“Datamatics Global Services Limited

Q1 FY '25 Earnings Conference Call”

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MODERATOR:	**MR. PRATIK JAGTAP – E&Y INVESTOR RELATIONS**

Moderator: Ladies and gentlemen, good day, and welcome to Datamatics Global Services Limited Q1 FY '25 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing the star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Pratik Jagtap from E&Y Investor Relations. Thank you, and over to you, sir.

Pratik Jagtap: Thank you, Steve. Good evening to all the participants in the call today. Welcome to the Q1 FY '25 Earnings Call of Datamatics Global Services Limited. The results and presentation have been already mailed to you, and it is also available on the website of Datamatics. In case anyone has not received a copy of this release and presentation please do write us and we will be happy to send you all.

To take us through the results today and to answer your questions, we have with us the top management of company represented by Rahul Kanodia, Vice Chairman and CEO; Sandeep Mantri, EVP and Chief Financial Officer; and Mitul Mehta, EVP and Chief Marketing Officer. Rahul will start the call with brief overview of the quarter on business, which will be then followed by Sandeep talking on financials, and then we will open the floor for Q&A session.

I would like to remind you that anything that is said on this call, which gives any outlook for the future or which can be construed as forward-looking statements, must be viewed in conjunction with the risks and uncertainties that we face. These risks and uncertainties are included, but not limited to what we have mentioned in the prospectus filed with SEBI and subsequent Annual Reports, which you can find on our website.

With that said, I now hand over the call to Rahul sir. Over to you, sir.

Rahul Kanodia: Thanks, Pratik, and a very warm welcome, and thank you, everyone, for joining our earnings call for Q1 FY '25 today. I will briefly discuss some of the key quarterly highlights, while Sandeep, will provide an update on the financials. After that, we will open the floor for Q&A sessions.

Our total revenue for Q1 stood at INR 394 crores and an EBIT of INR 42.6 crores, including revenues from Dextara. Our revenue grew at 0.7% in Q1. Dextara contributed to 3.1%, hence, our organic growth was the negative 2.4% on a year-on-year basis. The degrowth was mainly due to the slowness in the U.S. and European market and a flat growth in our existing business. Consequently, our EBIT margin reduced to 10.8%, which included the increments that we gave out for the year 2024-25 rolled out in Q1, and our ongoing investments in building AI solutions.

On sequential quarter basis, we see an improvement in EBIT for Digital Experiences, which grew from 11.8% in Q4 to 14.2% in Q1, an improvement in EBIT for Digital Technologies, which from 0.7% in Q4 to 4.6% in Q1. However, there was a shrinkage in EBIT for Digital Operations from 23.5% in Q4 to 15.5% in Q1. This is not comparable on a sequential basis due to the cyclical nature of this business. Although, our financial performance has been somewhat softer than expected our confidence in the overall business strategy is steadfast, we remain fully committed to this path.

Our business continues to progress according to plan. Datamatics is expanding its delivery centers in Philippines. We recently opened a delivery center in Dumaguete and we are opening another delivery center in Cebu in Q2.

In our products business, we integrated Generative AI technologies in TruBot, TruCap+ and TruBI and have rolled these features out to all existing customers. Furthermore, these products were listed on the Microsoft Marketplace in Q3, and we have sold over $1 million of licenses on this platform.

Regarding our recent acquisition of Dextara, a Summit level partner for implementing Salesforce, I would like to inform you that the integration is progressing well, and the teams are collaborating actively on new opportunities. We have submitted 10 new proposals in Q1.

This quarter, we expanded our client portfolio by adding 9 new customers, including a Fortune 500 company. Transport & Logistics is a focused vertical for Datamatics across all our lines of businesses. We have 15-plus customers in this segment. In Q1, we added another US Logistics customer to this list. We have aligned our organization structure and processes for higher growth going forward.

