HCL Infosystems Quarterly Investors Conference Call

November 18th, 2013

SPEAKERS: **Harsh Chitale, CEO, HCL Infosystems Ltd.**
Sandeep Kanwar, CFO, HCL Infosystems Ltd.

Moderator: Very good afternoon everyone. Welcome to HCL Infosystems quarterly investor conference call. I would like to hand over the proceedings to Mr. Harsh Chitale, CEO

Harsh Chitale: Good afternoon everyone. We have our CFO, Mr. Sandeep Kanwar with us on the call. We will talk about our last quarter performance and walk you through the restructuring exercise. The final written approval was received on 1st November, 2013; consequently the balance sheets of different businesses were transferred into three different subsidiary companies. We will share what the restructuring exercise entails and the financials of those entities. One of the objectives of restructuring was to bring greater granularity and visibility to operational and financial parameters of our different businesses. We will use this opportunity of quarterly analysts' call to give a greater depth in that view of each of those businesses by those subsidiaries.

We would like to begin with a mandatory disclaimer. This call may contain forward-looking information including statements concerning our outlook for the future as well as some of our other statements of belief, future plans and strategies. These forward-looking statements and information are subject to risks and uncertainties that they always entail.

Beginning with our scheme of arrangements and where do we stand today. The scheme of arrangement on restructuring became effective on 1st of November 2013. The process had started in January 2013 with the Board approval for going ahead with scheme of arrangement. Then there was a series of hearings held involving investors, creditors and suppliers. After the final hearing before the honourable High Court on 18th of September, the final approval for this scheme was received. The written intimation of the court order was received on 1st November making the scheme of arrangement effective from 1st January 2013.

Financials were restated for 1st January 2013 to 1st November 2013 into the respective subsidiaries. In a way, business was held in trust by HCL Infosystems for those three businesses, which are now moved into subsidiaries.

Now, the enterprise solution in the hardware business has been moved to HCL Infotech Limited, services business has been moved to HCL Services Ltd. and the Learning Business has moved to HCL Learning Limited. The three large parts of the businesses are now into wholly owned three subsidiaries.

The Parent company continues to handle large distribution and residual parts of consumer computing and Mobility businesses.

The restructured organization now looks like; HCL Infosystems' parent which holds our distribution business and HCL computing and mobility products business. We will spend a little more time on our computing products business as we have some specific plans and actions around that.

HCL Services Limited, a subsidiary, will handle consumer care and enterprise services businesses. This company would also have Singapore step subsidiary to manage the infrastructure managed services deals of Singapore Government. The approval with RBI and FIPB are in process to move this subsidiary under HCL Services Limited.

HCL Learning Limited will hold our education learning & solutions business, and HCL Infotech Limited will handle the B2B hardware, enterprise hardware and SI businesses. Our Middle East subsidiary which handles largely enterprise businesses will become a subsidiary of HCL Infotech Limited in a short time. We are in process of getting FIPB and RBI approvals to move HCL Infosystems MEA as a subsidiary of HCL Infotech Limited.

The restructuring was fundamentally done to give a focused management to each of the businesses with individual specialization and leadership vision. Each of them has very different needs. HCL Infotech Limited is a severely challenged business in terms of its working capital, overdue collections from some customers and exposure to volatility in foreign exchange. To fix this business, leaner operations and faster collections are required. HCL Services Limited, on the other hand, is a growing business. Distribution business is one of our growth areas, and a different management focus and talent requirements are in those businesses.

Our second objective behind the restructuring was to have a greater visibility for shareholders and other stakeholders into the operational and financial performance of each of the businesses. With independence in the operations of each of the subsidiary, they can now operate with the competitors of their sister company without firewalling of the operations. For instance, HCL Services Limited continues to serve our competitors such as Dell, Lenovo, and Educomp in the services arena without having a conflict of interest or tradeability, and this is a big benefit for the business’s growth. This structure also creates platforms & flexibility for strategic partnerships and strategic investments into the different arms of this consolidated organization in future.

So let’s start with HCL Infosystems Limited entity, the parent entity, which houses the distribution business and some part of our computing product, the residual computing products business.

