



Q1 FY 11 Earnings Conference Call August 2, 2010

Members of Nucleus Management

- | | |
|-----------------------|-------------------------|
| - Mr. Vishnu R Dusad | Managing Director & CEO |
| - Mr. Niraj Vedwa | Chief Operating Officer |
| - Mr. Pramod K Sanghi | President Finance & CFO |
| - Mr. Ravi Verma | President and Head HR |

Conference Call Participants

- | | |
|----------------------------|----------------|
| - Mr. Manik Taneja | Emkay Global |
| - Mr. Deepak Radhakrishnan | UNIFI Capital |
| - Mr. Neerav Dalal | Capital Market |

Nucleus Software Exports Limited

Meenakshi

Thank you Sandhya, and I wish good afternoon and a warm welcome to all of you from Nucleus Software and welcome you at our investor conference call for the first quarter ended June 30, 2010. We have with us today Mr. Vishnu R. Dusad, our CEO and Managing Director; Mr. Pramod K. Sanghi, the Chief Financial Officer; Mr. Niraj Vedwa, Chief Operating Officer; and Mr. Ravi Verma, President and Head HR. We will begin with the initial comments on the performance of the company from the CEO, and after that, we would be open for the question and answer session. With this, I would like to hand over the floor to Mr. Dusad for his comments.

Vishnu:

Thank you Meenakshi and good afternoon ladies and gentlemen. I am pleased to announce the results for First Quarter ended June 30th, 2010.

This has been a difficult quarter with both revenue and profitability declining on a year on year and sequential basis. The decline in revenue is a consequence of the weak order book at the beginning of the quarter. At the end of the quarter, with the improvement in the economic environment and 15 new order wins, there is an improvement in the order book and we are on course to improve performance in the coming quarters.

Now I will take you through the numbers.

- **Our consolidated revenue from software products and services** for the quarter is at Rs.66.14 crore against Rs. 80.54 crore for the corresponding quarter previous year.
- **Revenue from the product business** for the quarter is at Rs. 42.95 crore, 65 % of the total revenue against Rs. 47.31 crore, 59 % of the total revenue for the corresponding quarter previous year.
- **Product revenue from own business**, products developed by Nucleus, for the quarter is Rs. 39.55 crore, 60 % of the total revenue against Rs. 41.58 crore, 52 % of revenue for the corresponding quarter previous year.
- **Projects and services business revenue** for the quarter is Rs. 23.19 crore, 35% of total revenue against Rs. 33.22 crore, 41% of the revenue for the corresponding quarter previous year.
- **EBITDA** for the quarter is Rs. 4.71 crore, 7.12% of revenue against Rs. 16.02 crore, 19.88% for the corresponding quarter previous year.

- **Net profit** for the quarter is Rs. 5.29 crore, 8% of revenue against Rs. 10.13 crore, 12.58% of revenue for the corresponding quarter previous year.
- **EPS** is at Rs. 1.63 for the quarter against Rs. 3.13 for the corresponding quarter previous year.
- **Our total Current investments and bank position** is at Rs. 181.33 crore as on June 30, 2010 against Rs. 162.40 crore as on March 31, 2010.
- In terms of **manpower**, we are at 1528 as on June 30, 2010 against 1558 as on March 31, 2010.

Going forward it is incumbent on us to deliver value to customers and increase shareholder value and we have to work extremely hard and manage business far better to achieve our potential. We reiterate our commitment on returning to Top line growth and increasing market share.. With all the new orders we have won, we are confident of maintaining the Nucleus edge. Thank you very much and over to you Pramod.

Pramod

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

- **On a sequential basis, revenues** are at Rs.66.14 crore, decrease of 8.46 % from Rs. 72.25 crore previous quarter.
- **Product revenue** at Rs. 42.95 crore against Rs. 48.11 crore previous quarter, decline of 10.72%.
- **Traded revenue from products** included in this product revenue is Rs. 3.40 crore against Rs. 12 crore previous quarter.
- **Revenue from own Products is** Rs. 39.55 crore against 36.10 crore previous quarter and this is a positive sign
- **Revenue from projects and services is** at Rs. 23.19 crore, against Rs. 24.14 crore previous quarter, a decline of 3.95%.
- **Cost of delivery** has increased to 70.28% of revenue against 66.85 % previous quarter.
- **Marketing expenses** are at 11.56% of revenue this quarter, against 7.55 % of revenue previous quarter. In absolute terms, this is Rs. 7.67 crore against Rs.

