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Scrip Code: 543933

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Scrip Code: CYIENTDLM

Sub: **Transcripts of Earnings Call**

Please find enclosed transcripts of earnings conference Call, in connection with the second quarter Financial Results held on 16 October 2023.

This information will also be hosted on the Company's website, at www.cyientdlm.com

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Thank You

For **Cyient DLM Limited**

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"Cyient DLM Limited

Q2 FY'24 Earnings Conference Call"

October 16, 2023

MANAGEMENT: MR. KRISHNA BODANAPU – NON-EXECUTIVE CHAIRMAN – CYIENT DLM LIMITED
MR. ANTHONY MONTALBANO – CHIEF EXECUTIVE OFFICER – CYIENT DLM LIMITED
MR. SHRINIVAS KULKARNI – CHIEF FINANCIAL OFFICER – CYIENT DLM LIMITED

Moderator: Ladies and gentlemen, good day and welcome to the Cyient DLM Conference Call. As a reminder, all participant lines will be in the listen-only mode and anyone who wishes to ask a question may enter star and one on their touchtone phone. To remove yourself from the queue, please enter star and two. Should you need assistance during the conference call, please signal an operator by pressing star, then zero on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Krishna Bodanapu, Non-Executive Chairman, Cyient DLM. Thank you and over to you, sir.

Krishna Bodanapu: Thank you very much. Good evening, ladies and gentlemen. My name is Krishna Bodanapu and I am the Non-Executive Chairman of Cyient DLM. Welcome to the Cyient DLM Limited's Earning Call for Q2 of FY24. Present with me on this call are Mr. Anthony Montalbano, the CEO of Cyient DLM and Mr. Shrinivas Kulkarni, the CFO of Cyient DLM. Before we begin, I would like to mention that some of the statements made in today's discussions may be forward-looking in nature and may also involve risks and uncertainties.

A detailed statement in this regard is available on our investor update, which has been posted to our website. While I will let Anthony and Shrini take you through the details of the quarter's performance, in summary, I would like to state that we've seen a lot of traction in aerospace and defense segment in Q2 that contributed to significant growth in revenues. Our clients are more invested in us than ever before and that puts us in a very good trajectory of growth.

As many of you are aware, Israel contributes to a significant or to a meaningful portion of our revenue and also a meaningful portion of our supply chain. The Israel-Hamas war is a new variable that we have to be aware of. Firstly, I would like to say we have reached out to all our clients, suppliers and the employees we have in the region and can confirm that they and their families are safe and we hope that that continues to be the case.

The war is likely to cause some challenges to the supply chain in the short term. However, it will also likely increase the demand for defense products in the long term. While it is too early to comment on the impact of growth, we're monitoring the situation closely to see how it unfolds for our customers, our suppliers, and ultimately on our business. I will now hand over the call to Anthony and Shrini to walk you through the business updates and the financial performance for Q2. Anthony, over to you.

Anthony Montalbano: Great. Thank you, Krishna. Hello, ladies and gentlemen. Let me take you through the highlights of the quarter and the business updates. We posted revenue of INR2,918 million with 71.5% year-on-year growth. A good part of that growth are from aerospace and defense segments. Our EBITDA for the quarter is INR235 million, with EBITDA margins at 8.1%, down 571 basis points in year-over-year terms, and we'll cover this in more detail in the finance section. Profit after tax is at INR147 million. This is higher by 106.4% year-on-year, and this is aided by other income that we earned.

Profit after tax margins are at 5%, which is 85 basis points higher on year-on-year terms. Our order backlog is at INR22,855 million, with a drop of 2,601 million from last year. This is primarily due to seasonal orders from the defense and aerospace segment. And let's move on and cover some of the key highlights of the quarter. So we had some awards that we've been recognized by. We've been recognized by IPC as a top Indian company, contributes significantly to the electronics sector's mission of build electronics better.

We also are the recipient of the Supplier Excellence Award from Honeywell Aerospace for developments of products in early supplier engagement. And another business update is that we have a new Bangalore facility that we're inaugurating in December, and we're also looking to expand our facility in Mysore to support cable harness business along with some other opportunities. From the pipeline perspective and key wins, we had wins across air and defense, industrial, we're 16.4 million TCBs spread over two to five years, and year-to-date order intake is a 41.9 million.

We did add two new logos in Q2 which we will be providing more detail on as we start to ship revenue to those clients. So some of the trends that continue to drive the growth for us in our business and really contributed to the momentum. The complexities in product design and development continue to drive an opportunity in the market for more partnership, more products that need to come to market, and it just has an overall impact on just literally the quantity of products that are available for our industry segment and also that are really available now to be supported in the regions that we operate in, specifically in India.

There's also really more so now than ever pressure on total cost of ownership. This really gets into the end-to-end cost of really what it takes to get a product into our client's hands. This is no longer measured at what it costs at the end of the production line. This takes into consideration costs such as inventory, supply chain, agility, flexibility, and this really all drives a more diversified supply chain, bringing risk down for our clients and helping them get a shorter time to market. So this is some of really the global EMS industry trends that have paid favorably for us.

