"TeamLease Services Q3 FY2017 Results Conference Call"

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MODERATORS: **MR. ABHISHEK GUPTA -- IDFC SECURITIES LIMITED**

Moderator: Good morning, ladies and gentlemen, welcome to the TeamLease Services Q3 FY 2017 Results Conference Call hosted by IDFC Securities Limited. 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 the operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded.

I would now like to hand the conference over to Mr. Abhishek Gupta from IDFC Securities. Thank you and over to you, Mr. Gupta.

Abhishek Gupta: Good morning, everyone and thank you for joining for the Q3 FY 2017 Earnings Call of TeamLease Services. Today we have with us Mr. Ashok Reddy -- MD and CEO of TeamLease Services along with N. Ravi Vishwanath -- CFO of the Company.

Without any further ado, I would hand it over to Ashok for his opening remarks and then we can open it up for the Q&A. Over to you, Ashok.

Ashok Reddy: Just wanted to update and I think the numbers are there. But effectively we have had a year-on-year growth of about 29% in net revenue and about 125% in EBITDA, PBT and PAT levels. I think the reality and fact that we have a much diversified portfolio of clients which we have always been harping on as a buffer to vagaries in the market. We have about 1,900 clients across industries; across regions have held us in good stead even with the demonetization and other events.

We have grown about 8,700 associates in the last quarter. So, effectively our associate count now is about 125,000 on that front. Even the NETAP program where we the trainee has been seeing a growth. We have now got about 19,400 trainees through that. I think all of this growth again, we continue to manage with existing headcount which we had intended to at the start of the year saying that a number of technology and process intervention that we had invested in last year were going to bear fruit in terms of productivity aspect our core employee and that kind of continues to play out. So, we are able to handle the element of growth nearly 16,000 odd employees with the same headcount that we had at the start.

One variable it has been the element of the average realization per associate while it is up from the comparable quarter of last year, it is down from the aspect of the start of the year and I think that an element of some renegotiations that have happened and also the volume play with certain clients that have come at a lower margin play. But I think what we are looking at while we continue to do this we have the value-added services that are ready to roll out and some discussions happening on that which will kind of compensate some of the that revenue loss that is rupee realization per associate.

The dispersion of the client base and play across clients with no concentration continues to be there. So, the top five, top ten customers account for about 14% and 19% of our net revenue. So, the diversified portfolio play I think has been a key variable for us and that effectively will continue as a focus element.

I think if we look at it the IT staffing business, the two acquisitions that we did earlier of ASAP and Nichepro have had complete quarter under us. We have done a small acquisition thereafter of Keystone, it is really small but it was more an acquisition done for the element of the client growth potential and the client and the margin play that existed and at the price point that it came we thought it was attractive to integrate with the opening balance of ASAP and Nichepro that we already had. So, we would continue to look at consolidating the three and thereon building it as we go forward.

The HR services businesses have seen an element of growth on the top-line but the margin play has not been as we had expected. I think some impact from the demonetization coupled with an element of receivables, delays that are happening onto businesses, so we do a provisioning once it exceeds 180 days of outstanding. There are not bad debts I think just delayed payments from customers we hope to flip that around as we go forward.

So, I think overall, the element of growth, the element of margin improvement, and the element of tight control on usage of funds and capital efficiency has been the focus and will continue to be and I think the quarter plays out on that front.

Happy to take any specific questions and answer that.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the Question-and-Answer Session. We will take the first question from the line of Abhishek Gupta from IDFC Securities. Please go ahead.

Abhishek Gupta: Two questions, one is on the co-staffing business and the other one on the other HR services. On the co-staffing front, we had talked about using the self-service app to drive value added services a couple of quarters back. So, what is the status there and what are the kinds of discounts we have given to larger customers, you said there have been some renegotiations driving mark ups down. So, how is it looking like over the next two quarters, three quarters that is on co-staffing? On the other HR services, you alluded that a couple of verticals are facing some receivable issues, which are those verticals and what is the growth plan going forward for other HR services? Are we looking at realigning ourselves in those verticals or what is the strategy there basically?

