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Q2 FY2025 Earnings Call Transcript

MAIN Participants:

A.S. Lakshminarayanan, Managing Director and Chief Executive Officer

Kabir Ahmed Shakir, Chief Financial Officer

Rajiv Sharma, Vice President and Head, Investor Relations

Sudeshna Patnaik, Deputy General Manager, Investor Relations

Sudeshna Patnaik

Good evening, everyone, and a warm welcome to you all. Thank you for participating in the Q2 FY25 Earnings Call for Tata Communications. My name is Sudeshna Patnaik, and I'll be your host for the call. We are joined today by our MD and CEO, Mr. Amur Lakshminarayanan; our CFO, Mr. Kabir Ahmed Shakir; and our Head of Investor Relations, Mr. Rajiv Sharma.

The results for the quarter ended 30th September 2024 have been announced today and the quarterly data pack is available on our website. We will begin today's call with opening remarks from Lakshmi on the business performance and outlook, followed by Kabir on the company's financial performance. All participant lines will be muted for the duration of the call. There will be an opportunity for you to ask questions after the management remarks.

Some of the statements made in today's call may be forward-looking in nature and are subject to risks and uncertainties. The company does not undertake to update these forward-looking statements publicly.

With that, I would like to invite Lakshmi to share his views. Thank you, and over to you, Lakshmi.

AS Lakshminarayanan

Thank you, Sudeshna. Welcome to the Q2 FY25 earnings call. I am very pleased to share that this quarter we have delivered a good revenue growth driven by our digital portfolio.

Our consolidated revenues grew 18.4% YoY and 2.4% QoQ. Data revenues were up 21% YoY and 3% QoQ. Digital revenues grew 52.4% YoY and 3.6% QoQ. Core connectivity growth is muted at 3% YoY and accounts for 54% of our data revenues this quarter. Digital services account for the rest, 46%.

Our EBITDA margins came in at 19.4% and our PAT grew by 3% YoY and came in at Rs. 227 crore. Muted growth in core connectivity, combined with the expenses due to Red Sea and other cable cut related costs dragged our margins this quarter. That said, Red Sea cable is largely repaired and starting Q3, the revenue drag due to these cuts will be behind us. Consolidated EBITDA improved 10% YoY. However, it was down marginally by 0.6% QoQ.

Our net debt-to-EBITDA ratio stands at 2.37x. I would like to apprise you of the progress we are making on the asset monetisation side. We have submitted for shareholder approval, the sale of the land parcel in Ambattur Chennai. This is in line with our strategy to enhance shareholder value by unlocking non-core assets.

On the order book and funnel side, our funnel continues to be robust. Although the funnel addition has remained subdued in H1, we have witnessed an improvement in our win rate across all the regions. The improvement in win rate in H1 can be attributed to the large deals that have come in this year. On the back of this improving win rates our order book in Q2 has increased by upwards of 25% YoY. The growth in order book is driven across all segments in India and international, except the service provider segment. Our international region has registered the highest quarterly order booking in the last 5 years.

Our core connectivity order book is driven by hyperscalers and OTTs. Our core connectivity revenues came in at Rs. 2,613 crore and grew by 2.5% QoQ and 3% YoY.

India's data centre industry is rapidly expanding, and we continue to be the market leaders in data centre to data centre connectivity space. We have signed major deals with hyperscalers for multi-year network build and capacity upgrade.

For instance, for one particular hyperscaler, we are building the long-haul dedicated network, connecting their data centres across different states. The deal is large and complex and its scale of operation in terms of the size with a multi-million-dollar TCV. Spread over a period of 10 years, the revenue for this deal will start coming from FY26.

We continue to expand our fibre network infrastructure in the country. We have a strong network presence in Tier 1 and Tier 2 towns and serve large enterprise needs. The rising prominence of Tier 3 and Tier 4 towns is creating new pockets of growth. We have been deepening our capillarity of our network in these areas to further augment our leadership in the enterprise data network market.

Coming to the digital portfolio performance. This quarter, our revenues came in at Rs. 2,221 crore and 3.6% QoQ and 52.4% YoY, this growth is broad-based.

We are pleased to report that our incubation business, which is our IoT fabric, and it has grown in revenues by 33.8% QoQ and 58% YoY. The key highlight has been MOVE platform, which benefited from robust usage growth coming from addition of new vehicles. Further, there was an increase in our platform revenues as there was a rise in SOTA campaigns. We deepened our relationship with our existing customers by signing them on for enhanced platform proposition, particularly our intelligent connectivity solutions.

Our collaboration and managed CPaaS portfolio, which is our interaction fabric, grew by 6.6% QoQ and 174.2% YoY. The Media business has seen a QoQ decline of 14.2% on the back of the sports calendar and large one-offs in Q1 like the T20 World Cup and Olympics, which we had in Q1.

Cloud and Security revenues are flat this quarter. The segment continues to see improving traction within the BFSI space particularly. The pipeline of deals in this segment is healthy. We are encouraged by the opportunities in this segment, and the deals that we have signed in Q1 and Q2.

The next-gen connectivity, which is our network fabric, grew by 4.5% QoQ and 7.7% YoY. The three pillars of next-gen connectivity services, namely the managed Wi-Fi, IZO hybrid WAN and IZO Multicloud Connect are addressing the enterprise customers' end-to-end network transformation needs to connect the end users and enterprise to the applications in the cloud.

Our digital fabric continues to resonate well with our customers. We now have industry analyst recognition across all the four fabrics, reflecting our strong value proposition. You may refer to our Q2 press release for more details on the same. Our solid value proposition, coupled with our long-standing relationships with large enterprises gives us the conviction to profit from the market opportunity.

With that, I'll now request Kabir to share the financial highlights.

Kabir Ahmed Shakir

Lakshmi, thank you. Hello, everyone. Let me walk you through our financial performance for the quarter. The Q2 FY25 revenue growth driven by data and digital portfolio came in at Rs. 5,767 crore, consolidated growth of 18.4% YoY and 2.4% QoQ. Data revenue for the quarter came in at Rs. 4,834 crores, a growth of 21% YoY and 3% QoQ.

