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# *Asian Investing Summit 2018, Hosted by MOI Global*



## Case Study: Teamlease Services

An Emerging Domestic Platform

Soumil Zaveri

5-6 April, 2018

**DMZ Partners Investment Management LLP is a SEBI Registered Portfolio Manager (Registration No.: INP000005944)**

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## Agenda – Asian Investment Summit 2018

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### Part One

- I. DMZ Partners: Our firm
- II. Recap on Asia Investing Summit 2017 Idea
- III. Our investment approach in India
- IV. Setting the stage: A big macro-call on India?
- V. Indian Employment Sector Overview



*15 mins*

### Part Two

- I. Teamlease Services – an emerging domestic platform
- II. Questions & Answers

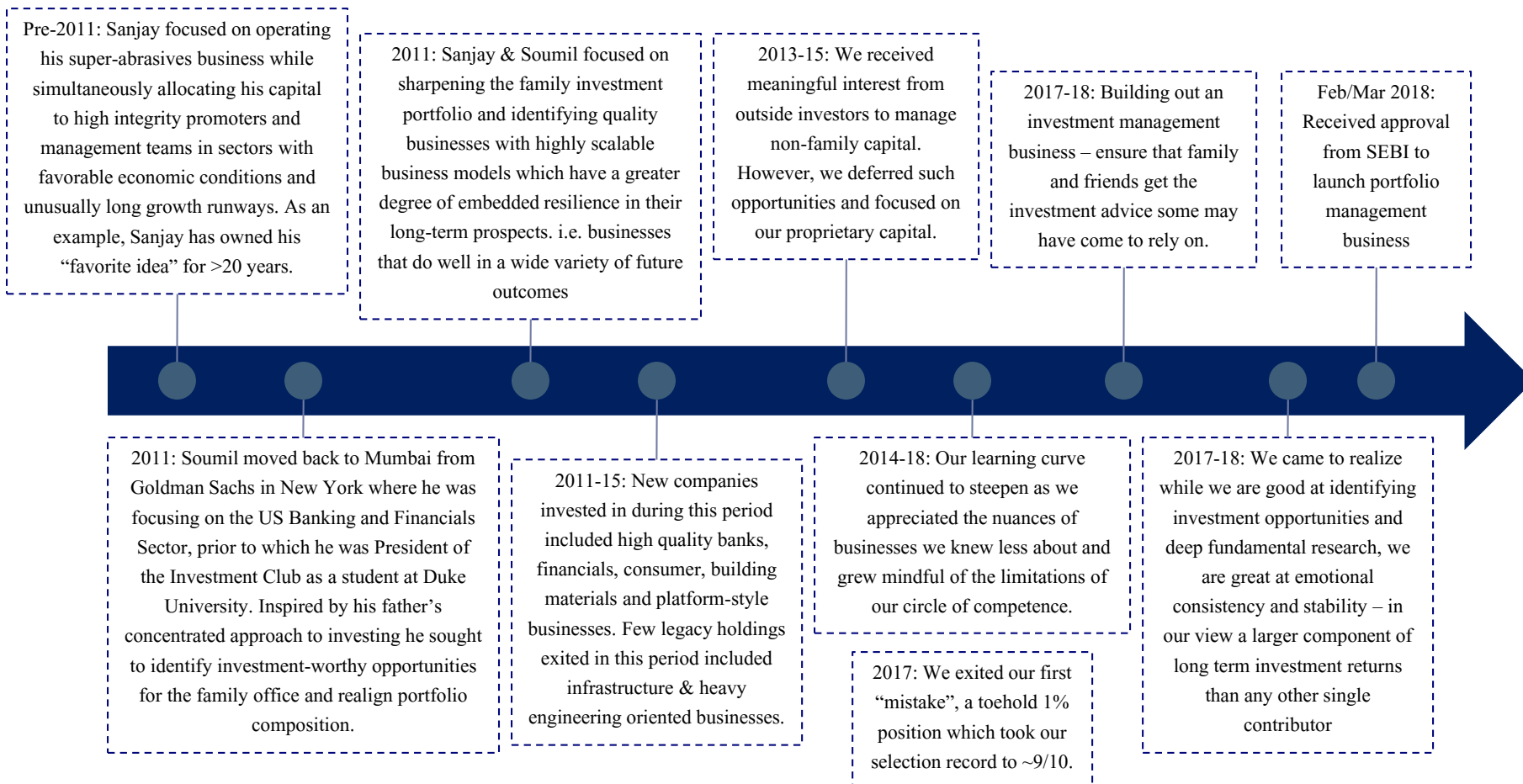


*20 mins*

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## Our story 2011 – 2018

### *A father & son investment partnership*



## AIS 2017 Idea Recap

### ***Exited Capital First in January 2018***

#### ***13<sup>th</sup> January, 2018 – Capital First and IDFC Bank announced a merger***

- *This led us to revisit our original thesis to own Capital First as a niche non-banking financial entity with a very long runway ahead*

#### ***Our decision:***

- *Exited the position post announcement of the deal with IDFC Bank.*
- *We estimate our personal returns on our original investment in 2014 to be approximately >30% CAGR*
- *Note that these returns are unaudited and any errors in our estimates are regretted. Importantly, the return estimate is over simplified as it does not capture the impact of incremental purchases/ sales, if any.*

#### ***Our rationale:***

- *We would have preferred to own CAPF as an independent entity for a substantially longer timeframe than circumstances dictated.*
- *In our view, while the merged entity may turn out to be an interesting opportunity, the standalone entity had +++characteristics*

<b><i>Capital First</i></b>		
Early purchases	~ 325	Oct/Nov 2014
Later sales	~ 840	Jan 2018
Multiplier (x)	~ 2.6	times
Approx Return	~ 35% CAGR over ~3.25 years	

