



AXISCADES Engineering Technologies Ltd.

Q4 FY17 Earnings Conference Call Transcript

June 2, 2017

Moderator Ladies and Gentlemen, Good Day and Welcome to AXISCADES Engineering Technologies Q4 FY17 Earnings conference call. As a reminder, all participants' 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 * and then 0 on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Varun Divadkar from CDR India. Thank you and over to you, Mr. Divadkar.

Varun Divadkar Thanks Janis. Good afternoon everyone and thank you for joining us on AXISCADES Engineering Technologies Q4 FY17 earnings conference call. We have with us today Mr. Sudhakar Gande, the Vice Chairman and Mr. Kaushik Sarkar, CFO. Before we begin, I would like to state that some of the statements made in today's discussion may be forward looking in nature and may involve certain risks and uncertainties. A detailed statement in this regard is available on the Q4 FY17 results presentation that has been sent to you earlier. Now, I request Mr. Gande to begin the proceedings of the call.

Sudhakar Gande FY2017 has been a challenging year for us on multiple fronts which impacted us. The worst seems to be over. The performance is expected to improve in FY18.

During these challenging times we have focused on our long term objective of creating a world-class organization and are continuously investing in the business to acquire additional capabilities and diversify into other industry verticals to expand our value proposition to the client. We are glad to inform that we have been rated as "A" on technical competency by a large Aerospace OEM.

We are happy to report that the work sub-contracted over the last few quarters has now been insourced as we have acquired the required skill-set, and will translate into proficiencies in this space going forward. This lends credence to this business strategy which we will continue to imbibe till we attain the desired scale.

These investments made in the business, together with the weak revenue growth, has had a negative impact on margins in FY17. Given that we are a mid-sized company, we are still attaining the scale to withstand these aberrations better, and in the long run our endeavor would be to deliver 15-18% EBITDA margins which are inherent to this business.



We have some key additions this quarter to our list of marquee clientele. This includes one of the largest utility supply company in the United States. The engagement has extremely strong growth potential. We have seen strong traction in the Energy space and are delighted to announce our proposed JV with Assystem Engineering and Operation Services SAS (France) for exploring opportunities in the Energy and Nuclear sector. The deal wins during the quarter also included a strong brand in the Heavy Engineering space in India. We have a robust pipeline across all geographies and will be announcing some more wins shortly. The deal wins and pipeline provide good visibility for growth in FY18.

With the closure of the ACATL acquisition this year, we have a well-rounded offering of Product Engineering and Strategic Technology Solutions, which positions us strongly to address large domestic and global programs. We have signed several MoU's during the recent Aero India, which augurs strongly for the coming years, expands our product solution offerings and places us as one of the premier companies in India catering to the needs of the aerospace and defence sector.

Overall, FY18 looks to be a promising year. We will maintain a sharp focus on operational efficiency, delivery and quality, constantly innovate and be of relevance to our customers.

With that, I now hand over to our CFO Mr. Kaushik Sarkar who will take you through the financial performance of the quarter.

Kaushik Sarkar

Thank you, Mr. Gande. Good afternoon, everybody. I will take you through the financial performance for the fourth quarter and year ended 31st March, 2017.

At the onset, kindly note that the consolidated performance for FY17 includes the financials of AXISCADES Aerospace and Technologies, which is now a 100% subsidiary of ACETL. Hence financials for FY16 are not strictly comparable. Starting with our consolidated performance for the full year, revenue from operation grew ~29% YoY to Rs. 4,836 million, largely driven by the acquisition of ACATL. On an organic basis, the Engineering Services business revenue was at Rs. 3,813 million in FY17 as compared to Rs. 3,793, million in FY16 which is 0.5% growth Year on Year. Consolidated Operating margin in FY17 stood at 10.6%. Operating margin for Strategic Technology Solution business in FY17 stood at 18.4% whereas for the Engineering Services declines to 8%. As Mr. Gande mentioned earlier, the margins for the Engineering Services were impacted due to inadequate fixed costs absorption on low revenue and significant investments made in acquiring capabilities in the form of higher project consultancy costs and investments in leadership hiring.

To summarize the performance for the quarter ended March 2017, The total operating income stood at Rs 1,087 million, down 0.9% QoQ and up 10.9% YoY, led by the merger of Strategic Technology business. On an organic basis, total income increased by 1 % QoQ and declined by 6 % in Q4 YoY FY17. Consolidated Operating margins stood flat at 9.9% in Q3 and Q4 FY17. Profit after tax for Q4 FY17 stood at Rs. 15 million as compared to Rs. 20 million in Q3 FY17.