The Distribution business did well with 16% growth sequentially. This is second double digit sequential growth in revenues. In Q4 FY13, Telecom Distribution Revenues were Rs. 1130 crores, which grew to Rs. 1308 crores in Q1 FY14. The IT and digital entertainment stayed flat sequentially with Q4 FY14 revenues at Rs. 201 crore and Q1 FY14 at Rs. 199 crore. Telecom and IT & digital entertainment, both put together, businesses registered a 13% Q-o-Q revenue growth.

This came on the back of two significant developments. Firstly, in the telecom distribution, sales of various phones Lumia, Asha as well as the entry level have picked up in the last two quarters from the lowest sales levels in December 2012. One entry-level phone was introduced end of June, that sold over a million units in its second month of introduction.

Besides the growth in Telecom Distribution business, number of new partners such as HP, Delta for UPS, and Lenovo for tablets were added in Non Telecom Distribution business. In fact, almost half of the tablets from Lenovo, Lava and Karbonn that are sold are distributed by our distribution business. Due to such new tie-ups, this non-telecom business of IT and digital entertainment saw a 25% Y-o-Y revenue growth from Rs. 158 crores in Q1 FY13 to Rs. 199 crore in Q1 FY14,

The telecom distribution revenue drop on a year-on-year basis, from Rs. 1591 crores in Q1 FY13 to Rs. 1308 in Q1 FY14, was due to portfolio shift in handset business during July to December 2012. Sales have inched up from January 2013 onwards, resulting in a double digit sequential in the last two quarters.

Revenues from Distribution business for the quarter reported at Rs. 1507 crore with profit from ordinary activity before exchange at different rates and provision of doubtful debts at Rs. 25.4 crores. There are only few brands which are imported in USD and hence are relatively immune to any variation in exchange rate. Exchange loss for the quarter was reported at Rs. 1 crore and profit from ordinary activity transcended into PBIT of Rs. 24.7 crores for the business.

The Computing products business has two parts B2B Hardware business and B2C business. The B2B business has been moved to HCL Infotech Ltd. The B2C part of the business, which is sold through various channels and the entire manufacturing organization has been retained in the parent company. This is referred as residual part earlier. We will be winding down our manufacturing operations in the future as they are not globally competitive, lack global scale and are exposed to significant exchange rate fluctuations.

The computing products and mobility business, revenues grew over 30% Y-o-Y from Rs. 133 crore in Q1 FY13 to Rs. 166 crore in Q1 FY14. The sequential drop in revenues from Rs. 184 crore in Q4 FY13 was due to sudden spike in exchange rate. A spurt in exchange rate turned the entire product pricing into negative gross margins, thus forcing us to halt the trade for containing the margin erosion. The loss from ordinary activities before exchange stands at Rs. 2.2 crore for the quarter.

The PBIT was a negative Rs. 6.4 crores for the quarter due to Rs. 4.2 mark-to-market accounting exchange rate implication on the open payables on the day of September 30th. The Rs. 166 crore business revenues delivered a PBIT loss of Rs. 6.4 crore for Q1 FY14.

As the imports and manufacturing operations are progressively wind down, the residual manufacturing operations in parent would have reduced/limited/no exposure to exchange rate loss and thus improvement in the distribution business margins.

For our second subsidiary, HCL Services Limited and its subsidiary HCL Insys PTE Limited, the revenues grew by 13% Y-o-Y from Rs. 136 crore in Q1 FY13 to Rs. 153 crore in Q1 FY14.

The enterprise services grew at 18% and the consumer care services had a decline in line with decline in the handset volumes. Every handset sold through our distribution business has an attached warranty related repair work done by Care business. The year-on-year drop in handset distribution business translated into a drop in our Care business. HCL Care is adding new principles to mitigate the decline in business. Bajaj Electricals and Samsung have been signed recently to operate consumer care in some part of the country. Care business portfolio now has brands such as Nokia, Blackberry, Philips, Samsung, Bajaj Electricals and Lenovo. The network of walk-in service centres has grown to about 200 all over the country. This network is expected to cross 400 walk-in centres and closer to 500 walk-in centres by June 2014. The business registered a healthy growth in contract booking and partner sign up in enterprise services that finally resulted in revenue of Rs. 153 crores this year, growing from Rs. 136 crores last year. Revenues of Rs. 153 crores for the quarter of HCL Services Limited along with its subsidiary HCL Insys PTE Limited, delivered a PBIT of Rs. 7.6 crores. Both distribution and services entities are delivering good growth and profits.