Digital services revenue for the quarter came in at Rs. 2,221 crores, a growth of 52.4% YoY and 3.6% QoQ. Emphasising that business fundamentals continue to be strong. The most heartening part of our digital businesses is that we are incubating new businesses to drive long-term sustainable growth.

As Lakshmi mentioned, we have put forth for shareholder approval the proposal for land parcel sale in Ambattur. The estimated range for final sale consideration is expected to be between Rs. 750 crore – Rs. 850 crores. This action is in line with our strategy to monetise non-core assets.

Let me add that we are taking multiple strategic measures, which will start benefiting us in the quarters to come. These include strategic review of non-core assets, an assessment of their monetisation opportunities, strategic evaluation of pockets which may not offer longer-term leverage and strategic review of subsidiaries, which we had suggested earlier. And we are making good progress there. These measures will allow us to reposition our assets to drive longer-term value creation and maximise resources to invest behind our growth.

Additionally, another set of measures are being pursued towards simplification, be it on the process side or the cost structure to ensure that our company is competitive for future opportunities. To drive all these measures, some of the costs will be upfront and are being incurred now. And over the next couple of quarters, we believe that with these strategic measures, combined with the right capital allocation, and a robust governance framework, we are well placed to accelerate growth and maximise shareholder value.

Our EBITDA margins for the quarter were at 19.4%. We'll continue to make efforts to stay in the range of 20% for the consolidated full-year FY25. Our interest costs were higher this quarter, driven by an increase in short-term borrowings and the change in mix as there was an increase in INR borrowings. On the tax component, there are two highlights. First, there was a one-off tax payout of Rs. 113 crores as we accelerate our process of streamlining and aligning various entities in various geographies to enable longer-term beneficial outcomes. The second being, we assessed the certainty of utilising the past capital losses and recognise a deferred tax asset of Rs. 84 crores for the quarter and the period ended September 30, 2024. Our PAT was up by 3% YoY.

FCF for the quarter was negative Rs. 194 crores, significantly better than the previous quarter, and the drag was primarily driven by increase in working capital. Net debt for the quarter stood at Rs. 10,483 crore and net debt-to-EBITDA is at 2.37x. With our land monetisation stated above, we see our leverage ratios improving meaningfully over the next couple of quarters. Cash Capex for the quarter stood at Rs. 447 crores. ROCE came in at 16.4, a decline of 110 basis points QoQ. As of this quarter, the full impact of Kaleyra has been picked.

Moving to subsidiaries. TCTS revenues declined by 26.4% YoY. EBITDA margins came in at 12% and EBITDA improved by 36.3% QoQ. Our payment business reported a healthy double-digit EBITDA margin of 11.2% this quarter. As you already know, the business is completely on the franchisee model.

Let me now ask Sudeshna to open the forum for Q&A.

Sudheshna Patnaik

Thanks, Kabir. We'll wait for a minute for the question queue to assemble. Interested participants may click on raise hand icon at the bottom of the page on Webex application to join the Q&A.

The first question is from the line of Sanjesh Jain from ICICI Securities. Sanjesh, you have been requested to unmute yourself. Please proceed with your question.

Sanjesh Jain

Good evening. Hi, thanks for this opportunity. A couple of questions. First, Lakshmi, you have said in your opening remarks that we have signed multiple hyperscaler and OTT contracts, and you particularly mentioned about 1 multi-million 10-year contract, which you are connecting the various data centre of an hyperscaler, I hope so. Because it's a 10-year scale, so what kind of growth can this deal bring to us from an opportunity standpoint? That is number one.

And number two, because we need to now also lay out the network in Tier 3 and Tier 4, so what is the incremental investment does this deal require us to do, additionally probably?

A.S. Lakshminarayanan

Yes. Sanjesh, first of all, the hyperscaler deal, this kind of build we have been doing for some time for many hyperscalers. As we said, some of these were passed because they had built capacity post-COVID, they all spent money on the back of increasing traffic after the COVID. And then there was a period of utilisation of that capacity, and now we believe there is more demand, and these opportunities have come up.

So that is one example of the deal is what we highlighted in this call today. But we have been doing these data centre to data centre connectivity for multiple customers, whether it's enterprise or the hyperscalers. I don't want to break out the revenue of what it means because we don't give that breakup.

The second question that you asked was on the Tier 2, 3 expansions of capillarity in what it means by Capex. We have been actually steadily increasing our capillarity in those spaces, and we are doing it very scientifically. We've analysed all the pin codes where there are demands, and we have identified those clusters, and we are expanding our network in those spaces. So, this is not a big one-time exercise. We've been steadily doing it over the past four years, and we will continue to do so in order to make sure that we can address the opportunities of enterprises moving to the Tier 3, 4 cities in India.

Sanjesh Jain

That's clear. That means the $300 million, $350 million of Capex, what we speak also includes the Capex for laying out fibre in the Tier 3 and Tier 4 cities? That's right.

A.S. Lakshminarayanan

That's right. That's what we have been doing, yeah.

Sanjesh Jain

Got it. Lakshmi, second question on the core connectivity. Even last quarter, we said that the Red Sea and other cable cuts has hurt us. Is this completely behind us with the cable getting completely repaired? And the 5%, 6% growth what we have been speaking of that should be back from Q3 onwards?

A.S. Lakshminarayanan

No, I don't want to comment immediately on the Q3. To your first question, whether it is behind us, yes, it is behind us. I think the last of the cable cuts was repaired. And we will now look for how to start utilising that capacity more meaningfully.

Sanjesh Jain

Got it. But we are not seeing any issue from the demand side or any higher pricing erosion, none of those issues which can otherwise impact revenue is visible, right?

A.S. Lakshminarayanan

No, no. The demand side has been steady. So just to remind you, we have been saying that the core connectivity as a business globally is in a declining trend in the market, right?

Sanjesh Jain

Correct.

A.S. Lakshminarayanan

In that market. We had called out in our strategy that we will be in the low-to-mid single digit growth. There was demand and also the fact that the customers trust us to deliver because these are all very critical connections to data centres across the globe. They value the kind of services that we provide. We have been able to garner more market share out of this and deliver a higher growth compared to the market.

So, we don't see any issue in the market as such. But the overall market is having the colour, which I just painted, I don't think that would change in the short to medium term.

