"HCL Technologies Q1 FY21 Earnings Conference Call"

July 17, 2020

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Moderator: Ladies and gentlemen, good day and welcome to the HCL Technologies. Q1 FY'21 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 '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Sanjay Mendiratta – Head, Investor Relations, HCL Technologies Limited. Thank you and over to you, sir.

Sanjay Mendiratta: Thank you, Aman. Good morning and good evening everyone. A very warm welcome to the HCL Tech Q1 Fiscal '21 Earnings Call. Trust you all are safe and healthy.

We have with us Mr. C. Vijayakumar -- President and Chief Executive Officer, HCL Tech; Mr. Prateek Aggarwal -- Chief Financial Officer; Mr. Apparao -- Chief Human Resource Officer and the entire senior HCL business leadership to discuss the performance of the company during the quarter followed by the Q&A.

Before we open the call, I want to highlight that in the course of this call the company can or will provide forward-looking information. Certain statements that will be made are forward-looking which involves a number of risks, uncertainties assumptions and other factors that could cause actual results to differ materially from those in such forward-looking statements. Forward-looking statements made in this call should not be regarded as representation by the company or any other person that the objective and plans of the company will be achieved. All forward-looking statements made herein are based on information presently available to the management of the company and the company does not undertake to update any forward-looking statements that may be made in the course of this call. In this regard, please do review the Safe Harbor statements in the formal 'Investor Release' document and all the factors that can cause the difference. Thank you and over to you, CVK.

C. Vijayakumar: Thank you, Sanjay. Good evening and good morning to all of you. I hope all of you are safe. Thank you for joining us today. We started this fiscal year in the middle of this global health crisis. The business impact that we saw was slightly lower than what we anticipated in the beginning of the quarter as the recovery continued all through the quarter from the April lows. We closed the quarter with a dip of 7.2% in our revenues on a sequential basis in constant currency and an uptick of about 1% on a year-on-year basis in the constant currency.

Not all of the impact was due to COVID-19. Part of the decline was due to offshoring of large deals that we signed in the last year which saw offshoring and accordingly some revenue impact. Another aspect would be Q1 saw the full impact of some of the supply constraints compared to only seven days of impact in the March quarter.

Overall, team HCL executed exceptionally well on almost all the dimensions during the last quarter. Our EBIT performance was good; EBIT came in at 20.5% which is almost 3.5% more than the same quarter last year. Several reasons for this -- Of course, FOREX was a help; significant cost management initiatives; right-shoring, automation. Also, the changing mix of

our business, the increasing mix of Mode-2 and Mode-3 revenues. All of these contributed to the increase in the EBIT. Our net income increased 31.7% year-on-year; it is 2,925 crores in the last quarter which is a very smart increase over the previous year. We also saw very strong cash conversion.

However, the most important aspect of last quarter was we reimagined every aspect of our business with tremendous agility. It is just not work from home, it is about onboarding new talent, hiring from campuses, training freshers, the whole sales process doing the entire large deals on a virtual model, collaborating across multiple solution teams all virtually and making a big impact in front of our customers, winning their confidence and signing new deals is a tremendous validation of the sales power that we saw during the quarter.

COVID-19 impact on the demand side stabilized after some initial impact through ramp-downs, some volume reductions and some discounts that some customers asked for in some of the stressed sectors.

The supply factors have been well managed even though it continues to be a little volatile with the new lockdowns and unlock rules. Overall, we believe the worst is over from the revenue decline perspective and we are confident of a good growth trajectory from here on.

In terms of different segments, the IT and Business Services revenue declined 5.6% year-on-year in the constant currency. Some of the main reasons are some segments such as Manufacturing, Media, Retail, Energy, Travel and hospitality are the major segments which saw decline while Life Sciences and Healthcare, Financial Services, the Tech segment, Telecom and even CPG held up quite well during the quarter. Engineering and R&D Services saw a revenue decline of 5.1% year-on-year in constant currency. This is primarily due to the impact in Aero, Auto and Office Automation segments. Both Engineering and R&D Services saw some impact of offshoring of large deals that were transitioned last year. The bookings in ITBS and ER&D segments have been healthy. This gives us confidence on the growth for the rest of the year.

In the Products and Platforms, we had solid performance from the HCL Software business in the June quarter. This was the first full year of operations for HCL Software. We had a number of significant highlights.

In terms of customers and transactions, we completed around 17,000 sales transactions across 11,000 plus unique customers in more than 100 countries and we onboarded around 2,500 business partners and resellers.

In terms of innovation and new product releases we released a number of new products across our portfolio and also many product components and modules that were released. All of this demonstrates our commitment to innovate, invest in R&D and help customers to be successful and more importantly derive value from our products.

In terms of new growth, we added over 250 plus new customer footprints during the first year including 100 plus in the June quarter alone led by BigFix and AppScan and including new footprint wins across every product in the portfolio with new customers across every geography and industry. This is a great validation of the progress that we are making on the customer-centric innovation and winning in the market.

In terms of the transition, we remain largely on track with our business case and expected transition timelines. As we have noted previously, we did experience some ramp up in the first couple of months of the transition last year but has seen solid and consistent performance over the last three quarters which we do expect to continue and remains largely in line with our expectations.

In terms of COVID impact on the P&P segment, the impact has been very-very limited. We attribute this to three factors – First, we have worked very well with our customers demonstrating our relationship beyond the contract philosophy which has been very well received and it has been a refreshing change for customers who have been dealing with the software product companies.

Second and very important is our software business is very diversified across many industries and geographies. And the deal sizes are relatively small and the products are mission-critical with a lot of long standing deployments. So they are intrinsically sticky.

