# "R Systems International Limited
# Q3 FY '22 Earnings Conference Call"
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**Moderator:** Ladies and gentlemen, good day, and welcome to R Systems Q3 2022 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 this conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Kumar. Thank you, and over to you, sir.

**Kumar Gaurav:** Thank you, Neerav, good morning to all. On behalf of R Systems, I welcome all the participants to Q3 2022 Earnings Conference Call. We have senior management of R Systems with us in this call. We will start the call with opening remark on the performance of the company by Dr. Rekhi, following by financial overview by Mr. Nand and business overview by Mr. Avirag. Thereafter, we will have a closer statement by Dr. Rekhi. Subsequently, we will open up for Q&A session.

Before I hand over, let me read out the customary disclaimer statement on behalf of the company. Investors are cautioned that this presentation contains certain forward-looking statements that involve risk and uncertainties. The company undertakes no obligation publicly to update or revise any such statement. These statements may undertake revision because of new information, future events or otherwise. Actual results, performance, or achievement could differ from those expressed or implied in such forward-looking statements.

Now, I pass it to Dr. Rekhi for his opening comment. Thank you. Over to you, sir.

**Satinder Singh Rekhi:** Thank you, Kumar. Good morning, everybody, and thank you for being part of this Investor Call. I would like to present an overview of R Systems for the benefit of all those who are joining us for the first time. R Systems was established in 1993 in California as a software engineering company and is now spread across 3 continents with 18 development and service centers worldwide.

R Systems delivers digital transformation services with new types of innovation and creativity to businesses in various industries, technology, telecom, digital media, healthcare and life sciences, finance and insurance, retail and e-commerce. Our deep industry domain knowledge, combined with our expertise in big data, advanced analytics, AI, mobility, IoT, RPA and cloud, help us in transformation of businesses in this digital age.

We continue to witness revenue growth during Q3 2022, especially for digital and product engineering services. Our revenue grew year-over-year 30% to INR 398 crores, that is USD 50.1 million. We have accomplished milestone of USD 200 million annual revenues on a run rate basis. Q3 EBITDA was 14.5% as against 13.1% last quarter. On a nine-month basis, however, it was 13.3% as against 14% in financial year 2021. Although we have improved the margins in Q3, but still margins are under pressure on account of salary hikes, attrition challenges and muted utilization.

Our efforts for rate hikes and higher rack rates has supported the margins to some extent. During the quarter, we have on boarded more than 190 associates and 10 new logos with bigger deal sizes. Profit after tax was INR 36.7 crores as against INR 31.8 crores in the last quarter. We continue to have a strong balance sheet with shareholder funds of INR 490 crores and net cash balances of INR 229 crores to support liquidity and growth. We serve 45-plus million dollar-plus customers as against 38 a year ago.

I will now hand over to Nand Sardana, our CFO, to provide a detailed financial analysis.

**Nand Sardana:** Thank you, Dr. Rekhi. Good morning to all. Thank you, everybody, for attending the call. Hope you and family are doing fine. Let me go into detail of each line item of profitability statement. Revenue for the quarter was INR 398 crores or $50.1 million, quarter-on-quarter increase of 6.2% and year-on-year increase of 30.2%.

As Dr. Rekhi said, with this 50 million revenue in this quarter, we have achieved the milestone of $200 million annual on run rate basis. The increase is primarily on account of volume growth and rupee depreciation. We witnessed good revenue growth for our technology and digital services. We are optimistic for continued traction for product engineering and digital services. However, in last few months, we have witnessed demand softening. There has been good growth from existing customers on top of adding 10 key wins during the quarter.

Getting down to gross margins, it was 36.4% in this quarter compared to 35.3% in last quarter and 37.6% in the same quarter last year. Increase of 1.1% is on account of increase in billing rates and rupee depreciation as offset by impact of higher average salaries. We got rate hikes from existing customers plus improved rack rate for new customers over last few quarters. It has, to some extent, helped us to offset the impact of salary hike.

Getting down to SG&A expense line, SG&A expense has increased quarter-on-quarter by INR 3.6 crores, it was INR 87 crores in this quarter compared to INR 83.4 crores last quarter. The increase is mainly due to increases in sales related costs and other SG&As. EBITDA in this quarter was INR 57.9 crores or $7.3 million compared to INR 49.1 crore or $6.4 million last quarter and INR 48.9 crores or $6.6 million in the same quarter last year.

As a percentage of revenue, EBITDA was 14.5% in this quarter compared to 13.1% last quarter and 16% in the same quarter last year. Revenue growth as supported by exchange rate has led the margin improvement quarter-on-quarter but was impacted due to impact of salary hike. We are committed for further improving the yearly EBITDA number by efficient operations.

Getting down to depreciation, the total expense was INR 8.7 crores compared to INR 8.2 crores last quarter and INR 7.1 crores in the same quarter last year. Interest expense is INR 1.1 crore in this quarter compared to INR 1 crore last quarter. Interest expense is primarily due to adoption of Ind AS 116 and we are near debt-free.

