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DEUTSCHE BANK INVESTOR TOUR

CORPORATE PARTICIPANTS

N.R. Narayana Murthy
Founder, Executive Chairman, Board

Rajiv Bansal
Chief Financial Officer

ANALYSTS

Aniruddha Bhosale
Deutsche Bank

Janakiraman
Franklin Templeton

Anuj
SBI Mutual Fund

Prasun Gajri
HDFC Life

Prashant Jain
HDFC Mutual Fund

Harish Trivedi
DSP BlackRock

Sandeep Mahindroo

Hello everyone and good afternoon. Thanks a lot for being able to make it and coming to Infosys for this session. We have Mr. Narayana Murthy, Chairman and Mr. Rajiv Bansal, Chief Financial Officer. The way we are planning to structure the session is we will have some initial remarks by Mr. Murthy. After that we will open it up for Q&A. It is about one hour session that we planned till 4 P.M. With that I will pass it on to Mr. Murthy.

N.R. Narayana Murthy

Thank you, Sandeep. First of all, good afternoon and welcome to every one of you. It is an absolute pleasure to interact with you all. I want to thank each one of you for taking time off from your busy schedules and visiting us here. I thank Deutsche Bank for providing us this opportunity to meet up with you all.

We appreciate your deep affection and interest towards us over the last several years. We are extremely grateful to you for the trust you have shown to us over the last several years. We are also very grateful to you for your good wishes.

I will talk about our strategic priorities, our focus areas and how we are planning to achieve our objective of building what I once termed “A Desirable Infosys.” During this interaction, I will also try and address your concerns and your interests.

First of all, our vision was, is and will be, to be a globally respected corporation that provides best-of-breed business solutions, leveraging technology and delivered by best-in-class professionals. Nothing has changed there and nothing will change because respect from every stakeholder is our top priority.

Having said that, I must admit that we are not happy with our performance over the last 2-2.5 years. In the Financial Year 2012-2013, our growth plummeted to 5.8% which is almost half the Indian Software industry growth rate which was proclaimed to be about 11%. Next year that is the Financial Year 2014, as we have already forecast, our growth is expected to be between 11.5%-12% compared to about 13% growth that NASSCOM has articulated. In other words during the year 2013-2014, we would have doubled our growth rate. But even this is slightly short of the average industry growth rate as enunciated by NASSCOM and therefore we are not happy with it.

Parallely, there is another reason why we are not happy with ourselves. That is because our operating margins have come down from 29.5% in the year 2010-2011 to 23.5% for YTD Dec-13. In other words, we have lost about 6 percentage points in our operating margins. What makes it worse is the fact that rupee depreciated from somewhere around INR44 to $ 1 to somewhere around INR55 to $ 1which means there was a depreciation of as much as approximately 20% in the rupee. Given that between 50% and 55% of our expenses are outside India and about 45% of our expenses are all accumulate in Indian rupees, that margin would have gone from 29.5% to app. 40% if we had benefited from the devaluation of the Indian Rupee. But, operating margins went down to 23.5%. Therefore, we have had a huge drop in operating margins and therefore we are not very happy with ourselves.

Now, let me come to the next important issue: There has been a lot of discussion on whether ‘Infosys 3.0’ is the right strategy, whether we are revising it after I came back, whether we are taking a U-turn etc. Before I comment on it, first of all let me recapitulate what our strategy is, as part of Infosys 3.0. The first tenet of our strategy is to focus on opportunities that emanate from Consulting-led end-to-end business solutions leveraging technology. The second tenet of our strategy is to delink revenues from person month effort through Intellectual Property-based

Products, Platforms and Solutions. The third tenet of our strategy has been to win highly competitive, highly commoditized large outsourcing projects involving what we call 'BITS', which includes Application Development, Maintenance, Testing, BPO and Infrastructure Management. This is our strategy as was communicated in 'Infosys 3.0'. The revenue distribution across these three streams is about 33% came from Consulting-led solutions, about 5.5-6% came from Platforms, Products and Solutions and about 61-61.5% came from large outsourcing projects.

