

MANAGEMENT DISCUSSION AND ANALYSIS

(forms part of the Directors' Report of the company's Annual Report FY2009-10; figures mentioned are on a consolidated basis unless otherwise mentioned)

- ❖ Overview of the industry and business environment
- ❖ Mastek's differentiated business model: Verticals focused, IP led
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Cautionary statement:

This Management Discussion and Analysis of the company's performance and outlook may contain forward-looking statements that set out anticipated performance based on the management's plans and assumptions. Its aim is to facilitate a better understanding of the company's prospects and make informed decisions. We cannot guarantee that any forward-looking statement will be realized, though we have been prudent in our plans and assumptions. The forward-looking statements are subject to risks, uncertainties and assumptions that could cause actual results to differ materially from those reflected in the forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management analysis only as of the date hereof. We do not undertake any obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise. For any further clarification please contact Mastek Investor Relations (investor.relations@mastek.com).

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OVERVIEW OF THE INDUSTRY AND BUSINESS ENVIRONMENT

The past couple of years have been substantially more challenging for the Indian IT industry, which had otherwise been enjoying robust growth year after year as the country successfully leveraged its vast talent pool to emerge as an enabler of efficiency and cost saving for client organizations.

The global economic crisis that unfolded during 2008 and spilled well into 2009, was characterized by a sharp slowdown in the global economy, pushing almost all major economies into the grip of recession, except for a handful of emerging nations like India and China. This in turn translated into lesser demand, lower prices, or both for the Indian IT industry. Macroeconomic upheavals also led to increased volatility in factors such as foreign currency exchange rates. It has taken substantial state interventions across many countries to obviate any further worsening of the situation and bring the world's financial system back on track.

There has been some improvement in global economic conditions during the latter half of 2009 and first half of 2010, with visible signs of recovery in most countries including the US. Such recovery, however, is still seen by some as tentative, with country or geography specific crises continuing to pop up unexpectedly. The Dubai debt crisis and the financial crisis in Greece as well as the Eurozone have been clear reminders that the world economy's recovery stands on shaky foundations and there is some way to go before we can expect sustained, healthy growth.

In the face of such conditions, India's IT Services exports increased to US\$27.3 billion during fiscal 2010 as per NASSCOM estimates, underlining the resilience of the Indian IT sector.

An interesting trend that has been emerging is the accelerated pace at which IT and IT-led solutions are being adopted within India, especially by the government at both central and local levels. A slew of e-governance initiatives and large transformational projects announced within the public sector are very encouraging signs for both the average citizen as well as the country's IT industry.

The international markets too are beginning to see an uptake in demand, coinciding with a revival in consumer confidence in those markets, although a certain degree of uncertainty and unpredictability remains.

On an overall basis and in comparison to the past year, these initial signs of demand recovery in global markets and increased IT spending within the domestic market are

undoubtedly positive developments. Yet, for our industry to rapidly grow from its current base and enhance its share of the global IT spend, it will need to effectively penetrate the higher-value consulting, systems integration, strategic application development, and solutions market where the benefits for customer organizations are much more than just cost advantages. This will also allow Indian players to generate better revenues, earnings, and growth with lesser human resource utilization, resulting in higher returns on the talent they employ. The better operating margins derived from such increased returns on talent can enable IT companies to absorb wage inflation or foreign exchange volatility impacts to a larger extent.

Whether the industry is able to make the successful transition from a mostly linear, services led model to a non-linear model led by intellectual property (IP) and solutions architecture capability will depend upon multiple factors. These include domain expertise across multiple industries, an organization culture that fosters creativity, and willingness to invest in developing intellectual property. There are few players in the Indian IT sector today with such a broad range of competencies.

Mastek, in a way, has been ready for the business environment that is now emerging, with strong enterprise architecture capabilities, program management skills, and a portfolio of IP-led offerings.

MASTEK'S DIFFERENTIATED BUSINESS MODEL: VERTICALS FOCUS, IP LED

Mastek's business model is characterized by a focus on IP and enterprise solutions, with a presence on verticals where it already has a solid track record and commands a competitive advantage over its peer set. Unlike most of the firms in the country's IT sector that rely chiefly on labour cost arbitrage and scale, Mastek has over the years developed the kind of skill-set and intellectual capabilities that are key to designing and delivering high-impact projects and solutions aimed at helping customers in their own transformational initiatives. The company's 90%+ on-time delivery record, in an industry where hardly 30% of large projects are delivered on time, is a key reason why its partners and customers retain their relationship with the company for an extended period of time and it is a partner of choice for several systems integrators (SIs).