Ashok Reddy: So, on the staffing front, on the value-added services, we have five buckets of products that we have structured, one is attendance, second is sales reporting, third is asset tracking fourth is training and fifth is an HR IS module. All of these are tagged onto the app and portal that we have rolled out to clients and associates. Pricing for this has been between Rs. 100 to Rs. 400

depending on what the customers are going in for. None of these are effectively outcome based on us; this is a facilitating for reporting on all of these fronts. So, we have got about 15 customers who are ready to go live with this effective this quarter and obviously proof of concept being there and the platforms playing out to customer requirements and basis some customizations we will expand the element of the roll out as we go forward. So, I think basic platform for rolling out the value-added services is in place. We have been taking it to market there are the first 12 customers likely to go live full fledge manner in this quarter and I think once we have proof of concept with them customization as per client needs and feedback we will take it out in a bigger way into the next year. I think some of the renegotiations on percentage marks ups and also fixed marks up happened especially with some of the volume clients where they were looking to kind of adjust their cost of outsourcing which is where we have had the impact on realization coming to Rs. 691 against the Rs. 700 that we were earlier. I do not think we will have any more reductions on that front as we see it as this point. All the ones that had wanted and were in discussion have been done. So, I think we hold on that and hopefully as we go forward with value added services, we should be able to make that move up as we go forward. On the HR services front, I think the regulatory business, the permanent hiring business, and the training business all three have seen a growth in the top-line but clearly there has also been a receivables delay in all those three businesses. Not bad debts like I mentioned earlier but I think a delay which we are in follow-up with the customers and when we do have that collection loop closed out we will have a reversal on the cost taken on account of provision for bad debt. But I think as a way forward we are also just trying to see that if we are working with certain clients who are potential bad clients or if you are looking on working on certain mandates of training that are not aligned to the element of collections and payments and so on, do we restructure that into the next year. So, I think yes, we will be doing some element of review and restructure into the next year some lines of training that we did this year we will not be doing next year but that dose no mean that our growth will not happen in the business. We will focus on the line that effectively are making the payment so on. Similarly, even with certain clients in the hiring business or the regulatory business we will be taking a call whether we continue to work with them or realign to other customers. So, I think continuance of the vertical will there. There will be some element of review that we will take care as we go forward.

Moderator: Thank you. The next question is from the line of Deepak Poddar from Sapphire Capital. Please go ahead.

Deepak Poddar: Sir, my first question is around your organic and inorganic growth basically, what is your strategy going forward in terms of how you want to grow organically and how you want to grow inorganically basically?

Ashok Reddy: So, I think the organic growth element will continue as a focus area for us that are the largest base that we have and we will continue to have the diversified portfolio play and look to grow the business on that. On the inorganic front, at this point in time we have added the IT vertical with the acquisition of three companies and I think six months we were looking at consolidating that business into TeamLease and look at growth on that vertical as we go forward into next year. But I think we continue stay in the market to explore opportunities that would effectively add either clients or capability or traction to the growth for TeamLease. So, we I think over the year have generated about 30 plus crores of cash from business and we still do have a free cash of about Rs. 160 odd crores. So, I think opportunities if interesting and aligned with our growth is something that we will continue to look at.

N. Ravi Vishwanath: Also, you should remember that globally also the staffing industry has grown through what is called roll ups where the larger player, where the larger staffing companies have acquired smaller staffing companies in different jurisdiction, I guess the same would probably happen in India too. And we would be looking out for such opportunities as well.

Deepak Poddar: So obviously, we are looking for opportunities inorganic and we have been doing acquisition. So, you have to divide this 30% growth that we are doing between organic and inorganic over next few years so, how would that ratio would look like?

Ashok Reddy: The 22% to 25% growth in organic as we had stated which we have done in the last seven years is something that we are continuing to look to keep on the organic front inorganic will be a function of what all we bring on board and after acquisition I treated as organic thereafter.

Deepak Poddar: Okay, yeah, understood. And my second question revolves around your margin basically we are talking about value added services so, what is the steady state margin potential that we have or we might be looking at over the next two years to three years?

Ashok Reddy: Steady state margin realization on the staffing front?

Deepak Poddar: On the overall, overall business front.

Ashok Reddy: Net revenue realization or EBITDA?

Deepak Poddar: At the EBITDA level.

