

Infosys Technologies Limited and subsidiary

Consolidated balance sheets

	<i>(Unaudited)</i>	
	March 31, 2003 (1)	September 30, 2003
ASSETS		
<i>Current Assets</i>		
Cash and cash equivalents	\$ 354,362,918	\$ 375,967,500
Investments in liquid mutual fund units	-	98,257,986
Trade accounts receivable, net of allowances	109,119,856	129,442,231
Deferred tax assets	288,541	116,065
Prepaid expenses and other current assets	24,384,316	29,323,666
Unbilled revenue	19,702,186	18,694,049
<i>Total current assets</i>	<u>507,857,817</u>	<u>651,801,497</u>
Property, plant and equipment, net	157,194,190	172,741,594
Intangible assets, net	6,471,236	2,628,011
Deferred tax assets	7,264,885	6,826,125
Investments	4,613,833	3,259,660
Prepaid income taxes	4,452,678	149,868
Other assets	16,454,328	16,862,659
TOTAL ASSETS	<u>\$ 704,308,967</u>	<u>\$ 854,269,414</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
<i>Current Liabilities</i>		
Accounts payable	\$ 426,611	\$ 235,574
Client deposits	3,208,295	3,037,861
Other accrued liabilities	46,249,269	60,087,899
Income taxes payable	-	5,834,081
Unearned revenue	13,202,115	15,551,461
<i>Total current liabilities</i>	<u>63,086,290</u>	<u>84,746,876</u>
<i>Non-current liabilities</i>		
Preferred stock of subsidiary		
0.0005% Cumulative Convertible Preference Shares, par value \$ 2 each, 4,375,000 preference shares Authorized, issued and outstanding – 4,375,000 preference shares as of September 30, 2003	10,000,000	10,703,364
Other non-current liabilities	5,217,758	4,427,001
<i>Stockholders' Equity</i>		
Common stock, \$ 0.16 par value; 100,000,000 equity shares authorized, Issued and outstanding –66,243,078 and 66,268,972 as of March 31, 2003 and September 30, 2003, respectively	8,602,909	8,605,728
Additional paid-in capital	127,042,751	128,818,007
Accumulated other comprehensive income	(31,444,835)	(6,610,579)
Deferred stock compensation	(2,817,066)	(673,687)
Retained earnings	524,621,160	624,252,704
Total stockholders' equity	<u>626,004,919</u>	<u>754,392,173</u>
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	<u>\$ 704,308,967</u>	<u>\$ 854,269,414</u>

(1) March 31, 2003 balances were obtained from audited financial statements

See accompanying notes to the unaudited consolidated financial statements

Infosys Technologies Limited and subsidiary

Unaudited consolidated statements of income

	Three months ended September 30,		Six months ended September 30,	
	2002	2003	2002	2003
Revenues	\$ 181,446,939	\$ 250,768,976	\$ 337,761,808	\$ 484,024,612
Cost of revenues (including amortization of stock compensation expenses of \$ 729,994 and \$ 628,906 for the three months ended September 30, 2002 and 2003 and \$ 1,459,988 and \$ 1,257,812 for the six months ended September 30, 2002 and 2003)	97,292,593	140,742,637	183,297,362	273,645,026
Gross profit	84,154,346	110,026,339	154,464,446	210,379,586
Operating Expenses:				
Selling and marketing expenses	14,484,552	18,013,747	25,782,286	35,416,302
General and administrative expenses	13,102,320	20,437,144	24,961,448	38,161,371
Amortization of stock compensation expense	513,954	442,783	1,027,908	885,567
Amortization of intangible assets	615,904	3,322,455	820,025	4,071,573
Total operating expenses	28,716,730	42,216,129	52,591,667	78,534,813
Operating income	55,437,616	67,810,210	101,872,779	131,844,773
Other income, net	534,252	10,242,926	5,630,772	15,543,706
Income before income taxes	55,971,868	78,053,136	107,503,551	147,388,479
Provision for income taxes	9,271,397	13,339,383	17,958,780	24,404,180
Net income	\$ 46,700,471	\$ 64,713,753	\$ 89,544,771	\$ 122,984,299
Earnings per equity share				
Basic	\$ 0.71	\$ 0.99	\$ 1.36	\$ 1.87
Diluted	\$ 0.70	\$ 0.97	\$ 1.35	\$ 1.85
Weighted equity shares used in computing earnings per equity share				
Basic	65,567,135	65,591,028	65,567,033	65,587,368
Diluted	66,175,895	66,412,725	66,275,118	66,244,852

See accompanying notes to the unaudited consolidated financial statements

Infosys Technologies Limited and subsidiary

Unaudited consolidated statements of stockholders' equity and comprehensive income

