could just share your thought how does it affect the staffing industry per

se and whether it will be inflationary for the staffing industry some of your thoughts on that?

Ashok Reddy: One aspect of the GST is obviously it is going to increase the one time workload at our end, where we have to setup our systems and compliance requirements in line with GST especially if it comes with four different slabs addressing different markets, different industries and so on, but I think all of that is the one time activity that we need to do take care of in terms of the system setup and ability to build the customers accordingly, but I think the key variables that we have always been stating is that today over 30% of the workforce is outsourced, 98.5% of that is in the informal space, hopefully GST drives a lot more towards formalization as we go forward including hopefully the recent decision on the 500 and 1000 rupee notes, it kind of reduces the potential play in the informal sector and I think drives the possibility of formalization in a larger way. Having said that I do not think it is going to happen overnight, it is going to be a phased affair, better enforcement of statutory compliances including GST and other laws of the land will effectively drive up the element of formalization. I think as a preparatory mode to that what we are also doing is trying to expand our client base, because every customer not only works with his core employees, but with the formal sector and the informal sector. So having our foot-in with a larger client base effectively enables us to be prepared for a transition from the informal to the formal when whether by implementation of GST or other label and regulatory changes it becomes imperative for the customer to make that transition, so I think GST implementation should work to the positive of the formal sector. Staffing industry should benefit from that. I think we are positioning ourselves one with the backhand activity in terms of our technology platform for compliance and adherence. We are also looking at expanding the client base to have a foot-in for that formalization.

Ravi Vishwanath: To add to what Ashok said a lot of clients today are rationalizing the vendors that they currently work with. They are actually having a hard look at vendors who would probably be more compliant with the GST regulations, once they get implemented for a fear of loosing out on the GST credit and that is what we are actually hoping for.

Binoy Jariwala: What slab rate would you be potent to, just some thoughts on that?

Ashok Reddy: We would probably be under the 18% category.

Binoy Jariwala: Currently the service tax that you would be charging, would be?

Ashok Reddy: It is close to about 15% including all the cesses and everything else.

Binoy Jariwala: Again is that you have no abatement tax right?

- Ashok Reddy:** There is abatement for service tax except for trading companies and others actually where they would not be able to get it if it is a pure trading they would not get the benefit of service tax, but GST changes the rule completely where they get full input credit for entire GST client base.
- Binoy Jariwala:** Thank you so much.
- Moderator:** The next question from the line of Bharat Sheth from Quest Investment. Please go ahead.
- Bharat Sheth:** Good morning and thanks for the opportunity. In your initial remark you said that we plan to add a few verticals that is one and second thing an answer to an earlier question that some of the services where we have a debt with year so how do we see going ahead of selling the same?
- Ashok Reddy:** Could you repeat your question Bharat we just lost you a little there?
- Bharat Sheth:** In earlier your opening remarks you say that we plan to add new verticals one and second thing that our peers, which is providing other value added services where we keep missing in our portfolio who do really plan to add those two things?
- Ashok Reddy:** From verticals perspective I think we have already added IT vertical, which is a key play in the market so both ASAP Technologies and Nichepro gives us an entry into the IT vertical, one company plays to the services company that is a client base, and Nichepro plays to product companies as a client base. So I think we will post integration of the two companies from an operational perspective and everything. Our focus to increase penetration into the existing customer and also get new customers on board and also cross sell to our existing customers the possibility of IT staffing so I think the IT staffing vertical play is already live from TeamLease rollout perspective. The value added services when we talk about largely driven around attendance management, sales reporting, the aspect of reimbursement management, and so on. Like I mentioned earlier we have now rolled out with the apt for the associates has gained a good traction in terms of download. Our ability to integrate these services onto the app and have the reporting and control to the customer becomes very easy. So we will be doing it by leveraging technology.
- Bharat Sheth:** How do we really see improvement in margin with these leveraging of technologies, which is playing out for us?
- Ashok Reddy:** Typically if you look at the average realization that we have from an associate roughly about Rs.700 odd per associate per month. All these value added services that we are offering will go at a plus charge on the Rs.700 so by virtue of that our average realization per month per associate for those who are availing of these services will go up.

