Q3 FY2020 Earnings Call Transcript - February 04, 2020

CORPORATE PARTICIPANTS

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Mr. Ankur Maheshwari - Head Investor Relations

Moderator: Ladies and gentlemen, good day, and welcome to the Firstsource Solutions Limited Q3 FY 2020 results conference call. As a reminder, all participants' lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touch-tone phone. Please note, this conference is being recorded. I now hand the conference over to Mr. Ankur Maheshwari from Firstsource Solutions Limited. Thank you, and over to you, sir.

Ankur Maheshwari: Thanks Bikram. Welcome, everyone and thank you for joining us for the quarter ended December 31, 2019, earnings call of Firstsource.

To take us through the results and to answer your questions, we have with us today Vipul Khanna, our MD & CEO and Dinesh Jain, our CFO. We will be starting this call with a brief presentation providing an overview of the company's performance, followed by a Q&A session. Please note that the results, the fact sheet, and the presentation have been e-mailed to you, and you can also view this on our website www.firstsource.com.

Before we begin the call, do note that some of the matters we will discuss on this call, including our business outlook are forward-looking, and as such are subject to known and unknown risks. These uncertainties and the risks are included but not limited to what we have mentioned in our prospectus filed with SEBI and subsequent annual reports that are available on our website.

With that said, I now turn the call over to Vipul Khanna to begin the proceedings.

Vipul Khanna: Good afternoon, everyone. Thanks for joining. Hope the year has started well for everyone, although it seems like a long time. We're already into February. Times are flying by. Let me give you a quick sense from the presentation which Ankur referred, and then we can open up for Q&A.

Q3 for this year has been a solid quarter for us across most parameters despite the traditional seasonality of this quarter. Our revenues came in at Rs 10,535 million which is quarter-on-quarter growth of 7% in rupee terms and 4.7% in constant currency. This translates to a year-on-year growth of 6.9% and 8.3% on a constant currency basis. This growth has largely been secular across the segments that we play in, with Mortgage and Healthcare scaling up well with ramps in new businesses. We'll give a little bit more color as we go along in this conversation.

Operating margins came in at Rs 1,182 million which translates to an EBIT margin of 11.2%. As you may recall, from the last quarter, we've started to use this as an operating parameter of our operating performance. At EBIT is 11.2%, we have an increase of 239 basis points on a sequential basis and a growth of 35.9% in rupee terms. Year-on-year margins have declined by 66 basis points. And again, as we mentioned in the last call, this is largely on account of the investments for growth in digital that we are making relative to the last year.

Continuing with the same, profit after tax came in at Rs. 895 million or 8.5%. This represents a quarter-on-quarter margin expansion of 170 basis points and a year-on-year margin contraction of 150 basis points. And finally, this translates to a Q3 EPS of Rs. 1.29 as opposed to Rs. 1.41 in the previous year. Overall, our revenue and operating margin continue to track what we had set out for this year.

Next slide gives you a consolidated view and the different line items for Q3 as well as the 9-months ended FY20. The only thing I wanted to call out here is that our YTD 9 months operating margin has come in at 10.8% which is at the lower end of what we had forecasted. So, we have already hit the lower end of our operating margin in YTD December '20.

Quick qualitative comments. Our headcount increased to 20,482. Of this, 10,982 employees were in India and the remaining 9,500 were outside India, which means about 481 employees added in Q3 and majority of this addition has been offshore across the businesses that we serve. We have been very focused in Q3 on strengthening our talent sourcing, especially in UK, as well as increasing our retention. We are pleased with how the needle has moved thus far. Our onshore attrition has come in at 46% annualized compared to 55% in Q2. Some of the actions that we have taken are strengthening our operational and HR leadership teams. We've done some tweaks to our comp structure to make it progressive and linked to the skills which people bring to the job. And we're also looking hard at the recruitment mix across our business needs and across our centers there. A lot remains to be done, but we are happy with the progress that we have achieved thus far. On similar lines, offshore attrition came in at 36% this quarter as opposed to 40% in the previous quarter. On the foreign exchange side, we have outstanding foreign exchange hedges of $36 million and £83 million. And for the next 12 months, we have coverage of 60% in USD at Rs. 73.6 and 90% coverage for GBP at Rs. 101.9.

