THE VALUE CREATION PROSPECTS AND STRATEGIES THROUGH ECONOMIC VALUE ADDED (EVA) MODEL
- A CASE STUDY OF INFOSYS TECHNOLOGIES LTD

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Abstract

Economic Value Addition (EVA) developed by Stern, Stewart a US based consulting firm is a measure of corporate value creation. This measure tells the company whether the management of a company generates returns that cover the opportunity cost of scarce capital. EVA is the financial performance measure that aims to capture the true economic profit of an enterprise. It is developed to be a measure more directly linked to the creation of shareholder wealth over time. Hence, it helps company management to create value for shareholders and focuses on maximizing the shareholders’ wealth EVA refers to the net operating profits of the company less a charge for all capital invested in the company which is the opportunity cost.

The traditional performance measurements such as Return on investment ratio, Operating profit ratio and Earning per ratio etc. help the management to identify the unprofitable investment. Of course these ratios are precise and objective but they are less applicable in today’s modern and highly competitive business environment. The traditional financial measures are highly value based but fail to act as better indicators.

Moreover the traditional performance measures mainly focus on controlling overheads and enhancing employee productivity and they neglect the operational performance measures such as quality, responsiveness and flexibility. The EVA is an easy and effective way of understanding the economic reality. It shows the ultimate profitability of business and converts the critical accounting data into economic reality and facilitates the non- finance managers to understand the real value added. The present study basically aims to analyse the prospects of applying the Economic Value-Added (EVA) model for corporate valuation and using the same as a tool for value enhancement and an attempt is made to determine the economic value addition made by Infosys Technologies Ltd and the impact on its key financials.

Key words: Economic Value Addition, Harvesting, Throughput Accounting, Net operating profit, weighted average cost of capital, Risk free return

1. Introduction

A balance sheet discloses the financial position of a company. The financial position of an enterprise is influenced by the economic resources it controls, its financial structure, liquidity and solvency and its capacity to adapt to changes in the environment. However, it is becoming increasingly clear that intangible assets have a significant role in defining the growth of a hi-tech company. So quite often the search for the added value invariably leads the company to understanding, evaluating and enhancing the intangible assets of the business. EVA, developed by Stern, Stewart - a US based consulting firm is a measure of corporate value creation. This measure tells the company whether the management of a company generates returns that cover the opportunity cost of scarce capital. Economic Value Added (EVA) is the financial
performance measure that aims to capture the true economic profit of an enterprise. It is
developed to be a measure more directly linked to the creation of shareholder wealth
over time. EVA refers to the net operating profits of the company less a charge for all
capital invested in the company which is the opportunity cost. The EVA model is based on
accounting information but the model uses accounting data in a highly rationale manner for
taking key decisions. According to Erik Stern,
president international of Stern Stewart, “EVA
is not a metric but a way of thinking, a
mindset and while the language is technical,
the lifestyle is operational” (Finance and
Accounting, 2008). According to Steven
Orpurt, “One of the primary insights from the
EVA concept is recognition that growing
earnings does not necessarily increase firm
value or stock price. It focuses attention on
how a firm uses its capital by asking, “Is a
firm generating earnings above and beyond
that expected by the market (the providers
of the capital)”? (Finance and Accounting,
2008).

2. Objectives and Methodology

The present study basically aims to analyse
the prospects of applying the Economic
Value-Added (EVA) model for corporate
valuation and using the same as tool for value
enhancement. Following are the specific
objectives;

a) To analyse how far the Economic
Value-Added model converts the
critical accounting data into economic
reality

b) To study the value creation prospects
and strategies by adopting economic
value added model

c) To determine the Economic Value-
Added by Infosys Technologies Ltd
and the impact on its key financials.