As I mentioned on the last call, we are excited about the opportunities that artificial intelligence presents. Recently, we became one of the first digital technology companies worldwide to receive an ISO 42001:2023 Certification for AI Management Systems. This achievement will help our customers manage the risks and opportunities associated with AI, balancing innovation with governance. We have recently received a patent for AI in TruCap+. This further solidifies its position as a leading intelligent document processing solution. Microsoft, along with OpenAI, is leading the charter in the AI in the enterprises today. Along with Microsoft, we are co-creating and reimagining applications using the power of AI. One notable development is a partner onboarding Copilot developed at Datamatics, which is amongst the top three Copilots featured at Microsoft Build Annual Developer Conference in Seattle, Washington. Additionally, Microsoft recognized Datamatics as 'AI First Mover' in the recent publication highlighting the recognition of our AI solutions are receiving from the industry.

I am excited to announce the groundbreaking AI initiative that our team has successfully secured with a leading American supermarket chain. This project entails the implementation of advanced AI-driven video monitoring and analytics technology across 250 locations, aimed at enhancing customer experience while simultaneously mitigating instances of fraud. To date, Datamatics has delivered over 40 AI projects across various verticals.

Looking ahead, we are positive about regaining our momentum with anticipated improvements in both revenue growth and profit margins. Regarding our EBIT margins, through diligent cost management and operational efficiencies, we project an EBIT improvement of 150 to 200 basis points in Q2.

Before handing over the call to our CFO, Sandeep Mantri, I would like to express my heartfelt gratitude to Sandeep Mantri, on his last earnings call with us. His dedication, leadership and financial acumen have been instrumental in guiding our company in achieving significant milestones. Sandeep your contributions have laid a solid foundation for our future success, and we are deeply grateful for your commitment and hard work. On behalf of the entire Datamatics team, I wish you all the best in your future endeavours and look forward to your continued success. Thank you for everything. Sandeep, over to you.

Sandeep Mantri: Thank you, Rahul, for the kind word. Welcome, everyone, and thank you for joining us in Q1 FY '25 earnings call. Let me start with the financial performance for the Q1 FY '25. Our revenue for this quarter stood at INR 394 crores, which is a drop of 4.5% on a sequential basis and a marginal of 0.7% on a Y-o-Y basis. Our EBITDA for this quarter was at 13%, compared to 17.3% in Q1 of last year. So there is a significant drop in EBITDA. Our EBIT for this quarter was at 10.8%, compared to 15% in Q1 of last year. As explained by Rahul, the reason for drop in operational profit is primarily due to slow revenue growth, increment for 24-25 effected in Q1 and our continued investment in AI project. Our tax rate for the quarter is 17.2%, compared to 18.7% in Q1 of last year. Our EPS for the quarter was INR 7.37 per share, compared to 8.90 in Q4 and 9.35 in last year Q1.

When we see segment-wise revenue performance, our Digital Operation revenue was at INR 164.8 crores, which is a drop of 1.3% on a Y-o-Y basis. Digital Operation EBIT margin was at 15.5%, total contribution in revenue was 42%. Our Digital Experience revenue was at INR 67.9 crores, which is a growth of 2.4% on Y-o-Y basis. The EBIT margin was at 14.2%, and its contribution to total revenue was 17%. Our Digital Technologies revenue was at INR 161.3 crores, which is a growth of 2.2% on Y-o-Y basis. EBIT margin for Digital Technologies stood at 4.6% and the contribution of Digital Technologies to total revenue was 41%.

We continue to maintain a healthy balance sheet. As on June 30, 2024, our total cash and investments stood at INR 589 crores, and our DSO as of the end of this quarter was at 61 days. In terms of geographical footprint, U.S. remains our largest geography with 54% of our business coming from U.S., followed by U.K. and Europe at 13% and the Rest of World, including India, is at 33%.

In terms of industry footprint, technology and consulting remains the largest segment for us, which constitutes 27% of our revenue, followed by BFSI, which stood at 25%, then education and publishing and manufacturing, infra and logistics, each at 12%, then non-profit or non-government organization at 10%, retail at 9% of our business, other and retail is 5% of our total revenue. Our client concentration remains very healthy with top 5, 10 and 20 clients contributing to 23%, 37% and 50%, respectively.

As this is my last earnings call with Datamatics, I want to take a moment to express my gratitude. It has been an honor to serve you as your CFO and to work alongside such a talented and dedicated team. I want to thank our employees for their unwavering commitment, our investors for their trust and support and the entire leadership team for their collaboration and guidance. Together, we have achieved many significant milestones.