During the past few years, Mastek has been consolidating its position as an IP-led solutions provider. The company has crystallized its focus on two verticals - Government and Insurance - and its new, more flexible version Elixir4™ platform for the insurance industry has entered into the implementation and migration phase in the UK. While it is in the process of creating a North America version of that

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platform, the company launched two modules for the North American market during the year under review - Elixir Distribution Management (EDM) and New Business & Underwriting (NB+U), with one client win for EDM already secured during the year. In July 2010, Mastek announced its second Elixir deal in North America with Foresters, a large life insurance provider, choosing it to be part of their transformational initiative.

Mastek's unique business model helps it generate industry-leading gross margins that reflect its superior quality of revenues, although it also necessitates relatively higher sales and marketing costs inherent to a solutions-led business, and R&D expenses towards intellectual property (IP) creation.

The various IP offerings that Mastek has today are mostly an outcome of pioneering investments made by the company, such as Elixir™. The company has also added IP assets to its stable by way of acquisitions, such as the STG Suite™, or through a co-creative process, such as Swift2Move™ which is co-owned by both Mastek and Thales.

Insurance vertical

Mastek's solutions for the insurance industry address both the life and non-life segments. The Insurance vertical delivered revenues of Rs 258.6 crore during FY2010, comprising more than 36% of overall revenues.

The company's Elixir platform and its variations such as the new Elixir4 and ElixirAsia as well as modules like EDM, and NB+U are designed to serve the life and annuity (L&A) segment in insurance.

For the property & casualty (P&C) segment of the insurance industry, the company offers the STG Suite, comprising the point of sale, policy administration, billing, and claims modules. Many of these solutions are well regarded within the market, which often gets reflected in opinions and views of industry analyst firms like Gartner, Novarica, and Celent as well.

Elixir™ is an IP created by Mastek on its own with significant investments made over a period of time, while the STG suite was acquired (in March 2008). This acquisition expanded Mastek's presence into the non life segment of the insurance vertical. The company had also acquired Vector Insurance Services in July 2007, which added "software as a service" (SaaS) and "process as a service" (PaaS) capabilities to Mastek's offerings basket in the L&A segment, and that has since been fully integrated within Mastek's overall L&A insurance operations.

Government vertical

Mastek has many years of experience in working closely with governments on large-scale, complex projects that

have made a valuable difference to millions of people. The company conceptualizes, architects, and delivers new technology based solutions that enable cities and countries to transform.

Although there could be different end-uses within the Government vertical, ranging from health and transportation to defence and education, there is a common set of underlying capabilities that comes into play each time the company undertakes an assignment in this vertical. These include the ability to work along with multiple other vendors on the project and manage large programmes. The company has created a database of metrics that enable it to better price and manage such programmes. It also has entered into, and grown, several partnerships in the UK, including one with Capita, where Mastek has a broader partnership covering the Insurance vertical as well, BT, with whom the company has been engaged on the NHS programme, and Thales, where the company created and now co-owns an intellectual property "Swift2Move" for the UK's Defence Information Infrastructure.

During the year under review, this vertical contributed Rs 196.7 crore to overall revenues, which is lower than Rs 336.7 crore last year chiefly due to the ramp-down of project development in the BT/NHS programme and a weaker pound sterling (given that most of the revenues in this vertical emanate from the UK).

Others

Mastek also derives a significant part of its business from customers that may not fall within the Insurance or Government verticals but are still important accounts from a strategic, historic relationship or long-term growth potential perspective. These include clients in other financial services and IT. The knowledge acquired by way of collaborating with some of these clients may enable the company to add new verticals to its offerings portfolio in the future. Some of these clients are also services-led, and there the company did face some pricing pressure during the year under review. The company plans to make efforts to try and compensate for that either through increased volumes or better pricing terms during the course of the next couple of years.

REVIEW OF FINANCIAL AND OPERATING PERFORMANCE

Financial performance review

The company's performance for the full financial year under review (FY 2010) includes the impact of adverse forex conditions (especially a weakened pound sterling), ramp-down of the remainder phase of the BT/NHS project development revenues by the end of the first quarter of FY2010, increased hiring, wage hikes implemented in the

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third quarter of the financial year and induction of multiple senior business leaders across geographies.

These factors impacted both revenues and margins. Resultantly, total income for the year was Rs 721.9 crore compared to Rs 964.9 crore last year. EBITDA for FY2010 was Rs 87.2 crore, lower than Rs 159.2 crore last year. Profit after Tax (PAT) was Rs 67.7 crore in FY2010, compared to Rs 141.2 crore in FY2009. Diluted EPS reported for the year under review is Rs 25.16.

