"Expleo Solutions Limited

Q2 FY '24 Earnings Conference Call"

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MANAGEMENT: **MR. BALAJI VISWANATHAN – MANAGING DIRECTOR AND CEO**
MR. DESIKAN NARAYANAN – CHIEF FINANCIAL OFFICER
MR. PERIAKARUPPAN PALANIAPPAN -- CHIEF FINANCIAL OFFICER (NEWLY APPOINTED)

MODERATOR: **MS. ASHA GUPTA – INVESTOR RELATIONS, E&Y LLP**

Moderator: Ladies and gentlemen, good day, and welcome to Expleo Solutions Limited Q2 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 star then zero on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Ms. Asha Gupta from E&Y Investor Relations. Thank you, and over to you, ma'am.

Asha Gupta: Thank you, Seema. Good afternoon to all participants in the call. Welcome to the Q2 FY '24 Earnings Call of Expleo Solutions Limited. The results, press release and presentation have been already mailed to you, and you can also see the same on the Company's website. In case anyone does not have a copy of press release and presentation, please do write to us, and we will be happy to share with you all.

Representing the management today, we have Mr. Balaji Viswanathan, Managing Director and CEO; Mr. Desikan Narayanan, Chief Financial Officer; and Mr. Periakaruppan Palaniappan, newly appointed CFO. Balaji will start the call with a brief overview of the quarter gone by, which will be then followed by a Desikan, who will be getting into detailed financials. After that, we will open the floor for Q&A session.

As usual, I would like to remind you that anything that is mentioned in this call, which gives any outlook for the future or which can be construed as forward-looking statements must be viewed in conjunction with the risks and uncertainties that we face. These risks and uncertainties are included, but not limited to what we have mentioned in the prospectus filed with the SEBI and subsequent Annual Reports, which you can find it on our website.

Having said this, I will now hand over the call to Mr. Balaji. Over to you, Balaji.

Balaji Viswanathan: Thanks, Asha. Good afternoon to everybody who's joined the call. Thanks once again for taking the time.

Q2, July to September quarter financial results have closed yesterday during the Board meeting. We have had some positive momentum during the quarter compared to the previous quarter where we showed a marginal decline in our revenues. However, we still have pressures on our profit margin. This quarter, primarily the profit margin is around bench and some of the investments that we have done on people, so the people cost is slightly higher and the training costs and upskilling costs are slightly higher.

There was also some impact due to some onetime cost that which we had to incur in terms of consultancy and other stuff. But overall, the business pipeline looks reasonably good but will be a little soft in the next couple of quarters and in line with what you see in the overall industry as well.

We have signed some good engagements in this quarter, primarily on the digital space around DevOps and some part of digital transformation process that we have signed. But the larger deals are still in the works. And that is one of the challenges that we are trying to address as the customers start getting more budgets and increased their discretionary spends, which they are approaching with a little bit of caution in this particular month's time.

We had some challenges with the cash collection cycle for the last quarter because of some of the larger payments getting delayed due to some procedural challenges. But subsequently, during the month of October, most of them have been collected, and we are in the range of around 85 to 90 days now, which is our expectation is closer to around 80 days range, and we are very close to that target in terms of DSOs.

I will now hand it over to Desikan, he's unwell but he'll try and cover a bit of what we could talk about in detailed financials, but more he will try and answer during the question and answer. Over to you, Desikan.

Desikan Narayanan: Thanks, Balaji. Good afternoon to all. I will walk you through the quarterly performance. I will start with the quarter-on-quarter performance. The performance has been almost flat. The revenue for the quarter ended at INR 334 crores against INR 225 crores in the previous quarter, 4% up. EBITDA margin was at 15.1% against the previous quarter of 15.4%. EPS slightly increased to INR 13.2 against INR 13.01 in the previous quarter.

On the cash balance, as Balaji has mentioned, we ended up with a cash balance of INR 129 crores against INR 164 crores in the previous quarter. The DSO was almost flat at 119 days compared to 118 days in the previous quarter. It is important to note that we had a huge collection in October, around INR 126 crores. If I apply that in the DSO, it will in the range of 85 to 90 days.

Cash balance end of October is around INR 177 crores. Now, we talk about the year-on-year for the same quarter, revenue is a 6.6% increase, we ended up with a revenue of INR 334 crores. Please note that we had some onetime revenue in the previous year same quarter for an amount of INR 106 crores. To make it as an apple-to-apple comparison, if I do that, then my revenue increase will be around 12%. And since this revenue did not have any cost related to it as it was due to change request accepted by the customer after a long follow up, the comparable EBITDA margin from the previous year same quarter is 17.4% against 15.1%. So, the drop is mainly due to the payroll increase in this year. Net cash balance last year same quarter and the current year is almost the same INR 129 crores. With this, I'm opening it for a Q&A session. Please go ahead.

