



Q2 FY 10

Earnings Conference Call

October 26, 2009

Members of Nucleus Management

- | | |
|-----------------------|-------------------------------|
| - Mr. Vishnu R Dusad | Managing Director & CEO |
| - Mr. Pramod K Sanghi | President Finance & CFO |
| - Mr. Niraj Vedwa | President Sales and Marketing |
| - Mr. Prakash Pai | President Product Management |
| - Mr. Ravi Verma | President Human Resource |

Conference Call Dial in Participants

- | | |
|-----------------------|---------------------------------|
| - Mr. Ruchit Mehta | HSBC PMS |
| - Mr. Ravvichandran | UNIFI Wealth Management Limited |
| - Mr. Krupal Maniar | ICICI Securities Ltd |
| - Mr. Aditya | Nirmal Bang Securities |
| - Mr. Anuj Sharma | ASK Investments |
| - Mr. Chirag Setalvad | HDFC Mutual Fund |
| - Mr. Kevin D' Silva | Blackstone |
| - Mr. Nirjhar Handa | M3 Investments |

NUCLEUS SOFTWARE EXPORTS LIMITED

Moderator:

Good afternoon ladies and gentleman. I am Monali, the moderator for this conference. Welcome to the Nucleus Software Exports Limited conference call. For the duration of the presentation, all participants' lines will be in the listen-only mode. I will be standing by for the question and answer session. I would now like to hand over to Ms. Meenakshi Sharma. Thank you and over to you ma'am.

Meenakshi Sharma:

Thank you Monali, and good afternoon ladies and gentlemen. This is Meenakshi Sharma from the Investor Relations team at Nucleus Software. We accord a very warm welcome to all of you to the investor conference call of the Company to discuss the financial results for the quarter and half year ended September 30th, 2009. We have with us today Mr. Vishnu R. Dusad, CEO and Managing Director; Mr. Pramod. K. Sanghi, President Finance and the Chief Financial Officer; Mr. Prakash Pai, President Product Management; Mr. Niraj Vedwa, President Sales and Marketing; and Mr. Ravi Verma, President and Head HR. We would commence with the brief comments on the performance of our Company straight from the CEO and MD, and after that, we would be open for the question and answer session. With this, I hand over to Mr. Dusad for his brief comments.

Vishnu R. Dusad:

Thank you Meenakshi and good afternoon ladies and gentlemen. It gives me immense pleasure to announce the results for Second Quarter and Half Year Ended September 30, 2009.

I will now deal with numbers, first the quarterly figures:

- **Our consolidated revenue** from software products and services for the quarter is Rs. 70.75 crore against Rs. 75.46 crore for the corresponding quarter previous year.
- **Revenue from the product business** for the quarter is at Rs. 39.07 crore, 55% of the total revenue against Rs. 52.10 crore, 69% of the total revenue for the corresponding quarter previous year.
- **Product revenue from own business**, products developed by Nucleus, for the quarter is Rs. 37.70 crore, 53% of the total revenue against Rs. 49.58 crore, 66% of revenue for the corresponding quarter previous year.

Nucleus Software Exports Limited Second Quarter and Half Year Ended
September 30, 2009

- **Projects and services business revenue** for the quarter is Rs. 31.68 crore, 45% of total revenue against Rs. 23.35 crore, 31% of the revenue for the corresponding quarter previous year.
- **EBITDA for the quarter** is Rs. 11.95 crore against Rs. 8.40 crore for the corresponding quarter previous year.
- **Net profit for the quarter** is Rs. 9.88 crore, 14% of revenue against Rs. 4.07 crore, 5% of revenue for the corresponding quarter previous year.
- **EPS is at** Rs. 3.05 for the quarter against Rs. 1.26 for the corresponding quarter previous year.
- **For the half year our consolidated revenue** from software products and services is Rs. 151.29 crore against Rs. 158.35 crore for corresponding Half year.
- **Revenue from the product business** for the half year is at Rs. 86.38 crore, 57% of the total revenue against Rs. 109.36 crore, 69% of the total revenue for corresponding Half year.
- **Product revenue from own business**, product developed by Nucleus, for the Half Year is Rs. 79.29 crore, 52% of the total revenue against Rs.97.10 crore , 61% of revenue for corresponding Half year.
- **Projects and services business revenue** for the Half year is Rs. 64.90 crore, 43% of total revenue against Rs. 48.99 crore, 31% of the revenue for corresponding Half year.
- **EBITDA for half year** is Rs. 27.98 crore against Rs.22.59 crore for corresponding Half year.
- **Net profit for half year** is Rs. 20.01 crore, 13% of revenue against Rs. 12.10 crore, 8% of revenue for corresponding Half year.
- **EPS for half year** is at Rs. 6.18 against Rs. 3.74 for corresponding period previous year.
- **Our total Current investments and bank position** is at Rs. 130 crore as on September 30, 2009 against Rs. 137 crore as at June 30, 2009.
- **In terms of manpower**, we are at 1805 as on September 30, 2009 against 2000 as on June 30, 2009.