Third, some of the challenges today have created new demand and use cases for some of our products and we have seen new license growth in several areas, like eCommerce, digital marketing, digital experience and security. As an example, almost all retailers have increased eCommerce investment significantly. Similarly, work from home has created new security requirements.

Overall, we remain cautiously optimistic about this business segment and it will continue to perform stably in line with our expectations for all the reasons that I have mentioned.

In terms of bookings during the last quarter, the deal closures have been decent. We have had eleven net new transformational deal wins led by key industry verticals including Telecom, Financial Services, Manufacturing, Life Sciences and Healthcare. Our booking TCV is greater than the same TCV that we have had in the same quarter last year. When we talk about bookings, we always talk about net new booking and it does not include renewals. Our renewals have also been robust in the last quarter. A great amount of details on this wins are in our 'Investor Release' and you can go through them.

We also won a large consolidation opportunity in Europe that we have been pursuing for over a year. We have been announced as one of the strategic partners to benefit from the overall consolidation opportunity and we see the revenues will ramp up here gradually over the next few quarters.

I would also want to share a few more "Key Business Updates." We do an annual customer satisfaction survey every year which got completed a few months back and the results are available. We achieved one of the highest client satisfactions and in comparison to the industry we are almost at the top end of the client satisfaction across the industry. This is validating the trust and confidence our clients have on us and this is going to be all the more important in difficult times like this. We also were ahead of everybody else.

We organized Accelerate which is a virtual analyst and advisor day which saw about 400 analysts and advisors from 67-plus firms attend in the middle of May. This is analysts and advisors who are advising our clients. So this was hugely successful and it did create some good traction as a follow on impact.

During the quarter, as you might have seen, we announced our intend to acquire Cisco's self-optimizing network which is called SAN. This acquisition will take some time because it requires to go through the regulatory clearances. This along with some of the products that we have in telecom space under our ER&D segment is gradually helping us create a niche portfolio of telecom products which are particularly relevant in the 5G world.

We also announced an agreement with Temenos. This is an exclusive agreement to market Temenos mobility platform for non-financial services customers. As a part of this, HCL gets a license to develop market and support the mobility development platform. It also gives us the ability to integrate with other HCL software products.

During the quarter, we also expanded our preferred professional services partnership with Broadcom to include Symantec Enterprise Division as well. This helps us strengthen our security consulting and services capabilities significantly.

Last quarter, we also inaugurated our center in Colombo in Sri Lanka. As a part of our expanding footprint of global delivery locations, we plan to ramp up to 1500 people in our Colombo center during this fiscal year.

The quarter also saw a significant amount of analyst recognition and awards especially in a lot of our newer services in Mode-2 as well as several recognitions in the Mode-1 space. A special call out will be Cyber Security, IoT, Digital Masters are some call outs where we were rated very-very high.

Looking ahead, I see a very good growth in the pipeline. In the last quarter to this quarter, our pipeline increased 40% and a lot of this is driven by some of the key trends that I will talk about later. The pipeline richness is reflecting in Life Sciences, Financial Services, the Tech segment and Energy and Auto segments. As I said earlier, there are two broad themes which are playing out. I am sure this is not a surprise in an expected way. One is the momentum in cost transformation and vendor consolidation deals. That is one big space. This is a little more prevalent in sectors which are under a lot of stress, especially energy and auto are the two segments where we see this.

We are also seeing a lot of acceleration in digital initiatives. We see a great market interest for strong digital foundation which is our Infrastructure Services and Digital Transformation Services driven by Hybrid Cloud, DevOps, Scaled Agile operating models.

Digital workplace is again a strong momentum area which really will become an important component of the digital transformation journey for our clients. Customers are investing in cyber security frameworks in a fluid and evolving kind of world. We are seeing good deal creation activity in existing clients which is really where we are putting tremendous amount of focus at this point in time.

Overall, as I look forward and also kind of looking back to the three or four key things that has tremendously helped us, one is the resilience in our operating model; two, the portfolio mix that we have in terms of portfolio of services as well as the product mix that we have. Our employees have been the cornerstone in this pandemic response. We have come together extraordinarily well to respond and not only the immediate response but follow on rebadging every aspect of our organization has been done amazingly well. And of course the relationship beyond the contract philosophy in dealing with our customers has won several appreciations and a lot of goodwill for us in this time.

With all this, the future outlook looks quite positive which is enabling us to give a guidance of an average quarterly growth ranging between 1.5% and 2.5% quarter-on-quarter on constant currency basis. This is really coming from the recent deal closures and healthy pipeline in a fairly mature space. In terms of EBIT, we expect to deliver between 19.5% and 20.5% for FY'21 which is actually 100 basis points higher than our FY'20 guidance.

With this commentary I will hand it over to Prateek to provide the next level of details on financials. Over to you, Prateek.

Prateek Aggarwal: Thank you, Vijay. Good evening, everybody in India and good morning and good afternoon to the ones outside. I will get into some more level of details on the financial numbers. Revenue as you know came in at $2,356 million or $2.3 billion; it was down quarter-on-quarter by 7.2% in constant currency, but the year-on-year number was a (+1%). The organic growth was about (-5.3%).

The factors as CVK already pointed out, apart from COVID, there was some offshoring in some of the large deals which were closed earlier and some other one-timers were there.

So moving on to the profitability metrics, the number I specifically want to focus on is EBITDA. EBITDA came in at $603 million, that is 25.6% of the revenue and that was up 20 basis points on a quarter-on-quarter basis. And EBIT came in at $484 million, 20.5% and it exceeded last three quarters average. I am not comparing specifically with the June quarter of last year and taking the next three quarters purposely and 20.5% exceeded that average. And the (PAT) profit after tax came in at 386 million which is 16.4% of revenue, and that was down 56 basis points quarter-on-quarter.