Nucleus Software Exports Limited
First Quarter Ended June 30th, 2010

- 4.95 crore previous quarter. For the full year FY 10 the amount was Rs. 22.67 crore and the current run rate is reflecting the increased spend on sales and marketing planned this year
- **G&A expenses** are at 11.59% of revenue this quarter, against 7.54% of revenue previous quarter. In absolute terms, this is Rs. 7.28 crore against Rs. 5.44 crore previous quarter.
 - **Total expenses** in the quarter are at Rs. 61.43 crore, against Rs. 58.42 crore previous quarter.
 - **Total expenses** in the quarter excluding trading related costs are Rs. 57.91 crore against Rs. 51.35 crore in previous quarter.
 - **EBITDA** is at 7% this quarter against 19% in the previous quarter with lower revenues
 - **Other income** consisting largely of investment income is at Rs. 2.19 crore against Rs. 2.06 crore previous quarter.
 - **There is a foreign exchange gain** of Rs. 1.50 crore against a loss of Rs. 2.43 crore previous quarter. This is a result of Dollar appreciation to 46.70 on June 30 against 45.09 in March end, and the effect on receivables and other foreign currency denominated current assets. At the same time there is a Rs. 0.57 crore gain on forwards which is part of the revenue.
 - **Withholding taxes** are Rs. 12 lakhs against Rs. 34 lakhs last quarter.
 - **Total taxes including withholding taxes** are 11% of PBT against 17% of PBT last quarter at a group level.
 - **Depreciation** is Rs. 2.47 crore against Rs. 2.36 crore previous quarter.
 - **PAT** is Rs. 5.29 crore, 8 % of revenue against Rs.9.19 crore, 12.72 % of revenue previous quarter.
 - In terms of **foreign currency hedges**, we had on Jun 30, USD 12.25 million dollars of forward contracts at an average rate of 46.27 which are designated as highly probable forecast transactions. There is a mark-to-market loss of Rs. 87.55 lakhs which is taken to hedging reserve in the balance sheet. We do not have any options outstanding as on Jun 30, 2010.

- **Our total hedge** is USD 12.25 million and we are basically covering close to our India receivables which are USD 13.46 million as of Jun 30, 2010.
- March 2010 we had a total hedge of USD 10.40 million.

- **Current Coverage** is USD 11.75 million at an average rate of 46.40.

- With regard to **receivables**, we are at Rs. 42.69 crore against Rs. 57.68 crore previous quarter and the **DSR** as on 30th June is at 59 days against 72 days as on March 31st.

- **Top 5 clients** at 64 % against 67% last quarter.

- **The order book position** is Rs. 190.12 crore, including Rs. 156.82 crore of products business and Rs. 33.31 crore of projects and services business, against Rs. 164.25 crore last quarter with Rs. 116.95 crore of products and Rs. 47.30 crore of services.

- We have mutual fund investments of Rs.105.14 crore against Rs. 95.65 crore in March 2010 our cash holding has gone up to Rs 180 crore end of June.

Niraj

I will first start with the order booking position. We have had a record in terms of the order booking numbers. We have for the first time in any quarter won 15 product orders from across the world for 48 modules, to be implemented across 22 countries, out of which 16 will be new countries. Also happy to state that one amongst these orders is from one of the top ten banks in Europe, and this is for implementing our cash management solution in 14 countries. Seven of them would be in Latin America, six in Europe and one will in USA. Our investments in the European market as well as Latin American markets have begun to, bear fruit.

Also wish to state that these orders in revenue terms are equivalent to 84% of the orders booked in the last full financial year for the product business. So, whatever we booked in the last financial year in terms of product booking, we have done 84% of that booking in this quarter through these 15 orders and also to recall that we had done 31 orders in the full financial year 2010 and we have done 15 in the first quarter of this financial year itself.

We have also a very, strong pipeline, in this quarter, and have received 43 requests for proposals from customers and more than 100 demonstrations of product have been given. Our pipeline count in terms of number of prospects to close, for a decision, has become stronger and it is reaching up to almost 120 in number.