I will now talk briefly on the quarter. While we saw a drop in top line, both on a QoQ basis and a YoY basis, we have endeavored to maintain net profit by curtailing expense and converting fixed costs to variable cost .

Nucleus Software Exports Limited Second Quarter and Half Year Ended
September 30, 2009

We have a promising pipeline including large prospects in Japan and Europe and we are making sustained efforts to close deals in the second half of the year and ensure that we continue on the growth curve

Pramod Sanghi:

Good afternoon everybody. This is Pramod Sanghi and welcome to the conference call.

- **On a sequential basis, revenues** are at Rs.70.75 crore with a decline of 12% from Rs. 80.54 crore previous quarter.
- **Product revenue** at Rs. 39.07 crore against Rs. 47.31 crore previous quarter, a decline of 17 plus percent.
- **Traded revenue from products** included in this product revenue is Rs. 1.37 crore against Rs. 5.73 crore previous quarter.
- **Revenue from own Products** is Rs. 37.70 crore against Rs. 41.58 crore last quarter , a decline of 9.3%
- **Revenue from projects and services** is at Rs. 31.68 crore, against Rs. 33.22 crore previous quarter.
- **Cost of delivery** has increased marginally to 67.39% of revenue against 66.85% of revenue previous quarter. In absolute terms, this is Rs.47.68 crore against previous quarter R s.53 .84 crore.
- **Marketing expenses** are at 8.94% of revenue this quarter, against 7.55 % of revenue previous quarter. In absolute terms, this is Rs. 6.33 crore against previous quarter Rs.6.08 crore.
- **The general and administration expenses** are at 6.77% revenue this quarter, against 5.72% of revenue previous quarter. In absolute terms, these are at Rs. 4.79 crore against Rs. 4.61 crore in previous quarter.

It is to be noted that expense reduction has resulted in the total cost of delivery varying closely with revenue, with no reduction in absolute marketing expense.

G and A expenses are also sticky and it is our endeavor to vary cost of delivery while making sure that both Marketing and G and A expense are absorbed over a larger revenue base.

- **Total expenses** in the quarter are at Rs. 58.80 crore, 9% lower than Rs. 64.53 crore in previous quarter, and we are moving towards achieving a 10% reduction in overall expense for the year while endeavoring to maintain revenue base.

Nucleus Software Exports Limited Second Quarter and Half Year Ended
September 30, 2009