The company continues to have a strong balance sheet, with Rs 198 crore in cash & equivalents (amounting to Rs 73.5 per share) as on 30 June 2010.

Operations review

Mastek made some progress during the year under review towards achieving its longer-term business objective and these are thus strategically quite significant. The company secured its first Elixir deal in North America, moved into the next phase of its relationship with Capita in the UK life and pensions marketplace, successfully launched ElixirAsia™ with a new win in Thailand, and initiated a partnership with Genpact.

- Update on Capita partnership in UK Life & Pensions market: Mastek's partnership with Capita in the UK Life and Pensions marketplace moved into the next phase focusing on customer implementations and migrations during the year. Towards this, Capita is taking a more active role in overseeing the development and it entered into an arrangement with Mastek to pay for the required development, implementation and support related services with an initial contract value of £25m over the next 24 months from date of agreement. The migration work began during the third quarter of FY2010 and is in progress, with the first go-live for Zurich Life happening in the last quarter of the year.
- New account wins for Elixir in North America: In January 2010, Mastek acquired the first customer for its Elixir™ Distribution Management offering in the North American market. Later, in July 2010, the company achieved another key milestone in North America for its Elixir platform for the insurance industry with Foresters, a large life insurance provider, choosing it as a technology partner in its transformational initiative. Initially, Mastek will be implementing its New Business and Underwriting (NB+U) solution for this client and will progressively leverage Mastek's insurance technology solutions in three major areas of business transformation - Policy Administration, New Business and Underwriting and Producer Portal, enabling the client to derive dramatic

cost savings in both policy acquisition and inforce maintenance. The successful implementation of NB+U will allow the client to leverage configurable rules engines and accelerate underwriting decisions and business processes, ensuring optimal efficiency with straight-through-processing wherever possible. With the Elixir Policy Administration System, the client will be capable of launching ground-breaking products across multiple distribution channels while maintaining both a low-risk business transformation and a low-cost of ownership. These developments represent an important breakthrough for the company, because while the company has already had multiple clients for Elixir™ offerings in various geographies, it did not have any in North America until these new wins. North America is the single largest market for enterprise solutions in insurance and thus remains a focus area for Mastek. Successful implementation for these new clients is likely to accelerate the company's penetration of this large and lucrative market.

- Strategic partnership with Genpact for insurance industry: Mastek's wholly-owned subsidiary in the US (MajescoMastek) and Genpact entered into a new strategic partnership focused on the insurance industry. The companies will offer joint IT and business process management solutions to large and mid-sized insurance carriers. In addition, both parties plan on developing innovative platform-based business process management solutions across the industry value chain including policy services, billing, claims, distribution management, and new business/underwriting. This partnership brings a new model to help transform insurance carriers' operations, leveraging both business process management and technology solutions.
- Tie-up with Focus Solutions: During the year under review, Mastek joined hands with Focus Solutions (the UK-based, AIM-listed provider of multi-channel distribution solutions to the global financial services industry) to deliver powerful, integrated front and back-office solutions to life & pension and wealth management organizations globally. Under the terms of the agreement, which will generate revenues for both the companies over 5 years, Mastek will become Focus Solutions' systems integrator for direct engagements with clients, providing Focus Solutions with scalable resource capabilities around the world. Mastek will also have the rights to distribute Focus Solutions' focus:360° product globally outside of the UK.
- Successful launch of ElixirAsia with a new win in Thailand: In August 2009, the company launched

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ElixirAsia, a platform for life insurance carriers in the Asia-Pacific region that will enable new carriers 'go live' with their businesses in 90 days. An out-of-the-box platform with ready to deploy pre-configured products, interfaces and reports, backed by a proven implementation methodology, ElixirAsia helps insurance carriers go live with their business in 3 months. Within a few months of launch, Mastek received confirmation to implement ElixirAsia Individual Life and Group Life Projects for an insurer based in Thailand.