Sanjesh Jain

Got it. And this hyperscaler contract that we mentioned, that will be part of the core connectivity, right?

A.S. Lakshminarayanan

Yes, yeah.

Sanjesh Jain

The second question on the digital side of the business. If I look at the net revenue, the growth for this quarter is 1.4% QoQ and on the gross side, it is 3.6%. We are still hitting only 15% growth, and the ambition was to touch 25%. Is this the demand side issue? Or it's just that the order book and the sales funnel conversion has been slow, but the discussions are encouraging. Where is that gap versus what we were targeting and what we are delivering today?

A.S. Lakshminarayanan

I think we have set ourselves a highly ambitious target. There's no doubt about it, and we are going after it. But the macro conditions and the challenges that arise are something that we don't factor in when we create ambitions. And I don't want to do that. So, setting that apart, our ambition continues to be that. And you're right in your observation that 6% translates to the number that you said, but our ambition remains the ambition, and we are gunning for it.

From the demand side, we are very, very happy to see that the order booking has improved, and we have been calling out that there is slowness, and you can see not just from our commentary, I think that's been true for everybody else in the markets. But we are calling out the increased order booking, because I was always of the opinion that as you continue to improve your funnel and work your way through, something will come out of the funnel at some point in time, and that this last two quarters has proven to be the case.

But the market conditions are still the same. I think the conversion of the decision-making time has not improved in any significant way. But as it may, we can't change the conditions. What we are focused on is continuing to invest in our fabric products, continuing to engage with our customers. That coupled with what we said on increasing our sales footprint and we did that and that is delivering an improved order book.

And some of this, I've also been saying that as you increase the sales footprint, it takes time for the new sales team to understand the propositions, build relationships and make an impact in the market. So, I'm quite pleased with the outcome that we have had. And for this to continue, we have to continue to invest in our products and invest in our sector.

Sanjesh Jain

That's fair. Kabir, I got three questions on bookkeeping very quickly. One, last quarter, you said that you want to achieve 20% EBITDA margin for FY25? Do we hold that guidance still true?

Second, is this the only land parcel, which is put in asset held under sale? Or are there any more land parcels we can expect in, say, next 12 months' time frame? And what is that amount we are looking at?

Number three is on the working capital, a sharp increase in the first half. This is significantly different than what we have seen in the last four years. So, what has changed suddenly in the working capital side of it? Yeah, that's it. Thank you.

Kabir Ahmed Shakir

Thanks, Sanjesh. Look, our ambition is still in the range of 20%. I said range of 20%. We will maintain that ambition of range of 20%. Yes, cable cuts. I mean that's not the only reason, but if I were to filter out, there are multiple noises within that as you would have in any company in any quarter. It did have a dent, and we are a little bit impacted by that. But our ambition is still in the range of 20% for the full year.

On your second question on land, it is a significant one, and it's a related party deal, so it needs as per the regulations to go to shareholder approval. So, it's in the public domain. I've given you the value of it, although it is there in the shareholder notice as well. I've called it out for easy reference for all of you. This quarter, we also had a small land parcel in Vikhroli that we sold and that is already recognised.

As I told you guys about almost 18 months ago, there was a real estate strategy that was approved by the Board. And the team is constantly working on cleaning all the title issues and all the hindrances that were actually coming in the way of monetisation. Now to go into specifics, we just got, after enough follow-up with the local government, we got the patta issued in our name. And unless until you have the patta issued in your name, you can't really get on with the sale process, although we did the valuation, we did all of those work. So that's the reason why we are today in a stage we're able to do the monetisation for Ambattur. In fact, STT is a current tenant there already, and it makes logical and strategic sense for them to become owner and then that's where we are awaiting shareholder approval to consummate the transaction.

We have a plan. I can't give you a number because all of those are mired with all these complicated problems. And as and when we unwind each and every one of them and get it ready, we will go on. I mean there is no large thing coming up in the next 12 months. A lot of them are in the Rs. 50 crores to Rs. 70 - Rs. 80 crore kind of a bracket. Some of them we went and there were some technical issues, we had to actually halt. We will restart them. So those are operational in nature, Sanjesh.

Lastly, coming to working capital, yes, I do recognise that it has gone up. Let me reassure you that the operations are completely under control. Nature of it, about, I would say, year-to-date, about Rs. 500 crores of the receivables of the total Rs. 600 crore that you see, Rs. 500 crores are not due. I mean those are the conditions either in the large deal contracts that we have where we have billed and we recognised revenue, but they are not yet due. So, they're not collectible as such.

So that has contributed to a big portion. Plus, also the flavour of our deals is also changing in a way where we had to accept some of them came with conditions of higher payment terms as well. So that was a conscious business call that we always take between margin and working capital and then do a right trade-off per se.

So that is, I would say, the anomaly of working capital, but nothing I would say is alarming that way. Also, Lakshmi alluded to large contracts that we actually signed. So, when we see the holistic picture of it, a little bit of a cash timing is not something that I would be overly worried about in doing economically the right thing for Tata Comm.

Sanjesh Jain

Very clear. Just one follow-up on the land, what you said. You said that they are already a tenant on that land. That means other income will reduce. Will that be a fair assumption? And if, yes, how much will it dip?

Kabir Ahmed Shakir

That is correct. That's exactly the reason why I set it out even though you didn't ask for it. Look, you will have to look at other income that we actually have. And as I monetise, it will keep coming down.

Sanjesh Jain

Got it. And now that ST Telemedia has announced a very large expansion plan in India worth $3 billion. Is it fair to assume that they will keep requiring this land and we have land at the very prime locations. These deals can continue. And number two, what will be our contribution in $3 billion from the equity side of it? Will we maintain this 26% equity stake and all the equity infusion will be funded by Tata Communications to the extent of our shares, sorry?

Kabir Ahmed Shakir

Yeah. No firstly, I mean they have an ambitious plan of $3.2 billion, which they have communicated. That is a total outlay over five years. There is a large component that will be funded by debt. So then there is a balance equity portion. As of now, our stated position, which you have seen in the last few quarters as well, we will continue to maintain the 26% stake in STT.