- Bharat Sheth:** Can you give some just directionally, over one year and two year how do we see?
- Ashok Reddy:** Let me not give a guidance on that front primarily from a perspective that we have started rolling out the proposals, started initiating the discussions with the customers, we have already actually added about five customers in Q3 on this service front, but I think we will see more traction as we go forward and we will be in a better position to comment about this as we go forward.
- Bharat Sheth:** With this GST coming in where these trading people who are not getting abatement or input credit now with that available so how do we see again a new vertical that will start, which is deploying staffing services?
- Ashok Reddy:** It will not be a new vertical, but we will have a larger target audience of customers who will be open to the aspect of staffing per se.
- Bharat Sheth:** So which sectors can you just if you can elaborate a little more?
- Ravi Vishwanath:** We are manufacturing services where it could be services, it could be SME, it could be any trading, any kind of trading enterprise will probably be actually involved in this.
- Bharat Sheth:** What we understand from the industry that it is like a QSR as well as retailing, which is not currently getting or all manufacturing and retailing are getting so only pure third party retail how do we see that?
- Ashok Reddy:** All sectors today, see most sectors where they have a service element and they have a service tax obligation get the credit today. Going forward we say it is not just going to be restricted to just a service company, which have a service tax obligation, but even for companies that have a VAT obligation today, if your trader today will not be able to get the benefit, so even those companies will get the benefit of the GST input credit actually going forward.
- Bharat Sheth:** So that will expand out base correct?
- Ashok Reddy:** That will expand the base yes.
- Bharat Sheth:** Thank you. That is all from my side.
- Moderator:** The next question is from the line of Abhishek Gupta from IDFC Securities. Please go ahead.

- Abhishek Gupta:** Thank you very much Sir. I have couple of questions, but first one is the question, Ravi how much was the one time bonus revenue that we had booked in the previous year Q2?
- Ravi Vishwanath:** It is about 45 Crores in Q2 of last year.
- Abhishek Gupta:** 45 Crores was a one time revenue that we have booked?
- Ravi Vishwanath:** For the one time revenue that we are booked at yes.
- Abhishek Gupta:** In terms of the strategic questions one is on the volume growth side Ashok the quarter on quarter addition of about 2700 associates, first does it include the IT staffing vertical or is it excluding the IT staffing vertical?
- Ashok Reddy:** Exclude the IT staffing vertical.
- Abhishek Gupta** It excludes you are saying?
- Ashok Reddy:** Yes.
- Abhishek Gupta:** But still at about say 2%-2.5% quarter on quarter on rate we are kind of in the mark of 10%, 11% annually looks slightly softer than what we had about a couple of quarters back.
- Ashok Reddy:** No, but if you look at like I said Abhishek earlier typically the second half of the year accounts for about 60% of the volume so by virtue of that I think we will be on track to history again.
- Abhishek Gupta:** The third question would be something on you said about increasing the client base from our side so any insights into how the sales and marketing or go to market strategy has changed from your side how are you increasing your testable base anything on that perspective would be helpful to understand?
- Ashok Reddy:** I do not think it is anything of a changed strategy per se, but I think it is just continued focus on the element of getting more customers on board and typical realization that we have had is that most customers come on board with very small numbers to start with, but getting them on board is essential because quite a few of them turnout to be babies that grow with you over a period of time, so I think if you look at the continuous focus from a business development perspective to saying that we need to add more clients and then the follow through along with operations and customer relations to say that we need to keep these customers happy, which also reflects in our retention of our customers and the growth that we will see with these customers as we go forward.