Let me give you a little bit of colour by segments. As I mentioned, all business units have grown quarter-on-quarter. Mortgage has led the pack and is about 19% of our total revenue for this quarter. The macro tailwinds with the benign interest rate environment continue to help the origination business across our clients, including new wins, strong demand for origination. And we expect this will continue for at least the first half of next financial year. But we are also as much focused on building the services side of the business. The services side grew 30% over this period, and it now contributes about 40% of our overall mortgage business. And given the trend of digital that we've been talking since the last couple of quarters, we have early workings and ideas, a couple of business processes and service ideas in the mortgage value chain. And given our continued push to go for the mortgage value chain, we've also kicked off our underwriting academy to build the skill sets, both on and offshore, for this demand on the underwriting side. So, coupled with the advanced skills and automation, we see good set of modes developing for us in the mortgage business. Collections business also scaled up well despite the seasonality of the headwinds of the holiday season. The digital collections product continues to do well, and we're seeing good traction in the card and the traditional student loan market that we play in. We're also starting to see some early push into the fintechs for taking our digital collections capability.

On the industry verticals, coupled with strong growth in Mortgage, collections as well as the UK BFS portfolio, BFSI is now nearly 43.7% of our total revenue. It continues with the trajectory, if you look at the slide in front of you from last year to last quarter and now. This continues to be strong and now the largest vertical we have. Others are also growing. But in the overall scheme of things, their percentages start to decline, but overall, we've kind of shown growth quarter-on-quarter.

If I take a quick view across the geographies, US is now 63.3% of our revenue, UK is 35.3%, and others is 1.4% – clearly reflects the growth in mortgage and collections businesses which are primarily North America for us today. And also, that's the larger market. But we are as much focused on the UK, where we have our strongholds in the CM area, and we see a good deal pipeline in the CM as we look at now and the next quarter or so.

By delivery, offshore is now 25.2% of our total revenue and onshore, which is US and UK, is about 74.8%. This is by design. As we look towards CM, healthcare, and mortgage businesses, we are conscious of growing our offshore portfolio, given the superior margin profile that, that business has.

As far as client concentration, kind of the same as before. Our largest customer, there is an element of stability. We have a couple of smaller ramps going up with them. We've engaged with them on the whole attrition and retention situation. The comments I made earlier about the progress there also bakes in the results for them. There is a good alignment there. And we don't expect any surprises in the near term from that account.

Let me quickly close by giving a quick sense on the business outlook, and then we'll go to questions. We had good traction in Q3. We had 3 new logos added in Mortgage and 2 in healthcare. As we continue to digitalize our CM offering, we are seeing good deal traction there and it has also been recognized. We won a couple of good awards in the UK for our solutions for Now TV as well as giffgaff. And also, recognition in the US from our healthcare automated audit solution. BFSI, healthcare, and Utilities continue to scale well. We see the momentum going into next quarter.

As I've been saying, Digital is a key focus. Couple of areas to report on. Our Chief Digital Officer, Sundara Sukavanam, is on board and his primary focus will be to build a practice for intelligent automation and analytics as well as work with business leaders to develop digital offerings. Digital collections is an example of a digital offering that we're going to take on. And as we look to other ideas across our businesses, he will work with business leaders to translate that into a BPaaS solution. As I mentioned, digital collections are getting good traction. We have a couple of interesting dialogues with fintechs to help them on the collections side using our offering. And I'm also happy to report that our digital collections offering has now been adapted for the healthcare receivables management. With our first anchor customer we've implemented it, it has gone well and now the focus is to take it to the broader market.

Finally, for the FY20, our revenue growth is likely to be around 7.5% to 8.5%. We had earlier given a range of 7% to 9%. As we come to the last quarter, we've narrowed the band to 7.5% to 8.5%. And operating margins, we had given you guidance of 10.8% to 11.2%. We've kind of taken the lower band up, and now we are forecasting between 11% to 11.2% for the full year FY20 as far as operating margin is concerned.

That's all I have. Let me open it up for your comments and questions, please.

Moderator: Ladies and gentlemen, we will now begin the question & answer session. We will wait for a moment while the question queue assembles. We have the first question from the line of Pavan Ahluwalia from Laburnum. Please go ahead.