- 12-month order book at end of year at Rs 306 crore: The company's 12-month order book as on 30th June 2010 was Rs. 306 crore, which is slightly higher than Rs 300 crore a year ago. The order book position did not witness a stronger expansion as the faster than expected BT/NHS project revenue rampdown and delays in initiation of some projects had an adverse impact on the orderbook size. The company plans to focus its sales effort towards consolidating and expanding its order book during the next financial year.
- Acquisition of Kognitio's Data Migration Offering: Mastek acquired the data migration offering from the UK-based Kognitio comprising its Data Factory Tool Kit (DFTK) and data migration methodology, which has long been considered the industry leader in data migration for the insurance market there. With over forty man years of development invested in its software, the DFTK solution provides the technology to support the end-to-end data management environment covering all aspects of data processing in a data migration project. This transaction was in line with Mastek's move towards strengthening its position as an IP-led enterprise solutions provider, with Kognitio's data migration tools and processes embedded at the heart of Mastek's Migration Centre of Excellence.
- Update on Board of Directors: The Mastek Board currently has 8 members, of which 4 are independent directors and the remaining 4 are founder directors. The Directors' Report in this Annual Report discusses the changes within the company's Board of Directors in greater detail.
- Update on leadership team: In a significant addition to its leadership team, the company has appointed Mr Mrinal Sattawala as Group President in July 2010. Mr Sattawala has close to 25 years of experience in the IT industry with an established track record in sales and operations, having held several key leadership roles in sales, marketing, business unit

management, and regional management. In his last role at Patni Computer Systems, Mr Sattawala was the Chief Operating Officer, responsible for the performance and management of all business units and functions. As Group President he will report to Mr Sudhakar Ram, the company's Chairman & Group CEO, and will lead the company's operations across its key geographies, playing an active role in expanding the opportunity pipeline in larger markets such as North America. Earlier during FY2010, Mr John Dowd, Group President & CEO, resigned from the organization. Mr Sudhakar Ram, the company's Chairman & Managing Director, has since taken over additional charge as Group CEO. In the UK, Mr Barry Yard, who had been driving the company's client engagement with BT Global Services was named Managing Director, Mastek UK.

- People: As on 30th June 2010, the company had a total of 3,243 employees, of which about 24% were based on-site while the rest were at various offshore locations. The company has resumed recruitment of fresh talent and intends to add more technical resources at various levels during the new fiscal. In the fourth quarter of the year under review, the company also decided upon a wage increase for its junior-to-middle level employees in the delivery, sales, and support functions. This increase in wages is to be implemented for employees in specified grades at both offshore and onsite locations, with the average increase likely to be approximately 20 per cent and 3.5 per cent, respectively. The revised compensation will come into effect starting July 1st, 2010. This initiative will enable the Company to retain and attract the kind of superior talent that is necessary given its focus on intellectual property (IP)-led and high-end IT solutions for global clients.

Recognitions and ratings

Mastek's efforts to emerge as a high-end IT solutions provider of choice have been gaining recognition, with some key ones summarized below:

- Ranked fastest growing P&C insurance billing solution provider in U.S. market: The company's STG Billing Solution has been recognized as the most widely used Property & Casualty insurance billing solution in the US market by Novarica, a research and advisory firm focused on markets, operations, and technology for insurers and wealth management firms. This was reported in Novarica's report titled "U.S. Property/Casualty Billing Solutions 2010 (Q1)," released in January 2010.

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- Mastek rated 'promising' in Gartner's ICM Marketscope: The leading analyst firm Gartner, in its research report, "MarketScope for Insurance Incentive Compensation Management Applications" published on December 16, 2009, rated Mastek as "promising" after evaluating vendors operating in the ICM solutions space. Mastek's Elixir Distribution Management (EDM) offering is a play in this particular space.
- Celent recognizes success of Mastek's ElixirAsia policy administration system: In a recent report "Asian Policy Administration Systems 2009 - Life and Pensions ABCD Vendor View" issued during the year under review by Celent, the company's ElixirAsia enterprise-wide policy administration system was well rated on several parameters. The company received a good rating, based upon customer feedback, on the product design/development, rating, policy issue, policy service, disbursements, billing and premium accounting, workflow, forms and correspondence functions.

BUSINESS OUTLOOK

During FY 2011, the company intends to build upon the progress made by it on the operational and strategic fronts in order to add new accounts, grow partnerships, and expand its order book noticeably. The company is also committed to restoring its margins and will be taking multiple steps during the next year to increase its productivity as well as operational efficiency. Mastek continually strives to develop strategic customer accounts and new partnerships where necessary, and this in turn should over time result in better quality of revenues and

much deeper client engagement. The company's leadership team remains fully aligned to the long term vision and growth strategy. Implementation of Mastek's growth strategy is expected to get reflected in the company's performance in each of its chosen verticals and in its operating metrics going forward.

INTERNAL CONTROL SYSTEMS AND RISK MANAGEMENT

Mastek's systems for internal control and risk management go beyond what is mandatorily required to cover best practice reporting matrices and to identify opportunities and risks with regard to its business operations.