Other income in this quarter was negative INR 2.6 crores compared to negative INR 56 lakhs last quarter. The other income mainly consists of interest income and net exchange gains or losses. Interest income for the quarter was INR 83 lakhs, exchange income during the quarter is negative INR 3.6 crore compared to negative INR 3.1 crore last quarter, mainly due to mark-to-market on forward covers. At the end of quarter, we had total forward cover of $42.9 million with average rate of INR 80.16 and euro cover of 1.7 million with average rate of INR 88.4, which have already been mark-to-market at closing rate of 30 September.

Over the last two quarters, the rupee has depreciated sharply due to global environment, and we have been taking forward cover as per our hedging policy. Our tax expense was INR 8.7 crores in this quarter as against INR 7.4 crore last quarter. Our effective tax rate during the quarter is 19%, primarily due to SEZ benefits and lower corporate tax rate in European and Singapore subsidiaries. Net profit after tax was INR 36.8 crores or $4.6 million compared to INR 31.8 crores or $4.1 million in last quarter. The resultant EPS for the quarter is INR 3.11.

Getting down to the asset side in the balance sheet, total receivable, including unbilled at the end of quarter were INR 311.7 crores compared to INR 230.8 crores at the end of December quarter. The receivable in terms of DSO were 61 days as at the end of this quarter compared to 52 days at the end of December quarter. This is mainly due to timing reasons and our realization from the customer has been broadly in line except for few early-stage companies, where we have taken conservative provision as per the accounting policy.

Net cash balance was INR 229.4 crores at the end of the quarter compared to INR 277.4 crores at the end of December quarter. The reduction is mainly due to interim dividend paid, capex for expansion in SEZ facility and taxes paid during the period. We have been constantly generating cash from the business. R Systems shareholder fund was INR 489.9 crores at the end of the quarter compared to INR 460.3 crores at the end of December quarter. We have a strong balance sheet to support liquidity and growth.

With that, let me hand over to Avirag ji for review of operations. Avirag ji

**Avirag Jain:** Thank you, Nand ji. Thanks, everybody, for being on the call. I hope everybody is doing good. We continue to focus on digital technology and digital transformation project. The strategy has helped us to get momentum for the last few years. I'll give you a brief flavor of our global operation.

Digital transformation continues to be the focus for us on select key verticals like technology, telecom, finance, insurance, healthcare, life sciences, retail and e-commerce. Our digital transformation offering includes cloud, analytics, machine learning, artificial intelligence, data, speech analytics, robotic process automation, IoT, salesforce. These continued to be our arrowhead for growth. On the cloud side, we work on our leading platform such as Amazon, Microsoft Azure and Google. We are advanced partner with Amazon and Gold partner with Salesforce. This is a significant traction in this space. And these are giving us growth in our revenue now.

On analytics, we see high growth in ML/ AI, data and speech analytics. We are currently serving many key clients in this space.

On mobile side, we work on a wide range of technology and devices such an Android, iOS, hybrid and web-app, right from small app to enterprise class application. We had 10 key wins during this quarter. The brief of few key wins are under product lifecycle management, a leading provider of cloud-enabled dental software solution in North America has engaged R Systems to enhance user experience of their products.

Another client is the US-based oncology institute, and they've mandated R Systems to develop a business intelligence and robotic solution, along with enterprise data warehouse and UI improvement for data integration to deliver operational efficiency.

Another customer is a Canada-based IT solution provider. They have partnered with R Systems to redesign and develop a web-based interactive canvas and provide UI/UX services for designing new products.

Another customer is a medical technology company dedicated to bringing diagnostic blood testing to the retail pharma counter. They have engaged R Systems to develop and implement a lab order management solution on AWS cloud.

In Southeast Asia, a leading provider of confectionery products and services across Singapore has awarded R Systems to implement Microsoft Dynamics Business Central and LS Central to digitalize its finance, sales and distribution operation for their multiple outlets.

In terms of headcount, it increased from 3,718 in Q2 to 3,899 in Q3. We have added 180 technical associates during this quarter. Utilization decreased from 77.8% in Q2 to 76.9% in Q3, as we are still keeping some bandwidth and provision for Q4 growth and also to handle attrition. On a quarterly basis, geography-wise, North America contributed 75.6%, Europe 9%, Southeast Asia 12.8%, and the rest of the world 2.6%. On a quarterly basis, client concentration, top 10 client contribute 22.9%, and with largest client above 6.4%.

With this brief overview, I hand over to Dr. Rekhi for his closing comment. Over to you, sir.

**Satinder Singh Rekhi:** Thank you, Avirag. Our performance in the first three quarters of 2022 is encouraging in terms of revenue growth. However, the margins are shy due to increased salary cost and attrition challenges. Our efforts for improving the realization rates, improvement in utilization, coupled with pyramid rationalization will help us to improve margins in coming quarters.