Pavan Ahluwalia: Vipul, a couple of questions. First of all, it's great to hear that you've put the digital head in place. There were a couple of other positions you mentioned you might be looking to fill, specifically a US sales head, a head of CM, and an overall delivery head. Any progress on those hiring decisions? And over what period of time would you be putting these individuals in place? Also, if we could get a little background on Sundara and why you think – I don't know if it's a man or a woman – why they'd be a good fit for this role?

Second, on the cost issue at Derry that had created problems last quarter. Obviously, we've seen a margin normalization because some of the one-offs last quarter weren't there this quarter. I'm just curious about how we see that cost situation evolving at Derry. Have we been able to put in place levers that might mitigate that?

Finally, as we move in the next several months to potentially build out parts of the organization that have been underbuilt, which, obviously, over time, will expect us to achieve a higher revenue growth run rate than what we've achieved so far, do you expect that we'll be able to maintain margins roughly similar to what we're doing right now? Or do you think that the steady-state margin adjusted for the reinvestment you need to do in sales, business development, platform development, all of that could be significantly lower than present margin run rates?

Vipul Khanna: Pavan, let me try to address the question that you raised. Sundara is a male. He is based in the US. He has a deep background of selling technology services. He has been part of the CIO organization, so the user organization to take some of the new tools. And for the past few years, he was running the intelligent process or RPA practice for Cognizant, that's what was his responsibility. As we brought him on, clearly, RPA, as we're calling it or intelligent automation that's holistic that takes care of intake, automation, workflow capabilities, and then as the world evolves to machine learning and AI, kind of across that spectrum, we have the capabilities and partnerships to help our clients whether on outsourced contracts or retained operations. That's one focus that he's going to drive. And second, build partnership with SaaS platforms so we can start to think of pretty specific BPaaS ideas to take to our clients. That's his background and mandate.

On the other position, we made good progress. I expect between now and end of March, a couple of other key positions to join in, and some will overflow, given some of the geographies have longer notice periods. A couple of more positions will flow into Q1 of next year coming on Board amongst the 3 or 4 that you have outlined. Those are your first 2 questions on the leadership team.

Pavan Ahluwalia: Just to clarify Vipul so by June, you will expect all of these to be filled?

Vipul Khanna: Barring any unforeseen, yes, majority of the leadership positions should be done by the end of Q1 next year.

Now as far as UK and Derry, etc., is concerned, as I mentioned, a few examples of actions that we have taken. A very close, hard look at who we're hiring, how we're engaging them, how we're measuring them, how we're paying them across the life cycle. Some of the actions are kind of long ranging and they will play out in this CY20. We were very focused on making sure that we were harnessing the growth opportunities. We were not doing any revenue leakage as well as meeting our service commitments. That was our priority focus in Q3. I think they should start to play better and the financial upside that we expect from some of these actions on revenue and margins, I'd expect that to start to play through in the next couple of quarters. First, Q3 was very focused on making sure that we met our commitments, and we captured the opportunities that were up there. But it's a long haul, right? We are very focused that a lot remains to be done as far as attrition and operational resilience is concerned of our UK operations, especially so that we have a decent pipeline of growth opportunities. I want to make sure we have the right foundation to be able to harness and deliver on those opportunities.

The last question you had was on the margins going forward. Again, as I had said, we've modelled in an element of investment for growth, both in terms of leadership as well as sales capacity in the forecast that we had set for March of '20. How it plays out next year, that budget work, we have just started. And hopefully, when we come to the end of Q4, we'll have a better position for outlook for next year, baking in the growth investment as well as how much we can harvest from operational excellence in our existing portfolio.

Moderator: We have the next question from the line of Dipesh Mehta from SBICAP Securities. Please go ahead.

Dipesh Mehta: Sir, just a couple of questions from my side. If you can provide some perspective about industry outlook; how you look at BFSI, healthcare Payer/Provider side, telecom, media? And then to some extent, if you can provide perspective on the healthcare customer management side. How you expect next quarter as well as next calendar? If you can provide some perspective.

Second question is about the seat fill factor. This quarter, it seems to be much higher, 87%. Historically, we have generally remained below 85%. So, this quarter, it seems to be unusually high. If you can provide some perspective there.

Third question is about CAPEX. First 9 months, CAPEX seems to be on a higher side. If you can provide whether it is largely growth CAPEX and likely to continue going forward or there is some one-off which led to a higher number in first 9 months? And a related question is about, if you can provide OCF and FCF number, operating cash generated in first 9 months, and free cash flow in 9 months.