	Common stock		Additional paid-in capital	Comprehensive income	Accumulated other comprehensive income	Deferred stock compensation	Retained earnings	Total stockholders' equity
	Shares	Par value						
Balance as of March 31, 2002	66,186,130	\$ 8,597,001	\$ 123,079,948		\$ (45,441,148)	\$ (7,620,600)	\$ 363,764,165	\$ 442,379,366
Common stock issued	19,050	1,961	646,906		-	-	-	648,867
Cash dividends declared	-	-	-		-	-	(16,956,889)	(16,956,889)
Income tax benefit arising on exercise of stock options	-	-	438,139		-	-	-	438,139
Amortization of compensation related to stock option grants	-	-	-		-	2,487,896	-	2,487,896
Comprehensive income								
Net income	-	-	-	89,544,771	-	-	89,544,771	89,544,771
Other comprehensive income								
Translation adjustment	-	-	-	5,473,659	5,473,659	-	-	5,473,659
Comprehensive income				\$ 95,018,430				
Balance as of September 30, 2002	66,205,180	\$ 8,598,962	\$ 124,164,993		\$ (39,967,489)	\$ (5,132,704)	\$ 436,352,047	\$ 524,015,809
Balance as of March 31, 2003	66,243,078	\$ 8,602,909	\$ 127,042,751		\$ (31,444,835)	\$(2,817,066)	\$ 524,621,160	\$ 626,004,919
Common stock issued	25,894	2,819	1,105,240		-	-	-	1,108,059
Cash dividends declared	-	-	-		-	-	(23,352,755)	(23,352,755)
Income tax benefit arising on exercise of stock options	-	-	670,016		-	-	-	670,016
Amortization of compensation related to stock option grants	-	-	-		-	2,143,379	-	2,143,379
Comprehensive income								
Net income	-	-	-	122,984,299	-	-	122,984,299	122,984,299
Other comprehensive income								
Translation adjustment	-	-	-	24,834,256	24,834,256	-	-	24,834,256
Comprehensive income				\$ 147,818,555				
Balance as of September 30, 2003	66,268,972	\$ 8,605,728	\$ 128,818,007		\$(6,610,579)	\$(673,687)	\$ 624,252,704	\$ 754,392,173

See accompanying notes to the unaudited consolidated financial statements

Infosys Technologies Limited and subsidiary

Unaudited consolidated statements of cash flows

	Six months ended September 30,	
	2002	2003
OPERATING ACTIVITIES:		
Net income	\$ 89,544,771	\$ 122,984,299
Adjustments to reconcile net income to net cash provided by operating activities		
Loss on sale of property, plant and equipment	24,787	2,153
Depreciation	17,386,573	19,365,934
Amortization of intangible assets	820,025	4,071,573
Provision for investments	3,163,560	1,419,662
Deferred taxes	(1,561,294)	907,313
Amortization of deferred stock compensation expense	2,487,896	2,143,379
Changes in assets and liabilities		
Trade accounts receivable	(25,241,313)	(15,922,435)
Prepaid expenses and other current assets	(2,819,465)	(5,535,317)
Unbilled revenue	(9,355,693)	1,736,340
Income taxes	(3,908,096)	10,456,367
Accounts payable	337,610	(204,409)
Client deposits	1,298,162	(288,926)
Unearned revenue	7,270,897	1,818,558
Other accrued liabilities	14,401,660	11,860,194
Net cash provided by operating activities	93,850,080	154,814,685
INVESTING ACTIVITIES:		
Expenditure on property, plant and equipment	(17,174,194)	(28,804,288)
Expenditure on intangible asset	(2,901,487)	-
Proceeds from sale of property, plant and equipment	36,366	47,375
Loans to employees	(3,796,946)	1,802,363
Investments in liquid mutual fund units	-	(97,960,961)
Purchase of other investments	-	(78,906)
Net cash used in investing activities	(23,836,261)	(124,994,417)
FINANCING ACTIVITIES:		
Proceeds from issuance of common stock	648,867	1,108,059
Proceeds from issuance of preferred stock by subsidiary	10,000,000	-
Payment of dividends	(16,641,276)	(21,514,587)
Net cash used in financing activities	(5,992,409)	(20,406,528)
Effect of exchange rate changes on cash	3,802,239	12,190,842
Net increase in cash and cash equivalents during the period	67,823,649	21,604,582
Cash and cash equivalents at the beginning of the period	210,485,940	354,362,918
Cash and cash equivalents at the end of the period	\$ 278,309,589	\$ 375,967,500
Supplementary information:		
Cash paid towards taxes	\$ 21,888,054	\$ 13,029,716
Non cash transaction (see Note 2.2)	\$ 5,000,000	-

See accompanying notes to the unaudited consolidated financial statements

Infosys Technologies Limited and subsidiary

Notes to the unaudited consolidated financial statements

1 Company overview and significant accounting policies

1.1 Company overview

Infosys Technologies Limited (“Infosys” or “the Company”) along with its majority owned and controlled subsidiary, Progeon Limited (“Progeon”) is a leading global information technology, or IT, services company. The Company provides end-to-end business solutions that leverage technology thus enabling its clients to enhance business performance. The Company provides solutions that span the entire software life cycle encompassing consulting, design, development, re-engineering, maintenance, systems integration and package evaluation and implementation. In addition, the Company offers software products for the banking industry and business process management services.