So the sectors that we operate in are really the high value sectors within the EMS industry. In aerospace and defense, we are a market leader and we continue to see strong growth in this sector and this is along with what is being happening in the market. This is also a sector that is in a positive cycle and also falls into the low volume, high mix, mission critical, safety critical type of work that we do. Similar to what we see in medical and technology and healthcare, very similar type of quality standards and stability that we see in this sector and this is also an opportunity of growth for us in this area.

And industrial is another sector for us that continues to have, the need for, may not be, safety critical, but definitely mission critical applications that fall very nicely into the type of work we do for our clients. And all these sectors are amongst the, not only the highest value, but they're also the highest growth sectors that we're seeing in the areas that we operate. So, to expand a little bit more on our growth plan looking out, we are looking for new geographies and new industries.

Our clients are very global in nature and we see opportunities to expand our engagement with them in other locations outside of India. There's also -- it leads to an inorganic expansion, which can help enable that type of opportunity. And it can also have focus on expanding really the capabilities that we can bring to our clients and really bringing a -- more of a global model to our clients where you have a type of operation that is closer to their locations and then more scale available where we operate today.

We continue to strengthen our go-to-market strategy and account planning process. For us, this is a little bit more unique as we operate with a relatively smaller number of clients in our client base relative to the size of the business we have. Part of our strategy is to grow with large industry leaders and bring very high value services to them which lead to relatively low client turnover and program turnover.

Another opportunity that we see is to strengthen our participation in the India defense. This is a significant part of our offering and business today, and this is an area of growth that we will continue to expand in across various channels. And then we also see, due to our offerings and due to the types of engagements which involve design and manufacturing that we can leverage for our clients, we find that this enables some larger transactions that provide more turnkey solutions which allow us to close larger, longer term, more strategic programs which we plan to be announcing.

So I'm going to turn it over to Shrinivas who is our CFO to bring you through some of the finance updates.

Shrinivas Kulkarni: Thank you, Anthony. I'll take you all through the highlights of our Q2 financial performance and some other key metrics. In Q2, we did a revenue of INR291.8 crores which represents a growth of 71.5% year-over-year. With this the revenue for H1 is INR509 crores, which represents a growth of 49.6% year-over-year. I also want to highlight that the revenue split between H1 and H2 has roughly been 45% in H1 and 55% in H2 for the past three years. We expect the same trend to continue in this area as well.

Now EBITDA for the quarter has been INR23.5 crores which is 8.1%. From a year-on-year perspective, the EBITDA margin has declined by 571 basis points. Now this is on account of a few factors which I'll outline now. In Q2 FY '23, we had a significant one-off gain from the purchase price variance. Now this is not expected to repeat going forward and therefore we see that one-off playing out in this variance.

The second reason is the adverse revenue mix in the current quarter. The mix of revenue from low margin accounts was almost 2x of what it was in Q2 FY '23. This has also resulted in a sharp decline in terms of the percentage points. Lastly, the sales and G&A is higher in the current quarter compared to what we had in Q2 last year. These are planned investments for future growth.

PAT in Q2 is INR14.7 crores, which is a growth of 106.4% year-on-year. This is largely aided by other income gains due to the investment of IPO proceeds. So for the first half, we have a revenue and PAT growth of close to 50% year-on-year.

Moving on, this slide gives a mix of the revenue between various categories. Now aerospace and defense make up almost 70% of our business today. We expect industrial and medtech segments to represent the higher mix going forward as we are seeing more deals in those industries. The product category mix is like what we have seen in the past. We have several opportunities in cable harness and box build businesses. These businesses need higher realistic capacity and we are looking to expand to cater to these requirements.

Lastly, the export business is 58% in Q2 and domestic business is 42%. Now we don't have a particular preference and we will continue to look for opportunities in both these areas. Covering some of the key indicators, the order book for the period ending September 2023 is INR2,287 crores. Now this is reduced marginally compared to the previous quarters. One due to higher revenue in Q2 and two due to the seasonality. Now there are several large deals in the pipeline and we should see this number inching up as we move forward as those deals get converted into orders.

Our DIO -- inventory days for the period has reduced to 144 days. However, you can see that the customer advances have also reduced by almost an equivalent amount. Most suppliers are insisting on advances, which is bringing down our DPO. So consequently, despite the reduction in inventory and DSO, our overall net working capital has increased to 111 days in the quarter. Now this results in a free cash flow consumption in Q2 and overall even for H1 it's a negative free cash flow conversion.

We are working on a few initiatives in H2 to reduce the inventory and improve other levers on the working capital. On a full year basis, we expect the free cash flow to be moderately positive. This sort of concludes our presentation. We can now open up the floor for Q&A, if any. That's on the IPO proceeds. I'll just walked through that. Quickly, so far from the IPO proceeds, we have only utilized in two areas. One is to repay the external loan as we have stated in the RHP and the other is to sort of use the funds towards working capital. But the usage is given in the report.

