Geometric Software Solutions

Q1 FY08 post results Conference Call

July 17, 2007

Moderator: Good evening ladies and gentlemen. I am Pratibha, the moderator for this conference. Welcome to the Geometric Software conference call hosted by Edelweiss Securities. For the duration of the presentation, all participants' lines will be in the listen-only mode. After the presentation the question and answer session will be conducted for participants at international bridge followed by a Q&A session for participants at India. I would now like to hand over to Mr. Kunal Sangoi. Thank you and over to you sir.

Kunal Sangoi: Thank you Pratibha. Good evening and a warm welcome to all of you joining on Q1FY08 post results conference call of Geometric Software Solutions Co Ltd on behalf of Edelweiss Securities. At the outset we extent our appreciation to the management for giving us the opportunity to host this conference call. We have with us today Mr. Manu Parpia, Founder and Vice Chairman; Dr. Ravi Gopinath, CEO and Managing Director; Mr. G. Ravishankar, Chief Financial Officer; Mr. Shashank Patkar, VP - Corporate Strategic Initiatives; and Mr. Michael McConnell, CEO of Modern Engineering to represent the company. Without further ado let me hand over the floor to Dr. Ravi for his opening remarks. Over to you sir.

Dr. Ravi Gopinath: Good evening everyone, this is Ravi Gopinath here. Thank you for joining us in this call for our quarterly results presentation. I believe that the presentation has been mailed to you and the format that I would like to follow is to give you a set of brief introductory remarks and then throw open the line for questions so that we can spend a maximum amount of time answering any questions that you folks may have.

So, if I were to sum up the quarter's performance as seen in the presentation, in terms of top line, we experienced a decline in revenue of 1.3% in sequential operating revenue in dollar terms. The appreciation of the rupee vis-à-vis the dollar also had a significant impact on operating revenue which flowed all the way down into the operating profits of the company. This effect was obviously mitigated by our systematic coverage of foreign exchange exposure and that impact was helped.

In terms of how the business has essentially transformed, I know many of you have questions in terms of the top line and sales, but I would like to first of all comment on some of the disaggregation of the top line performance. So as we start, a 1.3 decrease in operating revenue in dollar terms. Services revenues, and what we are classifying as services is - the PLM services, the outsourced product development services, and the engineering services - overall decreased by 0.7% vis-à-vis the previous quarter. Within this the offshore revenues grew by 5.7%, but offsite revenues and onsite revenues both came down. This has had an positive impact because offshore revenues essentially account for higher profitability for us and our emphasis on delivery efficiencies have ensured that some of the productivity gains that we have delivered in our offshore project have helped mitigate the adverse impact of rupee appreciation and also the fact that in the first quarter we absorbed the salary hikes that were implemented.

In terms of the other segment of our business vis-à-vis products, products revenues declined on a more significant basis, there was an 8.6 reduction over the previous quarter and even on an yearly comparison vis-à-vis Q1 of last year. There was a 11.2 decrease in terms of our product revenues, and this is something clearly from a 'go-to-market' perspective an improvement of the sales efficiencies we are paying a great deal of attention to.

In terms of my comments on what have been the chief factors with regard to the top line slow down - There are two things as I had mentioned starting from our analyst conference in January that we made a very conscious decision as a company at that point in time and we continue to remain true to that decision that it is important for us from a long-term perspective to ensure that Geometric goes directly to the end-users of PLM in the context of our software business, and of course in the engineering services business, which has added significant momentum through the acquisition of Modern Engineering, the customer base was anyway direct, and we wanted to ensure that we had adequate leverage of that engineering resource base and also convey our deep PLM competencies more and more directly to the end-user segment. In the Q4 of last year we kicked off a sales initiative on a global basis with that direct initiative in mind, and what we are seeing today in terms of the top-line impact is essentially a consequence of that change in direction wherein when you are talking to the end-users of PLM. We automatically start dealing with longer sales cycle, probably less predictability in terms of how much time it will take to close, but the up-side as far as we are concerned is that, as we have started closing the deals we are clearly seeing a benefit in terms of the realization that we are able to command through much better billing rates and indeed the strategic nature of the engagements that we are now winning is certainly pointing in the favorable direction. So, as I have said also in our media release that in Q1 has completely new business that we just did not have in Q4; we closed over $5 million worth of new business. This momentum is continuing in a significantly positive direction even in Q2, but the outcome is that as we close these deals the maturity into billing is going to start from the second quarter and the third quarter and go progressively forward from there. So, I believe what we have seen in terms of the Q1's marginal dip in revenues is an outcome of our changed 'go-to-market' strategy on the core software business of Geometric, a lengthier sales cycle, but all that we have put together as a go to market proposition; I have been very happy with the response that we have seen in the market and which is certainly reflected in the pipeline that we built in terms of orders booked in Q1.

As far as the engineering business is concerned and I am sure all of you also have questions in terms of Modern Engineering and what progress we are making there, but let me talk about the sales first. In terms of the engineering business, as you know Modern Engineering has a very very strong automotive engineering brand. They have been in the business of automotive engineering for a long time and that certainly is a strength and a strategic reason for why the acquisition was made. But the Detroit automotive market has its own complexities, has its own challenges, and I had pointed that out. I believe in our Q4 analyst call as well, and what the management of Modern and we have been doing over the last one quarter is to ensure that we take the competencies of Modern and sell them to a much broader industry vertical footprint. I am also happy to say that amongst the deals that we closed in Q1 and we are now closing in Q2 there is a definite reflection of the vertical diversification of Modern into sectors outside of the automotive domain and into regions of the US outside of Detroit. Both of these trends in my view will have a positive impact in terms of how the business pipeline will build up for the future.

