



**Geometric Limited**

**Conference Call Transcript**

**July 24, 2009**

**Moderator:** Ladies and gentlemen - good morning, good evening, and welcome to Geometric Limited's Q1 FY10 Earnings Conference Call. As a reminder, all participants will be in the listen-only mode, and this conference is being recorded. There will be an opportunity for you to ask questions at the end of today's opening remarks. If you should need assistance during this conference call, please signal an operator by pressing star (\*) and then zero (0) on your touchtone telephone. I would now like to hand the conference over to Mr. Saurabh Gada. Thank you and over to you, Sir.

**Mr. Saurabh Gada:** Thank you and welcome to Geometric Q1 FY 2010 Conference Call. We have with us today Mr. G. Ravishankar, MD & CEO; Mr. Raja Ramana Macha, Chief Operating Officer; and Ms. Priya Jadhav, VP – Finance. At this moment, I would like to hand over the floor to Mr. Ravishankar for his opening remarks.

**Mr. G Ravishankar:** Good evening everyone, and thanks Saurabh. In this call, I would first talk about the market environment, and walk you through the financial performance of Geometric in the first quarter. And then we will open it up for question/answer, so that we have more time to discuss on the questions that you have.

With regards to the business environment, the economic downturn continues, and we didn't see much of a difference as compared to the previous quarter. The customers did not decide in this quarter also, and they decided to postpone their investments in the areas, where they can avoid investing in this quarter. But we are seeing a good pipeline building in this quarter, as the customers are very interested in starting investing as and when the markets improve. We believe that the downturn has really hit the bottom, and thereafter, it is going to be an increase as we move along.

In terms of our performance in this quarter, we consciously decided to decrease our revenues in the U.S. engineering services operations that we had; which is the acquired operations that we bought sometime in end 2006. The full impact of the ramp-downs that we had, because of the adverse economic environment was

also very evident in this quarter. The number of deals that we have in the pipeline, has increased, and the impact of these new deals, that we have closed or we are in the process of closing, is expected to be seen only after the economic upturn starts, which we expect to happen sometime in the last quarter of this year.

The movement of the business that we did, from onsite to offshore, to take care of the price reduction that customers demanded, also positively impacted the margin. If you remember, in the last quarter, we set out three principles for us:

1. To ensure that the U.S. operations turn around to a positive PAT number during this year,
2. To consciously cut our SG&A and other costs, which we could avoid, and
3. To align our organization in line with what we can expect to deliver to our customers.

We had good impact or improvement in these three fronts. The organization structure was changed into a business unit vertical-wise structure. Therefore, the business unit heads were able to interact more effectively with the customer, work on improving the revenues, and mine those customers; as we find that it is easier to get more revenues from our existing customers rather than go and find new customers. The cost reductions that we put in place in Geometric yielded very good results, and you will see that the SG&A cost has decreased by about 36% as compared to the previous quarter, and is 18% lower as compared to the previous year.

Thirdly, on the other initiative of turning around the business operations in the U.S., we had very good success. As against the approximately US \$3 million loss that we made in the previous year in our acquired operation; in this quarter, our loss was restricted to just US \$300,000. Reducing the revenues, which did not contribute positively to our contribution margin, also played a very significant role.

If you see our financial performance, the operating revenue was lower because of these reasons that I mentioned. One is consciously reducing our revenues in the U.S. operations; the second is the full impact of the ramp-downs that we saw in the previous quarter. The exchange rate was also lower as compared to the previous quarter by about 3.5%, whereas as compared to the previous year, the same quarter, we gained significantly. We increased by about 15%.

Our focus on containing the cost of revenue, and increasing our utilization helped us; the contribution margin as a percentage of operating revenue was 40.8% as compared to 35% during the same quarter in the previous year. The significant focus on SG&A expenses ensured that our SG&A expenses are significantly lower, and as compared to the previous quarter, they were lower by about 36%. Overall, as a result of all these activities, the operating profit significantly jumped to about 13.2%, as against 4.3% we saw in the previous quarter. The other income loss was also restricted, and I will share more in detail about the forward contract that we have done, and what is our strategy in that space as we move along.

Overall, the quarter was very good for us. The profit after tax improved by about 6.9% from a (-17.9%) in the previous quarter; and the earnings per share (EPS) increased to about Rs. 1.34 as against Rs. 0.55 in the whole of previous year.

In terms of our operating revenue during this quarter, our services revenue decreased by about 4.8%, as compared to the previous year. An important aspect is that our offshore revenue also decreased by about 3.6%, and onsite revenue came down by 9%. This was due to our conscious efforts to bring some of the onsite revenues offshore, to ensure that our customers benefit from the price reductions that we can offer because

of this. At the same time, doing this also helped us improve our margin. Our contribution margin significantly increased during this quarter, and coupled with this, the savings in manpower, software and facility costs helped us maintain a good profitability position.