1.2 Basis of preparation of financial statements

The accompanying consolidated financial statements are prepared in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”). Inter-company balances and transactions are eliminated on consolidation. All amounts are stated in U.S. dollars, except as otherwise specified.

Interim information presented in the consolidated financial statements has been prepared by the management without audit and, in the opinion of management, includes all adjustments of a normal recurring nature that are necessary for the fair presentation of the financial position, results of operations and cash flows for the periods shown, and is in accordance with GAAP. These financial statements should be read in conjunction with the consolidated financial statements and related notes included in the company’s annual report on Form 20-F for the fiscal year ended March 31, 2003.

1.3 Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities on the date of the financial statements, and the reported amounts of revenues and expenses during the period. Examples of estimates include accounting for contract costs expected to be incurred to complete software development, allowance for uncollectible accounts receivable, future obligations under employee benefit plans, provisions for post-sales customer support and the useful lives of property, plant and equipment and intangible assets. Actual results could differ from those estimates.

1.4 Revenue recognition

The company derives revenues primarily from software development and related services, licensing of software products and from business process management services. Arrangements with customers for software development and related services are either on a fixed price, fixed timeframe or on a time and material basis.

Revenue on time-and-material contracts is recognized as the related services are performed. Revenue from the end of the last billing to the balance sheet date is recognized as unbilled revenues. Revenue from fixed-price, fixed-time frame contracts is recognized as per the percentage-of-completion method. Guidance has been drawn from paragraph 95 of Statement of Position (SOP) 97-2 to account for revenue from fixed price arrangements for software development and related services in conformity with SOP 81-1. The input (efforts expended) method has been used to measure progress towards completion as there is a direct relationship between input and productivity. Provisions for estimated losses, if any, on uncompleted contracts are recorded in the period in which such losses become probable based on the current contract estimates. Costs and earnings in excess of billings are classified as unbilled revenue while billings in excess of costs and earnings are classified as unearned revenue. Maintenance revenue is recognized ratably over the term of the underlying maintenance agreement.

The company provides its clients with a fixed-period warranty for corrections of errors and telephone support on all its fixed-price, fixed-time frame contracts. Costs associated with such support services are accrued at the time related revenues are recorded and included in cost of revenues. The company estimates such costs based on historical experience and estimates are reviewed on a periodic basis for any material changes in assumptions and likelihood of occurrence.

In accordance with SOP 97-2, Software Revenue Recognition, license fee revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred, the license fee is fixed and determinable, and the collection of the fee is probable. Arrangements to deliver our software products generally have three elements: license, implementation and Annual Technical Services (“ATS”). The company has applied the principles in SOP 97-2 to account for revenue from these multiple element arrangements. Vendor specific objective evidence of fair value (“VSOE”) has been established for ATS. VSOE is the price charged when the element is sold separately. When other services are provided in conjunction with the licensing arrangement, the revenue from such contracts are allocated to each component of the contract using the residual method, whereby revenue is deferred for the undelivered services and the residual amounts are recognized as revenue for delivered elements. In the absence of an established VSOE for implementation, the entire arrangement fee for license and implementation is recognised as the implementation is performed. Revenue from client training, support and other services arising due to the sale of software products is recognized as the services are performed. ATS revenue is recognised ratably over the period in which the services are rendered.

Revenues from business process management and other services are recognized on both, the time-and-material and fixed-price, fixed-time frame bases. Revenue on time-and-material contracts is recognized as the related services are rendered. Revenue from fixed-price, fixed-time frame contracts is recognized as per the proportional performance method using an output measure of performance.

When the company receives advances for services and products, such amounts are reported as client deposits until all conditions for revenue recognition are met.

1.5 Cash and cash equivalents

The company considers all highly liquid investments with a remaining maturity at the date of purchase / investment of three months or less to be cash equivalents. Cash and cash equivalents comprise cash, cash on deposit with banks, and deposits with corporations.

1.6 Property, plant and equipment

Property, plant and equipment are stated at cost, less accumulated depreciation. The company depreciates property, plant and equipment over their estimated useful lives using the straight-line method. The estimated useful lives of assets are as follows:

Buildings	15 years	Plant and equipment	5 years
Furniture and fixtures	5 years	Vehicles	5 years
Computer equipment	2-5 years		

The cost of software purchased for internal use is accounted under SOP 98-1, Accounting for the Costs of Computer Software Developed or Obtained for Internal Use. Deposits paid towards the acquisition of property, plant and equipment outstanding at each balance sheet date and the cost of property, plant and equipment not put to use before such date are disclosed under “*Capital work-in-progress*”.