Unaudited data aggregated from personal records

#### ***A brief review:***

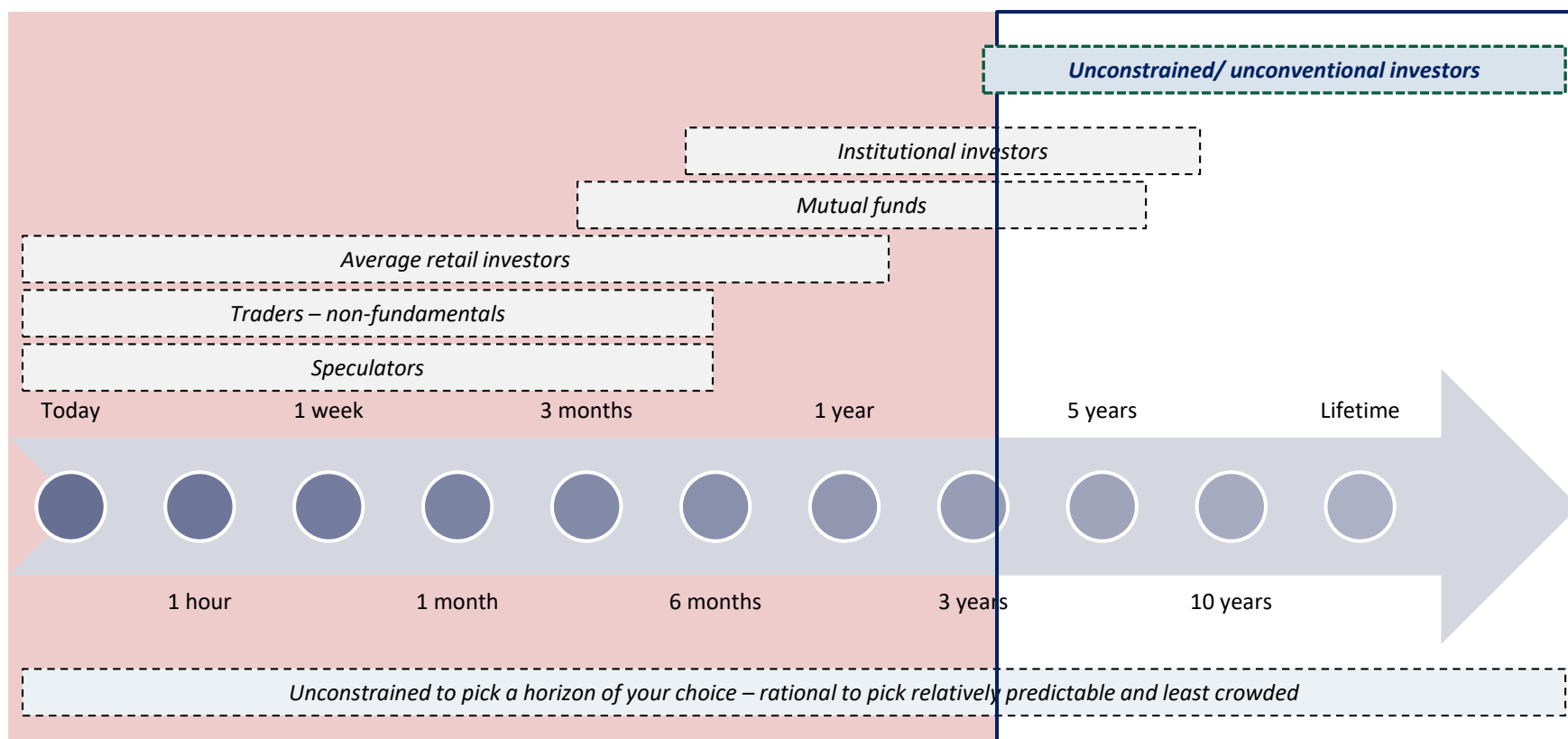
- *We believe there are lessons to be learned from such “special situations”, which might be difficult to foresee upfront at the time of making the investment.*
- *Although in this situation we were able to exit with sound investment returns, we will remain mindful of such dynamics dramatically altering the economic prospects of potential portfolio companies in the future.*
- *Another key learning is that our “best idea” is highly unlikely to perform as a “best idea” ought to in a single year. Two reasons: a) Noise factor is pronounced; b) Special situations may arise wherein “buy and forget” may lead to suboptimal outcomes*

**Personal investment details shared for educational purposes only. All personal records are unaudited and are not to be misconstrued as an investment track record.**

## Best idea 2018 is not necessarily optimal “for 2018”

*Time & Qualitative arbitrage are two key sources of edge for us as allocators*

*These two characteristics usually manifest themselves over a significantly longer duration than one year*



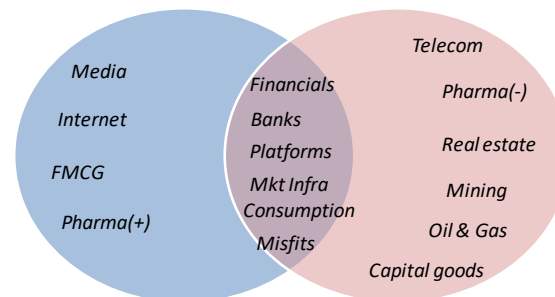
## Our investment approach in India

### Our Investment criteria

Seeking Compounders	
Universal	Understandability
	Competitive advantages
	Prudent capital allocation
Special India Focus	Scalability
	Resilience to alternative outcomes
	People - management & promoters
bought at a price which allows for the effect of compounding profits to manifest itself	

Finding "Hexagons"

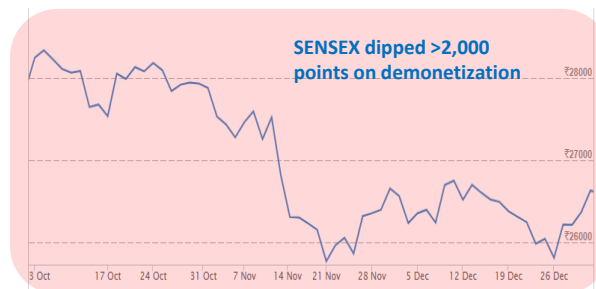
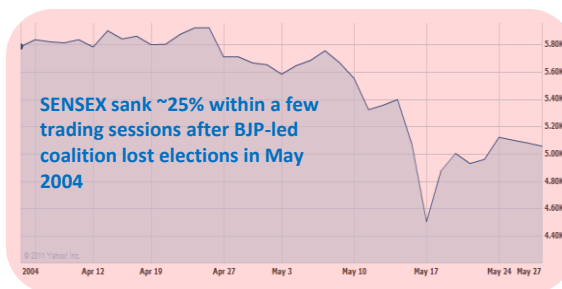
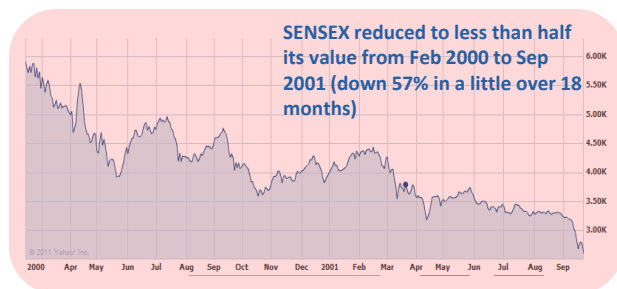
### Opportunity set



