

Equity | India | Computer Services  
07 May 2009

# Not out of the woods, yet

## Maintain Underperform post Q4FY09

Post Q4 results and management discussions, we maintain our Underperform and modify estimates. Stock trades at 10x FY10 PE and over 16x FY10 PE, if one adjusts for imputed interest on FCCB. We will look for stability in Credit Card collections (~10% of revs) and healthcare (~40% of revs, mainly eligibility services & collections) and progress in FCCB buyback before we would consider re-evaluating our rating. Impact of Fidelity National Information Services buying shareholder and business partner, Metavante, an uncertainty. Our PO of Rs15 at ~10x FY11 adj. EPS, treating FCCB as debt.

## 4Q FY09 operations in line, adj. profits below BAS-MLe

Revenue 8% higher than BAS-MLe, led by Credit Card collections. Apart from seasonal strength, FSOL also benefited from some commission hikes & higher productivity of collectors. US healthcare services continued to see payment delays, as govt. focuses on improving efficiency of monies spent on healthcare programs. Likely pricing pressure from hospitals too. EBITDA margins 67bps below BAS-MLe. Adjusted for non-recurring gain on FCCB buy back and 1-time expenses, profits at Rs102m vs BAS-MLe at Rs224m due to higher interest cost & forex losses.

## Rev challenges persist

We believe while worst may be behind in the collections business, it is still early to assume any improvement in liquidation rates. Outlook in healthcare services still murky, with delayed payments as US govt. looks to step up efficiency of healthcare programs & some states cap enrollment services/trim svc coverage. Also see risk of pricing cuts from hospitals/other clients.

## Estimates (Mar)

(Rs)	2008A	2009A	2010E	2011E	2012
Net Income (Adjusted - mn)	1,508	778	859	1,044	NA
EPS	3.25	1.43	1.66	2.03	NA
EPS Change (YoY)	30.0%	-56.0%	16.1%	22.0%	NA
Dividend / Share	0	0	0	0	NA
Free Cash Flow / Share	2.45	2.68	2.92	3.45	NA

## Valuation (Mar)

	2008A	2009A	2010E	2011E	2012
P/E	5.20x	11.81x	10.18x	8.34x	NA
Dividend Yield	0%	0%	0%	0%	NA
EV / EBITDA*	2.69x	2.68x	2.45x	2.08x	NA
Free Cash Flow Yield*	14.43%	15.88%	17.25%	20.41%	NA

\* For full definitions of *iQmethod*<sup>SM</sup> measures, see page 10.

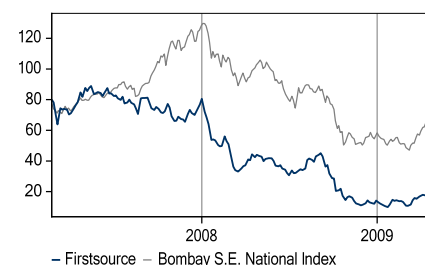


## RESEARCH

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## Stock Data

Price	Rs16.90
Price Objective	Rs15.00
Date Established	13-Apr-2009
Investment Opinion	C-3-9
Volatility Risk	HIGH
52-Week Range	Rs9.30-Rs50.80
Mrkt Val / Shares Out (mn)	US\$146 / 428.2
Average Daily Volume	9,598,343
ML Symbol / Exchange	FSSOF / BSE
Bloomberg / Reuters	FSOL IN / FISO.BO
ROE (2010E)	6.0%
Net Dbt to Eqty (Mar-2008A)	93.7%
Est. 5-Yr EPS / DPS Growth	15.0% / 0%
Free Float	31.8%



– Firstsource – Bombay S.E. National Index

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Refer to important disclosures on page 11 to 13. Analyst Certification on Page 9. Price Objective Basis/Risk on page 9.

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## iQprofile<sup>SM</sup> Firstsource Solutions Ltd.