Further, we have taken focused efforts for larger deal sizes to strengthen our margins. Rupee at present level against USD will also support us to improve margins. We continue to invest in sales, pre-sales, digital marketing and in newer technologies. These are helping us to win larger digital transformation projects. In last few months, we have witnessed demand softening amid weakening macro environment. That may affect the high-growth momentum for certain periods. However, we still remain optimistic. We endeavor to utilize strong balance sheet to support operations and growth.

And that brings us to the end of our presentation today, and I'll hand you back to the organizers for your questions and our answers. Thank you.

**Moderator:** Thank you very much. We will now begin the question-and-answer session. Anyone who wishes to ask a question may press '*' and '1' on your touch tone telephone. If you wish to remove yourself from the question queue, you may press '*' and '2'. Participants are requested to use handsets while asking a question.

Ladies and gentlemen we will wait for a moment, while the question queue assembles.

**Moderator:** The first question is from the line of Aspi Bhesania from AB & Company.

**Aspi:** I am Aspi from Bombay. Sir, nobody talked about the open offer. In the open offer, Blackstone wants to acquire 48% at INR 246 per share, when market price is INR 266. As per shareholding pattern on 30th September, Mr. Bhavook Tripathi holds 35%. Will he be prepared to give 35% at INR 246 when market price is INR 266? Sir, supposing Mr. Bhavook Tripathi doesn't give 35%, will Blackstone continue with the open offer and acquire R Systems or will the entire deal fall through?

**Nand Sardana:** Sure. Thank you for your question. So as you rightly said, Blackstone has given a conditional delisting-cum-open offer at price of INR 246. Now, it's a conditional delisting-cum-open offer, and they need 90% to consummate the deal. Dr. Rekhi holds 51.67% and the minimum 38.33% has to come in the delisting offer.

So you see, as of now, the process of shareholder approval, the filing of draft letter of offer and all the other processes are on. The delisting-cum-open offer will open, as I feel, sometime in February as per the timeline. So it will depend what is the price at that time. So to answer your question, when the open offer was given, the price was close INR 238 or INR 239, while price has increased now, which I cannot comment upon. Whether Mr. Bhavook Tripathi will tender or not tender, I cannot comment on that as well.

So what I can comment is that it's a conditional delisting-cum-open offer, if they do not get 90% in total, they are not bound by the deal. So if they don't get 90%, they have option to convert it to an open offer, where Dr. Rekhi still sells them, and they get 26% as per the SEBI rules, stock exchange rules from the open market. So this is what, but it is at their option. What will happen, not happen, honestly telling you, I cannot comment and I do not know that. We will come to know that once the delisting process open, the open offer opens. So, I guess, we need to wait for that.

**Moderator:** The next question is from the line of Abhay Jain, an individual investor.

**Abhay Jain:** First of all, congratulations to management for excellent set of numbers once again, and new journey with Blackstone. I just have a small question, sir. As reflected in the financials, your EBITDA margin has started to improve. What number do you see during close this year as it related to EBITDA percentage?

**Nand Sardana:** Thank you, Mr. Jain, for your questions. We have reported EBITDA margin of 14.5% for this quarter. And year-to-date number is 13.3% for the first nine months. Last year number was 14%. So actually, we are short of last year numbers. How much we'll be able to cover up in the fourth quarter, which is our last quarter and calendar year, I'm not sure, but it seems a little hard that we'll be able to maintain 14% EBITDA this year. We need to wait and watch.

**Abhay Jain:** And what percentage of EBITDA you are aiming in a two-year timeline?

**Nand Sardana:** Well, two-year timeline EBITDA percentage, you see there are several lever for the margin. The biggest lever of the margin, as everybody knows, is the growth. So it depends upon how much we grow. We have grown well in the last two years. But right now, to some extent, there is a US recession being talked off, and there are some ramp downs happening in some of the customers. So growth is the first factor.

The second is, of course, the utilization. We have a scope to improve the utilization. But again, attrition, we need to manage. Attrition had been high for the last two years. But we feel that it should get little bit under control. Other factors are the billing rates, we have got some billing rates, but now as rupee depreciation has happened, so it is little hard to get more billing rate increases. Average salaries have increased. So that is not going in our positive way. But we feel that with the softening of demand, probably this average salary and all that rationalization will happen.

Rupee depreciation is helping us. So rupee had touched INR 83, now it is close to INR 81, but that is helping us. The 3% depreciation of rupee in Q3 helped, we feel at least 2% to 3% again depreciation will happen in this quarter also. So to answer your question, what will be EBITDA margin? There are several factors to that, but we want to increase our EBITDA margin. That's the aim. What will happen, we have to wait and watch.

**Moderator:** Sir, we don't have anyone in the queue. I would now like to hand the conference over to Dr. Rekhi for closing comments.

**Satinder Singh Rekhi:** I want to thank everybody for joining the call and your questions. Have a good day.

**Moderator:** Thank you very much. On behalf of R Systems that concludes this conference. Thank you for joining us. You may now disconnect your lines. Thank you.

(This document has been edited for readability purpose.)

Please note that no unpublished price sensitive information was shared/ discussed during or in pursuance to this Earnings Call.