Cross-section of companies we've admired  
**(this is not our portfolio)**



# Investing in Indian equities = A big macro call on India?





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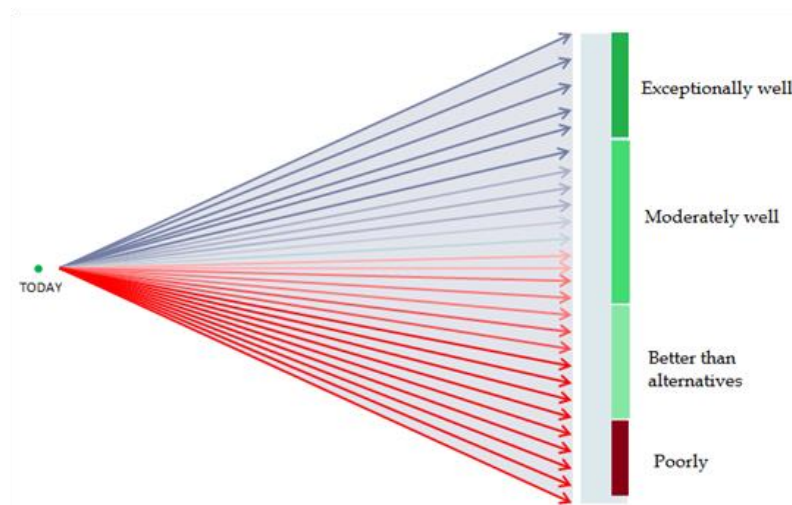
## Low base effect

Country	Vehicles / 1000 pax
India	13 / 1000
China	45 / 1000
Russia	188 / 1000
USA	1200 / 1000

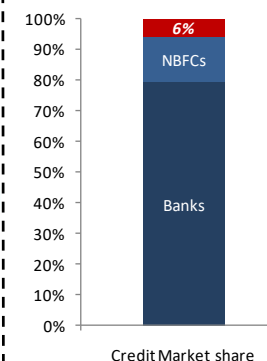
Country	Toothpaste per capita
India	127 grams
China	255 grams
USA	542 grams

Country	Power cons. per capita
India	~800 kWh
China	~3500 kWh
USA	~13,000 kWh

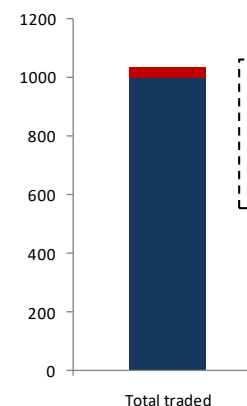
## Resilience



## Large addressable opportunity



*HDFC Bank Loans:  
~6 Tn  
Outstanding credit  
~100 Tn*

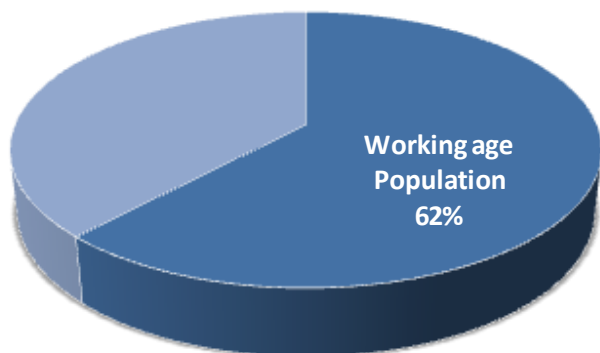


*<3% of total industry  
volumes traded on our  
portfolio company  
"platform".*

Note: Statistics and company data are a little dated but provide the broader perspective

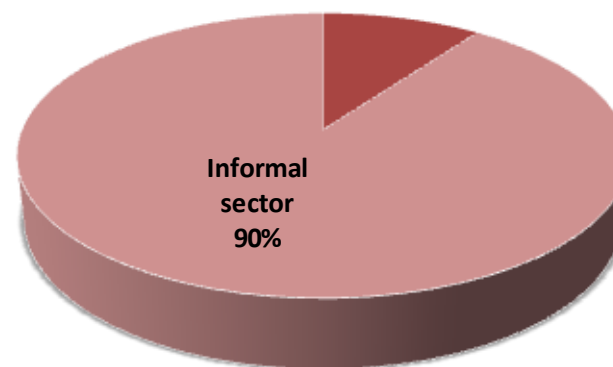
## Employment in India

*Demographic dividend of 1.2 bn people*



*Total  
workforce  
~450mn*

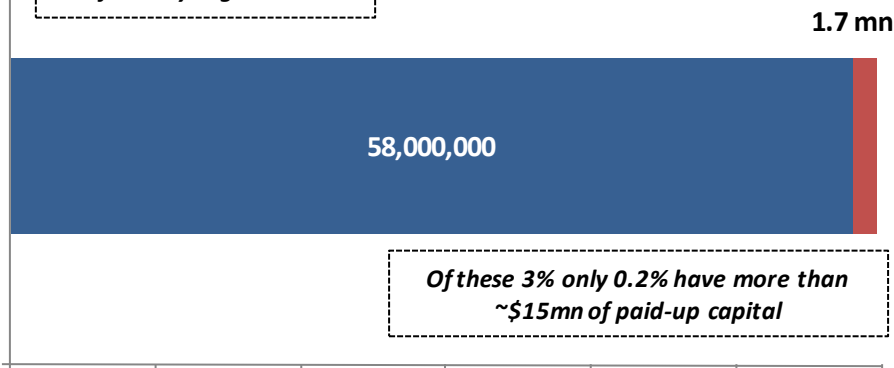
*...yet only 10% of workforce is "formal"*



*Non-farm  
workforce  
~240 mn;  
~1/3<sup>rd</sup>  
formal*

*Large proportion of enterprises "unregistered"*

*Only 3% of enterprises are  
formally registered*



*Of these 3% only 0.2% have more than  
~\$15mn of paid-up capital*

*Low element of formalization (ex-agri) driven by...*

### **1) Weak tax compliance**

*Well understood by analysts and investors*

### **2) Onerous labor laws**

*Contours of this are perhaps less clear to indirect allocators*

**"A company in India can't comply with 100 labor laws without breaking 20"**

**Refer to:** Industrial Development Act Section V-B, Industrial Disputes Act of 1947, Factories Act of 1948, Contract Labour Act of 1970

