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KPIT

EIGHTH ANNUAL REPORT 1998-99

KPIT Systems Limited

KPIT

Contents

Board & Management

Board Members

S. B. (Ravi) Pandit	Chairman
Ajay B. Bhagwat	Director
Dr. Vijay Bhatkar	Director
Dr. Naushad Forbes	Director
Shailesh V Haribhakti	Director
Sudheer Tilloo	Director
S. M. Patwardhan	Technical Director
Kishor Patil	Managing Director

Board Committees

Compensation Committee

Sudheer Tilloo	Committee Chairman
Dr. Vijay Bhatkar	
Shailesh V Haribhakti	

Audit Committee

Shailesh V Haribhakti	Committee Chairman
Dr. Naushad Forbes	
Sudheer Tilloo	

Management Team

Marketing

Sachin Tikekar	Head - US operations
Myles O'Connor	Director Projects and Services - UK
Pankaj Sathe	Senior Business Manager - UK
Anita Ganapathi	Country Manager - ME
Abhijit Dandekar	Country Manager - India
Pervez Daver	*Senior Manager - Corporate Marketing*

Delivery System

Anil Kulkarni	Vice President and Head - Delivery System
S. M. Patwardhan	Head -Technology and Facility mgmt.
Satish Ranade	Head - Customer Delivery Unit 1
Prabodh Teredesai	Head - Customer Delivery Unit 2
Anuradha Kanitkar	Head - Customer Delivery Unit 3
L. V. Gaopande	Head - Customer Delivery Unit 4
Anup Sable	Head - Internet Technologies
Vilas Joshi	*Senior Manager - Quality Management*

ASTRA

Girish Sandhane	General Manager - ASTRA

Support

Anil Patwardhan	General Manager - Finance and Administration
Ganesh Sanker	General Manager - Organisation Development
S. Patanjali	Head - Resource Management

Auditors

M/s. Sanjiv Katkar and Associates,Chartered Accountants
"Raj-Vihar", Plot No. 38, Sahakarnagar No. 2, Pune – 411 009

Bankers

ICICI Banking Corporation Ltd. State Bank of India. Janata Sahakari Bank Ltd.
Bank of Maharashtra. Times Bank Ltd.

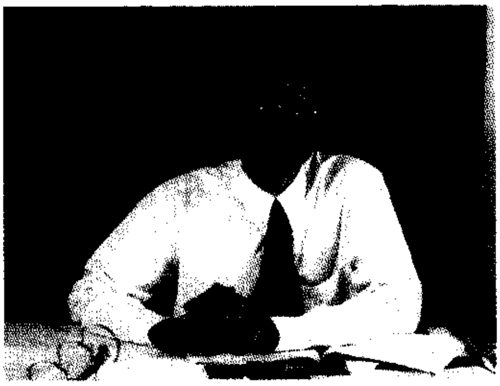
Financial Performance at a Glance

Particulars	1998-1999		1997-1998		1996-1997	
	USD Millions	Rs. Millions	USD Millions	Rs. Millions	USD Millions	Rs. Millions
Statement of P&L Account						
Sales & Income	5.75	250.62	3.72	159.58	2.94	125.86
Total Expenses	4.67	203.71	2.87	123.19	2.41	103.34
Profit before Interest & Depreciation	**1.08**	**46.91**	**0.85**	**36.39**	**0.53**	**22.52**
Interest & Financial Charges	0.07	2.98	0.15	6.49	0.11	4.67
Depreciation	0.24	10.29	0.25	10.90	0.18	7.79
Profit before Tax	**0.77**	**33.64**	**0.45**	**19.00**	**0.24**	**10.06**
Appropriations						
Dividend	0.14	6.28	0.11	4.61	0.09	3.69
Corporate Dividend Tax	0.02	0.69	0.01	0.46	0.01	0.36
Transfer to General Reserve	0.04	1.72	0.01	0.48	0.00	0
Surplus carried to Balance Sheet	0.57	24.94	0.31	13.46	0.14	5.99
Sources & Application of Funds						
Sources of Funds						
Share Capital	1.18	51.60	0.86	36.90	0.86	36.90
Reserves & Surplus	3.67	159.96	0.83	35.39	0.50	21.57
Shareholders Funds	**4.85**	**211.56**	**1.69**	**72.29**	**1.36**	**58.47**
Secured Loans	0.86	37.55	0.76	32.41	0.46	19.61
Total	**5.71**	**249.11**	**2.45**	**104.70**	**1.82**	**78.08**
Application of Funds						
Net Fixed Assets	1.96	85.51	0.84	36.18	0.76	32.75
Investments	0.46	20.17	0.17	72.25	0.00	0.10
Net Current Assets	3.29	143.43	1.44	61.27	1.06	45.23
Total	**5.71**	**249.11**	**2.45**	**104.70**	**1.82**	**78.08**

Chairman's Letter

Dear Shareholder,

This is our first Annual Report after the listing of the Company. We therefore have many new shareholders. I would like to sincerely welcome them all to our fold. In order to help our new shareholders acquaint themselves with KPIT, we have made this Annual Report far more exhaustive than the earlier reports. The report brings out our business model, our products and services, our clientele and our organisation structure. I do hope that the report will enable our new members to understand the Company better.