Thank you and over to you for the Q&A.

Moderator: Thank you very much, sir. We will now begin the question-and-answer session. We have our first question from the line of Mihir Manohar from a Carnelian Asset Advisor. Please go ahead.

Mihir Manohar: Yes, hi. Thanks for giving the opportunity. And congratulations on good set of numbers. So I just wanted to understand what is the direct cost this quarter? I mean, just wanted to understand the gross profit. I mean, this number we were declaring last quarter. So I just wanted to understand the direct cost number.

My second question was on the one-off PPV gains. I mean, you mentioned about this fact. I just couldn't get it. I mean, what is this exactly of one-off PPV gains which were there in last time, second quarter FY '23? And if you can quantify that, that will be really helpful.

And my third question was on the fact that, we are seeing Boeing as well as Airbus looking to set up their facilities in the country, as well as increasing the sourcing from country as well. So I mean, if you can mention what is the kind of impact which will be there, what kind of inquiries are you seeing? That will be really helpful, specifically both from the aerospace and defense side, even from the local defense, that will be really helpful. Yes, so those were the questions.

Management: So Mihir, I'll take the first couple of questions. On the gross profit look, I think the problem is the companies are all defining it very differently. We can discuss that and therefore I think it makes sense for us to look at the EBITDA numbers at this point in time. I do not think we declared that in Q1 also. So maybe if you are referring to the RHP or DRHP, that's a different matter. So that is one.

And on the PPV gains, look, I think there is price protection for us in all the customer contracts. And last year was a very unusual situation where there was significant supply chain constraints. And we had to sort of procure parts at a much higher cost than what they were originally in the contract. So while the original cost was margins that book, it took a while to sort of go back to the customers and get those -- the sort of recovery from them. And all of that came in Q2. So it had more than one quarter of PPV and a much higher level.

Now, we have PPV even in the current quarter, but it's a very different situation today. I think it's more stable supply chain situation. And therefore, the numbers are, there is a one-off in the Q2 of last year.

Mihir Manohar: Sure, sir, sure. And what would be the value, the Y-o-Y comparison for this one-off PPV gains, what was the value last time? And what is the value this time?

Management: No, I mean, look, the overall impact of 500 order of basis points that we see in terms of drop, half of it is because of the PPV, other half is because of the mix. Right? So you can do that.

Mihir Manohar: Okay, sure.

Anthony Montalbano: Yes. And then your question regarding the aerospace, growth in region, this is very much in line with what we are seeing in our discussions in this segment. This is probably the fastest growing area of our business today and is also a good part of our business as well. So we do see a lot of opportunity there and this will be a key area where we are looking to announce some programs here in the coming quarters.

Management: And I think, sorry if I may just add to that, when Boeing and Airbus announced their facilities, typically it's a system integration facility. So there's a lot of sourcing that happens in-country and that's what positions us actually very, very well because they typically build the whole plane or a major system at least. But all the components, the subsystems, the sub-assemblies are provided by us. So it's actually a very good news for us because they also want to localize the supply chain when they do an in-country facility.

Mihir Manohar: Sure. And just lastly, one more question. I believe you mentioned that you already told you logos this quarter. So I mean, it is difficult, particularly in this industry, to add logos. So I mean, which are these areas where these logos have been added? And what is the kind of potential which will be there? Because it is typically difficult to add logos in this industry. So just wanted to get an understanding of what kind of potential opportunity can be there from these two new logos?

Anthony Montalbano: Yes, so in this case, the two logos that we did add, they are primarily aerospace and defense, one of each. And again, we will be announcing the -- we plan to announce the company specifically once we start to ship revenue in that regard. So I hope that helps answer your question.

Mihir Manohar: Sorry, I didn't get it.

Anthony Montalbano: I said of the two logos, one is primarily aerospace and the other one is primarily defense. They're large, multinational, both cases, large, multinational suppliers in each one of these respective categories. And this kind of aligns with two logos of this caliber is very much in line with what we look to aspire as far as new client addition. For us, a couple key logos like this, a quarter, creates tremendous potential for us. So, our business is different as opposed to having to add 8 logos, 9 logos, 10 logos that might be more in line with a higher volume business where there's more churn in that regard.

Mihir Manohar: Sure. Understood. Yes, that's it from my side. Thank you very much. I will come back in the queue.

Moderator: Thank you. We have our next question from the line of Venkatesh Balasubramaniam from Axis Capital. Please go ahead.

Venkatesh B: Yes, thank you for this opportunity. Now, is it possible to share what was the forex gain in this particular forex gain or loss in this particular quarter in other income?

Management: Yes, there is no forex gain Venkatesh. There is a forex loss. It's due to our contract with one of the larger Indian defense players here, right? I think the contract does provide for protection on foreign exchange after a certain volume and we haven't hit that volume threshold yet. So this financially we will be exposed a little bit to the forex fluctuations.