Also, in the previous quarter we made some provisions for the receivables due from Chrysler and General Motors. I am very happy to share with you that the Chrysler and GM issues are behind us at this stage. We have been named as critical supplier and both these customers have paid us almost all the dues, and there is a very small amount of US \$250,000, which is under dispute, and we hopefully, will resolve that also in this quarter.

In terms of negative impact, the exchange rate moving down from Rs. 50.47 to a dollar to Rs. 48.51 impacted us in this quarter; and utilization was marginally lower by about 1% point. So overall, the quarter was good, and in fact, we were able to win some new orders, which are of significant importance to us as we move along. One was the quality assurance support engagement that we won for one of the software OEMs. We also won an embedded product development support contract for a global OEM major. The product engineering contract that we won from a global agricultural and construction equipment manufacturer for their European operation is also a significant one. As we move along, the order pipeline is stronger and we see good traction, especially in Europe.

If you see our revenues from Europe, it has increased to 26.4% from 21.6% in the same quarter of previous year. Consciously, we have been reducing our dependence on U.S. as an important market for us, and we have seen that as we move along, we will be able to improve our share of revenues from Europe.

At the end of this quarter - it is a very satisfying quarter - we see good traction as we move into the next quarter, and we feel that the losses are behind us. The strategy that we set out for ourselves in terms of ensuring a significant improvement in our profitability, reducing losses in our U.S. operation is working out, and we are in good state to meet our plans for this year. So with that, I would like to move on to the question/answer session, so that I can answer your questions rather than we talking more.

**Moderator:** Thank you very much Sir. Ladies and gentlemen, we will now begin the question-and-answer session. If you would like to ask a question at this time, please press star (\*) followed by one (1) on your touchtone telephone. Our first question is from Mr. Anubhav Khandelwal of B&K Securities. Please go ahead.

**Mr. Anubhav Khandelwal, B&K Securities:** Hi Sir. Can you break up the decline in revenues in terms of pricing and volume?

**Mr. G Ravishankar:** Yeah, the pricing dropped by about 1.6% during this quarter, and the volume dropped by 4%.

**Mr. Anubhav Khandelwal, B&K Securities:** Okay. So the 9% decline in revenues comes from the exchange rate movement?

**Mr. G Ravishankar:** Yeah, 5% is the decline at the dollar level, and the remaining comes from the exchange rate at Rs. 50.

**Mr. Anubhav Khandelwal, B&K Securities:** Okay. And Sir I wanted to check have all the unprofitable ventures of the U.S. been exited out or are there some more ventures also in the pipeline, which need to be exited out in the future quarters?

**Mr. G Ravishankar:** No, we acquired Modern Engineering that is the only entity that we acquired sometime in 2006 end. In terms of projects that we were to exit, we have exited almost all loss-making projects as of last quarter. Therefore, that's the reason, why you are seeing that the revenues declined significantly in the U.S. operations. And as we speak, we don't have any of those loss-making contracts that we used to do. But in this quarter, we feel that the impact of plant shutdown that auto majors in U.S. normally do in the second quarter of our financial year is likely to extend by a week or so. So that could impact the revenues that we will see in this quarter. We are planning to ensure that our profit after tax is close to zero in the U.S. operation as far as possible despite the plant shutdowns.

**Mr. Anubhav Khandelwal, B&K Securities:** Okay, thanks a lot. That's all from my side Sir.

**Moderator:** Thank you Mr. Khandelwal. Our next question is from Mr. Ruchit Mehta of HSBC Asset Management. Please go ahead.

**Mr. Ruchit Mehta, HSBC Asset Management:** In terms of your margins, the EBITDA you have about 18.5%, going forward where do you see this stabilizing at? What additional levers do you have or is this good enough for the current year? And then also looking ahead for two-three years, where do you see it heading towards?

**Mr. G Ravishankar:** Okay. So the EBITDA as for this quarter is about 15.6% and at a constant exchange rate we would like to see our EBITDA at a target I would say to be at least 20%+. So that's where we would target. The 15.6% that we have done in this first quarter is in line with our plan, or slightly better than the plan that we had set for ourselves for this year. I am sure, we will be able to maintain it for this year assuming that the market conditions remain the same and doesn't deteriorate any further.

**Mr. Ruchit Mehta, HSBC Asset Management:** Okay. And in terms of business, you mentioned your pipeline which starts kicking in, in terms of Q4, but are we in terms of quarter-on-quarter business, are you done with the ramp-downs and how do you see the quarter going forward panning out?