Slide #10 provides a balance sheet snapshot. The network has increased to Rs. 2,885 million at the end of Mar 2017 with the merger taking effect. Our balance sheet remains strong with a net debt to equity comfortable at 0.28 times. Please check



Slide #12 provides an update of various industry segments and geographies where we are present. 77% of the revenue contribution in FY17 was from Engineering Design Services while the remainder from Strategic Technology Solutions. (In terms of the industry split, Aerospace, our largest segment, contributed around 39% of our revenue in FY17 and 38% in Q4 FY17. Heavy Engineering accounted for 29.4% of our revenue in FY17 and 34% in Q4 FY17, followed by 23% in Strategic Tech Solutions of our revenue in FY17 and 17.4% in Q4 FY17.

To conclude, our financial performance for the quarter and the year has been muted. However, the skills we have acquired, through our continuous investments, are resulting in high quality deal wins and pipeline. Embedded is an area where we are seeing traction and will be a key growth driver. The MoU's we have signed, proposed JV, depending of relationship across our existing customers and the enquiries we are receiving further drives my optimism towards a promising FY18.

On this note, I once again thank you for your participation. And now request the moderator to open up for questions.

Moderator Thank you. Ladies and gentlemen we will now begin with the question and answer session. We take the first question from the line of Jaikant Kasthuri from Dolat Capital. Please go ahead.

Jaikant Kasthuri Sir, I have few questions, first one is what has been the progress on ACAT, the defense business, if you can give some light on that and on M&A to enhance capability, what is the progress on that front?

Sudhakar Gande On the ACAT, the defense side of business as we discussed, right now we are in the last leg of about four transactions. Two of the transactions are in the range of \$20-25 million, two other transactions in the range of \$65-70 million range. In all these we are in the final stages. We are fairly confident at least some good news should come on this, some of these things take little time, but still we are pretty confident this year we will share some good news on at least one of them or two of them.

Jaikant Kasthuri It is expected to happen by end of this Q1 quarter?

Sudhakar Gande It cannot be that fast, but I am sure it will happen shortly, in next one or two quarters.

Jaikant Kasthuri How do you view the project consulting cost, like when do you see it likely going to taper?

Kaushik Sarkar We have been continuously working on project consultancy cost, we are in-sourcing a lot of activities, especially in the delivery center in India that has reduced, but at the same time, we are taking up some new projects in US where we have to invest initially for couple of quarters and then we will pull it down again. So an investment to start with, once again the competencies will be acquired in-house will then subsequently taper down.

Jaikant Kasthuri Sir, which verticals do you see contributing to the growth in ACET?

Sudhakar Gande In terms of verticals, I will definitely look at a good possibility in Aerospace to continue and in Energy. In the Energy vertical, as you are aware, we have announced joint venture with ASSYSTEM. ASSYSTEM is close to \$1.2 billion company with more



than 13,000 employees and rated very high on technical competence, for example, companies like Airbus look at them as one of the top technically capable companies and we already had some good business understanding and were working with them on an Airbus project, based on that now they requested us to work on the Energy side with focus on nuclear energy. Now, the focus areas in coming years will definitely continue on Aerospace but we will look to scale up Energy as well.

In this joint venture it is very important to understand few things. Government of India has announced nuclear power contract to three countries, US, Russia and France. Each will get six reactors each, France will get six nuclear reactors, US six and Russia six, and each of this nuclear reactors normally cost about \$6-7 billion, it takes about six to seven years to build, so if you start the work today, the first reactor will be delivered in about six to seven years from now. By the time, you deliver all the six reactors, it could be anywhere 12 to 15 years, point number one. These are very large deals because each reactors cost about \$6-7 billion, so we are talking about \$36-40 billion transaction each country will get. In the typical nuclear deal, what happens is in the first phase, they do the design modified to the local condition, etc., so out of each reactor of \$6 billion, phase 1 itself minimum \$150 million is the design work. If I take six reactors, let us talk only about France because as you know the French reactor will be delivered by a company called Areva. Areva has a design contract with ASSYSTEM. That means all the six nuclear reactors which are going to be delivered in India will be designed by ASSYSTEM. Now, each reactor will have a minimum work of \$150 million of design work, so if you take six reactors into \$150 million, it is close to \$900 million, close to \$1 billion. Now, this is a business which cannot be shifted half-way through. Once you start, it will be 12-15 years transaction. Just to look at ASSYSTEM numbers, they have moved from \$40 million Nuclear Energy business to \$400 million per annum in last six-seven years, you can just go through an annual report, and ASSYSTEM is rated as number one nuclear energy for company in entire Europe, and globally among the top two or three. They did a lot of analysis on Indian companies and engineering suppliers, they finally signed up with us. For us it is of very, very strategic importance and we have signed a 50:50 joint venture after a lot of negotiations. This joint venture is going to be path breaking because we are expecting to create 500 people in the next three years and if everything goes well, it can go even up to 1,000 over a period of time. So for us it is one more very strong customer line that. We have Airbus, we have a large Heavy Engineering client, we have Siemens.