- **EBITDA** has decreased to 17% this quarter against close to 20% previous quarter with a larger fall in revenue.
- **Other income** is at Rs. 2.17 crore against Rs. 3.16 crore previous quarter.
- **There is a foreign exchange gain** of Rs. 34 lakhs against a loss of Rs. 4.28 crore previous quarter.
- **Withholding taxes** are Nil against Rs. 9 lakhs previous quarter. As credits get available, this is turning more into a tax at source rather than an expense.
- **Total taxes including withholding taxes** are 13.7% of adjusted PBT against 13.4% of PBT last quarter at a group level.
- In **Depreciation** there is a minor decline.
- **PAT** is at Rs.9.88 crore, 13.97 % of revenue against Rs. 10.13 crore, 12.58% of revenue previous quarter.
- In terms of **hedges**, we had on September 30, 2009, USD 7.50 million dollars of forward contracts @ 48.72 with a mark-to-market gain of about Rs. 27 lakhs which is taken to hedging reserve in the Balance Sheet. We have a 1. 6 million \$ option which is marked to market at 48.11, which was the closing rate on September 30.
- **Our total hedge** as on 30th September was USD 9.10 million and we are basically covering close to our India receivables. **As of date the coverage** is US \$ 12.33 million, with forwards increasing to US \$ 10.73 million at an average rate of Rs. 48.26. There is no change in the option amount.
- **Dollar moved** from 50.74 on 31st Mar 09 to 48.11 on 30th September 09, appreciation in INR value of 5.18% and today it has been quoting around 46.50. We have to see how we deal with it. For the current year we have based our working at Rs. 47 and we would average Rs. 47 plus for the year.
- With regard to **receivables**, we are at Rs. 75 crore against Rs. 74 crore previous quarter and the **DSR** is still at about 91 days.
- **Top 5 clients** at 67% against 62% last quarter.
- **The order book position** is Rs. 180 crore including Rs. 123 crore of products business and Rs. 57 crore of projects and services business, against Rs. 200 crore last quarter with Rs. 130 crore of products and Rs. 70 crore of services. You will see the services figure has fallen more than products.

Some details of our bank deposits:

- We have balances with scheduled banks in India of Rs. 18.37 crore.

Nucleus Software Exports Limited Second Quarter and Half Year Ended
September 30, 2009

- We have balances outside India including our subsidiaries of Rs.13.70 crore.
- We have fixed deposits with Citibank, HDFC Bank, Canara Bank, Bank, Punjab National Bank, ICICI Bank, State Bank of India, Corporation Bank and Bank of India totaling to Rs. 66.59 crore as of September end.

We have mutual funds of Rs.30.79 crore where the average maturity period is 60 to 90 days of maturity for the entire fund.

I will now handover to Niraj to take you through various aspects.

Niraj Vedwa:

Okay, good afternoon everybody. I will start by covering from a sales and marketing perspective. It has been a reasonable quarter for sales and marketing. This quarter we have won 5 new product orders for 20 modules taking our 6 month's tally to 16 product orders and 56 modules. Our product prospect pipeline is very healthy and we are pursuing 100 cases for closure. These are prospects where demos and RFP's have been completed. Markets globally are opening up and we do expect reasonable closure's before Dec end.

During the quarter, we participated in following events this quarter. SIBOS, the largest banking event at Hong Kong ; 4th Middle East Retail Banking event in Dubai : 6th CEE retail banking event at Vienna. We have generated many good lead's thru these events. We have had excellent coverage thru various research firms. Gartner has featured FinnOne in "Lending report" and Cash@Will in "Payment services Hub" report. Forrester research has recognized Nucleus for Banking platform deals in 2008 and so has Celent research in Islamic vendor report. Endorsement by these leading global research companies add's substantial brand value and recognition and creates a clear niche for us. We added 4 new channel partners. We have also closed our first 2 orders from US market for our payments product. Substantial number of prospects have been created in LATAM and Europe and we expect these markets to start generating good results. Thank you. This was from the sales perspective.

I would also cover "Delivery" on behalf of R. P. Singh, who is not available today. From a delivery perspective, During the quarter 25 modules were implemented successfully across the globe. Some of large implementations for global roll-out's have been doing well. GMAC is now live in Italy / Benelux and during the quarter we went live in UK. We have started work on new countries for GMAC. We continue to intensify our focus on process implementation. We had a slight lull in the market place and used this time into an opportunity to strengthen our processes and foundation. We have since then, enhanced many of our processes. One of our very large implementation for FinnOne multi-country roll-out has given us a Voice of customer rating of over 9.5 in two of our implementations. Delivery capability and productivity is being enhanced by addition of Business Analyst's and Domain Subject matter experts and by use of automated tools. We are making every effort to have very high Voice of Customer ratings for all our implementations through 100% process compliance.

Prakash Pai:

Good afternoon everybody. To keep pace with emerging trends in the global arena to continue on our path of being No 1 in Lending and Cash management, a number of product releases have been done and some new developments initiated. We have a new Java version of Cash@Will released. This product is also being upgraded to add "Financial supply chain" functionality.