To walk you through the EBIT movement during the quarter, the total movement on a quarter-on-quarter basis was (-34) basis points. This was helped by the FOREX movements giving us about 76 basis points during the quarter. So the QoQ reduction pre-FX was 110 basis points negative. There were four parts to this. And the first part is basically 67 basis points negative from the fixed and increasing depreciation and amortization costs which is as you know is based on the investments that we have made earlier.

The second part then was negative 12 basis points from the R&D expenditure that we basically put in, in all our products in the E&T segment largely and also in ERS and a little bit in ITBS as well which we did want to cut back on despite all the environment that we were going through.

The third part was a positive swing of about 40 basis points which we could reduce in our SG&A. The reduction is more due to costs like travel costs, etc., and some discretionary spend like marketing events and certain other administrative costs. While on the sales and marketing, we actually continue to increase our headcount even in this quarter especially in the HCL Software part in the P&P segment.

That then leaves us with the last part which is balancing (-70) basis points which is what we lost in the gross margin line pre-FX benefit basically the impact of lower volumes. The revenue reduction by 7.2% in constant currency could have made a significant adverse impact on gross margin; however, most of it was largely offset by operational efficiency leaving a small adverse impact of 70 basis points. You would have noticed; our headcount numbers were by and large flat about 100 headcount down which we have been very empathetic with our employees same as the empathy we have shown towards our customer. So that kind of sums up the EBIT walk.

Moving on to some more important numbers, the next segment is about cash flow. So the operating cash flow came in at 819 million for the quarter and free cash flow of 757 million respectively. That means it is 212% of net income. Operating cash flow and free cash flow was 196% of net income. FCF actually came in more than double the average of the last financial year. You may remember the last FY'20 FCF number was 1,480 million number and in one quarter we have delivered more than double of the quarterly run rate. These numbers, OCF and FCF are obviously very healthy and there have been some questions where is that cash flow coming from. And the simple answer proactively I wanted to put out is we have been shouting from the rooftops about cash EPS. And as I have said before, it is a number from the cash flow statement. As you will see in the cash flow that has been provided, there is about $120 million in this quarter of depreciation and amortization expense which hits the P&L but is a non-cash expense and therefore that is cash that is in HCL's hands. Similarly, as I explained in quite some detail, there is a non-cash element of the tax cost and that is about $20 million for this quarter as well. So, both these put together is almost $140 million which is hitting the P&L, which is hitting the net income but the cash in HCL's hands. This is one part of it.

The second part of course is $175 million came in from collections. And that is not a surprise. There is a very simple logic to it. It is there for every peer and every participant in the market when revenues come down a little bit like they have, there is a collection time lag and we have

a total DSO including unbilled of 86-days. When the revenue came down by about 175 million, 86-days worth of that is the cash that came in without revenue in this quarter. That is the 175 million. So within these, this explains the way that more than $315 million cash really came in from and the others are more business as usual net income kind of numbers.

So having spent the time on explaining the cash flows, the gross cash therefore at the end of the quarter was $1.95 billion which is about 80 million lower than the balance that we had in March quarter. Net cash interestingly is almost exactly the same as last quarter; it is at 1.33 billion compared to 1.36 billion last quarter. And mind you, this is after paying off the second and final tranche of the acquisition related payout of $812.5 million during the quarter.

Annualized earnings per share for the quarter comes up at 43.1 which is 32% increase on a year-on-year basis. On a quarter-on-quarter basis it is down by 7.3%. And annualized cash EPS is at Rs.58.6 for the quarter which is up by 42% year-on-year though decrease of 3.7% quarter-on-quarter.

Given all these, DSO is maintained at the same level of last quarter…I am talking about including unbilled, 86-days same as last quarter and the three days reduction over the same quarter last year. And excluding unbilled which is just the billed DSO, we were at 65-days, one day less than the 66-days reported last quarter.

The dividend for the quarter declared by the board is Rs.2 per share.

Moving on to other statistics, HCL Software completed first year of course and the incremental revenue in T&T is about 141 million reported and in constant currency that is about 144 million. And the last three quarters run rate of incremental T&T revenue is at about 600 million in constant currency. So, it is tracking well towards the 625 million guidance that we had given for the first 12-months albeit with a lag of one quarter, the teething quarter of September that we went through building up the business.

And equally important with the revenue is the EBITDA is running ahead of the business case and therefore the comments from CVK even earlier that this huge acquisition that we completed last year on 30th June is doing very well for us and better than the business case.

Look at the other line items, other income is a little higher this quarter. We benefited from about 18.4 million of profit from the sale of some land parcel in India. ETR for this year is about 24%. There was a question about the revenue guidance of 1.5% to 2.5% CQGR. What does it mean in terms of FY'21 growth over FY'20. That means a range of (-2.3%) on the lower side to (-0.8%) on the upper side on a year-on-year basis. The bottom line guidance (EBIT Margin) remain that our traditional comfort band of 20% basically plus/minus 0.5%.

And the last statistic to look at it is the return on equity which continues to be at a healthy 23.7% on last 12-months basis.

Moderator: Thank you very much. Ladies and gentlemen we will now begin the question-and-answer session. The first question is from the line of Mukul Garg from Haitong Securities. Please go ahead.

Mukul Garg: I have two quick ones; one for CVK and one for Prateek. CVK, if we look at the last few days, the commentary from your peers, we have actually heard a lot about cloud. Given we are expertise in the infra space, do you see this impact from COVID-19 as an opportunity to super-charge your infra business or will we see a more gradual benefit of growth, so you have given the crack to the existing legacy business in the infra space? And Prateek, if you could help us with some color on the margin on the Mode-1, 2, 3 qualitatively, were the direction of kind of the margin movement was same in terms of levers or were their different strategies in each three modes?