While we look at that as the sales development and this transformation was a fundamental reason why we seen the dip in top line, it is also important to understand, what we have been doing in the operations end to ensure that we are creating a base on which we can scale and grow profitably. I had maintained in the last call and in our January conference that it is going to be our constant endeavor to ensure that we keep focused on profitability. What we are experiencing today in terms of the operating profit margins and the hit that we have taken essentially reflects downwards from the top line dip and the double whammy of the rupee appreciation, which of course has been a sectoral hit. But what we are doing in the delivery side and the operation side is two folds; one is, as I mentioned in the opening part of this call, a significant emphasis on the operational efficiencies, we know that as we grow in business, as we start pushing out our proposition more and more, as we start getting better and better deals which we clearly have been getting over the last quarter in terms of billing rates and in terms of strategic nature of the projects, our ability to execute more complex fixed price engagements have to increase. And what we have delivered, especially in projects over the last 3-4 months, has been a very high degree of offshore productivity and efficiency. What this means is that our ability to estimate fixed priced projects, our ability to deliver to those estimates and hence assure the profitability that we are modelling into the business at the beginning of the project cycle there is a much higher degree of assurance, and that has been a direct outcome of the investments that we have made in creating competency groups and delivery processes, which really started somewhere in the middle of Q4. This is one of the reasons why despite the hit of the rupee appreciation and the fact that we had to make wage increases, we were able to mitigate some of that through the productivity increase in the offshore business, which as I mentioned earlier, grew by 5.7% on a sequential basis.

As far as Modern Engineering is concerned, as you would see on the slide Modern incurred a net loss of $321,000. This was certainly not planned for, but the big reason is as following: as I said Modern's performance issues stem from two points; one is there has been a, just like in the rest of the business of Geometric, a time factor for the top line to drop, but that pipeline is building up and because of the slowdown in that growth and actually a delay in the growth that we have planned a lot of the slow down in to the bottom line got pushed out and which is what we are seeing as a profitability loss. The other issue is that the offshoring from Modern Engineering has been to a lower extent in Q1 that we had originally planned for, but we are firmly focused along with the Modern management in ensuring that the end of year goals, which is what we are really shooting for get achieved.

Now I just wanted to ensure that one dynamic of offshoring of Modern Engineering's business is clearly articulated and understood and that is the ability to offshore some of the work and in fact a lot of the work that Modern does which in fact the complexity and content is pretty much high end and at front end of the engineering cycle. It necessitates a high degree of competency in each one of our offshore centers, and when I am talking offshore, I am not just talking India but I am talking essentially a portfolio balance between India, Romania and China which are our global centers. So the creation of the competencies in each of our global centers so as to be able to absorb this work is a process that is very actively on right now. So some of the initiatives that we have kicked off, is in addition to locally training the people on work areas we have moved people from Modern in Detroit into Bangalore, and that embedding of Modern's Detroit competencies into our Bangalore center, we believe is going to have a significant impact on the momentum for offshoring, which in turn will translate into the bottom-line effect that we hope to see.

So, in summary, I would say that we have said upfront that Q1 and Q2 of this year are going to be tough because we wanted to emphasize and continue to focus on the building blocks for our future scaling pattern, and those building blocks are essentially ensuring that our 'go-to-market' strategy was aligned with out 2010 strategy which is to secure an added customer base, #2, create scalable delivery processes across all of our global locations, #3, create a very very strong competency framework at an institutional level across all of Geometric and its subsidiaries. We have focused our attention on this and it is our conviction as we continue down this path , the returns in terms of top-line growth of the right quality and in terms of profitability will definitely be felt. So, while we have seen a dip that we certainly did not want to see in Q1, the results of our activities on the ground in terms of the health of the pipeline and the way we are building up the business is certainly positive, and with that I will conclude my introductory remarks and so this call opens for any questions that any of you may have. Thank you.

Moderator: Thank you very much sir. At this moment I would like to hand over the floor to Salbia to conduct the Q&A for international participants. This will be followed by a Q&A session at India. Thank you and over to you Salbia.

International Moderator: Thank you Pratibha. We would now begin the Q&A session for participants connected to the international bridge. Please press 01 to ask a question. Participants who wish to ask a question please press 01 now. At this moment there are no questions from participants at the international bridge. I would like to hand over the proceedings back to Pratibha.

Moderator: Thank you very much Salbia. We will now begin the Q&A interactive session for participants connected to the India bridge. Participants who wish to ask questions please press *1 on your touchtone enabled telephone keypad. On pressing *1, participants will get a chance to present their questions on a first-in-line basis. Participants are requested to kindly use only handsets while asking a question. To ask a question please press *1 now.
First in line we have Mr. Sandeep Shah from ICICI Securities.

Sandeep Shah: Yeah sir, if we recollect the last 3 months back in the last conference call we had said that the guidance is conservative, but now incorporating the first quarter sales number, it seems that the guidance on the sales front seems optimistic. So what has been changed during the last 3 months where the conservative guidance is suddenly becoming optimistic and what kind of visibility to have outstretch our guidance of 50% sales growth in Indian rupee will be achieved?

Dr. Ravi Gopinath: As I said, the basis for the guidance, and the basis for the fact that we are maintaining our guidance, as of now remains our understanding of the sales cycle and how the pipeline is building up. If I were to just give you a sense of when we had kicked off the sales initiative in our major markets, which is US, in Q4, the number of new deals that we have closed, I am not talking about extension of existing contracts, I am talking of actually new projects that we had won was just a shade over a million dollars in value.
In Q1 of this year that similar number in terms of new deals that we have closed, whether it is from the new kinds of projects of existing customers or new projects from entirely new customers that value has gone up from just around $1 million to over $5 million, and then the trend is continuing in a similar direction. Ultimately our ability to grow the business is a direct function of our sales team and how we are taking our combined value proposition to the market, it is directly proportional to that, and what we have done consistently even from the time that we had our last quarterly call, in our main markets, we have added two more sales people. So, the momentum is in the right direction. We are making the investments in the sales team like I have said, and that is fundamentally the basis on which we assure that the business can be developed, because I have absolutely no doubt in my mind that any time we go to market and present the consolidated capabilities that we have as an organization it is a compelling value proposition to the customer, and we have seen that in action, because I have personally led sales calls.

Sandeep Shah: Sir, if we just put in the first quarter numbers and apply a 50% growth YOY, I think on a quarter-on-quarter basis we actually grow our consolidated sales by almost 17%, so do you believe such kind of growth is now expected to start from a second quarter or it will take even the second quarter will be something muted and the second half will have an accelerated growth?

