

ExlService Holdings, Inc.  
Form 10-Q  
May 04, 2012  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2012**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**FOR THE TRANSITION PERIOD FROM            TO**

**COMMISSION FILE NUMBER 001-33089**

**EXLSERVICE HOLDINGS, INC.**

(Exact name of registrant as specified in its charter)

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**DELAWARE**  
(State or other jurisdiction of

incorporation or organization)

**280 PARK AVENUE, 38<sup>TH</sup> FLOOR, NEW YORK,**

**NEW YORK**  
(Address of principal executive offices)

**(212) 277-7100**

(Registrant's telephone number, including area code)

**82-0572194**  
(I.R.S. Employer

Identification No.)

**10017**  
(Zip code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of April 30, 2012, there were 31,905,746 shares of the registrant's common stock outstanding (excluding 336,262 shares held in treasury and 9,907 shares of restricted stock), par value \$0.001 per share.

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**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****EXLSERVICE HOLDINGS, INC.****CONSOLIDATED BALANCE SHEETS****(In thousands, except share and per share amounts)**

	<b>March 31, 2012 (Unaudited)</b>	<b>December 31, 2011</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 82,272	\$ 82,393
Short-term investments	7,258	7,869
Restricted cash	834	934
Accounts receivable, net	58,837	55,672
Prepaid expenses	4,349	4,269
Deferred tax assets, net	5,774	6,228
Advance income tax, net	2,787	3,379
Other current assets	8,452	6,097
<b>Total current assets</b>	<b>170,563</b>	<b>166,841</b>
Fixed assets, net	44,840	42,320
Restricted cash	3,630	3,387
Deferred tax assets, net	14,334	16,495
Intangible assets, net	35,090	36,313
Goodwill	93,627	92,287
Other assets	21,353	19,768
<b>Total assets</b>	<b>\$ 383,437</b>	<b>\$ 377,411</b>
<b>Liabilities and Stockholders Equity</b>		
Current liabilities:		
Accounts payable	\$ 3,674	\$ 4,333
Deferred revenue	7,805	7,772
Accrued employee cost	16,016	27,700
Accrued expenses and other current liabilities	26,398	30,700
Current portion of capital lease obligations	1,832	1,729
<b>Total current liabilities</b>	<b>55,725</b>	<b>72,234</b>
Capital lease obligations, less current portion	4,027	4,244
Non-current liabilities	18,139	22,458
<b>Total liabilities</b>	<b>77,891</b>	<b>98,936</b>
Commitments and contingencies		
Preferred stock, \$0.001 par value; 15,000,000 shares authorized, none issued		

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Stockholders' equity:

Common stock, \$0.001 par value; 100,000,000 shares authorized, 31,880,218 shares issued and 31,549,366 shares outstanding as of March 31, 2012 and 31,496,461 shares issued and 31,173,064 shares outstanding as of December 31, 2011.	32	31
Additional paid-in-capital	179,604	173,926
Retained earnings	155,962	147,046
Accumulated other comprehensive loss	(27,200)	(39,858)
<b>Total stockholders' equity including shares held in treasury</b>	<b>308,398</b>	<b>281,145</b>
Less: 330,852 shares as of March 31, 2012 and 323,397 shares as of December 31, 2011, held in treasury, at cost	(2,875)	(2,693)
<b>ExlService Holdings, Inc. stockholders' equity</b>	<b>305,523</b>	<b>278,452</b>
Non-controlling interest	23	23
<b>Total stockholders' equity</b>	<b>305,546</b>	<b>278,475</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 383,437</b>	<b>\$ 377,411</b>

See accompanying notes.

**Table of Contents****EXLSERVICE HOLDINGS, INC.****CONSOLIDATED STATEMENTS OF INCOME****(Unaudited)****(In thousands, except share and per share amounts)**

	<b>Three months ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
Revenues	\$ 104,608	\$ 72,907
Cost of revenues (exclusive of depreciation and amortization)	66,672	44,219
Gross profit	37,936	28,688
Operating expenses:		
General and administrative expenses	13,347	10,471
Selling and marketing expenses	7,799	5,857
Depreciation and amortization	6,359	4,852
Total operating expenses	27,505	21,180
Income from operations	10,431	7,508
Other income, net:		
Foreign exchange gain	1,058	1,648
Interest and other income, net	447	325
Income before income taxes	11,936	9,481
Income tax provision	3,020	1,120
Net income	\$ 8,916	\$ 8,361
Earnings per share:		
Basic	\$ 0.28	\$ 0.28
Diluted	\$ 0.27	\$ 0.27
Weighted-average number of shares used in computing earnings per share:		
Basic	31,445,592	29,620,218
Diluted	32,783,855	30,911,066

See accompanying notes.