HCL Learning Limited, our third entity which operates in the digital education and learning space, saw a lot of turmoil last year and many listed entities focussing on this business went through a lot of strain and financial suffering. We have been extremely conservative and cautious, being a late market entrant. This business is suffering from a weak industry sentiment because of what’s happening with some of the leading players. We have taken a different approach of growing the Learning business as we believe that it is fundamentally a long-term play. The company has been very selective in booking of new classrooms. In fact, revenues from classroom booking dropped from Rs. 16 crore in Q1 FY13 to Rs. 13 crore in Q1 FY14. Nearly 70% of the business is done in the AMJ quarter, a period when new school sessions start and schools buy to be ready new session/season. All the selective bookings done adhere to our internal criteria of margins and assured collection through PDCs.

Looking into the financials of this business, Rs. 13 crore revenue finally translated to a PBIT of negative Rs. 2.7 crore. The margin has gone up by 300 basis points year-on-year. If we look at PBIT performance, this business actually had a better performance year-on-year from last year corresponding period to this year. There has been a margin improvement and as the volume picks up in the second half of the year in this cyclical business, this business would turn to a positive profit this year.

HCL Infotech Limited, the entity which had a significant financial stress due to working capital challenges in slow moving projects from public sector enterprises such as state-owned telecom companies and state-owned discoms, continued to face these challenges. Our objective for restructuring was to enable isolation of the challenged businesses into a separate entity and have a team focussed on addressing the challenges of slow moving projects and recovering all of the stuck receivables.

This business also operates the project phase of the UIDAI programme, which is going well. Over 40 crore aadhaar cards are generated under UIDAI programme. The new defence deals signed recently are moving on track, the first phase Airforce cellular network project has been rolled out and we won some new renewals from banks such as SBI and IDBI.

There was operational progress on projects in hand but we are consciously very selective in picking up deals in this business. Going forward there may be declining revenues in this business due to winding down of old accumulated backlog of projects as we focus on collecting the cash and unlocking the working capital deployed in this business.

This business, in future, will focus only in selective services-centric deals with limited exposure to long BR cycle or exposure on foreign exchange in projects or where there is a back-to-back partner who is willing to offer hardware in rupee terms and with back-to-back payment terms. Discipline has already been put in HCL Infotech Limited to pursue such deals. Our focus is on de-risking the business in terms of foreign exchange volatility and delay in liquidation of working capital. This may result in declining revenue as we wind down the existing backlog and move this business to a services-centric business going forward. This business reported a 20% Y-o-Y drop in revenues. Revenues came down from Rs. 521 crore in Q1 FY13 to about Rs. 400 crore in Q1 FY14.

HCL Infotech Limited had a PBIT before exchange rate and doubtful debts a loss of Rs. 19.7 crore on revenues of Rs. 399 crore for the quarter. Significant part of that loss in row number two came because of exchange rate escalation. While it's not a mark-to-market exchange rate difference, it's an increase in the cost of goods sold because of exchange rate going up. When a project budget made with Rs. 55 a dollar goes to Rs. 62 or 63 a dollar, project budgets get restated and that restatement of project budget translates to a reduction in the gross margin of that business. And when such restatement of project margin happens, that quarter gets a significant hit because that hit happens on the entire accumulated revenue of that project. Average project margin which was hovering at 14% in system integration projects came down to 6.7%.

There was a sharp reduction in the project margin as the imported portion of cost of goods sold became more expensive in terms of the overall cost to complete the budget of the project. Rs 399 crores which normally should have been positive at that row two level became negative Rs. 28.3 crores. On top of it, there was a mark-to-market payables restatement of Rs. 22.3 crore due to the exchange rate loss. The provision of doubtful debt for thw quarter was Rs. 3.9 crore. Consequently, the business reported a loss of Rs 54 crores on revenues of Rs. 399 crores.

The distribution business of Rs. 1500 crore generating Rs. 24.7 crore PBIT and pretty much all of that PBIT translates to PBT because of very small capital employed in distribution business. Services business of Rs. 153 crore translates to PBIT of Rs. 7.6 crore and a large part of that also translates to PBT because of relatively smaller capital employed. Learning business revenues of Rs.13 crore translates to for the last quarter PBIT of negative Rs. 2.7. The cyclical business has much higher revenues in H2 and would turn to profit at the year end. The solutions and consumer computing mobility, two hardware-linked businesses which have high working capital exposure and exchange rate exposure. Revenues of Rs. 399 crores in Solutions and Rs. 166 crore revenues in consumer computing and mobility, resulted in a combined loss of over Rs. 60 crore for the quarter.

