

Subex Limited
Quarter One Results Conference Call – Financial Year 2011
July 29, 2010

Moderator: Good evening ladies and gentlemen. I am Sandhya, the moderator for this conference. Welcome to the Subex Limited conference call. For the duration of the presentation, all participants' lines will be in the listen-only mode. I will be standing by for the question and answer session. Now, I would like to hand over to Mr. Subash Menon. Thank you and over to you sir.

Mr. Subash Menon: Thank you very much. Good evening everybody and thanks for joining the call. As usual, I will take you through the presentation, which has few slides. The presentation has been uploaded on our website and it has been emailed to most of you, I think, pretty much all of you. In case you haven't received the presentation or have not been able to download it from the website, there is nothing to worry. I will be reading out all the details. So, let us get going with that.

The first slide of the presentation, this has the title, Linking the Past. Now basically, what one is trying to do here is, over the past several months during our conversations with several investors, we have got a feeling that there is a lot of confusion prevailing at this point in time because of the different types of numbers that have been released by the Company over the past few years. In fact, the Company has looked at all the numbers that were there. I can't exactly remember what the reasons may have been at that point in time, ended up releasing different sets of numbers from time to time rather different definitions for the....at times even that way for the numbers that were released. So, that has caused confusion. For example, in this financial year....the beginning of this financial year, we said we have got 49 million dollars of backlog, whereas at the beginning of FY '09 financial year, we had said that we have got 85 million dollars worth of backlog. Now, when people look at these two numbers, they naturally get a feeling that two years ago, Subex had 85 million dollars worth of backlog whereas today it is 49 only. So, that means that there is a significant slide in the business, but that is not the reality because what we declared....the 85 million dollars which we had declared at that point in time had three components in it adding up to 85. The 49 million dollars that we declared this time had only two components in it adding up to 49. Now, if we are to look at all the three components for the current financial year as well like we did in the beginning of FY '09, the numbers stood at 88 million dollars. So, the reality is what was 85....the comparable number is what was 85 million dollars at the beginning of FY '09 actually was 88 million dollars at the beginning of FY '11, but since we did not quite give comparable numbers, everything looked quite negative.

So, I am essentially trying to take you through the numbers that were delivered over the past few years and also how.....and then people have had questions as to how does one arrive at the revenue number? How does one understand the revenue numbers? So, I am trying to take you through all of that at this point in time. So, it is slightly complex, but I will try to make it as simple as possible.

So, the first slide, Linking the Past, gives you different types of backlogs. Now, there are three types of backlogs that the organization works with adding up to the total backlog. One backlog is the Long Term Projects. Long Term Projects are.....as we know, we have three-year or five-year contracts with customers and that means the revenue of that three-year contract will be recognized over a three-year period. When we look at this from an annual perspective or the current financial year perspective, all of that revenue will not come into that particular year. So, Backlog-Long Term-Projects, actually that backlog will not come into revenue, will not get converted into revenue in the financial year that is under discussion. So, that is the Backlog-Long Term-Projects. We have given for RMS and for FAS and the total.

Then, Backlog-for FY-Projects is again, these are also projects backlog, but that also....but that is backlog which will get converted into revenue in that particular financial year. So, that is the difference between these two. So, that is the second one which is again for RMS and FAS and adding up to the total.

The third one is Backlog-for FY-Annuity which basically is all the support revenue that we have, you know, that happens in that particular year. So, that is mentioned there for RMS and FAS and the total.

So, in any year, the backlog which really will become revenue in that year is the second and the third put together, that is the Backlog-for FY-Projects and Backlog-for FY-Annuity. Backlog-Long Term-Projects is something which happens in the future years and not in that particular financial year.

So, now let us look at the numbers. In FY '08, the total was 70 million dollars, which moved up to 85 million dollars in FY '09 which moved down a little bit because of the problems in FY '09 to 81 million dollars and has now moved back up and that is at 88 million dollars at the beginning of the financial year. Those are the sum of the three components. Whereas in the different years, in FY '08, beginning of which we said 70 million dollars, that is the summation of all three. In FY '09, we said 85, again the summation of all three. In FY '10, we excluded Annuity from that and we gave you the sum of the other two only. While we should

have really given 81 as the number, we gave 56 as the number at that point in time.

