"Newgen Software Technologies Limited Q1FY19 Earnings Conference Call"

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MANAGEMENT: **MR. DIWAKAR NIGAM – CHAIRMAN AND MANAGING DIRECTOR, NEWGEN, NEWGEN SOFTWARE TECHNOLOGIES LIMITED**
MR. T.S. VARADARAJAN – WHOLE TIME DIRECTOR, NEWGEN SOFTWARE TECHNOLOGIES LIMITED
MR. VIRENDER JEET – SENIOR VP (SALES & MARKETING AND PRODUCT), NEWGEN SOFTWARE TECHNOLOGIES LIMITED
MR. ARUN KUMAR GUPTA – CHIEF FINANCIAL OFFICER, NEWGEN SOFTWARE TECHNOLOGIES LIMITED
MS. DEEPTI MEHRA CHUGH – HEAD (INVESTOR RELATIONS), NEWGEN SOFTWARE TECHNOLOGIES LIMITED

Moderator: Ladies and gentlemen good day and welcome to the Newgen Software Technologies Limited Q1 FY19 earnings conference call. As a reminder all the 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 telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Ms. Deepti Mehra. Thank you and over to you madam.

Deepti Mehra: Good afternoon everyone. I am Deepti Mehra Chugh – Head of Investor Relations, Newgen Software Technologies Limited and I welcome you all to the Q1 FY19 results of the company. I have along with me today Mr. Diwakar Nigam – Chairman and Managing Director, Newgen, Mr. Varadarajan – Whole Time Director, Mr. Virender Jeet – Senior VP, Sales & Marketing and Product and Mr. Arun Kumar Gupta – Chief Financial Officer.

Before we move onto the discussion, let me highlight that this call may contain certain forward-looking statements concerning Newgen's future business prospects and business profitability which are subject to a number of risks and uncertainties, and the actual results could materially differ from those in such forward-looking statements. Past performance may not be indicative of future performance. The company does not undertake to make any announcement in case any of the future and forward-looking statements become materially incorrect in future or update any forward-looking statements made from time to time by or on behalf of the company. For further details you may please refer to the investor relations section of our website.

I would now hand over to Mr. Nigam for the presentation of Q1 FY19 results.

Diwakar Nigam: Good afternoon and a pleasure to have all of you at our Q1 FY19 Post-Results Conference Call. As an organization we are constantly evolving in terms of scale, learning and expertise, and it has been our endeavor always to deliver growth through focus on innovation. We continue to strive towards improving our customer's ability to develop applications faster on our platforms, to adapt more easily and to allow them to innovate more effectively.

Continuing with the growth momentum we witnessed robust revenue growth compared to the same quarter in previous year. Looking at Q1 FY19 on a consolidated basis we reported a Total Income of Rs. 1143 million up by 28% YoY. Revenue from operations was up 20% YoY. The difference is largely due to foreign exchange. We are happy to report that we added 17 new customers during the quarter including some prestigious names. We made four new customer acquisitions in the US including a leading independently owned bank in Texas, a leading publicly listed bank headquartered in New Jersey and a large credit union. In the banking system we have also added a large commercial bank in Middle East and Africa region providing banking and financial solutions to personal and corporate customers. In Singapore we have successfully added a key customer in legal space. In India we added a leading cement manufacturer. We have also booked certain large orders during the quarter including the digitization project of the records of District and Subordinate Courts in the State of Maharashtra on a turnkey basis. And the impact of the same would reflect in coming quarters and years.

We witnessed broad-based growth especially across US, APAC and EMEA region. In US, we grew by 46%, APAC witnessed a growth of 25% and EMEA witnessed a growth of 17%. India market growth was a little muted at 5% on account of longer gestation in processing certain large deals which could not mature during the quarter and thus were shifted out.