**In fact:** 44 Central laws, ~100s state laws; 9/44 Central labour laws date back to 1947; 3 post 1990

## Indian Employment Sector: Flexi-Staffing Agencies

### Flexi-staffing globally vs. India

#### Globally

- Seasonal variations
- More expensive vs. permanent
  - Usually fewer benefits
  - Usually lower wages
- Perception/ stature concerns
- Very fragile in tough macro

#### India

- Regulatory compliance
- Search & recruitment costs
- Less expensive vs. permanent
- More benefits vs. informal
- Higher job security vs. informal
- Aspirational – upward mobility

**Even large corporations** often prefer meeting incremental, non-core headcount requirements through “employment specialists”

### Structural and secular formalization “shocks”

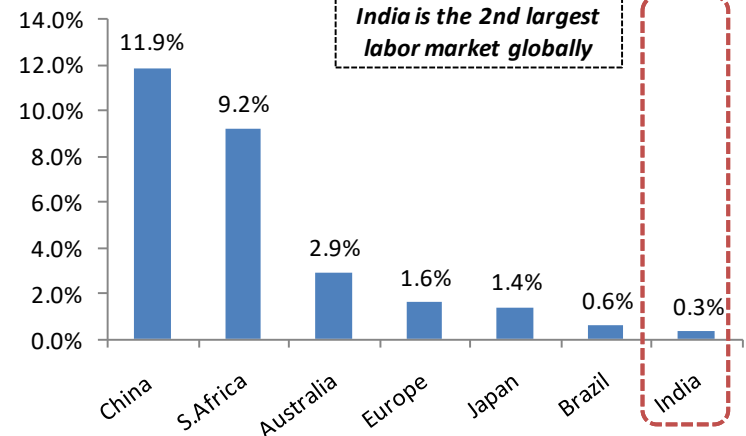
**Significant shifts in nature of employment & regulatory ecosystem** are increasingly nudging participants to “formalize”

**GST:** Single value-added tax on goods & services replaced a myriad of former taxes/ levies eg: central excise duty, service tax, octroi etc.

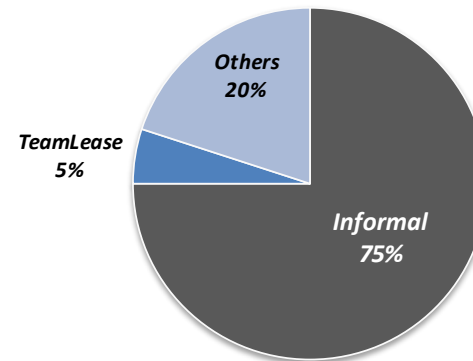
**Demonitization:** A one-time shock to the “undeclared cash” economy. Greater personal income tax filings, increase in formal savings

**RERA:** Real Estate Regulatory Bill to foster transparency in sector

### Very low flexi-staffing penetration in India



### Majority of flexi-staffing operates in the shadows



Regulatory arbitrage offered by informal operators – don’t pay indirect taxes; deny employees mandatory benefits etc.

**The flexi-staffing industry is likely to be one of the major beneficiaries of these gradual shifts over the next decade**

# ***Teamlease Services Ltd.***

***Listed on BSE & NSE***

***Share price: ~INR 2,300***

***Market Cap: ~INR 3,900 Crores (~USD 580 Mn)***

## About Teamlease Services

### Teamlease Services Business Model

#### **Teamlease is a “people supply chain” company:**

General staffing contributes >95% of revenue

>2,500 companies as clients

>170,000 associates (40,000 trainees) placed at

>6,000 locations across India

Specialized Staffing ~3% of revenue: +++ margin profile

Other services (Compliance, payroll etc.) ~2% of revenue

Revenues of >INR 3,000 crores (>USD 450mn)

Net margins >2% (cost plus markup model) & ROE >19%

Top 10 client concentration ~19%

Sectoral exposure: Retail 24% Manufacturing 20% BFSI 9%  
Telecom 7% FMCG 6% Agri 5% IT 5% Auto 4%; Ecommerce 1%

#### **Have placed 1.8Mn people since inception.**

Committed to education through the lens of employability

Like a true platform ignited the demand side and now working intensively on deepening the supply side – ie. Right-skilled people in the right place at the right time

#### **Competition** TL market share ~5% among 6 large players

However, >75% share remains with informal players who skirt compliance & regulatory costs by denying benefits etc.

***This dynamic is now dramatically changing***

### Founding team – Purpose driven industry veterans



#### **Manish Sabharwal (Co-founder, Executive Chairman)**

Manish provides leadership at the Board level and drives strategy. In 1996 he co-founded India Life Pension Services, a payroll and pension services company that was acquired by Hewitt Associates in 2002. He was Chief Executive Officer of Hewitt Outsourcing (Asia) based in Singapore for 2 years. Manish serves as a Member of the National Skills Mission, Member of the Central Advisory Board of Education, and an Independent Director on the Board of the Reserve Bank of India (RBI). He is an alumnus of The Wharton School, University of Pennsylvania.