1.7 Intangible assets

Intangible assets are amortized over their respective individual estimated useful lives on a straight-line basis, commencing from the date the asset is available to the company for its use. Management estimates the useful lives of acquired rights in software applications to range between one through two years.

1.8 Impairment of long-lived assets

The company evaluates the recoverability of its long-lived assets and certain identifiable intangibles, if any, whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying value of the assets exceeds the fair value of the assets. Assets to be disposed are reported at the lower of the carrying value or the fair value less the cost to sell.

1.9 Research and development

Research and development costs are expensed as incurred. Software product development costs are expensed as incurred until technological feasibility is achieved.

1.10 Foreign currency translation

The accompanying financial statements are reported in U.S. dollars. The functional currency of the company is the Indian rupee (“Rs.”). The translation of Rs. to U.S. dollars is performed for balance sheet accounts using the exchange rate in effect at the balance sheet date and for revenue and expense accounts using a monthly average exchange rate for the respective periods. The gains or losses resulting from such translation are reported as “*Other comprehensive income*”, a separate component of stockholders’ equity. The method for translating expenses of overseas operations depends upon the funds used. If the payment is made from a rupee denominated bank account, the exchange rate prevailing on the date of the payment would apply. If the payment is made from a foreign currency, i.e., non-rupee denominated account, the translation into rupees is performed at the average monthly exchange rate.

1.11 Earnings per share

In accordance with Statement of Financial Accounting Standards (“SFAS”) 128, *Earnings Per Share*, basic earnings per share are computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the period, using the treasury stock method for options and warrants, except where the result would be anti-dilutive. The dilutive effect of convertible securities is reflected in diluted earnings per share by application of the if-converted method.

1.12 Income taxes

Income taxes are accounted for using the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities, and their respective tax bases and operating loss carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of changes in tax rates on deferred tax assets and liabilities is recognized as income in the period that includes the enactment date. The measurement of deferred tax assets is reduced, if necessary, by a valuation allowance for any tax benefits of which future realization is uncertain. The income tax provision for the interim period is based on the best estimate of the effective tax rate expected to be applicable for the full fiscal year.

1.13 Fair value of financial instruments

The carrying amounts reflected in the balance sheets for cash, cash equivalents, accounts receivable and accounts payable approximate their respective fair values due to the short maturities of these instruments.

1.14 Concentration of risk

Financial instruments that potentially subject the company to concentrations of credit risk consist principally of cash equivalents, trade accounts receivable, investment securities and hedging instruments. By nature, all such financial instruments involve risk, including the credit risk of non-performance by counterparties. In management’s opinion, as of March 31, 2003 and September 30, 2003, there was no significant

risk of loss in the event of non-performance of the counterparties to these financial instruments, other than the amounts already provided for in the financial statements, if any. Exposure to credit risk is managed through credit approvals, establishing credit limits and monitoring procedures. The company's cash resources are invested with corporations, financial institutions and banks with high investment grade credit ratings. Limitations are established by the company as to the maximum amount of cash that may be invested with any such single entity.

1.15 Retirement benefits to employees

1.15.1 Gratuity

In accordance with the Payment of Gratuity Act, 1972, Infosys provides for gratuity, a defined benefit retirement plan (the "Gratuity Plan"), covering eligible employees. The Gratuity Plan provides a lump sum payment to vested employees at retirement, death, incapacitation or termination of employment, of an amount based on the respective employee's salary and the tenure of employment. Liabilities with regard to the Gratuity Plan are determined by actuarial valuation, based upon which, Infosys contributes to the Infosys Technologies Limited Employees' Gratuity Fund Trust (the "Trust"). Trustees administer contributions made to the Trust and invest in specific designated securities as mandated by law, which generally comprise central and state government bonds and debt instruments of government-owned corporations.

In accordance with the Payment of Gratuity Act, 1972, Progeon provides for gratuity, a defined benefit retirement plan covering eligible employees. The plan provides a lump sum payment to vested employees at retirement, death, incapacitation or termination of employment, of an amount based on the respective employee's salary and the tenure of employment. Liabilities with regard to the gratuity plan are determined by actuarial valuation.

1.15.2 Superannuation

Apart from being covered under the Gratuity Plan described above, certain employees of Infosys are also participants of a defined contribution plan. The company makes monthly contributions under the superannuation plan (the "Plan") to the Infosys Technologies Limited Employees Superannuation Fund Trust, based on a specified percentage of each covered employee's salary. Infosys has no further obligations to the Plan beyond its monthly contributions.

Certain employees of Progeon are also participants of a defined contribution plan. The company makes monthly provisions under the superannuation plan based on a specified percentage of each covered employee's salary. The company has no further obligations to the superannuation plan beyond its monthly provisions.