C. Vijayakumar: Thank you, Mukul. That was a very good question. We absolutely believe the cloud adoption is a great tailwind for our infrastructure business for a number of reasons. First, whenever customers are looking at cloud adoption, be it public cloud or hybrid cloud, I think you need to look at that opportunity a little more holistically and look at that as a digital foundation of a resilient digital enterprise which includes security, network, automation and very automation-led operations model which would mean that there are certain tools and capabilities that are required to deliver that. So we think this is a good services opportunity for us, not just one-time system integration services, but also ongoing operational services especially so in a multi-cloud world where customers are looking at multiple hyperscalers and on-prem or hybrid cloud kind of solutions. The other aspect is when you are into a client to kind of enable and strengthen and modernize their digital foundation, then naturally you are a very serious player to be considered for the application modernization. If you look at the reason why we integrated infrastructure and application and kind of call it as IT and business services, we see kind of triggered from hybrid cloud and cloud adoption, we see a good opportunity for us to kind of enhance the whole footprint in many of our accounts to really deliver a holistic both digital foundation and business application services. So I see it as a very good positive headwind. I think it has taken some time to get the full picture of what this hybrid cloud adoption will be in terms of overall impact to the business. I personally feel very-very confident that it is going to create a good impetus to our infrastructure business.

Prateek Aggarwal: Mukul, on a mode wise numbers, especially looking at the EBIT margins where the question was, the 34 bps reduction in margins at a company level primarily came from Mode-2 and Mode-3. So if you look at the numbers, you will see that on a quarter-on-quarter basis both Mode-2 and Mode-3 EBIT percentage is reduced by 0.7% or 70 basis points whereas the Mode-1 reduction was 20 basis points. Now, while there were several factors which were kind of similar across, there are a couple of things that I should point out. On the Mode-3, like I have mentioned earlier in several conversations, we did have a higher amortization part hitting us this quarter and that number is almost at a peak now. It has been going up through the last four quarters as the bulk of business shifts more and more from the IBM paper to HCL paper in terms of invoicing the end customers. The second thing then that also reduced margins a little bit in the Mode-3 was the sales and marketing investments that we continue to do which also I had spoken

about so many times. So, that is the reason why the Mode-3 reduction was a little higher than the complete total. And on the Mode-2, we have discussed that even in the last call at the end of March that there were certain one-timers that got recognized in the March quarter which basically came from previous quarters. And that was one of the reasons that the Mode-2 margins was a little higher last quarter. So, that is what I would attribute it to and leave it there. No specific color on Mode-1.

Moderator: Thank you. The next question is from the line of Pankaj Kapoor from CLSA. Please go ahead.

Pankaj Kapoor: CVK, my first question is on the products and platforms business where there seems to be a sequential decline in the HCL Software revenues. This is despite that there would have been a quarter-on-quarter shift of the licenses from IBM to HCL. So was just wondering that was it a factor of a slower renewal rate or was there also a factor of lower pricing?

Darren Oberst: First, it was not a function of lower pricing and generally speaking it was not a function of slower renewals or we are seeing significant delays in renewals. In fact, we saw a pretty consistent pattern in renewals over the last couple of quarters. It was largely due to first some minor kind of onetime FX over the last couple of quarters associated with that transition. So I think that is one contributing factor. The second contributing factor is in the non-acquired portfolio. We also had a couple of one-time FX that were a little more positive in JFM quarter and a little more negative in the AMJ quarter. We put those two together. That is what contributed to the very minor sequential decline quarter-on-quarter.

C. Vijayakumar: Just to kind of summarize it, on the products and platforms business, to kind of decipher the trends is a little early. We finished four quarters and other four quarters to really get a good sense of how the quarterly kind of variations of play out. And eventually it will always be a year-on-year comparison. That will really make sense in this business.

Pankaj Kapoor: My second question is on the vendor consolidation opportunities that you spoke about that you are following up as well as some of the ones that you have already won. Just wanted to understand what kind of a commercial construct are you approaching them with, are they requiring some kind of a reasonable pricing discount, any kind of upfront payments, etc., is that the approach which you are taking or this has got more to do with the pressures that the vendors themselves might be facing?

C. Vijayakumar: There are many dimensions to this. Of course, an easy low hanging fruit is what we call is a tail vendor consolidation. A lot of big companies, while they have a few large partners, they have a long list of tail vendors and there is an emphasis to consolidate that which is mostly coming at our rate cards and our normal pricing. Then there are accounts where we already have a few large vendors and we are not really there in any meaningful way. And given that there is a lot of emphasis on some of the digital technologies and some of the newer aspects, including digital foundation, clients are looking for evaluating the entire landscape and potentially bring in one or two new service providers as challengers. So those opportunities are getting driven purely by capability differentiation and some amount of fatigue with some of the existing providers, so

that's what is driving. I mean, pricing is important, but I don't think that is getting so much driven by price.

And in the vendor consolidation, where we are, there could be like some large incumbents who the clients are not happy with and they want to exit, sometimes there is a cost of exit, and customers expect us to kind of contribute to that cost to make it a little easier for them. However, that third scenario that they talked about is really a small fraction of such opportunities, the bigger opportunities are in the first and second segment that I talked about.

Moderator: Thank you. The next question is from the line of Kawaljeet Saluja from Kotak. Please go ahead.

Kawaljeet Saluja: Congratulations on a pretty impressive margin defense and April generation as well. Maybe if it's okay, I will ask a couple of questions, though, a little bit short. The first question is for CVK. CVK, you mentioned that your participation in setting up the digital foundation will enable you to participate in application management services and, of course, application stack in general. Now, actually if you basically go back into the past, maybe five, six years back, HCL Tech did have a strength on on-prem infrastructure management, though the similar dynamic of application management contracts did not play out to the desired extent. So just curious what is different this time around?

