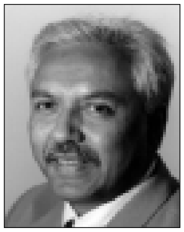
An Indian tech company worth keeping an eye on

By Sunil Vidyarthi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Someone (and I am sorry for not recalling his/her name) said that IBM has no chance of making it out of the current doldrums, as the next information-technology-services giant is located in India, not around here.

The credit goes to a number of rather world-class education institutions in India that are producing engineers, technologists and MBAs by hundreds of thousands. Some, of course, find their way to Europe and America, but the majority are employed by a handful of technology-services companies.

It is ironic that the leadership has shifted this way, as it was IBM that "taught" Indians and Indian companies the art of technology. No company examplifies this better than **Infosys Technologies Ltd.**, (INFY-NASDAQ, $52.79, 802-852-0261, *www.infosys.com*).

Founded in 1981, Infosys, together with its subsidiaries, engages in the design and delivery of information-technology-enabled business solutions. Unfortunately the technology guys are still enamored with arcane lexicon. I will try to make it simpler.

The company offers computer software products to businesses including the banking industry. Infosys, through its subsidiary, Progeon, provides offsite customer-relationship management or call centres, serving clients in financial services, manufacturing, telecommunications, retail, utilities, logistics and other industries in North America, Europe and the Asia-Pacific region.

Unfortunately I have avoided the likes of this company and, of course, missed a huge runup, simply because of an expectation that large technology companies like Intel, Microsoft and Cisco will bounce back and retake their eminence. I am not so sure anymore.

They did bounce back some, but the momentum of the shift in technology services to the likes of Infosys appears unstoppable. And the real reason for this fast growth has some to do with technology but a lot to do with cheap labor.

Here is a company that pays its executives the old-fashioned way — reasonably. The highest-paid exec makes $224,000 per year, not a billion dollars. Of course, many of them own tons of stock, making this one of the richest companies in India.

Another reason for Infosys's growth is its relatively small size; it is easier to double from a smaller base. INFY still has a revenue base of only $2 billion compared to $91 billion for IBM.

In the latest quarter ended March 31, Infosys's revenue increased by 45.5 per cent, adding 34 new clients. And it wasn't just the top-line story, it produced 67 per cent higher EPS numbers and increased margins at all levels. The liquidity position of the company continues strong, with $1.4 billion in cash and no debt.

But the stock is not cheap. Trading at 41 times its earnings per share, it is up there among the fast growers. The company claims it will grow at 30 per cent in the coming years, which will bring the P/E down to high 20s next year. All return numbers — like return on equity of 38 per cent, return on assets of 28 per cent — remind you of the software companies in the mid-'90s before silly season took the prices into the stratosphere. The big question is, is the current price a reasonable bet for us?

There are some problems surfacing in outsourcing. One is manpower. In spite of the thousands coming out of Indian schools, only a small percentage of them actually qualify to do Infosys's bidding.

The second is cost. The rupee has been strengthening, and wages are rising at a double-digit rate. In other words, is Infosys facing the same end as the bigger tech companies here? or is there still more to go?

First of all, the skills-requirement thing is a bit of catch-22. If you want great workers, you got to pay great salaries. What people forget is that outsourcing is being done at the lowest skill levels of the technology chain.

Naturally, there won't be too many Hot Mail developers coming from a B-grade School in Samastipur, but then, INFY doesn't do that high-level work. And as for wages, very good engineers from high-quality schools are making $5,000 per year. There are a lot of years at 15 per cent growth before you will come to western equivalency or even Chinese parity.

Am I buying the stock today then? No, but I am watching it for the next summer sell-off in India and China and further rhetoric about a weaker U.S. dollar. There is no hurry.

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