The new FinnOne Pro version which will be platform independent will be released in February 2010. This will have the latest SOA architecture. We are releasing a Core banking suite for small and medium sized banks. It is pertinent to mention that some of the recent modules released such as Forecaster / Lead Management / Customer Service module and Dealer Funding have started gaining high visibility and recall and a number of orders have been won for these modules.

Ravi Verma:

Thank you Prakash and good afternoon. Q2 has been very challenging, as we planned to managed all our requirements with the internal resource movements as far as possible. Selective hiring continued for skills not available internally. In addition, we continued to take temporary/ contract staff for short term ramp up requirements of the projects. Manpower numbers have therefore been reduced from 2000 to 1805 as most of the vacant positions due to employees leaving organization have been filled internally from resources released due to ramp down of few projects.

Cross platform training was a major initiative we have taken in the last quarter to bridge the skills gaps of employees to meet the business need. Resources are undergoing training and skills enhancement before allocation to the next assignments. Resources who have been ramped down are being prepared to support the new product releases. Extensive skills enhancement programs are being conducted for Technology and Framework knowledge for the new product. Product knowledge has been captured and is being translated in the form of Computer Based Trainings (CBT's). This has ensured the building of knowledge repository at organizational level.

Management review frequency was increased and is aimed at giving more focus to defect free delivery with process compliance. Project management and planning tools developed internally, have been rolled out at organization level. This tool is helping the projects in proper planning and monitoring productivity of the resources.

As far as attrition is concerned, it has been well under control and it has no adverse impact on business. Thanks.

Meenakshi:

Thank you and now we would be open to the question and answer session.

We have Mr. Ruchit Mehta from HSBC.

Ruchit

The large customer that we lost in the previous quarter, there was some pending settlement yet to happen. Any update on that?

Pramod

The only update is that we are in discussions with the customer and we do hope that we will resolve this within the financial year.

Ruchit

In terms of cost management, you mentioned that you are looking at about 10% reduction in cost for the year, but in terms of margins, where do you see margins stabilizing or sustaining at?

Pramod

You would have seen that margins this year have been, better than last year and we did close to 20% in the first quarter and though the revenue went off a little bit in the second quarter, we have still maintained about 17%. And we do expect them to remain in the same range.

Ruchit

So, it is between 17% to 20% range?

Pramod

Yes, I think we should talk on that only once we achieve it.

Ruchit

Thanks.

Monali

We have Mr. Ravvichandran from UNIFI Capital.

Ravvichandran

Good evening everybody I just have a couple of questions. First one is on the Japanese contract .Could you please repeat that update on the contract?

Pramod

We are in discussions with the customer, and we do hope that we will be able to resolve the issue within this financial year.

Ravvichandran

The order book position has come down even further from last quarter. What has been the reason for this?

Pramod

Firstly the order book has come down in the services business, where we had picked up some large orders last year and they have been executed. We are still making efforts to get more services orders and there is of course a decrease in the product orders. As Niraj had mentioned we picked up five orders against about eleven in the last quarter and let Niraj share a little bit more why it was a really weaker quarter than normal.

Niraj

As Pramod said, in the first quarter we had booked eleven and in the last quarter we booked five product orders. Primarily bulk orders that we were expecting was from the Middle East area where July-August are normally summer vacation period and then September was Ramadan period. So because of frequent travel and holidays, some of the decisions have delayed, this quarter. This is a regional trend, and we do expect that this quarter that we would bounce back in terms of business.

Ravvichandran

So the next quarter would presumably be better off?

Niraj

Presumably yes, it would be much better.

Ravvichandran

Any guidance for the order book that you provide?

Niraj

No, we do not provide any guidance on the order book. I think all I have mentioned is that we are following almost 100 odd prospects, where we have submitted proposals and that demos have also happened and with the markets opening up, people want to take decisions. This is an encouraging trend, so we do expect a lot of decisions to happen in this quarter.

Ravvichandran

Any major orders that are ending in this December quarter or coming up for renewal or something like that?

