DATAMATICS

"Datamatics Global Services Limited
Q2 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 Q2 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 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, Tanmaya. Good evening to all the participants in the call today. Welcome to the Q2 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 press 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, Mitul Mehta, EVP, and Chief Marketing Officer. Rahul will start the call with brief overview of the quarter on business, then 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 wishing everyone a very happy Diwali. Thank you all for joining our Q2 FY '25 earnings call. I will briefly discuss some of the key quarterly and half-yearly highlights followed by updates on the financials. After which, we will open the floor for Q&A discussions.

Our total revenues for Q2 stood at INR 406.8 crores, giving us a revenue growth of 8% on a year-on-year basis. Our EBIT for Q2 stood at INR 39.3 crores and our EBIT margin was 9.7%. Our total revenues for H1 stood at INR 800.7 crores, giving us a revenue growth of 4.3% on a year-on-year basis. Our EBIT for H1 stood at INR 81.9 crores, and our EBIT margin was 10.2%. Our revenue growth has been primarily driven by new client acquisition across all 3 business verticals, which is Digital Technologies, Digital Operations and Digital Experiences. However, we faced margin compression during the quarter due to lower volumes of tax processing business.

This quarter, we continued our investments in FINATO and AI solutions. Google has recognized us as a strategic partner for back office of the future. We have also partnered with Microsoft and developed our own copilot solutions focusing on process automation to accelerate business transformation for organizations. We continue to augment our sales and marketing efforts by hiring in USA and Europe and participating in industry events and conferences.

Our business continues to progress according to plan. This quarter, we expanded a client portfolio by adding 12 new customers. And regarding our recent acquisition of Dextara, I would like to inform you that the integration is in progress and is progressing well, and the teams are collaborating actively on new opportunities. We have already seen 2 wins for Salesforce-related services in Q2.

The transport and logistics businesses continue to be a key focus for Datamatics across all our lines of businesses. We have 15 customers in this segment. In Q2, we added a global logistics leader handling cargo movement in across 180 countries as a customer. For this customer, we will implement FINATO for finance transformation in over 50 countries.

We have been strengthening our leadership team by bringing in senior management talent and have augmented our Board with the introduction of Dr. Avnish Kshatriya, Kanika Mittal, and Himanshu Verma. We extend a very warm welcome to them as part of the Datamatics family and are confident that their extensive industry expertise will contribute significantly to our continued success. As you may know, our former CFO, Sandeep Mantri, left the organization last quarter. I'm pleased to introduce our new CFO, Ankush Akar. We warmly welcome Ankush to Datamatics and to our investor calls. Ankush, would you like to say something?

Ankush Akar: Hello, everyone. I'm excited about this new opportunity and looking forward to talking to you next quarter.

Rahul Kanodia: Thanks, Ankush. Since Ankush has recently joined, I will be presenting our financial performance for this quarter, and Ankush will address you starting next quarter. Let me start with the financial performance for Q2 FY '25. Our Q 2 FY '25 revenue stood at INR 406.8 crores, up by 3.2% on a quarter-on-quarter basis and 8% on a year-on-year basis. Our EBITDA for the quarter was at INR 48.8 crores, which is down by 5.1% on a quarter-on-quarter basis, and our EBITDA margin for the quarter was at 12%. Our EBIT for the quarter was at INR 39.3 crores, which is down by 7.7% on a quarter-on-quarter basis, and our EBIT margin stood at 9.7%. Our quarterly PAT after NCI was at INR 42.4 crores, which is down by 2.6% on a quarter-on-quarter basis. The PAT margin stood at 10.1%. Our tax rate for the quarter was at 19.9% compared to 16.4% in the last year same quarter. The primary reason for the increase in the profit mix of the various geographical entities that we have. Our EPS for the quarter was at INR 7.18 per share as compared to INR 7.37 per share in the last quarter.

When we see segment-wise revenue performance, our Digital Technologies revenue was at INR 162.2 crores, a growth of 0.5% on a quarter-on-quarter basis and 5.5% on a year-on-year basis. Its EBIT margin was at 4.2%, and its contribution to the total revenue was 40%. Our Digital Operations revenue was at INR 176.6 crores, a growth of 7.1% on a quarter-on-quarter basis and 7.3% on a year-on-year basis. The Digital Operations EBIT margin stood at 12.5%. It contributes to a total revenue of 43%. Our Digital Experiences revenue was at INR 68 crores, a growth of 0.2% on a quarter-on-quarter basis and 16.2% on a year-on-year basis. The EBIT margin stood at 15.2%. Its contribution to the total revenue was 17%.