And the last question is about Brexit. How one should look Brexit? Any kind of implication if you can quantify or qualitatively provide some perspective.

Vipul Khanna: Let me see if I remember all of them. Let me start with CAPEX. CAPEX is uniform, largely for funds or servicing growth. And it's spread across. There were some US investments for Mortgage, a lot of India investments in Bengaluru and Chennai to service growth for Mortgage as well as some of the healthcare accounts. And also, some expansion in the UK given some of the deals and extra orders we had. One or two are just extensions of our centers to add new capacity. So, in general, pretty much all is new center growth to service growth is where the CAPEX has gone.

Industry outlook: BFSI, obviously you know, is the biggest sector for the outsourcing world. It tends to consume and use it. It's a very sophisticated and mature buyer. And to that extent, they are at the leading edge of embracing newer trends like digital experience and stuff like that. We continue to grow that. We continue to modernize our offerings to be able to serve them. But to your question in terms of demand, the demand is shifting to newer offerings. Retail, Banking and Insurance both are asking for the next-generation customer experience. And to that extent, having those capabilities to play in the change spend, not just the run spend, is an opportunity for us as we look forward. We'll achieve that through people like Sundara and team that will join, but also by partnering with next-generation platforms and embedding those platforms into solutions. And in this regard, we've already signed up a couple of partners to embed their solutions in our offerings.

Healthcare: Again, break it down between Provider and Payer. Provider is going through significant change in the US. That's primarily a US market for us. Consolidation, value-based care, self-pay, these are the big mega trends out there. And hence, as we look at our offering of making eligibility at the core of our offering, modernizing it to make it more digital, extending self-pay making sure our product engages the consumers, that's kind of another trend that we're trying to play into. So, in terms of outlook for Healthcare Provider, I think it is going through significant change. And I generally believe it creates an opportunity for players like us to take their domain knowledge, stay very focused on extending that capability both in terms of value chain as well as modernizing the offering to capture a larger share of the wallet as far as the provider world is concerned. We're also seeing significant private equity interest in the Provider space. Companies which serve healthcare providers, they are attracting a lot of investment both in technology and operations, which kind of shows the validation of the opportunity in the healthcare provider space.

C&M: Clearly, it's colliding. You see big players are now transcending across communications, media, and increasingly behaving like tech companies. So, we also want to combine it and run it like a CMT vertical – comms, media, and tech – make sure that we are able to meet their traditional needs as well as the newer needs. Again, early days. I need time to kind of build that capability and come to you. But things like ad operations and content management are growth areas, even for traditional comms and media players as we look at that sector evolving.

I feel good about the sectors that we play in and what's happening there. Obviously, we are on a change and investment curve to make sure that our offerings capture the newer opportunities in those sectors.

Dinesh Jain: I think in the current quarter we have generated around $15 million of cash flow and free cash flow is around $8 odd million which we used for repaying the short-term borrowings. That's the number for the quarter.

Dipesh Mehta: Dinesh, I was more looking for 9 months.

Dinesh Jain: I think the range is around $30 odd million, the total cash flow generation. And most of that got utilized to repay the short-term borrowing or utilized for dividend payouts. From 9 months' point of view, most of the money is being used for repaying the borrowing and dividend payouts.

Vipul Khanna: Last question, Dipesh, you had was on Brexit. Let me offer a few comments on that. First, if you look at how it is playing out, clearly, more decisiveness in terms of the political action. What it means in terms of policies and specific actions is what's in store for the next 12 months as per the government's calendar. Impact on business is, if you think about it, the UK, despite the uncertainty of Brexit, had a strong economy over the last 3 years. With the new government talking about increasing spending, making it more regionally spread rather than just centered around London, I think the economy should grow stronger as they make better push on infrastructure investments or other skill-building areas in the developing parts of the UK. I think we play in some of them. That should benefit. And in general, as the economy kind of props up, our customers play largely, whether it's media or banking, on the retail side of it. That should have a good positive impact from a demand side.

Conversely, as the labor market continues to be the way it is, which is historically low unemployment rate, I am seeing more appetite, especially in the Utilities sector and increasingly from banking as well for embracing more offshore solutions. And it's also helping that as the world shifts a little bit more from voice to chat, it kind of opens up opportunities from onshore to offshore thing as well. It's kind of working in multiple ways – stronger economy, better regional growth, tighter labor market. So, demand side, I think, should play out well. And on the supplies side, it opens up more offshore demand, and then it's up to us to kind of execute well on our solutions and in sales to be able to capture a portion of that demand.

