L&T Technology Services
Q3 FY23 Earnings Conference Call Transcript

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MANAGEMENT: **MR. AMIT CHADHA – CEO,**
MR. ABHISHEK SINHA – COO,
MR. RAJEEV GUPTA – CFO,
MR. PINKU PAPPAN – HEAD, INVESTOR RELATIONS

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Moderator: Ladies and gentlemen, good day, and welcome to L&T Technology Services Limited Q3 FY23 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0'on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Pinku Pappan, Head of Investor Relations. Thank you, and over to you, sir.

Pinku Pappan: Thank you, Faizan. Hello everyone, and welcome to the earnings call of L&T Technology Services for the Third Quarter of FY23. I am Pinku, heading Investor Relations. Our financial results, investor release and press release have been filed with the Stock Exchanges and are also available on our website, www.ltts.com. I hope you have had a chance to go through them. This call is for 60 minutes. We will try to wrap the management remarks in 25 minutes and then open up for Q&A. The audio recording of this call will be available on our website approximately one hour after this call ends.

Let me now introduce the leadership team present on this call. We have Amit Chadha - CEO; Abhishek - COO; and Rajeev Gupta - CFO. We will begin with Amit providing an overview of the company's performance and outlook, followed by Rajeev, who will walk you through the financial performance.

Let me now turn the call over to Amit.

Amit Chadha: Thank you Pinku and thank you all for joining us on the call today. I hope all of you are keeping healthy and safe.

Let me start with the key highlights on our **Q3 performance**:

- Our deal wins were strong this quarter with 5 deals greater than $10M in TCV and a significant empanelment from Airbus for which we have also issued a press release today

- From a revenue standpoint, sequential growth was muted this quarter due to seasonality and higher than expected impact from furloughs, especially in Plant Engineering.

- Inspite of this, we have improved EBIT to 18.7% and crossed the ₹ 300 Cr milestone in Net margins per quarter.

- From a Technology standpoint, we surpassed the 1,000 Patents filing mark as an acknowledgment of the Tech Prowess of LTTS.

Let me now provide the segmental performance and outlook.

Starting with **Transportation,**

- We had a good performance with 4.4% QoQ growth that was broad-based across the sub-segments - Auto, Trucks & Off-Highway (T&OH) and Aero.
- In Auto, demand is being driven by electrification, connected cars and next-generation digital cockpits. We are also seeing increased demand for cybersecurity as part of the software development platform work that we do.
- For Trucks & Off-Highway, similar trends of electrification and platform development continue to provide us good opportunities. One of our 5 $10M deal is from this area.
- In Aero, driven by the rise in air travel, we are seeing demand for avionics. I want to highlight our selection by Airbus as a strategic engineering partner – This empanelment is significant recognition of our Digital engineering capabilities and Aerospace domain knowledge.

The growth in Transportation will continue into FY24.

In **Plant Engineering,**

- We were expecting a muted quarter, as we had indicated in our Q2 commentary. However, the unexpected furloughs at some of our top customers led to a weaker than expected performance in Q3.
- I want to highlight that this is a one-off and not a reflection of the demand environment. We see growth coming back from Q4 onwards.
- Key drivers of demand are localization of supply chains, sustainability in operations including energy, water and waste management leading to greenfield/brownfield expansions.
- In the O&G/Chemical sub-segment, many of our customers are continuing to change their product mix leading to design and digital engineering projects for us. One of our $10M wins has been in this area.

We see a strong deal pipeline in both US, Europe and Middle East that will help drive growth for us in Q4 and beyond.

At **Industrial Products,**

- We had a good growth in the quarter led by Electrical, Machinery and Power and Utilities.
- For Q3, three of the 5 large deals that we won were in Industrial Products in the areas of digital twin and sustainability-driven product development, innovation and research.
- We see good demand in Digital Manufacturing to support automation and Software platform development to improve equipment performance and reliability. These in turn will become annuity contracts.

- We have been talking about energy transition, including green energy initiatives using Hydrogen as a fuel, creating new opportunities for us.

Overall, for Industrial Products, we see growth continuing to be driven by digital manufacturing and sustainability-led new product and process development.

In **Telecom & Hitech**,

- We had a challenging quarter due to the weakness in ISV, Consumer Electronics and Semiconductors - where customers are spending less and frozen hiring. We did offset some of this weakness from better 5G spends.
- We are seeing growth in 5G lab-as-a-service, network engineering and cybersecurity. With SWC, we now have an end-end capability that will give us an edge in the market.
- As customers look to squeeze efficiency, we are also seeing Cost takeout deals in the pipeline. These could give us an opportunity to consolidate and provide greater value to our customers.

Overall, we expect the pace in Telecom and Hitech to gradually pick up as the environment improves.

Lastly, in **Medical**,

- We had a soft quarter which has had more to do with customers shifting their spend to 2023.
- Demand is being driven by Connected devices and digital health platforms, cybersecurity, regulatory compliance and QARA.
- In Q3, we won a large deal from a global OEM to assist in engineering solutions for their medical devices on annuity basis.

We see growth in Medical in Q4 picking back up based on our wins and good pipeline.