What we want to do with that stake is a review that we will undertake along with multiple other things that we are doing within the business. That's what I alluded to in the first part of my speech that there is a lot of value in this company to be unlocked.

So, a lot of costs are getting incurred upfront, which as per accounting get booked in my current cost, but these are all the right actions that we are taking for setting up the company for success, relooking at capital allocation, how we must invest behind growth, I think you should look at it from that larger perspective. We are a company in the digital transformation space. We are servicing the long-term infrastructure and transmission needs for our enterprise customers. We are the digital fabric; these have longer gestation periods.

And if our thinking as a management is not going to be long-term and if we do not take long-term actions, I don't want to get myopic into short term. I'm not saying it as an excuse, Sanjesh, but that is rightly the kind of thinking that Lakshmi drives in the organisation, and it's absolutely the right thing to do.

Sanjesh Jain

Fair enough. I have taken more than the fair time. But thanks for patiently answering all those questions and best of luck for the coming quarters.

Kabir Ahmed Shakir

Thank you, Sanjesh.

Sudeshna Patnaik

Thank you, Sanjesh. The next question is from the line of Amit Maskara. Amit, I'm requesting you to unmute yourself. Please proceed with your question. Amit, your line is unmuted. Please proceed with your question. Amit, we can't hear you. Please come back in the queue. We'll move to the next question. The next question is from the line of Balaji Subramanian from IIFL. Balaji, we are requesting you to unmute your line. Please proceed with your question. Balaji, please unmute your line and ask your question.

Balaji Subramanian

Thank you. So, I had three questions. So, the first one was on the revenue aspiration that you had laid out in the analyst meet earlier this year, which was Rs. 28,000 crores of top line by FY27, of which about 60% will be from digital portfolio. So that is basically around Rs. 17,000 crores. If I look at the annualised digital portfolio revenue for Q2, we are somewhere around Rs. 9,000 crores, give or take Rs. 100 crore or Rs. 200 crores. So how should one expect the Rs. 9,000 crore number to move to something like Rs. 17,000 crores in a span of 2.5 years or so? So that is one.

And even though you have stated many times in the past that you would not like to do M&A just for the sake of hitting the revenue aspiration. What are the potential areas you are looking at as far as inorganic opportunities are concerned? And in that case, how do you look to fund it? I do get that you are also exploring multiple monetisation opportunities, but how should one expect the funding to come through? So that would be my first couple of questions. Once I get the response, I will move to the last question.

A.S. Lakshminarayanan

Yes, Balaji, thank you. I think the aspiration remains intact, as I said in the previous question. And you are right in saying that for us to deliver this kind of a growth, our digital portfolio has to grow at a stronger clip, right? So that is the reason why we chose to invest in all the four fabrics. If you look at our next-gen fabric, next-gen connectivity in the network fabric, we've invested in a new platform called IZO Multi Cloud Connect.

And in the coming quarters, we will be releasing a product which connects within the cloud. So, with the increasing trend of people adopting more multi-cloud, that's an area which is today a small market, that is in a single-digit billion slated to growth in upwards of 20% CAGR in the networking space. So, we've identified such a pocket, and we have invested in our product, and it's in early stage. And we expect this to grow.

So, in many of these areas, that is one example. So, if you look at the interaction fabric today, the bulk of the revenues are coming from SMS, the clear reading of the market and the expectation is that it will diversify from SMS to other channels and also more of AI capability and orchestration across multiple channels will become the norm. And those are the areas we're investing in.

So, these are all new areas, and we have placed our bets in a lot of these new areas, all of which are white spaces with good growth potential. So, I think that is one dimension of where we are focused on in order to capture the opportunities. The second dimension is about the markets itself. The international market is a bigger white space as we've been calling out.

And that is a market where we are increasing our footprint. We do have a challenger proposition there. We have to go and replace the incumbents, and that is what we are working on. So, the way we have set out our ambition is based on what we see as the market opportunity, our reading of where the technologies in each of the fabrics will go, and we believe we have placed our bets and investment in all the right places.

To your question on funding, if we chose to do inorganic. I think Kabir talked about the several monetisation opportunities and value unlocking opportunities that we have. And those are the things that we would do. Kabir, do you want to add anything?

Kabir Ahmed Shakir

Yeah. Look, Balaji, I would say we have a lot of growth ambitions both organically and inorganically. To your point on M&A, we have clarified many a times, there are core principles that drive our M&A decisions. It has to be responsible, it has to be strategic, and it has to create value for everyone. The places where we will look at obviously are going to be DPS. Having said that, I am not averse to complementary capacities coming in the core connectivity space.

So, we will actively look at it. We have an active M&A funnel. And as and when that funnel progresses to a level, it will go to the Board and go through the due diligence before it's approved and then it's ready for us to communicate externally as well when we do such things.

Funding of it, both organic and inorganic, are something we constantly look at and as Lakshmi alluded, there are multiple levers, monetisation opportunities that we will examine. But let me rewind the clock 18 months before. What did we do? We did have an aspiration of M&A, we spruced up, we delivered a very healthy profitability in our business. We brought our net debt down to 1.3x, created the war chest and the capacity. We were operating at a very healthy 28% ROCE. And then we went and acquired these three assets.

And our task is to, of course, integrate and deliver on the synergies and the business case of these assets. And we have given you an indication of when net debt leverage, ROCE and EBITDA margins will come back to our ambition ranges. And when we get back there, I've said multiple times, our objective is not to stay there. Our objective is to use our financial muscle to invest behind growth.

Now what happens between the time we get there and now if there are interesting opportunities, that's why we will look at all these monetisation opportunities. With the robustness of our financial performance, our own headroom on debt capacity has also gone up. So, if required, we will look at avenues. We've also done theoretical exercise on varying target sizes, what is the right funding instrument that we need to use.

So, depending on the opportunity, depending on the target, I think, Tata Communications today has the right hygiene and a robust balance sheet to tap on to the right capital asset that is required to fund that opportunity. I'll leave it at that, Balaji, I can't give any further detail than that.