Calculation:

EVA = Net Operating Profit after Taxes
(NOPAT) - {Capital X Cost of Capital}

“Capital” refers to the total capital employed
in the business and “Cost of capital” refers to
the weighted average cost of capital of funds
deployed

Assumptions:

Weighted Average Cost of Capital (WACC)
Grant Thornton has estimated the Weighted
Average Cost of Capital (WACC) based on the
weighted average cost of equity and debt. To
arrive at cost of equity, the Capital Asset
Pricing Model (CAPM) has been used, the
formula being ke = rf + b (rm - rf) where
ke= Cost of Equity, rf = Risk free Return,
rm= Market Rate of Return. Hence, rm - rf =
Risk Premium; b (beta) is the Measure of
Market Risk.

Risk free return has been estimated based on
10 year benchmark Government of India
Security as on the date of valuation, risk
premium based on long term stock market
returns and beta based on stock price
movements compared to index movement.

Capital Employed is the average of the
opening and closing balances of shareholders’
funds and outstanding debt.

3. Economic Value Added converts the
critical accounting data in to
economic reality

According to Drucker (1998), what we call
profits i.e. the money left to service equity, is
usually not profit at all. Until a business
returns a profit that is greater than its cost of
capital, it operates at a loss. Never mind that
it pays taxes as if it had a genuine profit. The
enterprise still returns less to the economy
than it devours in terms of resources. Until
then it does not create wealth, it destroys it.
The traditional accounting system helps to
measure the firm’s earning per share, return on equity, return on asset but such measures simply ignore the key element of cost of capital. But the Economic Value-Added model helps to measure firm’s true profitability. EVA, the difference between after-tax operating profits and the total cost of capital, is promoted as a measure of a company’s real profitability (Worthington, Andrew and West, Tracey 2001). The capital charge is the most distinctive and important aspect of EVA. Under conventional accounting, most organisations appear profitable, but many, in fact, are not creating value. (Shane Johnson 2007). A US based, Whole Foods Market started in the year 1980 in Austin, Texas which has become the world’s leader in natural and organic foods, with more than 270 stores in North America & United Kingdom has been adopting the EVA model for business decision and for determining incentive compensation. According to Wholesale Food Market Inc., the EVA is extensively used for capital investment decisions, including evaluating new store real estate decisions and store remodeling proposals. The Company invests in projects only that will add long-term value to the company. The EVA decision-making model also enhances operating decisions in stores of the company. The Whole Foods Market adopts EVA based incentive plan for its 750 senior executive leadership, regional leadership and the store leadership team (store team leaders and assistant store team leaders) in all stores. The Company measures the EVA contribution at the total company level, regional level, stores level, facility level and the team level. The Company believes using EVA in multi-dimensional approach, best measures the results of decisions made at different levels of the organisation. The Company expects EVA to remain a significant component of its compensation structure throughout the organisation in the coming years.

4. **Value creation prospects and strategies by adopting Economic Value Added Model**

The concept and application of EVA is reality as long as business entities want to achieve growth. Basically EVA emphasises on appropriate method of project appraisal, reduction of operating costs and tuning the entire organization towards innovation and optimum utilization of resources is the unique feature of this model. The product mix and service mix of the entity is purely based on economic sense. According to Stern, “Some may say that EVA was a fad of the 1990s, but earning more than the cost of capital is not a fad. It is what all companies should do all of the time. That they do not, is surprising. All of the talk on governance, also not a fad, never demanded this simple requirement. Until boards do, EVA will remain as reality as it was in the 1990s.” (Finance and Accounting, 2008) The data on this model is the ultimate guide for the investors in selecting the real growth firms for strengthening their investment portfolio.