Just information to all of you, we are happy to share that the headcount in Siemens has crossed 100 now making us an important part of Siemens strategy to Hyderabad center.

Moderator

Thank you. We take the next question from the line of Aanchal Wadhvani from Quant Capital. Please go ahead.

Aanchal Wadhvani

Sir, I have three questions regarding the new deals and during the quarter, so first, what is the quantum and size of these wins and is this an existing area of expertise or should you expect a rise in sub-contracting expenses during FY18 as a result of these new deal wins and what would be the steady-state EBITDA margins in these deals?

Kaushik Sarkar

Most of the work is outsourced right now, but this quarter we are moving it in-house so you will feel lot of project consultancy costs tapering down from Q1/Q2 onwards.



Sudhakar Gande This customer has potential, in the first year itself, to hit a \$5 million. Other customers we added to this quarter included one very large heavy engineering company, several billion dollars company in size, and we just started the engagement with them. We are utilizing our own expertise here with no outsourcing because we are already working with other heavy engineering clients. Third area where we made a breakthrough is we had got the first client in medical electronics. As you know, medical electronics started sometime in beginning of the year and one of the prerequisites of the medical electronics is you have to design a specific product which needs to be certified and once it is certified then only you can go to a customer, otherwise, you cannot even go to a customer, so we made the product, got the certification done, we just entered the market and are very happy to inform you that we have just got the first client with a huge US company. Of course, scope of work is small. We also made a breakthrough with a company in Middle East which is working closely with one of the large Aerospace companies in the world where we already got an engagement, so we also had a breakthrough with that company in Middle East.

Moderator Thank you. Next question is from the line of Dipen Shah from Kotak Securities. Please go ahead.

Dipen Shah I had a couple of questions, firstly in terms of the ASSYSTEM engineering JV which you spoke about, could you just explain slightly more in detail like how is the work going to be distributed between the JV as well as the parent company and what exact work will be done in the JV, and the second question is how much investments do you envisage in the JV over the next couple of years?

Sudhakar Gande Let me explain this to you. ASSYSTEM, France has a master contract with Areva who is going to manufacture and deliver the nuclear reactors for India. A typical reactor takes five to six years to deliver and install, now that you are asking the details, let me explain a little more in detail. The first phase which is the design work is close to \$150 million per reactor, but as you go along installation, modification, etc., it may go as high as close to maybe as high as \$300 to \$400 million per reactor, it can even go to \$500 million depending on the complication, so I am not looking at that. I am looking at the first part which is like the no-brainer, which is a must, this \$150 million, so the joint venture will become a vehicle for ASSYSTEM to implement this project. Initial technical capabilities will come from ASSYSTEM for us and slowly we will build on those capabilities. The investment will be, at the end of the day this is not a very big investment, of course we have to start off with a facility for 100 people and it may go up to 500 in three years. The typical cost like renting an office, employee hiring, some IT cost, etc. will be there, but these we are working out the details, and hopefully, next quarter we will share the information because we will also have the next meeting where we will announce, how much investment both of us are doing.

Dipen Shah If we understand it correctly the purpose of signing of the JV with AXISCADES is it that they needed an off-shore capability, is that one of the important reason?

Sudhakar Gande There are two things, one is yes, they need offshore capability and also they have to show to the Government of India that they are doing indigenization. Now, let me go one step ahead, how this happened. ASSYSTEM was talking to us on an Energy client, one of the biggest in the world when we started before nuclear, so they wanted us to set up a facility for this client who is one of the most respectable names in the world, this is how we started. Finally, we have agreed that we start working on Energy along with ASSYSTEM and both they came and saw our office etc. Now,



ASSYSTEM and AXISCADES is starting the work some time in next month or so on that contract, on that business which is related to nuclear, because Energy is non-nuclear. We are partnering with them for a large contract in South Africa, ASSYSTEM and AXISCADES, which were going to compete with two other large global companies. When we started six years back, we had zero employees in Airbus, today we have 650 employees, so they could see the scale and how it has been done. For the information of some of you, Airbus is one of the most respected clients in the technology world. When you say they are working with Airbus lot of things get evened out very quick, so their teams came and saw what we had done etc., and decided we can work together. This is not going to end here, ASSYSTEM and us, we are going to look at even US market in a very big way after this transaction.