Dr. Ravi Gopinath: I have very consistently stated that the growth will start from the second half.

Sandeep Shah: Okay, and sir the guidance is in terms of rupee, just wanted to reconfirm that?

Dr. Ravi Gopinath: The top line was in dollars right, and the bottom line is in rupees.

Sandeep Shah: Sir the bottom line is in rupee and the top line is in dollars?

Dr. Ravi Gopinath: Yes.

Sandeep Shah: Okay, and can you give some sense in terms of the growth with the R&D and the PLM services as well as engineering design within the services vertical?

Dr. Ravi Gopinath: No, I am sorry, what …..

Sandeep Shah: Within the services, what are the growth rates in the R&D, PLM services, and the engineering design?

Dr. Ravi Gopinath: That is there in the business segment. If you look at what you call the R&D piece which is what we call the outsourced product development, that increased by 9% over Q4.

Sandeep Shah: Okay, and the PLM services?

Dr. Ravi Gopinath: Overall, the software segment, which includes R&D, which is software product development plus the PLM software solutions, the PLM system integration, is flat, which means that the PLM external services business showed a decline in revenues. Fundamentally the reason for that is the delay in two significant engagements which are now commencing in this quarter.

Sandeep Shah: Okay, so it was a delay from our front in terms of software delivery?

Dr. Ravi Gopinath: No, it was a contracting delay from the customer side.

Sandeep Shah: Okay, and what was the dollar revenue growth within the Modern Engineering?

Dr. Ravi Gopinath: I am sorry, what is the question again?

Sandeep Shah: Dollar revenue growth within Modern Engineering?

Dr. Ravi Gopinath: Yeah, Modern Engineering showed a very marginal decline.

Sandeep Shah: Okay, and sir the new deals we were earlier saying that whenever we will do, the gross margins in the direct business will be much higher than the partnership business, so what kind of billing rate increase you are witnessing in the direct business?

Dr. Ravi Gopinath: Yeah, we are seeing a definite increase in terms of the billing rates and there are at least a couple of examples where cross selling relationship has certainly helped promote a much stronger value proposition, and just to give an example in one of them, I cannot name the customer, but in one of the customers we have got now onsite rates varying between $75 and $100 an hour.

Sandeep Shah: Okay, and this if you compare it with the partnership then what was the rate like?

Dr. Ravi Gopinath: The partnership was between the 45 and 55 range.

Sandeep Shah: Okay, and this kind of revenue execution will start from the second half?

Dr. Ravi Gopinath: It will start, see the orders have closed and the revenue execution will start from the second half.

Sandeep Shah: Okay, and just on the book keeping side, the taxation has gone down significantly. So if we take out that then even the guidance on the bottom line seems optimistic.

Dr. Ravi Gopinath: Yeah, Ravishankar our CFO is here, so he will take that.

G. Ravishankar: If you see taxation for this quarter, it has been a 2% profit before tax which was compared to 15% in the previous quarter, it is essentially because most of the activities where we had profits this quarter are from the exempt units.

Sandeep Shah: Okay, so what kind of tax rate one should have ‘built- in’ going forward for the year as a whole?

G. Ravishankar: I think you should look at around 10% as the tax rate for this year on a PBT basis.

Sandeep Shah: Okay, and this current quarter tax doesn’t include any one time reversal of earlier provisions?

G. Ravishankar: There was a small reversal, which was about Rs. 2 million only.

Sandeep Shah: Okay, and sir depreciation has increased, so what is the reason and is it like going forward more depreciation is likely or it will remain more or less at this stage?

G. Ravishankar: No, it is going to remain around the same rate. This is because some of the investment we did last year on our computers and related investments, plus in the last year we also implemented our ERP systems, so the depreciation of which started hitting our books this year.

Sandeep Shah: Okay and just last question right now from me is to Mr. Ravi Gopinath. While getting direct business what kind of competition we have won, in the sense what kind of other vendors we have replaced?

Dr. Ravi Gopinath: We have been winning deals against big companies both from India and multinationals.

Sandeep Shah: Okay, thanks and all the best, I will come up in the follow up.

Dr. Ravi Gopinath: Thank you.

Moderator: Thank you very much sir. Participants are requested to kindly limit to one question in the initial round of Q&A session. Follow up questions will be taken later. Next question comes from the line of Mr. Ruchit Mehta with HSBC.

Ruchit Mehta: Hi. Good evening. On the margin front, your margins this time around have got 7% at EBITDA level, going forward and if you were to deliver on that balance because of 30-35%…..

Dr. Ravi Gopinath: I am sorry, you are breaking up, are you on a mobile?

Ruchit Mehta: No, no, can you hear me now?

Dr. Ravi Gopinath: Yeah, sounds to be better.

Ruchit Mehta: On your margins, you know this quarter we were about 7% at the EBITDA level, how much of a leverage are you seeing in the following quarters? Is it going to be the second half we will have absolutely no cost growth and incremental revenue growth for instance to the bottom line and therefore you may see the 30% bottom line growth? And, where do you see the margins stabilizing over the 2-3 year timeframe, can you scale it back up to the 15-16% levels?

Dr. Ravi Gopinath: Over a 2-3 year timeframe as I said in the 2010 plan that we have stated, our margin target was in the 18-20% range at the operating margin level, but if I look at you know your question on the EBITDA and what we are doing in terms of controlling, there are two or three levers we are working right now. As I said earlier, No. 1 is as we start driving business offshore and a greater mix in terms of the fixed price projects and the complexity of the projects, we are focusing on the productivity levers that we have in our project delivery. No. 2, we are driving up a ramp in terms of the offshoring that we are doing for Modern. No. 3, you will also see that we are very actively controlling and managing our SG&A expense. A lot of this unfortunately gets magnified when the operating revenue in rupee terms takes a significant hit because of the appreciation effect, of course it starts off with the marginal decline in our dollar revenues but certainly the effects are accelerated because of that. So, we are taking a very close watch on SG&A. We are looking at productivity in our offshore delivery particularly, and increased offshoring in our global engineering content; and these are fundamentally the three levers that we have got to operate.