There were certain unallocated common cost and certain eliminations, also some investment income in parent entity which resulted in an additional Rs. 5.5 crore of bottom line on consolidated basis. Hence, on the total consolidated revenue of Rs. 2201 crores for the quarter, the PBIT level was a loss of Rs. 25.4 of which Rs. 60 crore loss was in hardware and SI businesses. The Finance cost for the quarter was Rs. 43 crore. Bulk of that finance cost was on account of hardware business and solution business. Hence, on a consolidated basis there was a loss of Rs. 68.5 crore.

Going forward, entire focus is on driving growth on our two big growth platforms i.e. distribution and services. Both are growing and profitable with high ROI as the capital employed is low.

We will focus in growing learning businesses, in a very prudent, judicious manner without taking credit risks as some other peers may have done. HCL would focus to capture the opportunity of additional classrooms and some market share made available due to weakening of many other leading competitors.

The hardware part of the business of Enterprise Solutions business would pursue orders extremely selectively as we wind down large parts of that business and eliminate the import heaviness out of that business. Focus is on moving a business model which is largely services centric with selective deals where only some back-to-back hardware partner.

The Hardware and Solutions business would move towards leaner operations and cash recovery by liquidating the balance sheet. Distribution and Services are one growth agenda and Learning as a long-term growth. The current restructured organisational structure helps in focussing on these.

We would share transparently every quarter the progress of each business/entity.

With that I would like to throw open this call for any questions and would also invite, Sandeep Kanwar, our CFO, to answer any questions and queries that you may have.

Moderator: Thank you so much, sir. Participants with this we start the “Q&A” interactive session. So I request all the attendees, if you wish to ask any question, please press “0” and “1” on your telephone and wait for your name to be announced. I request all the attendees, if you wish to ask any question, please press “0” and “1” on your telephone keypad and wait for your name to be announced. We have our first question from Mr. Srivathsan from Spark Capital. Your line is open. You can go ahead and ask your question, sir, thank you.

Srivathsan: Yeah, hi, I wanted some more clarity on restructuring. Post restructuring and winding down manufacturing operations, would HCL Branded laptops or tablets still be manufactured or would it be outsourced?

Harsh Chitale: Yes, so it is a good question. The value chain of, say PC, is manufacture, sale and distribute, and service. A very little value addition happens in terms of manufacturing process. The total value addition in manufacturing process actually is low single digit as a percentage of revenue. Unfortunately, all the import risk and exposure is actually a part of that activity. HCL will continue to be a large go-to-market engine for selling distribution and service of PCs, but not necessarily manufacture it.

Focus would be on multi brand distribution and services player as opposed to just being restricted to a single brand of a PC player. Also, most importantly, to eliminate the entire import related risks that comes out of the manufacturing activity.

Srivathsan: To continue on this, the major loss is in HCL Infosystems. Would winding down manufacturing impact consumer computing and mobility business part as well?

Harsh Chitale: Yes. The loss in Consumer Computing & Mobility business and residual manufacturing plant, was on account of exchange rate. As we wind down that manufacturing activity that loss will also be over in the next few quarter.

Srivathsan: In terms of capital employed, it be helpful if you could tell us which business has what capital is employed, so that we can kind of get the number as to what fiscal cap will get released post restructuring.

Harsh Chitale: As per Clause 41, limited audit of our balance sheet is required every six months. This will be done on December 31st and balance sheet of these respective entities shall be shared with all of you as opposed to doing only a selective disclosure.
But just to give you an overview, there is a large capital employed in the Enterprise Solutions business which is now in HCL Infotech Limited. Manufacturing activity per se does not have a very large capital employed. So, winding down manufacturing operation will not release too much of capital employed, but it will eliminate the P&L risk, it is more for that as opposed to release of capital employed.
The total book value of plant and machinery is less than Rs. 10 crores and total value of land and building is under Rs. 40 crores. So it is relatively smaller capital employed in terms of manufacturing operation.

Srivathsan: Okay, in distribution business, a large income comes from Telecom business. Wanted to understand how it is spread, is it beyond Nokia or is ii predominantly in Nokia, what kind of vendor consolidation would we be having on the distribution side?