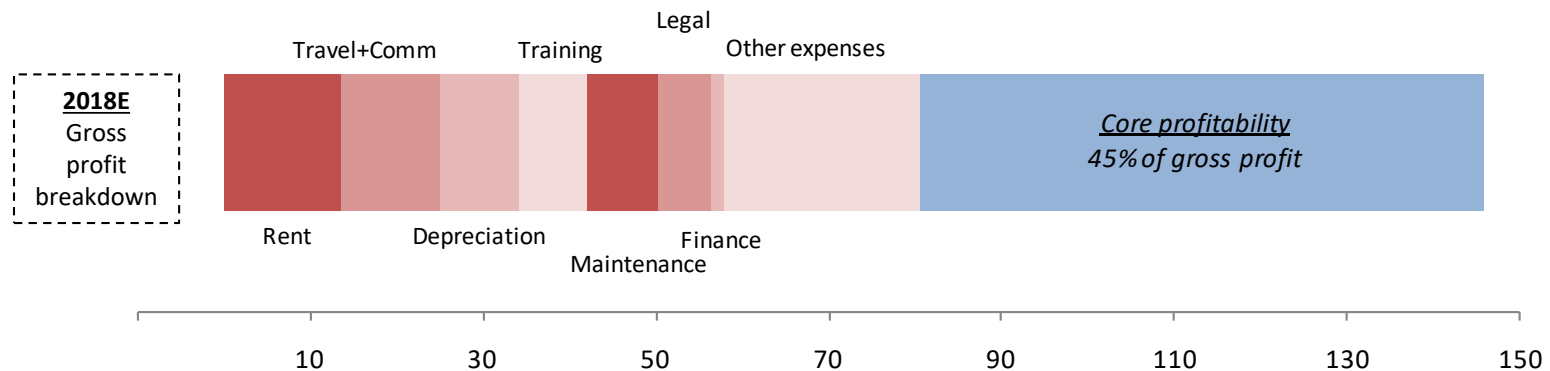
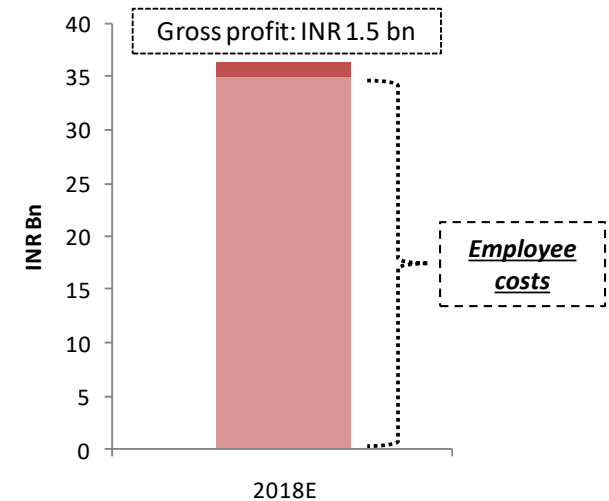
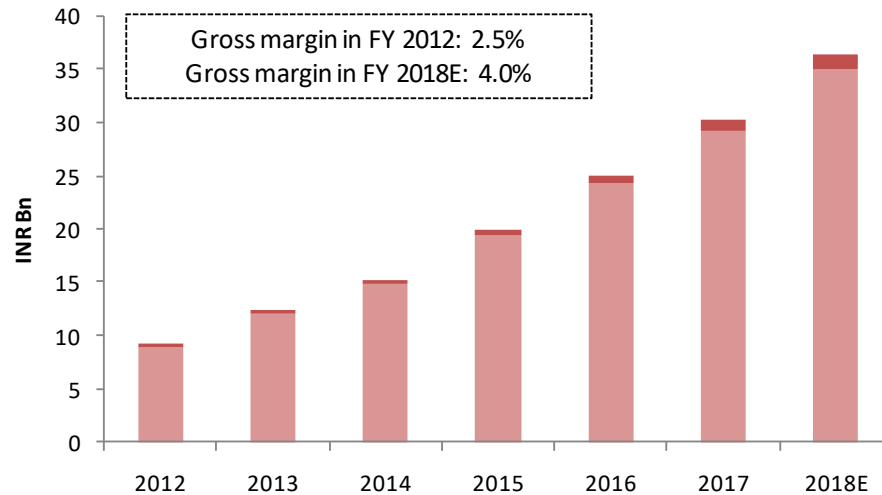
#### **Ashok Reddy (Co-founder, MD & CEO)**

Ashok oversees operations & represents the company in forums with major clients. He holds a bachelors degree in commerce from Shri Ram College, Delhi and a Diploma in Management from Indian Institute of Management, Bangalore. He is a first generation entrepreneur with over 17 years of experience in the industry of human resource services. He was a co-founder and Director of India Life Services, a pension and provident fund asset management company. He has been awarded the “Skills Champion of India” award in the category of Skills Champion & Emerging Warrior for his outstanding contribution to the field of skill development.



## Teamlease Services: Margins profile

*Limited margin for error!*



## Teamlease Services: Headcount breakdown

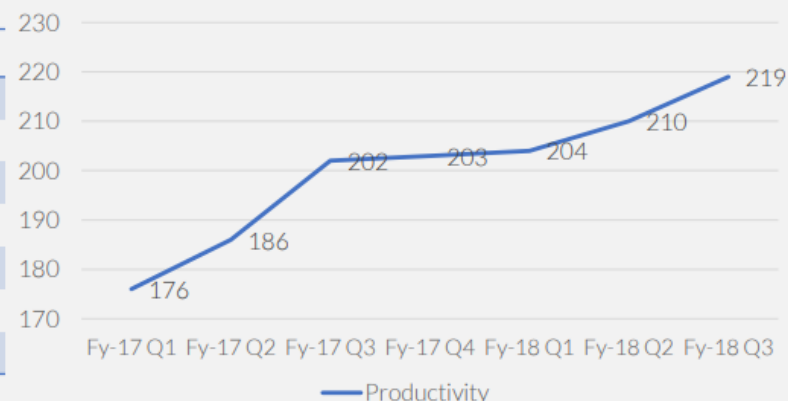
### Headcount growth and productivity

Quarter	General Staffing Associates	NETAP Trainees	Specialised Staffing	Total Outsourced	Core Employees	Total Headcount
FY-17 Q1	1,13,713	14,155	-	1,27,868	1,276	1,29,144
FY-17 Q2	1,15,397	17,787	1,103	1,34,287	1,386	1,35,673
FY-17 Q3	1,23,946	19,427	1,261	1,44,634	1,406	1,46,040
FY-17 Q4	1,26,463	23,439	1,251	1,51,153	1,436	1,52,589
FY-18 Q1	1,29,787	28,051	1,423	1,59,261	1,467	1,60,728
FY-18 Q2	1,27,844	32,615	1,631	1,62,090	1,466	1,63,556
FY-18 Q3	1,30,950	40,423	5,910	1,77,283	1,632	1,78,915

### Improvement in Core Employee Productivity

Quarter	Total Outsourced	Staffing Core Employees	Staffing Productivity
FY-17 Q1	1,27,868	727	176
FY-17 Q2	1,33,184	716	186
FY-17 Q3	1,43,373	710	202
FY-17 Q4	1,49,902	738	203
FY-18 Q1	1,57,838	773	204
FY-18 Q2	1,60,459	764	210
FY-18 Q3	1,71,373	781	219