Focusing on our business in US, we had our customer conference in June 2018 in Orlando US, which concluded on a very high note and brought together industry leaders, influencers and analysts from leading organizations across the US, Canada, Caribbean and South America. Newgen's customers across verticals presented their digital transformation stories and journeys through interesting case studies. The event was attended by 65 plus delegates from across verticals including banking, government, insurance, healthcare and other industries.

Cloud and SaaS continues to be our fastest growing revenue component and witnessed a growth of 157% YoY. Cloud-SaaS revenue was at Rs 49 million and we added three new customers for Cloud SaaS during the quarter. Our license revenue was Rs 127 million, annuity revenue (ATS plus Support) were at Rs 595 million.

Banking and Financial Services vertical comprise 51% of revenue, Government and PSU comprised 13% and Healthcare comprised 9% of revenues during the quarter. I would like to highlight once again that software license business is usually seasonal in nature primarily given the large enterprise account buying patterns leading to substantial revenue and profit booked in the second half of the financial year. The group adopted IndAS 115 – revenue from contracts with customers using the cumulative effect method. The date of the initial application is 1st April 2018 and the impact of the same on revenue is not material in our case.

Newgen continues to strengthen its horizontal product platform with vertical service accelerators to enhance the overall portfolio. Continuing with our attempt to innovate and provide the most advanced features and functionality, enhanced user experience to customers, improved information security and easier integration, we have released various product updates during the quarter including our flagship products, OmniDocs, OmniOMS, OmniScan and OmniFlow iBPS. Our new offering includes mobility, virtual repository services and dynamic case management, RPA with BPM, digital sensing and flexible designing and authoring. Equally important are the applications built on our platform which are extremely powerful and help organizations achieve this critical objective. Our applications are scalable, secure, cloud-ready, highly available and usable on all major mobile devices.

Our go-to market strategy consists of direct sales supplemented by sales through our channel partners. Our direct sales are made by our company in India and our subsidiaries located in USA, UK, Singapore and Canada through our sales and marketing teams of 270 plus employees. We are more than 300 channel partners globally helping us in improving our business. We continue to expand across geographies and are starting investments in South Africa and Australia. Canada is showing good traction in business as well.

We have attracted multiple recognitions from leading advisory and research firms including Forrester and Gartner from time to time. This quarter Newgen and Bank Muscat, Sultanate of Oman together were the winner of the Asian Banker Award for "Best Retail Payment Initiative, Application or Program in the Middle East", 2018 for automating financial processes including outward remittances and standing orders, speed transfer overseas and inward inquiries using Newgen's solutions.

Also, Newgen and one of the world's largest banking and financial services organization together were the Gold Stevie Award Winner for Asia Pacific Stevie Awards for "The Innovative Use of Technology in Customer Service", 2018 for delivering premium customer experience with digitization of credit cards, on-boarding using Newgen's solutions.

Profits and Margins

Despite the fact that the business is seasonal in nature with substantial revenues and profits in the second half of financial year, the company witnessed an improvement in its EBITDA adjusted for other income which was at Rs 5.6 million compared to an operational loss of Rs (-) 3.6 million in Q1 FY18. Profit after tax was Rs 38.7 million compared to a net loss of (-) 15.0 million in Q1 FY18.

Expenditure

During the quarter we do see increased costs compared to Q1 FY18 on account of pre-hiring to tap the growth opportunity, key marketing events and activities such as the US Customer Meet during the quarter and some currency impact on costs like travel etc.

R&D is a key area of investment for us and R&D expenditure comprised approximately 11% of our revenues.

We continue to focus on sales and marketing efforts of the organization especially in new geographies US and UK. The sales and marketing expenditure comprised approximately 26% of our revenues in Q1 FY19.

Trade Receivables

Our gross trade receivables as on 30th June 2018 are Rs 2,421 million as against Rs 2,249 million as on 30th June 2017. The net trade receivables are at Rs 2,018 million. We continue to work towards improvement in our debtor position through stringent collection policies and related incentives and improvement in contracting. During the quarter, DSO (net of allowances) stood at 139 days considering the revenues of trailing 12 months.