Balaji Subramanian

Thanks, Lakshmi and Kabir for the detailed response. My next question was on the interaction fabric that you had mentioned. So, you did allude to the diversification of enterprises towards non-SMS channels. But based on what I gather from market sources, it does look like even though WhatsApp volumes are on a tear, there have been some renegotiation of terms from WhatsApp's side towards CPaaS players.

And I do understand that they have taken up the threshold, which needs to be crossed to be eligible for the incentive. And there is chatter that eventually the gross margins in the WhatsApp business will also settle down to something like 15%, 20%, which is what we see in the domestic SMS market. So how do you kind of reconcile the fact that at the end of the day, something like a channel like an SMS is something which is owned by the telco while WhatsApp as a channel is owned by Meta.

So, considering the typical lack of ownership of these channels by a CPaaS vendor, do you think that that will come in the way of monetisation of CPaaS in the long run? Thank you.

A.S. Lakshminarayanan

Yes. So, we cannot really speculate on what will happen. There are not just these channels. There are voice channels, for example, which we own, and programmable voice is another big opportunity. There are video opportunities. There are RCS opportunities. So, the channels will continue to expand. We cannot also predict on which channels are going to pick up the most with the customer. So that is one area we do need to develop the products, which we are doing and taking it to customers.

The second is, I think the customers also will settle on looking at what are the optimal channels to use in terms of across these channels, which is where our ability to orchestrate across multiple channels, build out those orchestration layers and bring AI to that will be crucial. So, after all, channels will be channels.

Balaji Subramanian

Got it. Thanks a lot, and all the best.

A.S. Lakshminarayanan

Thank you.

Sudeshna Patnaik

Thank you, Balaji. The next question is from the line of Vibhor Singhal from Nuvama. Vibhor, we have requested you to unmute yourself. Please proceed and ask your question.

Vibhor Singhal

Hello, hi. Thanks for taking my question. So, Lakshmi, a couple of questions from my side on the overall growth environment. So, as I think you have been asked by the earlier participants, I think the growth in this quarter was kind of stable, but of course, there's a big gap between what our aspirations are and what we are delivering at this point of time. How is the overall macro looking like, especially with respect to the second half of the year? We've seen a lot of IT services vendors talk about the interest rate cut having reinvigorated talks about discretionary spends. Is that also something that we are also hearing that will be applicable to us as well? But on a broader note, what is the kind of overall growth trajectory that we're looking at for the second half of this year?

A.S. Lakshminarayanan

Yes. I don't want to comment on the immediate quarters. I think we are very encouraged by the order bookings that we have had in the last two quarters. And the second data point that I have is that the time taken to convert these orders actually have been longer as well. As I've been saying, as we put more in the funnel at some point in time, it will come out, right? So, our effort has been to see how do we put a good quality of deals into the funnel, increase our engagement. And those are the things entirely in our control, and that is what we are focused on.

To the question on macro, there are different readings of it in terms of the geopolitical risks that is even more heightened and in fact, worsened. Yes, the interest rate cuts have been encouraging. So, it's hard to read into some of these. And the second aspect, which I have been highlighting also in the area of network, for example, they are the customers do not replace it just like that, because it's a fairly complex process that they have to go through. And that is an inertia for them to do. So, there is a lot of work that we are having to do with the customers to switch from incumbents.

And having done that, the time to realise some of these revenues are also longer. So yes, macro plays a role in which case, if they build more applications and if they put more into the cloud, their existing network architecture and infrastructure begins to crack, and that is when they look to transforming the network.

So, in a sense, that's a relationship between macro. As macro improves more applications, more things moving to cloud, more stress on their legacy network and therefore, the need to transform. So, it's a longer cycle from our perspective. But the good thing is we stay focused on. And the encouraging thing is also we have multiple fabrics, right? So, if hopefully, the discretionary spend goes up, our interaction fabric, I believe will continue to stand to benefit from such a move.

Vibhor Singhal

Right. Thanks for that very detailed answer. But if I were to marry the answer you just gave with the answer to

Sanjesh's question in the beginning. You mentioned that, of course, there is a macro factor, there's market dynamics when we build aspirations, we of course, don't take market dynamics into account, and we hope for the best. So, what exactly are the market triggers or, let's say, drivers that you are waiting for? We've had an interest rate cut, there is a talk of discretionary spends which are picking up. What exactly are we waiting for? I mean what are those events or what is that something which you believe is going to drive our revenue growth to our aspirational levels?

A.S. Lakshminarayanan

No. As I said, we're not waiting for anything for happening. So, if you look at each, I think I gave an elaborate answer. So, when do people undertake network transformation is particularly when they go to cloud, they see that their current network architecture is not able to cope, they've come under cost pressure, and therefore, they look to replace their traditional network with more internet-based architecture.

And as they move to more internet-based architecture, there is more need for the network security and SASE, which is where again, we have invested. So, I think the trigger would be largely where the enterprises get to a point where as they move their applications to cloud as they have more distributed touchpoints from their users accessing in multiple places, the application performance begins to go down. And as they go to use more Internet, they get more worried about security. And therefore, the network transformation, implementing network security-related thing sort of accelerates. So that's a trigger point as far as that is concerned.

So, in our cloud and security fabric, I've spoken to the security fabric. So, the network security is one. The second is we are seeing a lot of opportunities on implementing a state-of-the-art SOC for customers. And that is what we announced as a deal last quarter, for example. And there are multiple such opportunities where, the threat landscape is increasing. So, in a couple of these deals that we are implementing, it's a complex implementation, integrating over 20 different OEM technologies to deliver and we are enabling it through threat intel from our network and bringing AI capabilities to that, right? So that is another trigger event for that portfolio.

And of course, in the cloud, we are strengthening our infrastructure as a service as well as the platform. We expect to announce some relaunch of these products in this coming year. And we are investing in AI cloud, which is in a very, very early stage. So, these are some of the examples I can talk about for each of the fabric. There are clearly trigger points in each of the fabric, which we believe will drive the growth.

Vibhor Singhal

Right. Sure. I got that Lakshmi. So, I mean, okay, I'll probably just have a couple of more very specific questions. The media revenue saw a very sharp decline in this quarter. Any specific reason for that? I'm sorry, if you have addressed that already. I missed the initial part of your opening comments.

