

ExlService Holdings, Inc.  
Form 10-Q  
May 10, 2010  
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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, 2010**

**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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<b>DELAWARE</b> (State or other jurisdiction of incorporation or organization)	<b>82-0572194</b> (I.R.S. Employer Identification No.)
<b>280 PARK AVENUE, NEW YORK, NEW YORK</b> (Address of principal executive offices)	<b>10017</b> (Zip code)
<b>(212) 277-7100</b> (Registrant's telephone number, including area 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 <input type="checkbox"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

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, 2010, there were 29,168,714 shares of the registrant's common stock outstanding (excluding 252,502 shares held in treasury and 270,012 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, 2010 (Unaudited)</b>	<b>December 31, 2009</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 99,240	\$ 132,215
Short-term investments	2,244	4,009
Restricted cash	298	65
Accounts receivable, net of allowance for doubtful accounts of \$626 at March 31, 2010 and \$262 at December 31, 2009	35,094	34,856
Deferred tax assets, net	4,444	4,872
Advance income-tax, net	935	
Prepaid expenses and other current assets	7,509	5,529
<b>Total current assets</b>	<b>149,764</b>	<b>181,546</b>
Fixed assets, net of accumulated depreciation of \$39,670 at March 31, 2010 and \$35,812 at December 31, 2009		
Restricted cash	7,461	3,895
Deferred tax assets, net	6,905	8,482
Intangibles, net of amortization	10,047	627
Goodwill	40,839	19,619
Other assets	13,781	11,487
<b>Total assets</b>	<b>\$ 257,031</b>	<b>\$ 249,620</b>
<b>Liabilities and Stockholders Equity</b>		
Current liabilities:		
Accounts payable	\$ 3,145	\$ 5,345
Deferred revenue	3,585	4,745
Accrued employee cost	11,452	16,020
Income taxes payable		543
Accrued expenses and other current liabilities	13,301	11,674
<b>Total current liabilities</b>	<b>31,483</b>	<b>38,327</b>
Non-current Liabilities	7,218	5,575
<b>Total liabilities</b>	<b>38,701</b>	<b>43,902</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, 29,339,538 shares issued and 29,092,508 shares outstanding as of March 31, 2010 and 29,278,103 shares issued and 29,031,073 shares outstanding as of December 31, 2009.	29	29
Additional paid-in capital	126,582	124,493
Retained earnings	91,297	85,674
Accumulated other comprehensive income/(loss)	1,378	(3,515)
	219,286	206,681
Less: 247,030 shares as of March 31, 2010 and December 31, 2009, held in treasury, at cost	(976)	(976)
ExlService Holdings, Inc. stockholders' equity	218,310	205,705
Noncontrolling interest	20	13
<b>Total stockholders' equity</b>	<b>218,330</b>	<b>205,718</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 257,031</b>	<b>\$ 249,620</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>2010</b>	<b>2009</b>
Revenues	\$ 54,489	\$ 40,986
Cost of revenues (exclusive of depreciation and amortization)	31,485	24,356
Gross profit	23,004	16,630
Operating expenses:		
General and administrative expenses	9,305	6,733
Selling and marketing expenses	4,150	3,184
Depreciation and amortization	3,073	2,430
Total operating expenses	16,528	12,347
Income from continuing operations	6,476	4,283
Other income/(expense):		
Foreign exchange gain/(loss)	606	(1,309)
Interest and other income, net	418	311
Income from continuing operations before income taxes	7,500	3,285
Income tax provision	1,877	263
Income from continuing operations	5,623	3,022
Income/(loss) from discontinued operations, net of taxes		(139)
Net income	\$ 5,623	\$ 2,883
Earnings per share:		
Basic	\$ 0.19	\$ 0.10
Diluted	\$ 0.19	\$ 0.10
Weighted-average number of shares used in computing earnings per share:		
Basic	29,128,741	28,843,190
Diluted	30,157,956	29,079,675