Balaji Viswanathan: Yes, I'd like to take this opportunity to thank Desikan. Desikan has decided to move and he's been with us for close to 8 years and almost 5.5 years as the CFO. I'd like to thank Desikan for all the help and support and in managing the organization as a CFO. And I would also like to welcome Periakaruppan Palaniappan, we call him Mani, as the new CFO who will take over from the 1st of December onwards. Mani comes with extensive experience in financial planning and analysis and many other finance functions. He was with Fractal Analytics prior to joining us, but he's been vigilant with multiple other technology services companies in the past. So, thanks, Desikan and welcome Mani. Over to the Q&A session.

Moderator: Ladies and gentleman, we will now begin the Q&A session. The first question is from the line of Rohit from iThought PMS.

Rohit: So, a few questions, Balaji. One is in terms of our engineering services business, if you can just give us some numbers, what's been the growth there? Or are we seeing any growth, if you can just share some numbers of that division first and then I'll get to the other questions.

Balaji Viswanathan: So, the Engineering Services business, there are 2 parts to it. One is what we do here locally within what we call it as the India, Asia markets, and what comes from the Group. The growth in the engineering services of the business that is transferred from the group, there has been significant growth. We're seeing good traction in the last 6 to 9 months that is probably the share of the group revenue is increasing primarily because of what has been transferred from the engineering services rather than the technology services where we have seen a decline even from the Group business as well.

As far as the direct business is concerned, we certainly see some slowdown in engineering services as well as we're not seeing the same amount of traction as what we used to have in the previous years because most of the work that we do in the engineering services, in the direct market is not so much in the digital space, like what we had mentioned earlier. And that particular segment is certainly not growing. And it's almost flat and in some specific segment around the production engineering it's same and there has been some amount of decline as well.

Rohit: So, I mean is it possible to give any numbers in terms of what are we doing because we used to give out numbers from a subsidiary standpoint when you are not listed. So, will you be able to share some numbers as to what the engineering division is doing right now? And also, right now, broadly, what would be the share of digital versus whole mechanical kind of engineering services in our portfolio today, a combined - direct versus business from the Group.

Balaji Viswanathan: Yes. I'll probably try and give it at an approximate range rather than getting into specific number per se and I'm probably trying and restrict it in the euro millions rather than in rupees. So, the engineering revenue, typically what we do in the direct business that is what we do directly with the end customers, normally has been in the range of around EUR 1 million or so in a month, EUR 1 million per month is what our normal revenue is, which is approximately INR 8.5 crores to INR 9 crores. That's what our range used to be earlier in the direct business.

And that is now, almost dropped by a little over 10% and it is in the range of around INR 850,000 to INR 900,000 per month or approximately INR 7.5 crores to INR 8 crores a month. And on the group business, we normally try and count it with a number of head count. We were close to around 550 to 600 people delivering for the group in terms of headcount last year. And this year, we are close to around 800 people doing the same amount of business. So, close to around 20% to 25% growth in the engineering services business that we do for the group.

Rohit: Got it. And so I think roughly, you can say based on the numbers that you've given about 40% would be direct business and the remaining would be Group business in engineering services, would that number broadly be correct?

Balaji Viswanathan: Yes. This time, it is probably even less or 1/3 is the direct business and 2/3 is the group business in the engineering services.

Rohit: Right. And sorry, the other part was around digital versus more mechanical kind of engineering services or non-digital, if you will, on the engineering services side of mix.

Balaji Viswanathan: So, the production or mechanical engineering work we do earlier used to be around 70% of the business and 30% was on embedded and digital services. But right now, it will probably be around 60% versus 40% that's the sign that is growing.

Rohit: So, Balaji, 2 years out, can the mix reverse from 40% can it go to 60% from the digital side.

Balaji Viswanathan: That is the line of the business that's growing Rohit, right now. And we expect that that's what will grow as well in the future. And our expectation is that it should be 60-40 or 70-30, maybe in a couple of years' time.

Rohit: And will that also have an impact to the margins over that time 2 to 3 year period?

Balaji Viswanathan: So, the Group's business will not have a very significant impact at the margin because the Group's business, as we all know, work on the cost-plus model. So, it may not really have too much of an impact. Most of the margin impact will be as we grow the direct business.

Rohit: Got it. Okay. Understood. So, from a direct to group business, are you looking at some optimal mix for the company in the engineering side. Obviously, right now, it is growing, the group business is growing. But from an overall, let's say, 2, 3 years, what's your sense there?