C. Vijaykumar: Yes. It is a very, very insightful question, Kawal. And I think this was the trigger for us to really integrate infrastructure and application business. In the on-prem and the traditional infrastructure, even the client organizations managed infrastructure as a group and applications as a group. And there was very little linkages, except for some things like monitoring service management, application operations. But in a hybrid cloud world and significant adoption of public cloud, I think the whole DevSecOps as a concept is becoming very prevalent. So here, the infrastructure and application teams are integrated into one cohort. And then a lot of application capabilities are available as innovation of features on the public cloud or hyper scalars, whether it is analytics or Big Data, data warehousing, many of these features are a part of the overall cloud landscape. So instead of they becoming application capabilities, they really become a platform capability. So that is also driving this to be looked at more like the plumbing or the foundation. And then only composing some capabilities are really the business application capability. So there, I mean, this can happen either ways, it can even happen that an application vendor could consolidate the infrastructure work or infrastructure vendor has a potential to consolidate application work. But given the strong capability that we have in infra and understanding of cloud migrations, and very strong experience in doing that, I think puts us in a very positive position there.

Kawaljeet Saluja: That is insightful, VCK. Just to follow-on on that, in the last two years, I believe, we have one of your contracts which essentially involves setting up a digital foundation. How do you see this dynamic of application in a contract and integrated deals coming through? And if you can just throw light on one or two of those, that would be very, very helpful.

C. Vijaykumar: Yes. In fact, one of the large deals that we won this time in the last quarter, in fact, it is the largest deal of the quarter, where we had one of the traditional providers providing infrastructure services, both on the workplace and on the data center site; and another service provider providing all of the application services for almost 15 plus years. But on the strength of our whole digital foundation and DevSecOps proposition, we have been able to consolidate both, the traditional infrastructure work, which includes workplace and the data center, and all of the application management work. So this is a classic example. This is in a large client, but there are several midsize clients, like last year we announced two deals in a couple of utilities in Europe, where this integrated approach has helped us gain the entire business stack. And even the Stanley Black & Decker deal that we had announced in the last JFM quarter, it's again the similar proposition which really strongly resonated with our customers.

Moderator: Thank you. The next question is from the line of Prashant Kothari from Pictet. Please go ahead.

Prashant Kothari: My question is on the overall performance. I mean, because HCL has a share of revenues from the products business, it's also very strong on the infrastructure side, somehow our expectation was that on a sequential basis the performance should be much stronger than the peers, which has not turned out to be the case. Could you explain why order dynamic has not really worked as per what we would have expected?

C. Vijaykumar: I think I would attribute it to two things. One is, as we said, some part of the impact is not really due to COVID, it is because offshoring of a couple of large deals that we had signed last year, on which offshoring was more or less done, and the second year is when the reduction in revenue happens. And since they were large deals, obviously, there is an impact there. And I mean, we were also very ahead of the curve in providing the whole work from home and we had very, very little impact in the March quarter. However, whatever remaining pieces which could not get delivered from home, they continued for a much larger number of days in the AMJ quarter. So this was one reason. And second, of course, I think it's to do with the whole portfolio mix. For example, our engineering services, almost half of the portfolio, a little less than half, comes from asset heavy industries which aero, auto, office automation and some of the other industrial manufacturing kind of companies, which saw closure of factories, some kind of scaled down in discretionary spend. So that's what created the impact there. And in some of our traditional infrastructure work, we do what we call as device based billing. So their volumes came down, like when a big automotive manufacturer shuts down 20 of the 24 plants that they had globally, then obviously they have said, a lot of employees have gone on furloughs. So which means wherever we were doing billing by the number of users, then obviously that comes down. So these were the reasons, I think it's some unique things about our own Q4 and now Q1, and a little bit to do with the portfolio mix. That's what I would attribute it to.

Prateek Aggarwal: CVK, I will just add on to that answer. Prashant, I think your basic hypothesis, saying that products and in-shop business should be more sort of contracted kind of revenue, right, your basic hypothesis is correct. The only thing is, we are not that type of a company who will sort of show the customer the contract when the customer is going through a really bad time in their own business, right. So in this pandemic, you know the impact that several large customers have

had. And if I was to sort of just stick to what the contracted the billing was, I could have probably shown a much better revenue curve. But we are a company who takes relationship beyond the contract. And we said this even in the last call, we are being empathetic to customers, we are being empathetic towards our employees. And therefore, that means that when a customer who is hurting badly, reaches out to us for some help in reducing the contracted billing, we have worked very collaboratively with those customers to see how we can help them. And of course, it works both ways, they have helped us in turn to help us reduce our costs while we try to get them the reduced billing. So I just want to summarize that your basic hypothesis is right, but we have to be empathetic at this kind of a crises time. And that is why potentially the difference in what he thought would happen, and what actually happened.

Moderator: Thank you. The next question is from the line of Sandeep Agarwal from Edelweiss. Please go ahead.

Sandeep Agarwal: First of all, congrats on a very good execution in a tough quarter. So CVK, I have just a small strategic question. So, how do you conceive the whole tax situation, IT industry situation after this pandemic? Obviously, no one predicted this pandemic and cannot, but pre-pandemic whatever your thoughts were, and post-pandemic whatever your thought is on the industry, have they changed in a material way structurally? That is number one.

