India

From Emerging Country to High Growth IT Engine

August 2007

Avendus

goetzpartners

Foreword

Dear Executives,

It's no secret that India is firmly established as one of the globe's most attractive economies. The world's second-most populous country has undergone a dramatic transformation over the past decade, moving from its role as a supplier of cheap labour for foreign companies to a robust player with its own vibrant economy.

With annual average GDP growth over the last years of around 7 percent and a highly-skilled workforce, India has emerged as a hub for high growth businesses such as IT services, business processing, pharmaceuticals and the automotive industries. It will continue to provide compelling offshoring opportunities for European enterprises that know how to correctly identify them. In particular, the areas of IT-related services, pharmaceuticals, healthcare, media, automotive, real estate and technology transfer will show growth.

As a result, India is a very interesting market for Europe. With predictions that it could be the world's richest economy by 2020, and more than 544 million Indians expected to join the consuming middle class (annual household income exceeding 3,000 US$), we believe the business opportunities for Europe to increase.

Beyond that, large Indian players, newly-confident and flush with cash, are now looking to Europe to further their own growth ambitions. Large IT services players, for example, are in a good position to achieve market leadership via large acquisitions, while buying up small-and-medium sized players will help them penetrate niche markets. But these efforts require a deeper understanding on the part of Indian companies on how to approach Europe's fragmented landscape, with its wide range of languages and cultures.

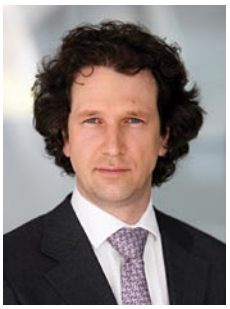
In conjunction with its partner, the leading Indian investment bank Avendus, goetzpartners is in a unique position to help companies make the most of these opportunities. Providing corporate finance and M&A advisory services, as well as management consultancy, goetzpartners works with companies both to conclude successful financial transactions and to develop and implement long-term and sustainable growth strategies.

We anticipate a host of new challenges arising from these joint Indian and European activities and are looking forward to sharing our experiences with you.

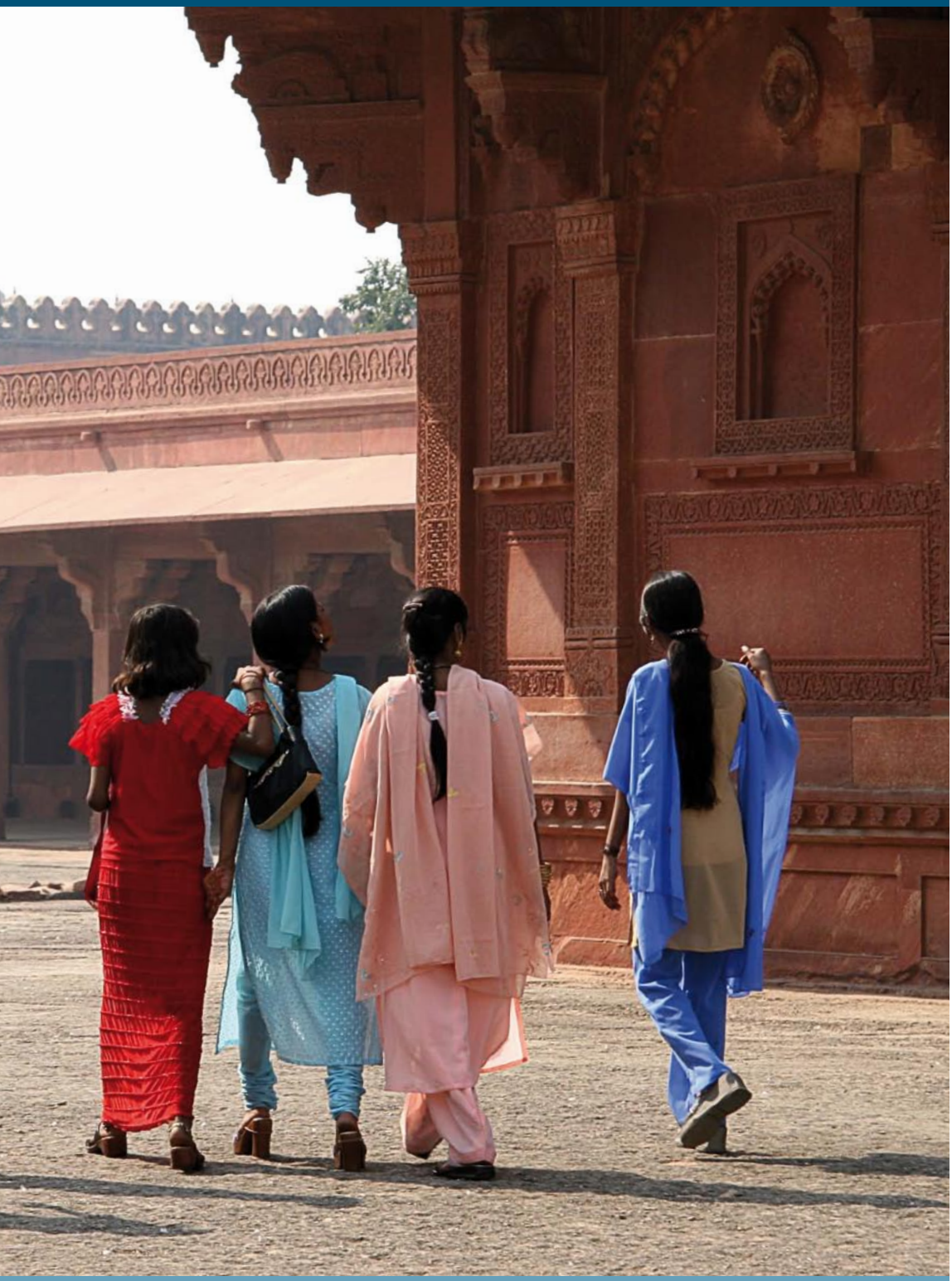
Sincerely yours

Dr. Stephan Goetz
Managing Director

Frank Ewerdwalbesloh
Managing Director



Armin Raffalski
Partner



Content

Management Summary

India's economy is booming, driven by its status as one of the world's top locations for offshoring. Given the high speed and dynamics India showed in the last years, and their successful development of the economy, India's appetite for acquisitions and joint ventures in Europe has increased.

- The Indian economy grew by around 7 percent per year over the past decade. In 2006, growth totaled 9.2 percent and economists expect continued vigorous growth.

- India's IT Services and BPO offshoring market is one of the world's fastest growing, generating US$36 billion in exports annually and growing at a rate of 40 percent per year. Other high growth businesses include pharmaceuticals and automotive exports.

- Foreign direct investment has increased considerably, with some US$11 billion flowing into the country in 2006, up from only US$2.6 billion in 1999. With about US$1.7 billion direct investments from August 1991 to April 2007, Germany is the 3rd largest European investor in India. Compared to other countries, the amount seems still low. However, as investments in India prove to be successful if business rules and mentalities of both India and its partner are considered it is highly likely that Germany will increase its activities in this market.

- India attracts foreign companies looking to cut costs and locate skills not found domestically. Fierce competition from Asia and high labor costs drive European companies to increase Indian offshoring. Europe will see compound annual growth rates of offshoring of 60 percent through 2009.

- Foreign retailers see opportunities in selling to India's burgeoning middle class, which is expected to surge to 544 million people in 2015, up from 3 million today.

- European markets are an interesting growth opportunity for Indian companies looking to expand outside their own borders. After years of recession in the early part of the decade, Europe's diverse economies have recovered somewhat, with expected average GDP growth of 2.9 percent.

- The European IT services market is expected to grow faster than the US IT services market over the next three years. The Western European IT services market totals US$217 billion and should grow by 5.8 percent annually by 2010, to a total market size of US$287 billion.