I am confident that Datamatics well positioned for continued success, and I look forward to seeing the company's future accomplishment. Special thanks to Rahul for always believing in me and trusting me, and thank you all for the incredible journey.

With this, I will now pass on the call to operator to open the floor for questions. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Grishma Shah from Envision Capital. Please go ahead.

Grishma Shah: Good evening to the management team and I just wanted to understand the softness in growth a little better. I mean, as evident, you can see some pain in the top 5 and the top 10 accounts. So, if you could tell us how is the trajectory is going to be for the rest of the year with the key accounts? And where is the growth going to come from and what's the guidance for the entire year?

Rahul Kanodia: Sure. So on the Digital Operations side, there was some delay and shrinkage in the volume. We expect some of the volume to come back in Q2 and Q3 of this year. On the technology side, certain projects got a little bit pushed out. And again, we expect that to happen in Q3. So overall, from a growth point of view, in the last earnings call, we talked about 4% organic growth and another 3% to 4% from inorganic. And we, at this point, maintain that projection. So I think we should be in that range once we grow back some of the volumes and some of the default projects kick in.

Grishma Shah: Okay. Yes. I get that. How has Dextara grown for this quarter year-on-year basis? And what's the outlook for Dextara?

Rahul Kanodia: Dextara is flat. Dextara this quarter has not grown. But that does not concern me because we had a call for Dextara specifically when we acquired them. So they, as a company, were bidding for smaller deals, ranging between $50,000 to $100,000, and the deals that Datamatics was getting in the range between $0.5 million to up to $3 million per deal. So, our strategy behind that was with their competence and expertise, we will convert a few of the larger deals that we are getting, and that will give the upside in terms of growth. Now in quarter one, it's very difficult to close it so fast, I mean that's too short a period. So they have been working very closely with our team. And as I mentioned, we've submitted 10 proposals in Q1 of this year. So I'm actually very positive about their ability to close a few one or two large deals, and that will get the growth going for Dextara.

Grishma Shah: You called the small deal growth with Dextara was traditionally doing.

Rahul Kanodia: No. We've not paused it. But yes, quarter one is a little soft. So they have been working on several deals. So we've not paused these small deals, but the upstream will come inside one of the large deals, and we have that pipeline from Datamatics.

Grishma Shah: Okay. And have you disclosed the total pipeline this quarter? What does it stand at?

Rahul Kanodia: Our pipeline last quarter was about $200 million. We've seen the softness. So that's come down to about $170-ish million.

Grishma Shah: Okay. And how much of the increment that we've rolled out in quarter one will continue in quarter two and ongoing investments? Can you give me some margin outlook for the entire year?

Rahul Kanodia: Yes. The increments that we gave on an average was roughly about 9%-9.5%. And obviously, when you give that increment, it's stays through the whole year, it goes up and down a little bit depending on churn. Some people leave, some new people come, but roughly 9.5% will stay through the whole year. But all IT services companies go through those motions when they tighten the belt, they join some staff and then it is sort of cut back to normal.

Grishma Shah: Sure. Yes. And overall, I mean, if Q2 is going to see the margin recovery, do you see the trend of recovery continuing to the subsequent quarters? Or what's the sense?

Rahul Kanodia: Yes. The subsequent quarter should see the trend continuing. The reason is that, as I mentioned, some of the volume that came down in Digital Operations will kick in, in Q2 and Q3, and also some of the projects in the IT, which we have pushed out because of it. So they will kick in. And the moment you get the revenue is coming in, the margin by default improve because the cost structure has not moved. Q4 for us always tends to spike a little bit. So Q4 will always be healthier than the other three quarters. So quarter two, three and four should be better than quarter one.

Grishma Shah: Okay. And there is an exceptional item of INR 3 crores in the P&L.

Rahul Kanodia: Yes, it's correct.

Sandeep Mantri: So that is the amount we paid towards acquisition of Dextara to the adviser who helped us in getting this deal.

Grishma Shah: Okay. So that is the exception and not sitting in the operational costs.

Sandeep Mantri: That is not operational.