Dipesh Mehta: Just a couple of follow-ups. First is about the Payer side. I think you touched upon about Provider in healthcare. Payer, earlier, we have seen some challenges in the beginning of the year. How the Payer is playing out and your expectation about the next few quarters?

Second question about the seat fill sector, which I earlier asked about. It seems to be very high. Any specific reason is driving it or now considering operational excellence, you expect it to remain high going forward?

And the last question is about, is it possible to share 9 months' constant currency YOY growth?

Vipul Khanna: Let me give you a couple of Payer comments. From an industry sector standpoint, a couple of comments. One, a lot of consolidation continues to feed the Payer sector as well. Second, Medicare and Medicaid, which is government-sponsored healthcare plan, continue to be the growth drivers of the US healthcare market and plans which have strong presence continue to make strong progress as well as a number of other plans who were not in government sponsored healthcare plans or who were providers and want to be pay-widers continue to kind of come into the Medicare and Medicaid world to capture a share of the spend that's out there.

We have a reasonably strong portfolio, although I would say that we do need to kind of step back and think about what are the growth opportunities that we want to pursue. And I think part of my endeavour will be to come to you in the next couple of quarters to say in that changing landscape, given our profile, what is a sustainable growth pool for us. I need some more time to come back with the specifics, but I like the fact that the government plans are going and beyond traditional services, when we look at analytics or some of the middle office services, those seem to be early ideas of us trying to capture a share in those markets.

Dinesh Jain: Dipesh, on the seat fill factor, I think you're aware of in the last quarter, we talked about that for Mortgages, we are setting up centers in India and also in the US. Current quarter, I think most of those seats got filled as you can see that in the revenue upside which has taken place. I think the seat fill factor is a clear indication of the growth which is coming in Mortgages and the utilization of the empty seats which we are doing.

Vipul Khanna: And Dipesh, to your question on the 9 months year-on-year, it's 6.1% on constant currency basis.

Dipesh Mehta: And we are guiding around 7.5% to 8.5% for the full year?

Vipul Khanna: That's correct.

Dipesh Mehta: So, we expect a reasonably strong quarter because last year, Q4 was a reasonably strong quarter for us.

Vipul Khanna: Correct. The seasonality will help. Plus, looking at sort of the contracts under implementation, we are reasonably confident about the 7.5% to 8.5% range that we have at this point in time.

Moderator: We have the next question from line of Devanshu Bansal from Emkay Global. Please go ahead.

Devanshu Bansal: Vipul, congrats on a strong execution in the quarter. My question is we are already doing quite well on the collections and mortgage business segments. The only area not going for us is the CM part. The focus of new hires or those which are going to be hired is going to be on the CM side or to build new capabilities in the fast-growing segments or to develop new avenues of growth for you guys?

Vipul Khanna: Devanshu, you're right. Mortgage and Collections had a strong quarter. CM, while optically, year-on-year, it kind of looks flat, but partly, we have talked about in the past, that was some of the Sky reallocation of portfolio, which played out in the first 2 quarters. But if you isolate for that, it's growing reasonably and I feel good about the pipeline that we have. Clearly, bringing in new partners and bringing in new skills to be able to give more contemporary offerings with digital, CX and stuff, that is the focus here. That is one focus of bringing new skills, both in-house as well as partnerships. Tech is an aspirational area. We have started to kind of think about where do we start. What can allow us to get a fast track start in a newer sector like fast-growth tech? Fintechs is one area. Content is the other area that we're starting to poke around on. And clearly, our current strengths are both customer support and product support that we start with, and then we kind of extend into the service value chain. So, yes, both in terms of building capabilities and bringing sales capacity to target that is a focus, and I'm looking forward to closing some of those hires in this and next quarter.

Devanshu Bansal: Vipul, can we think of building capabilities through inorganic means as well? Do we remain open to those opportunities?

Vipul Khanna: Absolutely. Devanshu, the way I'm thinking is that we need a fairly systemic M&A program. We have laid out our vertical focus areas as well as service focus areas like digital and CX and Collections. Within that, our endeavour is to have a good visibility towards targets which could add capability to us either in terms of service line or go-to-market in geographies or sectors that we are not there. But early stage, nothing specific, but at a philosophy level, at a strategy level, we do want to look at it systematically as an accelerator for our capability build or GTM. Yes, definitely on the cards.