- The UK, Germany, France and Spain are the four most important markets for Indian IT services companies. With a size of US$66 billion in 2005, the UK is the largest and most interesting market due to infrastructure, language and cultural ties. But future growth is expected to come from Continental Europe, and the approach used in the UK cannot simply be applied to Europe's other distinct markets.

- Significant consolidation within European IT services has led to the emergence of large European companies with a pan-European presence, such as Capgemini and LogicaCMG. M&A activity is expected to continue, but Indian vendors have yet to participate in this wave of consolidation.

- Indian IT services firms are increasingly turning to Europe for growth, which will drive them to acquire or partner with European companies, especially in Continental Europe. This trend is expected to continue as Indian vendors seek to move up the value chain.

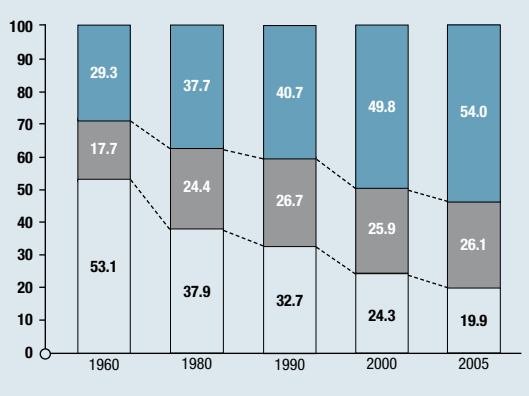
- Formulations and contract research will witness the maximum activity in terms of transactions in the India-Europe corridor. Product portfolio and marketing network will be the key attraction for deals in the generics space, whereas customer relationships and niche capabilities will be the drivers for transactions in contract research.

- Both Indian and European companies face challenges in carrying out cross-border transactions. European companies must overcome domestic resistance to outsourcing, while Indian vendors must grasp that Europe is not one market.

Cross-border activities between India and Europe are interesting for both countries. However, to be sure to transform them into successful results, it is key to recognize the challenges and rules of the European and Indian markets. Therefore, the cooperation with a reliable partner is highly recommended.

India – High Growth Powerhouse for IT Services

Figure 1: India's economic transformation



(Central Statistical Organisation (CSO), Government of India, IMA India)

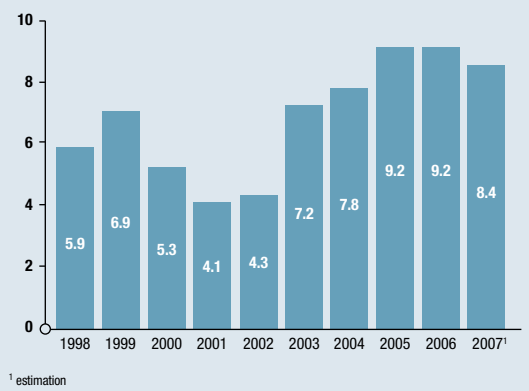
India is booming. Not a week goes by without an announcement that yet another multinational company plans to outsource parts of its business to India, or, in turn, that large Indian vendors are buying up competitors at home and abroad. In this section we take a look at the fundamental reasons for India's success, and what factors are drawing European companies to locate to India.

India's Growth Economy

India has transformed itself over the past 15 years from an agricultural-based, third world economy to one with vibrant growth rates, making it highly attractive to foreign investors.

Spurred initially by government reforms, the Indian economy has grown by around 7 percent annually over the last few years. In 2006, GDP growth totalled 9.2 percent, and economists expect that the country will continue to grow vigorously over the next decade, based on the strengths of its powerful services economy. While India has significantly expanded its manufacturing base, current economic growth rests mainly on services, which account for more than half of the country's output.

Figure 2: GDP in India in % (1998 – 2007)



(bfai, May 2007)

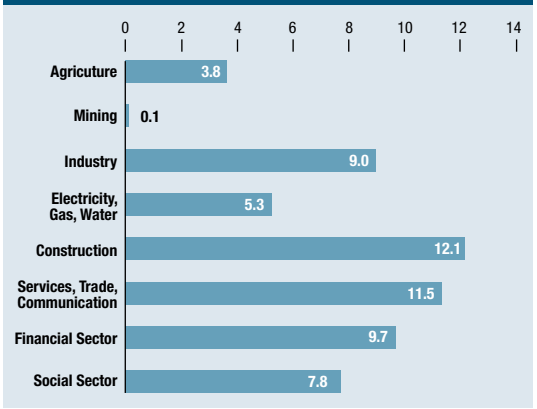
The country's well-educated, English-speaking workforce has helped transform India into the world's top location for offshored IT services. Very straightforward and open-minded in it's way of doing business, it is a major exporter of software services and workers, and India's offshoring market is one of the world's fastest growing, generating some US$36 billion in exports annually, and growing at 40 percent per year. By 2010, India's BPO business is expected to generate US$60 billion in revenues.

Besides becoming one of the top global hubs for business process outsourcing, India has also attracted a number of other high growth businesses to its shores. For example, the country is the fourth-largest producer of pharmaceuticals, with an export volume of some US$3 billion. It also exports US$4 billion in automobiles and automotive components, and, driven by domestic consumption, is the world's second largest car market and the largest motorcycle market.

But the economy is not just geared to serving export markets. With economic growth has come booming domestic consumption, which in turn is driving industries such as retail, media and entertainment, telecommunications and real estate.

The picture has also greatly improved for foreign direct investment (FDI) in India. The FDI Confidence Index ranked India the second most attractive location after China in 2006. India traditionally has received much less foreign investment than other developing countries, as it only recently began liberalizing regulations to attract investment. In 1991, the government overhauled the country's industrial policy to reduce export barriers and reform the country's monetary, fiscal and regulatory policies. Over the past seven years, the rate of FDI has more than quadrupled, with some US$11 billion flowing into the country in 2006, up from only US$2.6 billion in 1999. In conjunction, foreign institutional investment increased to a record US$9.5 billion in 2005. In addition, foreign exchange reserves have increased to approximately US$131 billion in the same year. Compared to other countries, these figures may seem still low. However, due to easier industrial regulations and the attractiveness of the Indian economy, investments may increase considerably.

Figure 3: Economic growth by sector in % (2005/06)

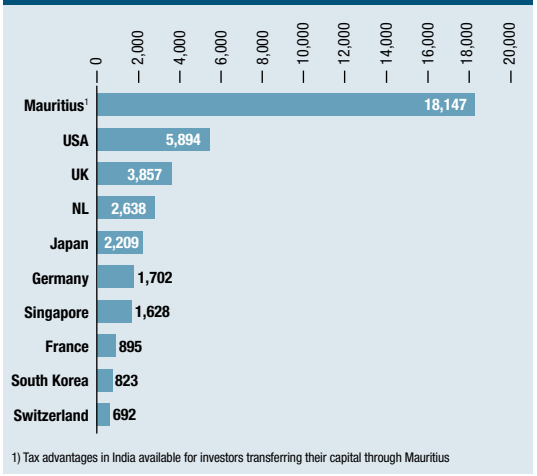


(bfai, Wirtschaftsdaten kompakt, Nov. 2006)

Despite the substantial progress India has made, the environment is still challenging, and the boom has not transformed all of the Indian economy: about 3/5 of the country's total work force is still engaged in agriculture, and 25 percent of India's more than one billion inhabitants live below the poverty line.

Also, the country's physical infrastructure of poorly-maintained roads and railway networks, as well as an enormous lack of electricity leaves room for improvement. But the government has committed to investing some US$350 billion over the next five years in roads, railways and electricity. On the other hand, India has done a good job of putting in place digital networks in large centres such as Bangalore. It can take advantage of excellent data communication links, and Internet access is common in large cities.