5. **Focus on shareholders’ value and linking incentive plans with Economic Value Addition**

Focus on shareholders’ value is the key area of EVA model. The model focuses on profit and capital. All the business divisions are responsible for contributing towards economic value addition. The return from each division should be more than the cost of capital of that division. EVA also sets the expected return, the cost of capital, as a hurdle rate below which performance is unacceptable. (Justin Pettit (2001). The implementation of the model results in effective decentralization of accountability in the organization towards shareholders. Each and every level in the organization has to function in such a way that the economic value is added to shareholders. The practice of EVA concept requires well defined approach towards cost
of capital of various sources and this process helps the management in assessing the accurate profitability of project proposals. The shareholders appreciate when there is significant value addition and this stand of shareholders motivates the management in careful selection and successful execution of investment proposals. The e-commerce has given unimaginable new dimensions and abundant business opportunities in service sector. There is bright scope of adding significant economic value without making huge investment by identifying business opportunities in service sectors. New business models are often based on services, outsourcing, partnerships and other innovative ways of doing business. (Justin Pettit (2001). Moving towards the drivers of Economic Value-Added is important. The Corporate world adopted Stern Stewart’s EVA model and has greatly benefitted. Handling business activities with value addition objectives provides the platform for value based planning and employees motivation (G. Bennet Stewart 2002). According to Stern Stewart Study, the corporate that have implemented the EVA model successfully have achieved a higher level of performance compared to their peers; they have outperformed their peers by an average of 8.3% per annum over the five years following adoption and created total excess shareholder wealth of $116 billion. (G. Bennet Stewart 2002). Linking Economic Value-Added to incentive plan is an essential one. The success of the model mainly depends on the contributions of highly motivated human resources. Taking up challenging tasks, constantly adding new value to the activities so as to get back the desired value addition are highly possible when the employees are really motivated through EVA linked incentive plans. According to Stern Stewart study, the companies that have reinforced EVA as a performance measure and decision tool by tying management incentives to EVA have earned a 64.5% total return since the market peak and beat the S&P 500 by 91.3% whereas companies that used EVA only for performance measurement earned a 20.2% return and beat the market by 53.5%. (G. Bennet Stewart 2002).

6. Harvesting - Investments based on returns

The Harvesting is an important strategy in Economic Value-Added ® model. The investment in both long term assets and working capital are purely based on the expected value addition. If the expected rate of returns fails to add economic value, then the investments are not at all considered by the management. The existing investments are also subject to periodic appraisals. If the current investments fail to continue to generate economic value, such investments should be harvested through outright sales or curtailing investments.

7. Most accurate value addition performance

The EVA is considered as measure of “total factor productivity”. The selection of investment projects based on projected economic value addition becomes highly rationale and ensures the growth of the firm. Focusing on value addition enables the organization to understand the real growth drivers. Motivating employees through incentive plans based on value addition results in aligning the interest of employees with shareholders. Concentration on current and future value addition are very important. The management should concentrate on adding value through performance of the current activities and it should plan for improving the performance of future operations. Through innovation, controlling costs and inspiring employees, the overall efficiency can be improved. Identification of the value creation is an essential aspect of this model. The conventional way of measuring the performance through the accounting profit cannot help to identify the value creation. The model emphasis on
improving the returns above the opportunity cost of capital. Adopting sound pricing strategy leads to economic value. Pricing strategies adopted by the firm should be evaluated in terms of value addition. When the price elasticity of demand is negligible, the firm can leverage on its pricing policy. When slight price increase does not affect the demand the firm can go ahead and enhance its value addition.