In FY '11, the focus was on what could get converted in this financial year. So, we gave you only the sum of two and three, that is, FY-Projects and FY-Annuity, 22 and 27 adding up to 49, while once again for comparison sake, we should have given you 88.

So, while the 70, 85, 56, 49 declared numbers kind of show a negative trend from FY '09, the reality is a positive trend in FY '11, and when we started FY '11, we had backlog which like never before, so that is the number that we should focus on. So, out of that 88 of course, 49 only will get recognized as revenue in the current financial year, the rest will get carried forward to the future financial years. So, that is how we need to link and look at these numbers.

The next sheet talks about things like pipeline and success rate and all that. Two to three years ago, our success rate was fairly high and we had as high as....success rate actual as you can see was like 28%. We expected it to be 40, it was 28. In the next financial year, we expected it to be 31, it was 20%, and in the third year, FY '10, we never declared any number, we had about 18%. Now, we are looking at 20%. So, in short, 18% to 20% is something that has been consistently happening over the past two years. So, we think, we have kind of, you know, bottomed out there on that front and it will not go below the 18% numbers. So, if we were to assume 18% to 20%, the conversion for this financial year on a 379 million dollar pipeline, then certainly that is achievable.

Now, when you look at what the revenue....what the potential revenue of this company could be, you should look at from the backlog what would come into this year, then you should add this potential, you know, revenue that will come out of orders that will get converted.... into fresh orders that will get converted into revenues. So, how would that look like then?

As you can see, the order intake is arrived at by multiplying the pipeline with the success rate actual and then you get the order intake. From the order intake, you have to convert into revenue in that particular year. Now, as you see there, our overall order intake....sorry, conversion from order intake to revenue in a particular year was 50% in FY '08. It improved to 64% in FY '09, which is improved to 66% in FY '10. Of course in between, FAS has gone down and RMS has gone up, but the weighted average was 50%, 64%, and 66% respectively in the three years.

Now, when you look at FY '11 and try to project what could potentially be, we have not given a guidance, so naturally you may

want to project. So, when you look at that the way you should look at it is the first component of this whole revenue is that 49 million dollars which comes from backlog which will get into revenue this year. The second component is after winning orders in the current financial year, what out of that will get converted in this financial year into revenue. Now, the third slide shows that for the past three years. So, based on the order intake for the past three years and the actual conversion from order intake into revenues, order intake of that year getting converted into revenue in that year itself, we have given the order intake converted to revenue numbers and the summation of that and the Backlog-for FY-Projects and Backlog- for FY-Annuity was actually the revenue for that year.

So, let us look at, for example, let us look at FY '08. The Backlog-for FY-Projects in FY '08 was 30. The Backlog-for FY-Annuity was 22. That is 30 and 22 and I am taking the total for RMS and FAS of course, and OI that was converted in that year to revenue in that year was 43. So, when you add 30 plus 22 with 43, you get to 95, which was the revenue in that year. If you were look at FY '10, for example, I mean just keeping one year here, so if you look at FY '10, the corresponding numbers were 16 of Backlog- for FY-Projects and 25 of Backlog-for FY-Annuity adding up to 41 at this point in time and then you add the OI converted to revenue which was 42 million dollars, that is OI in that year converted to revenue in that year, so 41 plus 42 is 83 and that was the revenue in FY '10.

So, this is how you need to understand these numbers, and if you have to work out what could potentially happen in FY '11 by way of revenue, the way you need to go about it is, you look at the Backlog- for FY-Projects for this year, that is 22 million dollars, Backlog- for FY-Annuity for this year that is 27 million dollars adding up to 49. Then, you look at the pipeline, which is 379 million dollars. You apply a potential success rate, and if you apply between 18% and 20%, I don't think you will go wrong and then you will get the order intake for the year. Now, from the order intake for the year, let us say you get X million dollars, now from that order intake for the year, how much will get converted into revenue in that year? For that you have to apply a percentage. Last year that was 66%. We expect that to get better, but let us say you apply 66% or 67% on that and then you will get a number, let us say Y million dollars, which is nothing but the order intake in FY '11 which will get converted into revenue in FY '11.