Now a few highlights on our **Digital engineering and Technology progress**.

- On the innovation front, our engineers continue to innovate and have filed 25 patents for us and 30+ for our customers in Q3.
- We have been able to maintain this pace of about 25 + 25 patents per quarter for 7 quarters now.
- We are also proud that we've crossed 1,000 patent filing mark.

Let me now discuss the **Outlook.**

- As we highlighted last quarter, there was a caution in spending which played out in our Hitech segment.

- Coupled with the furloughs in Plant Engineering, we had a muted Q3 in terms of revenue growth. However, we are optimistic about growth coming back in Q4 on account of
  - The 5 deal wins and the significant empanelment with Airbus that we won
  - A growth bounce back at Plant Engineering in Q4 with the furloughs behind us.

- We are now looking at FY23 USD revenue growth to be around 15% organic, on constant currency, using Q4 FY22 currency rates as baseline.

- Finally, as we start the new year, we are having conversations and deal discussions have picked up pace over the last few weeks. Therefore, Q4 will see us adding at least 500 net headcount in order to get ready for FY24 as well as service Q4.

I now request Rajeev to walk you through the Financials.

Rajeev Gupta: Thanks, Amit. Good evening to all of you and hope you're doing well.

Overall, our Q3 FY23 performance showed another quarter of double-digit revenue growth on a year-on-year basis, good operational execution resulting in improvement of EBIT margin and crossing a new milestone of ₹ 300 Cr in Net profit.

Now let me take you through Q3 FY23 financials, starting with the P&L.

Our revenue for the quarter was ₹ 2,049 crores, a growth of 2.7% on a sequential basis. Our double-digit YoY growth trajectory continues with Q3 revenue up 21.4% on a YoY basis.

EBIT margin at 18.7% increased by 60 bps compared to Q2 FY23. This has been the 6^{th} consecutive quarter of 18% plus EBIT margin.

During the quarter, we had benefits from improved employee productivity, better offshore mix and exchange gains, offset by a slight increase in SG&A%.

Moving to below EBIT

Other income came at ₹ 62 crores, higher on a sequential basis due to higher foreign exchange gains compared to previous quarter.

Effective Tax Rate for Q3 was 31.5%, higher due to conclusion of certain past year assessments, we expect this to stabilize in the 27% range going forward.

Net income touched a new milestone of ₹ 304 Cr at 14.8% of revenue and up 8% on a sequential basis, driven primarily by operating margin improvement.

Moving to Balance sheet, let me highlight the key line items.

DSO improved to 77 days at the end of Q3 compared to 78 days in Q2. The combined DSO including Unbilled improved to 94 days compared to 96 days in Q2, and in our target range of less than 95 days.

Let me now talk about cash flows – Our YTD Free Cash Flow was ₹ 826 Cr, at 96% of Net income.

Our cash and investments rose to ₹ 2,652 crores by end of Q3 FY23.

Moving to Revenue metrics:

On a sequential basis, $ revenue was flat on a constant currency basis and up 0.4% in reported terms, mainly led by Transportation and Industrial Products segments.

The segmental margin performance was better in all the 5 segments on a sequential basis led by Plant Engineering and Medical Devices.

Now let me comment on operational metrics:

The Onsite:Offshore mix has shifted towards offshore and is at 57%. Our aspiration is to improve this ratio to 60% level in the medium term.

Client profile – which indicates the number of Million dollar plus accounts – has shown a sequential improvement in the $10M+, $5M+ & $1M+ categories. The client profile numbers have seen an improvement over the past few quarters, and this trend will continue in the coming quarters.

In respect of client contribution to revenue, all three categories, Top 5, Top 10 & Top 20 have shown a slight decline as compared to Q2, which is due to stronger growth in Top 20-30 accounts.

Headcount improved sequentially by 175 employees, while Attrition moved down to 23.3% and is showing signs of softening.

We continue various employee engagement measures to manage attrition.

Realized rupee for Q3 was around 82.6 to the dollar, a depreciation of over 2% compared to Q2.

I would now like to hand it over to Amit to spend a few minutes on our recent SWC acquisition. Over to you, Amit.

Amit Chadha: Thanks, Rajeev. I hope it is clear there seems to be some disturbance in the line, so I just pushed on.

The **SWC acquisition** is a significant move, deliberative and thought about and thought through to add capabilities, solutions, technology and most importantly, pre-qualifications that help us getting qualified for large deals in the Communications segment

Post our call on the 12th, where we shared initial details and rationale of our acquisition. We received feedback and queries from you.

We would like to acknowledge and thank you for the feedback. The queries were in three broad areas:

1) How are we going to achieve the turnaround of shifting the business to services?

2) What are our integration plans and

3) What is the roadmap for revenue/margins for this business and the company?

I shall address the first one, and Rajeev will address the subsequent ones.

Starting with **How will we achieve the turnaround?**

We go down to basics. SWC business is broadly, three parts, **Communications, Smart Cities and Cybersecurity**.