Ashok Reddy: I do not think I will give a projection on the number but I think like we were saying that intend between general staffing which is a low margin play but volume play and higher margin verticals of IT and other thing is to say that we can move up on incrementally on a recurring basis towards the 3.2% margin play over the next five years, six years.

Deepak Poddar: 3% to 3.2% that is what, right?

Ashok Reddy: Hopefully.

Moderator: Thank you. We take the next question from the line of Garima Mishra from Kotak Securities. Please go ahead.

Garima Mishra: Ashok, could you just give us some sense of how your IT staffing businesses are progressing? And for each of the three companies could you give us some sense of the current client base and the associate base and the growth expectations that you have for them in the coming year?

Ashok Reddy: So, we did the three acquisitions and we had mentioned earlier that we would look at three months to six months as an element of team integration and the business integration and I think that is going well at this point in time. So, ASAP has about a core employees of about 150 employees and 1,100 associates. Nichepro had about 24 employees and 150 associates. The Keystone effectively had about 100 associates and 5 core employees who will be moving in to our office. I think, the IT industry has an element of clustering of clients. So, if you look at ASAP, TCS, HP, Cognizant, Accenture, are their large clients. Keystone only has Mercedes-Benz as their clients and small numbers with others. Nichepro works with Google, Cisco, Adobe, and few others. So, I think effective what we are looking at and we have been having dialogs with all of these companies they do seem to be a statement of demand still. How the U.S. play out is going impact and stuff we have to wait and see but as of now they does seem to be an element of a demand statement and I think we will focus next year on growing this base of associates with these customers and there is also a long tail of customers that each of these clients have where the associates deployed are in single digit and I think we would like to build those relationships to increasing the exposure with these accounts. So, the element of focus to integration for this year hopefully done we will start focusing on growing the business and leveraging the long tail of client base to larger number while we continue to try and maintain the EBITDA margins, the higher EBITDA margin that these businesses carry.

Garima Mishra: Okay. At least on the IT services side where there has been some slowdown in business due to global demand etc., what kind of indications are you seeing for say hiring in the next couple of quarters? Is there some slow down there or things appear normalize, I understand that you mention that there is a statement of demand which is coming from there but just some more granularity on that?

Ashok Reddy: At this point in time, I do not think we are seeing an impact on the demand that gets outsourced to us. At a company level, if I look at it from hiring perspective surely the demand volumes have come down but in the outsource space the demand reduction has not yet happened. I can say it as of now and as this is being projected by the company for the next two quarters. And we do have a healthy pipeline of open positions even from the services companies that we are working on servicing. So, I think the aspect of the potential to grow in the services in the captives and in the product companies is still there at this point in time.

Moderator: Thank you. The next question is from the line of Nirmal Bari from Sameeksha Capital. Please go ahead.

Nirmal Bari: My question is on the IT staffing business, I understand that it is early days and we have just had one full quarter but the EBITDA margin that we are having of 16%, are there EBITDA margin sustainable or going forward as we grow the business they would come to a lower level?

Ashok Reddy: Our belief is that these are sustainable, the key variable obviously is to have the right mix of clients and positions to which we have to deliver and that is what I mentioned earlier. I think we do have and one of the key reasons for making the acquisitions was the opening balance of clients that we get and the long tail of the clients that these acquisitions have had which we intend to leverage to growth. Sustaining the numbers and growth we will look at by maintaining the EBITDA margin and that will be a key focus area and we believe at this point in time that they are sustainable.

Nirmal Bari: And sir, second on the IT staffing again, what would be our organic growth rate that we are targeting from these three businesses?

Ashok Reddy: So, I think 15 to 20% is what I would target at this point internally for the team given the macro factors and unknown variables that are cropping up. But I think we will be in a better position to target on that front probably after quarter.

Moderator: Thank you. The next question is from the line of Rajesh Kothari from Alfaccurate Advisors. Please go ahead.

Rajesh Kothari: Sir, what is the total provision you made for bad debts in the current quarter?

Ashok Reddy: Okay. Can I just take the next question; I will just get you the number from the financials.

Rajesh Kothari: Sure. And what will be your policy for providing for these bad debts?

Ashok Reddy: Anything more than 180 days ageing is provided for bad debts.

Rajesh Kothari: I see. And what kind of client profile is it, they are regular client, is it because of the demonetization effect or how do you see that?