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>2010</b>	<b>2009</b>
Cash flows from operating activities		
Net income	\$ 5,623	\$ 2,883
Loss from discontinued operations, net of taxes		139
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,073	2,430
Share-based compensation expense	1,828	1,539
Non-employee stock options		71
Unrealized foreign exchange (gain)/loss	599	(373)
Deferred income taxes	(1,000)	(758)
Noncontrolling interest	7	
Change in operating assets and liabilities (net of effect of acquisitions):		
Restricted cash	(3,582)	(4)
Accounts receivable	(317)	2,491
Prepaid expenses and other current assets	926	(698)
Accounts payable	(161)	67
Deferred revenue	(1,166)	(27)
Accrued employee costs	(5,660)	(7,545)
Accrued expenses and other liabilities	1,269	(2,249)
Income taxes payable	(1,472)	(36)
Other assets	(818)	830
Net cash used for operating activities	(851)	(1,240)
Cash flows from investing activities		
Purchase of fixed assets	(5,385)	(5,013)
Business acquisition	(29,122)	
Proceeds from redemption of short-term investment	1,843	
Proceeds from sale of discontinued operations		1,448
Net cash used for investing activities	(32,664)	(3,565)
Cash flows from financing activities		
Principal payments on capital lease obligations	(36)	(27)
Proceeds from exercise of stock options	261	
Acquisition of treasury stock		(45)
Net cash provided by/(used for) financing activities	225	(72)
Effect of exchange rate changes on cash and cash equivalents	315	(702)
Net increase/(decrease) in cash and cash equivalents	(32,975)	(5,579)

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Cash and cash equivalents, beginning of period	132,215	112,174
Cash and cash equivalents, end of period	\$ 99,240	\$ 106,595

See accompanying notes



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**EXLSERVICE HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**March 31, 2010**

**(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 and with 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, 2009.

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 these periods. 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.

Certain amounts in the prior year's financial statements and related notes have been reclassified to conform to the 2010 presentation.

**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 minority interest represents the minority partner's interest in the operation of exlService.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 minority partner's interest in the operations for the three months ended March 31, 2010 and 2009 was \$7 and \$0, respectively, 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, future obligations under 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.

***Recent Accounting Pronouncements***

In January 2010, the Financial Accounting Standards Board ( FASB ) issued Update No. 2010-6, *Improving Disclosures about Fair Value Measurement* ( ASU 2010-6 ) to amend the disclosure requirements related to recurring and nonrecurring fair value measurements. The guidance requires new disclosures on the transfers of assets and liabilities between Level 1 (quoted prices in active market for identical assets or liabilities) and Level 2 (significant other observable inputs) of the fair value measurement hierarchy, including the reasons and the timing of the transfers. Additionally, the guidance requires a roll forward of activities on purchases, sales, issuance, and settlements of the assets and liabilities measured using significant unobservable inputs (Level 3 fair value measurements). This guidance is effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures regarding Level 3 fair value measurements which are effective for fiscal years beginning after December 15, 2010. The adoption of this new guidance did not have a material impact on the Company's unaudited consolidated financial statements. See Note 6 for further details.

In September 2009, the FASB issued Update No. 2009-13, *Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force* ( ASU 2009-13 ). It updates the existing multiple-element revenue arrangements guidance currently included under ASC topic 605-25, which originated primarily from the guidance in EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables* ( EITF 00-21 ). The revised guidance primarily provides two significant changes: 1) eliminates the need for objective and reliable evidence of the fair value for the undelivered element in order for a delivered item to be treated as a separate unit of accounting, and 2) eliminates the residual method to allocate the arrangement consideration. In addition, the guidance also expands the disclosure requirements for revenue recognition. ASU 2009-13 will be effective for the first annual reporting period beginning on or after June 15, 2010, with early adoption permitted provided that the revised guidance is retroactively applied to the beginning of the year of adoption. The Company has chosen to adopt the new guidance from January 1, 2011. Currently there is no impact from the adoption of ASU 2009-13 as the Company currently does not have any multiple-deliverable revenue arrangements.

**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****March 31, 2010****(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.

Any cash or in-kind dividends paid with respect to unvested shares of restricted stock and restricted stock units are withheld by the Company and paid to the holder of such shares of restricted stock, without interest, only if and when such shares of restricted stock and restricted stock units vest. Any unvested shares of restricted stock and restricted stock units are immediately forfeited without consideration upon the termination of holder's employment with the Company or its affiliates. Accordingly, the Company's unvested restricted stock and restricted stock units do not include non-forfeitable rights to dividends or dividend equivalents and are therefore not considered as participating securities for purposes of earnings per share calculations pursuant to the two-class method. However, the Company's vested restricted stock units against which the underlying common stock has not been issued, contain non-forfeitable rights to dividends or dividend equivalents and are therefore after vesting considered as participating securities for the purposes of computing basic earnings per share pursuant to the two-class method. Application of this treatment had an insignificant effect on the computation of basic earnings per share.

