Infosys Technologies Limited

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FINANCIAL HIGHLIGHTS

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CFO

Good morning friends. It is great to meet you again and talk to you about Infosys. In the next few minutes, let me take you through the financial highlights for Infosys.

When we started the year, it was an uncertain macro-economic environment. In fact when we gave the guidance, some of the investors called me and said “Are you sure, you guys are so aggressive?” When we gave the guidance for the 3rd quarter they are saying “You are too conservative.” The world has changed in the last six months. So when we started the year, the macroeconomic challenges were much bigger. Some of the customers got impacted. In fact they had a huge change in their operating environment and to that extent, it impacted their IT spending. There was pressure on volume growth, there was pressure on pricing and customers were not even finalizing the budgets in the beginning of the year. Add to that the currency volatility was too much. We have never seen currencies being so volatile. It is changing around 10-15% each quarter. So we started the year in a much more uncertain environment but when we went through the year, things started stabilizing. We responded to the situation very well. We worked with the clients very closely, understood the pain points, tried to become their transformation partner. In fact recently we did a customer survey and customers ranked us very high. In fact it is the highest ranking we have seen in last many years. They really think we are transformation partners, we understand their needs and they need us more now. And we focused on cost control and efficiency. We cut whatever we could. In fact we deferred the wage hike which we normally give in April because of the uncertain environment but recently we gave that. We focused on what we can control and controlled that much more efficiently. We focused more on risk because there are customers who were going through bankruptcy; the credit risk of the clients was deteriorating. In fact when the whole thing happened we started following credit default swap spreads for all the customers and made sure wherever the credit risk was very high, we go and collect the money much more timely from the clients. In fact on the BFSI side, our DSO days were less than 30 days. We normally give a credit period of 30-45 days. Overall for the company, it is 56 days, on the BFSI sector it is less than 30 days. And also the contractual risk, clients are asking for much more credit period, contractual terms were becoming tougher. So we put in place checks and balances internally to make sure we are not over-exposed to any contractual risk.

We maintain a liquid balance sheet. We have $ 2.8 billion of cash. Cash is becoming God. If you have, you worship it. That is what we did. We kept $ 2.8 billion of cash. It is still there. We actively managed our foreign exchange exposures. In fact if you noticed, some of the competitors went and hedged for the whole industry. We made sure we hedge only for ourselves that too, for the short-term. We never took a long-term view, we took a short-term view because we felt in a volatile environment there is no point in taking a long term view, it helped us in this volatile environment.

So the first two quarters came out better than what we guided. In fact for the 1st quarter we guided $1.06-1.08 billion of revenue, we did $1.12 billion and again in 2nd quarter we did much better than what we guided. And we increased the guidance for the full year. Our current guidance is a decline in revenue between 1-1.3% and EPS between 6.7-7.1%. But there are also a lot of good things. We increased employee addition guidance from 18,000 to 20,000 and we also increased the wages for employees. This shows the flexibility we have in the financial model. We are able to make the right investments at the right time and make sure the growth is not impacted.

These are the highlights for Q2: Our revenue grew 2.9%, guidance was 1.1%. Pricing went up by 0.4% but in constant currency, it was still a decline of 1.1%. So whatever pricing adjustments we did in the past few quarters, it will have a tailwind affect in the next few quarters. You could see that coming in. But the top 10 customers grew by 6%. That is a very positive thing because we are able to mind them more. Clients really see us as a transformation partner because we worked through tough times with them. And we added 6,000 employees. Our guidance was 5,500. We added 35 new customers. Attrition came down, DSO days is 56 days one of the best in the industry and we saw increase in volume growth offshore which was around 3%. So there are a lot of positive things in the actuals for Q2 and that could percolate in Q3 and Q4. Our guidance for Q3 and Q4 show 1% growth, that is a realistic guidance based on what we see at this point of time.

We have a very flexible business model. We are able to maintain our operating margins in both tough times and good times. In good times when you have flexibility, you make the right investment. In tough times, we have to control certain costs which are discretionary which we can live without and we try to make sure that our operating margins are less impacted. Today our operating margin is 30.2% which is the highest in the industry. There are some competitors who are trying to catch up on the margins but more than the quantity of the margins, quality of margins is very important. I will take you through some of the accounting policies we have. So in terms of quality of margin, in terms of quantum of margins, I think we have one of the best in the industry. The income tax - effective tax rate has gone up this year because some of the STPs went out of tax holiday, so the tax rate came up from 4.2% of revenue last year to 7.1% this year but still the net margin is same, 27.7% because we have a lot of levers on the cost side. Like the revenue mix from different services – if you are able to do more business on the enterprise solution or consulting side, the margins are higher. That could give you some buffer on the margins and the scale benefits on the G&A costs. We can get some savings on the discretionary costs if we need to, to make sure the margins is less impacted. Onsite-offshore mix - if you are doing more work offshore where the gross margin is 70-75% as against onsite where the gross is something around 20-25%. So if you do more work offshore it is beneficial to the margin. Second, subsidiaries - some of the subsidiaries are making losses. Today most of the subsidiaries are contributing positively to our gross margin. Employee utilization is a big lever. Today our utilization excluding trainees is around 73% including trainees is around 67%. For every 1% movement in utilization, we could have a 40 basis point impact on the margin. So that is a big lever we have on the cost side. And also the employee pyramid, people keep worrying about the employee wage increases in India. In good times it work out up at 15%, they all think at some point of time U.S. and India cost will narrow but that is not going to happen in our lifetime. It’s going to take a long time. Since we have a pyramid structure, the average cost per employee does not go up so much because we add a lot of people in the bottom of the pyramid and make sure we manage it more efficiently. We also have variable compensation structure. 30% of offshore wages is variable salaries linked to performance of the company both in terms of top line and operating margins. So that is a big lever we have on the cost side and some of the discretionary cost we can cut. So since we have multiple levers on the cost side, we can use some of them at some point of time to make sure the operating margins are less impacted.