Ashok Reddy: Look, I would not say because of demonetization effect frankly we deal with organized corporate sector. So, to that extent it is not really dealing in cash or impact of cash at their end but I think it has just been alibi for just deferring the payment. So, if we look at it from the institutional training front, a lot of it is with the government state government and central government programs and if we look at it from the element of the regulatory business and the firm business it is with the corporate sector. I mean multiple companies most of them having necessarily gone bad or whatever and kind of driven up on that.

Rajesh Kothari: And in the current quarter you know this IT staffing with the revenue what we are showing this is the for the full quarter for all the companies put together?

Ashok Reddy: Keystone is not included in that because Keystone acquisition happened in February.

Rajesh Kothari: And other two are the fully for three months?

Ashok Reddy: Yes, for the full quarter.

Rajesh Kothari: Other two are for the full quarter, understood. And Keystone will add how much to the revenue on a quarterly basis full quarter basis?

Ashok Reddy: They have about Rs. 7.5 crores per annum revenue, so it will be roughly about Rs. 2 crores a little less than Rs. 2 crores per quarter.

Rajesh Kothari: Understood. So, basically what you are saying is that on combined basis therefore Rs. 24 crores on a quarterly basis this on an annualized basis you expect it to grow it around 18% to 20%, that is what you are saying?

Ashok Reddy: Sorry. Just come again on that.

Rajesh Kothari: I am saying Rs. 22 crores is your current IT staffing services, added Rs. 2 crores from Keystone on a quarterly basis. So, that gives you Rs. 24 crores on a quarterly basis. So, once you annualize these and then on that you will grow at 18% to 20% that is what you are saying?

Ashok Reddy: I said 15% to 20%.

Rajesh Kothari: 15% to 20%, okay. So, basically then your operating profit per person and if I am not wrong it is at around. 275 something like that, am I right?

Ashok Reddy: Yeah.

Rajesh Kothari: So, that. 275 like when we were discussing you were saying that our target should be to get around. 325,. 375, over a period of time. So, how do you see that traction?

Ashok Reddy: If you see our margin play has been playing, so our fixed cost have been rather fixed for the last two quarters, three quarters. So, we have not had headcount increases other cost has been non-liner to the element of revenue growth and which is where the margin improvement has been happening in the general staffing business. And as disused earlier the IT staffing vertical has a higher margin realization per associate. So overall, a combination of these two should see us getting to that higher margin play.

Rajesh Kothari: So, this IT staffing is how much total number of employees in IT staffing?

Ashok Reddy: So, about a 1,250.

Rajesh Kothari: Including Keystone, excluding Keystone?

Ashok Reddy: Keystone has about 100 employees, 100 added there on.

Rajesh Kothari: So, Rs. 1,350 on Rs. 24 crores that is what you mean?

Ashok Reddy: Yes. I am sorry, to address your earlier question, it is Rs. 1.1 crores provision for the last quarter.

Rajesh Kothari: Okay. And would you mind giving the number for last full year how much was the…

Ashok Reddy: 2.3 for the last nine months.

Rajesh Kothari: For the nine months, I see and last year?

Ashok Reddy: 1.8 for the last year.

Rajesh Kothari: All right. So, is that part of kind of a regular kind of thing it is not something….

Ashok Reddy: We do not really have much in bad debts really, most of this get collected but it is delayed collection but just from a prudent approach perspective we provide anything beyond 180 days in every P&L.

Moderator: Thank you. The next question is from the line of Kashyap Jhaveri from Capital 72 Advisors. Please go ahead.

Kashyap Jhaveri: In one of the earlier questions you highlighted of the 30% growth overall in revenue that you are looking at about 22% to 25% will come from organic and rest could be inorganic. But if I look at the newer acquisitions, EBITDA is a meaningful number as a percentage of the consolidated then in that case one expect that trend to continue because incremental probably you would do only IT acquisitions?

Ashok Reddy: So, the top-line growth will come from both the general staffing and the IT staffing vertical. But obviously the volume play is in the general staffing side. When we look at margins the general staffing margin improvement is there is because of economies of scale and IT staffing vertical will overall because of a higher margin play improve the margin realization even with lower number. So, yes, the whole portfolio approach was that there is a volume and economies of scale play from the general staffing and value and higher margin play from the IT staffing side.