What is the change that we are making in view of our slow growth? The only change that we are making is we are focusing on winning a larger share of the outsourcing deals where focus got blurred in the past. Our people were extremely enthusiastic about transformational projects which are consulting-led. These were complex projects, these were advanced technology projects, these were critical projects for the customers, but by definition, consulting projects are smaller in size. Therefore, our people focused enormously on Consulting-led transformational projects and they became the leader in that area. As we all know Infosys was far ahead of any of the Indian competitors in the consulting-led projects – we had 33%and the next candidate perhaps had about 18%. Therefore, we are not going to change anything in that. We are not going to say we will reduce our focus on complex, advanced technology, transformational projects. No, we will not do that. Similarly, we are still in early stages of Products, Platforms and Solutions. Even though Finacle is a mature product, it has been installed by 181 banks, it is ubiquitous Core Banking Solution. But we still have a long way to go in order to make Finacle contribute a significant percentage to our revenue. Therefore, we are not going to defocus on that. In fact, we are focusing even more on bringing the focus on Products, Platforms, and Solutions. The reason why we did not grow as well as we wanted in the period 2011-2012 & 2012-2013 is because we lost focus on large outsourcing projects. These are highly commoditized and highly competitive. In order to succeed in that area, we have to adopt the adage "the market determines the price and therefore the company has to determine the cost" to have adequate margins. So therefore, the only change that we have brought about and that you will see is in the execution of this strategy, is in focusing even more on outsourcing projects. In order to be successful in the adage, "market determines price and the company determines cost", we discussed and debated and we found that there are 3 levers that we have. First one is obviously, a short-to-medium-term one which is cost optimization. Second one is improving our sales effectiveness so that we sell more than what we could do in the past. That will take between 9 and 21 months. The last one is effectiveness to improve our software delivery productivity and to bring in whatever automation is possible in development of Software, in Infrastructure Management Services, in Independent Validation Services, in Business Process Management, in Application Development and Application Maintenance, etc. We believe that will take anywhere from 18 to 36 months.

Insofar as the cost rationalization project is concerned, we are using multiple levers. One, we are saying that we should all eliminate all wasteful expenditure, leverage the power of localization, optimization and put the right level of people and the right competence in the right jobs. Then we said, we will reduce onsite-offshore ratios. As a result of these efforts, which are still in work-in progress, our offshore effort improved by about 1.3% from 68.8% in Q2 to 70.1% in Q3. The result has been an improvement in the operating margins of about 1.5%. Our operating margin in Q2 was 23.5% and the operating margin in Q3 was 25%.

Insofar as the sales effectiveness is concerned, we are putting in lots of systems to enable our sales leaders to train our people better, to measure the performance of our people better, to improve the quality of our solutions and proposals, to measure the performance of our sales people to link the variables to the performance and to create better coordination between our sales people and software delivery people. We are also putting in lots of ideas to enhance our differentiation. As I pointed out, this initiative will take 9 to 21 months, therefore we still have at least another year.

Insofar as improving the software delivery effectiveness is concerned, we believe that it is time that we put back Infosys as the 'Gold Standard' in software delivery execution which was what we were known for. As you people know very well, we used to command a premium of 20-25% compared to our Indian competitors at a given customers place. We realize the only way we can get back to that scenario is if we reestablish ourselves as a 'Gold Standard' in software delivery excellence.

We have to reenergize our people. We have to bring a new sense of confidence, hope and enthusiasm in our people which we are doing. We have to increase our focus on meritocracy, with a strong focus on hiring competent people, with a strong focus on training our people, with a strong focus on assessment of competence of our people and providing an opportunity for better and better career opportunities for our internal people before we hire from outside.

Our revenue per employee in Q3 increased by 1.8% onsite and about 1.7% offshore in constant currency. However we need to see whether it is indeed a trend or it is one-off. We have lots of initiatives which will take anywhere from 18-36 months, more like 36 months and we believe at the end of the 36 months period, we will have a reasonable chance of bringing back the delivery excellence of Infosys to its original standard.

Of course, at the end of the day, the only way we can say we have succeeded is if we bring back the 'PSPD' model of Infosys into play – that is Predictability of Revenues, Sustainability of those Predictions, Profitability and De-risking. If we can make a success in these four directions, I believe that there is reason enough for us to be happy about whatever we are doing.

Many of you have been wondering about the so-called 'Management Exits'. But, let me once again say very clearly that barring a few exceptions, no one who was adding commensurate value with his position or compensation, has left Infosys. Period. Second, there is considerable depth of leadership available within Infosys, it is a very-very important point. Third, we have conducted surveys amongst our customers and these surveys show that the quality of our software delivery, level of service and the speed of response have not been impacted an inch by these exits.

Now, let me come to the last item which is the CEO's succession and organization restructuring. We believe that the creation of the position of 2 presidents, with every one of the segment heads having independent P&L responsibility, our disbanding the Executive Council, are all extremely well thought out and positively impactful initiatives for the company. Mr. Shibulal is retiring in March-2015 and we will ensure that there is a suitable person to replace him by that date. We have had changes in the internal Board of Directors. We have had Ashok Vemuri leave us, we have had V. Balakrishnan leave us. We have had B. G. Srinivas and UB Pravin Rao promoted to Presidents and Directors on the Board.