I would like to begin the report by covering some major events of the last year.

Continuing with our decision to focus on the on-site / offshore model, your company continued to change its product mix. The increase in offshore assignments was quite pronounced in line with our efforts. During the year the company delivered major offshore projects for clients in the UK and in Japan. We also commenced our first full responsibility project in the ERP domain.

The gross revenues increased by 57% during the year. However, one of the consequences of this growth was over-reliance on some customers which introduced risks into our operations. As a matter of fact, changes in the business policy of two of our major clients towards the end of the year created a substantial vacuum in the order pipeline which affected our top line as well as our bottom line in the first quarter of the current year. The Company has covered itself from the risk of over-reliance on certain customers by taking steps to ensure the spread of its business.

VILAS JOSHI
Senior Manager - Quality Management

"The adoption of the SEI-CMM model will drive the technological and software development processes towards an era of continuous development with exciting revenue implications through productivity and repeat orders from satisfied customers."

During the year the Company set up its operations in the US through the formation of a wholly-owned subsidiary. The US continues to be a major market for the entire Indian software industry. Our revenue from this market was limited due to the lack of our presence. We corrected this by setting up the US subsidiary. The response to our operations has been encouraging and we expect that during the current year a substantial part of our revenue will come from the US market.

The highlight of last year was the public issue. We are grateful to the investing public who subscribed to the issue so enthusiastically. The applications that we received amounted to 48 times over-subscription. We were of course unable to offer shares to all those who had applied. We however took it as our responsibility to make sure that those who could not be allotted shares were granted refunds in an expeditious manner. Although we received 55,000 applications from 21 centers in the country, the complete processing was done in a record time of 16 working days and the refund warrants were dispatched. I would specially like to thank Intime Securities, Enam Associates and Corporation Bank for fulfilling this herculean task. I would like to state here that we received many communications from applicants appreciating the speed with which we refunded their money and our concern for them.

The last year also saw some changes in the Board of Directors. Mr. B.V. Chitnis who has been on the Board of your company since inception retired on account of his age. On account of his experience as the head of India's largest engineering consulting company viz. Tata Consulting Engineers, Mr. Chitnis brought to us benefits of many years of his experience in consulting and project management. We would like to place on record our sincere thanks for the contribution he made to the Company.

SHIRISH M PATWARDHAN
Head - Technology and Facility Management

Managing our technological environment and building up our knowledge warehouse is a challenging task that helps both maintaining a competitive edge in the market as well as providing a high level of professional satisfaction and value addition to our people."

We expanded the Board of the Company by admitting two more members to the Board. Dr. Vijay Bhatkar, who joined our Board, is well known in the field of science and technology, having been the Father of India's first Supercomputer. He has won many accolades at national and international levels and he brings to the Company a strong technology vision. Mr. Sudheer Tilloo, Managing Director of DGP Hinoday has also joined the Board of the Company. Mr. Tilloo brings to the company his experience in corporate management for over a decade.

Prior to going public, the Company had issued shares to the KPIT Employees' Welfare Trust for issue of Stock Option Plans. The purpose of ESOP is to align the goals of the key employees of the Company with the goals of the shareholders. We have taken the first step by issuing ESOP entitlements to the senior members of the Company. This constitutes approximately 6.5% of the total employees. Over the next two or three years a greater and greater proportion of company's employees will be covered by the ESOP scheme. The details of the scheme are given elsewhere in this report.

We see many new opportunities and challenges in the current year. I would like to discuss some of them with you.

In the context of changes in global technology and business, we see the following as major trends in the IT industry:-

TRENDS

The increasing pace of changes in the business environment will induce end-users to opt for configurable packaged solutions over custom development. Software companies and service providers who have the ability to build software products will therefore have greater chances of success.

Enterprise Applications will pervade the entire value chain. They will cover plant automation at one end and CRM / SCM at the other. Due to this reach, the ability to collect plant level data and integrate it with the corporate database would be valuable. Enterprise Application Implementation will move into mid-size companies and geographies other than the US / Europe. These markets will call for price-sensitive solutions and would need resources which will appreciate less organised business environments. Enterprise applications users will move into a post-implementation support phase.