**Mr. G Ravishankar:** No, I think most of the ramp-downs that we witnessed in the last year, the full impact of that has been in the first quarter. But, however, we have our doubts on one or two customers, which could impact us during this year. But that's where our efforts in building the pipeline is very important for us, to ensure that we meet the targets that we have set for ourselves during this year.

**Mr. Ruchit Mehta, HSBC Asset Management:** In terms of your balance sheet, you have repaid some debt also in the quarter but in terms of, there was also goodwill write-offs that you needed to take off with regards to Modern if I am not mistaken, what's the status on that and what is the total quantum outstanding?

**Mr. G Ravishankar:** Right. So we have applied to the court for a restructuring exercise and the court has admitted our application. It is now going through various processes of approval post submitting the application. We expect that to happen in the next week or so. The total amount that we have set aside in our restructuring reserve is about Rs. 130 Crores.

**Mr. Ruchit Mehta, HSBC Asset Management:** Okay. So you need to write-off Rs. 130 Crores against your reserve.

**Mr. G Ravishankar:** Yes. That's the amount that is set aside. The actual number will be known in the next week or so.

**Mr. Ruchit Mehta, HSBC Asset Management:** Okay great. And just in a broader sense last year you did about US \$130 million odd in revenues, and your current run rate is just a shade above US \$100 million. Would it be too tough to hit the last year's revenue mark and how badly will you be down from last year's US \$130 million run rate.

**Mr. G Ravishankar:** No, revenue reduction that we have done is a conscious reduction because, as I have explained to you, on an average in the U.S. engineering services, we used to do close to about US \$9 million in a quarter but now we have reduced it to about US \$5-5.5 million level. So that's a conscious reduction that we

want to do, because our complete focus for this year is on improving the profitability rather than doing more revenues. And as far as the estimate for this year is concerned, we have decided that we are not going to give out any estimates at this stage. But our whole effort is on improving the profitability in the business rather than chasing the top-line.

**Mr. Ruchit Mehta, HSBC Asset Management:** Interestingly, you also have increased your hedges on a quarter-on-quarter basis, in the current quarter what you have disclosed is higher than the second; is there any reason for that?

**Mr. G Ravishankar:** Yes, in one of the businesses based upon our visibility, etc., we have decided to get into forward contract for more than 12 months, and we wanted to take advantage of the rate that we see at this stage. The customer also wanted to do that and therefore, the forward contract that we see is higher than what we did for the previous quarter.

**Mr. Ruchit Mehta, HSBC Asset Management:** So these are essentially 12 months and beyond, not for the current year, this US \$99 million?

**Mr. G Ravishankar:** No, US \$99 million is both for 12 months as well as some portion is beyond the 12 months' period.

**Mr. Ruchit Mehta, HSBC Asset Management:** Okay, good thanks.

**Moderator:** Thank you Mr. Mehta. Our next question is from Mr. Janish Shah of Quantum Advisors. Please go ahead.

**Mr. I. V. Subramaniam, Quantum Advisors:** Yeah, hi this is Subbu, Janish's colleague, here. I just wanted a flavor on the SG&A expense, which you have reduced. What exactly did you do, and are they more temporary in nature or structural? And will this remain low going forward, if you can just indicate?

**Mr. G Ravishankar:** Sure. This is something that we talked at length in the previous quarter as well. So the restructuring of the organization that we did, is to ensure that we are aligned with our customers, and we

ensured that there is faster decision making, which helped us rationalize a significant amount of manpower – that’s number one. We also are very cautious on the other expenditure that we do. And if you compare our previous quarter SG&A and this quarter, even after removing the unusual; we are significantly lower than the previous quarter - this is more structural in the nature and we expect this trend to continue as we move along. For previous quarter, we decided to exit some of the facilities that we had in the U.S. There also we exited by paying some premium as they were locked up for a longer term. Now we have done all that, and I see, unless there is something extraordinary that’s happening, our SG&A expenses will remain at this level.

**Mr. I. V. Subramaniam, Quantum Advisors:** Thank you.

**Moderator:** Thank you Mr. Subramaniam. Our next question is from Mr. Saurabh Gurnurkar of Kotak. Please go ahead.

**Mr. Saurabh Gurnurkar, Kotak:** Yeah, most of my questions have been answered, just one thing if you could throw some more color on the demand environment that you see, is there some material improvement over the last three months since we last interacted? And if yes, which are the parts of the business where you are seeing a perceptible difference? Thank you.