A.S. Lakshminarayanan

Yeah. So no, I did mention that the media is a bit cyclical, based on the sports calendar, a lot of our media revenues comes from our coverage of live sporting events, right? So, we are the leaders in a lot of global sporting events like the Formula One and others. Last quarter, the T20 match in the U.S. and the Caribbean. And we also had Olympics. So, all of that were in the last quarter. So, depending on the sports calendar, it has a bit of cyclicity.

Vibhor Singhal

Got it. Sure. That's helpful. Just last question for Kabir. So, Kabir, this quarter margins, I suppose, were impacted because of the maintenance expenditure in the core connectivity segment. But excluding for that, are we looking at a trajectory in which we are looking to expand margins every quarter, especially in the digital space, as we should now be starting to reap the benefits of integration of both Kaleyra and Switch. Is that understanding, correct? And is that also what we can also build in, let's say, for the next year as well.

Kabir Ahmed Shakir

Well, look, what I've said we want to get back to our ambition of 23% to 25%, and that will come in two years' time. This year, I've said we will be in the range of 20%. That's where we would like to be. To get 0.5% here and there is not the point, but that is the range we will get back in.

On your point, I will not say only for Kaleyra, but all for the entire digital products itself, we have a glide path. We have mentioned this that we have a glide path, and there are multiple drivers, and the drivers differ from product category to product category. And those are tracked in terms of margin expansion.

So absolutely, yes, we want to be able to drive faster, better growth in DPS and also profitable growth. So therefore, even that profitable trajectory needs to go up. Even from the current levels when we drive faster growth, we have a headwind because of the mix effect on our margin profile. Despite that, our ambition is to stay in the 23% to 25%.

Vibhor Singhal

Got it, Kabir. That was really helpful. Thank you, guys. Thanks a lot for taking my questions.

Kabir Ahmed Shakir

Thank you, Vibhor.

Sudeshna Patnaik

Thanks, Vibhor. The next question is from Vinit Manek from Karma Capital. Vinit, we request you to unmute yourself and ask your question.

Vinit Manek

Just one question for Lakshmi. So, Lakshmi, not specifically on the numbers, but we have seen a good growth Q-o-Q for this quarter and with a lot of revenue coming back on our core connectivity and good order book growth that we have seen for the last two quarters. So, can we expect a better second half versus the first half revenues? Or any comments on that?

A.S. Lakshminarayanan

So Vinit, I sort of gave a colour to some of these order books, while I cannot give specific guidance. I've also given a colour on the order book that some of the orders I think I mentioned about the large hyperscaler network build. I mean that will come almost towards the second half of FY26. Some of our network deals we have booked the order; the revenues will take longer to come. But there are certain portfolios where booking the order to conversion is faster. So, the various portfolios have different colours. While we know how it's going to translate, we don't want to break that out and give a guidance for the H2 based on this.

Vinit Manek

Got it. And two bookkeeping questions for Kabir. So, Kabir, any sense on the kind of usage of the cash that we're going to do from the divestment that we had announced? So, will it be more towards the debt repayment or it will be required for some accelerated investments on the AI cloud or the GPUs that we will be doing mostly in the second half?

Kabir Ahmed Shakir

Yeah. I would have liked if you did not call it bookkeeping questions. Finance in Tata Comm is quite strategic, and we add value to the business in a fundamental way. So, yeah, bookkeeping is what we do to earn our salary, but we are here to drive business forward.

Yes, we look at source of funds and use of funds. We have a strategic plan that drives our actions. We have our ambitions to be the digital fabric for our enterprise customers. And we have Rs. 28,000 crores as our Northstar in FY27. We have digital portfolio that we want to drive as an acceleration. So those are all our guiding factors.

And yes, each and every opportunity will be evaluated based on the ROI that it needs to deliver. So, we are measuring from a very careful angle of driving profitable growth, yet delivering the ROCE that we want to do. And maintain a certain healthy debt-to-equity ratio and leverage. So, there are multiple places from where this is optimised. So, I would say we will look at every element, both in the P&L and in the balance sheet and sweat each and every piece of asset that we have towards driving profitable growth.

If you had probably been exposed to the finance strategy. There is a big pillar called Fit to Grow and the Fit to Grow is not just a conceptual model. It's a strategic planning model backed with multiple scenarios that the team updates on a monthly basis, which guides us in terms of the resource allocation for the business, both for organic and inorganic activity.

Vinit Manek

Got it. And can you just repeat the onetime expenses that were there in the interest cost of Rs. 193 crore this quarter. And could this be the peak absolute interest cost for us, because we have already hit the threshold of the debt-to-EBITDA ratio that we had on the aspiration side, or so can we say that this is the peak interest cost?

Kabir Ahmed Shakir

Firstly, it's sort of onetime cost, that's my interest cost bill for the quarter, Rs. 193 crores. Well, you tell me that the Central Bank of India and the U.S. will not increase rates. I will give you the guarantee that that is the peak. Look, we have hedging that we do, we have an interest rate management policy that we actually run. In this particular quarter, the costs have gone up because of increase in short-term borrowings and a mix of INR versus dollar debt. So that is the reason. I'm sorry, I can't give you guarantees whether we have reached the peak or not, because I do not control interest rates.

Vinit Manek

Okay. But how much was that? Can you quantify that for the quarter?

Kabir Ahmed Shakir

It's very marginal. Our weighted average cost of debt is still lower than the previous quarter. It's only the absolute that's gone up, because of the mix between the short-term borrowings that we have taken in India. So, it's a few crores here and there.

Vinit Manek

Got it. Thank you. Thank you for answering all the questions.

Sudeshna Patnaik

Thanks, Vinit. The next question is Priyank Parekh from Abakkus Asset Managers. Priyank, please go ahead and ask your question.

Priyank Parekh

Yes. Just wanted to understand from the perspective of that we have multiple segments. And within the digital portfolio, we have five segments. So, when we are projecting the growth for next three years, I want to understand how correlated these segments are? Are they quite heavily driven by certain levers, or they are completely diversified?

A.S. Lakshminarayanan

You mean if in each of the segments, yeah. I don't think there is much of correlations. There might be some correlation between the network fabric, and for example, the cloud and security fabric. I think I answered in the last call, as people do network transformation and tend to use more of Internet. There's going to be more need for a different security architecture in the network through SASE and other new technologies, which is linked to the network transformation that takes place. So that is one linkage.