### Productivity



~20% CAGR of Associate headcount over past 5 years

~27% CAGR of Revenue over past 5 years

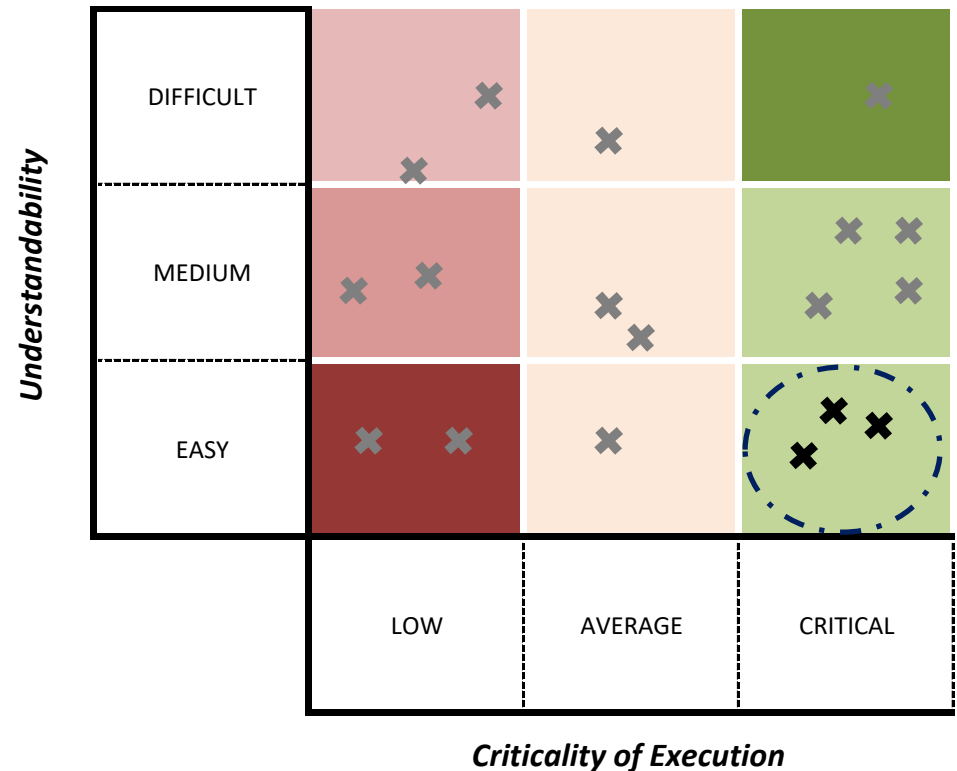
## A business that is easy to understand but very difficult to do!

*Low barriers to entry but High barriers to success*

*Easy to understand but difficult to do*

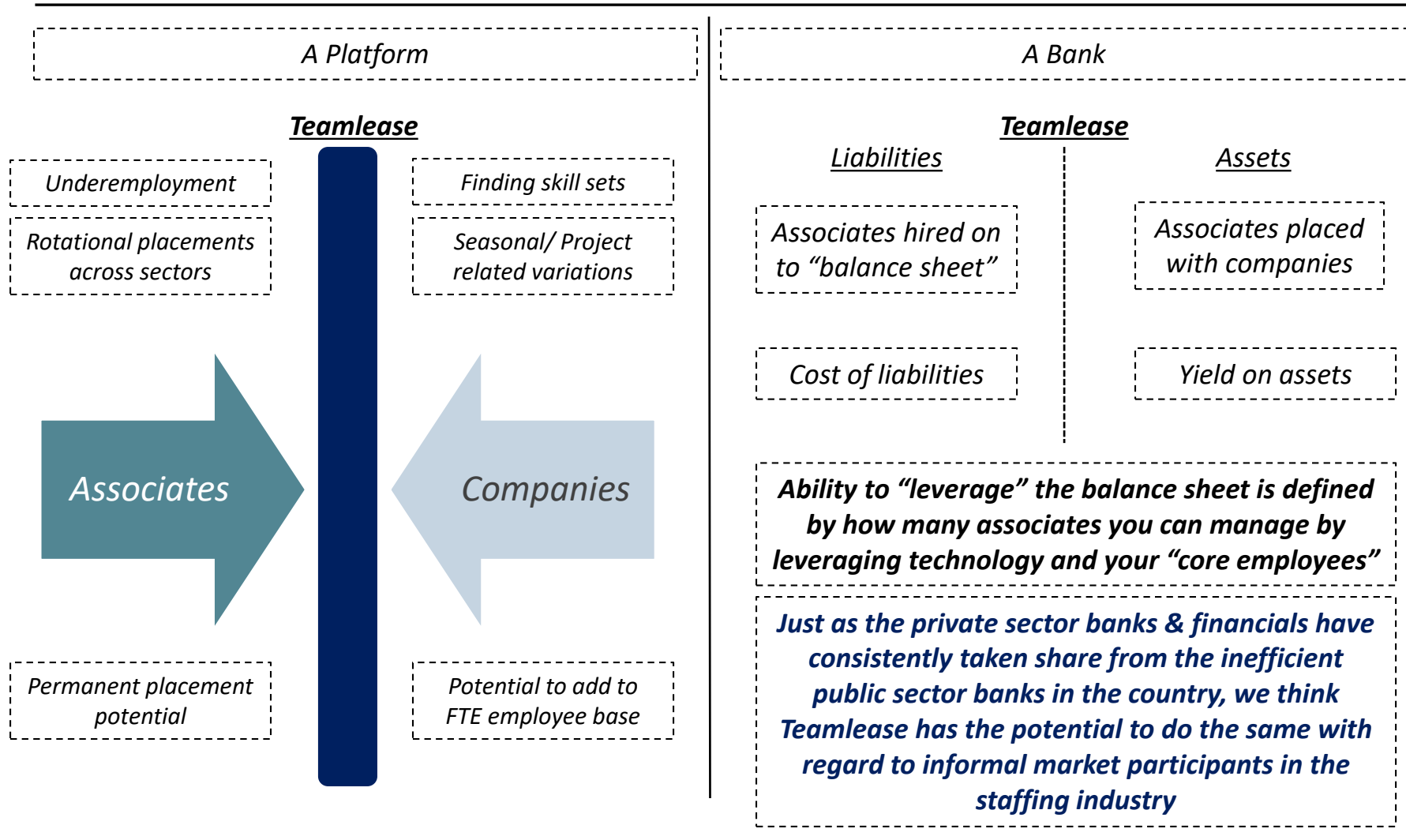
Attribute	Quantum
Barrier to entry	<u>Low</u>
Pricing power	<u>Low</u>
Switching costs	<u>Low</u>
Execution & cost control	Critical