- Abhishek Gupta:** But most of these are still in our focus verticals of BFSI telecom and retail?
- Ashok Reddy:** Most of these clients are from across the industries that we cater to so there have not been any clients concentration that has happened again so our top ten customers contribute about 16% of our revenue so there is still no client concentration at this point in time.
- Ravi Vishwanath:** Also Abhishek going back to your question of associate headcount we also saw some amount of shift in transition happening to Q3 as opposed to Q2.
- Ashok Reddy:** Q3 and also I think if you look at it even our trainee growth has been quite consistent and strong and Q3, Q4 we will also have the IT vertical associate count coming into play.
- Abhishek Gupta:** Has the first half of Q3 be in line with your expectations on the ramp up of festive demand?
- Ashok Reddy:** Yes.
- Ravi Vishwanath:** Yes it has.
- Ashok Reddy:** We did 3000 hires effectively in the October month. This is hard hiring that we did for the last two years.
- Abhishek Gupta:** 3000 hires in October month. In terms of going back to the verticals any progress in terms of the hospitality vertical we have find two large deals with I think the Taj and the Oberoi Group how is that progressing?
- Ashok Reddy:** Going slow. I think primarily because both the organizations had inherent knee jerk throwback from their internal departments because each properties under the kingdom itself so instead of doing a big bang transition and across the properties roll out it is become a phased roll out so we are moving property wise one after the other so the roll out is happening, but in a phased manner slower than what we had expected earlier.
- Abhishek Gupta:** Is the margin profile slightly better than the traditional staffing model over there or?
- Ashok Reddy:** About the same. Not much higher because we are doing right now from the client perspective we are doing the base level staffing. The so-called value added services they said they would go in for at the next level.
- Abhishek Gupta:** You alluded to the demonetization part in one of questions. I know it is too early, but what is your opinion in terms of the client behaviour in the near term with cash economy getting ahead are you seeing some early signs of in terms of your discussion with your clients in terms of ramp down of some retail sales and all those things?

Ashok Reddy: Not yet look frankly in the formal sector that clients are working with us is all above board and all salary payments are by cheque or by bank credit so there was no usage of cash at all in the formal space, but I think where it will impact over a period of time is the possibility to transition the informal where cash payments were being made so what we are hearing at least from not customers right from the market is that in the immediate term it would not make a shift because some of the companies are actually paying two three month salary in advance so that the individuals can bank the monies and these people who had the cash are also moving the cash out in that sense so what has happened is that I do not think the money will disappear it will all enter the formal banking sector and going forward if it is made difficult for the money to flow back into the black then the potential for formalization increases substantially.

Abhishek Gupta: My final question would be on the ancillary HR services we have seen some margin improvement over there. Your opinion and how to look for those services for the next half of the year?

Ashok Reddy: I think we continue to stay positive on those two like I said the investment in those businesses were done breakeven happened last year marginally came into the positive in Q1, better margin in Q2 I think we will see a continued improvement on the HR services front as we go forward.

Abhishek Gupta: Recruitment continues to be the key over there?

Ashok Reddy: There is training there is recruitment and the regulatory compliance business so all of these three continue to play for us.

Abhishek Gupta: Thank you very much.

Moderator: Thank you. The next question is from the line of Garima Mishra from Kotak Institutional Equities. Please go ahead.

Garima Mishra: Thank you for the opportunity. Just referring to the previous question where you said that you are targeting some of the hospitality sector for basically rolling out your staffing services to them. Essentially some of your competitors do provide combined services including facilities management, etc., so versus them I am just trying to figure out what your competitive advantage would be because from a hotels perspective would not they rather go in for a packages deal as opposed to having separate vendors for staffing and the other services?

Ashok Reddy: At least in the hospitality sector per se they do not go for managed services on the housekeeping and stop of that sort some of the smaller properties do, but if you look at the

bigger things most of them run the services themselves with outsourced staff, so typically what we have seen is about 40%-50% of the staff deployed in the hospitality sector are on the roles of the company, about the balance is outsourced, part of it in a managed service model, part of it in a pure manpower model. So I do not think aspirationally we want to get in to doing the managed services, our belief is that there is a volume of requirements in the hospitality sector and in other spaces, which still works to the pure staffing model and I think that is really what we are focusing on as our target audience.

Garima Mishra: How much would hospitality be contributing to your associate employee count currently?

Ravi Vishwanath Right now very much rounding of error because like I said initial plan when we signed on two, three of the larger hotel groups was that big bang migration could happen and that is what corporate HR was looking for, but given the throw back that they have seen from some of the properties it is happening in a phased manner so right now frankly the hospitality sector numbers are at rounding of error.

Garima Mishra: Also in your view how was the festive season demand this quarter or at least in the month of October from an e-commerce and a manufacturing retail industry point of view and was it meaningfully different from the ramp up in demand that you saw last year?