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

	<b>Three months ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
<b>Numerators:</b>		
Net income available to common shareholders :		
Continuing operations	\$ 5,623	\$ 3,022
Discontinued operations		(139)
	\$ 5,623	\$ 2,883
<b>Denominators:</b>		
Basic weighted average common shares outstanding	29,128,741	28,843,190
Dilutive effect of share based awards	1,029,215	236,485
Diluted weighted average common shares outstanding	30,157,956	29,079,675
Weighted average common shares considered anti-dilutive in computing diluted earnings per share	1,328,643	3,103,074

**4. Segment Information**

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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, interest expense or 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, 2010 and 2009 for outsourcing services and transformation services segments, respectively, are as follows:

	Three months ended March 31, 2010			Three months ended March 31, 2009		
	Outsourcing Services	Transformation Services	Total	Outsourcing Services	Transformation Services	Total
Revenues	\$ 41,590	\$ 12,899	\$ 54,489	\$ 33,393	\$ 7,593	\$ 40,986
Cost of revenues (exclusive of depreciation and amortization)	23,579	7,906	31,485	18,261	6,095	24,356
Gross profit	\$ 18,011	\$ 4,993	\$ 23,004	\$ 15,132	\$ 1,498	\$ 16,630
Operating expenses			16,528			12,347
Other income/(expense)			1,024			(998)
Income tax provision			1,877			263
Income from continuing operations			5,623			3,022
Income/(loss) from discontinued operations, net of taxes						(139)
Net income			\$ 5,623			\$ 2,883

**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****March 31, 2010****(Unaudited)****(In thousands, except share and per share amounts)****5. Business Combinations, Goodwill and Intangible Assets**

On March 1, 2010, we acquired the operations of the American Express Global Travel Service Center, a business unit of American Express located in Gurgaon, India, that provides the travel-related business process outsourcing services of American Express. The purchase price of the transaction, which was paid in cash, was approximately \$29,122.

The Company made a preliminary allocation of the purchase price to the tangible and intangible assets and liabilities acquired, based on their fair values, as mentioned below:

Tangible fixed assets	\$ 2,897
Current assets and liabilities, net	(1,459)
Customer related intangible assets	8,065
Leasehold benefits	1,289
Goodwill	20,672
Deferred tax liabilities, net	(2,342)
	<b>\$ 29,122</b>

Under ASC topic 805, *Business Combinations* (ASC No. 805), the preliminary allocation of the purchase price to the tangible and intangible assets and liabilities acquired may change up to a period of one year from the date of acquisition. The customer relationship is being amortized over a life of ten years and the leasehold benefits are being amortized over the remaining period of the lease (approximately three years).

**Goodwill**

The following table sets forth details of the Company's goodwill balance as of March 31, 2010:

	Outsourcing Services	Transformation Services	Total
Balance at January 1, 2009	\$ 772	\$ 16,785	\$ 17,557
Goodwill arising from acquisition	2,062		2,062
Balance at December 31, 2009	2,834	16,785	19,619
Goodwill arising from acquisition	20,672		20,672
Currency translation adjustments	548		548
Balance at March 31, 2010	\$ 24,054	\$ 16,785	\$ 40,839

**Intangible Assets**

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

	<b>As of March 31, 2010</b>		
	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Net Carrying Amount</b>
Customer relationships	\$ 9,072	\$ (322)	\$ 8,750
Leasehold benefits	1,323	(26)	1,297
	<b>\$ 10,395</b>	<b>\$ (348)</b>	<b>\$ 10,047</b>

	<b>As of December 31, 2009</b>		
	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Net Carrying Amount</b>
Customer relationships	\$ 794	\$ (167)	\$ 627
	<b>\$ 794</b>	<b>\$ (167)</b>	<b>\$ 627</b>

Amortization expense for the three months ended March 31, 2010 and 2009 was \$181 and \$0, respectively. The estimated amortization of intangible assets for the years ending March 31, 2011, 2012, 2013, 2014 and 2015 is \$1,567, \$1,418, \$1,269, \$896 and \$828, respectively.

**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****March 31, 2010****(Unaudited)****(In thousands, except share and per share amounts)****6. Fair Value Measurements**

ASC topic 820, *Fair Value Measurements and Disclosures* (ASC No. 820) defines fair value as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk, including the Company's own credit risk.