Variables customers seek
On-time payments to associates
HR support to companies & associates
Robust statutory compliances



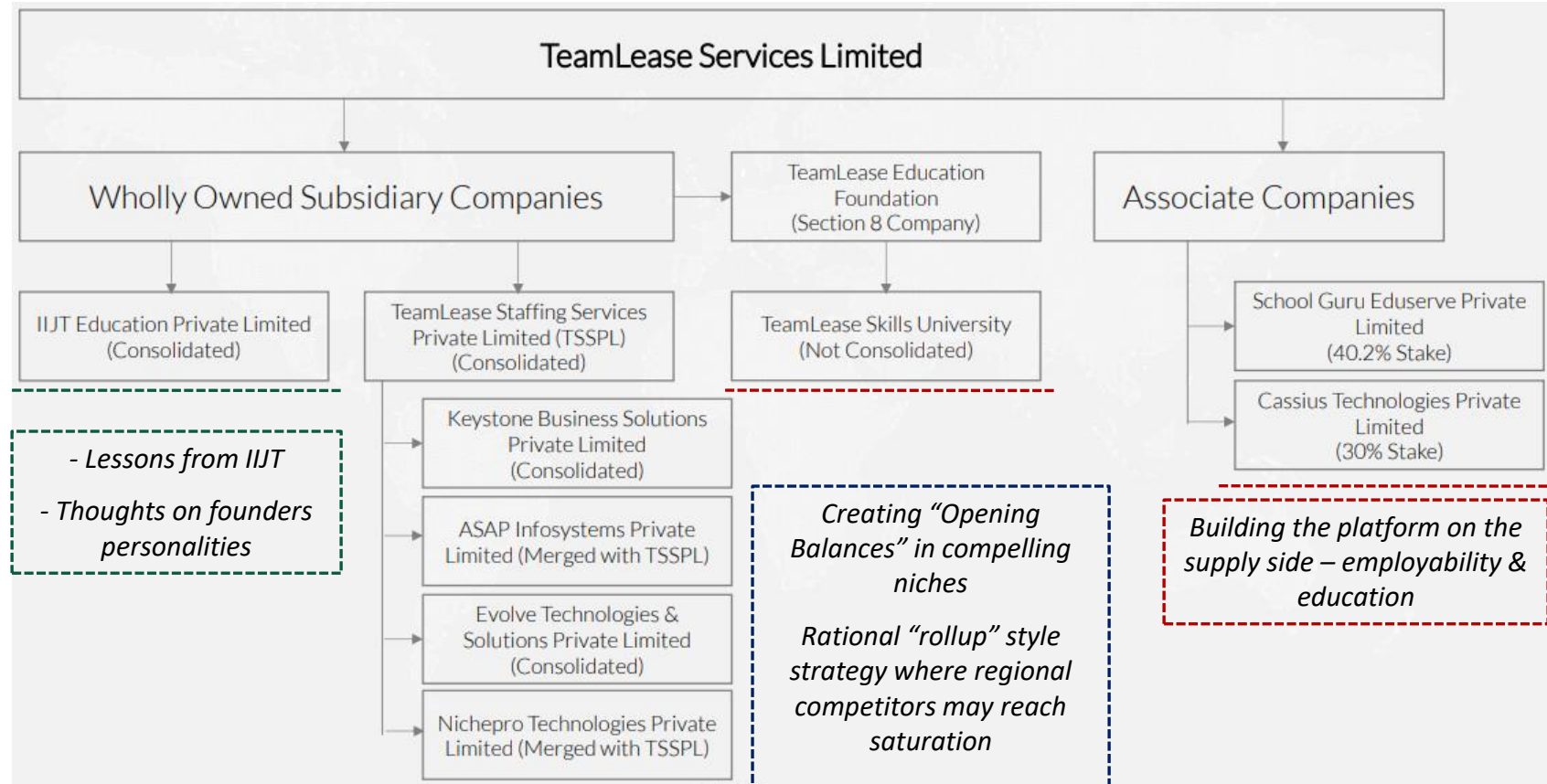


## Analogies for the business model



# Employment, Employability & Education

## Corporate Structure



## Power of past experiences

### *Learnings from past experiences*

#### Allocating Capital

*On a relative scale – Teamlease has been more focused on organic growth with regard to the core business than is typical in this industry.*

*However they follow a disciplined approach to acquisitions when they pursue them:*

- IIT Acquisition
- Acquisitions for IT/ Telecom Staffing
- Acquisitions for Sourcing
- Acquisitions/ Investments for Education & Employability

#### Sectoral exposures

*Teamlease was heavily dependent on the Banking & Financial Services Sector entering the Global Financial Crisis of 2008-2009. During that phase:*

- Revenues shrunk ~50%
- Headcount shrunk ~46%

*Now much more balanced in terms of sector contribution  
Even sectors with high concentration – Manufacturing & Retail tend to be more granular in terms of underlying clients*

### *Driven by purpose*



#### **Employability**

IIJT Education  
Schoolguru Eduserve  
NETAP



#### **Education**

TeamLease Skills University  
TeamLease Education Foundation  
NETAP  
IIJT Education  
Schoolguru Eduserve

### *Thought leadership creates opportunities for advocacy*

**EMPLOYMENT  
OUTLOOK  
REPORT**

TeamLease White Paper on RPO

Jobs and Salary Primer

**Regulatory ALERT**

**WORLD OF WORK SERIES**  
INSIGHTS INTO THE EVOLVING WORLD OF WORK



**NETAP**

*Public-private partnerships*

## Shareholding Structure & Going Public

### Shareholding structure

Category	% of shareholding
Promoter Group	37.0%
Exited Promoter	5.9%
Gaja	8.5%
Anchor FII	12.2%
Anchor DII	13.5%
Non-Anchor FII	13.7%
Non-Anchor DII	4.3%
Employees	1.9%
Retail/HNI	2.4%
ESOP Trust	0.6%

### Dec 2017 Institutional Shareholding:

HDFC Prudence Fund ~8.9%  
 FIL Investments ~4.4%  
 T.Rowe Price ~4.4%  
 Goldman Sachs India ~4.1%  
 Goldman Sachs Funds ~3.3%  
 Reliance Equity Opportunities Fund ~2.6%  
 Aditya Birla Sun Life Midcap Fund ~1.8%