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**EXLSERVICE HOLDINGS, INC.**

**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

**(Unaudited)**

**(In thousands)**

	<b>Three months ended</b>	
	<b>March 31,</b>	
	<b>2012</b>	<b>2011</b>
Net income	\$ 8,916	\$ 8,361
Other comprehensive income:		
Unrealized gain/(loss) on effective cash flow hedges, net of taxes	6,486	(314)
Foreign currency translation adjustment	6,223	902
Retirement benefits, net of taxes	(51)	20
Total other comprehensive income	12,658	608
Total comprehensive income	\$ 21,574	\$ 8,969

See accompanying notes.

**Table of Contents****EXLSERVICE HOLDINGS, INC.****CONSOLIDATED STATEMENTS OF CASH FLOW****(Unaudited)****(In thousands)**

	<b>Three months ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
<b>Cash flows from operating activities:</b>		
Net income	\$ 8,916	\$ 8,361
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>		
Depreciation and amortization	6,359	4,852
Amortization of debt issuance costs	38	
Stock-based compensation expense	2,743	2,248
Non-employee stock options	32	
Unrealized foreign exchange loss	1,711	297
Deferred income taxes	954	(1,553)
<b>Change in operating assets and liabilities :</b>		
Restricted cash	108	(118)
Accounts receivable	(2,839)	(1,051)
Prepaid expenses and other current assets	(2,292)	(544)
Accounts payable	569	(1,059)
Deferred revenue	21	1,436
Accrued employee cost	(13,229)	(10,109)
Accrued expenses and other liabilities	883	3,972
Advance income tax, net	817	609
Other assets	(422)	411
 Net cash provided by operating activities	 4,369	 7,752
 <b>Cash flows from investing activities:</b>		
Purchase of fixed assets	(9,299)	(7,158)
Purchase of short-term investments	(1,369)	(72)
Proceeds from redemption of short-term investments	2,223	
 Net cash used for investing activities	 (8,445)	 (7,230)
 <b>Cash flows from financing activities:</b>		
Principal payments on capital lease obligations	(446)	(51)
Acquisition of treasury stock	(182)	(34)
Proceeds from exercise of stock options	2,903	595
 Net cash provided by financing activities	 2,275	 510
 Effect of exchange rate changes on cash and cash equivalents	 1,680	 329
 Net (decrease)/increase in cash and cash equivalents	 (121)	 1,361
Cash and cash equivalents, beginning of period	82,393	111,182



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Cash and cash equivalents, end of period

\$ 82,272    \$ 112,543

See accompanying notes.

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**EXLSERVICE HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**March 31, 2012**

**(Unaudited)**

**(In thousands, except share and per share amounts)**

**1. Organization and Basis of Presentation**

***Organization***

ExlService Holdings, Inc. (ExlService Holdings) is organized as a corporation under the laws of the State of Delaware. ExlService Holdings, together with its subsidiaries (collectively, the Company), is a leading provider of outsourcing services and transformation services. The Company's clients are located principally in the United States and the United Kingdom.

***Basis of Presentation***

The unaudited interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements and therefore should be read in conjunction with the audited consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

The unaudited interim consolidated financial statements reflect all adjustments (of a normal and recurring nature) which management considers necessary for a fair presentation of such statements for the interim periods presented. The unaudited consolidated statements of income for the interim periods presented are not necessarily indicative of the results for the full year or for any subsequent period.

**2. Summary of Significant Accounting Policies**

***Principles of Consolidation***

The accompanying unaudited consolidated financial statements include the financial statements of ExlService Holdings and all of its subsidiaries. All intercompany balances and transactions have been eliminated in consolidation.

The non-controlling interest represents the minority partner's interest in the operation of exl Service.com (India) Private Limited (Exl India) and the profits associated with the minority partner's interest in those operations, in the unaudited consolidated balance sheet and unaudited consolidated statement of income, respectively. The non-controlling interest in the operations for the three months ended March 31, 2012 and 2011 was insignificant and is included under general and administrative expenses in the unaudited consolidated statements of income.

***Use of Estimates***

The preparation of the unaudited consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the unaudited consolidated financial statements and the unaudited consolidated statements of income during the reporting period. Estimates are based upon management's best assessment of the current business environment. Actual results could differ from those estimates. The significant estimates and assumptions that affect the financial statements include, but are not limited to, allowance for doubtful receivables, service tax receivables, assets and obligations related to employee benefit plans, deferred tax valuation allowances, income-tax uncertainties and other contingencies, valuation of derivative financial instruments, stock-based compensation expense, depreciation and amortization periods, recoverability of long-term assets including goodwill and intangibles, and estimates to complete fixed price contracts.