ASC No. 820 establishes a three-level hierarchy of fair value measurements based on whether the inputs to those measurements are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. The fair-value hierarchy requires the use of observable market data when available and consists of the following levels:

Level 1 Quoted prices for identical instruments in active markets;

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets; and

Level 3 Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

The following table sets forth the Company's assets and liabilities that were accounted for at fair value as of March 31, 2010. The table excludes short-term investments, accounts receivable, accounts payable and accrued expenses for which fair values approximate their carrying amounts.

**Assets and Liabilities Measured at Fair Value**

	Level 1	Level 2	Level 3	Total
<b>Assets</b>				
Money market and mutual funds	\$ 80,900	\$	\$	\$ 80,900
Derivative financial instruments		5,729		5,729
Total	\$ 80,900	\$ 5,729	\$	\$ 86,629
<b>Liabilities</b>	\$	\$	\$	\$

*Derivative Financial Instrument:* The Company's derivative financial instruments consist of foreign currency forward exchange contracts. Fair values for derivative financial instruments are based on broker quotations and are classified as Level 2. See Note 7 for further details.

**7. Derivatives and Hedge Accounting**

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The Company actively looks to mitigate the exposure of foreign currency market risk by entering into various hedging transactions, authorized under Company policies, with counterparties that are highly rated financial institutions. The Company's primary exchange rate exposure is with the Indian rupee. The Company uses derivative instruments for the purpose of mitigating the underlying exposure from foreign currency fluctuation risks associated with forecasted transactions denominated in certain foreign currencies and to minimize earnings and cash flow volatility associated with changes in foreign currency exchange rates, and not for speculative trading purposes. These derivative financial instruments are largely forward foreign exchange contracts that are designated effective and that qualify as cash flow hedges under ASC topic 815, *Derivatives and Hedging* (ASC No. 815). The Company also uses derivatives consisting of foreign currency exchange contracts not designated as hedging instruments under ASC No. 815 to hedge intercompany balances and other monetary assets or liabilities denominated in currencies other than the functional currency.

The Company had outstanding foreign exchange contracts totaling \$105,688 and GBP 8,758 as of March 31, 2010 and totaling \$90,000 and GBP 7,662 as of December 31, 2009. The Company estimates that approximately \$3,675 of net derivative gains included in accumulated other comprehensive income (AOCI) could be reclassified into earnings within the next twelve months based on exchange rates prevailing as of March 31, 2010. At March 31, 2010, the maximum outstanding term of derivative instruments that hedge forecasted transactions was thirty-three months.

The Company evaluates hedge effectiveness at the time a contract is entered into as well as on an ongoing basis. If during this time, a contract is deemed ineffective, the change in the fair value is recorded in the unaudited consolidated statements of income and is included in foreign exchange gain/(loss). For hedge relationships that are discontinued because the forecasted transaction is not expected to occur by the end of the originally specified period, any related derivative amounts recorded in equity are reclassified to earnings. No significant amounts of gains or losses were reclassified from AOCI into earnings as a result of forecasted transactions that failed to occur during the three months ended March 31, 2010.



**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****March 31, 2010****(Unaudited)****(In thousands, except share and per share amounts)**

The following tables set forth the fair value of the foreign currency exchange contracts and their location on the unaudited consolidated financial statements:

*Derivatives designated as hedging instruments:*

	March 31, 2010	December 31, 2009
<b>Prepaid expenses and other current assets:</b>		
Foreign currency exchange contracts	\$ 3,675	\$ 1,451
<b>Other assets</b>		
Foreign currency exchange contracts	\$ 2,039	\$ 957

*Derivatives not designated as hedging instruments:*

	March 31, 2010	December 31, 2009
<b>Prepaid expenses and other current assets:</b>		
Foreign currency exchange contracts	\$ 15	\$ 62

The following tables set forth the effect of foreign currency exchange contracts on the unaudited consolidated statements of income for the three months ended March 31, 2010 and 2009:

Derivatives in Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in AOCI on Derivative (Effective Portion)		Location of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)		Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing)	
	2010	2009		2010	2009		2010	2009
Foreign exchange contracts	\$ 2,955	\$ (3,926)	Foreign exchange gain/(loss)	\$ 589	\$ (1,415)	Foreign exchange gain/(loss)	\$	\$ (42)

Derivatives Not Designated as Hedging Instruments	Amount of Gain or (Loss) Recognized in Income on Derivatives	
	2010	2009