Look at our accounting policies: We have one of the most aggressive depreciation policies in the industry. We amortize all the computers in two years. Our policy is 2-5 years, building 15 years, all other assets 5 years. All the R&D costs - we fully amortized, software – we fully amortized, we do not capitalize it. Accounts receivable - we provide for all receivable more than 180 days at any point of time whether it is collectible or not. We also provide for all doubtful receivables. We mark-to-market all our hedging instruments. It all flows through the income statement. We do not have many defined benefit plans. We have only one that is gratuity which we actually value every quarter and provide for it. We fully funded the trust. So if we look at the quality of the earnings, it is one of the best in the industry. If you look at the balance sheet of this company, I do not think you can find a clean balance sheet than this in any part of the world.

In terms of balance sheet, zero debt. We continue to be zero debt. We have $ 2.8 billion of cash. Free cash flow generation, it's one of the highest, $ 1.12 billion last year, $ 743 million in the first half. 30% of the revenues is free cash flow. How do we do it? The biggest thing is account receivables. There are two things that the top management sees every day in this company. One is cash and bank balances because we have to make sure whatever revenue we have shown, that is real and that exists and we have the cash. Second - account receivables, because selling is easy, collecting is very difficult, unless the client is very clear that you have done a good job he is not going to pay. So these are the two metrics which the senior management sees every day. Our DSO days of 56 is one of the best in the industry. So I think in terms of free cash flow generation, 30% free cash flow (as percentage of revenues) is one of the best in the industry. Quality of account receivables - 77.9% of receivable in less than 30 days. We do not have any long overdue receivables. We pay up to 30% of our net profits as dividends every year. Our Return on Capital Employed is 41%, Return on Invested Capital excluding cash is 75%. So we are a cash generating machine which is running more efficiently year-on-year.

What are the key challenges for us today? Currency - today we have around 10% of the revenue coming from U.K. pound, around 7% from Euro and around 5-6% from Australian dollars. These currencies are moving something around 10-15% each quarter. That is a big challenge for us because we report numbers both in U.S. dollars and Indian rupees. Add to that the Indian rupee-dollar volatility. We have never seen this kind of volatile environment in the past. So we have to proactively manage all the moving parts and we do it through hedging. We have around $700 million of hedges as of September 30th. We have taken a view that we are going to cover our exposure for next two quarters at any point of time, net exposures not gross. Every quarter our revenues are close to $1.1-1.2 billion, 50% of it is net earnings. So we can cover up to a billion dollars, we have covered 70% of it for next two quarters. We believe that currency markets, whether we like it or not, is going to be too volatile because there are a lot of moving parts. It is not only how the Indian economy performs against other economies, the cross-currency also matters. So we have taken a short-term view and we will continue to take a short-term view till there is some stability or sanity in the global currency markets.

These are details on the currency exposures. You can see the movement. GBP moved 12.3% against dollar in the last quarter and Euro and Australian dollar moved by 4-5%, a huge movement for any company to manage. We have seen the currency rates at different levels but still, we have made sure the impact on margins is very minimal. If you look at rupee, it went to 50.72. That is the highest average rate we have seen. The operating margin was 29.5%. We have seen Rupee at 40.02. Our operating margin was still 27.8%. What this shows is we have a flexible financial model which can take some of these shocks even if the revenue declines. Even if the currency volatility is high, we are able to pull out some of the levers and make sure the impact on the margins is minimized. So the flexibility in the financial model helps us to go through tough times and also give us flexibility to invest when things are really good.

Income tax - we have two schemes in India. The STP scheme, which gives a 10-year tax holiday and the Special Economic Zone scheme which gives a 15-year tax holiday. Most of the STPs will get out of tax holiday this year and next year and SEZ scheme will continue and in India we also have a new tax code which is coming into effect in 2011 where they are trying to remove all the tax exemptions and trying to reduce the statutory income tax rate. Today our effective tax rate is somewhere between 20-21%, next year it could go to around 25-26%. So when the new tax code comes and when all the exemptions go, the step functions for us on the income tax is very low. We may go from 25% to maybe around 26-27% or somewhere closer to 30% but other companies have to go from 15-16% to maybe around 25-30%. So the impact for us when we get into full tax regime is very less as compared to others.

There are details on subsidiaries: Today all of them are contributing more positively to the margins. To that extent the impact because of subsidiary will come down, that will be a good buffer for our margins.

We continue to invest in sales and marketing. This is a story we are keep hearing, we are not investing in sales and marketing. We have around 815 employees in sales and marketing, we have 571 clients; our repeat business is 98.4%. We have very good investment in sales and marketing. We continue to invest in sales and marketing. We have not cut down that even in tough times. At the same time we do not need to spend huge amount of money in getting a brand ambassador because we are not in a consumer business. We are in a relationship business. That is why we get 98.4% of our revenues at repeat business. So our sales and marketing spends will be purely people's spend, that is number of hires. We will continue to do that. We are not under spending on sales and marketing. This is a story I keep hearing. That is not true. We are sufficiently invested in sales and marketing today.

So in conclusion I will say we are focusing on high quality growth. We want high revenue productivity, superior growth, superior margins. There is no trade-off between margin and growth. If somebody says there is a trade-off, it is wrong. Dropping your margins is very easy to do. Tomorrow we can bring it down to 20%. If we have to take it up to 25% or 30%, it is going to be a huge climb. We have high quality margins; the quality of our margins is extremely good. We are focused on margins and at the same time we are focused on growth. We are doing a balancing act. We want both. We are not focused on one against another. With this I conclude. Thank you.