Venkatesh B: Okay. Now, is it possible to quantify, I think the first quarter you had like a three million kind of a forex loss. What is the forex loss this quarter?

Management: It's a roughly half percentage of the current quarter's revenue.

Venkatesh B: Okay, okay, fine. Now, you mentioned about the Israel-Hamas war. Now, what I remember is you do have some amount of exposure to Israeli defense. Is it a direct exposure or is it via Bharat Electronics?

Management: It is via Bharat Electronics. There is some direct as well.

Venkatesh B: Okay. Now, why will – will this Israel-Hamas war in any way affect your execution per se? I mean, I don't see why it should impact your execution because you're executing in India. I mean, are you getting raw materials or components which are coming in from Israel?

Management: Yes, we do have some components that come from within the country and that also is one key aspect and we're also just very cognizant that there can be the opportunity for potential logistics or supply chain disruptions. Now, we are cautiously optimistic based on direct feedback that we've received from all our suppliers that we've reached out to within region. I think there's maybe two that we have not directly but again, basically the full feedback has been business as usual, but again, we are feeling it's important to set appropriate expectations that such disruptions could occur based on the situation.

Venkatesh B: Okay, understood. Now is it possible for you to share what is the pull form for PPV? What is PPV?

Management: Purchase, price, variance.

Venkatesh B: Okay, and what is TCV? You mentioned TCV in your presentation.

Management: Total Contract Value.

Venkatesh B: Okay. Okay. Thanks a lot. Now, is it also possible for you to share first half, what was the growth of your export business and what was the growth of your domestic business, Y-o-Y? Some approximate numbers.

Management: I'll have to get back to you.

Venkatesh B: Okay, now the reason why I'm asking is one of the other players, listed players are telling us that the US clients that they have, they used to hold a lot of inventory at the time of COVID. But now they're holding less inventory. So what is happening is a lot of US clients are actually destocking. So because of that, Indian EMS players who export to US, they're having some kind of a slowdown. Is this something that you are experiencing or in your clients, you're not experiencing this?

Management: We are not seeing a slowdown in the sectors that we are engaged in. We are seeing inventory lead times come down and we are seeing in certain applications outside of aerospace and defense where there are long lead aspects that material is being consumed. And so, as that's being consumed based on the fact that it was maybe bought beyond their need to address a short-term supply issue we are kind of -- that's kind of now getting worked through. So I would call it more of an equalizing of how the supply is getting consumed as opposed to it genuinely being a slowdown. At least that's how it relates to the sectors we're in and the clients that we're engaged with.

Venkatesh B: Okay, that is very insightful. One last question from my side. Now, this is how, what we hear from other EMS players, that normally the active and passive components are made either in Taiwan, Malaysia, or China. And then these active and passive components are then brought in by traders who are based out of Singapore. And it is from Singapore that you people purchase the entire Indian EMS inventory. Companies actually purchase a lot of these products. Now, is this, what I'm communicating, is this correct? Or please do correct if I'm mentioning something wrong. And are any of these people who actually bring in products to India, are they talking about setting up warehouses in India? And is that a way to reduce inventory cycles for the Indian EMS industry? Is it possible?

Management: So the supply path can vary and so what you've highlighted, some aspects of it sound correct. For us, some aspects are maybe a little different. So, specifically, we don't have – I don't think we actually have any supply coming from China in our business. And then, the path through Singapore, I think we have some of that, but I don't think that's a material portion, as in a large portion of the scenario that you highlight.

A lot of our components do come relatively globally, and then the other piece is there is a significant trend and a significant ask from our suppliers to localize. And so that supply chain over time will start to become more local. And that is a key strategy for our company and also for what we are seeing as direct asks and aspirations from our clients.

Venkatesh B: Okay, thanks a lot. All the very best for the second half.

Management: Thank you.

Moderator: Thank you. Ladies and gentlemen, in order to ensure that the management is able to answer queries from all participants, please restrict your questions to two at a time. You may join back the queue for follow-up questions. We'll take our next question from the line of Nitin Sharma from M.C. Pro Research. Please go ahead.

Nitin Sharma: Yes, thanks for taking my question. To start with, just want to understand the new projects build. So all of these are PCBA or there's a mix of box build in there. And also, how do you see the medical technology business recovering in the second half?

Management: Could you repeat the second part of the question? I understood your first part about the type of work, but what was the second part of the question?

Nitin Sharma: The medical technology business, so this is second quarter of the decline, how do you see the recovering in the second half of FY'24?

Management: Okay, got it. So, first of all, as far as the type of work that's making up what we are shipping out, it is the PCBA is the – PCBA assemblies are the, from a revenue perspective, the most significant part of our business, right? So that would probably make up, on average, 70% of the overall revenue. You are then looking at maybe 20% additional that's associated with the box build. That can vary in each one of those, plus or minus 5% or so. And then we do have some other type of mechanicals and cabling business, which is a little bit more I'd call vertical integration or additional offerings in that regard.