Figure 4: FDI in US$ million (August 1991 to March 2007)



(www.ibef.org)

Summary

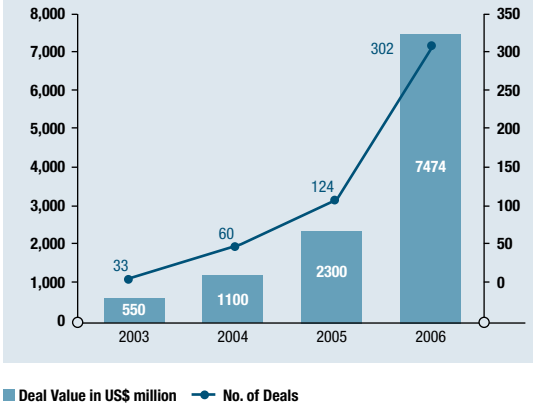
Over the last 15 years, India has developed from an agricultural-based, third world economy to one with enormous growth rates. The country's well-educated, English-speaking workforce has helped transform India into one of the world's fastest growing market for offshored IT services. Another reason for the increasing attractiveness of India as an economic partner for foreign investors are the governmental reforms decreasing the hurdles to enter this market. The growing economy also leads to a booming domestic consumption driving industries like media and telecommunications. However, the poor physical infrastructure and lack of electricity leave room for improvement.

Hotbed for Cross-Border Deals

The interest of foreign investors in the Indian market can also be clearly seen in the rising number of cross-border activities taking place, from joint ventures to private equity investments and strategic mergers and acquisitions.

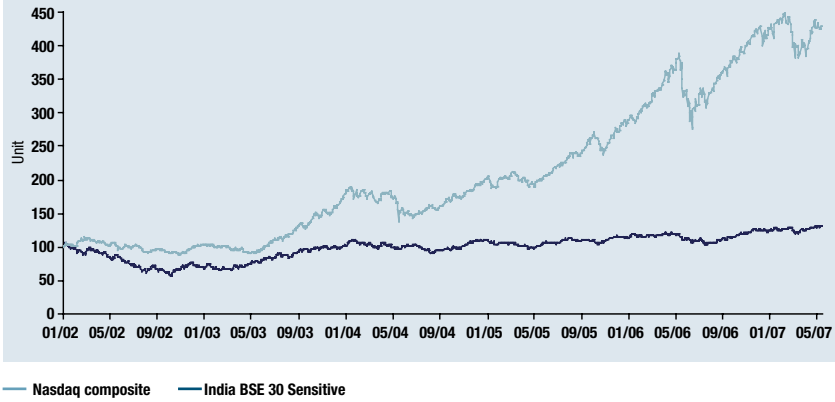
North American private equity houses have shown a marked interest in Indian targets over the past few years. New private equity deals, mainly buyouts and later-stage transactions, rose from 33 deals valued at US$550 million in 2003 to 302 transactions totaling US$7.5 billion in value in 2006. In the IT sector, for example, US buyout giant Kohlberg, Kravis & Roberts (KKR) invested US$900 million in Flextronics Software Systems and General Atlantic Partners invested US$66.6 million in Hexaware Technologies. In the life sciences arena, the Blackstone Group put US$50 million into Emcure Pharmaceuticals and Actis and Sequoia Capital India made a joint US$52 million investment in Paras Pharmaceutical.

Figure 5: India Private Equity investments



(Grant Thornton, India)

Figure 6: Development of BSE and NASDAQ



(Thomson, 16.5.2007)

Mergers and acquisitions are also on the rise, growing 58 percent since 2003, with a focus on IT and IT-enabled services (ITES), real estate, telecommunications, energy and life sciences. A majority of these deals have been cross-border transactions; out of 480 deals with a value of US$20 billion last year, 75 percent were cross-border deals. Most of these transactions were Indian companies looking outward, a trend that is expected to continue as these companies look to Europe and the US to attain a global footprint.

In conjunction with the economic boom, India's capital markets have soared 260 percent in value since 2002. The Bombay Stock Exchange has grown ten times faster than that of the NASDAQ. Last year the markets saw IPOs by 70 private-equity backed companies with a total market capitalization of US$5.5 billion. Corporate governance rules have been harmonized to model themselves on US GAAP, making it easier for foreign investors to assess the value of these companies.

Summary

India is a very attractive market for foreign investors which can be seen in the increasing number of cross-border private equity and M&A activities. Due to the harmonization of corporate governance rules with US standards, foreign investors can more easily assess the values of Indian companies.

India's Attractiveness for Europe

Besides investing in India, foreign companies increasingly view offshoring more and more as a means not only to dramatically cut costs but also to locate skills not available on-site. In addition, India's highly-skilled population is a young one, which means more individuals are flexible, optimistic and ready to take risks, making its work force attractive. About half the population is under 25 years old.

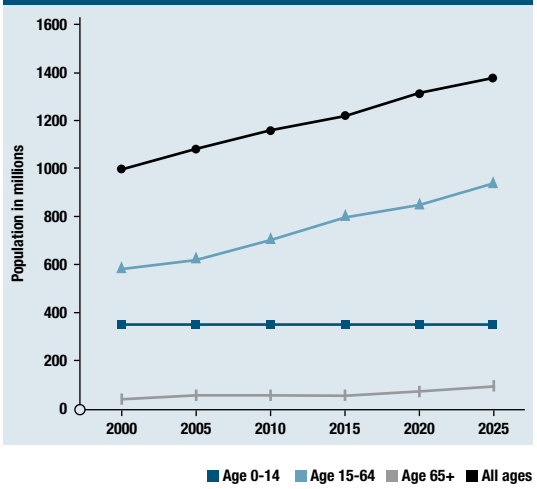
Companies are also continuing to expand non-core business process outsourcing to India. Besides IT services and call centers, that increasingly includes functions such as purchasing, billing, cash management, payroll and even human resources. Multinationals including Citigroup, GE Capital, Dell, Sun Microsystems, American Express, British Airways, Ford, and IBM all have extensive offshore operations in India.

Fierce competition from Asia and high labor costs continue to drive European companies in particular to increase their Indian offshoring activities. According to industry experts, Europe will see compound annual growth rates in offshoring of 60 percent through 2009, compared to only 35 percent in North America for IT Services.

Foreign retailers also see opportunities in selling to India's burgeoning middle class (annual household income exceeding US$3,000), thirsty for new products. Currently around 3 million people, it is expected to grow to around 544 million by 2020. Total consumption is up, generating an estimated US$550 billion in revenues in 2006, up from US$300 - 340 billion in 2002. Over the past decade, a market for luxury products has also emerged at an estimated value of US$444 million. The look ahead to the future is also bright: whereas today about 1.6 million people earn more than US$100,000 a year; the number is expected to grow to 3 million by 2010.

With increasing affluence has come a rapidly growing consumer financial services market in which foreign companies also hope to partake. Uptake of credit cards, for example, is soaring by 80 percent annually. India also has one of the world's fastest growing consumer mobile market, with six million new contracts concluded monthly. More than 70 million households are now wired to receive cable and satellite channels and overall media and entertainment is expected to generate revenues of US$850 billion by 2010.

Figure 7: Population structure in India



(Indian Demographic Scenario, 2025, P.N. Mari Bhat, Population Research Centre, Institute of Economic Growth, Delhi)

Summary

For Europe, India is a very attractive market for cost reasons as well as for locating skills not available on-site. Very young and flexible population makes India's workforce attractive. High domestic labor costs and strong competition from Asia are driving European companies to increase their offshoring activities. In addition, booming consumption in India makes the country a sought-after partner for European retailers and consumer financial services companies.