Key Income Statement Data (Mar)	2008A	2009A	2010E	2011E	2012
<b>(Rs Millions)</b>					
Sales	12,988	17,494	18,547	20,680	NA
Gross Profit	2,309	2,311	2,534	2,976	NA
Sell General & Admin Expense	NA	NA	NA	NA	NA
Operating Profit	1,449	1,375	1,425	1,728	NA
Net Interest & Other Income	(17)	(868)	(309)	(293)	NA
Associates	NA	NA	NA	NA	NA
Pretax Income	1,432	507	1,116	1,436	NA
Tax (expense) / Benefit	(127)	(199)	(257)	(389)	NA
Net Income (Adjusted)	1,508	778	859	1,044	NA
Average Fully Diluted Shares Outstanding	464	544	517	515	NA

### Key Cash Flow Statement Data

Net Income	1,316	307	859	1,044	NA
Depreciation & Amortization	861	936	1,109	1,248	NA
Change in Working Capital	NA	NA	NA	NA	NA
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	85	887	30	115	NA
Cash Flow from Operations	2,261	2,129	1,998	2,407	NA
Capital Expenditure	(1,217)	(980)	(750)	(931)	NA
(Acquisition) / Disposal of Investments	(14,059)	0	0	0	NA
Other Cash Inflow / (Outflow)	1,131	0	0	0	NA
Cash Flow from Investing	(14,145)	(980)	(750)	(931)	NA
Shares Issue / (Repurchase)	(215)	0	0	0	NA
Cost of Dividends Paid	0	0	0	0	NA
Cash Flow from Financing	(1,428)	(131)	(223)	(223)	NA
Free Cash Flow	1,044	1,149	1,248	1,477	NA
Net Debt	11,527	12,979	11,954	10,698	NA
Change in Net Debt	12,418	(1,037)	(1,025)	(1,256)	NA

### Key Balance Sheet Data

Property, Plant & Equipment	2,226	2,261	1,902	1,584	NA
Other Non-Current Assets	19,065	23,016	23,016	23,016	NA
Trade Receivables	2,054	2,380	2,576	2,872	NA
Cash & Equivalents	1,025	967	1,491	2,747	NA
Other Current Assets	1,672	1,810	1,810	1,810	NA
Total Assets	26,041	30,434	30,795	32,030	NA
Long-Term Debt	12,552	13,946	13,446	13,446	NA
Other Non-Current Liabilities	0	0	0	0	NA
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	6,052	2,639	2,643	2,831	NA
Total Liabilities	18,604	16,585	16,088	16,277	NA
Total Equity	7,437	13,849	14,707	15,754	NA
Total Equity & Liabilities	26,041	30,434	30,796	32,030	NA

### iQmethod<sup>SM</sup> - Bus Performance\*

Return On Capital Employed	8.0%	3.5%	3.9%	4.4%	NA
Return On Equity	16.7%	7.3%	6.0%	6.9%	NA
Operating Margin	11.2%	7.9%	7.7%	8.4%	NA
EBITDA Margin	17.8%	13.2%	13.7%	14.4%	NA

### iQmethod<sup>SM</sup> - Quality of Earnings\*

Cash Realization Ratio	1.5x	2.7x	2.3x	2.3x	NA
Asset Replacement Ratio	1.4x	1.0x	0.7x	0.7x	NA
Tax Rate (Reported)	8.8%	39.3%	23.1%	27.1%	NA
Net Debt-to-Equity Ratio	155.0%	93.7%	81.3%	67.9%	NA
Interest Cover	6.7x	10.5x	6.4x	7.8x	NA

### Key Metrics

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 10.

### Company Description

Firstsource, an ICICI group company, is a leading India-centric Business Process Outsourcing vendor. Set up in Dec-01, it has complemented organic growth with inorganic initiatives. It offers transaction processing, collections management & customer acquisition/customer care services in Banking & Financial Services (abt 25% rev), Media & Telecom (abt 32% rev) & Healthcare (abt 40% rev) verticals. US is 60% rev and UK forms 25% of revs

### Investment Thesis

While worst may be behind, our Underperform is based on persisting risk to revenues and poor visibility in credit card collections business and banking vertical in the US, about 15p.c. of revs, as well as more recently, challenges in healthcare services, over 40p.c. of revs. We also find valuation rich, when we impute interest on the FCCB, and we would watch for progress in further buyback of the FCCB.

### Stock Data

Price to Book Value 0.5x

## Not out of the woods, yet

Post Q4 results and management discussions, we maintain our Underperform and modify estimates. Stock trades at 10x FY10 PE and over 16x FY10 PE, if one adjusts for imputed interest on FCCB. The FCCB is convertible at Rs93/share in Dec 2012, which looks difficult compared to the Rs16 price currently.