8. Application of Throughput Accounting System

The traditional costing methods apportion the entire fixed overheads on the actual level of capacity utilized. When the actual output is less than the capacity, then the actual output level has to absorb the entire fixed costs including the cost of capital. The situation becomes worse if the actual output is intentionally reduced to trim down unprofitable products & customers, because the remaining products or customers have to absorb the entire fixed overheads. The result is that determining the true drivers becomes a difficult task. To overcome this problem, the EVA model advocates for adopting the Throughput Accounting, wherein the full costing is adopted by assuming cent percent capacity utilization. When utilization is less than 100%, a portion of overheads remain unallocated. Thus, volume variance does not impose any burden on either customer or product profitability (Justin Pettit, John Dower, Karl Pichler, Jorge Perez, 2001). The throughput accounting assumes that the profitability is independent of capacity utilization and this model helps to identify the profitability of customers and products accurately. The implementation of EVA model requires sound and accurate costing system. Each and every activity’s investment and the returns generated by it, is the key for measuring the exact value addition. Such segmented data analysis helps in identifying the drivers of value addition. Besides accurately measuring the various elements of cost, the apportionment of overhead cost on meaningful basis such as activity based costing, becomes essential. The optimum level of inventory should be fixed by considering the potential demand and cost of working capital but not wholly based on plant capacity or targeted cost per unit. Determination of the accurate opportunity cost of fixed asset is essential. The book-values of fixed assets shown in the balance sheets fail to indicate the actual opportunity cost of capital employed. The book values may be overstated or understated for other accounting reasons. Therefore for determining economic value added, the opportunity cost of fixed assets should be calculated on its net realizable value. Net realizable value (NRV) is a more accurate measure for the opportunity cost of fixed assets (Justin Pettit, John Dower, Karl Pichler, Jorge Perez, 2001). The net realizable value of a fixed asset is the expected salvage or liquidation value after meeting the required closure costs.

Analyzing the profitability of customers is another essential aspect. The value addition initiatives should be applied on all the business activities. The usual practices should be relooked from different angle. Firms normally prefer to supply to large customers for the sake of increasing sales and market share. But retaining large customers involves offering heavy trade discount, extending credit period and heavy inventory and all these eventually results in increased cost of working capital, customer default risk and less margin and ultimately lead to negligible value addition or sometimes negative value addition. Large customers have the power to force a supplier into longer terms, higher inventory requirements and lower margins (Justin Pettit, John Dower, Karl Pichler, Jorge Perez, 2001). The focus on customer segment should be based on the profitability and contribution to value addition.
9. Determination of Economic Value-Added by Infosys Technologies Ltd and the impact on its key financials

Background of Infosys Technologies Ltd

Infosys Technologies Ltd provides consulting and IT services to clients globally - as partners to conceptualize and realize technology driven business transformation initiatives. With over 100,000 employees worldwide, the company uses a low-risk Global Delivery Model (GDM) to accelerate schedules with high predictability.

As one of the pioneers in strategic offshore outsourcing of software services, Infosys has leveraged the global trend of offshore outsourcing. Even as many software outsourcing companies were blamed for diverting global jobs to cheaper offshore outsourcing destinations like India and China, Infosys was recently applauded by Wired magazine for its unique offshore outsourcing strategy; it singled out Infosys for turning the outsourcing myth around and bringing jobs back to the US.

<table>
<thead>
<tr>
<th>Table 1 Economic Value-Added by Infosys Technologies</th>
</tr>
</thead>
<tbody>
<tr>
<td>(In Rs.crore, except as otherwise stated)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
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<th></th>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Cost of capital</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Return on risk free investment (%)</td>
<td>7.0</td>
<td>8.00</td>
<td>8.00</td>
<td>7.50</td>
<td>6.80</td>
<td>5.20</td>
<td>6.0</td>
<td>7.3</td>
</tr>
<tr>
<td>Market premium (%)</td>
<td>7.0</td>
<td>7.00</td>
<td>7.00</td>
<td>7.00</td>
<td>7.00</td>
<td>7.00</td>
<td>7.0</td>
<td>7.0</td>
</tr>
<tr>
<td>Beta variant</td>
<td>0.74</td>
<td>0.76</td>
<td>0.99</td>
<td>0.78</td>
<td>0.98</td>
<td>1.27</td>
<td>1.57</td>
<td>1.41</td>
</tr>
<tr>
<td>Average debt / total capital (%)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Cost of debt - net of tax (%)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Average capital employed</td>
<td>16025</td>
<td>12,527</td>
<td>9,147</td>
<td>6,177</td>
<td>4,331</td>
<td>3,125</td>
<td>2493</td>
<td>1735</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Economic Value-Added</th>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating profits</td>
<td>6433</td>
<td>4,640</td>
<td>3,877</td>
<td>2,654</td>
<td>2,048</td>
<td>1,357</td>
<td>1079</td>
</tr>
<tr>
<td>Less: Tax</td>
<td>919</td>
<td>685</td>
<td>386</td>
<td>313</td>
<td>326</td>
<td>228</td>
<td>201</td>
</tr>
<tr>
<td>Cost of capital</td>
<td>1952</td>
<td>1,669</td>
<td>1,369</td>
<td>801</td>
<td>590</td>
<td>440</td>
<td>424</td>
</tr>
<tr>
<td>Economic Value-Added</td>
<td>3563</td>
<td>2,286</td>
<td>2,122</td>
<td>1,540</td>
<td>1,132</td>
<td>689</td>
<td>454</td>
</tr>
</tbody>
</table>