In an increasingly competitive environment, clients will want to work with consultants who can provide business inputs and then back up the solutions by providing technological solutions. Clients will also expect technically sound and cost-effective remote support. It will involve enhancements / modifications to suit evolving business needs. 24 x 7 support will be an advantage.

With the availability of large transaction-level data, there will be a greater need for business intelligence software. The demand for Data Warehousing, Data Mart & OLAP solutions will grow exponentially.

There will be a pervasive exploitation of internet-based applications. Most users would prefer to either enable their own proven legacy applications for the web or implement proven packaged solutions. There would be significant demand for people who understand multiple technologies and have integrating skills.

Mobile computing including Windows-CE will become important.

ANURADHA KANITKAR
Head - Customer Delivery Unit 3

"Business Intelligence Systems will be the key in the era where markets and technology change rapidly, and corporates look for increasingly sophisticated information analysis to guide their management decisions."

KPIT's RESPONSE

> KPIT has concentrated on the technology end of the spectrum, building strong offshore development capabilities.
> KPIT has put together resources, which are flexible, technically competent & price effective.
> KPIT has set up a team, which is proficient in legacy databases and platforms as well as internet tools and technologies.
> Over the last six years, KPIT has developed a growing team of competent technical personnel and has helped large international clients in implementing OLAP & Data Mart Solutions. KPIT has one of the most experienced teams in this area in the Asia-Pacific region.
> KPIT has targeted mid-sized companies and is spreading into other markets like the Middle East and Far East besides US and UK..
> KPIT's methodologies lay emphasis on post-implementation support.
> KPIT is geared to render off-site support in a cost-effective and round the clock manner. Our global presence will enable us to provide 24 x 7 support.
> KPIT has identified CRM / SCM as the new focus areas for skill building.
> KPIT has built ASTRA - a world-class SCADA software for plant data acquisition and analysis. ASTRA runs on Windows CE-based palm-held devices.
> KPIT has not only built world-class software products, but has also worked with software product companies who compete in the international arena. Consequently, it has developed an ability to build packageable software products.

In tune with the changing requirement of technology and business, we have re-organised our operations. Our delivery units reflect the thrust that we want to give on different product offerings and customer groups. The focus of the operations would be on delivery of services to individual customers. The business model is therefore essentially customer-centric where any product or service is essentially used as a strategy to first satisfy the immediate need of the customer and use the opportunity to get to know his company well. Having done that, the thrust would be on identifying, proposing and satisfying as many needs of the customer as possible, thereby increasing the scope of our relationship. We have therefore put into operation, processes of client qualification and client penetration.

We have also put in place internal operating processes including setting and reviewing quarterly goals, which would help us remain in tune with the stringent requirements of being a publicly listed company. While the business planning takes into account the long-term changes, sharp focus is now given to setting and executing quarterly goals.

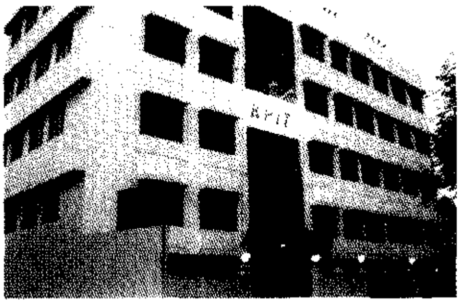
Your company has always valued quality in its operations. The Company has, over the last three years, developed standardised operational processes, which give it a control on the quality of deliverables that it makes to the customers. While the Company was certified under ISO 9001 over three years ago, during the current year we have decided to go for industry-specific assessment, namely, SEI-CMM. Adopting the SEI-CMM model, we believe, would be the most suitable model that would create the confidence in our customers that we possess a sustainable capability to deliver good work products to them.

We recognise that the industry would present significant benefits for scale of operations. Therefore, we have put focus on growth through proper client and services selection. The Company is however, conscious of the need to look at inorganic growth through mergers and acquisitions. The Company has put into operation policies and processes for growth through mergers or acquisitions which will be useful as and when such opportunities come up in future for evaluation.

To conclude, we at KPIT recognise that the IT industry provides great global opportunities and challenges to make a name not only for our own company, but for the industry and the country. However, it needs from us speed, discipline and teamwork. Everyone at KPIT is aware and conscious of this, and I am confident that the KPIT team will deliver what is expected from this high-potential company.

SB (Ravi) PANDIT

Chairman



CORPORATE GOVERNANCE

Your management believes that good Corporate Governance is the key to creation of value. The Confederation of Indian Industries (CII) has come out with a code of Corporate Governance. We are giving below the details of the recommendations given under this code and your company's status and performance vis-a vis the code.

Recommendation 1 - *The full board should meet a minimum of six times a year, preferably at an interval of two months, and each meeting should have agenda items that require at least half a day's discussion.*

The Board met nine times during the year. The pre-set agenda is made available to the board members prior to the Board meeting.