- Dipen Shah** ASSYSTEM Engineering is also working with Airbus right now?
- Sudhakar Gande** Yeah, if you look at top five vendors of Airbus, ASSYSTEM is one of the top three, they do more than \$150 million.
- Dipen Shah** That is the next one, how do we expect the Airbus business to scale up from our angle?
- Sudhakar Gande** That is a good question you asked me. We are very happy to tell you we just cracked China, they have just selected our company as partner for Airbus in China beating about six-seven large global companies. Second, we just started work in UK with Airbus which was not the case earlier and we are taking away some work from our other competitor company. Third, our work has been predominantly in commercial aircraft till now and a bit of defense, and little bit on helicopters. Now, we are going to expand helicopter also in a big way, they have started working on that.
- Dipen Shah** This work we are doing along with ASSYSTEM or this is our own individual contract?
- Sudhakar Gande** For example, the UK part little bit we do with them, because they have capabilities which we do not have, other than that completely we are on our own whether it is China or helicopters, everything on our own. Our model is very simple, our model is where we do not know fully, we collaborate, we take the best guy to help us whatever cost it takes, but we are smart enough to make sure we solve it at the earliest.
- Dipen Shah** How do we do the scale up in Airbus in terms of number of employees just as we are looking at the ASSYSTEM JV to be 500 employees, how do we see Airbus?
- Sudhakar Gande** I can only tell you one thing, if you look at historical data, in Airbus suppliers, the last two years everybody's volumes have decreased. We are the only company whose volumes have gone up by more than 20% from Airbus, you can verify that through whichever source you would like to have.
- Dipen Shah** How do we see the profitability in both these businesses, the Airbus business as well as the ASSYSTEM JV, will it be very similar to our own existing business or it should be higher?
- Kaushik Sarkar** The Engineering Services business we intend in the long run to go at somewhere between 15-18%, we have been consistently speaking about that. We had made an investment in FY17 in leadership or building competencies, and that is why our margins are low in that business, but sooner or later that will turn around that is the first part of the story. For the other business, the Strategic Technology Solutions



business, the margins are generally higher, wWe anticipate , I cannot give you the exact number, anything around 20%.

Sudhakar Gande

One important thing also I want to share with you guys is some of the business opportunities that come, we move very fast. For one of our Heavy Engineering clients, they needed urgent requirement in one location. We built a team from zero to 200 in less than one year and we had margins as high as 30-35%, so in next two years, all the 10 Indian companies reached there, so our margins are down to some 10-12%. The same thing happened with one of the subsidiaries of Airbus when we started working, we moved from close to 8 to 88 people in one year and we had margins of 35% plus, but that lasted about two-three years. Then a lot of other giants come in, so now my margins are down to 15%, so we are looking at opportunities. For example, in one of the top heavy engineering companies, we are working on a proposal where they want to centralize their manufacturing operations in US. It talks about closing close to 25-30 plants and moving everything to the State of Arizona because the State is giving close to \$1 billion of concessions, capital etc., so the number of jobs at stake are 1,000 plus and you know typical Americans, nobody moves so easily from some place to go to Arizona and all, so we have given a proposal that we will do the delta that means whoever does not come, we will put our employees, we are opening an office there and we are moving fast. Of course seeing us, two-three other companies have moved, but we are already ahead of the curve and I had a personal meeting with the CEO of the company where they liked this whole idea, so we moved. When we are moving like this, nobody is bothered about margins, everybody wants availability. Once it gets stabilized, of course, your margin comes down.

Dipen Shah

How many employees do we have currently and what is the total number of the clients which we serve today?

Sudhakar Gande

One important thing I want to share with all of you is the fact, we had just one client, one heavy engineering giant and then we added one aerospace client. Today, we have close to 16 large marquee customers; it took us five-six years to reach here.

Kaushik Sarkar

To answer your question, we have around 1,800 people on our rolls and if you want the concentration, around 88% of our business revenue comes from top 10 customers.

Moderator

Thank you. We take the next question from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria

Sir, could you please give us some update on the heavy engineering business where you had faced some client specific issues?

Sudhakar Gande

As you know, one of the large heavy engineering customers with whom we have been working, they had difficult times for last few years, but the good news is last quarter they turned around which is evident, all along we have been asked to reduce the manpower, so first time we have been asked to add the manpower. As far as we are concerned, the worst is over for heavy engineering customers, and we see a real traction this year on this.

Gaurav Rateria

This year it should start growing you are saying?