Source: The calculations are made as per the EVA Model from the financial figures taken from the Annual Reports of Infosys Technologies Ltd.

Note: 1. Cost of equity = return on risk-free investment + expected risk premium on equity investment adjusted for our beta variant in India

2. Figures above are based on consolidated Indian GAAP financial statements; Cash and cash equivalents includes investments in liquid mutual funds

3. Since the Company does not employ debt capital the average debt/total capital and cost of debt - net of tax columns are blank
Table 2: Economic Value-Added ® and the key financials of Infosys Technologies

<table>
<thead>
<tr>
<th>Year</th>
<th>EVA (in Rs Crores)</th>
<th>EPS (Rs)</th>
<th>Book value of equity (Rs)</th>
<th>Net worth (Rs in Crores)</th>
<th>Market capitalization (Rs in Crores)</th>
<th>Enterprise value (Rs in Crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>510</td>
<td>15.27</td>
<td>39.29</td>
<td>2080</td>
<td>24654</td>
<td>23627</td>
</tr>
<tr>
<td>2003</td>
<td>454</td>
<td>18.08</td>
<td>53.98</td>
<td>2861</td>
<td>26847</td>
<td>25163</td>
</tr>
<tr>
<td>2004</td>
<td>689</td>
<td>23.43</td>
<td>61.03</td>
<td>3253</td>
<td>32909</td>
<td>3036</td>
</tr>
<tr>
<td>2005</td>
<td>1132</td>
<td>34.63</td>
<td>96.87</td>
<td>5242</td>
<td>61073</td>
<td>58075</td>
</tr>
<tr>
<td>2006</td>
<td>1540</td>
<td>44.34</td>
<td>125.15</td>
<td>6897</td>
<td>82154</td>
<td>77445</td>
</tr>
<tr>
<td>2007</td>
<td>2122</td>
<td>67.82</td>
<td>195.41</td>
<td>11162</td>
<td>115307</td>
<td>109274</td>
</tr>
<tr>
<td>2008</td>
<td>2868</td>
<td>78.24</td>
<td>235.84</td>
<td>13490</td>
<td>82362</td>
<td>74055</td>
</tr>
<tr>
<td>2009</td>
<td>3563</td>
<td>101.65</td>
<td>310.9</td>
<td>17809</td>
<td>75837</td>
<td>64844</td>
</tr>
</tbody>
</table>

Source: Annual Reports of Infosys Technologies Ltd (From 2002-03 to 2008-09)

Table 3: Mean and Standard Deviation of the key financial variables of Infosys Technologies

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>EVA Rs in Crores</td>
<td>1537.0000</td>
<td>1076.94396</td>
</tr>
<tr>
<td>EPS Rs</td>
<td>47.9325</td>
<td>31.50481</td>
</tr>
<tr>
<td>Book value Rs in Crores</td>
<td>139.8088</td>
<td>98.06777</td>
</tr>
<tr>
<td>Net worth Rs in Crores</td>
<td>7849.2500</td>
<td>5719.46455</td>
</tr>
<tr>
<td>Market capitalisation Rs in Crores</td>
<td>62642.8750</td>
<td>32355.59127</td>
</tr>
<tr>
<td>Enterprise value Rs in Crores</td>
<td>54439.8750</td>
<td>34828.47185</td>
</tr>
</tbody>
</table>