Balaji Viswanathan: So, at this particular point of time, we are not growing really aggressively on the engineering side as the direct markets because we need to build some scale. And that is something which we will get some work that we do with the group. But these geographies that is in India and the Asia geographies is where some of the traction is for both automotive and in the transportation segment. So, we will have a more aggressive direct market plan, maybe a couple of years down the line, but not right now. Right now, our focus is to try and build the capability through what we can do for the group.

Rohit: Right. Got it. And just 2 more questions. One, on the hiring side. So, obviously, this year has been a bit slow. So, what is our thought process, we had shared our plans to get to 10,000 people. So, if you can just share what are our thoughts right now, I mean, let's say, next year or whatever you can share right now, given whatever circumstances in terms of business that we are sharing.

Balaji Viswanathan: So, this year, as you have mentioned, the hiring has been slow. Even the campus hiring, we initially thought that we will actually hire little over 500 people this year, but we have stopped at around 280. It's not that we are not hiring, but we are not really looking at building too much of bench at this particular point of time. We have some amount of bits that we've already taken them. And because of that, our target of getting to 10,000 by March, 2026 will take some amount of rethinking and realigning to see when we will be able to get there.

But we have committed in making that investment, we are also making some capital investment and expanding into new premises. We are also trying to look at changing our work policy similar to what some of the other tech companies are doing of how much we need to work from office to how much we need to work from home. We will never go to 100% work from office, at least not in the near term. But in terms of having larger physical presence, which will actually help us in building our talent and retraining and reskilling. We are looking at that as well.

So, the hiring plans as of now, we are taking it quarter-by-quarter. We are not taking a very long-term commitment on what kind of hiring we are going to do. But the expectation is we will by first quarter of next fiscal, which is April to June quarter of next fiscal. Hopefully, we should see a more clearer trend on where our customers are likely to spend and how they are likely to spend and from which geography they're likely to spend, which will actually help us in firming up the plans for the subsequent quarters after the first quarter.

Rohit: Got it. And just last question on margins. I'll join back in the queue for more questions. So, I mean, this quarter, we saw a very sharp jump in the other expenses. I think you alluded slightly in your opening remarks that there were some consulting expenses, et cetera, which go there. But can you just explain like other expenses that we used to report were around INR 55 crores, INR 56 crores, post the merger. But it's now down to INR 60-odd crores. Are there any one-offs here? Or is it something else if you can just explain that? And I mean, how should we think about margins in the probably coming quarters?

Balaji Viswanathan: I'll probably give it at a high level. So we are quite confident to be there in that 16% to 18% range that we talked about in terms of EBITDA. There is no specific challenges that I see in getting that to that particular target number. Like what we mentioned, we have had some amount of transformation expenses, some consulting expenses, which we have incurred in the last couple of quarters. And there are also some rates and factors which are adjusted as well, which is what is showing in the other expenses in some cases. I'll have Desikan explain a little bit more in detail, but our expectation is that we should be comfortable in the 16% to 18% range going forward.

Desikan Narayanan: Yes. if I speak to the other expenses, a couple of things. One is we had some training expenses, which we did during the quarter that slightly increased. And one more aspect is the travel expenses. We did have quite a bit travel on the Middle East side, which has contributed to the increase. Of course, we will have some revenue impact also. But majorly, this is on-site presence asked by the customer, we did that. And last, but not the least, what mentioned by Balaji is that third-party consulting cost is also a little bit higher than what we used to have in the last quarter. So those are the major reasons for the impact.

Moderator: The next question from the line of Faisal Hawa from H.G. Hawa and Company.

Faisal Hawa: So, this target of 10,000 employees, if you study the previous concalls, it was at one-time calendar year 2025, when it became FY '25. And why don't we have a clear, yes or no answer to this, whether this still remains the target or no, that's one. Second is, I mean, we are after all a very small company. But yes, with a very strong parent. So why are we not attempting a bigger revenue growth rather than trying to hide behind the macro tailwinds or headwinds?

Balaji Viswanathan: We are not hiding behind anything at Mr. Hawa.

Faisal Hawa: No, no. See, finally, this is a very small company, and the base of sales is so small that I don't think we should be saying that there is a macro headwind that we are facing.

Balaji Viswanathan: Even the group is facing the same macro headwinds as well. We are all in the same business. But we are a small company. And even if you look at other comparable companies, they also have a similar problem. I'm not able to figure out what you're trying to indicate here.

Faisal Hawa: You look at many other companies, they have still grown much better.

Balaji Viswanathan: Yes, yes, tell me which companies are you referring to?

Faisal Hawa: Let me tell you, for example, there is HCL Tech which has a much better growth. There is Persistent Systems doing good.

Balaji Viswanathan: Yes, how much of it is organic and how much of it is inorganic?

Faisal Hawa: Please don't interrupt me.