While the worst may be behind, we will look for sustained stability in Credit Card collections (~10% of revs). Also the demand outlook in healthcare (~40% of revs) is currently murky as the US govt. looks to tighten efficiency of the healthcare programs and hospitals try to cut costs, with likely bill rate implications too. Finally, we would watch the progress in FCCB buyback before we would consider re-evaluating our rating. The outcome of Fidelity National Information Services buying ~20% shareholder and business partner, Metavante, is an additional uncertainty. Metavante had entered into a 4-year agreement with FSOL in 2006 to use FSOL as offshore delivery partner for Metavante's North American Banking and Financial Services clients and also to work jointly with it to develop BPO offerings.

Our PO of Rs15 is at ~10x FY11 adj. EPS of Rs1.58, treating FCCB as debt.

Table 1: Adjusted EPS for imputed interest on FCCB

Assuming FCCB as ECB at 6.75%	FY09	FY10E	FY11E
PAT adding back FCCB option prem/MTM (Rs m)	892	969	1,166
Interest at 6.75% on FCCB amt (Rs m)	820	697	653
Effective tax rate	19.8%	21.0%	25.0%
Adj PAT (Rs m)	235	418	676
Share count, m	428	428	428
EPS (Rs)	0.55	0.98	1.58

Source: Banc of America Securities – Merrill Lynch Research

## 4Q FY09 Results Summary

**FSOL 4Q USD rev grew 7.1% qoq in constant currency terms** (adjusting for 8% depreciation in GBP/USD), 4.6% qoq in USD terms and 6.3% in Rupee terms. Rupee rev grew 29% yoy helped by Rupee depreciation.

**For the full year FY09, organic USD rev grew 10.6% in constant currency, ccy** (ex Med Assist), reported rev grew 25% in ccy and 17.6% in USD terms and 34.7% in Re terms.

**4QFY09 EBITDA margin was 67bps lower than BAS-MLe** due to margin pressures in healthcare. Not only are payments delayed in healthcare eligibility services & collections, pricing is also likely under pressure. Moreover, the company has invested in Selling and Marketing, which we believe should pay off over the next few quarters.

**Recurring PAT (ex 1-times) was lower than expected** due to higher interest cost, including likely some one-time ECB financing costs to buyback FCCB, lower treasury yields and higher forex losses on consolidation of subsidiaries.

One-times adjusted to arrive at our recurring PAT estimates are gain on FCCB buyback, tax-adjusted extraordinary expense on closure of certain centres including one in the US and write back of Rs236m loss on MTM on higher than expected non-designated forex covers, which we believe are unlikely to recur.

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**Reported PAT** ahead of estimates mainly due to gain on FCCB buyback.

**Company brought back USD50m face value of FCCB last quarter, spending approximately an estimated USD25m** and may do further buyback within the current window allowed by RBI until Dec 2009. USD225m of FCCB is outstanding as on Mar 31. They have funded buyback through long tenor ECB at under 10% interest.

**Employee attrition continued to be high in domestic business** (~12% of revs), post rapid ramp-up of a couple of large telecom svc provider wins in last couple of qtrs.