As far as the medical business, the decline that we have had is primarily due to a larger local client supporting COVID in India. And when I say supporting COVID, I mean it's a medical device that was assisted with the testing. So, that demand for that client has, of course, dropped. Medical, though, broadly is the growth area for us and a key opportunity that we see and are in various dialogues from an organic perspective and also an inorganic perspective. So, we don't see any slowdown from a market sector perspective. I'm not sure if that was your question or if it was more specific to that one client we had.

Nitin Sharma: Okay, and are you confident to maintain double digit bid margin EBITDA for the full year for FY'24? Given the how far staff has gone?

Management: Yes, so our target has been to have the double-digit margin, and as we look at the business, as we are investing in the business, especially with the growth that we have had, there are aspects to where we will look at making investments on the front end and our goal is to be close to those margins. And as the year progresses, as we see how costs come out overall, we'll maybe provide some more guidance in that regard. But our overall strategy is to run a business in the high-value segments that we've highlighted and we're going to continue to work on that.

Moderator: Thank you. We have a next question from the line of Arafat from Incred Capital. Please go ahead.

Arafat: Yes, hi, sir. Thanks for taking my question. So my first question is on order pipeline. Can you please guide what is the kind of order pipeline and order inflow for FY'24 and FY'25, if you can guide on that?

Management: So from an order pipeline, I don't know if we give specific numbers on a pipeline, but what we can say is that we really do vet our pipeline to make sure that it is representative of the true value of the opportunities that we have in front of us. As far as providing forward projections, what we can say is that it has continually been in the, roughly in the ballpark of a billion-dollar pipeline overall.

Now, again, that can move a couple hundred million either way as deals and opportunities come and go, but that just kind of gives you an idea of the overall scale of the pipeline relative to our current business today.

Arafat: Okay, so and my second question is on, let's say, I just want to confirm, how the business model or let's say bidding process has changed when you were part of client limited and now independent team. So how that has changed in terms of, let's say, bidding process and the new client edition, is there any change in that process?

Management: There is no change in that process as far as how we run business, right? Really the fundamental change is that we have a dedicated leadership team, a dedicated board of directors that is focused 100% on the business. And we've had to invest to put that structure in place, and this will actually enable us to continue to provide the growth that we have – we have for process if for this business. As far as have we've got the make decisions that we've make with key clients, I don't think there's really any fundamental change. If anything, I would say we're maybe even more cavalier with the focus on where the EMS business is going specifically, we're in a position to take investments and make the right that's on the right opportunities.

Moderator: Thank you. We have our next question from the line of Rakesh Wadhwani from Monarch AIF. Please go ahead.

Rakesh Wadhwani: Hi, Sir, thank you very much for the opportunity. Sir, I have a couple of questions. We can see in this quarter, there's a sharp jump in the networking cycle, and especially the better days and the payable days has come down, customer advances have come down. So is my understanding correct? One of the reasons for decline in payables is because of the execution of orders from the different segments and wanted to understand, what will be the networking capital cycle at the end of FY '24?

Management: So, look, the receivables coming down is good news. I think payables have come down for a couple of reasons. One, the sort of products we are consuming, the raw materials are in huge demand, and so the vendors also have stopped giving any credit. So they ask for advance, because there are many people buying the same product at this point in time.

See, we are working on all the levers right now. Our intention, as we have mentioned before also, is to hold networking capital days of between 90 and 100. And that is where we hope to be by the end of the year.

Rakesh Wadhwani: I am just repeating the point, 90 day to 100 day networking capital cycle by end of FY '24, is it?

Management: Right.

Rakesh Wadhwani: Okay, thank you. And can you please talk further on the Israel war? Has he, so has he procured, is anything that is coming from the Israel has been procured or anything that is about to come from Israel with respect to the raw material that we have not procured and that may delay the order execution?

Management: So at this point in time, there has not been any updates in that regard. So in the relatively short time this has been going on, we have not seen any changes to our business engagements at this time.

Rakesh Wadhwani: Okay. That's it from my side. Thank you.

Moderator: Thank you. We have our next question from the line of Deepak Poddar from Sapphire Capital. Please go ahead.

Deepak Poddar: Yes. First of all, thank you very much for the opportunity, sir. Sir, first of all, on the EBITDA margin, earlier also, we have been quite vocal about our margin range being 10% to 11%, right, and so this quarter because of revenue mix, we had some impact of maybe what 2.5%. So if we adjust that, we would be in that range 10% to 11%. So ideally how do we see that going forward? Is that the range, one should look at as we progress or the revenue mix that we have seen is more of a, in the medium term, it's more of a permanent thing?