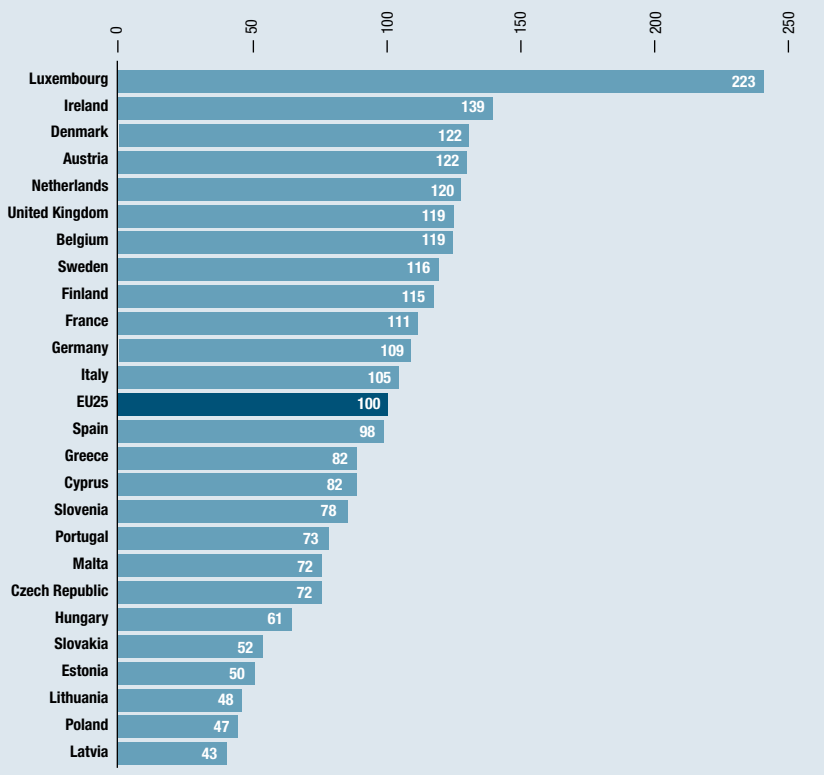
The European Markets

European markets represent an interesting growth opportunity for Indian companies looking to expand outside their own borders. After years of recession in the early part of the decade, Europe's diverse economies have recovered somewhat, with expected continued GDP growth on average of 2.9 percent in 2007.

Economic growth in the markets is driven by various factors. In the UK, for example, financial services, insurance and banking are strong drivers of growth. In Germany, long a sleeping giant, high-quality Mittelstand companies are helping boost the economy, while large German multinationals see growth abroad. Southern Europe's economies still tend to lag those of their Northern neighbors.

The enlargement of the European Union by 10 additional central and eastern European countries, with lower-cost labor forces and relatively high GDP growth, has also brought new economic impulses to Europe.

Figure 8: GDP per capita in PPS in the EU (2004)



(www.eurostat.com)

IT Services in Europe

Europe's improving economic environment is expected to have a positive impact on the demand for IT services, a market which was hard hit in the years 2000 - 2003. The need to catch-up now leads to a very optimistic outlook for Europe, the second largest IT market globally after the US, which is expected to grow faster than the US IT services market over the next three years. The Western European IT services market totals US$217 billion in size and is expected to show 5.8 percent compound annual growth rates through 2010, growing to a total market size of US$287 billion.

For Indian companies, the most attractive markets are the UK, Germany, France, Spain, and Italy.

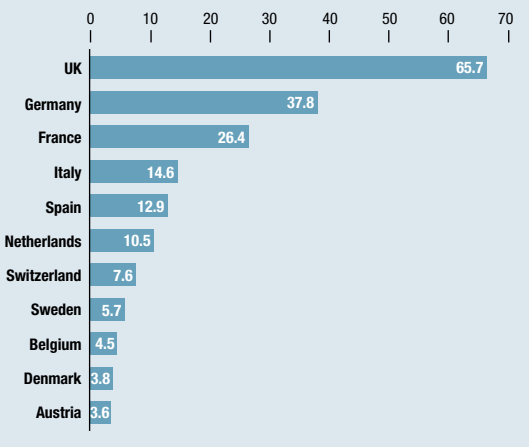
The European IT services market is extremely fragmented, with top player IBM occupying only 7.5 percent. The market is split into three tiers:

- The largest players are global and pan-European companies with annual revenues exceeding US$1.3 billion, such as IBM, Accenture, Capgemini, T-Systems and LogicaCMG.
- The second tier of companies has annual revenues of between US$130 million and US$1.3 billion, which comprise mid-sized regional playersand captive IT operations of large corporations, including Siemens Business Services, Computer Sciences Corp., Steria and Indra. These players compete fiercely in their territories of choice.
- Lastly, smaller niche players and local service providers abound, which are increasingly becoming acquisition targets for larger IT vendors.

Financial services, government, manufacturing and communications are the strongest sectors in Europe in terms of IT spending, accounting together for 70 percent of total spending.

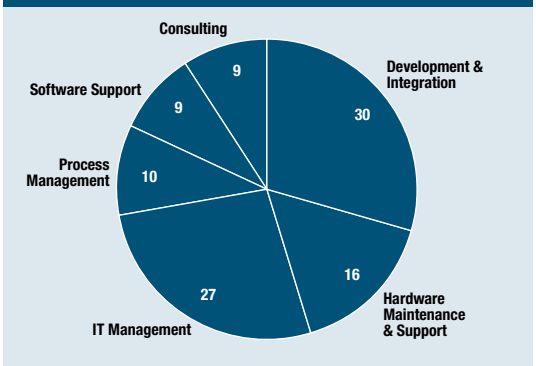
Software development and integration, as well as IT management are the largest service divisions, accounting for 57 percent of total spending, and experts predict continued growth particularly in software development and integration.

Figure 9: Top European country by IT spend in US$ billion (2205)



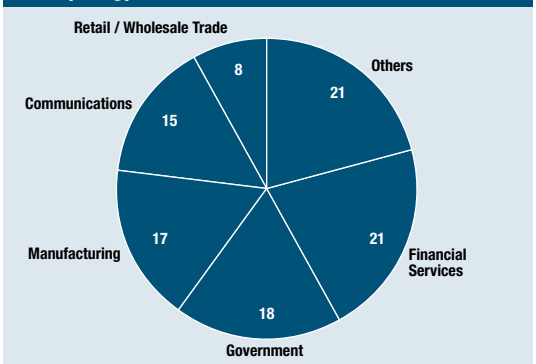
(Gartner Dataquest)

Figure 10: European IT break-up by services in % (2005)



(Gartner Dataquest; goetzpartners; Avendus)

Figure 11: European IT break-up by verticals in % (2005)

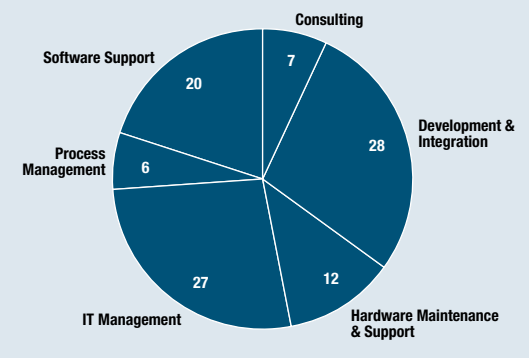


(Gartner Dataquest; goetzpartners; Avendus)

Summary

The European IT services market, a highly fragmented one and dominated by different players, is expected to grow faster than the US market over the next three years, in part as a result of an improving economic picture as well as an increasing awareness of outsourcing. The most attractive markets for Indian companies are the UK, Germany, France, Italy and Spain.

Figure 12: UK: IT spending break-up by services in % (2005)



(goetzpartners; Avendus)

Figure 13: UK: IT spending break-up by verticals in % (2005)

(goetzpartners; Avendus)

UK

With a market size of US$66 billion in 2005, the UK represents Europe's largest IT services market. It is also the most mature market with intense competition and aggressive pricing akin to that in the US. Top service providers include BT, EDS, IBM, Fujitsu, Capita, Accenture and Capgemini.

Managed services and outsourcing spending represents more than two-thirds of total IT services spending in the UK. Within outsourcing, application outsourcing ranks the highest and is expected to grow most strongly. The demand is expected to remain robust, driven by a healthy economy and rising discretionary corporate income.

Offshore spending in the UK is the highest in Europe, driven by a combination of no language barrier and a favorable and well understood regulatory environment. Up to 21 percent of employees serving the UK IT services market are based offshore. Demand is being fueled by financial regulatory changes as well as a growth in integration services and large e-government outsourcing projects. Application maintenance and BPO are expected to remain high growth areas.