And if I want to break down my question further, I want to basically know what kind of acceleration in tech spend you expect that will happen because of this substantial jump in online activity which has triggered due to pandemic? And I understand that some of it will be recede, but not all of them will recede because there is a behavioral change. And if that happens, then obviously, the digital transformation, cloud adoption and the transformation of the core could be a very substantial opportunity. So am I reading the right or you think there is some catch there? First of all. Secondly, I am not asking this question for FY '21, I am asking for a long-term, like medium to long-term perspective. Thank you.

C. Vijaykumar: Sandeep, your hypothesis is directionally right. I think I also strongly believe that the tech spend in an enterprise will meaningfully increase because of the experience that all the companies have gone through. And the most important thing is the whole tech, especially the infrastructure and the resiliency of the enterprise is really foundational, is founded on the premise of a very strong technology infrastructure. So a lot of CEOs have recognized, I mean, they already knew technology is very, very important for really transforming their businesses. But I think there is a much more sharper realization and appreciation, a very strong technology landscape is essential for everyone to even survive the business. So to that extent, when a CIO goes to seek a budget approval on any of the initiatives, normal questions would be, what is the return on this investment? But now it's all about, this is really an essential investment for the business to kind of survive and thrive. So the conversation changes, the priority for some of these things dramatically changes in the minds of key decision makers. So I would say, these are directional inputs and it will meaningfully change in the times to come. How much and how quickly is something which is a little difficult to predict. But tech industry, in my view, will benefit from the increased spend and the awareness of the criticality of the overall tech landscape.

Moderator: Thank you. The next question is from the line of Abhishek Shindadkar from Elara Capital. Please go ahead.

Abhishek Shindadkar: Just wanted to get your thoughts on the ER&D space. Just looking at the data in the previous cycle, the ER&D vertical had seen a couple of quarters of softness. Are you seeing anything different this time in terms of the client spends? Your thought would be helpful.

C. Vijaykumar: GH, I am not sure if you joined the call, if you could take this question around ER&D spend.

GH Rao: Yes, I am here very much CVK, I will take the call. See, we have two classes of industries, as mentioned by CVK, one is asset heavy and second is asset light. Asset heavy is mostly aerospace, automotive, industrial manufacturing and office automation. So specific to COVID, these industries got impacted a little bit higher. The other part of our business in ER&D is on asset-light industries be it ASVs, online consumer electronics, semiconductor, telecom. So those industries we don't see any impact. Apart from the impact on the demand side, in ER&D we do have another impact which is on the supply side. Because some other work needs to be executed on the labs, so in the first probably six to eight weeks of our lockdown we had an additional impact because of the supply issues where we were unable to fully work in the laboratories. So, that is the reason why you see the impact on ER&D a little bit higher than rest of the business at HCL.

Coming to you or other question, is there any generic softness that you see. I don't think there is any generic softness in ER&D, but for the impact of this COVID we do see in the asset light industries, the demand to be healthy as earlier. We do believe we have bottomed out in terms of COVID impact and we are expected to see some growth in subsequent quarters.

Moderator: Thank you. The next question is from the line of Ankur Rudra from JPMorgan. Please go ahead.

Ankur Rudra: Thank for the guidance and great execution on cash generation this quarter. Could you maybe elaborate on the progression of deal signings in the quarter? Did you see a significant improvement towards the end of the quarter versus statements from previous periods? And also, thanks for the guidance of the overall business, but are there dramatic differences in terms of how you see various parts of the business react over the rest of this year?

C. Vijaykumar: Ankur, see, definitely the deal closures, almost 30% of the deals or maybe 40% of the deals closed in the last 15 days of the quarter, that is the real situation. However, I don't think it has anything to do with improving situation on the pandemic, because certain things took a little more time and it kind of culminated towards the end of the quarter. But on the same light, we are seeing more traction in the early part of this quarter compared to what we saw in the April month in the last quarter. That's what I would say in terms of deal closures.

In terms of giving a view on how different segments would perform? Obviously, our guidance is on an overall perspective. And to make it easy, the P&P business should be really looked at it from a year-on-year perspective. And we hope to see some positive growth there. And I think

the recovery in engineering, I do believe we will see some good recovery in Q2 and it will possibly continue in Q3 and Q4. And in the IT and businesses services, I see the auto, aero and maybe some energy segments taking a little longer to recover. But financial services, tech, telecom, even some of the retail segments, I see it recovering a little quicker than the other segments. I won't be able to give any more finer color on this, Ankur.

Ankur Rudra: This is very helpful. Also, could you elaborate any sense of how does the decline this time break out into the supply and back? Because I think, I remember you mentioned, it was a little higher than the previous quarter versus the demand impact on COVID and the pre-planned offshore shift that you mentioned happening in some of the other projects. And somewhat related to that, is there any more such pre-planned offshore shifts in other large projects which may have already been baked into the guidance for the rest of the year?

C. Vijaykumar: Yes, of course, any reduction due to offshoring is baked into the guidance, because we have full visibility of that, because the deals are signed. However, the two large ones are generally which are the biggest components have already played out. And whatever may be there, may be somewhat smaller in nature. Sorry, I didn't remember your first question, Ankur.

Prateek Aggarwal: Supply versus demand.

C. Vijaykumar: Yes. So the supply impact, broadly you could consider about one-third of it was due to supply and the rest was due to demand of the COVID impact part of the overall decline.

Moderator: Thank you. The next question is from the line of Abhishek Bhandari from Macquarie. Please go ahead.

Abhishek Bhandari: CVK, I have two questions. First, we are approaching the US elections, so do you think in any ways the composition of the deal signing are likely to change from what we have witnessed until mid-July? And the second question is, in the press conference you mentioned that you won't be giving any salary hikes to the employees for the entire FY '21. But could it change if some of the peers decide to get some kind of increments towards the second half of this year? Thanks.