Now, in terms of the operations, we have focused very heavily in the last two quarters on improving our execution capability. We have focused very strongly on, quality of work and increase in productivity. Every piece of code that is going out from Nucleus is thoroughly tested and goes through quality assurance. We have put in new divisions like the Business Analyst Pool and Delivery Assurance Group to ensure that all the stated as well as unstated requirements from the customers are clearly documented, and the project is managed well. We do expect that with increase in delivery revenue, our cost of delivery would also reduce due to adoption of all these measures.

In terms of channel partners, we have added four new channel partners this quarter. Work has already initiated on all these orders that we have won. The teams are being set up, and in most of the cases, work has already started, our focus is to ensure that we do reasonable completion of work in this quarter for all these customers. Our higher focus is to ensure that we have a very short time-lag between receiving of customer order and start of a project and the end delivery to the customer at the shortest possible time. With the market now opening up, and a strong pipeline, we are quite confident of, booking many orders in this quarter and stronger revenues as we move on

Ravi

Good afternoon everyone. Q1 has been a quarter for consolidation and preparing for business growth challenges. We have continued with our focus to manage all our requirements with the internal resource movements as far as possible and improving productivity of the existing teams. There has been more focus on hiring to meet the new business needs as well as to take care of the reconciliations against employee separation. More freshers have been inducted. Manpower numbers have therefore been under strict control and reduced to 1528 from 1558. Role alignment of project managers and training on Project Management Knowledge, PMBOK and Business Analyst Training, BABOK were major thrust areas. Project management and planning tools developed internally were further enhanced for better project management.

Regular communications with the employees, open houses, for understanding and resolving their concerns, has been a major activity for the last quarter.

The attrition levels have increased slightly; however, are well in control and have no adverse impact on our business.

Meenakshi

Thank you Ravi and over to you Sandhya for the Q&A session.

Manik

Sir just wanted you to guide on what is the kind of pipeline you are seeing across geographies for both FinnOne and the Cash Management product. Last quarter you had mentioned, there were close to 170 odd RFPs in the market and now you are talking

about a reduced number. Secondly, I wanted to understand we had implemented wage increments for only a select few staff earlier. What have you done with regards to the balance staff, and once again if you could give us the status of your order book position?

Pramod

We have largely closed the increments effective April 1, 2010, and for the India employees we expect to close it between 12% to 13%, which is the average.

Manik

Is that for the entire staff?

Pramod

It is for the entire staff.

Manik

I remember last time when you had given your full year number, you had mentioned that there would be a selective hike for people with experience of two to four years or between the range of 13% to 14% and for the balance 60% staff, you were still to take a call.

Pramod

That is correct. When we had the last call we had already implemented appraisals for people in different categories and that figure was correct at that point of time. Now, I am giving you the overall figure. Which is for the entire India-based company. Secondly you had asked me for the order book position. The order book position is Rs. 190.12 crore, which includes Rs. 156.82 crore of products business and Rs. 33.31 crore of services business. Niraj will reply to your first part of the question regarding the business prospects region wise.

Niraj

In terms of the RFP bids, the figure is closer to 100. What I mentioned to you was that we have a strong pipeline for decisions in the coming quarters which has now increased from the figure of 100 and now that figure has gone up to 120. So, not only have the number of RFPs gone up but also the number of demos that we are giving has increased substantially. RFPs are coming from all across. We have, many enquiries which have come in from Latin America, Caribbean, Europe, Africa, Middle East, and also the Mediterranean belt. Also, we have put in a lot of focus in Eastern Europe, and now two sales people are dedicated for the Eastern European markets. We have an increased number of RFPs, and of course, from our traditional bases like India, Middle East, Africa, and South East Asia, we continue to get RFPs. So, the distribution is now from

all across the geographies. Perhaps with the exception, some RFPs coming from the US as such. We are getting enquiries from everywhere, and all those investment decisions that we had taken, to increase support and sales people in Europe, Latin America, etc., are now giving results. As I said before, we received a large order from one of the top ten banks for implementing our cash management product in, six countries in Europe, seven in Latin America, and one in USA., We also have our first order from Canada, Mexico, Australia. and Lebanon. So, these are the new countries from where we have received orders, So, there is an increased traction happening in Europe and also in Latin America.

Manik

Would it be fair to assume that FY' 11 will be an inflection point in terms of the kind of investments that we have been making in terms of sales staff for Europe, UK, and Africa..