Financial services, telecoms, utilities, technology, life sciences and biotech, manufacturing and the public sector are strong drivers of IT offshoring. In particular the public sector has embraced outsourcing and offshoring in order to control costs.

Figure 14: UK: Top 10 M&A deals (2005 – 2007)

Announced Date	Target Company	Bidder Company	Deal Value US$ million	Revenue Multiple
30.07.2007	Xansa Plc	Groupe Steria SCA	955.0	1.34x
28.06.2007	IXEurope Plc	Equinix Inc.	533.0	7.29x
15.01.2007	Vertex Data Science	GenNX360 Capital Partners; Knox Lawrence International Llc; Oak Hill Capital Partners LP	427.0	
31.03.2005	Service and Systems Solutions Limited (Sx3)	Northgate Information Solutions Plc	291.0	1.32x
27.09.2006	2e2 Group Limited	Duke Street Capital	243.0	1.26x
28.03.2007	ICM Computer Group Plc	Phoenix IT Group Ltd	214.0	1.53x
08.03.2005	Marlborough Stirling Plc	Vertex Data Science	139.0	0.77x
02.11.2005	Redbus Interhouse Plc	TeleCity Group	97.0	3.17x
05.04.2005	AttentiV Systems Group Plc	TietoEnator Oyj	96.0	1.66x
18.08.2005	INCAT International Plc	Tata Technologies Inc	83.0	0.71x

(mergermarket)

Figure 15: UK: Top 10 IT services companies by revenues (2005)

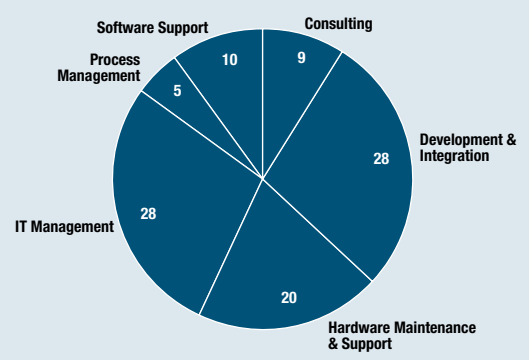
Company	2005 (US$ million)	Market Share	Growth Rate
BT	4,926	7.5%	10.2%
EDS	3,696	5.6%	-7.2%
IBM	3,500	5.3%	3.9%
Fujitsu	2,928	4.5%	9.6%
Capita Group	2,609	4.0%	10.8%
Accenture	2,472	3.8%	17.4%
CSC	2,155	3.3%	7.3%
Capgemini	2,151	3.3%	36.1%
Hewlett-Packard	1,668	2.5%	7.3%
Atos Origin	1,447	2.2%	-3.9%

(Gartner Dataquest)

Summary

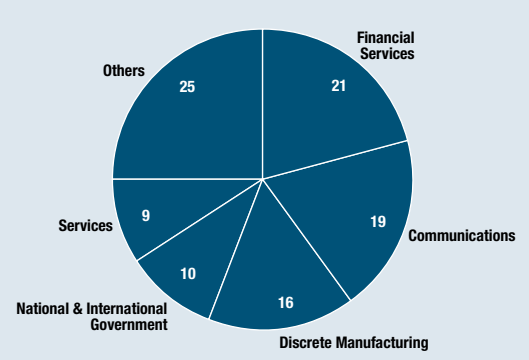
The UK remains the most interesting market for Indian companies due to size, infrastructure, its demand for outsourcing, language and cultural ties. However, the market approach used in the UK cannot simply be transferred to Europe's other distinct markets.

Figure 16: Germany: IT spending break-up by services in % (2005)



(goetzpartners; Avendus)

Figure 17: Germany: IT spending break-up by verticals in % (2005)



(goetzpartners; Avendus)

Germany

Europe's largest economy ranks second in terms of IT services. German companies spent US$37.8 billion on IT services in 2005, and this is projected to grow at an annual rate of 5.7 percent over the next five years. German IT service providers are among the most sought-after acquisition targets, as foreign players are eager to gain a foothold in this large and potentially lucrative market.

Nevertheless, Germany has been one of Europe's weaker IT markets over the past several years. German companies have been slow to embrace outsourcing, due to language and cultural barriers, a difficult business environment, strict domestic labor regulations and the strong influence of labor unions and employee councils. However, increasing globalization and competitive pressures from European and global players can be expected to change that. The German business confidence index rose strongly in 2006, although IT spending overall has lagged that index. The German automobile sector has the highest spend on IT, but that still only amounts to about 4.6 percent of overall spending.

Germany's IT services landscape is comprised of a few dominant multi-national IT services vendors, a small understaffed midmarket segment addressing the conservative German Mittelstand - privately-owned, small and medium sized companies - and small regional and niche players.

Outsourcing in Germany is strongly influenced by IT captives, which has created a fragmented market through the dominance of hundreds of small IT captives that are unlikely to be competitive over the long-term. This structure has caused stagnation in the market, with local heavyweights having minimal global presence, while global vendors are blocked out by local players.

Leading IT services players in Germany include T-Systems, Siemens Business Services, IBM and EDS. The Mittelstand drives most of the IT spending, in areas including infrastructure-related outsourcing and project based services.

Figure 18: Germany: Top 10 M&A deals (2005 – 2007)

Announced Date	Target Company	Bidder Company	Deal Value US$ million	Revenue Multiple
21.12.2005	gedas AG	T-Systems International GmbH	533.0	0.79x
11.12.2006	TDS Informationstechnologie AG	Fujitsu Services Limited	139.0	1.26x
31.07.2006	Fritz & Macziol GmbH	Imtech NV (formerly Internatio-Mueller NV)	64.0	0.43x
09.08.2005	Arxes Network Communication Consulting AG (formerly known as Arxes Information Design AG)	NDO Services B.V.	28.0	0.55x
27.09.2006	TUI InfoTec GmbH (50.10% stake)	Sonata Software Ltd	23.0	0.28x
07.02.2006	All for One Systemhaus GmbH Midmarket Solutions	AC - Service AG	18.0	0.67x
17.03.2006	mgm technology partners GmbH	MGM MBO GmbH	17.0	0.97x
15.06.2005	autinform AG	HAITEC AG	14.0	0.59x
09.02.2006	Viveon AG	SHS VIVEON AG (formerly known as SHS Informationssysteme AG)	12.0	1.37x
22.12.2005	Syskoplan AG (63.76% stake)	Reply SpA	11.0	0.47x

(mergermarket)

Figure 19: Germany: Top 10 IT services companies by revenues (2005)

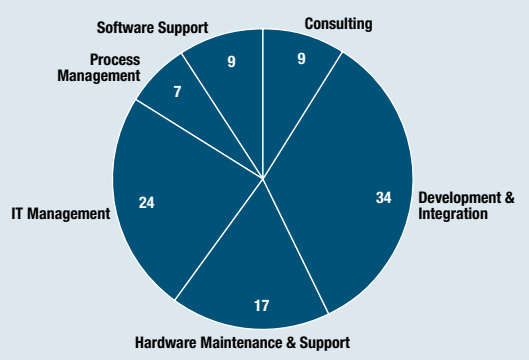
Company	2005 (US$ million)	Market Share	Growth Rate
T-Systems	5,799	15.4%	1.2%
Siemens Business Services	2,757	7.3%	11.5%
IBM	2,490	6.6%	3.8%
Hewlett-Packard	1,371	3.6%	1.9%
Siemens Communications	1,209	3.2%	3.0%
Accenture	997	2.6%	11.7%
SAP	924	2.4%	4.0%
Fiducia	905	2.4%	3.0%
EDS	619	1.6%	5.1%
Computer Sciences Corp	517	1.4%	2.8%

(Gartner Dataquest)

Summary

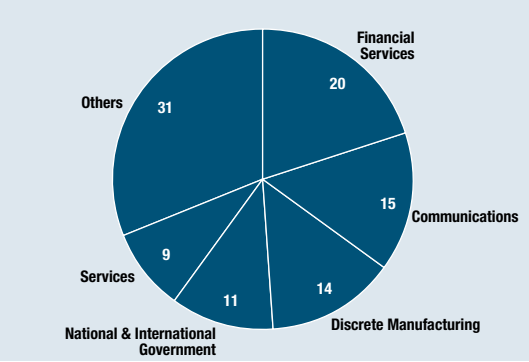
Europe's sleeping giant, Germany has been slow to embrace outsourcing due to stiff labour regulations and a slow economy. However, as the German economy picks up, and due to competitive pressure and globalization, old structures are unravelling. Service orientation is increasing and price/service ratios are changing significantly.