On **Communications**, which is a space in which LTTS has a solid presence – with a customer base of 6 of TOP 10 Telecom Infra OEMs and 4 of top 10 Telecom Operators in North America and Europe. We are going to leverage this customer base and our global sales engine and reach to sell these capabilities.

Let me divide the target market into two subparts. 1) **Enterprise** and 2) **Telecom** which includes Operators and Telecom Infra OEMs.

Within our **Enterprise** customer base, there is a demand for SOC, NOC, private 5G and localized datacenters. The competition is also fragmented here and the spending is also increasing. SWC now fills the critical gap of SOC, NOC and a greater and stronger 5G capability. I wrote to our TOP 100 clients about the acquisition after we announced it, and 55+ clients have confirmed interest in our expanded service offerings. In addition, we will leverage our partnerships with Qualcomm, Nvidia and Mavenir as well as our other hyperscaler relationships to penetrate the market faster.

Within **Telecom**, there are huge spends around network engineering where we now have both scale, onsite offshore model to offer cost arbitrage and track record or *pre-qual* as it's known in the industry - which is extremely critical in discussions and large deal processes. We will also work with our Indian customers and offer a more service led model around Core and RAN capability with the expertise that SWC and LTTS together possess.

In summary, for Communications, the LTTS heritage portfolio of around $60M combined with about $100M from SWC will together be a $160M business unit, henceforth referred to as **Next Gen Communication**. Both portfolios will grow going forward. The heritage LTTS portfolio will see accelerated growth as we offer SWC capabilities, while the SWC portfolio will keep growing at a slightly less pace as we change positioning to more services, for which the current pipeline and client relationships gives us a lot of confidence. The joint power of solutioning 5G use cases across a broad spectrum and technical assets like the *gEDGE* data center, 5G lab-as-a-service gives us the confidence that the combined portfolio will be transformed to be largely Service-led.

Moving to **Sustainable Spaces**

SWC brings capabilities in Efficient Campuses and Cities, Utilities, Mobility, Public Safety and Environment, while we have expertise in smart buildings. LTTS has tie-ups with Microsoft and other hyperscalers.

We have consulted experts who have validated that there is a sizable spending due to COP27 commitments from governments in US, Canada and Europe. We also spoke to our Top 100 clients who have expressed interest in our joint capability that they would like to leverage in their plants, to improve their sustainability and digitization quotient.

SWC's *Fusion* platform, coupled with our *i-BEMS* and *UbiqWeise* platforms along with their software foundry in Hyderabad will help us accelerate solutions that can be commercialized for customers. Additionally, their **integrated command and control centers** that have been built for cities is a real differentiator for us.

We will take SWC solutions to the US and Canada and select countries in Europe, Middle East and Asia, leveraging our existing footprint. We will have a direct sales team as well as leverage our extensive Partner network to expand these markets.

We will have a combined portfolio of around $40M, which is ~$30M from SWC and $10M from heritage LTTS. We expect an accelerated growth for the combined portfolio as we target our enterprise customers and new markets that are ready for such solutions at scale and transform from a master system integrator to a master software solutions player in this space.

Finally, on **Cybersecurity,**

We will leverage the SOC in Chennai from SWC along with the talent that both of us have recruited in respective companies. We have multiple ongoing engagements in Cybersecurity and the SWC team and leadership is a shot in the arm for us at the right time.

With SWC, we will be uniquely positioned to offer full lifecycle threat management, OT, Product, IIoT and enterprise security.

We are looking at almost tripling our combined revenues of $10M currently, over the next 2 years.

So the key messages that I want to leave you with around the ability to turn this around and grow are:

1) We have done our diligence, consulted experts and engage with our customer base on how our expanded capabilities can help them. Our global reach, existing strong relationships with Telecom Operators and Telecom Infra OEMs gives us confidence of growth.

2) We will transform the SWC business from being a master systems integrator to a master software solutions player.

3) Both SWC and LTTS portfolios will grow year after year, and together, we will grow the combined portfolio at a pace faster than company growth.

4) Another added synergy benefit that we will be able to leverage is a 360-degree partnership that will help us expand our relationship with Industrial Products customers or discrete manufacturing customers as they are vendors to our Sustainable Spaces business.

5) Finally, I would like to confirm that we have the leadership bandwidth to take up this integration and are excited to take this opportunity forward.

I would now hand over to Rajeev to address the Integration plan and our Revenue/Margin roadmap. Rajeev?

Rajeev Gupta: Thanks Amit.

Let me address: **How are we planning the integration?**

- The pre-integration exercise has been kicked off. The senior leadership team of both companies are planning for joint delivery and GTM.

- We will run an integration program for the next 180 days that will focus on 6 areas.

  - Top Line, Service Lines, Technology roadmap, Enabling Functions, Bottomline, Working capital and Cashflows.

- We are setting up an Integration Management Office with a full-time integration leader reporting into me.

  - The integration management office will be responsible for ensuring readiness on Day 1, preparing the road map for synergy realization and supporting various function leaders in planning and execution.

Now let me address the medium-term aspiration of Revenue and margins.

- On Revenue, with the acquisition of SWC, we reconfirm our aspiration of $1.5B run rate by FY25.