C. Vijaykumar: Yes. I mean, US elections generally had some impact to decision making that we have seen, so there could be some impact. But we have kind of taken some kind of models to plan it, I mean, to the best possible extent. So nothing more than that, that I can share. And if the overall wage hike scenario changes significantly, maybe we will consider it. But at this point, I don't see that happening during this fiscal year.

Moderator: Thank you. Next question is from the line of Sumit Jain from Goldman Sachs. Please go ahead.

Sumit Jain: Actually I had two questions, one for CVK and one for Prateek. So CVK, I think clearly you mentioned that there was a lot of tailwinds for cloud migration, digitalization for the hyper scale. And I am assuming that part of the business contributed in your Mode-2 revenues. So wanted to understand the kind of decline we saw there. Can you let us know what were the headwinds and the tailwinds?

C. Vijaykumar: Yes. Of course, Mode-2 has a lot of transformation projects. Some of it is discretionary spend. So, cloud and security, obviously, saw some increase, and there are others where there could be some reductions. That's what could have played out from a quarter-on-quarter perspective. But generally, this positive momentum should be seen in this segment due to the reasons that I highlighted, and you reiterated.

Sumit Jain: Go it. And secondly, for Prateek, I think you also mentioned that you have signed multiple partnerships with Symantec, Temenos, Broadcom. So one to understand, are there any upfront commitments we have made to these partners, somewhat similar to what we did with IBM in 2016?

Prateek Aggarwal: So, Symantec, or rather Broadcom deal with Symantec portfolio, and Temenos, are both capital organic kind of deals. So there is some license revenue we will be giving to Temenos, but it is over the period. It is a seven-year exclusivity period that we have signed up, and there would be some license fee payable during those seven years. Likewise, those payments are going to be factored in into the P&L over those seven years on an amortizing basis. So, yes, it is in that sense quite different from the IP partnerships that we had with IBM.

Sumit Jain: Right. So anything around IRR what we have in mind around these upfront commitments?

Prateek Aggarwal: So IRRs are the same, 10% to 15% post tax return that we normally work towards. There is no difference from that perspective.

Moderator: Thank you. The next question is from the line of Sandeep Shah from CGS CIMB India. Please go ahead.

Sandeep Shah: CVK, just wanted to understand some of your peers who are not that positive on infrastructure management have been sounding more optimistic about IMS. And you being one of the leader, what is your experience? Are you believing that pandemic is leading to more demand in terms of volumes?

C. Vijaykumar: I would say, it's not so much as volumes, I think it's really a faster adoption of newer technologies, whether it is in digital workplace or cloud adoption. And maybe what was expected to happen over a period of time has become a much more faster roadmap to adopt to these technologies. That's one. In some areas, I think it does increase volumes because the number of devices people use would increase, and some of the complexities around network and security would increase, creating some kind of tailwind from a volume perspective. But I think it's more of replacing traditional with new, I think is how I would put it.

Sandeep Shah: Okay. Secondly, in terms of the FCF, where I think good execution, but with four quarters already now integrated for the P&P business acquired, there seems to be a higher visibility for a robust and healthy FCF generation going forward. So is there any prospects for higher cash distribution of the FC? Like your peers who are giving anywhere between 85% to 100% of their FCF as a whole? And Prateek, just a clarification to the previous question where I lost out in

between, I think there is an $80 million worth of increase in the license IPR. So this is towards what, as you have said there is no inorganic deals which we have consummated.

Prateek Aggarwal: So, let me take your second question first, that is the easier one, that is towards the Temenos deal that I talked about. The total license that is paid over the seven-year period, so that is what we have sort of taken a fair value and included as an IP partnership, which is what it is. And the payment of that will be happening over the seven years as we have already said. Coming to your first question on basically payouts, so that question is a little too early in the year, practically speaking, because we are a company who typically gives interim dividend every quarter at typically Rs. 2 per share. That is what we have done this quarter and potentially for the next couple of quarters we will do that. The real question of whether we want to increase the payout comes up really in the fourth quarter and that is kind of three quarters away. Having said all of that, I think, the thought is that over the last four plus years, we have a proven playbook where we have invested significantly. And the good news for shareholders and good news for all stakeholders is that we have been able to deliver to the business case or exceeding, and therefore, this is probably also the time there might be opportunity. So that could be another area where those free cash flows might go. It's not something happening tomorrow, so don't get me wrong. But you know that that has the potential outflow as well. And that's where I will leave it. I think the comment you made about the software products business being cash accretive is absolutely bang on, and that is one of the reasons why in the last three, four quarters we have seen the excellent free cash flows coming in.

Moderator: Thank you. The next question is from the line of Ashwin Mehta from Ambit Capital. Please go ahead.

Ashwin Mehta: I had one question for CVK. CVK, given that you are seeing accelerated adoption of cloud, how does the interplay happen with our traditional data center services business? And historically, we had indicated some proportions of that business, as of now, given that most of your deals would have renewed out, what proportion of your business might be the traditional data center services?

C. Vijaykumar: Yes. Ashwin, see, of course, our overall strategy on infrastructure side was an asset light and the hosting light strategy, so very little of our infrastructure revenue comes from assets and hosting, a lot of it is, in fact, most of it is coming from services. So, to that extent, whether it is in public cloud or on-prem or hybrid, somewhat really doesn't matter. Now, the services footprint, there could be some up and down based on where it is, on-prem or on public cloud. Now, even here, over the last whatever four years, most deals which came for renewal had a very holistic solution approach where we have a roadmap of cloud adoption for our clients. I would say, maybe there is another quarter of our existing customers who may come up for renewal or they may choose the right timing to kind of pursue this. It is a very high level kind of a number, so just take it as a rough estimate.