So, going back to the three components which add up to give you the revenue for FY '11, one, Backlog-for FY-Projects 22 million dollars, Backlog-for FY-Annuity 27 million dollars and you are now at 49. Then, order intake that will of FY '11, it will get converted into revenue in FY'11, computed as I explained, whatever that

number comes to, Y million dollars. The 22 million plus 27 million plus Y million will be the revenue for the year.

Now, to arrive at Y, as I said, you have to have two assumptions here, you have been given the pipeline, so that is not an assumption and that is 379 million dollars. You have to assume the success rate from pipeline to order intake, then you have to assume a conversion rate from order intake to order intake to revenue. Once you apply these two percentages on 379 million dollars progressively, you will arrive at that third component which I have been calling as Y million dollars for FY'11 to arrive at the total revenue for FY'11. We felt we should give this absolute clarity. Now, with this, you can really take all the different numbers that we are giving on a regular basis and create your own model and arrive at the revenue. You all know what the expenses are there, you know how that has been trending, and based on that of course, you can come up with your complete financial model.

With that, let me move to the next slide which is order intake. Order intake has improved over the last quarter. Last quarter was 16 million dollars in all. This quarter, we have seen 17.3 million dollars. RMS which was 12.7 in the last quarter has improved to 14.1 which is an 11% improvement in this quarter over last quarter. In fact, this 14.1 of RMS is the highest number bar that 14.53 we had in the third quarter of last year over the past 5 to 6 quarters if you look. So, in short, RMS is doing very well. FAS has kind of steadied at 3.2 million dollars at this point in time, totaling 17.3. So, in short, I think order intake is trending in the right direction. We have to step this up in the coming quarter, but definitely that improvement is seen and the direction is correct, and as long as we keep going in this direction, we should be absolutely fine with order intake which fundamentally is the product of success rate actual and pipeline of 379 million dollars. We are looking at a 20% kind of number there, which is the success rate actual, which should take our order intake of 18% to 20% order intake like 72 to 74 million dollars, so going by that, we are pretty much on track with the quarter one numbers.

Looking at the next slide, Managed Services, we have been talking about this that Managed Services has been doing quite well. As you can see, there is a significant bump up on that front. This quarter, we had 17% coming from Managed Services and about 45% to 46% coming from license. These are the two revenue models that are comparable. When license kind of goes up, then in relative terms Managed Services could get impacted because that means we have more license contracts than Managed Services and vice versa. We do not think that for the whole year Managed Services, however, will be at 17%. It could potentially be, but it will definitely be higher than the 10% that we had last year. So, maybe in the 14% to 15% or something like

that. If of course it ends up at 17% or higher in the year, we will be more than happy because that is the direction that we want to take. Over time, we definitely want Managed Services component to keep on increasing. Support is continuing at a steady 27% to 28%. By geography, this of course keeps on fluctuating on a quarter-to-quarter basis. EMEA was fairly strong this quarter. America has went down a little bit, and APAC has kind of flattish, you know, wherever it was.

Other Metrics: Our pipeline at this point in time stands at 382 million dollars. The product revenue, as you know, we have been focusing, we have always been focusing on products, and there is sort of contribution from the products in the total revenue. That now stands at 86% of the total revenue in this quarter has come from products business.

The next slide gives the progression over years in the products business. This is something that we have been tracking on a regular basis for quite some time now. As you all know, our endeavor is to get to that 35% plus EBITDA in very short order, I mean, hopefully by next year. That is our expectation. So, this year, we are definitely expecting an improvement, a significant improvement in EBITDA over last year, and as we can see in the very first quarter, we have got the 31% EBITDA. So, that is a significant improvement over the whole of last year, which was 23.8%. We expect this to improve further in the coming quarters thereby taking so the number for the full year will be higher than 31%. That is our expectation. Operating profit which is EBITDA less interest has also improved. As you can see that number is almost like 33% to 34% of the full year number for last year. So, that is looking pretty strong. If you were to compare this to different years, you will see that this probably in absolute terms, this probably is higher that we have ever got to in the quarter or in a year.