Source: Calculations are made based on the financial variables of Infosys Technologies

Table 4: Impact of Economic Value-Added on Earning Per Share (EPS) of Infosys Technologies

<table>
<thead>
<tr>
<th>Variables</th>
<th>Coefficients and ‘t’ ratios</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>3.406 (1.116)</td>
</tr>
<tr>
<td>EVA</td>
<td>0.029 (17.447)*</td>
</tr>
<tr>
<td>Adjusted R Square</td>
<td>0.98</td>
</tr>
<tr>
<td>F - Ratio</td>
<td>304.384</td>
</tr>
</tbody>
</table>

Source: Calculations are made based on the financial variables of Infosys Technologies

Notes:
1. Dependant variable: EPS.
2. Values in parentheses are t-ratios.
3. * means significant at 1%

Table 5 shows the impact of EVA, on the Book value of Infosys Technologies. The overall model is significant under one percent level. The value of adjusted ‘R’ square indicates the significant level of impact of EVA on the Book value of the Company. The ‘T’ value shows the significance of the

Source: Calculations are made based on the financial variables of Infosys Technologies

Notes:
1. Dependant variable: Book value Rs in Crores.
2. Values in parentheses are t-ratios.
3. * means significant at 1%
relationship between the two variables. The ‘B’ value (Coefficient) indicates the proportionate percentage of change between the variables.

**Table- 6: Impact of Economic Value-Added on Net worth of Infosys Technologies**

<table>
<thead>
<tr>
<th>Variables</th>
<th>Coefficients and ‘t’ ratios</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>-219.313 (-0.363)</td>
</tr>
<tr>
<td>EVA</td>
<td>5.250 (15.985)*</td>
</tr>
<tr>
<td>Adjusted R Square</td>
<td>0.97</td>
</tr>
<tr>
<td>F - Ratio</td>
<td>255.524</td>
</tr>
</tbody>
</table>

Source: Calculations are made based on the financial variables of Infosys Technologies

Notes:
1- Dependant variable: Net worth Rs in Crores
2- Values in parentheses are t-ratios.
3- * means significant at 1%

Table 6 reveals the impact of EVA on the Net worth of Infosys Technologies. The overall model is significant under one percent level. Since the adjusted ‘R’ square is 0.97 the level of impact of EVA on Net worth is very high. The ‘T’ value reveals the significant relationship between EVA and Net worth. The ‘B’ value (Coefficient) indicates that one percent increase in EVA results in 5.25% increase in Net worth.

**Table- 7: Impact of Economic Value-Added on Market capitalization of Infosys Technologies**

<table>
<thead>
<tr>
<th>Variables</th>
<th>Coefficients and ‘t’ ratios</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>29323.158 (1.879)</td>
</tr>
<tr>
<td>EVA</td>
<td>21.678 (2.553)**</td>
</tr>
<tr>
<td>Adjusted R Square</td>
<td>0.44</td>
</tr>
<tr>
<td>F - Ratio</td>
<td>6.517</td>
</tr>
</tbody>
</table>

Source: Calculations are made based on the financial variables of Infosys Technologies

Notes:
1- Dependant variable: Market capitalisation Rs in Crores.
2- Values in parentheses are t-ratios.
3- ** means significant at 5%

Table 7 shows the relationship between EVA and Market capitalization of Infosys Technologies and it is evident that the overall model is significant under 5% level. The Adjusted ‘R’ Square is 0.441 indicating that 44% of change in Market capitalization is due to the change in EVA. There is significant relation between EVA and Market capitalization as revealed by the ‘T’ value. From the ‘B’ values (Coefficient values) of 21.678 it is very clear that one percent increase in EVA will result in 21.678% increase in Market capitalization.