Ashok Reddy: We always Q3 normally sees that festival demand and we are kind of seeing that element of a demand come in this year also. I think in addition to that some of the play that happened because of e-commerce or the new telecom player that has come in to play has also added to the element of a seasonal demand in Q3 so I think we are looking at a very strong quarter from a demand and requirement perspective.

Garima Mishra: So this 3000 associate employee count hiring in October the same sort of a run rate could have sustain in November, December as well or?

Ashok Reddy: It will not. This 3000 will typically continue for the festive season and you will have some additions thereafter, but you will not have 3000x3.

Garima Mishra: Right, got it and last question I had was on the IT acquisitions, so could you give us the number of associate in both Nichepro and ASAP currently?

Ashok Reddy: So ASAP has just short of 1100 associates and Nichepro has about 165 associates.

Garima Mishra: There have been talks of IT staffing demand or employment numbers actually coming under pressure so while I understand the industry is very, very fragmented from a staffing point of view but how do you view the growth of both these acquisitions particularly ASAP which is catering more to the IT services site.

- Ashok Reddy:** Like you mentioned earlier, it is clearly a very fragmented market with most of the companies working with very many number of vendors and I think what we are clearly hearing from the market and also from our existing client is an element of consolidation that is happening and I think the fact that we are a tier 1 vendors to the customers and now that ASAP has the backing from a compliance and financial requirement perspective of TeamLease, we stand a better chance in that consolidation play with the various companies, so I think like I said the financial aspect of the integration has been completed. We are looking at an operational integration into Q3, Q4, so we would not see a huge growth in these companies in this half-year but I think we will enable a strong platform with the existing customers with the BD activity to our existing customers or to wish list a lot of customers and kind of prepare ourselves for growth into next year on the IT staffing front.
- Garima Mishra:** Okay, and just one question for Ravi, when was the 49 odd Crores to be paid for Nichepro actually paid out, did it happen before September or after?
- Ravi Vishwanath:** The closing, one was not 49, it was 28 Crores and two was the closing happened as of October 1
- Garima Mishra:** As of 1st of October, so the amount was paid before 1st of October right?
- Ravi Vishwanath:** On 1st October.
- Garima Mishra:** On 1st, okay, okay, understood, that is all from side, thank you for taking my questions.
- Moderator:** Thank you. The next question is from the line of Abhishek Gupta from Goldman Sachs. Please go ahead.
- Abhishek Gupta:** Thanks for the opportunity, most of questions are directed towards Ravi. To start with, when we said that last year same time, there was one time bonus provisioning, was it like it is a push out this year, Q3 versus Q2 or it was just a one time last year which is not going to reoccur this year?
- Ravi Vishwanath:** It was a one time last year and for the current year bonus has already been factored into.
- Ashok Reddy:** This happened last year primarily because of a notification that came from government which effectively made a certain bonus payment applicable with retrospective effect and that needed to be provided for in the books of accounts, so it was a one time activity as an aberration because of notification by the government for an 18 month period, we will not have a repeat of that unless some law changes with a retrospective effect because that bonus payment has been factored in to the salary structures of the employees in the current period.

Abhishek Gupta: So, are you telling me just for the sake of clarity it was a one time provisioning which was needed because of change of law for the current year and henceforth you have more like pro rating it and hence you will not need to make an adjustment in any one particular quarter?

Ashok Reddy: That is right, yes.

Abhishek Gupta: Another question, Ashok, if I actually look at last first half numbers and even if I adjust for that 45 Crores of provisioning, your revenue was bit more like a 45-55 when it comes from H1 to H2, while what are alluding to this year, it is more like 40-60, so I am just trying to understand do we have a much stronger visibility this year in H2 versus last year or probably again given for the limited data, last year was more spread out but normally you have seasonality which tends to 40-60?

Ashok Reddy: The seasonality is what drives the 40-60 and I think even if we look at this year, quite a few of the mandate discussions that we had for September got pushed to October, so I think the 40-60 kind of a thing, plus-minus 2%-3% is a possibility that will play out this year.

Abhishek Gupta: General trend is 40-60 with obviously some amount of volatility within that number; so last year probably was more evenly spread out but that that should not be a kind of a trend to be assumed going forward. Two more questions, one on the goodwill, obviously because of acquisitions we have created goodwill now in our balance sheet, what is going to be philosophy about it, are we going to test it for impairment, are we going to keep it in the books and how will it get accounted in our P&L?