Going into the next slide, which is about FCCBs, in my interaction with several shareholders and potential shareholders, it has been clear that FCCB is a cause for concern for a lot of investors. So, we felt that we should address that and give you some clarity on that. When you look at FCCB1, now this is something that will never get converted because the conversion price is quite high. This will go into redemption in March 2012. At that point in time, the 39 million dollars will have to be paid back as 53 million dollars including redemption premium. Now, the way we look at it as to where we would have the money for that, if you look at the FCF for FY' 11 and FY' 12, we see accumulated FCF of 51 million dollars. Now, as you can see, that is within spinning distance of the 53 million dollars that will be required, so we will be short by only about 2 million dollars, and that is something that can easily be made up through very, very small bank loan. So, from what we see with regards to FCCB1, the company will generate enough

cash over these two years, FY' 11, FY' 12, to take care of that liability, that repayment.

Looking at FCCB2, the component which got restructured. Originally, we had 98.7 million dollars worth. In today's time, it is reduced to 54.8 after considering conversion of 43.9 million dollars. However, this entire 43.9 has not got converted as yet. Bulk of it has got converted. The rest is in the process, I mean, there is a conversion process. At times, it takes a few weeks depending upon on several things, so that is going on. So, with all of that, and naturally over the next couple of weeks or three weeks or something, that portion also will get converted, whatever is under conversion now. With that, 43.9 million dollars would have got converted, and the balance would be 54.8 million dollars. We expect that also to be converted over the next 4 to 6 quarters. So, we expect FCCB2 to be fully converted. In short, we are not concerned about FCCB1 because we will be generating enough cash to pay it back, FCCB1 holders. As regards to FCCB2 is concerned, our expectation is that they will get converted, given the kind of performance that we are expecting over the next few quarters.

Moving to the next slide on quantitative points, this is essentially to compare the just concluded quarter with the past. Product revenue increased 7.5% over comparable quarter of last year. That is quarter on quarter increase of 7.5%, and sequential of about 8.7%. We are definitely gunning for higher increase over time, I mean, once we are done with the year, you will see a 15% kind of growth in product revenue, so there is some catch up here, but then this is just the first quarter. We are winning orders, and we should easily be able to catch up over the next few quarters. In fact, that will be obvious to you when you arrive at your own potential revenue number for the company after applying success rate actual and order intake to revenue conversion percentages on the pipeline of 379 million dollars. Product EBITDA, as we said earlier, was 31% in this quarter as compared to 14% in the quarter one of last year, that is 62% increase. I mean, we had 326 million rupees of EBITDA this quarter as compared to 201 million rupees. So, that is 326 million rupees versus 201 million rupees for last year. That is 62% increase, and over the last quarter, there is a 1% increase. It was 30% then and now it is 31%, and so, we are definitely in line with the full year expectation, internal expectation for FY' 11.

Net profit. Here, we have to exclude exceptional items because exceptional items really is restatement of FCCB liability based on the dollar-rupee parity at any given point in time, which essentially is the end of the quarter the last day of the reporting quarter. So, if one is to exclude that, we had 170 million rupees in this quarter as compared to 21 million rupees in the comparable quarter last year, so that is significant, that is 800 odd percent kind of or 8.2

times increase over last year. So, as you can see, the nonlinearity in the business is definitely happening. While the revenue has gone up over comparable quarter last year, on quarter on quarter basis, while the revenue went up only 7.5%, the profit went up quite significantly. EBITDA went up, net profit went up, everything went up quite significantly. That is the nonlinearity that we have been talking about. Order intake, as I said earlier is in line with expectation. So, in short, for the whole of the year, the numbers are trending in the right direction. The business is trending in the right direction, and that is what we are trying to share in the next slide.