Ruchit Mehta: Okay, and can you just break up your 13.5 crores of other income into what was to forex gain and what is the recurring other income?

G. Ravishankar: This is essentially about 120 million of this is from the forward contracts. We follow a methodology of do a marked-to-market on our forward contracts, so accordingly we mark the contracts to the forward rate as of June 30th and because of this the effect of gains on the forward contracts which are there from the assets that we have in the books plus the forward contracts which are on the highly probably transactions got translated into other income this quarter.

Ruchit Mehta: See effectively when you are looking to…..

Moderator: Mr. Mehta, sorry to interrupt you sir. Can you please come for a follow up?

Ruchit Mehta: Okay, thank you.

Moderator: Thank you very much.

Dr. Ravi Gopinath: Thank you.

Moderator: Participants are requested to kindly limit to one question in the initial round. Next in line we have a question from Mr. Ajay Nandanwar with India Capital.

Ajay Nandanwar: Hi! Seems like a decent quarter with volatility. I was just trying to understand going forward you talked about delays in Modern work moving offshore and also some of the deals, as to you know what sort of your target offshore mix in terms of effort for the Modern business?

Dr. Ravi Gopinath: We are targeting in between 35-40% by Q4. As I said it is on the ramp, and currently if you look at the global offshore efforts that Modern is executing it is probably around 10-12% of their total effort, and we are targeting that by Q4. We move it in the 35-40% range, okay. As I said it is going to be ramped, and certainly in the next financial year we will probably have a higher target but we need to ensure that we are working this ramp carefully, because as I said earlier, it is very tightly linked to creating the ability to absorb that work in our global locations and then ensure that people in the US are appropriately motivated and incentivized to make this happen.

Ajay Nandanwar: Okay, in this 35-40% offshore effort target, do you expect this to come from cuts in the US manpower or is it going to be driven by growth?

Dr. Ravi Gopinath: Our emphasis is to see that we do this on growth as far as possible.

Ajay Nandanwar: Sure, and what kind of risks for variability exist at this point in being able to achieve that number, how much of further business development is required to reach that kind of target?

Dr. Ravi Gopinath: See for us it is going to be very strongly correlated to the sales bandwidth that we put on the ground. You know if you look at the sales mix that we had earlier, Modern had a sales force and Geometric had a sales force, and we brought them together, and in the combined sales force if you looked at the location concentration, a very very large I would say almost all of it was concentrated in Detroit. Because that was the strongest market both for Geometric in the US as well as Modern historically. So, what we are doing is through a rationalization of the sales force , we are now creating capacity in other parts of the US. So we are boosting up our sales team in Houston to go after the oil and gas manufacturing segment. We are increasing sales bandwidth in the West coast to look at some of the industries there, so we are carefully mapping out industry clusters and where we need to deploy our sales team. This is going to take a certain amount of time because we need to ensure that we are moving the right people and we are hiring the right people , who have the ability to hit the ground running. So we are being selective because we want to ensure there the success rate is high.

Ajay Nandanwar: Sure, given that the deal cycle is fairly long, 3-6 months, in the average case, and project ramp ups will take time, we are only looking at 3-4 months from now to actually close the business for 35-40% offshore effort.

Dr. Ravi Gopinath: Yeah, see there will be a mix of it. I understand your question. So what will happen is that if you look at some of the content of Modern's work, and I can hand this also over to Michael McConnell who is on the call right now to provide further details. But if you look at the cycle of projects and the way the projects evolved, there is a certain front-end work that is done in Modern in the US and they hand over the downstream activity in a specific project to any of the global locations. Now these projects can vary in duration from 12 to 16 weeks or 18 weeks, so it is a question of how the new business flows in and it is not just a new business that is only targeted for driving to an offshore location, because there is some of the downstream work that is already being done in the US. So the question is , as a new business comes in, focus the US team almost entirely on the front end engineering and start moving as much of the downstream engineering work to the global locations as possible. I will also let Michael chip in with any comments that he would like to make.

Michael McConnell: Yeah, as a relief to this cycle of business, our goal as Ravi mentioned, of embedding US business in our global locations and that not only includes India but also includes Romania and China delivery centers, and to scale up that competency , so that we are able to move further up in the design cycle, force the front end, and set up the downstream activities occurring in weeks 8, 12 or 16 where they get the global data content. As the global centers we are now looking to be in the 2-4 weeks portion of the design cycle to **mould** their content through a global delivery center sooner upstream.

Ajay Nandanwar: So from what you are saying is that the front-end cycles are roughly 2-4 weeks?

Dr. Ravi Gopinath: It depends on the capability set. Today if you look there is no front-end cycle because the entire project is done in one phase, but what Michael was saying where you can draw the line depends on the capability of the global location. So, as the global location capability gets higher and higher , that line in terms of defining "after this is back end and before this is front end" that line comes further and further ahead, but you would not get it further ahead than 2 weeks, because that is really involves high degree of proximity to the customer.

Ajay Nandanwar: Sure, and could you elaborate a bit on…..

Moderator: Mr. Nandanwar, sorry to interrupt you sir, can you please come for a followup?

Ajay Nandanwar: Yeah.

Moderator: Thank you very much sir. Participants are requested to kindly limit to one question in the initial round of the Q&A session. Next question comes from the line of Mr. Sunil Thirumalai with Credit Suisse.

Sunil Thirumalai: Hello sir.

Dr. Ravi Gopinath: Hi.

Sunil Thirumalai: Sir most of my questions have been answered, I just had two. One is regarding a statement in the release which said about a change in the accounting procedures, can you please elaborate on that?

Dr. Ravi Gopinath: Yeah, I will hand it over to our CFO.