Outlook

The future holds multiple possibilities for us and I am glad, we are in the right direction with market, customers, analysts and partners endorsing our story. We are now open to Q&A.

Moderator Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. We take the first question from the line of Nagaraj Chandrashekhar from Laburnum Capital, please go ahead.

Nagaraj Chandrashekhar: My question is on the US part of the business where you have done very well year over year. When we spoke earlier you said that there were roughly 400-450 mid-sized to small-sized banks coming to a tech cycle change out of which you have around 250 cases where you are targeting wins. Now that you have a sort of a critical mass of 10-15 banks that are your customers, could you give us a sense of using these banks as references, how really is the sales cycle sort of panning out, what is the typical sales cycle for you and bucket by bucket how many of these 250 banks are those where there are cases where you have just established leads and points of contacts to how many of them would be where you are close to sort of closing deals with these banks?

Virender Jeet: Thanks Chandrasekar for asking the question. As we spoke last time, the idea is that the addressable market base is pretty large and having established our key referenceables over last 2 years, we are in the right phase of capturing more banks. So, today I think at any moment, we are dealing with roughly around 120 banks at various stages of the funnel and at a mature stage you could have at least 40-50 accounts which are in the process of what you call higher degree of engagements, negotiations or closures. I think if you look at a year back it almost took a whole year to get 3-4 accounts. I think this year in the first three months we have got 3 orders. We expect that momentum to continue for the remaining part of the year and this year we do expect to capture at least 10-12 accounts in banking. And as we know it is a vast territory we also need to ramp up to address other parts of US market. So, I am sure as we keep on building these referenceable cases, we can increase our penetration and even further accelerate to get this account acquisition rate up to 20 or 35.

Nagaraj Chandrashekhar: Yes, and the follow-up would be, you had mentioned that the ticket size initially obviously depending on the size of the bank tends to be around half a million to one million and clearly ramps up, just wondering on if you could talk about some of the older clients out of the roughly 15 that you have, what has been the pace of ramping up at the older clients typically from that initial ticket size?

Virender Jeet: Yeah, I think the interesting part is that half of them are in the implementation cycles yet where the first implementation is still going on and the other ones which have gone live we have surely got more repeat orders from them and some of them have also almost reached a million-dollar kind of orders for us. So, the whole story in terms of customers, that we enter at a value of around 400K to 500K and then we ramp up accounts for million and two million that holds true. Since it is early days in US we are still 2-2.5-year-old in banking, still certain implementations are ongoing in the first phase. It does take the customer sometime to get the benefit of the first solution before they start investing in other ideas.

Moderator: Next question is from the line of Ranjeet Jaiswal from Jefferies, please go ahead.

Ranjeet Jaiswal: My first question is related to net trade receivables. So, can you please let us know how much of this would be greater than six months?

Virender Jeet: Roughly around Rs 60-64 crores of the gross receivables is greater than six months.

Ranjeet Jaiswal: Rs 60 crores is greater than six months. And I have another couple of questions.

Virender Jeet: You can get the data later, you can contact us, and we can send you more details on that.

Ranjeet Jaiswal: Yes, but I need to understand a couple of things. So, can you please help us understand what was the reason for high other income in this quarter? Next, I would also like to understand the contract with the Maharashtra government which you have published in BSE release. So, can you give us more highlight on that?

Virender Jeet: Other income is on account of two things. One is the FOREX gains eventually on the receivables which we received in the quarter and interest imcome. Interest income and FOREX earnings that constitute roughly around Rs 7 crores of income.

Ranjeet Jaiswal: Okay, so how much of this would be FOREX gain?

Virender Jeet: Rs 5 crores is FOREX gain.

Ranjeet Jaiswal: The last one is related to Maharashtra contract, can you give us more color on that?