- LTTS EBIT margin in Q3 stands at 18.7%.

- In Q1 of FY24, there could be an immediate impact of 180-200bps on EBIT margin resulting from consolidation of SWC.

- With the transformational levers that Amit has earlier discussed in respect to SWC acquisition, we aspire to get back to 18% EBIT margin by H1 FY26.

Thank you. And with that, I hand it over to the moderator for Q&A session.

Moderator: The first question is from the line of Bhavik Mehta from JPMorgan.

Bhavik Mehta: A couple of questions. Firstly, to Amit. If I look at what happened in 3Q, was it just a function of furloughs or whether also cases where, let's say, a lot of the deals you had won over the last eight to nine months did not ramp up as per your expectations? And how should we look at 4Q then, what are you hearing from clients when it comes to conversion of those deals into revenues so that's one.

And secondly, to Rajeev on 3Q performance on margins despite flat growth. So outside of SWC, can we expect 18.5% as a new base of margins going forward? Or do you think that 18% is the normal range to look at outside of SWC?

Amit Chadha: So, number one, I am confirming that Q3, you see normally, if you look at Q3, it has a lesser number of working days, right. I mean that's about, if I may be exact, I am an engineer & that's the problem we want to be exact. So about 3% lesser working days are there. So, we know that and that's how we had said we'll have a muted quarter.

We got hit by additional furloughs as we call it, because there were customers that came back and said that they would like to slow down the projects, etc. in Plant Engineering. But the good news is that they've since come back and they confirmed at the time when they were slowing it down that it will come back up on January 2nd onwards as 1st is holiday. And it did ramp back up from January 2nd, the team started again.

So therefore, it was a furlough impact more than anything else, and that's how I would leave it. From a deal velocity standpoint, I will say similar TCV, 3-digit of total deal closures that we have had. We are happy to share that the $10M+ deals that we have had. So, three of those clearly in Industrial Products, which is a high-margin business for us, one of them in Plant Engineering, which is again higher margin and the fifth one in T&OH for us, so which is Transportation.

We've had that plus there are multiple $5M deals that we have signed in Medical, in Telecom and Hitech, etc. Deal velocity is similar & we talked about the empanelment as well, and that also came through last quarter, so I do see that. In fact, I do want to say that other than Hitech, which we have called out in my commentary, the three sub segments that are there, we are seeing project approvals and continuation of teams, etc. In fact, we have done well on utilization last quarter. What we've done is that we've again given you a number, quantified the least possible increase in headcount. We're fairly comfortable at this stage. Now with that, Rajeev, margins?

Rajeev Gupta: In respect of margins, Bhavik, I just would like to say a few things. One, if you look at across all the five segments, we are certainly showing improvement in terms of EBITDA. I think the operating model that we've been talking about in the past, including the economies of scale has played out quite well for us.

We remain fairly comfortable that we should be able to hold for LTTS, the margin improvement that has come about. I did indicate that with consolidation of SWC in Q1 FY24, we should see a dip of 180-200bps, but that's something that would have been with any acquisition. But to sum it all, the operating model, the economics of scale have played out well for us. That gives us the confidence in terms of maintaining the margin going forward.

Moderator: The next question is from the line of Kawaljeet Saluja from Kotak Securities.

Kawaljeet Saluja: Just a couple of questions. The first is on demand. Amit, you did mention that the demand impact is largely furloughs, but when I look at your guidance, the guidance cut is $5M to $15M in revenues, whereas basis of furlough impact, the impact should not happen more than $2M to $3M

So just trying to reconcile some basic numbers behind the guidance cut. Is there more to it rather than just furloughs, which would have led to a change in your guidance that's the first question. The second question is more on relative comparison. That's something which I hate relative comparison but tempted to ask this for the first time. When I look at a company based in Delhi, a company, which has a business mix and portfolio similar to yours, they seem to be doing better on the far larger scale on growth.

Whereas LTTS, despite strong win announcements had continued moderation in growth rate. So is there any, I mean, shift in share or loss of share, which one needs to contend we're probably worried about in your case. So yes, those are a couple of questions, I'd appreciate it if you can answer them.

Amit Chadha: So, the change in guidance, we are saying we'll deliver 15% is basically based on muted Q3. So that's where that is, and that's where that stands. Now in terms of comparison, it was a specific Plant Engineering issue that I believe is since resolved. But of course, finally proof is in the pudding. You will see that at the end of Q4 when we come back and declare that to you.

I would, in fact, say that if I look at our market share and our size that we have got going on, I think we are expanding with our clients. In fact, if I look at the total number of clients itself, if I look at it year-on-year, I would say we've gone from 318 clients to 343. And you've seen a number of clients growing in the $1M bracket, the $5M bracket, the $10M, the $20M as well as the $30M.

I also want to add that I have visibility to the current run rate that we think we'll end up in Q4. And I can confirm to you that market share has expanded rather than declining. We were not getting invited to certain Telecom specific RFPs in network engineering given the size of the deals and what we had as capabilities in spite of buying Orchestra Technologies and growing organically, so we went in for this (SWC acquisition).