Rahul Kanodia: Yes. That is a one-time cost.

Grishma Shah: Okay. Fine. Thank you and good luck.

Sandeep Mantri: Thank you.

Rahul Kanodia: Thank you.

Moderator: Thank you. The next question is from the line of Nikhil from Kizuna Capital. Please go ahead.

Nikhil: Yes, sir. Thank you for giving me the opportunity. I just wanted to ask, the organic degrowth that we had, can you quantify them in terms of softness in demand, incremental -- increments and investment in AI?

Sandeep Mantri: Increment will be having about 9%, 9.5%, which means about 4%, 4.5%, increment is one of the major reasons. And coupled with the sluggish revenue growth, both have actually brought down the EBITDA or EBIT.

Sandeep Mantri: Even with 6%, 7% revenue growth, we would have better in terms of EBIT or EBITDA.

Nikhil: Okay, sir. And sir, any earnouts figure during this Dextara acquisition, there was a performance-based payout that was going to be triggered.

Sandeep Mantri: That will happen at the end of the year. First payment will be at the end of the year and second payment will be after 31st March '26. So this is a 2-year deal post acqusition.

Nikhil: Okay, sir. And then in terms of pipeline of $170 million. So sir, can you bifurcate them into the verticals, like how much in the ASP, how much in the product side? And in which vertical like BFSI manufacturing?

Sandeep Mantri: We don't give segment-wise bifurcation of pipeline. In fact, we started giving pipeline last to last quarter only. Right now, we are not giving segment wise -- that is because many of the deals are combined deals. So it is very difficult to figure out particular segments in hybrid deals. We are seeing more and more hybrid deals.

Nikhil: Okay, sir. That's from my side. Thank you, sir.

Moderator: Thank you. The next question is from the line of Ankur, an Individual Investor. Please go ahead.

Ankur: So my question is that the personnel cost phenomena is not a new phenomena. It will be there in every quarter. It would be there. So if we are targeting the revenue growth, what are the new verticals and markets we are scouting for?

And the second question which I just want to understand is, the AI and technology is quite a thing which is dependent upon R&D. And there has been huge inflow in different R&D organization across the world. So how we are keeping pace to be ahead of all these technological advancements? So these are the three questions that I have right now.

Rahul Kanodia: So to your first question. Yes, that is not a new phenomena. However, the growth particularly was sluggish. And when you have growth, it absorbs the increase in costs very easily. Unfortunately, because we didn't have the growth in Q1 of this year, the cost absorption was not at the same level. I am confident that as we go through the quarters, the growth will come in, and we should be able to absorb the cost. Having said that, we've already tightened our belt, and we are already seeing results of that tightening of the belt in the first month of Q2, which is July.

To your point about AI and how we are keeping abreast. We are very plugged in with the R&D team that we have. We have a whole team on the data labs that does a lot of R&D in the space. We are working very closely with Microsoft and with Google, and we are actually building cutting-edge technology, basis which, Microsoft has covered us in their coffee table book as an early adoper of AI. Also, it showcased Datamatics in their head office in Seattle, Washington, as one of the three companies globally from an AI point of view. We also got the ISO certification for AI.

So all of these things that we are doing, and also I talked about a very interesting project around video analytics that we got, which is a project that we signed up and we will roll it out to about

250 locations. So this is all, I think, testimony to the kind of work we've done on AI. And the R&D team, I must say has done some very cutting-edge stuff. So we will start seeing the benefits of all of this that we've done in the coming quarters.

Ankur: Thank you, Rahul, for this. And I extend my warm wishes to Sandeep also for his new entry where we have seen the company from life. I've been tracking it from last one and a half year and yeah, it's been phenomenal to see good leaders in the industry. Thank you, thank you both.

Rahul Kanodia: Thank you.

Moderator: Thank you. The next question is from the line of Nikhil from Kizuna Capital. Please go ahead.

Nikhil: Sir, I just wanted to ask you about the AFC pipeline, like how are you approaching the AFC deals? Like those are the large deals that we dealt with last time.

Rahul Kanodia: Yes. So on AFC, we have just kicked off Mumbai Metro Line 2B. It was delayed for a variety of reasons with COVID and all that type of stuff, but that we just kicked it off. We are currently in a bid for another large Metro in India, and we are awaiting the results for it. I am confident that within the next one month, we will get the results for sure.

