

Infosys Technologies Limited

2006 ANALYST MEET

July 30-31, 2006

Session 3 by Naren Koduvattat

Naren

My name is Naren Koduvattat and I am Vice President heading the Energy, Utility, Resources business unit in Infosys. A reasonably new business unit in Infosys, it came into formal existence in 2004 when we had the last reorganization. Now, I would like to quickly go over the market and then talk about what is our strategy, what we are doing, and what is the result so far. The resource, energy, utilities are three distinct markets, each of them with different challenges, different change drivers, different sizes and so on. But just to give an idea about the size of potential, out here you can see close to 100 out of the Fortune 500 belong to this segment and a lot of IT spend. There are some slides about IT spend coming up later but quickly to define the markets itself, energy is the definition we use for oil and gas markets which is further classified into upstream, midstream, downstream or exploration production (E&P), supply and trading, refining and marketing as the downstream. We have the utilities which is the public utilities. Predominantly we are talking about North America and Western Europe which is divided into three business lines from their side, which is transmission and distribution, generation and customer care/customer service and then we have resources which is a very large segment which is another acronym for process manufacturing which is covering chemicals, metals, minerals, mining, agro and so on. So three separate markets, very large potential out there and looking at the next slide you will get an idea about the spend. Conservative estimates would tell us that, close to \$ 30 billion is the annual spend in IT and services and Infosys is just beginning to realize the potential. To give an idea, fiscal 2006, the worldwide revenues from this particular segment was close to \$ 175 million dollars for us. So that is where we are.

Now the spend itself if you look at it oil and gas typically spent anywhere between 1.5% to 5% of their annual revenues depending upon the kind of company you are looking at. Utilities on an average, is 3% of their annual revenues and resources again depending upon the size, the global reach of these companies would be anywhere between 1.5% to 2.5% to 3% of their annual revenues would be spent in IT services. Now utilities particularly, the high percentage is also because they include energy management services and their planned operations, a lot of decision support systems and all that under IT. So that is why it is steady at the 3%. In terms of the market growth what you would see is oil and gas particularly worldwide, has been growing and it is projected to grow at around 9% increase in IT spend. Utility in the Western Europe is growing at close to 3% per annum whereas the US has been declining at 3% per annum. So it is kind of flat worldwide. Resources is growing close to 4% anywhere between 2% to 4% depending upon the geography you are looking at. Potential-wise it is pretty big out there, you can see the numbers.

Now market challenges, very distinct challenges for all these markets. The major drivers across the board are two things. One is the high oil prices which works advantageous for oil and gas companies because they make tons of money out of that but for other two segments, oil and gas being the major inputs into their operations are major cost concerns. The other consistent theme across all these companies is the ageing work force. All these companies, most of our prospects, customers have been in existence for multiple decades and are facing the threat of their knowledge and their processes walking out of the door when their people retire. And third of course is oil and gas companies, as well as the resource companies are on a major globalization spree. They are scaling up worldwide, their new markets are coming up, particularly the South East Asian, the South American markets and their challenge right now is to support those operations as close as possible and also with a cost-effective model. And the fourth of course is, they have been with the legacy the big four so to say, they have been with them for literally decades and there is a lot of pain being endured by them through those relationships which are typically multi-year lock-in contracts where in they feel that they need flexible contracts which will support them through the ups and down of businesses and so on. Most of these companies out here are very heavily regulated both in terms of compliance laws, reporting laws and also in terms of environmental and safety aspects. So their pressure on reporting is extremely high and that is also adding a challenge of getting the information in time, real time information and information accuracy. It is a big challenge for them especially when they are starting to spread all over the world. So a couple of such major issues out here. Now particularly in the utilities, the energy bill 2005 of the US, has been a major driver, prompting a lot of fresh capital to come into their transmission and distribution line of business and also leading to a lot of merges and acquisitions.

If you look at their sourcing habits, all these companies and utilities are traditionally national company. There are not many multinational global utility companies except for couple of European examples. All of them are either state centric or country centric but oil and gas and resources traditionally have been multinational. They have been having operations and expansions worldwide. They are masters in sourcing from the local markets. That is nothing new to them but when it comes to knowledge services, sourcing from the global markets and offshoring and all this is relatively new for these companies. You can see less than 10% of the companies are really into offshoring and then global sourcing and all when it comes to IT and knowledge services. So once again big potential out there and also what would it make them to source from offshoring Global Delivery Model? It is not just the technology capabilities but two main things would be the ability to scale up or down and two bring in very deep domain expertise because these companies for them the distinction between a business process and an IT support is very very little. For them it is all bundled into one. Most of their sponsors are actually from business and not necessarily from the technology side and they are very firm believers in building relationship with those people who understand their business and have the business capabilities. Given then what is the strategy from Infosys side. One, of course we want to leverage our operations excellence. Two, we want to leverage the full service capability which has been assembled at Infosys. I am talking about the multiple services and the subsidiaries what we have. We want to really employ the full service capability from day one and actually the low penetration of Infosys into these markets is giving us a great opportunity to position our brand very differently from what we have been positioned in a lot of other sectors and you will see the results of what we are trying to do in the coming slides. But the key thing which is being driven at our end, is the verticalization where we believe that this is the true differentiator. This is what is going to get us a new brand positioning at a higher premium which we believe we can command in the market and that is the only way to take on competition which is the entrenched players who have been their for literally decades and that is our primarily game plan and we believe that we need to demonstrate a lot of growth in terms of both client base as well as at the top line and differentiation in terms of how much of our services are being used by these customers and how much premium are they going to pay for us. And then finally like I said, we truly believe that here is a case where Infosys can actually achieve a completely futuristic brand position.