Ashwin Mehta: And just a follow-up, some of the traditional vendors are indicating that they are even seeing stronger traction on the on-prem data center side of things, largely due to separate levers to shift

on to the cloud. So is something like that being seen by us as well in terms of a surge on work on the on-prem side as well?

C. Vijaykumar: Yes, some customers are taking a phased approach, I mean, what we call as staging data centers, which is you first focus on consolidation and modernizing your applications in an on-prem kind of an infrastructure, and then kind of move it to cloud. And if you have modernized your application, movement to cloud is a relatively easy thing to do from on-prem to cloud. So, some customers are taking that approach. But I think a large number of customers are possibly taking an intermediate step before moving to cloud. But even if it is a smaller segment, you will see a lot of data center providers seeing hyper growth and that is possibly due to two reasons. One is this intermediate step and a lot of hyper scalars are also depending on some of these large data center providers, because their hosting is in one of these DC provider locations.

Moderator: Thank you. The next question is from the line of Yogesh Agarwal from HSBC. Please go ahead.

Yogesh Agarwal: CVK, just one question for you and one for Prateek. See, so Temenos, just delving a little deeper there. Temenos is known for financial products, and you will develop something with them which is non-financial services, enterprises. So, what is the idea to collaborate with Temenos and also pay them $70 million, $80 million?

C. Vijaykumar: Yes. I think Darren should answer this, as I think he is deeply involved in this. Darren, you want to take the product synergies.

Darren Oberst: Absolutely. So, Temenos, like HCL and like most companies does acquisitions from time to time. And if they are looking for technologies to bring to their banking customers, sometimes when they are acquiring these technologies, those technologies are also used by non-banking, non-financial services customers. And so from their point of view, it's a challenge, how do they take the parts of those acquisitions or other product portfolios, apply them to their core market. And then what do they do with the other parts of it, that might be very, very relevant either as a horizontal technology or have a lot of relevance into other industry segments. And so from our point of view, the partnership with Temenos is very much a win-win. In this case, they had acquired a technology called Kony, it is a great technology around low-code, no-code development, digital experience, mobile technologies, was rated very highly by analysts, was really a leading edge technology. From Temenos' point of view, they saw a great opportunity to exploit that technology with banking customers, and specifically take that horizontal technology and then build banking specific and core banking functionality on top of it. But then the question for them was, what do we do with all of the customers, all of the revenue, the product revenue, services revenue, and how do we exploit this IP that's also being used across multiple industries? And that was really the basis of the partnership. We really do see also the potential as we are building a relationship with Temenos in this way, that potentially it could grow over time and could expand into other parts of our business as well.

Yogesh Agarwal: Okay, thanks. And just a quick one, Prateek, so am I missing something, so the amortization amount for this year for the licensed IP of IBM, has that number reduced this year versus last quarter? I think it's gone down by almost $55 million or $58 million.

Prateek Aggarwal: No, Yogesh, it has actually gone up for quarter-on-quarter.

Yogesh Agarwal: No, the schedule for the full year. The guidance you gave for the full year, the amortization, that has come down, I think what you guided last year and this quarter.

Prateek Aggarwal: No, that must be because we are one quarter through, so maybe if you are just comparing versus last quarter for FY '21, the number in this quarter is for the balance three quarters. And when we gave the number last quarter, it was for the full financial year, maybe that' is the disconnect. But we can sort it out offline, no need to spend time on that right now, I guess.

Moderator: Thank you. The next question is a follow-up question from the line of Prashant Kothari from Pictet. Please go ahead.

Prashant Kothari: We are just wondering, how the role of Shiv and Roshni change after this rejig on the Board front. Obviously, Shiv has been instrumental in kind of reinventing HCL through decades, he still remains as the Chief Strategy Officer, so I am not sure how much more involved he would be. Are we kind of seeing changing at the Board level, how much more role Roshni would have in terms of steering the company if you can give some thoughts on that.

C. Vijaykumar: Yes. Roshni would play the role of a Chairperson, while Shiv was playing the role of Chairman and Chief Strategy Officer along with the position of Managing Director. So, Shiv will continue to play the role of MD and Chief Strategy Officer, and Roshni will play the overall governance role as the Chairperson of the Board. So from a strategy perspective, and all the attention that Shiv has on the company will absolutely continue. And I mean, we have a very seasoned and exceptionally strong leadership team, all of them contribute. HCL is built on the principles of ideapreneurship, so all the leaders contribute to the strategy. So I personally do not see any change in the strategy or directions as we move forward. And this is, I am sure, it's a part of a well-planned succession planning that the Board has taken attention to implement. And Shiv also has expressed his desire to step down from the role of Chairman. So it was a logical kind of progress.

Prashant Kothari: So are we like a few years away before Shiv disengages from the business?

C. Vijaykumar: No comments. I don't think I am going to answer any long-term questions on this.

Prashant Kothari: No, you said there is a succession plan in place, I am just trying to understand the timeline.

C. Vijaykumar: Yes, that's what from the Chairperson role Roshni is taking over, that's what I meant.

Moderator: Thank you. Ladies and gentlemen, that would be the last question for today. I now hand the conference over to President and CEO – Mr. C. Vijaykumar, HCL Technologies Limited for closing comments. Thank you. And over to you, sir.

C. Vijaykumar: Yes. Overall, I think we have had a very satisfying execution in a very, very difficult environment on almost all the fronts. And fortunately, the outlook that we have now and what we see are based on some performance in the last quarter and what is visible to us, and some fundamental trends which are positive for the business portfolio and mix that we have, we look at the quarters ahead in a very positive way. And we look forward to sharing further updates in the subsequent calls. And thank you everyone for joining and have a great weekend. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of HCL Technologies Limited, that concludes this conference. Thank you for joining us. And you may now disconnect your lines.