1.15.3 Provident fund

Eligible employees also receive benefits from a provident fund, which is a defined contribution plan. Both the employee and the company make monthly contributions to this provident fund plan equal to a specified percentage of the covered employee's salary. Infosys contributes a part of the contributions to the Infosys Technologies Limited Employees' Provident Fund Trust. The remainders of the contributions are made to the Government administered provident fund. There are no further obligations under the provident fund plan beyond its monthly contributions.

In respect of Progeon, eligible employees receive benefits from a provident fund, which is a defined contribution plan. Both the employee and the company make monthly contributions to this provident fund plan equal to a specified percentage of the covered employee's salary. Amounts collected under the provident fund plan are deposited in a Government administered provident fund. The company has no further obligations under the provident fund plan beyond its monthly contributions.

1.16 Investments

The company accounts by the equity method for investments between 20% and 50% or where it is otherwise able to exercise significant influence over the operating and financial policies of the investee. Non-readily marketable equity securities for which there are no readily determinable fair values are recorded at cost. Declines in value judged to be other than temporary are included in earnings. Realized gains and losses and unrealized holding gains and losses for trading securities are included in earnings. The cost of securities sold is based on the specific identification method. Interest and dividend income are recognized when earned.

1.17 Stock-based compensation

The company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board (“APB”) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations including FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation an interpretation of APB Opinion No. 25*, issued in March 2000, to account for its fixed stock option plans. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS 123, *Accounting for Stock-Based Compensation*, established accounting and disclosure requirements using a fair value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS 123, the Company has elected to continue to apply the intrinsic value-based method of accounting described above, and has adopted the disclosure requirements of SFAS 148, *Accounting for Stock-Based Compensation – Transition and Disclosure, an amendment of FASB Statement No. 123*. All stock options issued to date have been accounted as a fixed stock option plan.

The following table illustrates the effect on net income and earnings per share if the company had applied the fair value recognition provisions of SFAS Statement No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee compensation.

	Six months ended September 30,	
	2002	2003
Net income, as reported	\$ 89,544,771	\$ 122,984,299
Add: Stock-based employee compensation expense included in reported net income	2,487,896	2,143,379
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	27,864,077	29,093,503
Pro forma net income	\$ 64,168,590	\$ 96,034,175
Earnings per share:		
Basic – as reported	\$ 1.36	\$ 1.87
Basic – pro forma	\$ 0.98	\$ 1.46
Diluted – as reported	\$ 1.35	\$ 1.85
Diluted – pro forma	\$ 0.97	\$ 1.45

The fair value of each option is estimated on the date of grant using the Black-Scholes model with the following assumptions:

	Six months ended September 30,	
	2002	2003
Dividend yield %	0.2%	0.2%
Expected life	1-5 years	1-5 years
Risk free interest rate	6%	5.2-5.7%
Volatility	60-75%	60-75%

1.18 Dividends

Dividend on common stock are recorded as a liability on the date of declaration by the stockholders.

1.19 Derivative financial instruments

On April 1, 2001, the company adopted SFAS 133, *Accounting for Derivative Instruments and Hedging Activities* as amended, when the rules became effective for companies with fiscal years ending March 31. The company enters into forward foreign exchange contracts where the counter party is generally a bank. The company purchases forward foreign exchange contracts to mitigate the risk of changes in foreign exchange rates on accounts receivable and forecasted cash flows denominated in certain foreign currencies. Although these contracts are effective as hedges from an economic perspective, they do not qualify for hedge accounting under SFAS 133, as amended. Any derivative that is either not designated hedge, or is so designated but is ineffective per SFAS 133, is marked to market and recognized in earnings immediately.

1.20 Reclassifications

Certain reclassifications have been made to conform prior period data to the current presentations. These reclassifications had no effect on reported earnings.

2 Notes to the consolidated financial statements

2.1 Trade accounts receivable

Trade accounts receivable as of March 31, 2003 and September 30, 2003, net of allowance for doubtful accounts of \$3,010,568 and \$4,140,180 respectively, amounted to \$109,119,856 and \$ 129,442,231. The age profile of trade accounts receivable, net of allowances is given below.

Period (in days)	As of		In%
	March 31, 2003	September 30, 2003	
	0 – 30	65.8	
31 – 60	29.0	16.4	
61 – 90	3.9	7.5	
More than 90	1.3	5.2	
	<u>100.0</u>	<u>100.0</u>	

2.2 Intangible assets

During fiscal 2003, the company acquired the intellectual property rights of Trade IQ product from IQ Financial Systems Inc., USA for its banking business unit. The consideration paid amounted to US\$ 3.47 million. The consideration has been recorded as an intangible asset, which is being amortized over two years representing management's estimate of the useful life of the intellectual property.