G. Ravishankar: As I was mentioning in my previous answer, we have been following the marked-to-market system of recognizing the gains in the forward contracts that we enter into. So what happens in this, is the gains in the most probably contracts also gets recognized in every quarter. So what we would like to move into , is the international accounting practice, which is also proposed by the Accounting Standard 30 of the Institute of Chartered Accountants India , whereby the hedges will be classified as effective or ineffective, and effective hedges till the time that they come into the books , the gains from them will be classified in the balance sheet, and once the asset—the sale in this case gets into the P&L , the gain from them will flow into the P&L. So the effect of this will be of the smoothening the volatility that we would have by following the marked-to-market system.

Sunil Thirumalai: Okay, thank you sir. Just following up on the discussion regarding Modern. Am I missing something? Were these problems not visible at the time of the acquisition or is there something new that has come up which is forcing the offshoring to be delayed?

Dr. Ravi Gopinath: No, see the offshoring is not…., I don't think there was any expectation that we would be able to turn the switch and make offshoring happen. If you look at it , what we are dealing with is a two-fold problem. On one hand the problem that we are dealing with or the issue that we need to address together as a management team , is pretty much the same thing that any of our customers would have, and as a manufacturing customer whether they make cars or whatever it is , when they want to globalize engineering the internal challenges that they have in terms of you know what are the risk perceptions of doing a piece of work offshore, and clearly the risk perceptions are how do I control quality. This guy is not working next to me how do I know it will be done properly, how much of rework will I have to do, and these are concerns in the minds typically of our customer engineers. If you look at the relationship between a customer and a company like Modern, traditionally for example, you would find that none of these questions exist because there is a high degree of familiarity, a long history of working together, so none of this happens. But the drivers for our customer, Modern in this case, are equally severe, and the drivers are the fact that globalizing is an essential lever for profitability, so from a business and a management standpoint the imperatives are clear. But there are still concerns that people have at the people level and it is important for us that we address those comprehensively and take steps if necessary erring on the side of caution to start with that if we make that investment upfront then scaling up later on will be a lot easier. So, if we were to force something and people back away from the initiative, we don't want to create a situation where for us we don't have any assets beyond our people and that is the fundamental thing. Our customers have assets that they take to market and they work with. But our assets are our people and we have to be especially careful and cautious, which is why the trajectory that we are following was exactly the trajectory that we had put in place on the day that we closed the transaction and we are taking that to plan. What has been, I would say taking longer and which has not been that much in our control is the development of the new business. And there are two factors here. One, exposure and concentration of your customer base in Detroit and in that region comes with risk , because we are then subject to the same business cycles that our customers are subject to, and diversification out into new verticals taking the similar automotive proposition into other industrial verticals while it has certainly seen all the initial successes there is a time factor involved. So, for us we are sure of where this is going. It is according to plan. It is just that we wish that you know business will happen with a turn of a switch. Unfortunately there is a time factor involved, but I firmly believe that the management team and we are dong the right thing.

Sunil Thirumalai: Okay, thank you and all the best sir.

Moderator: Thank you very much sir. Next question comes from the line of Mr. Ashi Anand with ICICI Prudential PMS.

Ashi Anand: Sir, hi. I just have one question on Modern Engineering. You had mentioned taking offshoring from currently about 10 to about 35-40 and that are actually coming through top line growth. I wanted to understand where we see this top line growth coming in from? Because as you mentioned the new practices would actually take some time and assuming nothing much is happening on the auto or Detroit kind of a market, so where we are seeing this kind of traction of growth coming in which will drive our offshoring from Modern?

Dr. Ravi Gopinath: Just to give you sense of some of the areas where Modern has started to see the initial success in Q1 has been in the defense sector, the aerospace and the ground vehicle centric defense contractors, in the entertainment part business, in the marine business. So there are areas that are in a way linked with automotive sector, in the sense that they draw on the same competencies but completely new verticals. So the diversification strategy that we are following is essentially to say how can we leverage our experience base and our competency base to take it into new vertical industries, and these these are just examples of that, and the leadership is focused on driving growth in these areas. Michael, if you would like to add something else in terms of your diversification strategy, but that is essentially the key to the growth.

Michael McConnell: Right. And as Ravi mentioned what our key focus is on leveraging of course not only the same skill sets for a client in our technology, in our domain expertise, in the verticals that are very similar in nature, so when we look at defense , we are focused on defense ground vehicles where there is very close correlation to the same skill sets that relates in automotive. So, while it is a new industry the margins are much fatter because of the basis of the business and the ramp up time is much shorter because it is a very close correlation of our existing expertise. So that is a real focus for us in all of new industrial verticals we are going after, because the lead times are shorter to operational execution as well as greater margin opportunities.

Ashi Anand: Sir but in terms of the success and diversification when we are speaking of offshoring increasing from about 10 to 25, 35 to 40%. Are we seeing about a 30% revenue growth coming in Modern Engineering in the current year? Is that what one should be expecting, and is the bulk of this coming from these newer sectors?

Dr. Ravi Gopinath: Okay to answer your question. One is the work that Modern, I would say goes after and wins in the context of its historical relative business, okay. The other part that is happening there are a lot of engineering deals being bid out where the driver for the customers is essentially offshore engineering. So it is not just winning business in the US and saying now how do we offshore this, that is one part of it, and that is what Michael talked about in terms of diversification which was given in the top line. You need to remember that while Modern is a subsidiary company and we are closely tracking and reporting the numbers of Modern, the way we are managing it is as a consolidated engineering business and which includes our offshore operations here in India which has you know close to 250 people. So what we are also driving in terms of the top line growth is how are we starting to bid for and win deals that have very, very high offshore content to start with, and the numbers will be achieved fundamentally through that mix.

Ashi Anand: Okay, also sir you were speaking about 35 to 40% offshore mix. Are we looking at Modern breaking even and therefore what kind of margins as we enter Q4 of this year?

Dr. Ravi Gopinath: As I said, we are certainly looking at Modern turning around to profitability by the end of this year. At this point we will not be commenting on exactly what the margins will be there.

Ashi Anand: Okay, thank you so much and best of luck.

Moderator: Thank you very much sir. Participants are requested to kindly restrict to one question in the initial round. Next question comes from the line of Mr. Nandan with BNK Securities.