Devanshu Bansal: Vipul, not asking for a quantitative guidance as far as FY21 is concerned but the way we have guided for the 4th quarter which is expected to be on a good YOY run rate, FY21 seems to be much better than FY20. Your comments would be really helpful on this.

Vipul Khanna: Yes, Q4 looks reasonably strong at this point in time. As I mentioned, Mortgage has been a standout performer. Hopefully, next couple of quarters, the momentum on the origination side will continue. And after that, we'll see how the economic environment develops. So, there is that element to kind of consider. Also keep in mind, Q4 is historically strong for us in collections and healthcare, both. Some of that will taper off as we get to Q1 of next year. So, it'll be a little bit of a mixed bag. There should be positive tailwinds from our strong CM pipeline at this point in time. Again, it's a pipeline; we'll see how much we kind of net out in terms of wins out there. But yes, I acknowledge the sentiment that next year should be in line with or slightly better than what we have seen in FY20. But again, early days; we'll do more work. We just started the budgeting process for next year. And as we come to you 3 months later, we'll give you a sense of how next year looks like.

Moderator: We have the next question from the line of Sachin Kasera from Svan Investments. Please go ahead.

Sachin Kasera: Nice to see growth coming back after a few sluggish quarters and very nice to know that you're looking at a stronger ramp-up as we go ahead. Just a couple of things. One, when we see the segmental reporting that we have done, while in certain segments like for example, Mortgage, we have seen very strong growth but not seeing any major margin expansion. In fact, we see in most of the segments, there is strong growth, but margins are still not in place mainly because of the investment that we are doing. And as we go ahead, some of the segments will start to show margin expansion? How should we look at it?

Vipul Khanna: Sachin, I think your observation is right. Mortgage has been a little bit of a scramble to capture demand. Most of our clients have come back with strong demand, and it's about making sure we are able to hire the right skills in the right geographies. So, bulk of the margin has gone towards building those capabilities. You can't perfectly time the hiring relative to demand. We were kind of scrambling at that point in time. I'm hoping that we'll be able to balance it better in this quarter and as we go into next quarters. Also, inherently, origination is relatively low margin than servicing. So, at this point in time, that's what's growing. But as I mentioned earlier in my comments, we are very focused on making sure, in the background, we are building a strong service portfolio for the clients for whom we are doing origination. I think as we continue to build our servicing portfolio, that should auger well for our margins as well. But at this point in time, cost of growth and somewhat the lower margins of origination are what's playing out in our margin performance for Mortgage.

Sachin Kasera: Coming to the guidance for 7.5% to 8.5%, you mentioned that we have done some 5.5% to 6%, I think, for the first 9 months, right?

Vipul Khanna: 6.1%.

Sachin Kasera: While 7.5% itself would mean a very strong Q4, 8.5% would mean a very very strong quarter. So, are we looking at some significant deals in the Q4 and ramp-up?

Vipul Khanna: No, I think it's partly the seasonality. Historically, we see Collections kind of picks up; Healthcare picks up; Mortgage, we expect to continue the run rate of Q3. So, that will kind of play out there. CM is coming on a little bit of operational resilience. Hopefully, it will deliver more consistently on the revenue. When you add all that up, is where we look at Q4 coming in to kind of hit our overall numbers of 7.5% to 8.5%.

Sachin Kasera: And same is the case for margins because I think we have done 10.8% in the first 9 months from what I can see in the fact sheet.

Vipul Khanna: Correct.

Sachin Kasera: On the client concentration, the top 5 has increased from 39.5% to 42%. What has driven this? Any specific focus or some deal renewals or deal wins with existing clients?

Vipul Khanna: Mostly, it's been the growth in our mortgage portfolio. Our top client in Mortgage, that has shown significant growth. While our top client has remained static, the fact that Mortgage grew up and that too a chunk from the largest customer, that's showing up in the numbers as they have.

Moderator: We have the next question from the line of Madhu Babu from Centrum Broking. Please go ahead.

Madhu Babu: Sir, what is the net cash or net debt on the balance sheet? And what is the CAPEX plan for next year?