**Table- 8: Impact of Economic Value-Added ® on Enterprise value of Infosys Technologies**

<table>
<thead>
<tr>
<th>Variables</th>
<th>Coefficients and ‘t’ ratios</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>21614.692 (1.186)</td>
</tr>
<tr>
<td>EVA</td>
<td>21.357 (2.154)**</td>
</tr>
<tr>
<td>Adjusted R Square</td>
<td>0.34</td>
</tr>
<tr>
<td>F - Ratio</td>
<td>4.640</td>
</tr>
</tbody>
</table>


Notes:
1- Dependant variable: Enterprise value Rs in Crores.
2- Values in parentheses are t-ratios.
3- ** means significant at 5%

Table 8 highlights the impact of EVA on the Enterprise value of Infosys Technologies. The overall model is significant under five percent level. The adjusted ‘R’ square of 0.34 indicates the level of impact of EVA on the Enterprise value of the Company. The ‘T’ value reveals the significance of the relationship between the two variables. The ‘B’ value (Coefficient) indicates that one percent increase in EVA will results in 21.35% increase in Enterprise value of the Company.
10. Initiatives of Infosys Technologies to enhance Value addition

Infosys Technologies focus on long-term partnerships with its clients while addressing their IT requirements. This strategy helps the Company to achieve high levels of clients’ satisfaction. The Company derived 97.6% of its revenue from repeat business during the year 2008-09. (Directors Report, AR 2008-09). Infosys continues its journey of excellence with critical focus on quality and productivity with significant investments in quality development programmes. In September 2008, Infosys Australia became one of the country’s first IT Services Company to achieve the Software Engineering Institute’s CMMI Level 5 Version 1.2, the highest standard available, apart from continued focus and surveillance audits in ISO Certification. (Directors Report, AR 2008-09). The Company is able to build powerful brand equity and is ranked as the 14th most respected company in the World by Reputation Institute (Directors Report, AR 2008-09). The Company is ranked as second in the Global Sourcing list of 100 best performing IT Service providers. Infosys was named the best Indian Company in Corporate Governance by The Asset Magazine’s annual Corporate Governance Index 2008. Similarly the industry experts and analysts rate the Company highly for its key services and markets. Infosys is keen on developing leadership qualities among its employees. Hays Group and CEO Magazine ranked the company among the best company in the world for leadership qualities. The Company has made significant achievements in the areas of Corporate Governance, Corporations Partners progress, innovative strategy planning & execution capabilities and competitive differentiation marketing excellence. Infosys has been listed on Forbe’s Asian Fabulous 50 for the fourth consecutive year. The Company won the first ever RMMY Award for customer relationship management. The Company won awards for the best investor relations website and for best corporate governance practices in Investor Relations (IR) Global Ranking in APAC categories.

Infosys is particular in well planned capital expenditure to meet the expansion and modernization requirements. During 2008-09 the Company spent Rs 1177 crores against Rs 1370 Crores in the previous year for developing physical infrastructure, technological infrastructure and procurement of intangible assets.

Remarkably Infosys is one of the very few companies which is free from debt capital. The company is able to maintain sufficient cash to meet its strategic objectives. The sound liquidity condition really helps the company to balance over earning reasonable returns and manage financial and business risks. The efficient working capital management of the company helps to make a rapid shift in direction. During the fiscal year 2009, internal cash flows have more than adequately covered working capital requirements, capital expenditure, investment in subsidiaries and dividend payments, leaving a surplus of Rs 2600 Crores. As at March 31st 2009, the Company had liquid assets of Rs 10,289 Crores as against Rs 7689 Crores in the previous year end. (Directors Report, AR 2008-09) These funds have been invested in deposits with banks and highly rated financial institutions.

Having realised the importance of human talents, Infosys is very particular in providing a conducive working environment, so as to ensure innovation and respect for merit. Through its successful scalable recruitment and human resources management processes, the Company is able to attract and retain the best talent. The Company’s strategy of recruitment of the best and brightest human assets from leading Academic Institutions across the globe, supported by intense training and
development has greatly helped to differentiate its performance from the peers.