We are looking at some other lines that are coming in, Mumbai -Line 4, 5, 6, and 9. So as we go through the motions, we will give an update on that as well. Plus in addition to that, we are pivoting a little bit more into the U.S. So our sales team has now started focusing very actively on the U.S. market in this space.

Nikhil: Thank you, sir.

Rahul Kanodia: Thank you.

Moderator: Thank you. The next question is from the line of Pallavi Deshpande from Sameeksha. Please go ahead.

Pallavi Deshpande: You mentioned about Mumbai Line 9, 4, 5 and 6, when does that come up? And in terms of the U.S. that you're positing into it's just the first time we will be looking for contracts on this end?

Rahul Kanodia: In the U.S., we have done Memphis as a project. We have done a small project with San Diego. But now we've got a sales team in the U.S. that is looking at many other opportunities in the U.S. So we've done U.S. projects before, and I'm very confident we'll be able to deliver on those.

As far as Line 9, 4, 5 and 6 are concerned, the tenders have been processed. We will now be working on the tenders, and we will probably submit some of them in the next couple of quarters. So really, you're talking about Q3 where we start seeing some results which was materialized.

Pallavi Deshpande: And the profitability for this India versus the U.S. How will they be different?

Rahul Kanodia: Yes. So that is a concern. India is a far more of price-sensitive market and profitability is lower. And that's the reason why we are focusing more in the U.S. We've also hired a global head of sales in the U.S. We're looking at the AFC business in the U.S. as well. So increasingly, we are focusing more on the Western market. Europe is right now a little sluggish, because because of the Ukraine war, the inflation and things like that, there is a problem in Europe, but the U.S. is still looking good.

In the U.S, currently there is some degree of uncertainty because of the elections coming up. We don't know which way it's going to go. But outside of that, the economy seems to be quite alright. There is slowness, which we see more in terms of decisions being deferred and projects getting delayed. But on a little longer-term six months to one year, 1.5 years, I don't see too much of a trouble with the U.S. market.

Pallavi Deshpande: And sir, lastly, any other plans on the acquisition on the board on acquisition side?

Rahul Kanodia: So we are in dialogue with some companies, nothing that is at the serious level that I would like to announce right now. But as those mature, we will certainly go through the motions of having a board approval, informing SEBI and things like that. So yeah, we are in dialogue with some companies, but nothing right now that needs to be announced.

Pallavi Deshpande: Right sir. Thank you so much.

Rahul Kanodia: Thank you.

Moderator: Thank you. The next question is from the line of Nikhil from Kizuna Capital. Please go ahead.

Nikhil: Sir our next margin lever that is going to grow the bottom-line, is going to be the revenue growth, right, sir?

Sandeep Mantri: Not only revenue growth, we are tightening our belt also. So that also will give some sort of margin improvement.

Rahul Kanodia: Some cost control and revenue, it's a combination of both.

Sandeep Mantri: It’s a combination.

Nikhil: So sir, if you want to guide, what will be the exit margin for FY 2025?

Sandeep Mantri: For the full year?

Nikhil: Yes, sir.

Sandeep Mantri: Right now, we are guiding only Q2 for margin, which will be about 150 to 200 basis points.

Rahul Kanodia: So, if you look at the current one, we have talked about 10.8% at an EBIT level. We improved 200 basis points you're talking about 12.5% to 12.8%. So, I think we'll maintain a 12% to 13% range for the full year.

Nikhil: Thank you, sir.

Moderator: Thank you. As there are no further questions from the participants, I would now like to hand the conference over to the management, for their closing comments.

Rahul Kanodia: Thank you, everyone, for being on the call today. It is a pleasure talking to you. And I look forward to speaking to you again at the end of Q2. I'm sure we should be back with the growth momentum. Thank you once again for being on the call.

Moderator: On behalf of Datamatics Global Services Limited, that concludes this conference. Thank you for joining us. And you may now disconnect your lines. Thank you.

Note: This transcript has been edited for readability and does not purport to be a verbatim record of the proceedings