Table 2: Q4FY09 Summary

Rs mil	Q4FY09	Q3FY09	QoQ	Q4FY08	YoY	BAS-MLe	Variation
Revenue	4746	4473	6%	3692	29%	4384	8%
Other operating revenue (Grant/cashflow hedges)	-23	-31	-26%	64	-136%	0	n/m
<b>Operating Revenue</b>	<b>4723</b>	<b>4442</b>	<b>6%</b>	<b>3756</b>	<b>26%</b>	<b>4384</b>	<b>8%</b>
Personnel costs	2731	2683	2%	2115	29%	2543	7%
Operating costs	1386	1304	6%	1019	36%	1249	11%
<b>EBITDA</b>	<b>606</b>	<b>456</b>	<b>33%</b>	<b>623</b>	<b>-3%</b>	<b>592</b>	<b>2%</b>
Depreciation	246	255	-3%	227	8%	260	-5%
<b>EBIT</b>	<b>360</b>	<b>201</b>	<b>79%</b>	<b>396</b>	<b>-9%</b>	<b>332</b>	<b>8%</b>
Net interest expense	99	10	939%	17	484%	17	474%
Exchange (gain) on Foreign Currency loan	0	0	n/m	3	-100%	0	n/m
Forex MTM (gain)/ loss on FCCB	0	0	n/m	193	n/m	0	n/m
Amortised cost of fair value of FCCB	33	30	11%	0	n/m	30	n/m
Extraordinary expense	138	0	n/m	0	n/m	0	n/m
Gain on FCCB Buyback	635	0	n/m	0	n/m	0	n/m
Other income	-298	-11	n/m	36	n/m	10	-3151%
PBT	428	151	184%	219	95%	294	45%
Tax	19	33	-41%	13	50%	71	-73%
PAT before minority	409	118	247%	206	98%	223	83%
Minority	0	2	n/m	-4	-95%	-1	n/m
<b>Reported PAT</b>	<b>409</b>	<b>116</b>	<b>254%</b>	<b>210</b>	<b>94%</b>	<b>224</b>	<b>82%</b>
<b>Recurring PAT (ex FCCB MTM)</b>	<b>102</b>	<b>116</b>	<b>-12%</b>	<b>403</b>	<b>-75%</b>	<b>224</b>	<b>-54%</b>
							<b>Variation</b>
<b>Margins</b>	<b>Q4FY09</b>	<b>Q3FY09</b>	<b>QoQ (bps)</b>	<b>Q4FY08</b>	<b>YoY (bps)</b>	<b>BAS-MLe</b>	<b>(bps)</b>
EBITDA	12.8%	10.3%	257	16.6%	-374	13.5%	-67
EBIT	7.6%	4.5%	310	10.5%	-291	7.6%	5
Reported PAT	8.7%	2.6%	605	5.6%	306	5.1%	354
<b>Recurring PAT</b>	<b>2.2%</b>	<b>2.6%</b>	<b>-44</b>	<b>10.7%</b>	<b>-856</b>	<b>5.1%</b>	<b>-295</b>
Dep % to sales	5.2%	5.7%	-53	6.0%	-83	5.9%	-72

Source: Banc of America Securities – Merrill Lynch Research

## Organizational restructuring, sales investments

Effective March, Firstsource announced an **encouraging restructuring of the organization** into three vertical business units and one geography business unit viz banking, financial services & insurance, healthcare, telecom & media and Asia BU.

Each of these units would have integrated teams from selling to delivery, whereas earlier selling was more geography based and delivery somewhat more unified. This should help domain based selling, more efficient delivery and grow accountability.

Firstsource has also **expanded its sales persons in healthcare** and that should help grow pipeline by ability to win more hospitals and cross sell services.

**Table 3: Revenue by Geography**

	%revs	qoq	yoy
US	63.6%	5.7%	29.8%
UK	24.0%	0.5%	4.8%
India	11.9%	25.3%	57.5%
APAC	0.5%	6.3%	528.7%

Source: Banc of America Securities – Merrill Lynch Research

**Table 4: Revenue by Industry**

	%revs	qoq	yoy
BFSI	24.3%	11.4%	7.2%
Telecom and media	33.7%	10.9%	45.6%
Healthcare	39.8%	2.0%	26.7%
Others	2.2%	-22.0%	-4.6%

Source: Banc of America Securities – Merrill Lynch Research

**Table 5: Revenue by Location**

	%revs	qoq	yoy
Onsite	59.80%	7.22%	29.64%
Offshore	40.20%	5.02%	20.35%

Source: Banc of America Securities – Merrill Lynch Research

**Table 6: Client Concentration**

	Q4FY08	Q1FY09	Q2FY09	Q3FY09	Q4FY09
Top client	10.9%	9.9%	10.0%	10.5%	10.7%
Top 5 clients	31.2%	30.9%	32.2%	31.4%	31.7%

Source: Banc of America Securities – Merrill Lynch Research

**Table 7: Employee count decreased along with seat fill factor**

	Q4FY08	Q1FY09	Q2FY09	Q3FY09	Q4FY09
Employees	17369	18353	19576	22520	21570
Net addition	279	984	1223	2944	-950
Seats	14989	14968	15538	17715	18932
Seat fill factor	73.0%	76.0%	75.0%	74.0%	70.0%