Figure 20: France: IT spending break-up by services in % (2005)



(goetzpartners; Avendus)

Figure 21: France: IT spending break-up by verticals in % (2005)



(goetzpartners; Avendus)

France

France is Europe's third-largest IT services market, with US$26.4 billion spent in 2005 and annual growth of 5.8 percent in the same year.

The key verticals driving growth in French IT spending include financial services, followed by communications, with public services as the fastest growing sector due to modernization and cost reduction. According to IDC, the public sector will continue to grow at the highest rate of the French IT market with a 5.6 percent CAGR, driving spending to estimated US$9 billion in 2008. The most active areas are software development and integration, IT management, maintenance and support. Application outsourcing is still rare but is expected to grow with the increased used of project-based services and information management systems.

French companies tend to focus on near-shoring in countries where France has ties, such as Romania and North Africa, rather than on offshoring in India. Outsourcing could get new impulses, however, from government-owned privatizations. The government is seeking to dilute its holdings in such firms as Electricité de France, Gaz de France, Société Générale, France Telecom and Air France. These organizations will increasingly seek to efficiently structure their operations.

Reluctance to outsourcing is on the wane, with companies such as Renault cautiously moving towards outsourcing, using a mix of local and global vendors. Renault has outsourced its desktop environment including computers, printers and other equipment for all employees worldwide.

Competition is intense among local players in what is a very domestically-oriented market, giving an edge to French players such as Atos Origin, Sopra, Sogeti and Thales. Due to the high salaries in the IT market, French IT service providers are not attractive acquisition targets. That is one reason why large players such as Capgemini and Atos Origin are seeking to go off-shore for acquisitions in places such as India.

Figure 22: France: Top 10 M&A deals (2005 – 2007)

Announced Date	Target Company	Bidder Company	Deal Value US$ million	Revenue Multiple
19.09.2005	Unilog SA	LogicaCMG plc	1,159.0	1.37x
02.05.2007	GFI Informatique SA	Fujitsu Limited	608.0	0.73x
25.07.2006	INEUMconsulting (formerly Deloitte Consulting France)	Management Consulting Group Plc (MCG)	168.0	1.25x
05.12.2006	Group Silicomp SA	France Telecom SA	121.0	0.95x
23.02.2005	Osiatis	Groupe Focal	113.0	0.71x
16.10.2006	Datem Group (formerly Pole Presse Informatique)	Team Partners Group	51.0	
	Team Partners Group	Weinberg Capital Partners		
28.07.2006	Groupe Diwan (72.00% stake)	France Telecom SA	46.0	1.40x
07.09.2005	CGBI SA	Team Partners Group	19.0	0.82x
28.01.2005	Teamlog SA (42.00% stake)	Groupe OPEN SA	11.0	

(mergermarket)

Figure 23: France: Top 10 IT services companies by revenues (2005)

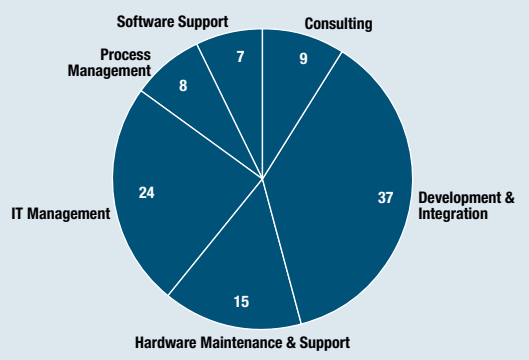
Company	2005 (US$ million)	Market Share	Growth Rate
Capgemini	2,071	7.8%	12.7%
IBM	1,976	7.5%	4.0%
Atos Origin	1,897	7.2%	11.7%
France Telecom	984	3.7%	0.3%
Accenture	830	3.1%	11.2%
Alcatel	798	3.0%	6.4%
Sopra	704	2.7%	6.9%
Unilog	666	2.5%	1.4%
Steria	601	2.3%	8.8%
Hewlett-Packard	550	2.1%	-0.5%

(Gartner Dataquest)

Summary

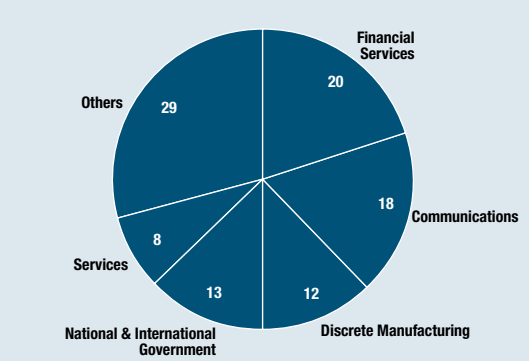
France is an attractive market, given its size and development. However, high salaries make French IT providers poor acquisition targets. In addition, French companies are focused on near-shoring for cultural reasons.

Figure 24: Italy: IT spending break-up by services in % (2005)



(goetzpartners; Avendus)

Figure 25: Italy: IT spending break-up by verticals in % (2005)



(goetzpartners; Avendus)

Italy

With a market size of US$14.6 billion in 2005, the Italian IT services market is Europe's fourth largest, and is expected to grow by 5.4 percent annually through 2009.

However, Italy has historically been a less attractive market for foreign vendors, with its linguistic and cultural barriers, as well as a relatively high level of bureaucracy, which raises the cost of doing business. The market for IT services has also been limited by low rates of economic growth; Italy currently suffers one of the lowest rates of GDP growth in Europe, and investing in IT services has not been a priority for Italian firms. Nor has M&A played a large role in the Italian IT services market. The top vendor in Italy is IBM, with strong competition among global and local players.

Of the overall IT services market, financial services makes up the largest segment, with an 18 percent share, and manufacturing ranks second, accounting for 16 percent of total revenues. The EUR 1.7 billion FIAT-IBM outsourcing deal as well as large wins by EDS in financial services and CSC in the government sector point to a broadening customer base for IT services, particularly in automobile manufacturing and the banking segment. Italian communications firms are also making sizable investments to upgrade and enhance their infrastructure, which could drive IT services revenues. Furthermore, the public sector is one of the most active in investing in IT services.

Italy remains largely unexplored by Indian IT vendors as firms tend to utilize nearshore delivery capabilities in Romania and Bulgaria, with whom there is some cultural affinity. However, the Italian market could prove lucrative if approached with a partner or through nearshore delivery at multi-lingual sites based in Romania.