Looking at that, I just want to give you an idea about what kind of verticalization strategy we have and how we are going about implementing that. What do you see in the outside, those circles are all about the implementation details, a lot of acronyms there but just quickly to walk through that, we are heavily investing into competency building through our competency framework which is the driver in that is what we call certification. We are engaging external agencies which are the worldwide reputed institutions who will give us the certifications at three levels. Level one is at entry level, level two is at a practitioner level and level three is at an expert level. To give an idea as of the 2005, beginning of 2006, we have 55 people and by 2007 we are targeting to have 350 people or more than that certified at level two. And these certifications are coming from industry-recognized universities which are actually used by our clients for their internal employee certification. So, Oxford Princeton is our partner in giving the oil and gas certification, and EEIA, Edison Energy Institute of America is going to be our partner for giving the utility certifications and so on. Similar to that if you look at it, you are partnering with the industry bodies like CIDEX and ChemIT, which are industry consortium who are working on industry standards in the chemical industry. Our people are part of that trying to help them to define the standards and also learning from that. And the other aspect is, we are trying to build competency around specific industry-niche products and some of them are listed out there. Plus the generic global ERP systems like an SAP, they have industry-specific modules like the SAP IS Oil which is very specific for oil and gas, SAP CCS which is very specific for utilities. We are investing into that and then building up capabilities around that.

The other one is the traditional ADM, the application development maintenance services revenue stream for Infosys or for that matter any similar company, we believe that will have to be transformed into a vertical services segment. So we will have the horizontal technology practices like an SAP or an Oracle or whatever and we need these niche vertical practices and that is where the customer is going to put their money on. We have already rolled out two of them both of them for utility companies, GIS and CIS, Global Information System and Customer Information Systems and then the work in progress is what I am showing in blue all over the place. We have an electronics trading and risk management system service which will apply for utilities as well as for oil and gas and the exploration production which is for upstream oil and gas companies. Now all these will have to be reflected in the kind of solutions which we are building out there. Some of them are already out there and some of them being build and that is what you would see there specific for each of the industries. These are point solutions which are being built. The IRP is a refinery portal solution. It is an application of a linear algorithm in the refining capability for a company. ITS is a trading solution. Retail natural gas storage, distribution and billing kind of a solution. CCSS is for Customer Care replacement and replenishment. Procure-to-Pay is improving the supply chain of oil and gas and utility companies. RFID applications are not in just the conventional movement of material but also possibly in human capital tracking and then reporting because that is a big concern area for a lot of these companies and corporate performance management and work on all these things along with niche industries players who are

there. For example, Pinnacle is a very boutique customer care consulting firm which is based out of the LA region. Triple Point is a trading and supply optimization product company, SV is a GIS tool and Kaleido is a decision making system. It is some where between a data warehousing and a business intelligent system very specific for, very heavily used in the oil and gas sector and like that work-in progress of a few others.

The other thing we are trying to do and have been pretty successful is instead of just being a service provider to some of our clients, we are also exploring whether we can be go to the market partners with our clients so that we can help them either to reach out to new geographies or to capture new segments in their existing markets. So we have at least four arrangements like that right now. Results are just starting to come in and that is why I did not list in them.

Where is it all of this leading to? If you look at the growth, that is where the critical numbers are. Combine the segments worldwide in Infosys revenues were 3.28% in fiscal 2004, which has risen to 6.68% as of last fiscal and trends wise it is continuing to increase. So we are pretty bullish about know what is happening in these segments. Majority of the revenue has come from non-US but I just want to clarify it out here. This non-US is also the companies who are head-quartered in Europe not necessarily where the work was delivered. It is delivered literally all over the world. We have close to 27 countries where our people are actually helping these customers to deliver projects and all that because many of them, especially the oil and gas upstream as you know operates all the way from South America all the way to the Siberian side. So our guys are going to all these places, in fact to the African regions also quite a lot of them. You can see the growth by industry out there. In terms of differentiation like I said, the question is how much of our services are going to be used by these customers. You can see in a short time, the spread of services being utilized by these customers have increased drastically. Almost entire service portfolio from Infosys is being lapped up by customers out there and particularly if you notice it, the consulting plus ERP space in this has grown tremendously. In fact our space, the energy resources utilities customers are the largest utilizers of our consulting arm. 10% of our revenues come from pure consulting itself. And this is not just consulting but it is always consulting which is leading to downstream. That is the standard Infosys model. We do not do just pure business consulting or strategy consulting for the sake of that. We look for an opportunity where we can actually get into business process definition and take it all the way down to the platform implementation. So that is a kind of focus we are developing right here. Another feel of the growth what we have and the kind of differentiation, if you look at it, there is a very large client-base being built and most of the clients with pretty good potential to grow to \$ 5 to 10 million kind of a range. So we are focusing on rapid expansion of the client base at this point of time. It will be really an opportunity out there investing into growing these clients.