You will see more changes in the next 12 months because Mr. Shibulal is leaving in March 2015, Mr. Srinath will be leaving in November and Mr. Kris Gopalkrishnan is leaving in April-2015. We have also had changes in the external Board of Directors. We have had Mr. Deepak Satwalekar leave in November-2013, we had David Boyles leave us in January -2014, we will have Mr. Omkar Goswami leave us in December-2014. Therefore you will see these changes in the coming months.

However, let me assure you as I did earlier that the company will continue to strive hard to regain its original luster despite all these changes. I am very confident about it. I believe that we will leave no stone unturned in moving towards our objective.

One thing I can promise the investors is and that is we will always follow the two adages that I have practiced during the 30 odd years of my corporate life - one "let the bad news take the elevator, let the good news take the stairs". Second adage "when in doubt, disclose". This is the way I have run the business and this is the way I will run the business during the remaining period that I am here.

Thank you very much for your patience in listening. Now we will be very happy to answer any of your questions.

Aniruddha Bhosale

Mr. Murthy thank you very much for taking time out. This is Aniruddha Bhosale. I am the IT Services Analyst at Deutsche Bank. Just a quick question on couple of things you mentioned. One you said that you have to readjust to the reality of market determining the price and the cost is to be determined by the company which is the reality of the last 3-4 years but you also mentioned that eventually the target is to move to a PSPD model where you will bring in predictability and also effectively meaning that your endeavor is to increase pricing as compared to competition? How do you intend to marry these two realities because the market determining pricing reality is not going away anytime soon, the way I read it.

N.R. Narayana Murthy

Between 1993 when we went public and 2006 when I ceased to be the Executive Chairman, Infosys had a price premium of 20% to 25%. That's data, that's a fact compared to our Indian competitor. That happened because of the various differentiated business value propositions we brought to the customer's table. We were the first Indian company to be certified at level 4 of Capability and Maturity Model. We had the largest and the most rigorous training program in the industry. We invested the largest percentage of revenue in technology. We came out with several initiatives in business value addition paradigm and we were the first company to create a consulting arm and BPO arm so that we help the customer connect the boardroom with the boiler room, we practiced our precept. Because of such differentiating factors we got the price premium, I don't think God is finished with us. Therefore if this company recreates its mindset to focus on creating further differentiation, I believe that our desire to compete in this crowded and highly competitive market successful while creating additional margins, will be possible. Therefore our focus has been on improving innovation, on bringing new ideas in automation, new ideas in productivity improvement, improving our training, ensuring that the quality of the proposals that we submit to our customers is better, developing systems, processes, tools and methodologies for making the organization more robust, bringing back focus on meritocracy, measuring individual productivity, all these initiatives will take time. Let me be very clear, as I said it will take at least 3 years. If we are successful in doing all these things properly, I believe that there is a reasonable chance that we may get back to our former position.

Jankiraman

This is Janakiraman from Franklin Templeton. You have articulated that one of your current objectives is to increase your market share in the large outsourcing orders. Perhaps for us to understand that a bit better, can you throw some light on why you actually lost market share in this segment in the recent past? Was it only because of the fact that sales team put far too much focus on transformational and consulting projects and took their eyes of this ball or were there other issues also which lead to this loss of market share?

N.R. Narayana Murthy

I think the primary reason was that we our enhanced focus on what is technologically challenging, what is exciting for our customers and what we believe would bring transformational value to our customers and the results are there. App. 33% of our revenues comes from consulting-led services and the next one I believe is 18%. Results are there. But when the senior leadership in the company started encouraging these things, unfortunately people in the trenches did not realize that not only should they succeed in these challenging areas, they should also continue to focus on large revenue yielding opportunities which are commoditized but which bring in large revenues. Whatever I have studied in the last 8 months, I would say this is the main reason. I haven't seen any other reason. But right now what we are doing is that we are developing systems that bring to light to every level of leadership, any time there is less focus than required in any of our services or any of our opportunities. We are building systems that measures the performance of people in selling different skills, different opportunities etc. We are going to some advanced level of information systems that will help us as we move forward. But if there is any thesis that you have, I would like to hear that because at the end of the day, you from outside in some ways, do not have the blurring picture that we would who look at things from very close. I cannot see things clearly if I go too near. You may have some better ideas. Kindly let us know and we will certainly analyze it, we will certainly look at it and learn from it.