Source: Banc of America Securities – Merrill Lynch Research

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## Financials

Table 8: P&L Statement

Profit and Loss statement (Rs 'mn)	FY06	FY07	FY08	FY09	FY10E	FY11E	2 yr g
Services Revenue	5,487.5	8,168.5	12,406.1	17,525.3	18,547.1	20,679.7	
<b>Operating Revenue</b>	<b>5487.5</b>	<b>8310.1</b>	<b>12987.9</b>	<b>17493.8</b>	<b>18547.1</b>	<b>20679.7</b>	<b>9%</b>
YoY	70.5%	51.4%	56.3%	34.7%	6.0%	11.5%	
Operating expense	1852.8	2518.2	3558.1	4971.6	5372.7	5893.7	
Personnel expenses	2830.1	4135.6	7120.4	10211.1	10640.4	11809.5	
Total expenditure	4682.9	6653.8	10678.5	15182.7	16013.0	17703.3	
<b>EBITDA</b>	<b>804.6</b>	<b>1656.3</b>	<b>2309.4</b>	<b>2311.1</b>	<b>2534.0</b>	<b>2976.5</b>	<b>13%</b>
D&A	449.7	641.5	860.8	935.9	1109.3	1248.0	
<b>EBIT</b>	<b>354.9</b>	<b>1014.8</b>	<b>1448.5</b>	<b>1375.2</b>	<b>1424.7</b>	<b>1728.5</b>	<b>12%</b>
YoY	81.1%	185.9%	42.7%	-5.1%	3.6%	21.3%	
Net interest expense	85.2	77.7	215.7	130.7	223.0	223.0	
Amortised cost of FCCB	0.0	0.0	0.0	113.9	109.9	121.9	
Gain on FCCB buy-back	0.0	0.0	0.0	635.0	0.0	0.0	
Extra-ordinary expense	0.0	0.0	0.0	138.2	0.0	0.0	
Other Income	0.0	72.0	349.2	-336.8	24.0	52.0	
<b>PBT</b>	<b>269.7</b>	<b>1026.3</b>	<b>1431.7</b>	<b>506.9</b>	<b>1115.8</b>	<b>1435.6</b>	
Taxes	27.0	60.1	126.5	199.1	257.4	389.4	
<b>PAT before minority interest</b>	<b>242.7</b>	<b>966.2</b>	<b>1305.2</b>	<b>307.8</b>	<b>858.4</b>	<b>1046.2</b>	
Minority Interest	-4.1	-6.3	-10.3	1.1	-0.8	2.0	
<b>PAT</b>	<b>246.8</b>	<b>972.5</b>	<b>1315.5</b>	<b>306.7</b>	<b>859.2</b>	<b>1044.2</b>	<b>85%</b>
<b>Recurring PAT</b>	<b>246.8</b>	<b>972.5</b>	<b>1315.5</b>	<b>0.3</b>	<b>859.2</b>	<b>1044.2</b>	<b>nm</b>
<b>Recurring PAT (excl'd FCCB MTM as well)</b>	<b>246.8</b>	<b>972.5</b>	<b>1508.0</b>	<b>778.5</b>	<b>859.2</b>	<b>1044.2</b>	<b>16%</b>
<b>PAT carried forward to Balance Sheet</b>	<b>246.8</b>	<b>972.5</b>	<b>1315.5</b>	<b>306.7</b>	<b>859.2</b>	<b>1044.2</b>	
EPS-basic (INR)	1.23	3.67	3.09	0.72	2.01	2.44	
<b>EPS-diluted (INR)</b>	<b>0.80</b>	<b>2.50</b>	<b>2.83</b>	<b>0.56</b>	<b>1.66</b>	<b>2.03</b>	<b>90%</b>
yoy	16%	214%	13%	-80%	195%	22%	
<b>Recurring EPS - ex FCCB MTM (INR)</b>	<b>0.80</b>	<b>2.50</b>	<b>3.25</b>	<b>1.43</b>	<b>1.66</b>	<b>2.03</b>	<b>19%</b>
yoy	16%	214%	30%	-56%	16%	22%	