### Teamlease went public in 2016

*IPO value ~4.2 Bn INR in February 2016*

*Listed at ~INR 860 vs. ~INR 2,200 CMP*

*Private equity investors made exits/ partial-exits at IPO*  
*Gaja Capital & ICICI Venture*

*~1.38 Bn INR fresh issue of shares*

### *Used proceeds for acquisitions including:*

Nov 2017: Schoolguru (40% equity for ~INR 135 mn)

Oct 2017: Evolve (INR 370 mn\*)

May 2017: FreshersWorld (30% for est. ~INR 60 mn)

Jan 2017: Keystone (INR 82 mn)

Oct 2016: Nichepro (INR 295 mn)







Sep 2016: ASAP Info Systems (INR 670 mn)

*\* Deal value for Evolve as reported by VCCircle*

## Global peers – Adecco &amp; Randstad

Companies	Adecco	Randstad	Teamlease
Associate headcount	700,000	670,000	180,000
Full time employees	34,000	38,000	1,600
Clients	~100,000	~100,000	~2,500
Revenue contribution	General staffing ~75%; Professional staffing ~20%; Other HR Services ~5%	General staffing ~55%; Professional staffing ~20%; Inhouse services ~25%	General staffing ~95%; Professional staffing ~3%; Other HR Services ~2%
Geographical spread	Europe ~65%; North America ~20%; ROW ~15%	Europe ~75%; North America ~20%; ROW ~5%	India 100%
Countries	60	39	1
Margins	EBITDA ~5%; Gross ~18%	EBITDA ~5%; Gross ~20%	EBITDA ~2%; Gross ~4%
Financial scale	Revenues € 23.6 Bn; Net Income ~€ 788 Mn; Mcap ~€ 9.9 Bn	Revenues € 23.3 Bn; Net Income ~€ 756 Mn; Mcap ~€ 9.4 Bn	Revenues ~€ 0.46 Bn; Net Income ~€ 10 Mn; Mcap ~€ 0.46 Bn
Return on equity	~20%	~15%	~19%
Organic growth	~6%	~8%	~15% - 20% over LT

## Our expectations over the long run

<b><i>Structural - Narrative</i></b>	<b><i>Check</i></b>	<b><i>Fundamental - Medium-term &amp; Long-term</i></b>
<i>Large inefficient incumbents controlling more than 75% market getting “disrupted”</i>		Robust headcount growth of ~15% over long-term
<i>A difficult to operate/ scale business for small/ medium/ inefficient practitioners</i>		Market share gains at expense of the informal sector
<i>Customers paranoid about compliance; very few practitioners with intellectual bandwidth</i>		Successful hunting & farming campaigns; focus on customer “wallet-share”
<i>Improving margin profile by targeting compelling niches – eg. Telecom/ IT</i>		Strengthening profitability margins from ~2% net to ~3.5% net over the long-term
<i>Leveraging technology/ AI to handle larger associate base without commensurate growth in core-staff (ie. Higher productivity)</i>		Productivity ratios to move north from ~219 associates/ core employees over the long-run
<i>Acquiring intellectual depth in tangential areas (eg. Jobs portal for sourcing talent; Online courses provider for enhancing employability etc.)</i>		Enhancing capabilities of associates and improving their employability prospects – widening the spread earned 5-6% Long-run realization growth

## Our expectations over the long run – detailed

### Snippets of our 10 year view: long-term earnings power & value

- 1y forward earnings ~42x; 5y forward earnings ~<15x; 10y forward earnings ~<5x
- “1y forward” can be very misleading in meaningful structural growth scenarios given that..
  - We expect bottomline growth in the long run to be >~25% over 5y and over 10y
    - This is likely to be driven by a combination of..
- Topline growth of ~20% and modest but consistent margin expansion over a decade bolstered by
  - 1) Higher margin profile of nascent, high growth businesses &
  - 2) Operating leverage – non-linear nature and impact of productivity growth

### However, no detailed 10 year models this time!

- We still build these for our mental clarity, intellectual curiosity & to appreciate natural limits/ tolerances
  - However more reticent in sharing these widely given how circumstances can change
- We still hold that very few businesses lend themselves to such a build-out in terms of “certainty”
- Do not want a case-study model to be viewed as consisting of “projections” with regard to regulations

## Risk factors

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### Company Specific Risks

- Continued rationality crucial in allocation of capital
- Changes in alignment of interests as shareholding structure evolves
- High exposure to single business line – general staffing

### Macro / Thematic Risks

- Softer than anticipated transition from informal sector to formalized economy
  - Weaker than anticipated employment generation over next decade
- Impact of artificial intelligence/ technology on relatively lower-wage, entry level jobs
- Consistency of regulatory support toward temporary staffing industry in form of incentives & recognition



## Teamlease scores well on our investment criteria

<i>Seeking Compounders</i>		<i>rationale</i>	
<i>Universal</i>	<i>Understandability</i>	<i>yes</i>	<i>we believe we understand the business and its prospects over the long haul</i>
	<i>Competitive advantages</i>	<i>yes</i>	<i>barriers to entry low but barriers to success high</i>
	<i>Prudent capital allocation</i>	<i>yes</i>	<i>experience has made founders very prudent in allocating free cash flows</i>
<i>Special India Focus</i>	<i>Scalability</i>	<i>yes</i>	<i>large market share gains likely from informal sector which is facing several structural "shocks"</i>
	<i>Resilience to alternative outcomes</i>	<i>yes</i>	<i>gains resilience with scale - vulnerabilities of 2008/09 have imprinted learnings</i>
	<i>People - management &amp; promoters</i>	<i>yes</i>	<i>Passionate and purpose driven founder-led management team creates strong alignment</i>
<i>bought at a price which allows for the effect of compounding profits to manifest itself</i>		<i>although not available at a bargain price, long-term allocators ought to take a closer look</i>	

## Q&amp;A

*Do reach out to us if you find yourself in our neck of the woods – [soumil@dmzpartners.in](mailto:soumil@dmzpartners.in)*



*Standing (L to R): Chandrakant, Mahesh, Soumil, Mitesh & Anil  
Seated (L to R): Shriya, Rushabh, Sanjay, Jinesh & Mihika*

*Our investment office team in Mumbai, India*