Nandan: Sir, I would like to know about the resources that we have in terms of offshore, number of people onsite, offsite. What is the breakup, and what kind of salary hikes are we giving?

Dr. Ravi Gopinath: Is that disconnected. Hello?

Nandan: Hello.

Dr. Ravi Gopinath: Yes sorry, could you repeat the question?

Nandan: Sir, what I was asking what is the number of people that we have offshore…, hello?

Dr. Ravi Gopinath: Yes can you hear us?

Nandan: Yes, I can hear you.

Dr. Ravi Gopinath: No, we did not hear your full question, could you repeat it please?

Nandan: Sir could you give us the number of people offshore, onsite, and offsite. And what is the plan for hiring? Are we going to ramp up more on the offshore or are we going to scale up in Romania?

Dr. Ravi Gopinath: So we had given the delivery location distribution in terms of how our revenue is distributed. I will just come back to you or we will send out the details in terms of the manpower number distribution by offshore, offsite, and onsite. In terms of the hiring plan, as I said the hiring plan is actually very closely linked with the revenue growth and how we are doing the sales and operations planning together. So if you look at the net additions that we have made in terms of the people, which was 77 net addition, it is directly correlated with the fact that the pipeline in the beginning of Q1 was developing slowly and the revenue was not there which has shown up in the results. But as we start building the pipeline we are certainly going to be looking at increasing our hiring, starting this quarter.

Nandan: Sir my question was have we frozen on a number that we would look at hiring for the year?

Dr. Ravi Gopinath: No we have not.

Nandan: Okay, my other question is regarding the forex hedge. For how much amount are we covered and for what duration and what rate?

G. Ravishankar: Yeah. Normally our policy is to cover systematically for about 12 months, so at the end of June 30th we have about $36 million of forward contracts and the average rate of this is around Rs. 45 to a dollar.

Nandan: Okay, thanks a lot sir.

Moderator: Thank you very much sir. Our next question comes from the line of Mr. Harish Krishnan with Kotak.

Harish Krishnan: Hi sir. Three specific questions if I may ask. One is on utilization levels, given the fact that you are going to increase the offshoring to a very significant level what kind of bench are you looking of by the second half?

Dr. Ravi Gopinath: Yeah, our utilization, as I said, if you see the presentation, with the trainees and excluding, trainees, excluding trainees it is 87.5%. We feel this is fine, okay. What we want to aim for is in the 84 to 85% range in terms of our target utilization. We will get there. A lot of what you are seeing right now is the fact that we were very conscious about rationalizing our bench in this quarter and we wanted to ensure that people on the bench were retrained depending on the kind of opportunities that we are seeing, a large part of that has been accomplished. So we will maintain bench which gives us utilization of around 84 to 85%.

Harish Krishnan: Okay. Second, any thoughts on how we are trying to repay the debt that we have taken on from Modern?

Dr. Ravi Gopinath: Yeah, if you see the debts are repayable from the first quarter of 2008-09. I think by that time our cash flow from the operations will be much better to start repaying those loans in time, which is how it has been planned to get repaid.

Harish Krishnan: Okay. You were also looking at some kind of sale and lease back of property in Pune, is that an option you are still looking it?

Dr. Ravi Gopinath: No we have not yet, we are not looking at that now.

Harish Krishnan: Okay, last question. I believe you have increased your stake to 100% of Modern from 95%, just wanted to check were there any clauses to hand over the extra 5% to you, was it on the basis of some fulfillment of clause or was it timed?

Dr. Ravi Gopinath: No, see there was a timing that had been recommended and it was a joint decision between the management at the time of the acquisition and we brought that forward by around 6 to 8 months because what we felt was that the completion of the acquisition of the remainder stake would hasten up the integration process.

Harish Krishnan: Okay, so any thoughts on what will now retain the Modern management because you have about 500 professionals or so over there, what kind of retention strategy is there for Modern management?

Dr. Ravi Gopinath: Retention strategy to the Modern management, so what we are doing is , see currently there has been just one change that has been effected at Modern, and as I said last time that there is a new CEO who is out on this call, there is a new Chief Operating Officer at Modern. Plus we are adding depth to the management team by making certain new hires. In terms of the retention mechanism what we are doing is, we are linking the management teams, the performance, the target very closely to an integrated plan which includes the total global content in the work that we are doing, as I said not just for Modern native business but for our consolidated engineering operation, so one of the big integrating drivers that we have put in place is ensuring that even the Bangalore engineering team, for example, it comes under the functional management of the focused Modern Engineering.

Harish Krishnan: Okay. Thanks a lot and all the best.

Dr. Ravi Gopinath: Yeah, thank you.

Moderator: Thank you very much sir. Participants who wish to ask questions may please press *1 now. Next we have Mr. Krishna Kumar from Sundaram.

Krishna Kumar: Hello sir, I just have a simple question. Do you still have the bottom line of 30% gross?

Dr. Ravi Gopinath: Yes, we are maintaining our guidance as of now.

Krishna Kumar: Thanks.

Moderator: Mr. Krishna Kumar.

Krishna Kumar: Yeah.

Moderator: Are you done with your question sir?

Krishna Kumar: Sure, sure.

Moderator: Thank you. Next in line we have Mr. Saurav from Kotak. Hello Mr. Saurav.

Saurav: Thanks, my questions have been answered.

Moderator: Thank you very much sir. Next question comes from the line of Mr. Suresh Guruprasad with Irevna Research.

Suresh Guruprasad: Hello, I have just one quick question. You were talking about increasing the target offshore for Modern to about 35 to 40% which will be linked directly to the absorption of work and increasing in the competency across your various centers. How is that going to impact your cost given that your onsite and offshore how will that be undermining your offshoring strategy?

Dr. Ravi Gopinath: No, I am not clear that I understand the question.

Suresh Guruprasad: You were talking about moving your offshore and increasing your offshore mix for Modern for about 35 to 40%.

Dr. Ravi Gopinath: Correct.

Suresh Guruprasad: Which will directly depend again on what will be your competency levels that you will have to ramp up offshore?

Dr. Ravi Gopinath: Yes.