**Mr. G Ravishankar:** Right. As I mentioned in the early part of my discussion that the market continues to remain as it was in the previous quarter, and we don’t see any significant change in terms of actual decision by the customer. All the customers have decided to postpone some of their discretionary spends, which is impacting our businesses at this stage. However, as we see it, there is an improved or a significant shift in the customers wanting to know as to what are the projects that they can invest in or they can do as and when the economy improves. Therefore, there is a good amount of pipeline that’s getting built and I am sure in the next couple of quarters, we will be able to see significant closures on those fronts. That’s why we said that from quarter three or quarter four, we will be able to see those revenues coming up based upon the economic outlook changing.

**Mr. Saurabh Gurnurkar, Kotak:** Okay, just one more question, your operating cost has gone down significantly sequentially. I just wanted to understand whether this cost structure you think is maintainable or do you see some more scope for optimizing costs?

**Mr. G Ravishankar:** No, to be on the safer side, I would say that you know we will maintain the current cost structure that we see in this quarter. While there are some more opportunities but I would reserve my comments on that until and unless such time that we are able to see a reduction there.

**Mr. Saurabh Gurnurkar, Kotak:** Okay, and any guidelines for CAPEX you are earmarking for this year?

**Mr. G Ravishankar:** I think about Rs. 250 million to Rs. 300 million is what we would expect as CAPEX in this year.

**Mr. Saurabh Gurnurkar, Kotak:** Okay, right, thank you. All the best.

**Moderator:** Thank you. We have a follow-up question from Mr. Ruchit Mehta of HSBC Asset Management. Please go ahead.

**Mr. Ruchit Mehta, HSBC Asset Management:** If you can give us a more sense on the product side of the business, and especially at some point in time we had gone from having a channel-based or partner-based model to being more aggressive on going directly to the market. How is that shaping up and in terms of products, what sort of visibility are you getting?

**Mr. G Ravishankar:** If you see our entire focus is on building a channel-based sales approach and we have been very successful at that. Between last year and this year, we have increased our geographic spread in the sense that we went into the European markets, and that's one of the reasons why our product revenue has more or less remained stable even when we saw reduction in the U.S. markets. We will continue to have our focus on the channels. In this year, we have introduced a new product called DFMPPro, and as we have seen in the first quarter, the traction is very good. The interest that is shown by the customers for this product is very good, and we hope that we will be able to make a good impact on this. We will continue to invest in our product lines as we feel that creating IP is a very important part of our business. We don't expect the product lines to drop as compared to the previous year.

**Mr. Ruchit Mehta, HSBC Asset Management:** Great, thanks.

**Moderator:** Thank you Mr. Mehta. Our next question is from Mr. Janish Shah of Quantum Advisors. Please go ahead.

**Mr. I. V. Subramaniam, Quantum Advisors:** Sir, this is Subbu again here. This acquisition, which you have made in Germany and renamed as Geometric Europe GmbH, can you just let me know what does this company do and what is it about?

**Mr. G Ravishankar:** Okay. We have started an entity in Germany, because we want to consolidate all our operations in Europe under a subsidiary in Germany. So there is nothing significant in this acquisition, I mean it's not doing anything. It's a shell company that we acquired to get all our operations under one legal entity in Europe.

**Mr. I. V. Subramaniam, Quantum Advisors:** Okay, Sir, thanks.

**Moderator:** Thank you Mr. Subramaniam. There are no further questions from participants at this time. I would now like to hand the conference over to Mr. Ravishankar to add closing comments.

**Mr. G Ravishankar:** I will request Mr. Raja Ramana Macha, our COO, to do the closing remarks.

**Mr. Raja Ramana Macha:** Thank you Ravi. Just to summarize, the current economic outlook, we have had some ramp-downs but we are seeing a lot of stabilization that's happening with our customers at this point of time. The economy, especially in the U.S., continues to remain challenging though we are seeing greater amount of traction from Europe. Our operational parameters have been under control, and our focus has been to constantly improve on productivity through the operational parameters. That's reflected in results as well, and Ravishankar, of course, touched upon the SG&A control and all the actions that we have taken at this point of time to ensure that our SG&A remains within the bounded parameters we have set for ourselves in this quarter and this year. Going forward, we would be working on a very strong sales force transformation program, and that should yield greater amount of results for us or ensure that we have stability in the output of the revenue generation model. The other aspect of the sales force transformation also is to introduce newer offerings into the market, and that will happen in the next quarter. We have had turnaround in the U.S. operation through careful focus on the manpower cost management, and that is something that we would continue going forward as well.

Lastly, I found that there is significant amount of pricing pressure from all our customers across the board. We intend to counter the pricing pressure through improvement in productivity, so that we maintain profits at the same level. Thank you so much for your attention.

**Moderator:** Thank you gentlemen of the Geometric Limited Management. Ladies and gentlemen on behalf of Geometric Limited that concludes this evening's conference call. Thank you for joining us on the Chorus Call Conferencing Services and you may now disconnect your lines.

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