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Foreign exchange contracts	Foreign exchange gain/(loss)	\$ 975	\$ (469)
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**8. Comprehensive Income/(Loss):**

The following table sets forth the change in the components of comprehensive income/(loss) for the three months ended March 31, 2010 and 2009:

	<b>Three months ended</b>	
	<b>March 31,</b>	
	<b>2010</b>	<b>2009</b>
Net income available to common stockholders	\$ 5,623	\$ 2,883
Other comprehensive income/(loss):		
Unrealized gain/(loss) on effective cash flow hedges	2,366	(2,511)
Foreign currency translation adjustment	2,513	(2,058)
Retirement benefits	14	26
Total other comprehensive income/(loss)	4,893	(4,543)
Total comprehensive income/(loss)	\$ 10,516	\$ (1,660)

**Table of Contents****EXLSERVICE HOLDINGS, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****March 31, 2010****(Unaudited)****(In thousands, except share and per share amounts)****9. Employee Benefit Plans**

The Company's Gratuity Plan provides a lump sum payment to vested employees on retirement or on termination of employment in an amount based on the respective employee's salary and years of employment with the Company. Liabilities with regard to the Gratuity Plan are determined by actuarial valuation using the projected unit credit method. Current service costs for the Gratuity Plan are accrued in the year to which they relate. Actuarial gains or losses or prior service costs, if any, resulting from amendments to the plans are recognized and amortized over the remaining period of service of the employees.

Net gratuity cost includes the following components:

	<b>Three months ended</b>	
	<b>March 31,</b>	
	<b>2010</b>	<b>2009</b>
Service cost	\$ 125	\$ 65
Interest cost	30	27
Actuarial loss	42	17
Net gratuity cost	\$ 197	\$ 109

The Company maintains both the ExlService Inc. 401(k) Plan and the Inductis 401(k) Profit Sharing Plan, (the 401(k) Plans) under Section 401(k) of the Internal Revenue Code of 1986 covering all eligible employees. The Company may make discretionary contributions of up to a maximum of 3% of employee compensation within certain limits. The Company's contribution to the 401(k) Plans amounted to \$77 and \$82 during the three month period ended March 31, 2010 and March 31, 2009, respectively.

During the three months period ended March 31, 2010 and 2009, the Company contributed the following amounts to various defined contribution plans on behalf of its employees in India, the Philippines, Romania and the Czech Republic:

Three months ended March 31, 2010	\$ 833
Three months ended March 31, 2009	\$ 439

**10. Leases**

The Company leases motor vehicles for some of its employees. Such leases are recorded as capital leases. Future minimum lease payments under these capital leases at March 31, 2010 are as follows:

Year ending March 31, 2011	\$ 207
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2012	103
2013	95
Total minimum lease payments	405
Less: amount representing interest	39
Present value of minimum lease payments	366
Less: current portion	184
Long term capital lease obligation	\$ 182

The Company conducts its operations using facilities leased under non-cancelable operating lease agreements that expire at various dates. Future minimum lease payments under non-cancelable operating lease agreements expiring after more than twelve months are as follows:

Year ending March 31,	
2011	\$ 5,501
2012	4,102
2013	3,148
2014	1,292
2015	526
2016 and thereafter	2,199
	\$ 16,768

The operating leases are subject to renewal periodically and have scheduled rent increases. The Company accounts for scheduled rent on a straight line basis over the lease period. Rent expense under both cancelable and non-cancelable operating leases was \$1,848 and \$1,257 for the three months ended March 31, 2010 and 2009, respectively. Deferred rent as of March 31, 2010 and December 31, 2009 was \$1,779 and \$1,437, respectively, and is included in Accrued expenses and other current liabilities in the unaudited consolidated balance sheet as of March 31, 2010 and the audited balance sheet as of December 31, 2009.

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**EXLSERVICE HOLDINGS, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**March 31, 2010**

**(Unaudited)**

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

**11. Income Taxes**

The Company recorded income tax expense of \$1,877 and \$263 for the three months ended March 31, 2010 and 2009, respectively. The effective rate of taxes attributable to continuing operations was 25.0% and 8.0% for the three months ended March 31, 2010 and 2009, respectively.

Certain units of the Company's Indian subsidiaries qualify for an exemption from taxable income under Section 10A or 10B of the Indian Income Tax Act, because their profits are attributable to work performed in Export Processing Zone