- Sudhakar Gande** Definitely, this is the first time it will have a growth in the last four-five years because numbers and the company's forecast, etc. all in the right direction, so the worst is over, so they will start moving in the positive direction.
- Gaurav Rateria** Sir, within Aerospace how concentrated that portfolio is between few clients and apart from Airbus, which are the few large marquee clients which could potentially become as big as Airbus?
- Sudhakar Gande** If you look at aerospace in the whole world, there are only four manufacturers of aircrafts, we deal with Airbus who is number one. Now, this year we are expanding, we also deal with another company in North America which is number three in the world in manufacturing aircrafts. We have been historically working with them on one specific line of business. Now they are restructuring the entire vendor portfolio and I am very glad to inform you that we have been asked to bid for two more lines that means, family line it is called, that is one line of business, from one we are moving into three and my team right now are giving the final presentations. I see a good traction on that. Right now, we work with Airbus, we work with Premium AEROTEC, we work with a Canadian company.
- Gaurav Rateria** Sir, apart from the manufacturers how difficult or easy for you it is to diversify into the engine manufacturing companies and the Tier-1 suppliers of these manufacturers based on your existing capability?
- Sudhakar Gande** The engines as you know, are only done by either Rolls Royce or Pratt and Whitney or GE etc., they have not yet come to India in a big way as far as the engines are concerned, I see some more time before it happens. Now, Tier-1s are relatively easy to work with, but some of those can get scared. For example, we were working with one of the large manufactures in US, we were working with Tier-1. The Tier-1, the manufacturer itself called us for one of the meetings, so we had to work it very closely and balance it with them like in the sense, some of the areas we work together, some of the areas we compete and I see two-three large Tier-1 coming to India in a big way. We have meeting with one of the companies whose revenue is close to \$14 billion out of which \$3 billion they just do with Airbus, so they are expanding in India in a very big way and we have been having discussions with them, but I see very clearly there is a business coming from Tier-1 in the coming years.
- Gaurav Rateria** When you say they are coming to India does it mean they are opening their captive centers and they will be expanding with the third parties also?
- Sudhakar Gande** Yeah, two things happen, what typically they do is first come and open captive center, so you get a chance to work with the captive center, but once the captive center is happy and you get access to the guys at the head office level, they start looking at you. Of course, the captive has never liked you talking to the bosses there, so you have to again be politically right, you have to make sure you work with the captive to some extent because if you go directly to the main guy, captive center's relevance will come down, so always we have to work, balancing it out within these two guys.
- Gaurav Rateria** Sir, one question on the Strategic Tech Solutions which you disclosed, how different it is than the engineering design services from a nature of the work and design of the contract and especially also does the IP belong to you, that is why you call it solutions, just wanted to understand it better?



Sudhakar Gande

Let me explain that; Engineering Services is a lot more easier and plain vanilla deals relatively. In Strategic Technology, you are marrying electronics and mechanical together. For example, we manufacture automated test benches for two large global suppliers, so when you make an automated test bench, there are something like 10-12 Indian companies, we work with them as subcontractors that means you have access to some 1,500-2,000 employees available from various companies to work on this, I encourage all of you to come and visit one of our facilities to see where a test bench is made, it will be really revealing. There are so many thousands of parts, components, everything has to be integrated, so the automated test bench is a classic example where you marry electronics with mechanical and once you get in, very difficult for them to replace you because not many people can do this. Second is Engineering Services contract historically, barring few exceptions, most of the deals are smaller, \$1-3 million, etc., but numbers here are far bigger. Suppose you become a part of the offset contract of a large company, it will be \$50 million, for example, we are doing automotive bench for one European company, our contract value is about \$3 million, we have to give about three to four machines, so in a very nutshell, this is more complicated business, extremely difficult to replicate, larger margins, and more repeat business and larger size.

There are two opportunities in the Strategic Technology businesses, what happens here is if you are a part of selection of offset contract, it is like a project for next five years. Second, most of these businesses are foreign related, you will never do T&M. If you are doing automated test bench, the contracts are fixed price. For example, we are now working with a global customer where our CAPEX is 1.5 units at any point of time, that means I can do 1.5 units. Now they ask us to increase to 6 units because we are working on a contract for Rafael aircraft in three different countries, so whatever I make whether it is India or Egypt or any other country, it is the same because aircraft manufacturing is same, automated test bench will be same, so it is a process driven, larger contracts, difficult to replicate. Further, I will give an example, we were working with a global company in X, it took us five-six years to build a relationship, deliver this automated test benches for a bit of five-six years, they were very happy. The second client took us less than 18 months. The three teams came and the super boss of that company came, one of the large companies in the world, luckily one of our test benches were ready to deliver, it was there. This gentleman, head of technology for the entire global company, who was supposed to spend one hour, he spent three-and-a-half hours with our team. He was completely into it. I also had dinner with him in the night then he told me Mr. Sudhakar, I felt I was in my office, so this is the statement he made. It is slightly different business, but it is interesting business, but finally what happens some of the clients become common for both these products. If somebody manufactures aircraft, he needs design; he also needs automated test bench.

Gaurav Rateria

Sir, just to understand better, does it mean that you do some amount of manufacturing-related work here along with embedding the design work?

Sudhakar Gande

What happens is we are system integrators. Final product goes in our name, we sign off, we know some manufacturer which outsources it to third party, it is subcontracted.

Gaurav Rateria

All of the manufacturing will be subcontracted or do you do it in some part of it...?

Sudhakar Gande

Yeah, we will not do much, everything is subcontracted. The beauty of this country is lots of mid-sized companies are there. They will not get access to the global company because they are smaller, they cannot take the risk or they cannot expand.