Balaji Viswanathan: We are tracking all the listed companies. If you look at whether HCLs, if you look at Accenture, look at Wipro.

Faisal Hawa: So do I.

Balaji Viswanathan: One thing which I don't want to accept is that you are saying that we are hiding behind something. We are not hiding behind anything.

Faisal Hawa: No, no, because even the target of 10,000 employees, if you study the last concall, every time it is pushed.

Balaji Viswanathan: Do you think that we will just hire and keep them here. It's actually based on the business as well, right?

Faisal Hawa: So sir, if the base is so small, there has to be a strategy to fight to get a better sales growth. Every time the CFO refers to onetime gain that we made in the last year and say that because of that, the EBITDA has to be adjusted. I mean we have to forget the past and look at it in a new page rather than saying that we had one-time.

Balaji Viswanathan: Because we don't compare quarter-to-quarter, of course, we can always do that. If we have to compare quarter-to-quarter, obviously, it has to be compared quarter-to-quarter.

Faisal Hawa: I would argue because you listen to some concall transcripts, and there are at least 8 to 9 companies which have done much, much higher sales and with a smaller base of sales. I mean, see, I've been a shareholder with you last almost 2.5, 3 years. And I kind of feel this is more a strategy and a management issue rather than a headwind issue.

Balaji Viswanathan: Sir, of course, I can't change your opinion.

Faisal Hawa: I'm on all the concalls, except for one AGM that I missed in between, I think that there is a strategy issue here rather than any headwind issue or anything. A small company like us cannot be saying that there's a headwind.

Balaji Viswanathan: Sure.

Moderator: We take the next question from the line of Romil Jain from Electrum PMS.

Romil Jain: Sir, I just want to understand more on the order booking side. So, I don't know if we can share that data. But it would be great to understand what kind of order book do we have right now? And how it has grown maybe quarter-on-quarter or Y-o-Y in the last 1, 2 years? And also how does the pipeline going ahead looks like so that we can understand the prospects over the coming quarters?

Balaji Viswanathan: Desikan, do you want to take that?

Desikan Narayanan: See on the pipeline per se, of course, next quarter will be a little bit slow quarter. A combination of markets going down a little and also, we have a lot of vacation coming in, so that will have an impact on that. One more aspect which we mentioned in our write-up is that the customer is not actually getting into a big kind of an investment. They are going slow. They wanted to look at the market and do investment. That has impacted us on the pipeline side.

But it is not that bad. There is a drop, but compared to this quarter, next quarter will be a little bit softer. And we expect that to increase in the next calendar year, that is Jan to March, considerably. And since Jan, most of the companies in the U.S. and Europe, will look at coming out with a new budget, which they are going through now for FY '24, we see that will grow.

If you take into technology and engineering, we see that technologies have softened, but engineering is doing recently good. It is wait and watch for the subsequent quarter. And we don't see that it will drastically drop, but there will be a softening happening in the next 2 quarters.

Balaji Viswanathan: So, yes, just to get this into perspective, from where we see at this particular point of time, if our current revenue that we are projecting for the financial year is at the current INR 449 crores that we have done for the first half of the year, it would probably be in the range of around INR 910 crores to INR 920 crores compared to the INR 900 crores that we did last year.

And out of that INR 900 crores to INR 920 crores, the order book looks pretty much confirmed for, say, INR 850 crores to INR 860-odd crores and the remaining INR 50 crores, INR 60 crores is something that we need to build over the next 2 quarters per se. And If I were to look at how it was in the past, normally, anywhere between 90% to 92% is the confirmed order book every quarter, and the remaining 7% to 8% is what we accrue organically during the course of the quarter as we had.

And if I were to look at the starting of the year to the end of the year, normally, we start the year with approximately 50% to 55% comes from order book. And as we grow during each quarter, we add the remaining 45-odd percent. So if that gives you what Desikan mentioned and what I mentioned is how you could probably put that into perspective.

Romil Jan: Okay. And sir, on the slowdown, I just want to understand whether the slowdown is specific to let's say, some top 5 or top 10 clients that we have something specifically to that on the technology piece of the business? Or is it across the board the clients that we have. Just trying to understand what is exactly the challenge because last 1 or 2 quarters, we have seen the slowdown starting, and we expect another 2 quarters to be slow. So, just if you can give some more granular data, it will really help us to understand what's exactly happening.

Balaji Viswanathan: So, the challenge that we have is that we don't have any of the existing customers significantly slowing down, but they are not growing either. Because most of the engagements we expect a certain amount of growth in our existing customers and then we want to add new customers. The challenge is that the existing customers, the growth has not been in the range of what we expected normally. It's not in the double digits. That's what we see.