I do believe that we stand in a position now, having crossed $1B revenue in constant currency and with now with Smart World, I do believe that we are head-to-head with a lot of people that are there and our aspirations to get to $1.5B, as confirmed by Rajeev FY25, remain.

Moderator: We'll take the next question from the line of Mukul Garg from Motilal Oswal Financial Services.

Mukul Garg: Amit, I just wanted to follow up on the guidance part only. We have seen historically, you tend to be fairly conservative when you provide your revenue growth guidance like generally not like to kind of cut it back as you had to do this quarter. There is obviously this is happening in the backdrop of the macro constraint which you are seeing across the board.

Are there any signs which have now started becoming visible whether the increased furloughs in Q3 also were a factor of the macro pressure and does this increases the risk to how you are kind of visualizing qualitatively despite FY24 spend from corporates?

Amit Chadha: I want to give you a long-ish answer, if you don't mind here. So, let's go segment-wise. When you look at Transportation, right, we have not seen any moderation in spend. In fact, we've seen the growth in that as well in spite of a, shall I say, smaller quarter seasonally. And we do see new programs kicking in, etc. And that's across Auto, Aero and T&OH. Industrial Products is spending in specific areas of digital manufacturing as well as digitization of their products and that continues to happen, we don't see any slowdown. You've seen that in the growth as well as our commentary for Q4.

Now Medical that you have has always been traditionally, the work we do, a very conservative sector. But given the QARA pressures that they are under and notices they're receiving from various agencies and their need to check that, etc, as well as digitalization, we are seeing spend and you will start seeing that growth, right? Fourth is Hitech. I will say this that there are five sub segments in Hitech. There's ISV, there is Consumer Electronics (CE), there's Semiconductor, there is Media & Entertainment (M&E) and then there is Telecom. We have not seen any cutback in Telecom, which is Infra and OEMs or in M&E. However, in ISV, CE and Semiconductor, we've seen a fair degree of caution that they were exercising last quarter also & this quarter also. But we believe that the growth in Telecom and M&E should be able to overcome that. In Medical, forgot mentioning one thing - Healthcare is investing.

Finally, come to Plant Engineering. Like I said, again, Plant was a one-off issue in the quarter (Q3), since addressed. I'm going to assure you that the Plant Engineering will come back in Q4 and beyond. We are actively hiring, ramping up in Baroda and Chennai as well as in the US and Europe for this particular segment.

So that's how I see this. Finally, other than parts of Semiconductor, ISV, CE, mostly, you see a company-specific cut in terms of spending, but not a sector-wide. So, I'm still cautiously optimistic about CY23.

Moderator: We'll take the next question from the line of Vibhor Singhal from Nuvama Equities.

Vibhor Singhal: So, two questions from my side. Amit, you mentioned, I mean, we saw a very strong growth in the Transport division in this quarter. And we also had all these deals with the Airbus as well. So just wanted to basically understand the traction that we are seeing in the Aerospace division. We've seen travel rebound significantly across the globe.

And is it that kind of leading to more traction in this division? And do you think it can sustain going forward in the next year, I mean, as an industry, do you think there could be more similar kind of deals either for us or for the industry as a whole in this segment over the coming quarters, given that most of the Airlines' profitability and other values are basically now into the green again, and they might start spending again on both the fronts.

Secondly, my question was just a big basically, a quick clarification of the SWC margin thing. As we have mentioned that the first quarter of next year, we will see a 180-200bps impact of margins. Would there be any non-recurring impact of that as well? Or is it just the integration, which is going to reset the margin to that level? And then gradually, we're going to wrap it up as the growth comes in and as we basically rationalize the operations. So that's the two questions from my side.

Amit Chadha: One on Airbus, I do want to acknowledge one thing. Dr. Panda, as you're aware, is an Aerospace engineer & this account is very close to his heart. So, we did start trying to pursue this while he was CEO. And I'm happy that after years, we got empaneled first as a provider and then got selected. In fact, he was in our Board meeting today, and he said one thing – "you delivered very nicely done." It has been a dream, right? So, I do want to say for an aerospace engineer, getting Airbus empanelment for digital manufacturing etc. is a dream. I do think and a lot of people to thank, compliment, etc.

Having said that, I'll tell you Aerospace, the spend that is coming back is one there are design cycle that is starting again for the next-gen aircraft, right? People are looking at smaller aircraft, they're looking at single aisle. There are people that are talking about it. You can read the press on that. There is hybrid aircraft that people are talking about, etc. So those design cycles, concept cycles are starting. These are generally about a seven-to-ten-year cycle, right? So that is starting up. So that's good news, number one & this is not just for us, but everybody. So you will see more spend coming out for structures or avionics, etc.

Second, what's happening is there is a technology conversion happening from mechanical to electric, power electronics, et cetera, within the existing aircraft. That again is a smaller cycle, that's about maybe a five-year cycle. So that's kicking off as well. So that's number two.

Number three, the digital manufacturing part that they are bringing to a shop floor for a more integrated delivery, full life cycle system as they deliver aircraft and people take deliveries. So that is what is happening.