**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)****March 31, 2012****(Unaudited)****(In thousands, except share and per share amounts)*****Recent Accounting Pronouncements***

In May 2011, the FASB issued update No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS* (ASU No. 2011-04). ASU No. 2011-04 was intended to improve the comparability of fair value measurements presented and disclosed in financial statements prepared in accordance with Generally Accepted Accounting Principles (GAAP) and International Financial Reporting Standards (IFRS). The amendments in this update result in common fair value measurement and disclosure requirements in GAAP and IFRS. The update explains how to measure fair value and does not require additional measurements. The adoption of this accounting pronouncement from January 1, 2012 did not have any impact on the Company's unaudited consolidated financial statements.

In June 2011, the FASB issued update No. 2011-05, *Presentation of Comprehensive Income* (ASU No. 2011-05). ASU No. 2011-05 effective retrospectively for the interim and annual periods beginning on or after December 15, 2011 (early adoption is permitted), requires presentation of total comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In December 2011, FASB issued update No. 2011-12, an amendment to defer the presentation on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income for annual and interim financial statements. The adoption of this accounting pronouncement from January 1, 2012 did not have any impact on the Company's unaudited consolidated financial statements. Refer to the Company's unaudited consolidated statements of comprehensive income for further details.

In September 2011, the FASB issued update No. 2011-08, *Testing Goodwill for Impairment* (ASU No. 2011-08), which allows entities to use a qualitative approach to test goodwill for impairment. ASU No. 2011-08 permits an entity to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value. If it is concluded that this is the case, it is necessary to perform the currently prescribed two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. ASU No. 2011-08 is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. The adoption of this accounting pronouncement did not have a material impact on the Company's unaudited consolidated financial statements and the Company does not expect this to have a material impact on its annual goodwill impairment assessment in the fourth quarter of fiscal 2012.

***Accrued expenses and other current liabilities***

	<b>March 31, 2012</b>	<b>December 31, 2011</b>
Accrued expenses	\$ 14,014	\$ 12,134
Derivative instruments	4,657	9,170
Other current liabilities	7,727	9,396
Accrued expenses and other current liabilities	\$ 26,398	\$ 30,700

***Non-current liabilities***

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	<b>March 31, 2012</b>	<b>December 31, 2011</b>
Derivative instruments	\$ 5,037	\$ 8,559
Unrecognized tax benefits	5,517	4,981
Deferred rent	3,754	3,319
Retirement benefits	2,172	3,068
Other non-current liabilities	1,659	2,531
 Non-current liabilities	 \$ 18,139	 \$ 22,458

**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)****March 31, 2012****(Unaudited)****(In thousands, except share and per share amounts)****3. Earnings Per Share**

Basic earnings per share is computed by dividing net income to common stockholders by the weighted average number of common shares outstanding during each period. Diluted earnings per share is computed using the weighted average number of common shares plus the potentially dilutive effect of common stock equivalents issued and outstanding at the reporting date, using the treasury stock method. Stock options, restricted stock and restricted stock units that are anti-dilutive are excluded from the computation of weighted average shares outstanding.

The following table sets forth the computation of basic and diluted earnings per share:

	<b>Three months ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
<b>Numerators:</b>		
Net income	\$ 8,916	\$ 8,361
<b>Denominators:</b>		
Basic weighted average common shares outstanding	31,445,592	29,620,218
Dilutive effect of share based awards	1,338,263	1,290,848
Diluted weighted average common shares outstanding	32,783,855	30,911,066
Weighted average common shares considered anti-dilutive in computing diluted earnings per share	338,237	611,069

**4. Segment Information**

The Company is organized around its outsourcing services and transformation services segments.

The chief operating decision maker generally reviews financial information at the consolidated statement of income level but does not review any information except for revenues and cost of revenues of the individual segments. Therefore, the Company does not allocate or evaluate depreciation, amortization, other income, capital expenditures and income taxes to its operating segments. Consequently, it is not practical to show assets, capital expenditures, depreciation or amortization by segment.