And the new opportunities are smaller than what we expected. And the sales cycles are getting a little longer than what we expected. Normally, the kind of engagement that we do, we don't sign any large multimillion dollar engagement. Most of the engagements are in the range of anywhere between $0.5 million to $2 million to $2.5 million. And the $2 million-plus deals are getting far and few. And the growth from the existing customers are either almost at flat or slightly more than what we were doing earlier.

Romil Jain; Okay. And sir, on the client mining side, if you can just explain, since now we are a small company right now and we have to grow in the coming years, so obviously, we would have strategized something on the client mining and how do we kind of keep growing. So one is, organically, we just tap the existing customers and go to the newer customers. But can we do something more aggressive there? Or maybe, if you would have already done, what kind of strategy are we looking there on the client mining side?

Balaji Viswanathan: So, we do have a key account planning and look at the top 10 customers and how do we actually find those top 10 customers, and that is not just based on the numbers, it is also based on the potential of customer as well. And for new accounts, the target that we normally have, which is what is probably the benchmark also is, approximately 90% of your annual revenue should come from your existing customers and close to around 8% to 10% of the revenue will have to come from new customers that you signed the last 12 months.

If I look at the last 2 years, we have been ranging at around 10% to 12% from new customers and around 88% from the existing customers this year. Close to around 94% of the revenue actually coming from the existing customers and our new customers, revenue contribution has actually slumped as well.

Even though the pipeline is there, I think it's taking longer to get the deals to close. And our business is that we are not a full-fledged system integrator, we are not end-to-end technology service forward. We play in some specific parts within the technology implementation life cycle.

So, if larger engagements are not happening, then that particular project also is going to see delays and slowdowns. And as the customers start spending more on transformation program, legacy modernization, moving to cloud, that kind of stuff then maybe basically that particular segment should start growing as well.

Romil Jain: So, just last question from my side, please. Sir, the digital revenue has increased. Still, we haven't seen that translating to the margin benefit. Because I think on the technology side also, there was a very strong engagement on the digital part of the business. So, are we seeing that increasing further from here and that will benefit the margins because 16% to 18% range, I remember you had always guided for that. But do we see exceeding that maybe in 2 years out from here?

Balaji Viswanathan: See, currently in the digital transformation or digital capabilities also come with a cost because the resources, whom we need to hire, the amount of training that we need to do. And some part of the teams who sit on the bench who will actually get retrained as well. So, while the margins are higher, the costs, at least when you're starting off or when you're in the growing phase within that particular practice, the costs are also higher.

And this time, like what I had mentioned earlier, we have a slightly higher bench costs and we also have a slightly higher training and up-skilling costs as well. But once we get to a size where the digital revenues, actually, contribute to the maximum over a 3-to 4-quarter period, then that will stabilize and that will actually help us in improving our margins as well. But it's a constant journey because the digital technologies are not the same. So what we do this year is not the same what we do next year. So, we need to keep the pace with what the market changes.

Moderator: The next question is from the line of Krunal Shah from Enam Investments.

Krunal Shah: My first question is that you mentioned that the parent business is on a cost-plus orders. So, can you help me understand what's the markup that we get in percentage terms?

Desikan Narayanan: Actually, this is more from a perspective of we do internal benchmark study and we have a Big 4 doing the study of business, what is the functional analysis and risk analysis, asset analysis we do and post that study, we come out with a margin percentage on the cost and then decide on that. It's arm's length pricing and confidential, so I could not tell you the percentage of margin.

But it is based on the study done by the Big 4, and we follow that because it is not only restricted to the India business, Group looks at it at a global level. We do a global transfer pricing study and also a local transfer pricing study, which will come out with this kind of a number.

Krunal Shah: So, sir, in this band that you guide for in terms of EBITDA? Or will be lower than that?

Desikan Narayanan: It will be around that.

Krunal Shah: Got it. Second question was on the management change. So, Mr. Prashant has resigned. So could you elaborate a little bit on what has happened, why has he resigned?

Balaji Viswanathan; So, why he has resigned, I think he'll probably be able to give you that answer. Unfortunately, he is not here on the call today. So, the management changes are evolving. And we also have a group level management org structure change as well. With those group org structure changes, there is more ownership on how do we deliver some of the global capabilities from each one of the locations and how the global capability leaders or people who are there in the respective country will actually contribute more to India. That's one of the reasons why some of roles in the respective countries also have some amount of responsibility changes and that could also be one reason. And the other one is, of course, what kind of prospects and opportunities that are available in the marketplace. We have a strong leadership team under Prashant. And I will manage this responsibility directly.

Moderator: We take the next question from the line of Mr. Rajesh from Banyan Capital Advisors.