So you will see spend in Aero growing as you move forward, right? So that's that. In fact, one more thing was that you remember at one time, Japan, they were trying to do something and they stalled it because of COVID, again starting to have conversations where it should come back, et cetera. So a lot of positivity in that sector that I believe gives a lot of breather to a lot of people.

Rajeev Gupta: Let me take the question on the consolidation impact. In the previous analyst call, I did indicate that the SWC margin is in the range of 8% to 10%. So, Q1 truly is the impact of consolidating the two financials and of course, the impact in terms of acquisition, etc. But from thereafter, it is going to be a progressive improvement, looking at both revenue synergies and cost synergies. What we believe is quarter-on-quarter, you will see that progressive improvement coming through, which is where our aspiration is to come back in terms of 18% EBIT in H1 of FY26.

Moderator: The next question is from the line of Ravi Menon from Macquarie.

Ravi Menon: Well, two questions. First, within transportation, would you say that at least this year, Automotive is

Moderator: Sorry to interrupt you, please use the handset mode. The audio is not clear.

Ravi Menon: So within Transportation, would you say that Automotive is the fastest-growing this year, followed primarily by Off-highway with Aerospace a little further behind. Amit from the way you sounded it looks like Aerospace is going to pick up. So how should we think about growth within Transportation overall for CY23?

Amit Chadha: Ravi, can you repeat that, please?

Ravi Menon: I was saying within Transportation over this year, would you say that Automotive was the fastest growing and maybe followed by Off-highway and Aerospace further behind? And how should we think about CY23?

Amit Chadha: Number one, Transportation did grow, right? And let's wait for April to conclude which grew the fastest and slowest. But I will say this to you that for CY23, see, there are a few trends that we definitely see happening.

A) One is a lot more electrification of Automotive, so that will continue. Companies, however, have to remain profitable to be able to spend. B) T&OH - Construction of highway is seeing added autonomous as well as electrification and connected spend coming in. So, that is definitely happening. C) Aerospace, we believe, is starting a design cycle, but more than mechanical, we believe this will be more avionics and electrification, etc. led and digital manufacturing led. The reason I make that point is that earlier design cycles used to be a lot more mechanical led. This time, we are seeing a change in that. And we believe that we are well positioned in that area because we are more electrical embedded driven than mechanical driven in this area. So overall, do I see the growth? I absolutely see good growth coming in this area, continuing in CY23

Ravi Menon: And a follow-up on the Telecom & Hitech. you mentioned that in ISV, there was some pressure. So how should we think about this? Will ISV shut down some of these older legacy products that should we say - do we see a hit? Or do you think that more shifts offshore will actually compensate for that or maybe even provide some growth?

Amit Chadha: See, for those that have followed us two years now and talk to us, ISV is one of our smaller sub segments, right? Our exposure to ISV is fairly limited from a hit standpoint. Having said that, ISVs are reconsidering their spends. There was a lot of pie in the sky ideas and projects that were getting talked about. All that definitely is taking a back - shall I say back bench because they also want to start delivering profit, they want to look at, etcetera. So that's there. But Telecom & Hitech, I do want to say that 5G spends are on and will continue to do that.

Second, ISVs are trying to stop some area of spending, but they are starting to spend in devices that they are building that will work with 5G and then tomorrow, 6G, WiFi 6, etc. So I do believe that, that part will continue to grow. I am hopeful Semcom will definitely come back because the amount of semiconductor required in Auto that's required in data center is there. Yes, the number of people buying laptops has gone down because all of us purchases a laptop they wanted to & going back to work now.

But having said that, it's just temporary because if you look at the kind of production capacities that companies are building and design there are talking about, I do believe it will come back. So overall, I do think that the Hitech recovery may start in the second quarter calendar year and then go up from there. That's how I broadly see it -- for us specifically, though my commentaries hold that I do see our Q4 Telecom & Hitech being better.

Moderator: We'll take the next question from the line of Sulabh Govila from Morgan Stanley.

Sulabh Govila: So a couple of questions from my side. One is on the Auto vertical, particularly, which has been doing well for us as well as industry as a whole. There seems to be no major wins listed this quarter, but so I just wanted to understand, has there been a change incrementally in the way clients are awarding deals? Or is it just a timing issue in this quarter? And the second is on the $30M client bucket, there's a moderation in that number QoQ. So, is that also related to the Plant Engineering related furloughs or that's related to some other client?

Amit Chadha: The number one, Auto, not having a single $10M deal. Again, I said this to some of you once that engineers think like engineers, they don't think like businesspeople, they don't know that $9M is not counted in $10M deals. I would confirm to you that there are deals in Automotive as well. In fact, there are incremental deals. I don't know whether we’ve made it press or not. There were a couple of new ODCs inaugurated in this last quarter. Maybe - they have asked us for names to not be published, so we didn't, but there are a couple of new ODCs that have been published.