Internal control systems

The company has mechanisms in place to establish and maintain adequate internal controls over all operational and financial functions. The company intends to undertake further measures as necessary in line with its intent to adhere to procedures, guidelines, and regulations as applicable in a transparent manner.

Mastek maintains adequate internal control systems that provide, among other things, reasonable assurance of recording the transactions of its operations in all material respects and of providing protection against significant misuse or loss of company assets. The company uses an enterprise resource planning (ERP) package that enhances the efficiency of its internal control mechanism.

The company's internal control systems are supplemented by an internal audit program and periodic reviews by the management. Mastek has appointed an independent audit firm as its Internal Auditors, and the Audit Committee



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reviews its findings and recommendations at periodic intervals.

Mastek's internal control system is adequate considering the nature, size and complexity of its business.

Management of risks and concerns

Mastek has a risk management framework that enables active monitoring of the business environment and identification, assessment and preemption or mitigation of potential internal or external risks. The company's risk management process encompasses five major activities:

- Risk identification and assessment
- Risk management and monitoring
- Exploiting risk to create opportunities
- Risk control and reporting
- Integrating with business strategy to keep ahead

Mastek is creating a more robust enterprise-wide risk management system with a governance and reporting framework that should help the company adapt to an increasingly volatile operating environment. As summarized in the chart above, the company's efforts include collation of detailed risk registers for each of its operating units and corporate functions, reviewing them at specified intervals on a regular basis, and formulating strategies aimed at avoidance or mitigation of identified risks. The risk reporting, review and monitoring process, which includes active participation of the senior leadership team and Board, is designed to enable the company operate effectively under varying conditions.

A discussion of key risks and concerns, and measures aimed at mitigating them, are discussed in the following paragraphs.

- ✧ *Strategic risks:* The company could be susceptible to strategy, innovation, and business or product portfolio related risks if there is any significant and unfavourable shift in industry trends, customer preferences, or returns on R&D investments. Mastek does have the benefit of being very entrenched with many of its customers, involved in their critical and strategic initiatives. Therefore, client concentration related risks are mitigated to an extent. The company's investments in intellectual property creation too are being done in a measured manner and are focused more on extending and strengthening existing offerings rather than on new business or end-use/application areas.
- ✧ *Macro-economic risks:* Risks emanating from changes in the global markets such as the recent financial meltdown, regulatory or political changes, and alterations in the competitive landscape could affect the company's operations and outlook. Any adverse movements in economic cycles in the company's target markets and volatility in foreign currency exchange

rates could have a negative impact on the company's performance. This risk is mitigated to some extent due to the company's presence in multiple, diverse markets from Europe to Malaysia and India. The company also takes necessary steps such as forex hedging to mitigate exchange rate risks.

- ✧ *Competition-led risks:* Mastek operates in a highly competitive industry, replete with much bigger competitors, in both India and abroad. Shifts in clients' and prospective clients' dispositions could affect its business. Changes in the pricing policy of competition could also lead to factors that may affect the company's profitability. While the company has strong domain expertise, robust delivery capabilities, and significant project experience, there is no guarantee that it will always get the better of competition.
- ✧ *Client and account risks:* The company's strategy is to engage with a few strategic customers and build long-term relationships with them. Any shift in customer preferences, priorities, and internal strategies can have an adverse impact on the company's operations and outlook. Mastek does have the benefit of being very entrenched with many of its customers, involved in their critical and strategic initiatives. Therefore, client concentration related risks are mitigated to an extent.
- ✧ *Contractual, execution and delivery related risks:* The company's operating performance is subject to risks associated with factors that may be beyond its control, such as the termination or modification of contracts and non-fulfillment of contractual obligations by clients due to their own financial difficulties or changed priorities or other reasons. Mastek does have mechanisms in place to try and prevent such situations, as well as insurance cover as necessary.
- ✧ *Acquisition/M&A related risks:* The company's growth strategy involves both organic and inorganic initiatives. Realizing the synergies of an M&A transaction involves addressing various aspects right from appropriate due diligence and proper integration to managing clients and the organizational culture. The entire process carries a wide range of risks that will need to be efficiently dealt with. The company would undertake all due care during any such transaction but these risks may not completely eliminated.

In addition to the aforementioned issues, there are multiple other risk factors that the company believes it will need to take cognizance of and manage. The Board and management team continually assess the operations and operating environment to identify potential risks and take meaningful mitigation actions. The company does take necessary insurance or related cover in cases as necessary.