During the six months ended September 30, 2002, the company entered into an agreement for transferring the intellectual property rights in a commercial software application product used in the design of high performance structural systems. The company will pay the committed consideration of US\$ 5 million within ten years of the contract date. The ownership of intellectual property in the product transfers to the company on remittance of the consideration. The committed consideration of US\$ 5 million is recorded as an intangible asset and was being amortized over management's estimate of the useful life, which was initially 5 years. In August 2003, management revised its estimates of the remaining useful life of the intangible asset to three months. The carrying amount of the intangible asset as is being amortized prospectively over the revised remaining useful life of 3 months from August 1, 2003. The additional amortization for the six months ended September 30, 2003 due to the revision in estimate of remaining useful life was \$ 2.6 million. The amount payable as consideration is disclosed as a non-current liability as of March 31, 2003 and September 30, 2003 and as a non-cash transaction in the consolidated statement of cash flows.

As of March 31, 2003 and September 30, 2003, intangible assets (net of accumulated amortization of \$ 2,360,799 and \$ 6,577,924) were \$ 6,471,236 and \$2,628,011.

2.3 Related parties

The company grants loans to employees for acquiring assets such as property and cars. Such loans are repayable over fixed periods ranging from 1 to 100 months. The annual rates of interest at which the loans have been made to employees vary between 0% through 4%. No loans have been made to employees in connection with equity issues. The loans are generally secured by the assets acquired by the employees.

The required repayments of loans by employees are as detailed below.

Year ending March/September	As of	
	March 31, 2003	September 30, 2003
2004	\$12,252,004	\$ 11,112,761
2005	4,298,780	4,474,097
2006	3,206,683	3,286,573
2007	2,416,202	2,510,530
2008	2,099,781	2,280,415
Thereafter	4,432,882	4,311,044
	<u>\$28,706,332</u>	<u>\$27,975,420</u>

The estimated fair values of related party receivables amounted to \$24,422,419 and \$ 23,637,104 as of March 31, 2003 and September 30, 2003 respectively. These amounts have been determined using available market information and appropriate valuation methodologies. Considerable judgment is required to develop these estimates of fair value. Consequently, these estimates are not necessarily indicative of the amounts that the company could realize in the market.

2.4 Share capital of Progeon

In April 2002, Progeon issued 12,250,000 equity shares of par value \$0.20 per share to its holding company, Infosys, in exchange for an aggregate consideration of \$2,500,000 ("First Tranche subscription"). In terms of the stock subscription agreement between Infosys, Citicorp International Finance Corporation ("CIFIC") and Progeon, Infosys is also required to subscribe to an additional 12,250,000 equity shares in Progeon during calendar year 2003.

On June 14, 2002, Progeon issued 4,375,000 0.0005% cumulative convertible preference shares to CIFIC at an issue price of \$2.28 (equivalent to Rs. 112) per share, in exchange for an aggregate consideration of \$10,000,000. Unless earlier converted, pursuant to an agreement between the company and CIFIC, these cumulative convertible preference shares shall automatically be converted into equity shares, (i) one year prior to the Initial Public Offering ("IPO") date or (ii) September 30, 2005 or (iii) at the holder's option, immediately upon the occurrence of any Liquidity Event; whichever is earlier. The term "Liquidity Event" includes any of a decision of the Board of Directors of the company to make an IPO, merger, reconstruction, capital reorganization or other event which, in the sole opinion of the holder of the convertible preference shares, amounts to an alteration in the capital structure of the company. Each preference share is convertible into one equity share, par value \$0.20 each. The dividend on the preference shares for the period ended September 30, 2003 is payable.

Each holder of these cumulative convertible preference shares is entitled to receive notice of, and to attend, any shareholders' meeting and shall be entitled to vote together with holders of equity shares on any matters that affect their rights as preference shareholders including any resolution for winding up the company or for the repayment or reduction of the company's share capital.

In the event of any liquidation, dissolution or winding up of the company, either voluntary or involuntary, each holder of the preference shares will be paid a dollar equivalent of Rs. 112 per preference share, as adjusted for stock dividends, combinations, splits, recapitalizations and the like, in preference to any distribution of any assets of the company to the holders of equity shares.

Upon the completion of the distribution described above, the remaining assets and funds of the company available for distribution to shareholders shall be distributed among all holders of preference shares and equity shares based on the number of equity shares held by each of them (assuming a full conversion of all the preference shares). CIFIC is also required to subscribe to an additional 4,375,000 cumulative convertible preference shares in Progeon during calendar year 2003.