One company in Chennai, about 20-year-old company, they are in precision engineering. They are absolute precision, so when we took the global company and went to this company, they were shocked. They said that is such a good technical company in this country. He said that some of these are better than even French companies. We have taken them as part of our system, so anything you have to do precision engineering, you outsource to them.

Gaurav Rateria Sir, is it similar to something like what one of your peers is doing in terms of design-led manufacturing contracts where they have acquired the manufacturing capability themselves?

Sudhakar Gande Let me explain, there are two things here. Lots of companies in Aerospace industry are trying to move into this, they are asking you please quote design and manufacture; they are putting the risk on your head saying that you have to give the final part and component. We are not in that game because manufacturing is a very serious business; it has its own requirements. We will do design and I can tie up with the manufacturer, so they are not in that. Engineering manufacturing is different from this electronics.

Moderator Thank you. Next question is from the line of Saurabh Mehrotra, an Individual Investor. Please go ahead.

Saurabh Mehrotra The first question is what was your attrition rate in the year that just went by and the other question in the last quarter or some months back, we just had a joint venture with the Airbus, now will this remain the same as what it was before say two or three years back or is this worth more or is it something that we have gained more in this year, for example, we were a Tier-2 vendor and now we are a Tier-1 vendor, could you elaborate a bit on that?

Kaushik Sarkar The attrition rate annualized is around 16%, somewhere between 15-16%.

Sudhakar Gande Some of the specialized areas attrition is as low as 4-5%, people do not leave.

Kaushik Sarkar Most of our attrition are not all are critical people, they are for long period of time, so that is not an issue from our side, it is only happening in the very, very junior level some of the fresher's we hire to broaden the pyramid, we see some attritions out there and we do not mind it.

Saurabh Mehrotra Could you clarify on that Airbus agreement, is it larger in scope, is it something that we have moved from being Tier-2 to Tier-1?

Sudhakar Gande We are always Tier-1 and continue to be Tier-1 even in this contract, point number one. Point number two is, this is an international bidding, they had got several companies worldwide bid for it and I am happy to say that technically and commercially we are rated in the best among the best. Of course,, pricing we have to do our own pricing to make sure we still make money, so the commercials I cannot share with you whether I am reducing the price or increasing the price, but one most important thing you have to understand is our scope has been enhanced, expanded which is a very big thing for us because in our line of business, when you have four suppliers getting work, if one guy gets little more than others, that is a big thing for us, so we are very proud to state that our scope has been expanded, that is where we got into UK, earlier we were not there.



Saurabh Mehrotra You said you got into China as well, very recently?

Sudhakar Gande One more thing happened is that they also added defense to our scope, primarily we are very, very proud of this achievement and a lot of work has gone into this to create this.

Saurabh Mehrotra The other thing is I joined a bit late, so I am sorry if I am repeating the question, but what would be our guidance for revenue and for margin for the current year? One question is on where do you do all the design that the previous person asked and do you outsource the manufacturing? Is there any space for integration with 3D printing, if so, where are we on looking at it?

Sudhakar Gande First, as a policy we do not give any guidance so I cannot share with you at this point of time, maybe sometime later. As far as the 3D printing is concerned, it is a very interesting area. We are already working on one specific project, design which goes into printing, we just started working on it and one more large Indian company is working with us, but once we are ready to share some information, we will be happy to tell you.

Saurabh Mehrotra Do we have any targets like you mentioned somewhere that our margin target is 15-18% or towards aiming for, any rough idea go in to the year where we have any plans to reach that target?

Kaushik Sarkar I think this question came up earlier as well and we again we have tweeted that our endeavour is to get into 15-18%. FY17 we made a lot of investments in Engineering Services that is why margins are low. We will see the upturn in FY18. For the other Solution business, the margins I told is more than 20% depending on project to project.

Saurabh Mehrotra What is the CAPEX that is lined for this year seeing that we are getting into new joint ventures and new areas, any guidance on that?

Sudhakar Gande We cannot give you the exact figure, but we are working on it possibly in the next call, because the joint venture is going to work out all the details, possibly next time we will be able to share what are the CAPEX requirements of the joint venture.

Kaushik Sarkar It is not highly CAPEX intensive, generally we have all the computers and other stuff and I do not think a lot of investment in CAPEX.

Moderator Thank you. We take the next question from the line of Sumeet Jain from Goldman Sachs. Please go ahead.

Sumeet Jain Firstly, I wanted to know the recent contract you have won particularly on the Aerospace side, can you comment on the nature of those contracts in terms of the duration of those contracts and when will they start hitting your revenues in which quarter and are they more fixed price or T&M in nature?

Sudhakar Gande They are completely project based with a global major. There is no T&M, it is completely fixed price. This is a three-year contract and it is fairly large by normal industry standards.