We continue to maintain a healthy balance sheet. As on September 30, 2024, our net cash and investments stood at INR 615 crores. Our DSO was at 58 days as of September '24 as compared to 61 days as of June 2024. In terms of geographical footprint, the U.S. remains our largest geography with 56% of our business coming from here, followed by India at 22% and rest of the world, including U.K. and Europe at 22%.

In terms of industry footprint: Technology & Consulting was the largest segment for us, which constitutes 27% of our revenues; followed by BFSI, which stood at 23%; followed by Education & Publishing, which was at 15%; Manufacturing, Infrastructure, & Logistics, collectively all stood at 13%; and nonprofit or government organizations at 10%; Retail at 8% of our business And the rest of all the other segments were 4%. Our client concentration remains very healthy with the top 5, top 10 and top 20 contributing 21%, 36% and 51%, respectively.

With this, I will now pass on the call to the operator to open the floor for questions. Thank you all for your patience and continued interest in Datamatics.

Moderator: The first question is from the line of Grishma Shah from Envision Capital.

Grishma Shah: Happy New Year to the management team. I am keen to understand 2 things: One, what is the outlook going ahead now that we've crossed the first half? How is the integration with the last acquisition that we did in quarter 4 how is that acquisition panning out? And why is the Digital Technologies EBIT margins at 4.2%? I mean that seems to be quite too low. And even in Digital Operations, we've not seen these kind of EBIT margins before.

Rahul Kanodia: So to take your question Grishma. The integration with Dextara is going well. It is very smooth, as I mentioned in my address that we've already closed 2 deals. We are chasing a few more deals, which is a whole cross-sell initiative that we've taken. So, so far, so good. The sales cycle, as you know, in this business is about 9 months. So I didn't expect anything substantial happening in the first 2 quarters. But from an integration point of view, both the teams are working very well together.

To your question on Digital Technologies' margins, as we've mentioned in the past, we continue to invest in the AI space. That's one reason, and that is significant in terms of investments. The second is that we have a large portion, which is the India-centric business and India-centric business tends to be lower margin anyway. To address that we are pivoting to the U.S., and we've augmented the sales team in the U.S., particularly and also in Europe. And I think that should start showing some results hopefully in the next 2, 3 quarters.

In terms of Digital Operations, we had a volume shrinkage, which was rather unexpected because the customer themselves had a volume shrinkage in the U.S., and that caused the impact on the Digital Operations. Hopefully, the customer turns around and they come back to speed in the future quarters. Once that happens, we will also bounce back. The outlook for the next 2, 3 quarters, I think we will be able to claw back some of the erosion we had in this quarter, and I'm quite optimistic that it will remain stable.

Grishma Shah: Okay. And now what's the outlook going ahead given that first half is already done?

Rahul Kanodia: As I mentioned, I think we'll have a stable next 2 quarters, and we will be able to claw back some of the margins that got eroded in the last quarter.

Grishma Shah: Okay. So we would grow only 4%, 5% this year. Is that the case?

Rahul Kanodia: That is correct. We are, in dialogue on some M&A, but they're dialogues. No deal happens until it's not happened. If we have any acquisition, then obviously, some of the outlook will change. But as of now you're right, we will maintain a stable current level performance.

Moderator: The next question is from the line of Farhad Bamji, who is an individual investor.

Farhad Bamji: My question is as follows. In my experience, most Indian companies aspire to grow at 2x the GDP, and smaller companies aspire for slightly higher growth because the base is less. If I look at our investor presentation in the last 10 years, we've grown at approximately 7.8 CAGR. Now that is substantially lower than what most companies would aspire to be. So my question is, how are we looking at growth going forward? Are we aspiring a 15%, 20% growth going forward? Do we have any strategy to be a $1 billion company, for example, in 4, 5 years? Is there any strategic thinking on those lines?

Rahul Kanodia: Yes. So we are, and our approach for achieving that kind of a growth is predicated on 3 or 4 key elements. One is our alliance with the hyperscalers. We've talked about that. We are investing very heavily in the whole AI space. Google has recognized Datamatics. Microsoft has recognized Datamatics. We're getting some good traction from whatever we've done with them in the market.

We have stepped up our activities in participating in events, both in Europe and the U.S., and they're giving us good traction when it comes to things like Copilot and AI. So that's one area. In that space, in particular, it's not the size that matters. It's really your ability to move fast, and we are moving as fast as we can. That should result in some growth, point number one. So one is the hyperscalers bolted on with the whole AI angle.

The second is the M&A. We have a very healthy cash balance, and we have done an acquisition in the last 2 years. You've seen we've done 2 or 3 acquisitions, the latest one being Dextara. We are in dialogue with a few more companies and as they materialize, obviously, that will give a boost to our growth. And then, of course, we leverage that from a cross-sell point of view and all of those things.