Harsh Chitale: Yes, we have Nokia in our Telecom distribution portfolio. We have accessories or gears like batteries, Bluetooth, covers for multiple brands. Nokia is one of them, but in multiple brands. We are selling a lot of tablets sold finally in the Telecom channel. So, all of them are a part of our distribution in the Telecom channel. Nokia does make the largest share of our Telecom distribution. But now it is not just Nokia. There is a growing part of accessories and a growing part of many brands of tablets.

Srivathsan: Okay, I will come back later, thank you.

Moderator: Thank you so much, Mr. Srivathsan. The next question we have from Mr. Ravi from Centrum. Sir, your line is open. You can go ahead and ask your question. Thank you.

Ravi: Sir, I like to understand a little bit more about where is the working capital getting stuck, the government contracts, what sort of entities you have issues with and whether there is any risks of actual default of payments or is it just that this is just a delay in payments based on disagreement about the milestones being not met or something like that?

Harsh Chitale: Yes, HCL Infotech, the Enterprise Solutions part, has most of the the stuck working capital. Some of the old contract signed with the state Telco's like BSNL, MTNL, their equipment suppliers like ITI, Ericsson Aicatel and from state Discoms like Rajasthan Discom, HP State Electricity Board Discom, Jharkhand ACB. So those state owned entities is where our receivable are stuck. And with these entities total receivable that has taken time to liquidate is in excess of Rs. 700 crores as we have shared in all our previous calls.

As a part of fair valuation process for transfer of businesses as per scheme, KPMG and our statutory auditors PwC, discounted these assets as per discounted cashflow method. And hence already as a part of this implementation to a court approved scheme, already there has been some discounting of value of these assets that has already been done.

Over and above this whether there will be any additional impairment is difficult but unlikely because they have been extremely conservative in the discounting and arriving at a DCF value for assets of that business.

Ravi: Right, sir. And this impairment was that part of a P&L hit for this quarter?

Harsh Chitale: No. The resulting impact out of that fair valuation was then taken into the share premium account in the balance sheet.

Ravi: Alright, sir, thank you. That is it.

Moderator: Thank you so much, Mr Ravi. Before we go ahead and the next question, once again, I request all the attendees, if you wish to ask any question, please press “0” and “1” on your telephone keypad to ask a question. The next question we have from Mr. Ankit Pande from Quant Capital. Sir, your is open, you can go ahead and ask your question. Thank you.

Ankit Pande: Hi, sir, good afternoon. Could you just specific what the order book is like for the hardware business?

Harsh Chitale: Yeah, as at September 30th order book for hardware business was Rs. 2900 crore of orders yet to be executed. That Rs. 2900 crore had three large new contracts which was UIDAI Managed Services Programme, Defence Communication Network and the phase two of this Air Force Cellular AFCEL Network. These three don’t have the issue of capital getting stuck. And about, Rs. 1100 crore of old contracts where working capital cycles have got stretched. Sandeep, do you want to add to that?

Sandeep Kanwar: Yeah that is about it.

Ankit Pande: I just wanted to understand if all of these or any of these contracts have any kind of limitation on how much Forex exposure **will** the company take. Have we at all bargained with the customers to have it included in the contracts?

Harsh Chitale: In the new contracts we have actually lined up all our procurement in INR. The supplier will hedge and give us the materials in INR. The new contracts have mitigated exposure by doing so because contractually customer has not agreed to exchange their variation clause. We were able to do so for most of the imports. For old contracts that was not the case and that is where this restatement of margin created an impact.

Ankit Pande: Could you give the approximate import cost?

Harsh Chitale: Yeah, I don't have it off hand.

Ankit Pande: Any idea of how much of that, sort of, not open to Forex damages in that sense?

Sandeep Kanwar: As of today, we have a cover on the commitments that we have already made and dollars is almost totally covered. So that is not an issue.
It is only going forward when we say that we are already contracted by an INR. That is what Harsh is talking about. So they there will be some exposure going forward. But that is not quantifiable because the effort is to convert everything to INR which we have been, I think, successful so far.

Harsh Chitale: Yeah, there was a $44 million of balance imported in the old contracts which by taking an estimate of timelines associated of those imports, we are covered in full.

Sandeep Kanwar: And the cost is already inside the book.