Source: Banc of America Securities - Merrill Lynch Research estimates

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Table 9: Balance Sheet

31st Mar - Rs 'mn	FY06	FY07	FY08	FY09	FY10E	FY11E
<b>SOURCES OF FUNDS</b>						
<b>Shareholders' funds</b>						
Share capital (equity share cap+ preference share cap)	3,994.7	4,250.8	4,273.1	4,281.9	4,281.9	4,281.9
Reserve and surplus	327.5	6,414.7	3,127.3	9,512.4	10,371.6	11,415.8
<b>Total Shareholders' funds</b>	<b>4,324</b>	<b>10,666</b>	<b>7,400</b>	<b>13,794</b>	<b>14,653</b>	<b>15,698</b>
Minority interest	49.2	42.9	36.4	54.7	53.9	55.9
<b>Loan funds</b>						
Secured loans	731.1	712.0	596.6	1,855.6	1,855.6	1,855.6
Unsecured loans	569.1	1,263.9	11,955.2	12,090.0	11,590.0	11,590.0
<b>Total</b>	<b>5,674</b>	<b>12,685</b>	<b>19,989</b>	<b>27,795</b>	<b>28,153</b>	<b>29,199</b>
<b>APPLICATION OF FUNDS</b>						
Goodwill on consolidation	4,072.6	5,419.2	18,880.0	22,875.6	22,875.6	22,875.6
<b>Fixed assets</b>						
Gross block	2,575.8	3,891.3	5,340.4	6,348.2	7,098.2	8,028.8
Less: Accumulated depreciation	1,486.5	2,171.1	3,203.6	4,157.5	5,266.8	6,514.8
<b>Net block</b>	<b>1,089</b>	<b>1,720</b>	<b>2,137</b>	<b>2,191</b>	<b>1,831</b>	<b>1,514</b>
Add: Capital work in progress	64.3	82.0	89.2	70.2	70.2	70.2
<b>Total Fixed Assets</b>	<b>1,154</b>	<b>1,802</b>	<b>2,226</b>	<b>2,261</b>	<b>1,902</b>	<b>1,584</b>
Deferred tax asset	3.9	5.8	184.5	140.5	140.5	140.5
<b>Investments</b>						
Current assets, loans and advances		1,152.5	221.2	18.2	18.2	18.2
Sundry debtors	1,006.9	1,364.0	2,053.8	2,379.5	2,576.0	2,872.2
Unbilled revenues	156.8	722.6	400.2	605.0	605.0	605.0
Cash and bank balances	170.3	3,010.0	1,024.7	966.9	1,491.5	2,747.3
Loans and advances	300.5	583.6	1,050.6	1,187.1	1,187.1	1,187.1
<b>Total Current Assets</b>	<b>1,635</b>	<b>5,680</b>	<b>4,529</b>	<b>5,139</b>	<b>5,860</b>	<b>7,412</b>
Less: Current liabilities and provisions						
Current liabilities	1,149.8	1,255.6	1,433.0	2,167.8	2,320.6	2,495.7
Provisions	41.2	113.2	4,619.3	471.4	322.0	335.3
<b>Total Current liabilities and provisions</b>	<b>1,191</b>	<b>1,369</b>	<b>6,052</b>	<b>2,639</b>	<b>2,643</b>	<b>2,831</b>
<b>Net current assets</b>	<b>444</b>	<b>4,311</b>	<b>(1,523)</b>	<b>2,499</b>	<b>3,217</b>	<b>4,581</b>
<b>Total</b>	<b>5,674</b>	<b>12,691</b>	<b>19,989</b>	<b>27,795</b>	<b>28,153</b>	<b>29,199</b>

Source: Banc of America Securities - Merrill Lynch Research estimates

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Table 10: Cash Flow Statement