Figure 26: Italy: Top 10 M&A deals (2005 – 2007)

Announced Date	Target Company	Bidder Company	Deal Value US$ million	Revenue Multiple
27.07.2005	Datamat SpA (formerly Datamat Ingegneria dei Sistemi) (53.00% stake)	Finmeccanica SpA	148.0	1.53x
24.02.2005	Finsiel SpA (60.00% stake)	Almaviva Technologies	102.0	0.21x
02.02.2007	Etnoteam SpA	Value Team IT Consulting & Solutions	91.0	0.64x
04.04.2007	Servizio Titoli SpA (90.00% stake)	Borsa Italiana SpA	39.0	3.61x
19.06.2007	Eunics SpA (65.00% stake)	Eutelia SpA	19.0	0.42x
02.04.2007	auSystems operations in France, Italy, Norway and UK	Devoteam SA	13.0	0.18x
05.01.2007	Met Sogeda SpA	Comdata SpA	13.0	0.17x
08.05.2007	Data Service SpA (45.63% stake)	Data Holding 2007	8.0	
25.10.2005	Comnet SpA (50.00% stake)	TietoEnator Oyj	8.0	1.10x
30.11.2005	Overnet Solutions S.r.l. (97.50% stake)	Kaitech SpA	6.0	0.77x

(mergermarket)

Figure 27: Italy: Top 10 IT services companies by revenues (2005)

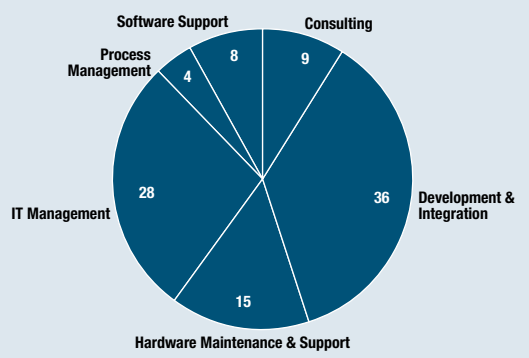
Company	2005 (US$ million)	Market Share	Growth Rate
IBM	1,784	12.23%	5.58%
Almaviva Group	1,032	7.08%	-2.30%
Accenture	957	6.56%	9.87%
Hewlett-Packard	668	4.58%	3.45%
EDS	471	3.23%	4.58%
Gruppo Engineering	463	3.18%	15.77%
Ericsson	392	2.69%	15.31%
Elsag SpA	381	2.61%	-12.41%
SBS	356	2.44%	9.42%
Atos Origin	337	2.31%	7.26%

(Gartner Dataquest)

Summary

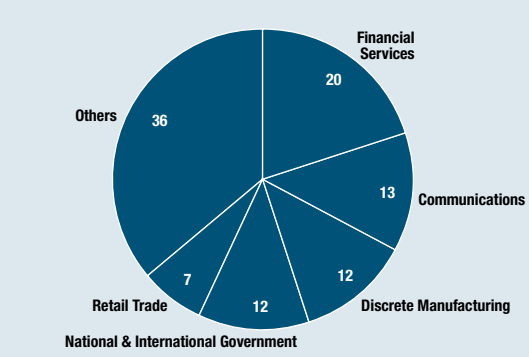
The Italian market presents high barriers to entry, but acquiring a near-shoring provider in places like Romania could open these doors.

Figure 28: Spain: IT spending break-up by services in % (2005)



(goetzpartners; Avendus)

Figure 29: Spain: IT spending break-up by verticals in % (2005)



(goetzpartners; Avendus)

Spain

The Spanish IT services market totaled US$10.4 billion in 2005. Like some other Southern European countries, Spain's economic development has lagged that of its northern neighbors. As a result local wages are 20 percent to 40 percent lower than the European average, dampening the attractiveness of offshoring for Spanish firms.

IT consulting and management services have grown by about 7 percent on average over the past decade, to reach US$3.8 billion in 2005. Development and integration accounted for an additional US$3.7 billion. Within managed services/outsourcing, infrastructure outsourcing ranks highest.

Spain has only a handful of companies with more than 5,000 employees, limiting the amount spent on IT. In 2005, there were only 9 Spanish IT outsourcing deals, five of which came from financial services firms. Spanish financial services firms are considering outsourcing for software development and banking customers are expected to move from customized development to packaged applications.

Strong regional government drives local IT services spending. For example, Palma de Mallorca awarded a comprehensive contract for system integration and support services to Gedas, which included developing and implementing an integrated administration system, customer relationship management software system and a quality management system, bundled with IT infrastructure services. 50 percent of the IT spending is driven by the Madrid region.

Figure 30: Spain: Top 10 M&A deals (2005 – 2007)

Announced Date	Target Company	Bidder Company	Deal Value US$ million	Revenue Multiple
11.03.2005	Amadeus Global Travel Distribution SA	Wam Acquisition SA	5,852.0	2.11x
11.10.2006	Soluziona SA	Indra Sistemas SA	350.0	0.79x
28.07.2006	Azertia, Tecnologias De La Informacion Sociedad Anonima	Indra Sistemas SA	181.0	0.78x
15.06.2007	Getronics Espana Solutions SL	Tecnocom Telecomunicaciones y Energia SA	127.0	
23.01.2007	Acens Technologies SA	Nazca Capital S.G.E.C.R.	59.0	3.10x
06.03.2007	BMB Gestion Documental SL (50.00% stake)	Indra Sistemas SA	42.0	
04.10.2006	Softgal Gestion SA; Softgal Servicios De Software De Galicia SA	Tecnocom Telecomunicaciones y Energia SA	25.0	0.74x
23.09.2005	Novasoft Sanidad SA	iSOFT Group plc	23.0	1.31x
13.04.2005	BMB Gestion Documental SL (37.00% stake)	Indra Sistemas SA	21.0	
21.04.2005	SIR, SA	Serdetec SL	20.0	

(mergermarket)

Figure 31: Spain: Top 10 IT services companies by revenues (2005)

Company	2005 (US$ million)	Market Share	Growth Rate
IBM	1,170	11.2%	2.6%
INDRA	964	9.2%	10.2%
Accenture	726	7.0%	14.2%
Telefónica	551	5.3%	8.6%
Fujitsu	435	4.2%	11.2%
Hewlett-Packard	389	3.7%	-0.8%
Informática El Corte Inglés	367	3.5%	4.1%
T-Systems	294	2.8%	4.1%
Atos Origin	280	2.7%	2.3%
Capgemini	264	2.5%	6.0%

(Gartner Dataquest)

Summary

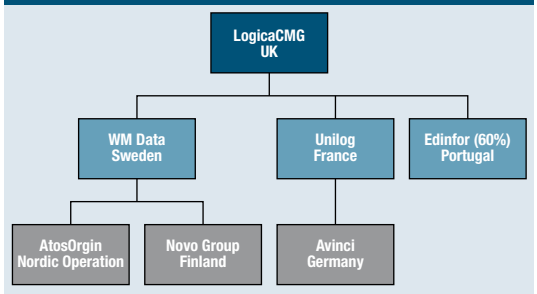
Spain's IT services market is less mature than in Northern Europe, with IT spending driven by regional government contracts. Low wages make it difficult for Indian companies to offer attractive conditions.

European Consolidation Wave

Taking IT Services as a proxy we have witnessed that the regional IT markets are on the move. As their structure doesn't enable them to successfully exist in the market on their own, significant consolidation within the domestic and European IT services market over the last two years has started. It partially has led to the emergence of large European companies with a pan-European presence, such as Capgemini and LogicaCMG, created via a series of acquisitions.

UK-based LogicaCMG has set out to become a pan-European IT services leader, completing acquisitions worth US$3 billion over the past few years. It bought Sweden's WM Data for US$1.66 billion. Prior to that, Logica acquired France's Unilog and Edinfor in Portugal. These acquisitions give LogicaCMG the opportunity to qualify for larger contracts, as European customers have begun to show a preference for bigger players who can support them internationally.

Figure 32: Company structure LogicaCMG



(Company website; goetzpartners; Avendus)

Regionally, some IT services players are shoring up their positions as well. Before it was acquired, WM-Data itself purchased Atos Origins' Nordic operations in June 2005. Atos acquired Schlumberger Sema and Itellium, and Steria bought Mummert. In Spain, the provider Indra recently acquired local competitors Azertia and Soluziona, giving it a boost in the Latin American markets as well.

M&A activity is expected to continue. There have been continued rumblings about potential mergers such as a rumored deal between Siemens and Atos. Both Atos and Capgemini are said to be aggressively seeking mid-sized acquisition targets in Europe. Some firms, such as France's Sopra and Steria, are looking to acquire mid-size players in offshore locations like India, as well as making attractive acquisition targets in and of themselves.

Meanwhile global IT players such as EDS, Accenture and IBM have also been strengthening their presence in Europe. IBM has made seven acquisitions valued at US$1 billion over the past three years. Other active players include HP and CIBER, while potential new entrants into the market include CGI and ACS. There are also rumours that Infosys might be interested in T-Systems and CapGemini.