Dinesh Jain: CAPEX plan, the next year also, we're looking at same around $12 million to $15 million. I think $10 million to $12 million is normal, looking like the growth which we have, and I think a lot of the digital intervention probably will continue into that range of being $10 million to $12 million. Cash flows, I talked about. I think for 9 months, we did almost around $30 million to $35 million cash flow. After paying the dividend, the balance we used for a borrowing to repay. There is no long-term borrowing in the company. Most of that is just a working capital line, and which, as of today, is around Rs. 500 crores for us.

Madhu Babu: What is the net debt position?

Dinesh Jain: Net debt should be Rs. 500 crores. The gross debt is around Rs. 630 crores, and Rs.130 crores is the cash in the company.

Moderator: We have the next question from the line of Pranav Tendulkar from Rare Enterprises. Please go ahead.

Pranav Tendulkar: Sir, can you just highlight what are the margin levers remaining for the next year? That is one. And if I missed this, growth outlook for each of the verticals.

Vipul Khanna: From a margin standpoint, I think with our continued focus on digital and automation, one is, developing automation as a service line to offer it to clients on their retained operations, that's an opportunity. But also deploying the same more consistently across our portfolio, that's one focus area that we're looking at, especially where we have outcome-based contracts, so that there is an equitable distribution of margin from automation between us and our clients. That's one lever.

Second, we continue to look at offshoring very discretely to say that as we chase deals, especially in CM, we are able to have a greater share of those deals which have the offshore component because the margin profile is slightly better in those deals. That's our second potent lever from a margin expansion standpoint.

And third, in general, although it may not show, I guess, in the next few quarters because it's still in the build phase, as kind of scale builds up, both in operational leadership as well as SG&A, at some point, I'd expect the scale leverage to start to play out. But that's kind of more medium to long term rather than short term.

Pranav Tendulkar: And growth visibility or growth outlook for the quarter qualitatively – I'm not asking quantitatively – versus last 12 months?

Vipul Khanna: To that comment, Mortgage, as I said, will continue with its current trajectory. We expect current volume levels to hold up as in Q3. Collections, a seasonally strong quarter. Provider, we are, besides delivering on what we have, put in a lot of focus on our digital eligibility services as well as the newly launched digital collections product. Again, meaningful revenue will follow, may not be in the short term. But I think in the medium term, it kind of shows us well to capture the opportunity besides the traditional opportunity that we are doing in Provider. Payer, I need more time to come back with how we play in that market, as I've said earlier. And then finally, on CM, I think Q4 will be kind of run rate, but as we go into next year, if the pipeline continues well, we should see a stronger CM with a more contemporary offering playing that out.

Moderator: We have the next question from the line of Rahul Jain from Dolat Capital. Please go ahead.

Rahul Jain: Congratulations on a very strong quarter. You talked about the kind of efforts you are taking to bring down the attrition and bringing it par with the capabilities. What are the kind of headwinds we would see on our wage structure? And what are these things that you are implementing?

Vipul Khanna: Rahul, it's a holistic action. Attrition is a complex topic. From who we hire and how we engage them and what we pay and how we pay, all kind of goes into that factor. We are trying to be innovative so that it's not just a blunt retention or a blunt wage hike, but it's a more targeted intervention to show a skill-based or a tenure-based compensation structure is a philosophy that we are trying to implement as far as compensation is concerned. The good thing is that most of our contracts have indexation to the National Living Wage in the UK where a bulk of our CM business is. So, as that moves, our baseline kind of moves in tandem as far as that is concerned. Our focus to the point on wage is to be smart about how we spend the money as far as comp and benefits is concerned, but also focus a lot on the engagement part of it – the things around the wage; the facility quality, the engagement with employees, showing them the purpose, the engagement calendars. A lot of them should give benefits on retention without necessarily too much drag on the wage cost there. That's kind of how we're looking at it. Does that give you a sense?

Rahul Jain: You are saying it's more about an HR activity rather than putting more dollars into the thing.

Vipul Khanna: A mix of both, yes.

Rahul Jain: Do you think in our kind of a business model, it is the right tool? And also, what I probably understand is that in our lot of business, especially on the outcome-based model, we have a good participation for the executives. Is that a more relevant way to attract or retain talent? Or you think the other ways are more potent?