Ashok Reddy: See goodwill will get tested for impairment, that is the new standard, the accounting standards will get tested, but we are going in with a High Court order, we are going in for a merger scheme which will probably enable us actually charge it over a period of time, it is a financial statement and claim a tax benefit out of that.

Abhishek Gupta: Is there any certainty on the policy and will it be flowing into our expense line or the depreciation amortization line from next quarter onwards.

Ashok Reddy: It will be flowing into the amortization line post high court order comes in.

Ravi Vishwanath: I think if we get the high court order before March, we have to leave it to amortize this amount over five years as we go forward.

Abhishek Gupta: Five years, and just one last question, if I understand from what you are saying there is a cash payout for the asset acquisition already, now the consideration which is even shown as the capital employed is about 655 million which is what the full amount is but then again you have put a qualifier saying that about 10 Crores or 100 million has been withheld for

the performance, so are we saying is thus which we have created a payable in our balance sheet have not paid it out yet and only 56 Crores have been paid out that number, so would you split that 65 Crores between what has been cash payouts so far and what has been retained?

Ashok Reddy: Effectively, Nichepro have been paid in full and there is no pending payment on that front, the way ASAP acquisition was structured was there is a 12 Crores amount that is structured to a pay out basis the FY2017 numbers, so it can either go down or be at par or go up a little bit depending on how the FY2017 numbers of ASAP are, so to that extent that payment has not been made yet.

Abhishek Gupta: My point of reference is if I look at the capital employed, you are showing about 655 million, which is the part of your IT staffing capital employed. I am assuming that is 100% from your ASAP acquisition only, so then you have created a liability in your balance sheet of about 12 Crores and you have paid out the residual, right?

Ashok Reddy: Yes.

Abhishek Gupta: Okay. I guess that should be from my side. Thank you guys.

Moderator: Thank you. The next question is from the line of Bobby Jayaram from Falcon Investments. Please go ahead.

Bobby Jayaram: How exactly do you distinguish between formal and informal employment?

Ashok Reddy: Formal, as we define it are the employees for whom all statutory compliances are being taken care of in line with the laws of the land, so today when we look at it at levels that we largely provide temporary sources to companies, there are compliances that we need to take care of in terms of various statutory deductions of provident fund, ESI, PT, EC and so on which to some extent takes away nearly 40% of the employee's CTC, so on average salary of 20000 that we have for the employees, typically their take home is about 12000-13000 because of the various statutory deductions. What the informal sector does, is that it does not adhere to the labour laws of the country, it works below the radar in that sense and when we talk about a 20000 CTC typically about 16000 or 17000 gets paid to the individual employee as cash in hand and the larger margin gets kept by the vendors who effectively uses that to manage the system. So, the informal players are not covered by the element of the various benefits and law deductions that are required by regulation, that is the distinction we make between formal and informal.

Bobby Jayaram: Essentially all the let us say shopkeepers all over India, right, the shop assistance you see in every quarter?

Ashok Reddy: Typically most of these shopkeepers are entrepreneurial players where the owner runs the shop but if he employs people and does not pay them a salary in line with the minimum wages and statutory deductions and stuff, yes that employed workforce is informal, why shopkeepers, even if we take most of the large manufacturing or services companies, they also continue to effectively work on a model where they do not comply with labor laws and pay a lump sum as a direct contract payment to people deployed on the shop floor or as resources.

Bobby Jayaram: Have you seen any change towards the formal sector because that does not look to be changing any time soon?

Ashok Reddy: It is happening in a gradual manner, so I think it is, as we keep saying not switching on or switching off the light but it is gradual sunrise or sunset. From a perspective if we look at it for the last 6-7 years we have grown about 20-25% year on year and that did not happen because employment growth has been 20-25% in India per se and GDP has been growing at that rate, it is largely driven by the formalization of the informal sector and also adoption of the formal staffing by a lot of industries and companies that historically was not doing it. So our belief is it is happening in a gradual manner. Can there be a kicker or boost to this formalization, hopefully GST and other compliance driven activities of the government would add fuel to that formalization.

Bobby Jayaram: Thank you very much.

Moderator: Thank you. The next question is from the line of Raunak Shah from SJC Advisors. Please go ahead.