2.5 Income taxes

The provision for income taxes comprises:

	Six months ended September 30,	
	2002	2003
Current taxes:		
Domestic taxes	\$ 8,413,825	\$ 6,553,958
Foreign taxes	11,106,249	16,942,909
	<u>19,520,074</u>	<u>23,496,867</u>
Deferred taxes:		
Domestic taxes	(918,227)	1,138,540
Foreign taxes	(643,067)	(231,227)
	<u>(1,561,294)</u>	<u>907,313</u>
Aggregate taxes	<u>\$ 17,958,780</u>	<u>\$ 24,404,180</u>

The tax effects of significant temporary differences that resulted in deferred tax assets and liabilities, and a description of the financial statement items that created these differences are as follows:

	As of	
	March 31, 2003	September 30, 2003
Deferred tax assets:		
Property, plant and equipment	\$4,719,124	\$ 5,034,949
Provision for doubtful debts	1,093,701	1,069,207
Investments	2,545,761	2,931,836
	<u>8,358,586</u>	<u>9,035,992</u>
<i>Less:</i> Valuation allowance	(614,004)	(1,637,567)
	<u>7,744,582</u>	<u>7,398,425</u>
Deferred tax liability on foreign exchange gains	(191,156)	(456,235)
Net deferred tax assets	<u>\$7,553,426</u>	<u>\$ 6,942,190</u>

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which the temporary differences become deductible. Management considers the scheduled reversal of the projected future taxable income, and tax planning strategies in making this assessment. Based on the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes that it is more likely than not the company will realize the benefits of those deductible differences, net of the existing valuation allowance at September 30, 2003. The valuation allowance relate to provision for doubtful debts and investments. The amount of the deferred tax assets

considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carry forward period are reduced.

All deferred tax expenses / (benefits) are allocated to the continuing operations of the company.

The provision for foreign taxes is due to income taxes payable overseas, principally in the United States of America. The company benefits from certain significant tax incentives provided to software firms under Indian tax laws. These incentives presently include: (i) an exemption from payment of Indian corporate income taxes for a period of ten consecutive years of operation of software development facilities designated as "Software Technology Parks" (the "STP Tax Holiday"); and (ii) a tax deduction for profits derived from exporting computer software (the "Export Deduction"). All but one of the company's software development facilities are located in designated Software Technology Parks ("STP"). The Government of India has recently amended the tax incentives available to companies set up in designated STPs. The period of the STP Tax Holiday available to such companies is restricted to ten consecutive years, beginning from the financial year when the unit started producing computer software or April 1, 1999, whichever is earlier. The Finance Act 2002 provided that the exempt income from an export oriented undertaking, for fiscal 2003 be restricted to 90% of its export income. However, this restriction is not applicable from fiscal 2004. Additionally, the Export Deduction is being phased out equally over a period of five years starting from fiscal 2000.

2.6 Earnings per share

The following is a reconciliation of the equity shares used in the computation of basic and diluted earnings per equity share:

	Six months ended September 30,	
	2002	2003
Basic earnings per equity share – weighted average number of common shares outstanding excluding Unallocated shares of ESOP	65,567,033	65,587,368
Effect of dilutive common equivalent shares – stock options outstanding	708,085	657,484
Diluted earnings per equity share – weighted average number of common shares and common equivalent shares outstanding	66,275,118	66,244,852

Options to purchase 823,285 shares under the 1998 Plan and 3,456,079 shares under the 1999 Plan were not considered for calculating diluted earnings per share for the six months ended September 30, 2003 as their effect was anti-dilutive.

2.7 Derivative financial instruments

The Company enters into forward foreign exchange contracts where the counter party is generally a bank. The Company considers the risks of non-performance by the counter party as non-material. Infosys held foreign exchange forward contracts of \$88,000,000 and \$ 150,250,000 as of March 31, 2003 and September 30, 2003, respectively. The foreign forward exchange contracts mature between one to six months.

2.8 Segment reporting

SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*, establishes standards for the way that public business enterprises report information about operating segments and related disclosures about products and services, geographic areas, and major customers. The company's operations predominantly relate to providing IT solutions, delivered to customers located globally, across various industry segments. The Chief Operating Decision Maker evaluates the company's performance and allocates resources based on an analysis of various performance indicators by industry classes and geographic segmentation of customers. Accordingly, revenues represented along industry classes comprise the principal basis of segmental information set out in these financial statements. Secondary segmental reporting is performed on the basis of the geographical location of customers. The accounting principles consistently used in the preparation of the financial statements are consistently applied to record revenue and expenditure in individual segments, and are as set out in the summary of significant accounting policies.

Industry segments for the company are primarily *financial services* comprising enterprises providing banking, finance and insurance services, *manufacturing* enterprises, enterprises in the *telecommunications* ("telecom") and *retail* industries, and *others* such as utilities, transportation and logistics companies.

Geographic segmentation is based on business sourced from that geographic region and delivered from both on-site and off-shore. *North America* comprises the United States of America, Canada and Mexico; *Europe* includes continental Europe (both the east and the west), Ireland and the United Kingdom; and the *Rest of the World* comprising all other places except those mentioned above and *India*.