Virender Jeet: I think we had two material disclosures over this, last few months. One was about Maharashtra and other was MP High Courts. So, both the orders are about the digitization initiatives of these courts where we are looking at providing the whole system for digitization of all court files as well as systems to eventually operate on those files through electronic content management system. So, we have got these turnkey orders. These orders are typically 3 to 5 years gestation. One is 3 years, one is 5 years and kind of delivery of software, setting up of the systems as well as doing the digitization of their records. And we expect that over next few quarters the revenues will start accumulating in our income.

Ranjeet Jaiswal: So, can we assume couple of quarters?

Virender Jeet: They are all started. One of the projects has already started but I think still initial ramp up is going on and the next one is also starting over the next quarter. So, in Q3 and Q4 we should see some impact of those orders.

Moderator: We will take the next question from the line of Keyur Shah from Emkay Global, please go ahead.

Keyur Shah: I would like to know what kind of investments have you started in South Africa & Australian markets and what are you looking at over there and how much investments are you looking at over 3 to 5 years or in near term, say for 1 year?

Virender Jeet: Both South Africa and Australia we are starting our investments in terms of setting up our initial sales presence out there. So, what we do is typically once we are exploring these territories we do set up the partner network and enable certain people either on the travel mode or to be there on permanent basis. So, initial investments will be in marketing activities, in sales cost, manpower cost – we will continue as we start finding traction it may further lead to setting up subsidiaries or having your own office out there. So, right now they are not very material because we have a large 270 people sales and marketing team baseand adding a few people in this territory is not a very material thing. But going further for the next 2-3 years we will do kind of sales investments out there which are needed. And if the territory shows promise and we are able to quickly get more orders, then we can even have much more serious investments to capture the market.

Keyur Shah: Are you looking at any acquisitions over there?

Virender Jeet: No, not really. Right now, I think the potential in our business on an organic basis seems quite high so we can surely do in our own area we have lot to do.

Moderator: Next question is from the line of Girish Shetty from Equity Masters, please go ahead.

Girish Shetty: Sir I wanted to ask on your cloud computing business, what is the expected revenue for FY19 and second would be what kind of companies are we competing for cloud computing business as in are those the bigger IT companies that we compete with?

Virender Jeet: So, when we say cloud computing we are not in cloud computing business, we are in offering our software product as subscription or what you call a SAAS business – so that's software sold as a subscription. So, the kind of customers we have are typically banks, insurance companies, shared services, the typical segments which we cover where we rather than providing our perpetual licensing, we onboard those customers as our subscription customers. We receive per user per month kind of a payment. And typical run-rate for our business right now - we have done roughly around Rs. 4-5 crores in Q1, that run-rate would continue and then we can build on further orders adding to the run-rate. So, we will be more like Rs. 16 crores right now and it will further increase as the year proceeds. Does that answer your question Girish?

Girish Shetty: And sir what kind of competitors are we looking at?

Virender Jeet: Competitors in our space (enterprise content management and business process management) include the traditional IBM, Pega, OpenText and then there is also competition for vertical solutions where we are selling solutions in commercial lending on platform and then there are vertical companies in different regions.

Moderator: We will take the next question from the line of Jaineel Jhaveri from J&J Holdings, please go ahead.

Jaineel Jhaveri: I am kind of new to this company, so this might be repetitive but in the March Quarter why is our revenues high? Is there seasonality in this business? And secondly why do we have such a high amount of PAT in that quarter compared to the whole year?

Virender Jeet: So, what is happening is that in most product companies, the nature of business is such that when you have lot of license deals the closures do happen around financial quarters. So, for us Q3 and Q4 become very important because traditionally what has happened in license business is customers do understand that what are the best discounts and what is the right time when they can get the best deals. So, as such our license deals are lopsided towards Q3 and Q4 and predominantly Q4 being a large part. Our revenues are largely high gross margin revenues and our cost basis are pretty fixed for the year. So, we expect to have a cost base growth of around 15-16% year after year which has been traditionally happening. And any revenue growth over that adds to the margin. So, as such what happens over Q3 and Q4 is that most of the margin gets accumulated. So, in our Q1 since the costs are very linear and we are also investing for the year, there are a lot of costs upfront in Q1. So, Q1 cost will be slightly even higher than 15-16%. Revenue growth being the same at roughly around 20%, the margins look very thin in Q1

& Q2. This has been the history of the company for the last 4 to 5 years. This is the same trend we see every year. And what we think as the company becomes larger in size and annuity revenues start becoming bigger through cloud and AMCs there maybe a gradual change in this pattern, but it will take some time.