There were earlier wins that have ramped up in Auto as well. There are some exciting deals in progress in Auto as well. And I believe that some of them, they're already closed or are closing in the current quarter. So, I would not be worried about not announcing a deal in Auto. I was focused more on making sure that we get - because last quarter, we got feedback on this, the $9M is $9M and it’s not $10M. So, we made sure that there are some deals between $10M, nearly close to $20M also. But we haven't called them out as $20M because we believe in the practice of being a little conservative on these things. But I would not worry about Automotive -- all I would say is that we continue to grow in this area, expand, hire, etc. Now in fact, we are doing walk-ins in Munich. So, anybody who has friends can even recommend people and in Bangalore & Mysore.

Now let me go on to the $30M. I agree with you that that $30M, there was one client, in fact, less in sequential LTM,. In fact, not just $30M, we were flat in $20M as well. Though $10M+ grew one sequentially and $5M grew one sequentially. And of course, $1M grew by 8.

So I have access to Q4 data, which I expect we will do. And you will see some of these furloughs did have an impact across, right, everybody there was a shorter quarter, etc. So, what I can confirm to you is that this will correct itself. As we move forward, our focus on account mining scale continues to be laser sharp so that we can expand.

Moderator: The next question is from the line of Mihir Manohar from Carnelian Asset Management.

Mihir Manohar: Largely, I wanted to understand on the North American geography side, I mean, North America hasn't grown for this particular quarter. So any signs of demand moderation across this particular geography? I mean your comments with respect to this geography. That will be helpful. And my second question was on this Airbus notification that we made. Earlier also, we were like a strategic engineering partner, and now we are there for advanced capabilities. So just wanted to understand, given the fact that our penetration and our capabilities are improving on the Aero side. So, what kind of spend could be there for us specifically over the next year from the Aero side? I mean could it be like $5M kind of a spend per quarter? Could that be the potential opportunity? So I wanted to understand that.

And my third question was on the guidance that we have given the 15% constant currency guidance that we have given, and it implies 4.5% to 5% kind of a growth for balance part of the year. So, I mean what is bringing us that confidence that given a muted growth this quarter, we are still hopeful about having 4.5% to 5% growth for the balance part of the year? Yes, those were the questions.

Amit Chadha: So Mihir, here are the answers. Number one, you can see that North America, actually, there was a 0.7% de-growth it shows here because of this revenue, the way we count currency, but India shows 6.4%. I can confirm to you that we don't work in India, right? Largely, our India revenue that we report is actually INR billing, but it is done for US and European customers. So, I would like to confirm to you that Europe, North America - both of these and ROW have grown, the India growth that you see, you should actually count it towards the 3 Geos because for India, we do very little, maybe some $1M/$2M per quarter to that extent, $3M. So please read it like that. In fact, next year, we will review this and see if there's another way to present this because we get asked this question every quarter. So, we'll review this.

Second, Airbus. See, please understand, Airbus is a very -- shall I say, -- I want to find the right word for you. They have a very process-oriented methodical empanelment exercise, etc. So, what happened last time around when we announced it was we have been chosen by Airbus for Skywise platform and they had empaneled us as a vendor and given us MSA, etcetera, signed global really, which was earlier only in India MSA.

Now what they have done is, specifically in digital manufacturing and the other area, they have qualified a spend and said we will spend X amount of money, and we have been empaneled as one of I again can't give a number who are not liberty by Airbus to do that, but one-off say N number of suppliers and N is a very small number. So, they will spend that XX dollars amongst those very little vendors in those two particular areas. They've in fact given us a ramp-up plan, etcetera.

The reason I am again not quantifying it is because that is a discussion we've had with Airbus on. But I'm fairly confident that it will ramp up. We actually started recruiting, training, etcetera, as well as building team organization structures, etc. I will actually request my colleague, Abhishek, our COO, to talk a little bit about the process he does to get ready for such ramp-ups.

Third, Aero do we see growth? In avionics and digital manufacturing. Lastly, guidance, 15% constant currency amounts to more than 3% growth as far as we are concerned. And a point was asked earlier, were we slowing down. So see, we were at about a 4% growth rate in last year, and we had done that whatever, 19% to 20% that we grew last year.

This year, we've been a 3%+ range. Quarter 3 was muted. And next quarter, we see it's not played out yet. That's why we give guidance and let's say, don't give a firm number. We still have to bill, we still have to invoice, to collect. I can assure you that it will be greater than 3%. Will it be 4%, will it be more is to be seen.

Abhi, would you like to add on Aero specifically what we're doing in terms of that?

Abhishek Sinha: I think you all would have heard about the center we opened in Toulouse about 4 months back. And no one invests in a center in France, if they don't have the confidence of growing in the region, and it was for Airbus, and that's the reason we opened that center. If you look at of course can't share number, but if you look at our growth, of Airbus in the last couple of quarters, it has been actually one of the fastest-growing accounts for us.

And this is all in the backdrop of a very structured academy program that we have, training program that we have created in partnership with the Airbus all our training materials, the way we go about it, there’s an engine running and how we hire people and train them & internally move people into the account. Our relationship with Airbus is at a very advanced very strategically placed. We have even won some awards again can't share details. But I think we are in a good space and this partnership that Amit spoke of that we won the empanelment. I think that augurs well for us in the digital manufacturing space, especially.