The third is that we have augmented our sales team in the U.S. and Europe, and we are also stepping up the marketing. So I think a combination of pushing the sales team more, augmenting the team in the investments we are making in marketing, the alliances with strategic partners like Microsoft and Google and the acquisitions, all put together will give us some of that boost that we are looking at, in terms of the growth rates.

Farhad Bamji: That was very helpful. And again, to just reiterate, given that last 10 years, we've grown at a CAGR of 7.8%. Would you all come up with some sort of a statement or strategy to say that we are changing gears and we're looking at more a 20% plus kind of CAGR or closer to higher teen CAGRs than single-digit CAGRs. Would you all come up with some sort of a thinking or strategy or statement around that?

Rahul Kanodia: Well, we are working on that, and you may have noticed we've also augmented our Board, and we've inducted several different people who are experts in the industry. So we are changing teams both at the Board level as well as the operating management team. And I'm confident that we will be able to come back with a more refined strategy for growth. Our business planning will start in January.

So I think in the next quarter, which is Jan, Feb, March, we should have our plans baked in for the growth that we're looking at. So maybe around the year ending quarter, we should have a little more insight into the strategy for achieving these growth numbers.

Farhad Bamji: That's really great. Much appreciated. Wish you a lot of good luck. And I would love to see our company be a $1 billion company in the next 4, 5 years or so. I would really wish for that.

Rahul Kanodia: Thank you very much, and that is our ambition as well.

Moderator: The next question is from the line of Nikhil Poptani from Kizuna Wealth.

Nikhil Poptani: Can you just highlight some points on our top 5 client concentration? It has declined from 25% to 21%. Can you just highlight something about that?

Rahul Kanodia: So that decline is largely because of some volume reductions that we saw, and I kind of mentioned that in my address as well. So essentially, it's a volume reduction that's causing it, and that was partly because of the softness that we saw in the markets earlier. Although we do see markets picking up. And if you may recollect that we signed 12 new logos in the quarter. So in terms of new customer acquisition, it's healthy. It's just that a few of the larger clients had a volume shrinkage, which is what impacted. I am sure that they will bounce back soon. And with them, we will grow as well.

Nikhil Poptani: Okay, sir. And sir, my next question is around about the more of a macro environment. Like how do you look at the macro environment going forward in the spaces of like our BFSI over different verticals? And how the interest rates are going to impact? Can you just provide some of your views on that?

Rahul Kanodia: So these are my personal views. I think the U.S. Fed is reducing interest rates, and they will do that a little more because they do need to spur the U.S. economy. But however, having said that, there is, of course, this looming issue of a war in the Middle East. We look at Turkey revving up. You look at Iran making some moves. Israel, of course, is getting aggressive. So there's some degree of uncertainty there. At this point, as we speak, some uncertainty in the U.S. with the U.S. elections, but that should be settled very soon because I believe the elections will be announced today, U.S. timing. So that uncertainty hopefully should go away soon.

But Europe remains a sort of in a little bit of a doldrums if I may. The economy is soft. And if you see North Korea getting involved with Russia in terms of the supporting Russia and the Ukraine war, that is some cause of concern. So overall, on a macroeconomic expectation, apart from the uncertainties of war in the Middle East and Europe, I think we should be all right once the U.S. elections are over. And that should be in another day or 2, we'll get the results. The U.S. with them reducing the Fed rates -- interest rates, I think the U.S. economy will bounce back, and things should look better.

Nikhil Poptani: Congratulations for good set of numbers.

Rahul Kanodia: Thank you very much.

Moderator: The next question is from the line of Sanjay, who is an individual investor.

Sanjay: So I had 2 questions. Sir, in last quarter call, you mentioned that the margins will get expanded by 150 basis points to 200 basis points in Q2. So we see I think instead of expanding, it contracted. So what are the reasons? And are we seeing now the margins get better in Q3? Or we have to wait till Q4? That's the first question.

Rahul Kanodia: Yes. So to your question, as I mentioned, there was some unexpected volume degrowth from our customers because their volumes degrew. And that is really what impacted us. That was rather unexpected. Having said that, we have taken further steps on automating and tightening our belt. So I think we will, in the next 2 quarters, Q3 as well as Q4, claw back some of those margin erosions. That will happen for sure. We are now in Q3, so let's see how this quarter ends. But whatever steps we are taking shows that we will be able to claw back some of the margins.

Sanjay: Okay. And about the annual increments, is it given to all employees already or it is scheduled in this quarter?

Rahul Kanodia: No. The increments are given. The next increment cycle will be in Q1 of next financial year. So for this year, there's no further increment as such.

