

Rising Re shakes BPO valuations

But PE investors haven't lost appetite for the sector

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With the rupee going from strength to strength and attrition a continuing concern for Indian business process outsourcing (BPO) companies, the new poster child of private equity (PE) investors is witnessing adjustments in valuations in the changed scenario.

PE investors feel that the interest in the sector continues, despite the rupee's rise, which has impacted their profitability. But, the valuations have changed.

"The rising rupee and the sub-prime crisis will affect the mood of investors in a big way," said Raju Venkatraman, joint managing di-

rector and chief operating officer, Firstsource. "However, we have not seen any hurry by our investors to move out. Rather, we recently raised \$275 million via zero coupon FCCBs." Westbridge and Aranda (an arm of Temasek) have invested in Firstsource.

"Valuations, at any given time, are reflections of profitability and growth. Also, there are not too many large players left now, and most of the time private equity players are looking at higher scales and, therefore, there are limited choices," said Ashish Basil, partner, Ernst & Young.

The rupee is at its strongest since February 1998, eating into the profitability of IT and BPO firms, which earn a bulk of their revenues in US dollars.

According to industry

estimates, at least 10 of the top 15 third party BPO companies have received PE backing in one form or the other.

PE firms invested \$227 million in 12 BPO firms in the first nine months of 2007, according to data from Venture Intelligence.

PE firms have invested over \$1.2 billion in the sector (across 50 deals) since 2004.

"Private equity players primarily look at two things, the market and the management team. The Indian BPO industry has ample growth potential from a market perspective. However, what they really look for is a company with a strong management team that will drive growth for the company," said Susir Kumar, CEO, Intelenet Global Services.

CHANGING MOOD

Top PE Investments in BPO by value in 2007 (First nine months)

| BPO | PE Fund | Investment |
|---------------|---------------------------|---------------|
| Intelenet | Blackstone | \$109 million |
| ISGN Tech | NEA, NEA-Indo US Ventures | \$25 million |
| Adventity | Norwest Ventures | \$20 million |
| Adayana | Kubera Partners | \$20 million |
| Amba Research | Helion Ventures | \$10 million |

Source: Venture Intelligence

Recently, US-based private equity giant Blackstone bought out Intelenet - a 50:50 joint venture established in 2004 by Barclays and HDFC - for close to \$109 million.

Akhil Gupta of Blackstone says, "We see good growth opportunity in the BPO segment. We expect their revenues to be five-six times over a period of time, as the number of processes companies are look-

ing to outsource is increasing." Sixty-five per cent of Indian BPO companies are captive units and the rest 35 per cent are third-party.

However, PE players are expecting more MBOs (management buyouts) in the captive BPO segment as many large companies are exiting from their non-core businesses. Also, the ticket size of MBOs will continue to increase.