Harsh Chitale: And that coverage cost will get amortised as our amortisation of the hedging cost and that's what will be seen in the exchange rate line. It will be an amortisation of that hedge taken. But at least it will remove uncertainty.

Ankit Pande: Alright, maybe, I can take some more details later. I just also wanted to understand in the Consumer Computing & Mobility business, you said, there is, obviously, some part that is going to go to Infotech. So can you give, roughly, what kind of percentage is that B2B versus…?

Harsh Chitale: Yes, the manufacturing plant is common for the PC and are sold through the direct channel which is the HCL Infotech, where HCL signed up PC projects and then Consumer Computing & Mobility all get sold through distributors and channel partners. So that is why that part is in the distribution entity.

Manufacturing part is common for the two and is still staying in HCL Infosystems Limited parent. Now, Rs. 166 crore of Consumer Computing & Mobility revenues, whatever was the manufacturing was done by that manufacturing. Additionally, about 130 crore of PCs were made for the Solutions business which are in HCL Infotech Limited by this manufacturing organisation. So the total manufacturing was Rs. 130 crore plus part of this Rs. 166 crores. And hence, let's say about Rs. 250 crore of where you are importing and getting the exposure part is sitting in that parent and when we say – that's what we want to wind down and move to a traded model where we buy the ready product in INR and sale in INR. It is that Rs. 250 crore exposure that will get eliminated.

Ankit Pande: What should we expect if the Infotech business is removed, what can we expect the margins to be?

Harsh Chitale: So Distribution, Services and Learning, these three businesses which are let's say our horizon 1, horizon 2 growth platforms. Going forward we do see them going strong and in fact margins improving as the revenue of services keeps growing and revenue of learning actually picks up in the second half. So we would see those margins moving up in those three. Solutions and Computing, the loss that one is seeing there on account of exchange rate related restatements will progressively get wound down as we wind down our import exposure in that business. And move that business only to services-centric business. So the Solution and Consumer Computing over the next few quarters, our effort will be to wind down the loss in those. And Distribution, Services and Learning, you will see margin at this level going up from where it is right now.

Ankit Pande: Can we expect a mid single digits or upwards by the end of the year?

Harsh Chitale: We won't be able to give a forward guidance on that.

Ankit Pande: Okay, thank you so much, I will jump back in the queue.

Moderator: Thank you so much, Mr. Pande. The next we have from Mr. Vikas. Sir, your is open. You can go ahead and ask your question.

Vikas Chiranewal: Hi, Harsh, Vikas Chiranewal.

Harsh Chitale: Hi, Vikas.

Vikas Chiranewal: Just a couple of questions. Just a follow-up on the last question itself. Margin profile of distribution, what is the margin profile currently at the gross margin level just for the distribution business?

Harsh Chitale: Yeah, so the gross margin for the distribution business for the various product line varies from 3% to all the way up to 12%. Average, right now, for the business as a whole is a little under 3 ½ %.

Vikas Chiranewal: Right. And it is fair to assume that Nokia would be much lower than that and others would be higher than that?

Harsh Chitale: That is right. But as we have taken on some additional activities in Nokia, actually, Nokia margin, gross margin have moved up quarter-over-quarter in our distribution business. There has been a reworking in the scope of responsibility between us and Nokia and some additional margin has been agreed between us and Nokia for the work that we do for them.

Vikas Chiranewal: Yeah, when you scope of work, what do you mean?

Harsh Chitale: So in the rural market, we are now doing more and more, let's say, direct to micro distributors, so covering the last mile. And for that last mile, we are getting additional compensation from Nokia.

Vikas Chiranewal : And for the services level, what would be the GM currently?

Harsh Chitale: So for the services as a whole gross margin is between25% to 30% closer to 28%; exact number is 28%.

Vikas Chiranewal: Sure. And blended for the year for Learning, how much would be the gross margin?

Harsh Chitale: Blended for the year, gross margin for Learning will be 40% to 43%. So actually, Learning, we have been able to grow to a very healthy gross margin. It is an issue of an SD&A for the scale. And as we keep adding – but add it in a very focused disciplined manner. We are just a few quarters away where this starts translating into profit, at healthy profit rate.

Vikas Chiranewal: But even for the Learning business, we have taken a provision on bad debts. Could you comment on that?