Rajesh: So one question is that you were talking about earlier that there were consulting expenses and training and re-skilling expenses. So, is this going to be structural in the sense that it will continue for next several quarters? Or was it one-off in this quarter? And if it was one-off, if you could quantify what that amount is?

Desikan Narayanan: I think when Balaji was mentioning about it, he was mentioning about the other expenses. It is currently in the range of INR 61 crores compared to last quarter. And of course, training is something which has increased and the travel has increased. On the basis of travel, it will be flatten in the next quarter because we do not have much travel coming in next quarter due to the holiday season.

On the training side, it will soften in the next quarters compared to what we did during the quarter. So I'm expecting the cost to be in the range of INR 58 crores to INR 60 crores. That's the way I look at the cost to be coming out in the next quarter.

Rajesh: Okay. And that is sort of the baseline that we should think about going forward as opposed to what happened this quarter?

Desikan Narayanan: See, the one thing as mentioned quite elaborately about the digital part of the business, is that whenever we think about training to be done, we always think about whether there is a revenue generating capabilities therefore the investment, what we do in training. That is something which always we look at before getting into training or before deploying the hire and train, deploy people.

So, that aspect, we ensure then only we invest in training, otherwise we don't do it. I mean the current state of things, even though the digital revenue is growing, it also contribute to the new technology, and we need to be updated in those technology and to get right people for that technology. And obviously, technologies are dynamic, and we need to have some kind of investment, we need to do for getting those business.

And having said that, if you look at even in the quarter and the coming quarter, we see more of a digital business, which is getting our revenues into a flat kind of a thing, so that way, now the dynamics are changing, the traditional QA kind of business is not that much growing and digital is growing. For that, we have a certain investment which we need to make. That is a combination. But we wanted to restrict it only, and we are always very mindful about investing on training to ensure that we do get a return on that investment. That's the way we look at the training as well as deploying people or including people.

Balaji Viswanathan: So, just to add to what Desikan said, that what we look at is what are these other expenses that we are spending as a percentage of cost and as a percentage of revenue as well. And some of these quarters where we have to make the investment in anticipation of some business in the future, the cost goes a little higher. But simply, we try to remain within the range of both the other expenses in terms of costs and in terms of revenue.

Rajesh: Understood. And my second question, Balaji, is that the guidance you gave for this financial year revenues, does that include anything inorganic or this is purely organic. Let's say, if you do any acquisitions between now and March, that would be an additional revenue.

Balaji Viswanathan: That's right, yes. This is only organic. Inorganic, we don't know and we can't expect what is likely to happen.

Rajesh: Okay. And are there any inorganic opportunities that you think we can convert in the next 6 to 12 months?

Balaji Viswanathan: So, as part of our normal business, Rajesh, similar to what we did last year, we are looking at options, but we are not sure as to whether there's anything that is going to materialize before much. We are working on a few which are in line with what our strategy is and the size that we are looking at. But we can't say with certainty whether something is going to happen or not.

Moderator: The next question is from the line of Kshitij Saraf from Tusk Investments.

Kshitij Saraf: Yes. sorry. Sir, my question was in terms of the CAGR, when you say you are looking to go to 10,000 employees and capabilities for the direct business later on. What are the kind of capabilities you're investing in or looking to invest in, which would give you probably the long-term annuity if you go beyond $1 million to $2 million deal value and sort of how do you plan the journey from here to, let's say, 3 to 5 years from now?

Balaji Viswanathan: So, in terms of what kind of capabilities we are trying to look at, we mentioned this a few years back as well in terms of strategy, what we're looking at is we are not trying to become a system integrator and build capabilities across the life cycle because one, is expensive and there are more competition doing that work. We have been a quality assurance, quality engineering company. And what we are trying to do is to shift left and shift right within that space, around business analysis, the implementation, support function and DevOps and automation. And that's the area that we have been investing as well, specifically on DevOps automation, data management, cloud migration. That's the area that we have been investing in.

And the last acquisition that we did was also primarily around the data governance and data quality, which will actually help us in making our entire offering around the entire assurance services or insurance services more complete. And in the engineering services, it's around the digital engineering, software engineering and also about embedded engineering piece, and that's where we are looking to grow, and that's where we see opportunities to grow as well.

And whatever we are trying to do, whether it is small acquisitions or what we are looking at in terms of our capability building with training and other stuff is also primarily around these specific areas at this particular point of time. And that we see opportunities, as everybody knows, it's primarily around the digital technologies, but also what supports the digital technologies as well which is around the data management, which is also very critical for both AI and machine learning and generative AI and other spaces as well.

We have also started a new program with a company for generative AI, how it will help us in the quality assurance journey. We have an external consultant whom we have taken along with our internal teams who will do specific work on using generative AI for the assurance services as well.