The qualitative aspects. As you know, our, you know, entire focus at this point in time is on the platform ROC and Managed Services. These two have been gaining significant traction over time. As you know, we have already won about 6 ROC contracts over the past 7 months. We had announced 5 over the past 6 months sometime ago, and as we speak now, it is 6 over the past 7 months, 6 contracts. Even, Managed Services, we have been winning multi-million dollar, multi-year deals on Managed Services, and as is shown by that 17% contribution from Managed Services in quarter one, Managed Services is trending up quite nicely. So, on the whole, both ROC and Managed Services, particular ROC as Managed Services, all these things are moving in exactly the direction that we want them to move. In fact, we are right now addressing an RFP from Telco, a fairly large RFP, probably the largest, that if we win would probably be the largest order that we have ever won, where the Telco has actually specified ROC as a product that they want. So, when competitors bid, well I don't know how they are going to be compliant because none of them have ROC, only we have that. That is our product. So, in short, over the last 3 years, I mean, 3 years ago people had not heard about ROC. We started talking about it. Over the past 3 years, they have got more and more accustomed to it. They have started contracting it. Now, we are seeing a situation where they are hopefully starting to specify that in their RFPs, in the tenders for everyone to bid. In fact, this tender that we are talking about is actually a tender that has been given out to systems integrators because of the very large tender with lots of things in it, and that is where they have aspected it out, so these SIs now have to bid our product if they have to be compliant with requirements of the tender. So, our endeavor, our dream, our expectation, our hope is to make ROC the de facto standard in the industry over the next 3 to 4 years. We are starting to see that happening at this point in time, and that to me is the most important aspect that I would like to share with all of you. Numbers, you know, are derived out of these qualitative achievements, and this qualitative achievement of customers starting look at ROC and specifying ROC is a significant qualitative achievement which will result in significant numbers over time. The company is moving in the right direction. Numbers

are showing that. Qualitative achievements are showing that, and we are quite confident of what we have set out to achieve in FY' 11 and FY' 12 and going forward. With that, I am done with the presentation. I would now like to throw the floor open for questions. Thank you very much. Questions please.

Moderator: Thank you very much sir. We will now begin the Q&A interactive session. Participants who wish to ask any questions, please press *1 on your telephone keypad. On pressing *1, participants will get a chance to present their questions on a first-in-line basis. Participants are requested to use only handsets while asking a question. To ask a question, please press *1 now. Participants who wish to ask any question, may kindly press * followed by 1 on their telephone keypad. I again repeat, participants who wish to ask any questions, may kindly press * followed by 1 on their telephone keypad. First in line, we have a question from Mr. Nihar Shah from Enam Holdings. Over to you sir.

Mr. Nihar Shah: Good evening sir. I just have a bookkeeping question, you know, given that you have taken some warrants for yourself and conversion of the FCCBs, you know, if you assume that all FCCBs of FCCB2 get converted, what is the total diluted share count that you would have currently.

Mr. Subash Menon: Okay, first of all, just for the sake of clarity, it was not warrants that have been taken. Preferential share allotment was what we went through, so they are actually shares that have been issued and have been fully paid for.

Mr. Nihar Shah: Okay.

Mr. Subash Menon: Once you had all that and upon full conversion, we will get to 98 million shares.

Mr. Nihar Shah: 98 million shares, okay. That was all from my side. Thank you sir.

Moderator: Thank you very much sir. Participants who wish to ask any questions may kindly press * followed by 1 on their telephone keypad. At this moment, there are no further questions from the participants. I would like to handover the floor back to Mr. Subash Menon.

Mr. Subash Menon: Okay, thank you very much. If you need more clarity at whatever point in time, please feel free to contact us. Once again, thanks. Have a great evening.

Moderator:

Thank you very much sir. Ladies and gentlemen, thank you for choosing WebEx's Conferencing Service. That concludes this conference call. Thank you for your participation. You may now disconnect your lines. Thank you.