Suresh Guruprasad: And also providing incentives to Modern employees to move here, so how will that actually impact your offshoring strategy because your cost will go up?

Dr. Ravi Gopinath: Okay good. We are not looking at creating a very large expat population. The people that are moving are sort of pioneers and they are not coming on a permanent basis, they are coming for medium term engagement. So they will, at any global location not just India, Romania, or China as Michael said earlier, it would vary between 3 months and 6 months as the case may be, because what they are doing is essentially starting the training, mentoring the initial execution of the project, and then letting the teams here in various global occasions take up the work and scale and run with it. That is not going to create any additional cost burden as far as we are concerned. Whatever minor cost increases are there in terms of travel and so on and so forth are obviously fully been planned for. In terms of the competency development at the offshore locations , as I said when we created our P&L plan for the year there was a planned investment in our practices and in our delivery process creation. That was part of the budget that we have created, and that very much included competency generation in our global centers necessary to facilitate offshoring in the engineering business.

Suresh Guruprasad: Okay sir, one last question. Since you are planning to increase and develop your competency level, does that involve some capex in terms of building more facilities?

Dr. Ravi Gopinath: The newer facility requirement will be on the back of the business, so we are not looking at facility expansion for competency generation. Today we are well covered in terms of the capacity that we have in our main operating locations in any part of the world, and as and when we need more capacity based on the projected growth in the business, we have actually lined up plans in terms of how we need to do that, so that is going to be linked to business growth more than competency development.

Suresh Guruprasad: Okay, thanks a lot sir, and all the best.

Moderator: Thank you very much sir. Next in line we have Mr. Neerav Dalal from Capital Market.

Neerav Dalal: Hello sir, I just wanted to know, it is a repeat question, the tax rate was down this quarter, I just wanted to have a clarification on that?

G. Ravishankar: As I was telling, most of the profits that we generated this quarter are from the units that are exempt under 10A and hence the tax provision for this quarter is lower, and also we had a reversal of provision which came from the earlier quarter deduction of about 2 million. So on an average; we would consider a 10% tax rate for this year as an appropriate tax rate.

Neerav Dalal: Thank you sir.

Moderator: Thank you very much sir. Next question comes from the line of Mr. Shekar Singh with Goldman Sachs.

Shekar Singh: Yes sir, I just wanted to know like what is the salary hike that you have given both to onsite and offshore locations. And, if you can give a breakup of the drop in margins which we have witnessed this quarter in terms of what was the impact because of rupee dollar and what was the impact because of salary?

Dr. Ravi Gopinath: Overall, if you see across the company, our average salary hike is 14.5% to 14.7% on a blended basis. In terms of the impact on the bottom line the rupee appreciation impacted our bottom line by 2.5% to 3%, salary hikes by 4% to 4.5%. This was offset to a certain extent by the offshore productivity increases, which offset it by around 1.5%.

Shekar Singh: Sir what will be your onsite salary increases that you have made?

Dr. Ravi Gopinath: We are tracking and reporting the salary increase on a consolidated basis, and that is 14.5%.

Shekar Singh: Okay sir, thanks a lot.

Moderator: Thank you very much sir. Next question comes from the line of Mr. Sanketh with IL&FS InvestSmart.

Sanketh: Yeah, I have actually logged in late, so hence a repeat question. Can you kindly repeat your guidance. I just got that your top line is in dollars and bottom line in you have given the guidance in rupee, so can you kindly repeat it?

Dr. Ravi Gopinath: Yeah, the guidance that we issued for the year in the previous quarter's call was 50% growth in top line in dollar terms and 30 to 35% growth in bottom line in rupee terms.

Sanketh: Alright, so that guidance continues?

Dr. Ravi Gopinath: Yes.

Sanketh: Alright, thank you so much.

Moderator: Thank you very much sir. Participants who wish to ask questions may please press *1 now. Next in line we have a follow up question from Mr. Ruchit Mehta of HSBC.

Ruchit Mehta: Good evening sir. Just a bit of a clarification of the bottom line guidance. Does it also include a significant portion of other income that may help in terms of achieving that guidance?

G. Ravishankar: Yes, this is at the net income level. Our guidance of 30 to 35% is at the net income level.

Ruchit Mehta: So does that mean that even if you get bit of efficiency improvements and you know margin expansion, EBITDA per se may actually be flat on a year-on-year basis even if you have that 50 odd percent?

G. Ravishankar: Yeah, so in line about this thing we do not want to go into the individual items. So as per our guidance the profit after tax will grow by about 30 to 35%.

Ruchit Mehta: Okay, and in terms of any capex transfer this year, if you can share that please?

G. Ravishankar: Yeah, actually it is mentioned in the last quarter call, our capex for this year is around Rs. 50 crores or Rs. 500 million.

Ruchit Mehta: Okay, that is great. And just one final thing on this revenue degrowth. I am a little confused that there was no loss of business. It is just an effect of change in business strategies to go direct and also the offering and the rupee dollar, apart from that there was no real loss of business per se.

Dr. Ravi Gopinath: That is correct.

Ruchit Mehta: Okay. Thanks a lot.

Dr. Ravi Gopinath: Okay. We actually had a hard stop at 6.00, but we can do one more question if it is there.

Moderator: Sure Sir. We take a last follow up which comes from the line of Mr. Sandeep Shah with ICICI Securities.

Dr. Ravi Gopinath: Hi, Sandeep.

Sandeep Shah: Yeah Sir, just the last question. Sir, on the Modern front the revenue growth from the next quarter onwards, do you believe that now we have a visibility or a order book where the revenues in the Modern is likely to increase on a quarter-on-quarter basis because it has not performed in line with the expectation for the last two quarters?

Dr. Ravi Gopinath: Yeah, see as I said I would look at all the entire growth story in terms of, and I just want to repeat and emphasize that I have been very consistent in my articulation on this, whether it is in our analyst conference calls or individual meetings that I have had, that we are going to start measuring the outcome of all of these steps that we have taken in terms of our new strategy, whether it is a top line growth or bottom line improvement and sending the right direction, all of those measurements will start in the second half of this year.