Niraj

Ours is not a renewal business. We are in product business, where in you get an order which includes the license and implementation along with the customization. After that, it gets into a support, which normally, varies between 15% to 25% in terms of annual maintenance, so renewals do not happen. On the services side, where contracts are of renewal nature, there we have some monthly and quarterly renewals.

Ravvichandran

So, that is a more volatile kind of a revenue source?

Pramod

In services, we have two major customers; one has been with us for 15 years and the other for 10 years. While of course, banks have the right to select their vendors, we do hope that in the short-term at least there is no major risk to any of those engagements.

Ravvichandran

The other question was on the employee front. Almost 200 employees have been reduced this quarter?

Pramod

Well, in terms of the numbers, that is correct. The number has come down by 200. I think "reduce" is not the correct term to use.

Ravvichandran

Would you be looking at bringing that number further down because your margins have improved majorly because of this?

Pramod

We had mentioned in a call, maybe two quarters before, that in 2008-2009, we did build up infrastructure and people hoping for better market space. But when that did not materialize, we had to look at curtailing our cost base. And today we feel that, we would be somewhere around these levels only. There would be some attrition, there would be some new entries based on skill sets, and we do not expect it to move significantly from this number at the moment.

Ravvichandran

Finally, on the tax rate, what is the effective tax rate right now?

Pramod

Effective tax at the group level of PBT is working to about 13% .

Ravvichandran

Is that expected to increase in FY'10 or FY'11?

Pramod

No, It is not expected to increase next year because there is no change in the income tax rules in next year. At the moment, one of our units has completed the tax holiday period, that is why the taxability is coming now.

Ravvichandran

Can you give some color on how the competition is building up in this space because there are other players also?

Niraj

There are both global and local players, and we have of course two lines, one is the lending area and the other is the payments area. In the lending business, in some markets we clearly have a very high degree of penetration like in the Middle East, where we are extremely strong.

Ravvichandran

Because players like I- Flex also, are moving into the Middle East market.

Niraj

iflex has already been there in Middle East and Africa, but they focus more on the core banking area and not on the lending area. Of course, they do come and compete with us a number of times. We have 3i which comes in, there is Fair Isaac. So there are a lot of regional and global players. In a lot of markets we come out as clear winners, like Middle East we are clear winners, and African

Nucleus Software Exports Limited Second Quarter and Half Year Ended
September 30, 2009

market, as of now we still have a leadership position. We have announced our 14th order over the period of time, but we have a leadership position in many markets.

Then if you come to the cash management area, if we come to the Asia-pacific markets, there is Fund tech, ACI, but if we go to Europe, then we have operators like Teatro and Clear2Pay. There are different players, and we are seeing some good traction in both these areas. As Prakash explained that on the product perspective, we are enhancing our product to basically retain our leadership position in these markets. And in the markets where we need to do something, we are creating some differentiators to win the results.

Ravvichandran

Differentiators in what way, like, is it specialized product that has been offered or module wise that differentiates?

Niraj

Differentiation can come in many ways. One is, differentiation comes in, in terms of functionality. Let us say we talk about cash management area, I think in terms of depth and breadth of our functionality, we are clearly very much ahead of many of our competitors, and we have added financial supply chain in the products, which will be available to customers. There is technology enhancements like coming up with the Java version, different levels of pricing, you could go for transaction based pricing or portfolio based pricing. So we can create a number of differentiators for customers, we also can cross sell, you buy something and you have something else at a good price.

Ravvichandran

All the very best.

Pramod

Thank you.

Monali

We have Mr. Krupal Maniar from ICICI Securities.

Krupal

Hi, I think we mentioned of some large pipeline in Japan and Europe, so can Vishnu throw some light on this?

Vishnu

Certainly Krupal. We are talking about our lending product to various players in both these markets, Japan as well as Europe. Likewise we are also talking about cash product in Europe, and Asia Pacific, so this seems to be extremely encouraging prospect for us, and we are very bullish about it.

Krupal

Thanks a lot.

Meenakshi

Thank you Monali and thank you everybody for making this a wonderful call. I would now like to hand it over back to Vishnu for his closing comment.

Vishnu:

We would like to take this opportunity to thank you all for your keen interest and support, and we look forward to meeting you in times ahead.