Management: No, the revenue mix is very unique to this current quarter, where the revenue coming from low margin account is very high compared to what we have seen in the earlier quarters. So it's a point in time thing. I don't think the same mix of revenue is expected in H2, for example, right? Compared to what we have in Q2. Having said that, on the margins, like Anthony also explained before, there are certain opportunities to sort of invest in supply chain and go to market, etcetera.

So while our operating margin, the expectation is that, we stay flat year-on-year or in a double-digit range, there will also be some calls that we will have to take on certain investments. And therefore, we don't want to be fixated on the margin. As long as we feel comfortable about running this business, we will not hesitate to invest in growth. And so therefore, that's how we should look at the margins.

And also, it's also a trade-off between ROC and margins, frankly. At some point in time, we might also get into businesses which yield better returns on capital employed and not so much on margins. So that might also change. But at this point in time, yes, our intention is to operate at a double-digit margin. But there are some practical realities on the ground which we are facing.

Deepak Poddar: Okay, so basically what you are saying is that, 10% to 11% or double digit margin is what we generally target, but if there is some investment or something that comes up, you would not hesitate to do that at the cost of EBITDA margin, right?

Management: Absolutely.

Deepak Poddar: Okay, fair enough. And in terms of order backlog, what's the current order backlog we have and how do we see that as we progress by the year end?

Management: So we have roughly INR2,300 crores right now, right? So we see that going up, it's hard to put a number, it all depends on how many deals we can close, but there are several deals in the pipeline and we are expecting good traction, we expect good traction in terms of closure, right, so yes.

Deepak Poddar: Okay, I think, that's it from my side, all the very best to you, sir.

Management: Thank you.

Moderator: Thank you. We have our next question from the line of Ankush from Axis Securities. Please go ahead.

Ankush: Sir, thanks for the opportunity. My question is related to the extension of the previous one. So last year, we had an order in flow in approximately in the range of $250 million. So just in the first half, it is $43 million. Just trying to understand, what kind of order inflow we are looking at the end of this year?

Management: It's hard to predict the number. We definitely have significant deals in the pipeline and we expect the order inflow to continue to increase, right? Now that the $250 million is a point in time thing, the moment you close one deal that number will change. We also have very good revenue in the first half of this year, so it's a function of that.

So our attempt is to sort of keep pace with that revenue growth in terms of order book as well. Right? And so it's hard to predict the number, but we are confident that the order book will continue to grow from the current levels.

Ankush: Thank you, sir. Thank you very much.

Moderator: Thank you. We have our next question from the line of Karan Sanwal from Niveshaay. Please go ahead.

Karan Sanwal: Yes, thank you for the opportunity. I have a couple of questions on the cable wire harness business that you have. Yes, so I have a couple of questions on the cable and wire harness business. I know that it's still a small segment for the company but I wanted to understand that, as they're expanding their capacity in the Mysore facility, so how much revenue can, how much contribution can the segment make in the overall revenue? And split between the current capacity we have and the expanded capacity?

Management: So we see a lot of potential in the cable harness business, right. There is a -- there is quite a lot of deals that we are working in the pipeline and even customers have reached out to us with demanding higher work. Now the cable harness business, it needs more real estate capacity than machining capacity, right? So therefore we are expanding in Mysore at this point in time. We will announce it as soon as the expansion takes place. But we are in very advanced stages of that expansion. And that will be sufficient to sort of grow that business 10x from where it currently is.

Karan Sanwal: Okay. And I also wanted to understand like, who would be our clients, like do we have a client in the defense or maybe we have clients in the commercial aerospace and what would be the sustainable margins in the segment as a whole?

Management: So the clients are across the board in all of the industries where we have presence, mostly in the industrial, aerospace, and defense segments. So they are some of our existing clients as well, where the conversations are happening. The margins in cable harness business tends to be higher than your regular margins, simply because it's a more headcount intensive business. So yes, we can expect to get the same sort of margins, so what we have currently in the business today, which is higher than our average margins.

Karan Sanwal: Any range, can you specify it?

Management: It will be hard to put a range. Each deal is different, but on an average, we can safely put them 250 to 300 basis points higher than the average.

Karan Sanwal: Okay, great. Thank you so much for that answer.

Moderator: Thank you. We have our next question from the line of Navid Virani from Bastion Research. Please go ahead.

Navid Virani: Hello. Hi everyone. Thank you for the opportunity. So I have two questions. First one is since we have a parent like Cyient Limited, with strong R&D, strong engineering and tech capabilities, what kind of synergies as an investor one can expect in the mid to long term by this virtue? Any directional thoughts there will be very helpful. And secondly, just wanted to understand as to, are we currently pursuing any inorganic opportunities? And if the answer to that is yes, can you give some sense there?

Management: Yes, so let me take the second question first. The inorganic piece is a key part of our strategy, and I'll just kind of highlight the two main items that are prioritized in that regard come down to the capability and also the footprint. And so we are in discussions with several opportunities and we hope to progress those, so that will really broaden our offering and footprint and capabilities to our clients and also expand our client base in that regard. So, and then, I didn't quite catch the...