But otherwise, I don't think there are huge number of linkages between an interaction fabric and the network fabric or an IoT fabric. And also, we find that the buying personas within enterprise for many of these are somewhat different. Even within the network fabric, the person who looks at network and typically, the people who have been looking at network security have been different.

And as it begins to converge, we are also seeing that there are changes in how the enterprises are making the decisions. So, there are certain convergence like the LAN and the WAN, the WAN and the security. But truly, there are different personas taking decisions, and there are different drivers. There are not many more links that I can think of.

Priyank Parekh

Okay. And when we are speaking that Rs. 280 billion of the revenue in next few years, which segment you are really seeing driving that growth within the digital?

A.S. Lakshminarayanan

No, all the fabrics. I think I have elaborated before, the network fabric, the cloud security, the interaction, IoT, the media, all of them have potential, and all of them can grow at a very healthy double-digit.

Priyank Parekh

Okay. Okay. Got it. And just the last one question for understanding, when we're saying that this land sale will impact our other income, that is the real estate income that we are reporting, right?

Kabir Ahmed Shakir

Sorry, if you repeat that again, please? I missed you.

Priyank Parekh

So, when we are saying that this land sale will impact our other incomes, that is the real estate income that we are talking about.

Kabir Ahmed Shakir

Yes, that is correct.

Priyank Parekh

Okay, understood. Yeah, thank you.

Sudeshna Patnaik

Thanks, Priyank. The next question is from Gautam Rathi. Gautam, please unmute yourself and ask your question.

Nishit Rathi

Hello, hi, this is Nishit, can you hear me?

Kabir Ahmed Shakir

Hi, Nishit.

Nishit Rathi

Hi, great. So just a couple of questions, you called out the best international order book in the last five years. Can you give some colour as to what is driving this? I know you gave a very detailed explanation with respect to some of the network transformation deals and how long it takes to kind of get some of those. Are we seeing some of those also in that kind of order book? Or this order book is without some of those network transformation deals?

A.S. Lakshminarayanan

No, no. I think the order book, again, as I mentioned, is across all the fabrics. But having said that, in some of the usage-based areas like the interaction fabric, we don't really include that in the order book because that is purely usage based, unless we have a firm commitment, we don't include that in the order book. But the order book colour that I gave is across all the four fabrics.

Nishit Rathi

Anything incrementally that has changed, Lakshmi, one thing you called out is increased sales productivity. You're basically saying that your funnel had increased so much that something had to convert because you had put more manpower behind it. But is there anything incrementally that you're seeing? Are you starting to win deals differently? Any other kind of colour would be very, very helpful?

A.S. Lakshminarayanan

I think it's early to call. I mean, obviously, the win rates have improved, which is simply a function of how much we are winning compared to how much gets dropped because the customer is not simply taking it forward or they choose to stay with the incumbent, those kinds of scenarios. So, the win rates improvement is encouraging.

Yes. Other than that, no, it's a factor of gaining the confidence with the customers because especially in all of these digital infrastructure areas, they are very, very core and fundamental to the enterprise. It is not that if something goes wrong in an area, they could easily replace it. It takes time. So, they are a lot more conservative. So that's the reason why it takes time. It takes time to develop the trust, and there is a long engagement cycle that goes behind that.

But in terms of colour, I don't think I can add any more colour to that. Yes, there are instances where we have won against certain incumbents consistently. But other than that, I can't give you any further colour.

Nishit Rathi

See, I just wanted to call out what I understand. And just if you could help me understand that, right? The way I'm thinking about it is that it's a long sales cycle and you guys have been adding for the last maybe 18, 20 months, adding more and more salespeople, which means that you've been adding to the funnel, but because of the long sales cycle, it takes time. And now you are starting to see fruit of some of those deals come through, though the market is still not improved, which is kind of showing up in your subdued funnel, right?

So, it is more gradual, but there is a possibility that as incrementally both your productivity of the sales improves as you keep adding more products and the market improves, this could accelerate, right? Is that the way you are seeing it? Or is there anything different?

A.S. Lakshminarayanan

That is our plan.

Nishit Rathi

Perfect. So that is one. And just the subdued funnel in the context of increased salespeople, so have things got even worse on the macro side because your salespeople are getting more productive, which means that even with the macro being soft, you should have actually seen the funnel growing, right?

A.S. Lakshminarayanan

So, I think you should read that in context with the conversions as well, right? So, we have got deals which means that we have fruitful conversion of the funnel and when you convert, then it gets out of the funnel. So, we have to replenish the funnel, right? So, what I'm saying is the funnel is remaining constant, which is why we said the funnel is still robust. But in terms of the pace of new additions, that had somewhat slowed down because, rightfully so, the teams are also focused on closing some of them.

Nishit Rathi

Okay. So, the staff, okay, he's occupied there. And just is there any update on the NVIDIA partnership because Q3 is when we were expecting back to go live. Any kind of colour you want to give on that? How do we see that starting? What kind of revenue impact should we see from Q4, Q1 onwards?

A.S. Lakshminarayanan

No, it's close to the period that you said Q3. So please wait for the launch.

Nishit Rathi

Fair enough. And just the media side, I understand the seasonality on a QoQ basis. What I'm not able to fully understand on a YoY basis given the kind of commentary that we were hearing with Switch and the kind of opportunities that were opening up there, are these again work-in-progress? What is happening out there, if any, kind of understanding there?

A.S. Lakshminarayanan

Yeah. I think we are closing deals. But some of the seasonality is not a yearly seasonality, Olympics doesn't come every year. The ICC T20 doesn't happen every year, right? So, some seasonalities are annual seasonalities, which reflect in the quarterly things like the Formula 1 race begins and ends in certain seasons. But some of the other events are not a yearly calendar one. So that's what I referred.

No, I think the integration with Switch is proceeding at pace. We were impacted somewhat by the Hollywood strikes last year, and things are beginning to pick up again. So, we're quite pleased with the revenue opportunities through the Switch integration, particularly on the production side because it does expand our capability beyond just the transmission side that we were in before.