Kashyap Jhaveri: Right. And you also highlighted that over the next three years to five years, you are looking at margins of about 3% to 3.2% EBITDA margin, did I hear that correctly?

Ashok Reddy: Five years to six years.

Kashyap Jhaveri: Five years to six years. Let us take your standalone margins which is general staffing is about 1.4%, 1.5 odd percent, to take it to about 3% then this other value added services and IT has to be a very meaningful proportion more than 50%, 60% of the total EBITDA. My question is that in your peers that you would be looking at are there those kinds of acquisition targets available in the industry?

Ashok Reddy: We will have to play it out. So, I do not think all the growth in margin for us will come from acquisitions. I think we are going to have to have an element of an organic margin improvement by virtue of economies of scale, coupled with vertical and value added services complimenting it and also the HR services businesses scaling up to contributing to the bottom-line. So, I think a combination of all this is really what will drive our margin improvement.

Kashyap Jhaveri: And in standalone business versus about 1.5%, 1.4% that you did this quarter is it possible to squeeze in more through the same number of associates and that number itself can expect?

Ashok Reddy: You cannot squeeze from the existing and of associates. But I think, as we add more associates we do not have liner cost for that. That is why I said, in the general staffing business, margin improvement is a function of scale and economies of scale.

Kashyap Jhaveri: Okay. And this 1.4% what is the best case that we can do?

Ashok Reddy: I am not going to take a guess on that. I think we will play it out to the economies of the scale because we had mentioned at the start of the year that growth in this year we look to handling with our existing employee headcount and we have sustained that for the first nine months and I believe we can do that for the next quarter also.

Moderator: Thank you. We will take the next question from the line of Abhishek Gupta from IDFC Securities. Please go ahead.

Abhishek Gupta: Just one more question on the goodwill part. Ravi what is the goodwill number as of now after the Keystone acquisition and how are we looking to amortize it over the period? Any plans over there would be helpful.

N. Ravi Vishwanath: Yeah, the total goodwill after the Keystone acquisition would be about Rs. 93 crores and the plan is to amortize this over a period of ten years which means that the annual charge, net of tax would be about Rs. 6.2 crores per year and about Rs. 1.5 crores per quarter starting in the first quarter of next year of 2018.

Abhishek Gupta: So, Rs. 1.5 crores quarterly starting Q1 2018?

N. Ravi Vishwanath: Correct.

Moderator: Thank you. We will take follow-up question from the line of Kashyap Jhaveri from Capital 72 Advisors. Please go ahead.

Kashyap Jhaveri: What is the cash balance as of December 2016?

N. Ravi Vishwanath: Rs. 165 crores.

Kashyap Jhaveri: Okay. And let us say apart from acquisition anything else that you would probably want to do with such high cash?

N. Ravi Vishwanath: We are not a very capital intensity company that way. So, as we had always stated, I think we focus on growth margin improvement and capital frugality, largely the business investments required for growth and sustainably have been done. So, the cash that we have largely we will be utilized as we go forward if right acquisition opportunities comes up.

Kashyap Jhaveri: And apart from that probably at this point of time there is nothing on….

N. Ravi Vishwanath: Nothing else, right now that we need to really be spending capital on.

Kashyap Jhaveri: Of course, I think just some time back you went through an IPO and raise the cash from investors but returning that cash flows invested probably than could not be on the table right now?

N. Ravi Vishwanath: Not right now, I think I will be a little silly to do that.

Ashok Reddy: Too early for that actually.

Moderator: Thank you. As there are no further questions, I would now like to hand the conference call over to Abhishek Gupta for his closing comments.

Abhishek Gupta: Thank you, everyone for joining for the TeamLease Q3 FY 2017 Call. Thanks Ashok and Ravi, Thank you, **(Inaudible) 34.04** as well for coordinating this. Have a good day ahead.

Ashok Reddy: Thank you, Abhishek.

N. Ravi Vishwanath: Thanks, everyone. Bye.

Moderator: Thank you. Ladies and gentlemen, on behalf of IDFC Securities, that concludes today's conference. Thank you for joining us and you may now disconnect your lines.