Raunak Shah: Congrats on a good set of numbers. My question is to do with the staffing and associate ratio, so obviously this side you guys have done a great job from kind of our perspective, I guess from the industrial perspective and as far as the employees and staff are concerned, are you finding that they are kind of struggling how to deal with the volume that suddenly increased over the last, kind of 4-5 quarters, is that becoming an issue or do you see more run away as far as that is concerned?

Ashok Reddy: The productivity play has not happened by sweating our resources more, I think this has come out primarily because of implementation of ALCS 10.2 that we had been working for 18 months on and also the app and portal rollout that happened towards the end of last year, so I think we have place to leveraging technology in a large way and also we have got in some senior leadership on the operations, customer relations front who have brought in better processes reporting control mechanism. We actually took a beating to some extent in our productivity play because we just moved from CRM platform which was Talisma

earlier into Salesforce and Salesforce as a platform is getting used to kind of volumes that we have to deal in on the mails and assigning front end staff, so I think that technology lever has been the key variable to productivity play and that will be the key lever to productivity play as we go forward. Hopefully, I can confidently say that employees have a better work like balance now with the implementation of 10.1 and Salesforce as against probably what it was earlier.

Raunak Shah: How much more room do you see in terms of being able to take this up over the next kind of one to three years?

Ashok Reddy: You know, I would like to put sky as the limit on that front, I think we do look to trying to take it to a much higher 100 numbers, but you know if you take it to a 1000 odd three years we should not be surprised.

Ravi Vishwanath: This activity of trying to improve productivity is an ongoing activity at our end, I mean just because the ALCS 10.0 got implemented in February, March of this year, it does not mean that there are no further improvements that are being planned or being implemented, we constantly keep reviewing, you know the productivity part and keep implementing new staff on an ongoing basis.

Raunak Shah: Thanks for that and also you mentioned about 55% or so of the associates are now on the app and also you spoke briefly about getting more revenues and value added services as the attraction improves, can you spend a bit more time on what these value added services are that we rolled out?

Ashok Reddy: One is from an app perspective. I think historically the way we used to service our associates because they are spread across 6000 plus locations while we have centralized operations in to Bangalore the primary mode of contact for the associates to us or for us to the associates was largely driven by call and mail, but when we started analyzing the queries that we used to get about 400,000 plus queries every month we realize that a lot of them were information related and a lot of that information resides in our system, so we said why do a pull of that information by associates calling us or mailing is why do not we do a push of that information, so the app roll out we did in the initial phase was primarily information access around their personal record, around their income tax declarations, around their salary slips, typically provident fund, things that they normally come to us for. What we are now building onto that aspect of attendance management as one value add service where an associate can be Jio tagged or Jio tracked in terms of where he is signing in from and especially if he is a sales guy and supposed to five to six calls, he can actually be tracked to where he went and stuff like that. There is also the element of reimbursement processing that can be driven through the app, so that has been built in, leave application

systems that have been built in, what we are looking at additionally is management which is to say that you know that is product information, sales monitoring, reporting of the sales activity and so on that will happen online through the app. There is also the element of HRIS and productivity as we look at it which is saying some elements of training can be imparted to the associate through the app, so these would currently form the spectrum of the value added services that we will drive through that.

Raunak Shah: I just have a followup on that first question, actually in the staff to employee ratio, how does the model work, do you kind of push a certain number of associates or jobs onto your staff or is it more of a pull model where they think they have a little bit more route to go and they can take on additional work and is there additionally any kind of incentive in place for them to handle extra associates as they come through?

Ashok Reddy: So there is an incentivization scheme by virtue of the productivity, the revenue handled and so on but I think it is a continuous review by the operations team which is the largest team actually in the entire element of the handling, to review their process, the technology implementation and the people training, these are the three variables we look at to continuously monitor the element of productivity enhancement with the people, so, one is, where am I making errors or why I am taking time or what is the kind of impairing the element of productivity from an individual perspective, so we have induction training, we have re-training, refresher training that happens on a continuous basis. That happens on a continuous basis. From a process perspective with about continuously looking and relooking at the process that we follow today to seeing if there is a need for reengineering and changing that and also I think you know some element of adult supervision and outside eyes have helped on that front to rebadging the process growth. The third element is the technology variable of saying how much can I automate? What is today offline or manual and how much of that can I automate so that it leads to productivity enhancement, so most of the asks that we have from technology gets factored back into the operations team to saying how does that lead to productivity and how many hours of productivity will I get which means how many more associates can I handle.