Two case studies I wanted to mention about. One is with a very large oil and gas major worldwide super integrated company. We had a new line of business coming out of the North American region for the natural gas liquids and Infosys was contracted to do the business blue printing all the way down to the SAP implementation. The technology chosen was SAP and this is the first time that the TSW, the Traders Work Station of SAP was implemented for a gas business. 15 months end to end consulting to implementation program and went live on budget on time line, and we employed our value realization model which is a consulting model where in up front, you can quantify the business benefits which will be derived out of an implementation and track them through the milestones so that there is a guarantee that the business is delivered. It is a question about managing the IT budgets and this was very successfully deployed in this particular one very large implementation.

And the second one is for a utility client. It is an American utility, \$9 billion client. They had a challenge that their client base was increasing very rapidly. In fact this is the largest growing client base in the entire US and their existing CCS system, the application as well as the call center, could not simply scale up to do this and their business was completely dependent on this because utilities in the US especially those which are regulated have to make a rate case to the respective public utility commission who will investigate into reduction of cost and increasing of customer care in order to award them an increase in the tariffs. That is how the regime works and this was so business crucial for them. And we did the entire blue printing, the change management, the entire training and the technology implementation and the rate case as of last month was approved. So that they could actually revise their billing rates and introduce some of their new products and all those things. This was measured, typically utility customers, their customer care efficiency is measured in what is called as 'Average Call Handle' time and the target was to reduce it between four to nine seconds and each second reduction typically goes for a \$ 1.5 m savings per annum. That is how it works, that is how the business case is because it leads to reduction in repeated calls, it leads to reduction in staff, it leads to reduction in infrastructure and other cost and that is how this business case was done and we could substantiate through the measurements that the business case was indeed implemented. So those are the two case studies I wanted to share with you.

Questions, I will be ready. Thank you.

Participant

I will just repeat the question it was about what is the onsite offshore mix and also what kind of a pricing trend are you seeing?

Naren

The onsite offshore, to begin with 2004, we were close to 45 to 55 kind of range. If I look at it today, I would say it is anywhere between 36% to 40% onsite and 60% offshore on a steady state. But it can be little misleading because depending upon the growth and the number of clients you add, to give an idea last quarter we added four clients. Obviously the onsite will go up at that point of time. But I would say steady state it will be close to 40% today.

Participants

Is this in terms of effort or revenues?

Naren

It will be in terms of effort, not in terms of the billing because when there is high percentage of consulting involved, the per capita productivity from the consulting side is significantly higher than our India based or the offshore based billing rates. So that could be not a good reflection. In fact if you look at the per capita productivity of this particular business segment, it is close to 30% higher than the Infosys average. I mean I do not have the exact number but I would say, it is around 30%. Billing rates, what we are seeing is all the new contracts we are winning, are coming with a better premium compared to a lot of competition. That much we know and like I said within Infosys also, we are able to command a premium over what has been the historic averages of Infosys and as long we can substantiate through the good spread of services and the verticalization, that is the domain knowledge, we are pretty confident that we can continue to command the premium. Because the entrenched players out there are just there either because they have been there, they have the relationship or because over a period of time they have built up that additional competency or the vertical knowledge, the business knowledge. If you can ramp up on that front, I don't think there is a cap on the premium. So the trend is possible.

Participant

So, in general, if I want to _____

Naren

We are able to, in fact many of our MSAs already have a built-in rate revision clause which is called the cost of living, COLA, COLA-related clause and also the new ones which we are signing on is dependent upon the large number of services which we are able to offer to them. So the trend is definitely there. Anyway I have to be very clear on this because I do not have the exact data, but I would say the last three years, 3% to 4% YoY is the per capita productivity improvement we are able to achieve. So, I would say that is also attributable to the rates.

One point I forget to mention in the earlier two sessions also, I forget to mention is that the resources in Infosys annual report and the quarterly reports is coming under the manufacturing segment. So you would not see separate resources being reported. It is close to around 15% to 16% of our manufacturing line item what you would see in our reports. I want to make sure that I mentioned that. Historically, we have been reporting it as manufacturing.

Okay, food for thought. Thank you very much.