Revenues and cost of revenues for each of the three months ended March 31, 2012 and 2011 for the Company's outsourcing services and transformation services segments, respectively, are as follows:

	<b>Three months ended March 31, 2012</b>			<b>Three months ended March 31, 2011</b>		
	<b>Outsourcing Services</b>	<b>Transformation Services</b>	<b>Total</b>	<b>Outsourcing Services</b>	<b>Transformation Services</b>	<b>Total</b>
Revenues	\$ 89,734	\$ 14,874	\$ 104,608	\$ 56,841	\$ 16,066	\$ 72,907

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Cost of revenues (exclusive of depreciation and amortization)	56,478	10,194	66,672	34,235	9,984	44,219
<b>Gross profit</b>	<b>\$ 33,256</b>	<b>\$ 4,680</b>	<b>\$ 37,936</b>	<b>\$ 22,606</b>	<b>\$ 6,082</b>	<b>\$ 28,688</b>
Operating expenses			27,505			21,180
Other income, net			1,505			1,973
Income tax provision			3,020			1,120
<b>Net income</b>			<b>\$ 8,916</b>			<b>\$ 8,361</b>

**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)****March 31, 2012****(Unaudited)****(In thousands, except share and per share amounts)****5. Business Combinations, Goodwill and Intangible Assets**

On May 31, 2011, the Company completed its acquisition of Business Process Outsourcing Inc., a Delaware corporation formerly organized as a Cayman Islands exempted company (OPI), pursuant to a Merger Agreement, dated as of April 30, 2011 (the OPI Acquisition).

On October 1, 2011, the Company also acquired Trumbull Services, LLC. (Trumbull), a market leader in subrogation services for property and casualty insurance companies, from The Hartford Financial Services Group, Inc. (the Trumbull Acquisition).

**Goodwill**

The following table sets forth details of the Company's goodwill balance as of March 31, 2012:

	Outsourcing Services	Transformation Services	Total
Balance at January 1, 2011	\$ 26,585	\$ 16,785	\$ 43,370
Goodwill arising from OPI Acquisition	54,604		54,604
Currency translation adjustments	(5,687)		(5,687)
Balance at December 31, 2011	75,502	16,785	92,287
Currency translation adjustments	1,340		1,340
Balance at March 31, 2012	\$ 76,842	\$ 16,785	\$ 93,627

**Intangible Assets**

Information regarding the Company's intangible assets is as follows:

	As of March 31, 2012		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	\$ 33,146	\$ (5,284)	\$ 27,862
Leasehold benefits	3,626	(850)	2,776
Developed technology	2,133	(405)	1,728
Non-compete agreements	1,317	(813)	504
Trade names and trademarks	2,722	(502)	2,220
	\$ 42,944	\$ (7,854)	\$ 35,090



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	As of December 31, 2011		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	\$ 33,100	\$ (4,456)	\$ 28,644
Leasehold benefits	3,474	(668)	2,806
Developed technology	2,133	(351)	1,782
Non-compete agreements	1,316	(606)	710
Trade names and trademarks	2,722	(351)	2,371
	\$ 42,745	\$ (6,432)	\$ 36,313

Amortization expense for the three months ended March 31, 2012 and 2011 was \$1,394 and \$636, respectively. The weighted average life of intangible assets was 10.1 years for customer relationships, 6.8 years for leasehold benefits, 10.0 years for developed technology, 1.5 years for non-compete agreements and 3.0 years for trade names and trademarks excluding indefinite life trade names and trademarks. The Company had \$900 of indefinite life trade names and trademarks as of March 31, 2012 and December 31, 2011.

**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)****March 31, 2012****(Unaudited)****(In thousands, except share and per share amounts)**

<b>Estimated amortization of intangible assets during the year ending March 31,</b>	
2013	\$ 5,136
2014	\$ 4,373
2015	\$ 3,828
2016	\$ 3,728
2017	\$ 3,723

**6. Fair Value Measurements**

The following table sets forth the Company's assets and liabilities that were accounted for at fair value on a recurring basis as of March 31, 2012 and December 31, 2011. The table excludes short-term investments, accounts receivable, short-term borrowings, accounts payable and accrued expenses for which fair values approximate their carrying amounts.

**Assets and Liabilities Measured at Fair Value**

<b>As of March 31, 2012</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<b>Assets</b>				
Money market and mutual funds	\$ 42,685	\$	\$	\$ 42,685
Derivative financial instruments		960		960
Total	\$ 42,685	\$ 960	\$	\$ 43,645
<b>Liabilities</b>				
Derivative financial instruments	\$	\$ 9,694	\$	\$ 9,694
Total	\$	\$ 9,694	\$	\$ 9,694
<b>As of December 31, 2011</b>				
<b>Assets</b>				
Money market and mutual funds	\$ 42,067	\$	\$	\$ 42,067
Derivative financial instruments		32		32
Total	\$ 42,067	\$ 32	\$	\$ 42,099
<b>Liabilities</b>				
Derivative financial instruments	\$	\$ 17,729		