The Global Delivery Model of the Company is keen on executing services in the most cost efficient manner and selling services in most profitable ways. The Company's Global Delivery Model is greatly supported by the large pool of highly skilled technology professionals, 24 hours execution capabilities across multiple time zones, the ability to accelerate delivery times of large projects and un-interpreted services. Infosys offer a complete end to end package of business solutions that facilitate leverage on technology and helps clients to achieve competitive edge and market differentiation. Infosys comprehensive service offerings to clients include; business and technology consulting, customer application development, infrastructure maintenance services, production support, package enabled consulting and implementation including enterprise solutions, product engineering solutions, product life cycle management, system integration, validation solutions, and software as service related solutions. These offerings are provided to clients located in various geographies and cross multiple industry verticals including banking and capital markets, insurance, communications, media, and entertainment, energy, utilities, manufacturing, aerospace, pharmaceuticals, health care and retail.

By building and strengthening enduring relationships with its clients, the company is successfully able to increase the business. The strategy for existing clients is to expand the nature and scope of services through enhancing number and size of projects. The strategy for new clients is to provide value added solutions through its in-depth industry expertise. The company's unique Global Delivery Model helps to build competitive edge over product engineering maintenance, infrastructure maintenance and business process management services. These services are basically long term in nature and require frequent client contact and eventually it results in ever lasting relationship with clients.

By establishing sales and marketing offices and global development centres, Infosys has expanded its presence in the global market. The company is further increasing its presence in China through Infosys China, in the Czech Republic and Eastern Europe directly and through Infosys BPO, in Australia through Infosys Australia and in Latin America through Infosys Mexico. This additional expansion really helps the company to serve the clients in the region and globe.

11. Conclusion

When EVA improves from year to year, the shareholders as well as the employees would be happy. The value addition is the outcome of improvement over operating efficiency. The following measures are recommended to enhance EVA further:

a) Measures should be taken to improve the operating profit by the core business activities. In fact a focus on core business will bring everlasting competitive edge to the organization.

b) Measures should be initiated to enhance operating profit without infusing additional capital. The existing resources should be utilized to the optimum extent. The value should be identified and undertaken.

c) Additional investments can be contemplated when there is potential to increase operating profits. Projects that can fetch a return more than cost of capital should be explored.

d) Capital should be withdrawn from projects which give less returns

e) The capital structure should be resigned to bring down the cost of capital.

Negative or negligible level of Economic Value-Added is an important signal to management to review the key strategies and operations. Just by seeing the negative value
addition, the Management must not shut down the operation of the division because the very cost of closure may be very high or the realizable value from the shut down division may be too low (Justin Pettit 2001). Though restructuring the operations, controlling cost, adding value to the product or service by innovation the ultimate value addition can be improved better.

The Management should emphasis across the organization for continuous innovation for improving sales, margins and minimizing the operating expenses. The EVA is the outcome of selection and successful implementation of highly profitable projects. To bring continuous innovation, investments in technology, expansion, modernization and restructuring are inevitable. However the screening of such investment proposals should be done from the point of view of expected contribution to value addition. Education and motivation of human resources across the organization towards achieving significant value addition is the major task. Designing an appropriate incentive policy based on EVA and proper education for the employees about the concept and key drivers will yield positive results. Motivation and relevant training for employees in identifying successfully handling innovative and challenging tasks are very much required.

EVA based bonus plan has gained a lot of significance and immense popularity in modern financial management system. It is considered as superior to traditional plan in measuring the performance. Many successful companies realized that the use of EVA sharpened their programmes. To implement bonus plan successfully, the employees at all levels of the organization must be trained in the very concept of EVA. They should be educated over the special features, advantages, the difference between traditional bonus plan and the EVA bonus plan and how it is calculated etc. Moreover the bonus plan should be designed in such a way that it aligns the interest of employees with share holders. The bonus plan should motivate the employees to think and act as share holders and the employees are to be compensated like share holders.

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