Rs Mil	FY06	FY07	FY08	FY09	FY10E	FY11E
<b>Cash Flow from Operating Activities</b>						
Net Income	247	972	1,316	307	859	1,044
Depreciation and amortisation	450	642	861	936	1,109	1,248
Changes in Operating assets and liabilities, net of effect of acquisition						
Accounts Receivables	(388)	(953)	115	(326)	(196)	(296)
Other current assets	22	893	(399)	(137)	-	-
Interest	80	64	181	131	223	223
Deferred Revenues	(157)	(566)	322	(205)	-	-
Other Current Liabilities	120	(49)	197	735	3	188
Others	(6)	(83)	(175)	732	-	-
<b>Total operating cash flow</b>	<b>369</b>	<b>914</b>	<b>2,261</b>	<b>2,129</b>	<b>1,998</b>	<b>2,407</b>
<b>Cash Flow from Investing Activities</b>						
Acquisition, net of Cash acquired	(73)	(1,837)	(14,059)	-	-	-
Capex	(594)	(1,154)	(1,217)	(980)	(750)	(931)
<b>Net Cash from Investing Activities</b>	<b>(653)</b>	<b>(4,046)</b>	<b>(14,145)</b>	<b>(980)</b>	<b>(750)</b>	<b>(931)</b>
<b>Free Cash Flow</b>	<b>(225)</b>	<b>(240)</b>	<b>1,044</b>	<b>1,149</b>	<b>1,248</b>	<b>1,477</b>
<b>Cash Flow from Financing Activities</b>						
Minority	-	-	-	18	(1)	2
Proceeds from notes payable, net of financing costs	-	923	11,327	(1,094)	(500)	-
Interest	(87)	(121)	(319)	(131)	(223)	(223)
<b>Net Cash from Financing Activities</b>	<b>183</b>	<b>5,972</b>	<b>9,898</b>	<b>(1,206)</b>	<b>(724)</b>	<b>(221)</b>
<b>Net change in cash and cash equivalents</b>	<b>(101)</b>	<b>2,840</b>	<b>(1,985)</b>	<b>(57)</b>	<b>525</b>	<b>1,256</b>
Cash and eq at the beginning of the year	269	170	3,010	1,025	967	1,491
<b>Cash and eq at the end of the year</b>	<b>169</b>	<b>3,010</b>	<b>1,025</b>	<b>967</b>	<b>1,491</b>	<b>2,747</b>

Source: Banc of America Securities – Merrill Lynch Research estimates

Table 11: Key Ratios

	FY06	FY07	FY08	FY09	FY10E	FY11E
<b>Margins</b>						
EBITDA	14.7%	19.9%	17.8%	13.2%	13.7%	14.4%
EBIT	6.5%	12.2%	11.2%	7.9%	7.7%	8.4%
PAT	4.5%	11.7%	11.6%	4.5%	4.6%	5.0%
<b>Per Share Data</b>						
Basic Reported EPS (INR)	1.2	3.7	3.1	0.7	2.0	2.4
Recurring Diluted EPS (INR) - ex FCCB	0.8	2.5	3.2	1.4	1.7	2.0
Recurring CEPS (INR)	2.2	4.1	5.1	3.2	3.8	4.4
Dividend Payout %	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Dividend Per Share (INR)	-	-	-	-	-	-
Book-value (INR)	13.9	27.4	15.9	25.4	28.3	30.5
<b>Growth Ratios</b>						
Revenue	n/a	51.4%	56.3%	34.7%	6.0%	11.5%
EBITDA	n/a	105.9%	39.4%	0.1%	9.6%	17.5%
EBIT	n/a	185.9%	42.7%	-5.1%	3.6%	21.3%
PAT	n/a	294.0%	55.1%	-48.4%	10.4%	21.5%
Basic EPS (INR)	n/a	199.0%	-15.9%	-76.8%	180.1%	21.5%
Diluted EPS (INR)	n/a	213.9%	30.0%	-56.0%	16.1%	22.0%
<b>Return Ratios</b>						
RONW (recurring ex FCCB MTM basis)	5.9%	13.0%	16.7%	7.3%	6.0%	6.9%
RONW ex cash	5.9%	16.3%	21.7%	7.6%	6.2%	7.2%
ROCE	7.4%	13.3%	11.7%	6.0%	4.6%	5.2%
ROCE ex cash	7.5%	15.9%	13.1%	6.0%	4.7%	5.4%

Source: Banc of America Securities – Merrill Lynch Research estimates



## Price objective basis & risk

### Firstsource (FSSOF)

Our PO of Rs15 is based on 10x FY11 adj. PE, adjusted to incorporate imputed interest on FCCB, in line with peers, WNS & EXL. This implies 7x reported FY11 PE. Key risks include delayed recovery in credit card collections and healthcare services. The outcome of Fidelity National Information Services buying 20% shareholder and business partner, Metavante, is an additional uncertainty. Expiry of income tax holiday in Mar. 2010, growing competition from integrated IT and BPO players and currency volatility are key industry-wide risks. Key upside risk: Faster than expected macro recovery in US.