Sandeep Shah: Okay and what percentage of our revenue from the Modern is Detroit based and what would you like to have it as a percentage of revenue from the Detroit going forward where you believe now even a slow down will not affect us in terms of growth significantly?

Michael McConnell: Currently, the Detroit revenue net is about 65% of Modern USA revenue mix, and we are looking to get that to about a 40% number over the next year and then fully decrease that down without losing the resources. So the key is that it is available and is currently troubled with some small growth through the opportunities arise, but that fully de-risked over the next couple of years.

Sandeep Shah: Okay, and sir last question. We are not now talking about the product, which might be performing in the quarters like second half, So, what is the strategy there because the enterprise products is likely to be, we can see could be a star product going forward, but the products are not growing and we are not talking about even on the enterprise products.

Dr. Ravi Gopinath: We certainly reported what happened to the product, and we have got a very clear strategy plan as far as products are concerned. We are looking at out products as a very integral part of our core business and it is a big part of our strategy and here is how. We are looking at our products in two parts. One is if you see the enterprise products. It is not just about the product play or the license revenue from the enterprise products, we view the enterprise products as a very strong enabler to our pitch as a PLM system integrator. So, to be an effective PLM system integrator we have to have the ability to support the customer across multiple platforms and drive integration across multiple platforms, and whether it is CAD PDM, PDM ERP, PLM manufacturing so on and so forth, and the enterprise products which is essentially about interoperability, which is now becoming a very important differentiator to our PLM system integration story. In fact at least two or three of the deals that we have secured as a result of our 'go-to-market' initiative, while they have not resulted in direct immediate revenues in terms of licenses for enterprise products, the enablement that the enterprise products surely provided was clearly there in our ability to win those deals. As far as the desktop products and technologies are concerned, just like enterprise with an enabler to the PLM business, the desktop products and technologies we believe , will be a significant enabler and differentiator for our global engineering business because each one of those products are centered around engineering and manufacturing productivity and there are two ways in which we will take this to market. One is directly address productivity needs of our engineering customers and second thing is if they can start to provide a greater layer of differentiation to the engineering services we provide currently as I said through Modern then that becomes a very important tool. So for me when I count product revenues while we are reporting revenues as you know decline in license revenues here, I am also significantly recognizing that the enabling factor is extremely high. So, product will continue to be a core element of our strategy going forward.

Sandeep Shah: But Sir does that mean that the enterprise product demand has not been as high as we had earlier envisaged?

Dr. Ravi Gopinath: I am not sure what the expectations you are working with, but I will make a point here and I will also request Manu who is on the call to point out his views here. But I think that the relevance of the enterprise product story has never been more than today. What we have seen is the initial articulation of the enterprise product as an integration between diverse CAD and PDM platform was an important part of how we started that pitch, No. 1. No. 2, what is happening is that the PLM world is expanding. It is expanding beyond traditional CAD PDM into integration with supply chain processes, manufacturing processes and there is whole range of expansion that is happening. The PLM world is rapidly expanding. We believe that the relevance is extremely high. Now how we go and convert this into license revenues for the enterprise products business is how we start taking the solution story forward, and we have already started doing that. We can talk off line and separately in terms of the specific aspect of this, but clearly we are bullish about it which is why we also invested in acquiring IPR to strengthen the product technology proposition. Manu.

Manu Parpia: Yeah, add to that I just want to mention that you know when we did enterprise products, when we started enterprise products, we always were aware we start a product line there is no it is not something that you can say guaranteed success, and we always looked at 2008 as being the kind of year in which enterprise products if we could find the right mix. Now we got the early traction in certain things and then there were some set backs because of certain changes in the customers' plans, but overall as Ravi mentioned we are very clear that this forms a very integral part of our way forward and the acquisition of MeritSpringTechnology is the key element of building the interoperability product portfolio , while especially keeping in mind that as time goes by the services are reentered architecture which in a kind of forthcoming plan or let us say a forthcoming platform will become very prevalent. So, we are pretty clear that the enterprise products will help us lead the way both in terms of getting some license revenues and attracting customers and leading to consequential revenues and services.

Sandeep Shah: Yeah, and just a last question, change in the accounting policy from marked to market to cash flow regime, this has happened from first quarter or will that happen from the second quarter?

G. Ravishankar: We are saying that we will be doing it in the second quarter.

Sandeep Shah: Okay.

G. Ravishankar: As per the hedge accounting policy, we need to have this documentation in place and so whatever contracts we enter in future that alone would qualify for this kind of an accounting policy.

Sandeep Shah: Okay.

Dr. Ravi Gopinath: I am sorry. I do not mean to be rude but we had many last questions, so right now we are getting late for a customer call.

Sandeep Shah: No, we understand Sir.

Dr. Ravi Gopinath: And if we do not do that then top line again will be an issue.

Sandeep Shah: No, no, we have to do that first. Thanks and all the best.

Dr. Ravi Gopinath: Thank you so much.

Moderator; Thank you very much sir. At this moment I would like to hand over the floor back to Mr. Kunal Sangoi for final remark.

Kunal Sangoi: Thank you all for participating in the call. I would like to thank the entire Geometric management for giving us the opportunity to host this call. With that I will hand over the call to Dr. Ravi for his final remarks.

Dr. Ravi Gopinath: Okay. Well thank you for joining us. As I said we have understood the tenor of the questions. We understand that it is important to focus on the fundamentals, but as we close this call I just want to assure all of you that we are keeping our sights well trained on our 2010 strategy. We clearly know what it takes to get there. It is not our intent or desire to back load the achievement of that plan in year three. We are very focused on ensuring that the building block process completes in the first half of this year. We are pushing hard into the market and as I said we will start measuring the results from the second half of the year. Q2 as I have consistently maintained will probably continue to show some softness, but that is part of the investment that we are making into creating a much more solid future. So, thank you for your patience. Thank you for joining us in this call and look forward to talking to you again next quarter if not sooner.

Moderator: Ladies and gentlemen, thank you for choosing Webex conferencing service. That concludes this conference call. Thank you for your participation. You may now disconnect your lines. Thank you.