Harsh Chitale: Yeah, what we have done is as a part of this entire restructuring, we also took a look all of the working capital and anything which is over six months of receivable, we chose not just to take a provision just of the overdue, those two quarterly instalments, but treat it as of banks NPA, you know, how bank will treat the entire value of the asset as NPA, and hence even the balance portion which is what is sitting in your books as of future lease rental recoverable. That means it is not yet build, but you are supposed to build it recover over the next three-four years. But if somebody has default that for six months, we said we will treat the entire asset as an NPA and take charge of that. And as we move to that way of working, there was some charge that was taken for the quarter.

Vikas Chiranewal : Sure. Just going back to the distribution business, on Telecom distribution what is the current ASP for Nokia that you are working with in volumes?

Harsh Chitale: Vikas, I don't have it of that now.

Vikas Chiranewal: Sure. On the manufacturing closure that you talked about, would we have to take additional cost for restructuring for that?

Harsh Chitale: So our total book value of plant and machinery is five or six crore. And luckily, in our services business there is a very large growing part of repair services. And in manufacturing, actually, pretty much all of that is just the workbenches. So it is very easy to move that to repair factory. And hence, we do reutilisation at a repair factory. So I don't expect on our fixed asset side.

In fact, we are in the process of creating more repair factory. So it has become immediate redeployment. In terms of some charges on account of wind down of old inventory, realisable value associated with that, we are assessing it, but it is not going to be significant because that business in terms of its inventory it is fairly.

Vikas Chiranewal: In terms of any employee related restructuring cost anything base on that?

Harsh Chitale: There could be some. Yes, there would be some. But if you see today for our services and distribution, we add hundreds of employees every month. Our attrition right now is running at little under 16% on a FTE basis. So FTEs of 15000, 16% annualised attrition means 2400. So every month about 200 leave. And they get replaced, close to 200 get replaced. So total number of employees diploid in that operation versus our natural attrition rate I think there won't be a significant impact. There will be some, but not significant.

Vikas Chiranewal: Okay, not a large cost that you will have to take?

Harsh Chitale: No.

Vikas Chiranewal: Okay. And just in terms of the HCL input at receivables. There would be a back-to-back payables as well, right, attached to it?

Harsh Chitale: Yes, there are payables attached to it.

Vikas Chiranewal: And what is the quantum of that as we speak today?

Harsh Chitale: The total payable in Infotech, Sandeep?

Sandeep Kanwar: No, definitely, the payables are not matched with the receivables because certain payables are contracted payables which would have got paid out, Vikas. And the fact is that there is an asset sitting there which still needs to be converted and collected.

Vikas Chiranewal: Right. But some of receivables would have back-to-back payables as well, right?

Sandeep Kanwar: Yes, some would have. Yes that is true.

Vikas Chiranewal: In some of the Telco contracts you will have back-to-back relationship with the vendor?

Harsh Chitale: Yeah, in fact, there would not be too many where there is back-to-back. There would be a firm payable versus uncertain receivable. So since you are using the word back-to-back, I think, that is what Sandeep was explaining. For all of our receivable there is payable in the books. But that payable is not necessarily back-to-back. It is not that once we get paid the vendor gets paid. Those are not the contract terms.

Sandeep Kanwar: Because as an integrator the OEM relationship is different from the customer relationships.

Vikas Chiranewal: Sure. And what is the payable number, total, of any kind in that business right now?

Vikas Chiranewal: And especially, if you could bifurcate it into the new contracts, the UIDAI type of contracts versus the old ones, that would helpful.

Harsh Chitale: Yeah, sure.

Vikas Chiranewal: I think that is it from my end, thanks.

Moderator: Thank you, Mr. Chiranewal. The next question we have is from Mr. Srivathsan from Spark Capital. Sir, your line is open. You can go ahead and ask your question, thank you.

Srivathsan: Yeah, hi. Sir, any broad number you could kind of give us an indication of to what extent capital release for the five, five quarters that will reduce HCL Infotech and manufacturing business?

Sandeep Kanwar: I think, it will be difficult for us to give the future projections on capital release on this thing because as Harsh said the amount of capital invested is not significant to make a difference.

Harsh Chitale: No, in the HCL Infotech Limited, the capital employed after taking the discounted cash flow base fair valuation is in excess of Rs. 600 crore, and the computing plant, we just gave the numbers is not much. Now, it is that portion that gets released over a period of time. There is a fair degree of uncertainty to be frank on the release of the net working capital of HCL Infotech in terms of timing because the receivable has to come and that timing is where the uncertainty has been so far.