Revenue in relation to segments is categorized based on items that are individually identifiable to that segment, while expenditure is categorized in relation to the associated turnover of the segment. Allocated expenses of the geographic segments include expenses incurred for rendering services from the company's offshore software development centres and on-site expenses. Certain expenses such as depreciation, which form a significant component of total expenses, are not specifically allocable to specific segments as the underlying services are used interchangeably. Management believes that it is not practical to provide segment disclosures relating to those costs and expenses, and accordingly these expenses are separately disclosed as "unallocated" and adjusted only against the total income of the company.

Fixed assets used in the company's business are not identified to any of the reportable segments, as these are used interchangeably between segments. Management believes that it is currently not practicable to provide segment disclosures relating to total assets and liabilities since a meaningful segregation of the available data is onerous.

Geographical information on revenue and industry revenue information is collated based on individual customers invoiced or in relation to which the revenue is otherwise recognized.

2.8.1 Industry segments

Six months ended September 30, 2002

	Financial services	Manufacturing	Telecom	Retail	Others	Total
Revenues	\$ 128,013,740	\$ 56,687,555	\$ 50,209,456	\$ 38,547,834	\$ 64,303,223	\$ 337,761,808
Identifiable operating expenses	52,959,562	23,698,477	17,139,646	12,309,458	23,868,523	129,975,666
Allocated expenses	33,917,196	13,942,755	12,351,052	9,482,195	15,869,311	85,562,509
Segmental operating income	\$ 41,136,982	\$ 19,046,323	\$ 20,718,758	\$ 16,756,181	\$ 24,565,389	122,223,633
Unallocable expenses						20,350,854
Operating income						101,872,779
Other income, net						5,630,772
Income before income taxes						107,503,551
Provision for income taxes						17,958,780
Net income						<u>\$ 89,544,771</u>

Six months ended September 30, 2003

	Financial services	Manufacturing	Telecom	Retail	Others	Total
Revenues	\$ 184,711,932	\$ 74,009,744	\$ 72,726,342	\$ 56,389,866	\$ 96,186,728	\$ 484,024,612
Identifiable operating expenses	77,786,449	31,798,523	28,917,492	20,830,320	39,434,015	198,766,799
Allocated expenses	49,788,676	19,012,833	19,831,339	14,489,772	24,709,533	127,832,153
Segmental operating income	\$ 57,136,807	\$ 23,198,388	\$ 23,977,511	\$ 21,069,774	\$ 32,043,180	157,425,660
Unallocable expenses						25,580,887
Operating income						131,844,773
Other income, net						15,543,706
Income before income taxes						147,388,479
Provision for income taxes						24,404,180
Net income						<u>\$ 122,984,299</u>

2.8.2 Geographic segments

Six months ended September 30, 2002

	North America	Europe	India	Rest of the World	Total
Revenues	\$ 246,881,743	\$ 60,017,683	\$ 7,488,804	\$ 23,373,578	\$ 337,761,808
Identifiable operating expenses	98,082,819	21,167,925	2,587,166	8,137,756	129,975,666
Allocated expenses	61,950,015	14,939,186	2,267,115	6,406,193	85,562,509
Segmental operating income	\$ 86,848,909	\$ 23,910,572	\$ 2,634,523	\$ 8,829,629	122,223,633
Unallocable expenses					20,350,854
Operating income					101,872,779
Other income, net					5,630,772
Income before income taxes					107,503,551
Provision for income taxes					17,958,780
Net income					\$ 89,544,771

Six months ended September 30, 2003

	North America	Europe	India	Rest of the World	Total
Revenues	\$ 359,534,575	\$ 85,744,877	\$ 9,046,654	\$ 29,698,506	\$ 484,024,612
Identifiable operating expenses	151,279,970	34,302,876	2,755,024	10,428,929	198,766,799
Allocated expenses	95,431,837	22,442,369	2,320,901	7,637,046	127,832,153
Segmental operating income	\$ 112,822,768	\$ 28,999,632	\$ 3,970,729	\$ 11,632,531	157,425,660
Unallocable expenses					25,580,887
Operating income					131,844,773
Other income, net					15,543,706
Income before income taxes					147,388,479
Provision for income taxes					24,404,180
Net income					\$ 122,984,299

2.9 Litigation

The company is subject to legal proceedings and claims, which have arisen, in the ordinary course of its business. Legal actions, when ultimately concluded and determined, will not, in the opinion of management, have a material effect on the results of operations or the financial position of the company.

Ms. Jennifer Griffith, a former employee, has filed a lawsuit against the company and its former director, Mr Phaneesh Murthy. The lawsuit has not yet been served on the company. Management is reviewing the allegations. Based on its present knowledge of facts, management estimates that the lawsuit will not have material impact on the result of operation or financial position of the company.