Nishit Rathi

That's fair. Kabir, you spoke about a lot of the cost getting booked upfront and a lot of investment being made. Can you just help us understand maybe a few examples for us to kind of just get a better understanding of this?

Kabir Ahmed Shakir

Nishit, there a lot of them are there already in the public domain. We've, for example, been preparing ourselves to play really well in the acquisition game. We are reorganising our subsidiaries. Now TC UK is a direct subsidiary of India. That's there in the regulatory filings. It's there in the public domain. So that's from an M&A perspective that we are competitive to be able to do that. Then there are other projects in preparatory stage for any monetisation opportunities that we may get, which are not yet approved by the Board.

So, I'm not privy to share any, these are preparatory works. When it happens and when it reaches and when the Board approves, then this will be the reason for public disclosure. Until then, I can only tell you that as we're poised for growth, and a lot of you have been asking the question on use of funds and how will we do it. So, you've looked at all of them and say, how can we do that in a tax-efficient and a least costly way. And our structure, if that was coming in the way, we are trying to simplify that structure. That's the best level of information I can provide. I can't provide any more detail than that.

Nishit Rathi

That's very fair, Kabir. The employee cost also is this normal increment or the Rs. 50 crores increase QoQ? Just can you help us understand, is there anything out there that we need to understand? Did you add more, what was that?

Kabir Ahmed Shakir

No. It happens every Q2. If you look at it historically, so we accrue for a certain SIP cost and for the full year of the previous year, that gets paid out in the first quarter. And when there are excess provisions then they get reversed. So therefore, you're comparing against the base effect, that's why it looks increased, but it's not any increased increment. It's not an increment cycle. Q2 is not our increment cycle. So, it's not increment cycle, not any extra hires. So that is not contributing for it. Q1 had some reversals and Q2 is more normalised, and this is how you should be seeing this.

Nishit Rathi

Okay. And this Rs. 86 crores, which has been included in revenue, what exactly is it? Is it like a debtors or provision made, which has been reversed? Is that understanding, right?

Kabir Ahmed Shakir

No, it's not. Look, it's BAU for us. These are excess customer credits that we had, which would have otherwise given to customers on renewals and stuff like that and negotiations turn up better. So, it's normally a very BAU activity that happens every quarter, every year because sometimes renewal happens and you go and close the discussions two months, three months later on. And so, you obviously take a view that you may end up giving so much as a discount, but you get better than that.

The reason why we've called out this time is because it's an aged customer credit, which is greater than five years. And therefore, just as part of good governance, we said since it's an aged credit and not within the year, we've called that out. But otherwise, these are regular BAU stuff.

Nishit Rathi

Understood. And just one last thing on the working capital side. The inventory number seems to be very high. And also, is there any impact of Kaleyra in our working capital because it's a kind of business where you have to give advances upfront. So, can you just help us understand the inventory and Kaleyra?

Kabir Ahmed Shakir

Inventory is deal-specific, Nishit. So, there's one large deal where we've procured the inventory, but we are unable to bill the customer because of the RFP condition that we have to stitch a solution and then only we can do it. So, we have procured it for that particular purpose. Most of our inventories are for customer orders. We don't have an inventory policy. We don't stock inventory per se. So, this is directly linked to one large deal.

Nishit Rathi

And Kaleyra, is there an impact of Kaleyra on our increased working capital because you need to give advances to the telcos and stuff like that?

Kabir Ahmed Shakir

No. There is one specific deal in Kaleyra, where there was an advance payment that had to be given, which is factored in. As I responded earlier to Sanjesh, also, I would say this is BAU, and we have taken an economic call in totality per se.

Nishit Rathi

No, this is very helpful. Just one last request, Kabir, whenever you think it's right, it's very interesting what you spoke about the core and the noncore and you guys have a very detailed plan towards that, whenever you guys can share maybe whatever you can share in that context for us to kind of take a long-term view on that business, because I believe it could have a very material impact because you have a lot of capital coming out and costs getting saved, which will then be used to reinvest for further growth, right?

And if you could share that plan with us at any point of time, it will be very, very helpful. It's a request from our side, you can consider whatever best you can.

Kabir Ahmed Shakir

It's not about request. Sorry, Nishit, let's not be irresponsible with that comment. We are a public listed company regulated by financial markets and SEBI. There are very clear laid out disclosure requirements. When proposals of this nature go to the Board, Board approves, we are under obligation to report to the market. This is not a request. So please don't consider it. We, as a management, are obligated, and we will absolutely do everything in compliance with the law and to the strict levels of corporate governance. So don't even have an iota of doubt on that.

Nishit Rathi

No, no, I agree with that. I'm not saying what happens. I'm saying what is the way forward, what is strategic, what is not strategic? What kind of amounts are you looking at saving?

Kabir Ahmed Shakir

That's what I'm trying to say, Nishit. The moment I say this is an asset that I want to dispose, I'm obligated to call it as asset held for sale and put it in my account. So, until that review has happened, until the Board has approved it, we cannot do it, and I can't be flippant with those remarks.

Nishit Rathi

Understood. Got it. Understood. Fair enough. Thanks a lot, Lakshmi and Kabir. Really helpful.

Sudeshna Patnaik

Thank you, Nishit. We will take the last question, and this is from the line of Amit Maskara from Sephira. Amit, please unmute yourself and ask your question. Amit, please proceed with your question. Amit, we still can't hear you. We will request you to please reach out to the IR team, and we'll help address your question.

With that, we come to the end of the Q&A session. Thank you, ladies and gentlemen. I will now request Lakshmi to please share his closing comments.

A.S. Lakshminarayanan

Thank you all. I think it's been a good interaction. I think we covered a lot of ground. Very pleased with the quarter in terms of the growth, both in the top line and in the EBITDA and PAT. Also pleased with the order booking in the first two quarters that we have had. We commit to stay focused on executing on our strategy. Thank you.

Sudeshna Patnaik

Thank you, Lakshmi. Thank you, Kabir. This brings us to the end of the management call. In case of any queries please write in to investor.relations@tatacommunications.com. The recording will be available on the website in the next 24 hours. You may disconnect now. Thank you.

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