And that's where we see our opportunity growing. We don't think that we will sign $100 million or $200 million, but our objective is that to combine these 2, we can certainly go to the $5 million, $10 billion opportunities internally, and we can support the group which signs the larger deals with customers with these specific capabilities which we have in India.

Moderator: We take the next question from the line of Mithun Aswath from Kivah Advisors. As there's no response from the current questioner, we move on to the next question from the line of Amit Tavani, an Individual Investor.

Amit Tavani: So, the first thing is that can we get some more granular details like how much was the growth in automobiles and how much was the growth in Financial Services? Because I don’t think there is that much granularity in the presentation.

Balaji Viswanathan: Desikan, do we have industries covered in that?

Desikan Narayanan: We did have one slide showing about how much this technology versus engineering and what is the mix of both quarter-on-quarter and the year-on-year same quarter maybe that will provide and where engineering is majorly for auto, aero and transportation business and technology majorly capture the BFSI. I think that will show you the mix change during the quarters. That can give you an idea about how the engineering part of business is running and also the technology part of business is running. That may give you view of it.

Amit Tavani: Can you give a sense of how the market is performing versus how we are performing because what I am noticing is that people who are in aerospace and in automobiles are doing exceptionally well.

Balaji Viswanathan We can certainly share the next level of detail for this particular quarter or for the first half of the year in terms of how it is. But like what I mentioned at the beginning of this call, the business that is coming in for auto and aero from the group to us, we have seen significant growth in this half of the year compared to what we have been able to sell direct in these markets.

Amit, also, the other thing is that when you look at auto and aero, what you do locally for the Indian customers, the margins are relatively lower. So, the way we look at it is that it's probably easier to build the capability for the work that we get from the Group rather than doing it locally here because most of the aerospace business is either coming in from Europe or from the U.S. That's where the quality of the work and also the margins that you do is also higher.

And that's something which we are not operating at this particular point of time because Europe is managed to the group, and that's growing. In U.S., we are not a predominant player at this particular point of time in that market. And we haven't really done that investment to grow in that particular market so far. But we can certainly share with you what the group versus a direct trend for the first half of the year.

Moderator: The next question is from the line of Mithun Aswath from Kivah Advisors.

Mithun Aswath: My question is more a little bit in terms of what is your strategic thinking at the global level. I think, Rajesh, was on some calls before, but just the thinking of the group of why merging all the India businesses into this company, the Puna-based business, which is unlisted because we were delivering maybe stronger margins and growth when we were stand-alone. And the expectation was with the merger you could grow even faster.

So, I just wanted to understand because I think when Rajesh was on the call, he was talking about India being a very important destination for outsourcing. And obviously, you piggybacking on that growth. So, I just wanted to understand from the group level, what is the thinking of the Indian entity because there were some reports that there could be an exit of this India business as well in the newspapers.

So, I just want you to put to rest if that is not true and where this is going in terms of the next 3 to 4 years? And maybe if even Rajesh can be on the call next time, it will help minority investors to get an understanding of what is the strategic direction of this listed company.

Balaji Viswanathan: Sure. I'll try and answer this. I obviously can't talk about the speculation on the group exiting India business because that's something which I'm not aware of and not even came across those kind of thoughts. Of course, there were some media reports about somebody buying us, but that was not only for India is what my understanding is.

But nevertheless, the group strategy is that they have 3 centers, India, Morocco and Romania or rather India, Romania, Morocco in that order. Whatever group's business that they want to bring because that's what the customer demands are and that's both the cost and the scalability advantages. India is not being looked at only from a cost perspective, but also scalability.

And the expectation is for the group's business to grow in India. And I had mentioned when we were talking about the merger as well when the merger happened, the group business that we were doing was approximately 25%, 25% to 26% and the direct business was around 74%. And by 2025, the end of financial year 2025, which is March '26, we are expecting that the group business will be 45% and the direct business will be 45%, which doesn't mean that the direct business will not grow. But the group business is supposed to outgrow the direct business by that much.

And the group business, even though might be at a much higher margin, but it is a far safer and lesser cost work for us because we don't really have to invest in the sales element. And that's what the plan is as well, and that particular strategy still stands. And at this particular point of time, as of first half of this year, the group business is approximately 33%. So, it's grown from around 25%, 26% to 33% of the total business.

And the direct business, unfortunately, for this 2023 has not really seen a significant growth per se. But we are still growing in a marginal 2%, 3% per quarter range in the direct business, which will translate to lower 10% of the direct business growth. But the Group business is growing faster in terms of headcount, and that's what the plan is. I'll certainly request Rajesh to be there on the call, 2024 hopefully, he should be here during that time. But I'll certainly request for him to be there to answer any questions and concerns.