Sumit Jain Typically how is the revenue realization from these contracts, is it more towards the second half of those contract duration or more initially, how do you recognize them?

Sudhakar Gande By and large it is even over a period of three years, there will be little bit 5-10% variation here and there, but largely same.

Sumit Jain I can see the proportion of fixed price and time and material for you guys like time and material is really high at 64%, so is there any conscious shift towards the fixed price contracts and is it a low-hanging fruit in terms of margin improvement?

Sudhakar Gande No, what happens is, there are two things here. Companies also do not gear up very quickly on fixed price, but companies are technically more savvy and more advanced, some of them have already moved in. We are now working on some of the customers which have been T&M, we are trying to move part of the business to the fixed price, so there will be trend, but it will take some time.

Kaushik Sarkar How it happens is since we are diversifying and acquiring new customers both in India and overseas, our Indian strategy is to stop with T&M and then move into projects, so you cannot get a project in day 1, so what happens is you put around 5-10 people and slowly over a period of six months to nine months or even a year, you convert into projects, that has been our success *mantra* over the years.

Sumit Jain Do you guys have any long-term vision as to any of your revenue or margin targets in next three to five years reason being I mean the Engineering Services were pretty difficult to scale in the long run and it is more dependent on the individual client related projects, so any thoughts on that?

Sudhakar Gande At the end of the day, margins as you mentioned engineering will be within 15-18% and Strategic Technologies is around 20%, of course, sometimes it is more than that, but if you ask me as a company overall, we should be aiming a margin about 18% over a period of time, which is stable and is possible.

Sumit Jain Any revenue targets you have in the long term?

Sudhakar Gande I do not want to comment on revenue target at this point of time, but once we are ready to announce the guidance etc., we will be happy to share with you.

Kaushik Sarkar The other thing just to get back to your question, we have the other wing, Strategic Technical Solutions business where most of the contracts are fixed price nature, so over a period of time in any case, we will see more fixed price contracts for us, but I have given you the business inside, how we do it, so that you understand better.

Sumit Jain Are fixed price projects typically higher margin in nature over longer term because of the productivity you can achieve and all?

Sudhakar Gande Absolutely, you are right, spot on.

Moderator Thank you. We take the next question from the line of Gaurav Rateria from Morgan Stanley. Please go ahead.

Gaurav Rateria Sir, you talked about winning a contract in Airbus account from one of the key competitors, could you highlight who are the Tier-1 vendors both offshore and even



at onsite for these large accounts and how disproportionately large or small your share is with respect to your wallet share in this account and how much further it can go up to?

Sudhakar Gande As I said, we have won from other competitors working with Airbus. We got a part of that business, which is very important for us for expanding the scope. That piece of business will be not very big, not very small, it is a reasonable size, I cannot give the exact details, but it is a reasonable size, but it is very important for us because of the new line of business with the company and also new location so from strategic point is also very important for us.

Gaurav Rateria My question is actually to understand which all companies are Tier-1 suppliers, who do we compete with for such contracts and what is our wallet share?

Sudhakar Gande At the end of the day, globally Airbus has finally announced 16 companies as Tier-1, they bought down this 28 to 16 in last five years, so all the business is only given to this 16 companies, they are all listed in Airbus site, you can go through details, they are only few Indian companies are there,, so whatever work they give they will be confined to this. For the contract we won, what is called ODC, Overseas Development Center, where all these guys are competing and finally we have been selected for two lines of business, fuselage as well as defense.

Gaurav Rateria Second question on the margins front how easy or difficult it is to move margins in one year, is it going to be more revenue led because you have already made the investments and revenues will take care of the margins or is it going to be more around, you are going to rationalize the cost and hence that margin recovery will be far quicker?

Kaushik Sarkar It has to be a combination of both I will say, yes those solutions business, the margins are higher so we aim to get more of those, but at the same time on the cost side, we have levers like utilization where we want to move into around 70% minimum blended, then the rolls ratio of the pyramid, we strongly strive to have the pyramid in place. The other thing is improvement of number of shifts as well as how you utilize your licenses, some of the aerospace business, the license are very costly, so those are the levers we have plus we have possibly capacity to grow around 15-20% more on the existing facilities, so those are the levers we have to improve our margins going forward.