Vipul Khanna: Fair enough. Some of the contracts, especially sales contracts or collections contracts which are outcome-driven, we have the opportunity to show a higher variable weightage to our employees. The more they perform, whether selling or collecting, they are able to make more. And we see that behavior playing out differently. But when I look at service side of it or the chat side of it, where the contracts, it's harder to measure outcomes, then that's kind of pretty much the industry norm, we're not in isolation. That's where it gets to more either operational performance or tenure and some other factors to which you try to link the variable pay. So, as I said, there is no one perfect answer. It's a balance of engagement. It's a balance of how we pay them and it's a smart way. And then making sure they are bought into what they're trying to do for themselves as well as for the clients they serve. So, there's kind of a balance up across, also varies per the nature of the contract, sales collections versus service contracts.

Rahul Jain: Lastly, on the same thing. Do we even intend to put ESOP as one mechanism attached to it? Or we are not considering that at the moment?

Vipul Khanna: We do have an ESOP plan, mostly for our senior and middle level. To make it meaningful, we continue to plan it at that level only and not take it down to frontline leaders and our customer service officers.

Moderator: We have the next question from the line of Tanmay Mehta from SBICAP Securities. Please go ahead.

Tanmay Mehta: What will be the ETR for FY20? And do we share any number around the deal wins, like TCV or something?

Dinesh Jain: The ETR will be between 13% to 15%. I think that's what the range is going to be. Because, again, in the last quarter, most of the deferred tax adjustment a lot of time happens in the last quarter. But it will be between 13% to 15%.

Tanmay Mehta: It will be the same in next year as well, for FY21?

Dinesh Jain: Next year looks to be similar level because as we are seeing that a lot more growth coming on the offshoring side, too, and again, a new center which we set up and most of them are in SEZ, I think the range will remain the same. 1% probably here and there, but I don't think it's going to be materially moving from any other.

Vipul Khanna: Tanmay, your other question on deal wins, this quarter, we had ACVs of, give or take, $20 million. I don't remember the specific number. It's about $20 million, but that's ACV.

Tanmay Mehta: And if you could share for the 9 months as well?

Vipul Khanna: I don't have that handy. Can give it to you offline.

Moderator: We have the next question from the line of Sachin Kasera from Svan Investments. Please go ahead.

Sachin Kasera: Just two small data-keeping questions. One, what is the net debt figure as on December versus March?

Dinesh Jain: March 31st was Rs.390 crores. And as of December, we are at Rs.500 crores.

Sachin Kasera: So, the net debt has gone up primarily because of the dividend payout?

Dinesh Jain: Dividend payout, no. I think the CAPEX spends are much higher as well as I think if you really see the debtors levels have increased. On the number of days, it is lower, but I think at unbilled levels, it is slightly higher. We see that getting normalized in Q4. And Q3, seasonally, when the holiday season, so I think the collectability is slightly at a low level. But we don't see that increasing on a year-on-year basis. Probably it'll be at the low end of or probably around Rs 400 crores should be the net debt on 31st March '20.

Sachin Kasera: Then in that case, sir, how do we see FY21? Do we see net debt going down? Or it will remain at these levels?

Dinesh Jain: I think it should drop down. Till the time we don't do any materially M&A transaction, I think all the cash we generate. We expect at least between $20 million to $30 million of net cash surplus we should do in the coming year easily. I think that should drop the working capital lines.

Sachin Kasera: Sir, just one question on the dividend payout. Is there any change in the time like last 2 years, we have a dividend policy in place? That is broadly going to remain the same. Or that's also something that we're going to have a relook as we move ahead?

Dinesh Jain: We have not had any discussion, or we have not heard from the board level. So, the dividend policy what we have as of today remains intact. There's no change in that.

Moderator: Thank you very much, sir. Ladies and gentlemen, that was the last question. I'd now like to hand the conference over to Mr. Vipul Khanna – MD & CEO, Firstsource Solutions Limited, for closing comments. Sir, over to you.

Vipul Khanna: Thank you everyone for your time. Great questions. Enjoyed the conversation. We are hard at work. This quarter, a lot of work to do both in terms of servicing the business as well as growing it. We look forward to your increased participation and questions to us, and we'll come back in the next 90 days to report how Q4 was. Thank you very much.

Moderator: Ladies and gentlemen, on behalf of Firstsource Solutions Limited, that concludes this conference call. Thank you for joining with us, and you may now disconnect your lines.