Sanjay: Okay. So generally, we have like H2 generally is better than H1 and Q4 is generally on higher side. So that trend will continue this year as well, right?

Rahul Kanodia: Yes. Q4 tends to spike, and we will see a spike in Q4 anyway because we have that very cyclical business in our financial F&A business.

Moderator: The next question is from the line of Amit Agecha from HG Hawa.

Amit Agecha: Congratulations for good set of numbers and greetings to all for the festive season. My question was with respect to like what are the initiatives being taken for artificial intelligence, like the investment being made and the impact on the revenue and how are the new products being taken up in the market?

Rahul Kanodia: So we have taken a lot of steps, and we've invested significantly on the whole AI space. I think we are, in many ways, ahead of the curve, if I may, in terms of the kind of solutions that we've built. We've started taking them to the market, and we are getting some very good response from the market. Mitul is on the call as well. Maybe Mitul, since you are attending a lot of these events, maybe you want to say something on that. But just to conclude on that, we are getting some good responses. And hopefully, in the next quarter or 2, we are able to close a few deals. Mitul, do you want to add to that anything?

Mitul Mehta: Yes. So I've been traveling across U.S. and Europe over the last couple of months, and we see a huge opportunity especially on the Copilot and on that front, where a lot of enterprises have taken the first step to go ahead with copilots into their enterprises. Now they're looking at how that can be further leveraged into their enterprises. That's where the service providers like Datamatics come in where we can extend the usability of copilots into their organization. So those conversations have been very promising, and we're hoping that, that would be strong.

Also, a lot of customers are looking at applications, which will natively have AI built into it. That is why we are upgrading FINATO, which is our CFO transformation platform and bringing in all the built-in features of automation, AI, and analytics into it, which makes a CFO back-office more modern and alive for the next about decade or so. So, I think that's in short, would be where we are seeing the AI opportunity.

Rahul Kanodia: And I think some of the investments that we made has been also recognized by Google and Microsoft, which is very good because when you have partners at that scale and those kinds of companies, they bring opportunities to you, and they present us very good avenues for growth.

Amit Agecha: Any color on the investments being made in that?

Rahul Kanodia: We are not tracking that very specifically for multiple reasons. So AI is permeating every part of the operations and every product and platform that we have. So we've got little, little things going across the board. So therefore, if you just look at an AI layer per se, it's difficult to identify exactly what is AI and what is not because a lot of the existing teams are also sort of pivoting into AI and then we've got a whole AI team also working on it. So I don't have a number at the tip of my fingers, but perhaps we can collate that number and track it for the investors going forward, but I need to do some homework on that.

Moderator: The next question is from the line of Jathin from Choice Broking.

Jathin: I just have one question. With recent acquisitions like Dextara Digital, what other areas or capabilities is Datamatics targeting for future acquisitions to enhance its product offering or geographical reach?

Rahul Kanodia: Yes. Dextara was focused on Salesforce. And with them, we have showcased in the Salesforce event that was there in Washington, in San Francisco recently. We brought in a lot of AI flavor to that, which was really appreciated by a lot of the customers. Our going-forward targets are around cloud, data, digital content. I think these would be and maybe customer experiences. We are talking to several companies in this spectrum. All of these areas, whether it's digital experiences, digital content, cloud, or data will augment our existing business. So we're not acquiring to get into a new space. We're just going to use them as bolt-ons to our existing business to deepen the expertise and competence that we have. And of course, by default, when you acquire, you'll get a bunch of new customers as well, so it will add to customers. It will add to our capabilities and depth. We are not looking at a geographical expansion or a new area that we are not present in.

Moderator: The next question is from the line of Sanjay, who is an individual investor.

Sanjay: This is a follow-up on my previous question. So sir, you mentioned about the Google partnership, because Copilot is already, announced and it was probably in last quarter. So a recent partnership with Google, how is that going to help in getting the business?

Rahul Kanodia: Yes, it is a recent development. And Google is taking us to their customers, and they are coming along with us to our customers, so there's a much stronger collaboration where we're doing a joint go-to-market, or they are bringing opportunities to the table. And as those opportunities materialize, we should see an uptick in the business that we get around Google's AI, which is Gemini.

Sanjay: That's great. So was there any announcement? Or are you planning to do an announcement?

Rahul Kanodia: We will make an announcement soon. It is very recent. We are still working on some of the press releases and things like that.

Mitul Mehta: Some paperwork is going, but we will make an announcement.

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

Rahul Kanodia: Thank you, everyone, for being on the call. I really appreciate the time you spent with us, and I wish you all a very happy Diwali once again and prosperous New Year. I look forward to speaking to you once again at the end of next quarter. Thank you again, and bye for now.

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

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