Anuj

I am Anuj from SBI Mutual Fund. I have two questions. First question is that one of the key components of Infosys 3.0 was a focus on digital, analytics and mobility. Now, when we try and talk to people in the industry and try and talk to different companies, even companies outside let's say the top 3 or 4 companies, then the general sort of coherent feedback is that TCS and Accenture are definitely ahead in analytics and mobility. These two were definitely a part of the focus areas. If there are any data points that would showcase how Infosys has done quite well and has had a good win rate or large revenues run rate in these areas that would be helpful, because it appears from the outside that even in the focus areas the results have not been delivered.

N.R. Narayana Murthy

Now, first of all we do not comment on our competitors. Therefore I don't want to say anything about what our competitors are doing. We have tremendous respect for everyone of them. At the end of the day if this country has to improve there should be thousand companies like us who have to succeed, perhaps do even better than us. As an Indian I have nothing but appreciation for anybody who does better than us.

Having said that the projects that we have done in Digital space are marquee whether it's in France, I do not have the exact details of the specific projects but if you come to my room I will show you a wonderful booklet that has been produced by Infosys France on Digital Transformation. Whether it is in the United States, whether it's in Australia, let me assure you one thing. In advanced technologies, Infosys will not lag behind, that is a fact. But the reality simply is these are small projects, these are $ 1 million, 2 million, 3 million kind of projects. The world has still not evolved into a stage when there $50 -$ 100 million digital transformation projects, it's not there. That's how in spite of all of that, app 33% of revenues came from transformational projects which is the highest in the industry. That's data, that's not manufactured by me, that's data. The next one we hear is 18%. Second, in terms of Mobility, Airtel Money is powered by our solution. Just to give you 1 example, we have done several Mobility projects in the US, Europe and in Australia. Therefore all that I can say is in the area of Mobility, Infosys is second to none. That much I can say. But also remember for example Airtel Money will take time to pick up. We have invested enormously in that. It will take several years for people in rural India, people in mofussil India, people in semi-urban India to start using the power of the Infosys solution which is being sold under the brand of Airtel Money, it will take time. Therefore there is nothing that is less then appreciable as far as Infosys is concerned in Analytics, in Mobility area or Embedded Systems or Engineering Solutions, absolutely nothing.

Anuj

Second question is that if one were to go back a year or so even then in our interaction with the management, we got a clear understanding that the management had realized that there were certain course correction steps that need to be taken, certain steps needed to be taken to correct the course and that market share in deals and the win rates needs to go up. Many of those steps are quite similar to the steps that you outline so it will be helpful to understand how over the last one year those steps have yielded results in terms of a higher win rate or higher deal flow.

N.R. Narayana Murthy

So, how they are today compared to earlier? Is that what you are asking or they did not take any steps, what is your question?

Question

Let me elaborate. Before you joined or even a year back or so, there was realization that win rates have gone down and steps need to be taken to correct that. As far as the steps that were required at the marketplace at the customer end are concerned, the steps or that the 3 points that you highlighted are in sync with the steps that got highlighted even 1 year back. As far as I understand where you differ is on the cost optimization part and on more aggressive offshoring etc. But as far as the action points related to win rates and sales effectiveness and things to be done at the customer end are concerned, those appear to be things that were clear to the management even 1-1.5 years back. So it will be helpful to understand how those steps have yielded results in terms of win rates.

N.R. Narayana Murthy

I don't know what steps were taken when I was away. Therefore I am not the right person, I will request Rajiv to answer that.

Rajiv Bansal

As you know, our growth rates were coming down right growth rate came down to around 26% to 15.8% to 5.8%. The fact is that all of us realized that there is an environment issue, the discretionary spend is coming down. But at the same time in the same environment, the competition has delivered much better results. So there are certain things that we need to correct in-house. We need to improve our sales effectiveness, we need to focus on large deals. Some of these steps were identified towards the end of the last financial year. When Mr. Murthy came back and he sat with the senior management, he sat with the employees, he spoke to the clients and he also put together list of things that we need to do, some of them were continuing from what was identified prior to his coming back and some of the new steps were added to add more focus to get back to what Mr. Murthy called as a “Derisible Company”. So it’s not that in the last 9 months, we have tried to create something completely new from what was being done earlier. There are lot of new steps has been added, there is lot of more focus, lot more energy in doing those things and more accountability and timeline drawn to that. We realized that there are certain things that we have gone wrong on, that we need to correct and we started the journey. If you look at it, we have bridged the gap vis-à-vis the competition. Last year we grew 5.8%, for this year our guidance is 11.5%-12%, so we are on the right path. We are bridging the gap with our competition. We are more confident about our margin profile. It may not be on a quarter-to-quarter basis but in the medium to long-term basis, we are improving on the margin front because of the cost optimization. We are looking at different operating models. The data shows that we are on the right path. As Mr. Murthy said, we are putting in all the right efforts, we are doing all the right things and we believe that if we do all the right things we will get reasonable results.