Raunak Shah: Thanks a lot and good luck.

Moderator: Thank you, the next question is from the line of Shariq Merchant from Quest Investment. Please go ahead.

Shariq Merchant: Thank you for the opportunity. Just wanted to understand how the fixed variable ratio has moved this quarter and also incrementally when you all are adding clients, are they coming under the fixed structure or under variable structure?

- Ashok Reddy:** When you are saying, fixed, variable you are talking about.
- Shariq Merchant:** The fee structure.
- Ashok Reddy:** It has kind of been flattish, so while we continue to make proposals, our starting premise for a proposal is a variable fee, that basis, the customer requirement or prior experience or existing relationships and so on, you know renegotiation of the pricing mar up happens, so we have not seen a quantum shift from the element of fixed to variables. It is kind of staying on a gross billing perspective, percentage is about 70% and variable is about 30%.
- Ravi Vishwanath:** In Q1 and Q2, the number of employees have actually increased by about 3000 employees, have increased more on the variable side.
- Shariq Merchant:** Would this essentially be new clients or when you negotiate with existing clients they are willing to move to variable structure?
- Ashok Reddy:** Associate growth could come from clients who are already in the variable mark up, you know those clients growing, when we go for renegotiation, it is very rare that a customer will shift from fixed to variable but if we look at it the new contracts are where we will be getting more from percentage basis.
- Shariq Merchant:** You all are able to negotiate markups in the fixed structure as well?
- Ashok Reddy:** To some extent, yes. I would not say that. When we look at marginal increase in our average realization per associate per month, it comes threefold. One is because of the percentage structure we have when we just go up the average realization goes up. The element of new customers who come on board some element of higher pricing that we have for the new mandate and the third element is the renegotiation that happens with old customers for a price hike.
- Shariq Merchant:** My second question was on the goodwill side, so could you help me understand what is your total quantum of goodwill from both these acquisitions that you intent to once the approval comes to write off over five years?
- Ashok Reddy:** We have about 80 Crores of goodwill.
- Shariq Merchant:** So that will be roughly 16 Crores a year of depreciation, but post tax it will be 11 odd Crores or so.
- Ashok Reddy:** Yes.

Shariq Merchant: What was the thought process behind writing off the goodwill was this keeping around the balance sheet?

Ashok Reddy: We probably get a tax break on it, you know instead of keeping in balance sheet, you get a tax benefit on the write off of goodwill.

Shariq Merchant: Essentially, driven by tax purpose only.

Ashok Reddy: Yes.

Shariq Merchant: Lastly on the long tail that we have in the 1500 odd clients that we have, how many would be the bottom 20% of revenues?

Ashok Reddy: About 600-700 customers would account for about 15-18% of our revenue. The only variable to that is that I do not know which of them are dwarfs and which of them are babies. It is a long tale with the hope that there are more babies in there than there are in dwarfs.

Shariq Merchant: But some from a cost of servicing point of view, if you are to work with only these customers at the moment, would you be working on a loss or a cash burn?

Ashok Reddy: We would not actually be working at a loss because most of these customers actually do not have much customization, when they are small the demands are lesser from the customers, so your ability to roll a standard product offering and not offer any other variables is higher, also your average realization for the smaller customers is normally higher than for the larger customers because as the customer starts growing larger he starts asking for volume discount.

Shariq Merchant: So, this would take care of the cost of servicing our client?

Ashok Reddy: Yes.

Shariq Merchant: All right. That is from my side. Thank you so much.

Moderator: Thank you. The next question is from the line of Surya Narayanan from DSP BlackRock. Please go ahead.

Surya Narayanan: Thanks for the opportunity. I have two questions, one is the value plus-plus services that you are talking about, how are you taking this to the market, you said that you have added about five clients in October on this model? Are you taking this mainly to new clients at

this point in time or are you also trying to take it to your existing clients especially the larger ones where you could derive significant value from this kind of model?