So, yes, so then just regarding the engineering capabilities, this still remains to be a true differentiator for an EMS company, let alone an EMS company of our size to really have 7,000 design engineers available to us. And when I say available to us, this is part of Cyient Limited. And so, even very large EMS companies would not have anywhere close to this scale of design capability.

And so, we are in a unique position where we can go to clients and sit at the table and really provide true design through manufacturing offering. And this is a key part of our strategy. And so, even though today, this is a relatively smaller portion of our revenue, this is going to continue to fuel some of the new opportunities and newer larger programs that we plan to announce.

Navid Virani: Sure. So lastly, just in continuation with your answer, can one expect, again, I'm not talking about one year or two years, I'm talking about three years to five years gap, can one expect the build to specification part to maybe reach closer to 20% of that chart? Is that...

Management: Yes, so that's a very good question. My point of view is, if you look at the industry, I'd say the build-to-specification aspect is probably 90%, maybe even 95% of the EMS industry. If you look at the revenue, especially in the sections we play, it's primarily built to print. Build-to-spec is maybe 10% of that. Now, in our business specifically, which aligns to those percentages, we see the built to spec piece growing in a material way.

Now, what that means is, if it's 10% for us today, in three years, it’s not going to be 30% or 50%, but it'll probably be 15%. Maybe in five years, it might be 20%, which is actually quite significant when you look at how long it takes to have a shift in a business model in these sectors. And so this is our outlook on it, and we see this as a differentiation and an opportunity for us.

Moderator: Thank you. We have a next question from the line of Vipraw Srivastava from Incred Capital. Please go ahead. Mr. Vipraw Srivastava, please go ahead with your question. Since there is no response, we'll move on to the next question from Prafull Rai from Arjav Partners. Please go ahead.

Prafull Rai: I wanted to – in the earlier part of the call you said that you have a billion-dollar kind of a pipeline. I just wanted to get some handle in terms of what is the success rate of this pipeline into actual orders. Is there a percentage you can quantify, say 20%, 30% or some kind of a number that will help us in terms of understanding the future position of the company?

Management: Was the question how much of that is firm orders? Or no.

Prafull Rai: No, you said your pipeline is a billion dollars. What is the expectation of conversion of this pipeline to actual orders? And generally, what is the hit rate like?

Management: Yes I think that's going to be difficult to give guidance on. You know the pipeline is I think that's maybe a bit difficult to give guidance on. Maybe you know conversion rate in our industry for a pipeline like that might be about 30%, 40% would be a good conversion rate. Some companies operate at 20%, even 25%, which I think is on the lower end of what an appropriate conversion rate would be.

Since we tend to play in a more higher capability, higher quality segment, we believe that we are going to run in the higher bounds of those conversion rates due to the type of work we provide.

Prafull Rai: Okay, what is a typical, see once you get an order, I'm talking of a blended as a whole, what is the kind of execution time that the customer gives us?

Management: You mean the execution time to deliver? Well, that can take, our current pipeline today is averaging over two years to deliver on it. Our current order book at least, as far as what we have booked. Now, so it depends on the nature of the program. So in the sectors that we play, especially, air and defense, medical and industrial, air and DB and a little bit longer, bit longer, you're looking at a longer conversion time to work through that due to the nature of those programs.

So, it could be a year and a half, it could be a year, or even more, just depending on the specific program and the development aspects of it.

Moderator: Thank you. We have our next question from the line of Vipraw Srivastava from Incred Capital. Please go ahead.

Vipraw Srivastava: Okay. Just had a couple of questions. I wanted to understand that you have businesses across aerospace and defense, industrial and medical. So if you can give me any semblance about segmental operating margins. I mean, roughly, roughly, if you don't want to give the exact numbers of that, or which is the highest, which is the lowest?

Management: Yes, so the sectors overall, if you take specific accounts out of it, and you just look at the sectors overall, they actually in our business deliver similar margins. Now, we do have a couple large specific defense programs, which do run at a lower margin. But that's not to be representative of defense work in general.

So our forecast as we look our split of business across these three sectors, air and defense, medical and industrial, we see the share of that business equalizing. We expect our overall margins to remain consistent as the returns across these three sectors are relatively similar. Where we see more variability in margins come down to specific client and specific product type engagements. That's where we'll actually see more variability in the margins.

Vipraw Srivastava: Right. Just had one more question. So the PCB assembly, which we do, if you can tell me what is the average number of layers for a PCB assembly, which we do? I mean, roughly, if you can give me that idea, just to understand how complex it is?

Management: Yes, two is probably even thin. Yes, we're kind of trying to, Yes, we're guessing somewhere between two and 14. Even two seems a little bit low. So, you know, it really is high complexity, low volume, high mix, high complexity type product. So, this is just the nature of our business. We really don't run any high-volume, consumer, low-layer type product. That's kind of a different business model.

Vipraw Srivastava: Right. So, is it more than 600 roughly, any number you can give?