Jaineel Jhaveri: So, as the cloud revenue keeps on increasing that should normalize across all quarters then, right?

Virender Jeet: Yes, right now the cloud is less than 5%. Cloud, ATS and Support are linearized revenues but then still that constitutes roughly around 40% of our revenue. We still have other major part which is slightly more lopsided.

Jaineel Jhaveri: And are you all expecting faster growth in cloud which would mean that the revenues would be more not front ended anymore, so the growth should look like it is showing down?

Virender Jeet: I think a part of that impact you can still see. When we are saying that the cloud business will grow at a much-accelerated rate and that has been growing over the last 7-8 quarters but when we are projecting our current growth rates, we are accommodating that transition as well. So, in case if we did not have a cloud transition we would have been growing at a much faster rate. But it is not a choice since the market is moving towards cloud and we are ready with our products as all the territories and customers start shifting. We are ready for that opportunity, but we think we can continue to maintain the growth momentum.

Jaineel Jhaveri: And who would be our competitors in the kind of products that we are selling?

Virender Jeet: I think generally the competition is from companies like IBM with its products in what you call FileNet, Lombardi and we have Pegasystems, a pure play BPM company. Appian is an interesting company in US which competes with us. Then there are also vertical companies, which compete in vertical areas with us. So, the competition is typically on a global scale, there are 4-5 top companies in ECM-BPM space and then vertical competition which is very geo-specific.

Moderator: Next question is from the line of Nagaraj Chandrasekhar from Laburnum Capital, please go ahead.

Nagaraj Chandrasekhar: You just mentioned Appian and you mentioned its an interesting peer – when I look at its financials, it is also a Nasdaq listed company, they just seem to be running at sort of cash breakeven levels and investing all their sort of gross profit dollars into R&D and sales and trying to grow as fast as possible and just raise lots of equity financing whenever possible. Just wanted to understand how you compete in the US for business with peers like that. What are the sort of advantages we have? I guess we have the advantage of implementing our product software into customers' platforms a lot faster than an IBM would. Does it also hold true for the case again Appian?

Virender Jeet: I think it is a good question. The core differentiation which we take to market is around vertical solution accelerators built on our products. So, for certain industries like banking, we are in areas like digital on-boarding, commercial lending, we are very strong in these domains and we are able to deliver the end value to the customer better than any other company. Beyond your product platforms, your go-to market has been always verticalized. So, in areas like Banking, similarly in areas like Health, with our deep domain and our product we are able to provide far better value than any other. But the competition as you said is head-on sometimes, so you know we do compete with Pega, IBM and Appian and it is typically the guy who can deliver best value in the least possible time to the customer, who ends up being the winner. So, if you have done business in similar areas, you have customer references in those areas that do help. So, there is no shortcut basically. We are very good in certain areas. In our five core verticals we have deep domain knowledge and we do our deliveries very fast. The customers get a commitment of a single company delivering products, solution, vertical domain knowledge that is the advantage they receive. And we do win quite a lot against all competition in these areas, while other companies could be very strong in other verticals.

Moderator: Thank you. Well, ladies and gentlemen, that seems to be the last question for today. I would now like to hand the conference over to Ms. Deepti Mehra for her closing comments.

Deepti Mehra: Thank you everyone for attending the call. If you have any further queries you can always get back to me or write to me and we will try to resolve the queries. Thanks.

Moderator: Thank you ladies and gentlemen. On behalf of Newgen Software Technologies Limited we conclude today's conference. Thank you all for joining us. You may disconnect your lines now.