Sudhakar Gande At a macro level, actually I want to leave two-three points for all of you to review. Engineering Services is a business very close to heart of manufacturing. They do not outsource so easily, but now you see a trend. For example, I was told based on various reports, in US alone there are more than 900 companies which can outsource engineering to Indian companies outside US. Out of 900, only 225 are outsourced, the balances are yet to outsource. Out of the 225, maybe some 50 or 100 are outsourcing at a reasonable level, the rest of them they outsource more out of the existing business. This is on one side of our business. Other side of business of Strategic Technologies, as you know the Government of India is placing orders for several defense, aerospace contracts whether fighter aircraft or submarines or tanks etc., all of them have components which is offset which is done in India, so there are very few companies in India who were able to capitalize on this opportunity because you have to be groomed, you have to be trained, you have to be certified, you have to be tested, so there are very few companies which fall in the category, and I am very proud to say we have done our bit to be one of them because we worked very, very closely with couple of global majors, and working with these guys



is not easy, they will have so many orders, so many reviews, etc., but it is interesting. Once they like you, scaling up is very, very easy. Given this large contract India is facing now, very few companies have really benefitted out of that and we are pretty sure, we will be one of those companies who should be benefitted on the larger scheme of things.

Gaurav Rateria

Sir, what portion of that Strategic Tech Solutions is part of the offset related contracts?

Sudhakar Gande

Strategic Technology, we have two lines of business. One is you do an offset contract, part of a global OEMs deal you are one of the companies involved in the deal as an offset partner. Other thing is we directly bid with the Indian defense. For example, as a company we won three bids in last four years in the international competition, three bids we won and some of them we hopefully we should be filing some patents also and these are all which we fought against Israelis, Americans everybody, so currently our business is little more towards offset versus in direct bidding, but the important part is when you work with the global major as an offset partner, the similar product, for example, we do automated test benches, the similar product is required by the global OEMs all over the world, so in one of the cases, we learned with them a whole bit of in India and finally they made us as part of global supply chain. The moment you become part of the global supply chain, it is for eternity, right now we are working externally to make sure that what piece of action we can get but even I am hopeful that some of these things could end up with a \$10 million a year on the current \$4-5 million, but this is for eternity because as long as the company runs and the products are required globally, so that is one very good thing happened with this, when you do an offset contract, win their competence you will be a part of global supply chain then you have an annuity business.

Gaurav Rateria

Sir, you talked about that joint venture and the nuclear reactors and also highlighted the design component of \$150 million per reactor, when do you think, this \$150 million is something which will be taken entirely by the joint venture or part of that will be taken by the joint venture ...?

Sudhakar Gande

These are the details we are working out, but most of the work need to be done in joint venture because everybody is cost competitive. The work what we can do in India will be less costly as well as we will learn the skills, so initially it may take little extra work there, but eventually lot of work will move in here, so there is a benefit. The joint venture, my guess is will do most of the design work over a period of time, to what quantum and all, we will share maybe in next couple of months once we do the joint venture plan, we will definitely have a conference or analyst meet to announce the details because this is very, very strategic in nature both for the country and for us that and I see this as one of the strong businesses in the coming years.

Gaurav Rateria

From a timeline perspective what are the milestones you are looking for this to happen...?

Sudhakar Gande

First what happens is already Government of India and Government of France has signed the agreement saying that they have to deliver six reactors. Now ASSYSTEM has already signed an agreement with Areva who manufacturers that they are the design partner and ASSYSTEM has announced the investment of 5% into Areva actually as part of the deal. So ASSYSTEM is bound to get this work, there is no question on that and the joint ventures will automatically get the work. When the revenue start I will not be surprised it starts in next two-three months in the August-



September as the timeline is indicated but once we do the detailed plans, we will let you know, but it is not too far, may be September.

Gaurav Rateria

Basically this year itself?

Sudhakar Gande

Yeah, they are under pressure, they have to deliver, they have deadlines when to deliver. Sometime in September-October I cannot pin-point, but I will tell you may be after two-three months when we are ready with the plan. One point I want to tell you is that while Nuclear Ministry will take some time, couple of months, we are working on the Energy vertical with ASSYSTEM already for the US client, which will start in a month's time.

This is a classic example of international competitiveness, the moment the joint venture is announced other than nuclear business, I do not want to name the country, there are some other countries, there are close to 50 people working and they do not see much scaling up there, they already spoke to me saying, Sudhakar, can we move this to India, I said most welcome, so it might end up with they are closing shop somewhere else to put this here.

Gaurav Rateria

The nuclear work whenever it comes, what is the nature of the work, the nature of the work will be immediately a large chunk will come like \$100 million kind of a contract or it will be like few number of people will start the work and then eventually you will ramp up the number of people?

Sudhakar Gande

This will be one of the fastest ramp ups in joint ventures in ODC, we are talking about 500 people in three years. It took us five years in Airbus to do 500 people, so this is superfast.

Moderator

Thank you. That was the last question. I now hand the floor over to the management for their closing comments.

Sudhakar Gande

I would like to thank all of you once again for participation support. We look forward to interacting with you soon. Thank you very much.

Moderator

Thank you. Ladies and Gentlemen, on behalf of AXISCADES Engineering Technology Ltd., that conclude today's conference. Thank you for joining us and you may now disconnect your lines.