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India - Software & IT Services Coverage Cluster

Investment rating	Company	ML ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	Educomp Solu	EUSOF	EDSL IN	Pratish Krishnan
	Mphasis Ltd	MPSSF	MPHL IN	Pratish Krishnan
	Patni	PATIF	PATNI IN	Mitali Ghosh
	Patni Computer	PTI	PTI US	Mitali Ghosh
	Tata Consultancy	TACSF	TCS IN	Mitali Ghosh
	Tech Mahindra	TMHAF	TECHM IN	Pratish Krishnan
	WNS (Holdings) L	WNS	WNS US	Mitali Ghosh
<b>NEUTRAL</b>				
	Genpact Ltd	G	G US	Mitali Ghosh
	Infosys Tech	INFYF	INFO IN	Mitali Ghosh
	Infosys Tech - A	INFY	INFY US	Mitali Ghosh
<b>UNDERPERFORM</b>				
	ExlService Holdi	EXLS	EXLS US	Mitali Ghosh
	Firstsource	FSSOF	FSOL IN	Mitali Ghosh
	HCL	XHCLF	HCLT IN	Mitali Ghosh
	Hexaware Tech	XFTCF	HEXW IN	Pratish Krishnan
	Infotech Enterprises Ltd	IFKFF	INFTC IN	Pratish Krishnan
	Mastek	MSKDF	MAST IN	Pratish Krishnan
	Rollta India	RLTAF	RLTA IN	Pratish Krishnan
	Rollta India-GDR	XLROF	RTI LI	Pratish Krishnan
	Wipro	WIPRF	WPRO IN	Mitali Ghosh
	Wipro	WIT	WIT US	Mitali Ghosh
<b>RVW</b>				
	Aptech Limited	XZUYF	APTR IN	Pratish Krishnan

*iQmethod*<sup>SM</sup> Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	$\text{Total Assets} - \text{Current Liabilities} + \text{ST Debt} + \text{Accumulated Goodwill Amortization}$
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
<b>Quality of Earnings</b>		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
<b>Valuation Toolkit</b>		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

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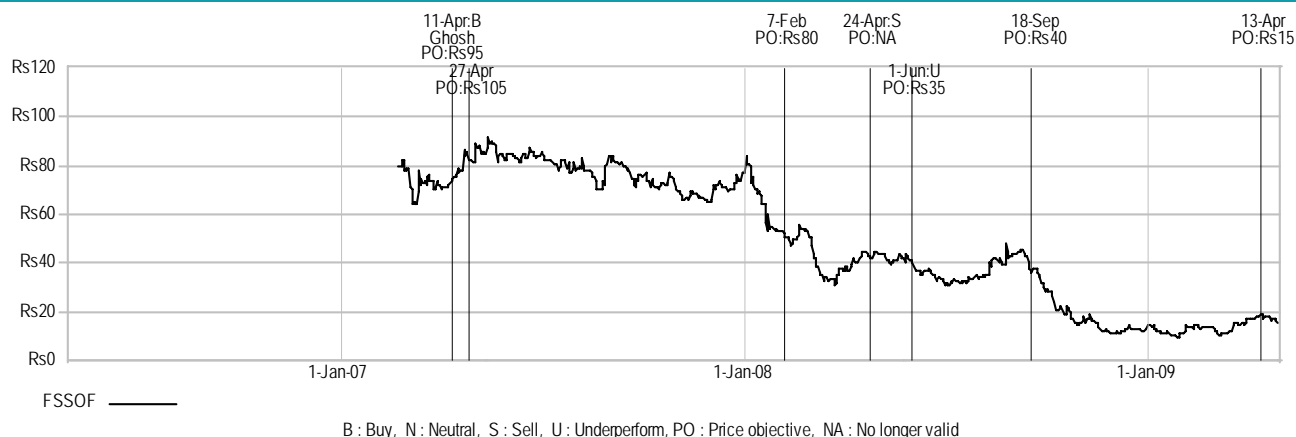
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### FSSOF Price Chart



\*Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of April 30, 2009 or such later date as indicated. BAS-ML price charts do not reflect analysts' coverage of the stock at prior firms. Historical price charts relating to companies covered as of April 30, 2009 by former Banc of America Securities LLC (BAS) analysts are available to BAS clients on the BAS website."

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Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	83	40.10%	Buy	32	43.24%
Neutral	46	22.22%	Neutral	23	58.97%
Sell	78	37.68%	Sell	27	36.99%

### Investment Rating Distribution: Global Group (as of 01 Apr 2009)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1243	38.21%	Buy	520	46.39%
Neutral	841	25.85%	Neutral	349	47.04%
Sell	1169	35.94%	Sell	388	36.30%

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster*
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

\* Ratings dispersions may vary from time to time where BAS-ML Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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