N. R. Narayana Murthy

I think there are a few things that are new. First one is we have reorganized our sales structure. The efficiency or the effectiveness of our sales organization is better today and therefore hopefully we will get positive results tomorrow. That is one thing that has happened recently. Second, we have started some initiatives in measuring individual productivity. But that will take some time for it to be accepted by everybody and to get the results. Third, our costs had gone out of control. We made lot of analysis and focused on how do we control this cost without losing focus on our objectives. So I think these are some of the things that we are doing, in addition to all the things that Rajiv spoke about.

Prasun Gajri

Sir this is Prasun from HDFC Life. On both the sales effectiveness as well as software delivery, clearly you have stated that these are longer term deliverables and could take some time. Need to understand couple of things on this. Number one, what is the trajectory of improvement from both these measures likely? Is it like it to be very back-ended or are we going to see some gradual improvement coming through in the interim. If so, how do we track that whether we are on the right track on these measures or we need to do a mid-way correction on these issues?

N. R. Narayana Murthy

First of all, I do not think we have done a 2 or 3 year, quarter-by-quarter analysis of what the impact of each of these will be on the revenues and the bottom line. At any point of time we look at only one year and when we come to the end of the year, we start making analysis and then we give our guidance for the next year. Therefore there is no issue of back-ending, forward-ending stuff, nothing of that kind. What we have said is that there are some fundamental initiatives that will likely result in the organization becoming stronger. For example, individual productivity, automation, meritocracy, better information systems, elimination of waste, location optimization, improving onsite-offshore mix. These are all initiatives that will add value to any organization. It may be that some organizations have already reached the optimal level. Therefore they do not need to do anything. But some organization like Infosys, in some ways slipped on this and therefore they need to do what is necessary. Therefore all that I can say is whatever we are doing is no rocket science, are things that are well understood, are things that we had to do. We have not done it with a timetable of quarter by quarter by quarter improvement. No, we have not done that. But we believe just as the cost optimization initiative has shown, it has already given us approximately about 1.5% operating margin improvement. We believe that other initiatives too will yield us benefits as we move along, but we know that some of these initiatives will take time. For example, sales initiative has to be accepted, people have to be trained and practiced, this is for about 1,300-1,400 people, that is going to take some time. The software delivery effectiveness thing will have to be accepted, people have to be trained and practiced for almost as many as 150,000 people. That is going to take time. We know that. That is the reason why we have not drawn any quarter-by-quarter topline target and bottomline target. Therefore I am not in a position to say whether it is front-ended, back-ended, none of that.

Prashant Jain

Sir good afternoon, this is Prashant Jain from HDFC Mutual Fund. Sir is scale a disadvantage for growth rates? We have seen different industries; smaller companies grow faster. In the past in IT services, we have seen bigger companies have continued to grow faster for fairly simple reasons. Are those reasons still valid or because of the commoditization and increasing maturity of tier 2, tier 3 players is that unlikely to happen in the future?

N. R. Narayana Murthy

Well, the conventional wisdom in all industries is that as you grow larger in revenue, growth rates generally come down. If you are a $1 bn company, if you want to grow at 20%, then you have to add incremental revenues of $200 mn. If you are a $10 bn company if you have to grow at 20%, you have to add incremental revenues of $2 bn. Finding market opportunities for the incremental $2 bn requires lot more effort than $200 mn. But as you rightly said there are companies and we salute them, who have demonstrated that they can continue to grow better than the industry average growth rate at larger revenue basis. That is an area where we are discussing, debating, criticizing ourselves, learning from all possible channels and trying to improve. Therefore all that I would say is that we have to learn from people who have performed better than us. Hopefully we will be able to learn and put that into practice.

Harish Trivedi

Harish Trivedi from DSP BlackRock. Sir how do you ensure backup plan for the management that can take Infosys to the next level even in your absence?

N. R. Narayana Murthy

First of all, as I told you, we will have a new CEO in place before Mr. Shibulal terminates his office in March 2015. We are focusing more and more on the Infosys Leadership Institute. We have identified several people for each senior position so that the organization is completely insulated from any possible risks. We are spending more on training of our people. In other words, we have taken all possible steps that will mitigate the risks from the exit of any critical position employee. That is what I would say.

Sandeep Mahindroo

We thank everyone for coming here and spending time with us. We hope you found interaction useful. I would also like to thank Deutsche Bank team for organizing this visit. Thanks everyone and safe travel back.