Srivathsan: On the distribution side what is the typical working capital cycle that we have just on the distribution side?

Harsh Chitale: So on a distribution side, actually, we are close to zero net working capital. So we operate our inventory and credit within the total credit limits that we get from principals.

Srivathsan: Okay and in terms of the mixture because of the change towards more on non-Nokia or non-telecom business, do you see that the working capital cycle could change materially?

Harsh Chitale: So far we have been able to manage it within that same cycle, which is get credit from vendor and manage inventory and receivable. Now, in terms of non-Nokia piece, while there is a higher inventory and receivable that we have to give in the market, we do also get higher credit. So far it hasn't been materially very different. But as that business starts becoming more and more part of distribution mix, we will get a better picture there. As of now, it hasn't been materially very different.

Moderator: Thank you, Mr. Srivathsan. The next question we have from Mr. Nitin from Macquarie. Sir, you line is open. You can go ahead and ask your question. Thank you.

Nitin: Thanks for the opportunity. I had two questions. Firstly, post the restructuring, I just wanted to understand the competition of the services business from you other promoted company HCL Technologies. How exactly would you guys handle given your focus is now services? And the second thing if I could understand was on the balance sheet side just the nature of investment what exactly are those? And post the restructuring, how would that change? Is there no change over there?

Harsh Chitale: In terms of business mix in services, there is a very large portion which is a break fix services both to our consumer as well as enterprise. That is almost annualised over Rs. 320 crore, or Rs. 80 crore a quarter. Then there is a large part which is office automation services such as managed print services, document management services. That's another Rs. 40 crore a quarter. When you put these two together and in both of these, other sister company has no play. So a large part of services business is actually of a very different nature. It is a break fix service. It's an AMC services. It's office automation, managed print services, all of that.

Now sometimes in those contracts, customers do want an end-to-end managed service responsibility where they say you do this, do my management service, do my break fix, but I also want you to do infrastructure managed service on my data centre or for my application. So we do have some infrastructure managed service and application services play which today both put together is a little under one-third of the entire business. That's the business where there is a potentially skill trade also available with HCL Tech. Our approach has been we go to the market as a stand-alone independent entity. Wherever we think there is a merit in partnering and taking some services from there which comes to us at a competitive rate we do take from them. Wherever that economy doesn't work out, we actually do it ourself. So to answer your question, bulk of the business is non-overlapping. There is some business where there is a skill set available with both. There we look at whether it is making economics sense in make or buy.

Nitin: Got it. On the investment front which is there on the balance sheet, approximately about Rs. 9 billion worth of investments that are there on your balance sheet as of June…

Sandeep Kanwar: Those are liquid investments which are largely in liquid fund.

Harsh Chitale: Normally we have about 5 billion which is always there and about Rs. 4 billion is what is operational surplus. That comes typically at the end of the quarter and then gets consumed. So month-on-month it varies because of operational working capital related cycle. So all 9 billion is in liquid investments but within that I would say the 4 billion is even more liquid and goes in and comes out, and we are still at a similar kind of a ballpark right now.

Nitin: Thanks for taking my question.

Moderator: Thank you very much, Mr. Nitin. So at this time, there is no further questions in the queue. So I like to hand over the floor back to Mr. Harsh for the final remarks. Thank you and over to you, sir.

Harsh Chitale: Thank you all for taking time and joining us today. We are happy to have any follow-up queries and some queries that we have noted down for which we have to get back to you. Feel free to get in touch with our investor relations cell, and we will get back to you with your query. I think one very important milestone in terms of restructuring we have now achieved, through this now we believe we will be able to give you much better visibility of each of our operations. We will also, through this, now be able to focus on our big growth pillars as we decide in the call which is distribution and services in the short term, learning in the mid term. And with this restructured organization, also we will give a laser sharp focus on liquidating and winding down some of the stress part of our businesses as they now have been separated out.

So with this, I think it has created a platform for reinvigorated operation and look forward to talking to you about this and how we are now taking this agenda forward in our next quarter call. Thank you.

Moderator: Thank you so much, sir. That does conclude the conference call for today. You may all can disconnect your line, and have a great day ahead. Thank you very much.