Ashok Reddy: The one I clearly have a captive audience that I would like to draw on, so the existing customers are being reached out to and being offered this, also in addition to that we are reaching out to new customers when you are having discussions with them, so it is a combination when I even look at the five customers we have on boarded, two of them are new clients who came on board starting with this service and three of them are existing customers who have extended their service in to this.

Surya Narayanan: So what proportion of your client base do you think you would have penetrated with this kind of a model so far?

Ashok Reddy: Right now it is very small number, so if we really look at it, 70% of our associate base largely into sales logistics and customer support and our belief is that a lot of these value added services are very applicable to this lot of employee base, so we have just started on the path which is why it is difficult for me to give a guidance on how that will grow but our belief is the addressable market is quite large.

Surya Narayanan: If I just look at it in terms of clients that you have added, you now have about 1800 odd clients as opposed to 1200 clients sometimes last year, so just from an incremental client addition perspective, you seemed to be adding a lot of clients, but the number of clients you are adding on this model seems a little low as a proportion of increment?

Ashok Reddy: Let me correct that, the 1800 is the overall client growth, it is 1500 for the staffing business. The 300 more are for the other HR services, businesses and so on, so it is 1500 but that is also a 300 client number growth. But having said that, the service we just rolled out in terms of an offer. It is all of one and half months old.

Surya Narayanan: Okay, understood and what kind of additional realization are we talking about here on the value plus-plus, you said that on an aggregate it is about 700 per associate that you have right now per month, so just a broad range or a broad percentage number?

Ashok Reddy: I need some more time for me to comment on that because you know with five customers, be a reflection of what it could be or what it will be, so I think you know as a proposal we are pegging it quite high but I think you know where the market will come to accept it and work it out, give us another quarter or two and we will be in a better position to make that stage.

Surya Narayanan: Sure, I understand, but any broad trend that you can talk to me about just basis is the fact that some of your competitors are already doing that in the market. So you must have done a market study?

Ashok Reddy: I think we look at ourselves to what we are and work up on improving on that front; I have not been benchmarking myself to competition on that front at least.

Surya Narayanan: Fair enough, understood, thank you very much for taking my questions.

Moderator: Thank you. We will take one last question from the line of Binoy Jariwala from Sunidhi Securities & Finance. Please go ahead.

Binoy Jariwala: Thank you for the followup question opportunity, just correct me on my understanding, so what you are saying on GST is that currently manufacturing sector do not get complete set off on service tax paid to us and therefore when GST comes in, it will get a complete set off, is that right?

Ashok Reddy: Yes.

Binoy Jariwala: Secondly Sir with GST expediting formulization of the sector, what kind of opportunities do you see in payroll and compliance from payroll and compliance coming up?

Ashok Reddy: We have been looking at opportunity. There are definitely opportunities in the payroll and compliance space and we do have an offering around that as well. We have our compliance business, which takes care of compliance, and we also have rolled out the payroll part of the business very recently and so these two businesses also continue to see some amount of traction as we move forward.

Ravi Vishwanath: We have got about 200 plus customers now that we are servicing on the regulatory compliance front and that number has been growing quite aggressively over the quarters, so our belief is that the regulatory compliance and the payroll services complement the product offering and will be a focus area for us.

Binoy Jariwala: Does GST play a role in this specifically?

Ashok Reddy: Not really, if we talk about regulatory compliance, we are really talking more about the labour laws than other taxes, so GST will not have an impact on payroll outsourcing and labour law compliance business but it would clearly have an impact on the staffing business.

Binoy Jariwala: Sir the manufacturing sector what percentage of the service tax paid they get a set off on, about 15% is the service tax paid, how much they can offset on?

Ashok Reddy: I need to come back to you on that.

Binoy Jariwala: Thank you. That is from my side.

Moderator: Thank you. Ladies and gentleman, that was the last question and I now hand the conference service to Mr. Abhishek Gupta for closing comments.

Abhishek Gupta: Thanks Ashok and Ravi. Thank you Margaret as well for conducting the conference call. Thank you very much. Have a good day every one of you.

Ashok Reddy: Thank you very much.

Moderator: Thank you. On behalf of IDFC Securities Limited that concludes this conference. Thank you for joining us. You may now disconnect your lines.