Niraj

What we can say here is that the decisions we took are already bearing results, and with the market opening up, in lending, the area where we have been really badly hit in comparison to most of the other companies because we are a company into lending and cash management area and lending business had come to an absolute zero all over the world. Clients are not lending any money, so now with things opening up, , we have started receiving these orders. This is a very encouraging sign, and now we also have a very strong pipeline for this quarter and with, lot of decisions happening in this quarter and in the subsequent quarters, the pipeline is very strong and these are all cases where we are in the, last stages of decision making where you have customer references or price negotiations

Manik

Sure sir, and I have another question for Mr. Sanghi. Sir, generally, we used to give salary increments which were significantly ahead of the industry at least versus the services guys. This year, you have just given a 12% to 13% salary hike which would at best be on par with the services guys. Do you think that you will be able to address employee churn?

Pramod

First, we did give one increment in December also which was approximately 10%. So, we have followed that up by another increment in April as well. Secondly, you are right that there is a lot of churn in the industry and people are talking different kind of methods of retaining people and so on, but we will take it as we go.

Manik

Could I get the attrition number?

Ravi

It is nearly about 23%.

Manik

And that is on a LTM basis or on a quarterly annualized basis?

Ravi

Annualized basis, quarterly annualized basis.

Manik

Best of luck for the future. Thank you.

Ravi

Thank you very much.

Deepak

I just wanted to understand if you would be concentrating on any particular geography as such or is it across the globe?

Niraj

We have grown from one region to the other, but at this stage I think, we have adequate sales people in almost all the regions, but obviously if you want to win the big orders, they come from our traditional strongholds like Japan, so obviously there is a high focus on Japan. We are increasing our sales strength in Japan to bring in a Japanese team and we already have one Japanese person. They will be focusing on securing large orders. Japan and Europe are two markets where investments will continue, and these will be of high focus.

Deepak

How do you manage competition? I have seen a lot of companies having similar products. Do you face real competition from the Indian players?

Niraj

We face competition from almost all the Indian core banking vendors and we also face competition from the international global vendors like Mysis, SAP, Fidelity, Fair Isaac, etc. We face competition from the local players also. If we are in Middle East, besides the European, American vendors and, Indian vendors, we also face competition from the

local vendors. In RFP's also, there may be about 10 to 11 bids , but in most cases we reach the last two or three stage. So, that is not really an issue.

Deepak

Do you provide any guidance on the top line and bottom-line?

Pramod

No, we have not been providing and we will not be able to provide.

Deepak

Will there be a better number compared to at least last year, any thoughts on that?

Pramod

That is same as providing guidance. We are here in the business to grow and to deliver shareholder value, obviously we will look at growing. We would not like to define specific numbers.

Deepak

On the pricing front, do you still face pressure?

Pramod

Yes, we do face pressure of course on pricing.

Deepak

Thank you and all the best.

Neerav:

Good afternoon sir. Sir, I had two questions. One is your software development expenses have gown down in spite of a salary hike. Could you comment on that and the second one is where do you see the absolute numbers for the SG&A for the year?

Pramod

I mentioned in my opening comment that we were looking at marketing expenses of almost Rs. 8 crore in this quarter and that is the current run-rate which we expect to maintain during the year. If you look at G&A, , we are at about Rs.7.3 crore, and the last

year's number was about Rs. 20 crore. So, we should not be very much away from our last year's numbers.

Neerav:

Okay, sir and the software development part?

Pramod

Software development, as you know, is something which is more variable as such definitely and while what you are saying is that from March we have come up a little bit from Rs. 48 crore to about 46 crore.

Neerav:

Despite the 12% wage hike.

Pramod

But then we have had attrition, and net numbers have gone down slightly and we have also been able to control some part of the variable cost there.

Neerav:

Thank you.

Meenakshi

Thank you ladies and gentlemen for being with us for the duration of this call. I would like to hand it over to Vishnu for his closing comments. Over to you Vishnu.

Vishnu:

Thank you very much ladies and gentlemen for your continued interest in Nucleus Software, and as I had mentioned in my opening remarks, we reiterate our commitment on returning to top line growth and increasing market share, and with all these new orders that we have won in this quarter, we are confident of maintaining the Nucleus edge. Thank you very much.