Management: It just depends on the product. Is there a certain outcome you're looking for that?

Vipraw Srivastava: Okay. So, just one last question. So, the kind of assembly which you did, let's say, five years ago in 2017-18 and the kind of assembly which you're doing now, has the level of complexity increased or has it remained the same? I mean, any qualitative view on that?

Management: I don't know if it's necessarily increased. We've been operating in this sector for decades. So this has been the nature of our business. We are not necessarily taking on more complex programs, and I wouldn't even tie the number of layers on a PCB directly to the complexity, right? So, testing requirements can play a big part of it.

The type of product – so, for example, an RF product might have more variability compared to another type of product. So, it's really specific to the product, the test requirements, the yields, are there power supplies involved which have, you know, more variability? Like, you know, conformal coding that go on the board. There's many, many aspects that really play into that.

Vipraw Srivastava: Right, right. And one last question. So, with the SG&A expense increase, I mean, what is it for exactly? What exactly is High End DLM doing with the increased expense? Just wanted some clarity on that?

Management: So we are looking, you know, we are looking – we mentioned some expansion in – from a go-to-market perspective. And when we look at the types of opportunities in front of us and building out really a global type of solution that we can bring to market at this scale, and then also the growth rates that we have, we're taking calls on leadership that include areas like supply chain, program management, go-to-market, we're looking at facilities, capabilities like cable, wire harness that we discussed.

So all these types of investments, be it facility, capability, people, leadership, execution, those are all the types of examples. And so, we're calling this out that the margin expectations, we want to make sure we capture the growth that's available to us, but also balance that we don't take too much of a hit on the bottom line. So again, right now we're in growth mode and we are looking at making the right investments, and that's why we're taking certain calls where we need to.

Vipraw Srivastava: Right. And last question, so this imports currently, export is around 60% and last quarter it was around 70%. So how do we see it? I mean, where should ideally be for the entire year, 60, 70 only or we expected to further decrease? How are you seeing that?

Management: I think it stays about the same. Yes, it stays the same in that ballpark. I think it might change a bit over time, but no, I think it will be consistent for now.

Vipraw Srivastava: Okay. And any Indian players…

Moderator: Mr. Srivastava, I request you to join back the queue, please. Thank you. We'll take a last question from the line of Deval Shah from Rbsa Investment Managers. Please go ahead.

Deval Shah: Yes, I just have a question with regards to the design capabilities. I was understanding that we are relying on our parent's time for the design capabilities. So what is our arrangement with our promoter? And also, what are we thinking about building up the same capability in-house going forward to four or five years or 10 years down the line?

So are we thinking on building up our own independent design capabilities so that we are able to provide this service in a more independent and flexible way? So these are the questions.

Management: This is a very good question because the execution of it is really what really differentiates what Cyient can bring to the table. So we can go and meet with a client. I can bring the CEO of Cyient Engineering into that meeting and we can provide a solution that can provide $10 million of design work and $100 million of manufacturing and that's a solution and we have, we're one company.

We really are one Cyient. So that's just a natural advantage where we can bring that solution. We don't have to negotiate terms with a partner or go in with a partner, design, decide who's prime and who's secondary and then get into markups on services etcetera.

So for us it's very much like going in with a family member or let alone the same team. We work together on programs, everything from design through pricing through execution. So it's really very much an integrated solution.

Deval Shah: Okay, just a follow up on this. So what I can see that even after five years, then you have said that optimistically you would like to have your Build-to-Spec approximately 18% to 20% of the revenue contribution. So the margin difference between the Build-to-Spec it's not going to be much different, right? It is going to be in line with our overall margin?

Management: We believe it will actually be higher. Build-to-Spec programs do yield higher margins because we can design in our own supply chain and it provides higher value to the client. It also has engineering services, which are higher margin services in general. So you add that all up, what might be 9%, 10% program in a build to print scenario, it'd probably be maybe two to three points higher in a Build-to-Spec scenario. And that's to mean we're not owning IP, which is not part of the plan.

Deval Shah: Okay, so why I was asking this question was that because we'll be sharing a part of this revenue with our parent also, so that was the reason I was coming, I was saying that the difference between those won't be that much of material. Anyways, I got my answer.

Moderator: Thank you. Ladies and gentlemen, I would now like to hand the conference over to Mr. Krishna Bodanapu for closing comments. Over to you, sir.

Krishna Bodanapu: Thank you very much and thanks to all the participants. As you heard from Anthony and Shrini, we had a good quarter, but of course there's also good momentum that's building up on the business. There are some uncertainties, especially with some of the geopolitics and the dependency that we have on Israeli customers and supply chain.

But I want to assure all our investors and shareholders that we're well-focused on not just identifying but mitigating risks and really focusing on delivering the growth that we committed for the rest of the year. Thank you for the support and we'll again speak next time. Thank you.

Moderator: Thank you. Ladies and gentlemen, that concludes this conference. Thank you for joining us and you may now disconnect your lines.