Moderator: We'll take the next question from the line of Akshay Ramnani from Axis Capital.

Akshay Ramnani: So, first question was on offshoring. So, in your opening remarks, you mentioned that we see offshore revenue mix going up to 60%. I wanted to understand what are the drivers of this trend and which are the verticals where we expect this to be play out?

Amit Chadha: So let me start by sharing the verticals, and then I will request Abhi, my colleague, COO to address the drivers for offshoring to increase. From a vertical standpoint, see, as you look at it, we expect it to be, and I want to say this, you'll see this across verticals. It's not a vertical or a second vertical, you'll see this across verticals. I would also say that digital engineering – digital products and services as well as embedded, testing, parts of digital manufacturing. We'll see this a lot more, right? So, it's across. It's not like it's one or the other. Abhi, would you like to give the drivers for offshoring? Traditionally.

Abhishek Sinha: Yes. I think when we looked at our operational strategy, while everyone knows utilization freshers pyramid, these are all usual levers that you look at for margin growth. But offshoring is probably one of the biggest levers that we have, as a company, decided to work on. Our near-term aspiration is to go to 60% of our revenue coming from offshore. And we know that, that's a big lever from a margin perspective.

One of the things we have done well this quarter and hope to continue to in the coming quarters is a very high degree of focus on fresher utilization. The freshers that we take every quarter anywhere between 500 to 600 freshers that we take every quarter. Not only do we make sure that they are ready to get into billable projects that helps in margins, but more importantly, that also help in pulling more work offshore.

The last point I would like to mention is we have very actively started engaging with our customers in pushing the work to offshore, we have kind of created an 'offshorablity index' of our various service offerings. And we engage with -- we have started engaging with the customers actively on why a certain piece of work must be done offshore and of course, leveraging the whole hybrid working model that the COVID has taught us to see this work can be done from outside office, can be done anywhere. That whole engine between sales and delivery are starting to show results. We have been working on this for some time, and I expect this to continue.

Akshay Ramnani: And second one was on headcount addition. This has been soft for past four quarters now. So would it be fair to say that our utilization, which came back to about 75% would have now normalized to the comfort range of 78% to 80%. And here on, we would need to add headcount going forward. Is that the situation now?

Amit Chadha: Yes. So, number one, we did -- so number one was, yes, Q2 and Q3 saw us improving utilization, rationalizing pyramid, etc. I do want to confirm that Q4 onwards, I do believe that headcount addition sequentially will come back.

We've reached levels that we are comfortable with because we are a tech company. We do invest in labs, we invest in people working in labs, people creating solutions, practices, widgets, etc. We are comfortable with the utilization that we see now. And therefore, you will see headcount increasing now sequentially as we move forward quarterly.

Moderator: We'll take the next question from the line of Kawaljeet Saluja from Kotak Securities. Please go ahead.

Kawaljeet Saluja: My question is for Rajeev. Rajeev now when you are doing some back of the envelope calculation on margin guidance. And it seems that the way you have given guidance implies no contribution or a bit from the acquisition, SWC acquisition. Now is this largely because of amortization charge? Or do you expect the core organic margins also to deteriorate from that 18.5% you reported?

Rajeev Gupta: Let me clarify, this does not bake in any deterioration on the organic margin. I did mention it earlier that given we've done 18.7% EBIT in Q3 with all the operational levers and improvement in offshore and many of those things that we've talked about earlier, we do see a fair bit of comfort of sustaining this margin organically as we spoke.

As far as the SWC acquisition, there is part of amortization also baked into it. Plus, there may be some investment that we would have to make. And as you would appreciate, the strategy that Amit talked about in terms of Next-gen Communication, Sustainable Spaces and Cybersecurity, we will bring in experienced sales leaders to be based in respective geographies where we want to drive growth, right, and be able to position this to the existing customers and also solicit newer customers. So, part of that will be investments. But like I have said earlier that progressively, we should be able to see both revenue synergies and cost synergies play out.

Kawaljeet Saluja: So, Rajeev, what would be the EBIT margin? Let say you given the EBITDA margin for SWC, 8% to 10%. What would the EBIT margin be? How much do you think it trends down to before it starts recovering once the synergies kick in?

Rajeev Gupta: So, Kawaljeet, I can answer to what is historical. Like I've said, we've been in an EBITDA range of 8% to 10%. In terms of EBIT, very similar. I mean, there is not much of cost between EBITDA and EBIT that that business entails. So that is where it is. To your specific question, I may have said this in the previous call also, as we get more color, we will certainly provide that when we come back in Q1 FY24.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I would now like to hand the conference over to Mr. Pinku Pappan for closing comments.

Pinku Pappan: Thank you, everyone, for being present on the call today. And we hope we have answered most of your questions. We'll be happy to connect with you during the course of the quarter to clarify any other questions that may remain. With that, I would like to say bye and wish you all a very good day. Thank you.

Moderator: Thank you. Ladies and gentlemen, on behalf of L&T Technology Services Limited, that concludes this conference call. Thank you for joining us, and you may now disconnect your lines.

Note: This transcript has been lightly edited for clarity and accuracy.