Mithun Aswath: My next question was just on obviously, maybe because the group business is becoming a larger portion, is it difficult for you to kind of model what kind of growth your company is going to deliver? Because on a quarter-to-quarter basis, there is a bit of variation. And actually, this quarter, you saw some quarter-on-quarter growth in revenue despite you guiding for maybe kind of subdued quarter.

So, I just wanted to get a sense on that. And are we at the worst in terms of the margin picture? And when things pick up from the global side from your parent, you see overall revenue starting to pick up. And also wanted to know whether the parent has any exposure to the U.S and they still haven't made that step. So, just wanted your thoughts on that?

Balaji Viswanathan: Sure. So, the Group business is more predictable, but one thing I just wanted to add, whatever group business that we are getting is not an existing business that has been delivered, which is moving to India. It's only whatever new businesses that have been won are moving partially to India because that's something which we are including as part of the solution and as far as selling to the customers. The existing business moving into India is a little slower I mentioned even earlier as well because the markets in which we operate in the group are more protected markets, you can't just reduce the number of headcount and that market can move to India because there is a lot more impact in many of those elements as well.

And this year, the group also is going to grow close to around 10% to 11%, even though the market is a little subdued. And that's what we are seeing in our group headcount growth as well for this year. Hopefully, this should help us in the coming quarters once this particular trend because it is something which has been happening for the last 3, 4 quarters. Once we are able to see the trend and how we are able to tap the pipeline that the group is winning actual work for us, here in India, we should be able to make that at least the group revenue side more predictable for the full year rather than quarter-on-quarter.

And for the direct markets, we anyway have our own budgets, which we defined and make sure that we go to meet those particular budgets. This year, like what I mentioned, we are not able to meet some of those targets which we set for ourselves. But hopefully, 2024 should be different.

Moderator: Our last question is from the line of Amit Tavani an Individual Investor.

Amit Tavani: Thank you for allowing for a follow-up question. The margins seem to have dropped in the last 2 quarters, is it related to some wage hike that we have taken this year that has not been able to pass on or is it related to some rate reduction that has happened from the client front, can you give us some color there?

Balaji Viswanathan: Sure. So, yes, the first point is right because last year, as we all know, in 2022 to 2023, there was a significant amount of wage increases that we had to go through during 2022, which is impacting us in 2023 as well. And obviously, there is a lag between when we do the wage increase to when we'd be able to translate that to the customers. But that's only one part of it.

The other part is this year considering what we were not expecting that the year is going to be slow. So we've made some investments on talent, people, bench service also is contributing to some part of the costs. And the other one, Desikan, do you want to add. I'm not sure about that the rates and taxes piece. Do you want to add anything more beyond the cost piece.

Desikan Narayanan: No. On the people cost, of course, compared to the last year, the current year, we have increase in the headcount. And also, it contributes with the increase in headcount.

Balaji Viswanathan: Not just increase in headcount, but the cost per headcount as well, particularly in the digital...

Desikan Narayanan: Correct. So, first one is the headcount increase quantity wise and also from the increment perspective, it will also contribute to the overall increase in the cost and that is one part. And as I mentioned, compared to the previous quarters, we had a travel increasing for the APAC and Middle East region.

And of course, the last but not the least is the training aspect of it, which we are doing it for the purpose of generating more revenue and generating our capability. Those are the major aspects of things and also the consulting fee because where in case if you don't have an in-house, we need to go for a third party.

If I look at compared to last year, where we had one client having a lot of consultants that has reduced. But having said that, we do have some increase on a quarter-on-quarter basis on the third-party consultant costs for ensuring that we get the revenue, which is on the table and not waiting for us to improve our capability in-house and deliver it. So, those are the couple of things which I can say that is the contributor for a cost increase compared to the last year.

Amit Tavani: Since that we have realized that the demand is not as per our expectation. Do we expect to go a little slow on hiring in the future? Or are we still looking to hire?

Balaji Viswanathan: No. We have taken that quarter-on-quarter now because I mentioned this earlier in one of the other questions as well, earlier, we were planning to do almost 500 people to be hired from the campuses. We reduced it to 270 because we are not seeing the same level of demand. And even the other hires, we are actually taking a look quarter-on-quarter rather than hiring well in advance. But obviously, that will also impact our ability to grow in the future. So, we are trying to balance between the two.

Thank you so much. Seema, we can probably close the call. Thank you so much for all the investors and participants who joined us today. I wish you all a very happy, safe and colourful Diwali and hope to see you all in the next call again. Thank you.

Desikan Narayanan: Yes. Happy Diwali to you and your family. Thank you very much.

Moderator: Thank you very much. On behalf of Expleo Solutions Limited, that concludes today's conference call. Thank you for joining us, and you may now disconnect your lines.