Indian offshore vendors have for the most part not yet participated in this wave of European consolidation. In terms of joint ventures and M&A, local European vendors have a natural advantage over Indian players in terms of language, culture, knowledge of regulations and relationships. However, analysts believe this will change dramatically over the next few years.

Summary

European markets are on the move. Consolidations in the home markets and expansions to other countries lead to the existence of important players that have still advantages compared to Indian players. However, analysts believe that India will gain importance significantly.

Europe's Attractiveness for India

Analysts predict that the improved European economic environment will have a positive impact on the demand for IT services. That is driven by a combination of intensifying competition, consolidation and regulatory compliance issues, in particular among companies within the banking, financial services and insurance (BFSI) and communications sectors.

This trend will open the doors for Indian IT services companies that are looking to expand to establish themselves as important players in the European market: the opportunity to move up the value chain and directly connect to their end-customers will be pursued by acquiring or partnering with European companies. Thus Indian companies will be able to develop and offer expertise in higher-end businesses such as infrastructure management services, which demands local presence and delivery.

Local manufacturing companies, facing increased competition from low-cost bases such as China and India, are also looking to cap IT spending and reduce operating costs, leading to consolidation. At the same time, however, IT spending is expected to increase as a result of accelerating M&A activity across Europe, which has increased the demand for consulting, system integration and business process outsourcing services. Companies are looking to rationalize their application portfolios and increase the efficiency of their business processes.

Up until now, Indian offshore vendors have focused their European expansion efforts mainly on the UK, deriving anywhere between 75 to 90 percent of their income from there. However, analysts believe Continental Europe is poised to become the next large outpost for Indian growth. That will in part be driven by an increased appetite on the part of European players for more comprehensive outsourcing solutions, which will make them natural partners for Indian companies both domestically and abroad. A large outsourcing contract such as that awarded recently by ABN Amro points in this direction.

Summary

Driven by the increased importance of outsourcing to European countries, they will highly likely look for partnering with Indian companies domestically and abroad.

Going Cross-border

As seen, there are numerous opportunities for both European and Indian companies to grow their businesses by cooperating with one another, either organically, by building out their presence in these countries, through joint ventures or via selective acquisitions in markets that are more difficult to penetrate.

The offshoring phenomena will continue to drive European companies to enter into cooperations with Indian players. For example, offshore IT services spend expected to grow 60 percent annually through 2009; the next few years could be watershed years for Indian IT vendors. Given the growing importance of providing global delivery capability to clients, small to mid-sized European players may look to develop their offshore and near-shore capabilities, and will seek to deepen ties to Indian companies.

India is well positioned to take advantage of this trend. Top Indian players including TCS, Wipro, Infosys, Satyam and HCL have repeatedly demonstrated robust revenue growth from Europe in the last five years.

Indian IT companies have already established a name for themselves as leaders in key sectors such as financial services and communications. They also enjoy a reputation for high quality and commitment. Well-trained, well-educated Indian employees still offer companies cost-savings of up to 60 percent compared to their Western counterparts. Bilateral trade between India and the European Union is also bringing these partners ever closer.

These are ideal conditions for Indian companies to move up the value chain and touch base directly with the end-customers. Large, well-financed Indian players are looking to Europe to fuel their own growth ambitions. Large IT services players, for example, are in a good position to achieve market leadership via large acquisitions, while buying up small-and-medium sized players will help them penetrate niche markets. Indian IT vendors could establish beachheads through acquisitions of small-to-mid sized companies that help them overcome existing entry barriers. Larger acquisitions of over US$150 million could be leveraged to cement leadership positions.

Summary

The increasing economic importance of India and Europe's demand for outsourcing for competitive reasons are laying the ground for mutual cross-border activities.

Opportunities and Challenges

Yet both Indian and European companies face challenges in making these deals happen. European companies must overcome domestic resistance to offshoring, seeing the Indian market as an opportunity rather than a threat, in order to take advantage of the chances that cooperating with Indian vendors offers. Indian vendors, for their part, must grasp that Europe is not one market. Besides different languages, markets can be highly fragmented and have their own peculiarities. The leading vendors vary from country to country, and each vendor has its own unique image in these respective markets. Indian vendors must also pay attention to EU regulations, as well as how they are implemented domestically in various markets.

Until now, Indian IT vendors have not successfully breached these hurdles in Continental Europe. The European market share of the Top 6 Indian vendors has doubled since 2003 but is still low at around one percent. And even though some leading India vendors have a pan European sales presence, their success in penetrating non-English speaking markets has been limited. More than 75 percent of these revenues come from the UK and several other English-language oriented countries, such as the Netherlands, indicating huge untapped potential in Continental Europe, in particular in Germany and the Nordic Countries. Mid-sized firms such as Hexaware and Mastek, however, have managed to establish themselves in Europe through a focused and localized market penetration strategy, setting an example for other Indian firms to copy.

Large European corporates have been following the trend towards out-sourcing and have established important presences in the country, like IBM, and SAP. The German Mittelstand, however, has not yet found its way to India as it cannot take advantage from cost synergies like the big players do. The question for them is how to successfully enter the market. If they do not find the right way, they might be consolidated by either an Indian company or a European one.

Summary

The previous examples show that for establishing successful business relationships in either market careful preparation and understanding of the dynamics in every geography are essential.

A Dependable Partner

goetzpartners is uniquely positioned to help both European and Indian vendors to overcome these hurdles, advising them on how best to undertake cross-border deals, whether that be via organic growth, joint ventures or mergers and acquisitions.

With its one firm, two services approach, goetzpartners can offer customers a comprehensive, integrated means of making strategic decisions. This is realized via its unique structure, which encompasses both a corporate finance advisory firm and a management consultancy, as well as through its extensive network of contacts across Europe and India. goetzpartners, based in Munich, Düsseldorf, Frankfurt, London, Madrid, Paris and Prague, and in partner offices in Budapest and Moscow, has a deep understanding and experience with various cultures across the globe. It offers companies in both India and Europe the support they need to establish themselves outside their own borders. In particular, goetzpartners' strategic cooperation with Avendus, one of the leading investment banks in India with a market share of 70 percent of all deals between US$10 and US$200 million, enables it to provide a deep understanding of the markets there. It is the perfect partnership for creating synergies for clients on both sides.

Table of Figures

About goetzpartners

With about 150 employees in Munich, Düsseldorf, Frankfurt, London, Paris, Madrid, and Prague, and cooperations in Budapest, Moscow, and Mumbai, goetzpartners is one of the leading European independent advisory firms. By offering profound expertise in corporate finance (goetzpartners Corporate Finance GmbH), management consulting (goetzpartners Management Consultants GmbH) and interim management (goetzpartners Interim Managers GmbH) under one roof, goetzpartners combines deep functional expertise with a unique market approach. goetzpartners Corporate Finance offers M&A, corporate finance, fairness opinions/valuations and corporate partnering advisory. goetzpartners Management Consultants is focused on strategy, operational excellence, business development, strategic due diligence and public private interface management in growing and mature industries. goetzpartners Interim Managers assume responsibility for the achievement of results defined in restructuring and growth programs. For further information, please visit www.goetzpartners.com

About Avendus Advisors

Avendus Advisors is an investment bank offering M&A advisory and Equity and Structured Debt syndication, for high growth corporates and funds. Avendus has strong research capabilities and relationships, which it leverages to close transactions for its clients in aggressive time frames. With a strong Indian presence and global relationships, Avendus has been an investment bank of choice both for international investors and companies who are scouting for business opportunities in India and Indian companies looking at strategic initiatives in overseas markets. With 20 transaction closures aggregating more than US$ 500 million, Avendus is one of the leading investment banks in India. For further information, please visit www.avendus.com

2007, goetzpartners and Avendus Advisors joined forces to undertake cross-border transactions for European and Indian clients.

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