Recommendation 2 - Any listed company with a turnover of Rs. 100 crore and higher should have professionally competent, independent, non-executive directors, who should constitute at least 30% of the board if the Chairman of the company is a non-executive director, or at least 50% of the board if the Chairman and Managing Director is the same person.

The Company has five independent non-executive Directors who are professionally competent.

> Mr. Ajay Bhagwat is an expert in the area of Control Automation
> Dr. Vijay Bhatkar is a nationally renowned scientist in the field of Information Technology.
> Dr. Naushad Forbes is a well-known industrialist and is also a visiting faculty at the School of Industrial Management at the Stanford University, USA.
> Mr. Shailesh Haribhakti is a highly respected Chartered Accountant and brings with him knowledge of finance and law.
> Mr. Sudheer Tilloo is a business executive with extensive experience in top management of growing industries in competitive areas.

The non-executive Directors constitute more than 60% of the total Board Of Directors.

Recommendation 3 - No single person should hold directorships in more than ten companies.

Only one of nine directors holds directorship in more than 10 companies.

ANUP SABLE

Head - Internet Technologies

"To enable our customers take advantage of the Internet opportunity, we are working hard towards a model where all our service, business and technology groups are equipped to handle Internet Technologies. In the process, over 12% of our developers have been trained on Internet Technologies in Q1 and this figure will go up to about 33% by Q4."

Recommendation 4 - For non-executive directors to play a material role in corporate decision-making and maximising long term shareholder value, they need to become active participants on the board, not passive advisors. have clearly defined responsibilities within the board such as the audit committee; they should know how to read a balance sheet, profit and loss account, cash-flow statements and financial ratios and have some knowledge of various company laws. This, of course, excludes those who are invited to join boards as experts in other fields such as science and technology.

The non-executive Directors contribute to corporate decision-making through formal board meetings as well as through informal discussions throughout the year. The Company actively seeks the inputs of the Board members in issues such as technology directions, business strategy formulation, financial strategy decisions and issues relating to organisation structure.

Recommendation 5 - To secure better effort from non-executive directors, companies should pay a commission over and above the sitting fees for the use of professional inputs. The present commission of 1% of net profits (if the company has a managing director), or 3% (if there is no managing director) is sufficient; consider offering stock options, so as to relate rewards to performance. Commissions are rewards on current profits. Stock options are rewards contingent upon future appreciation of corporate value. An appropriate mix of the two can align a non-executive director towards keeping an eye on short-term profits as well as long term shareholder value.

Presently the Company remunerates its non-executive Directors by payment of sitting fees alone. It proposes to pay a commission to the non-executive Directors on the basis of the profits of the Company. A resolution to that effect is being tabled at the ensuing Annual General Meeting.

The Company believes that the proper and internationally recognised practice of remunerating the Board of Directors is the issue of stock options. The Directors however are presently not being issued stock options.

Recommendation 6 - While re-appointing members of the board, companies should give the attendance record of the concerned directors. If a director has not been present (absent with or without leave) for 50% or more meetings, then this should be explicitly stated in the resolution that is put to vote. As a general practice, one should not re-appoint any director who has not had the time to attend even one half of the meetings.

The Company proposes to follow this guideline in the case of re-appointment of Directors, subject however to the assessment of the contribution of the Directors outside the Board meeting.

ABHIJIT DANDEKAR
Country Manager - India

"Our India strategy consists of working with transnational and world-class organisations helping us to leverage our consulting and system building experience to create reference sites for us in the software project business."

Recommendation 7 - Key information that must be reported and placed before the board must contain:

> Annual operating plans and budgets, together with up-dated long term plans.

> Capital budgets, manpower and overhead budgets.

> Quarterly results for the company as a whole and its operating divisions or business segments

> Internal audit reports, including cases of theft and dishonesty of a material nature.

> Show cause, demand and prosecution notices received from revenue authorities that are considered to be materially important (Material nature of any exposure that exceeds 1% of the company's net worth)

> Fatal or serious accidents, dangerous occurrences, and any effluent or pollution problems.

> Default in payment of interest or non-payment of the principal on any public deposit, and / or to any secured creditor or financial institution

> Defaults such as non-payment of inter-corporate deposits by or to the company, or materially substantial non-payment for goods sold by the company.

> Any issue which involves possible public or product liability claims of a substantial nature, including any judgement or order which may have either passed strictures on the conduct of the company, or take an adverse view regarding another enterprise that can have negative implications for the company.

> Details of any joint venture or collaboration agreement.

> Transactions that involve substantial payment towards goodwill, brand equity, or intellectual property.

GANESH SANKER
General Manager - Organisation Development

"The demand for software professionals globally will outstrip supply for many more years. In this technologically vibrant field, companies will be able to retain talent only by building careers and adding economic and psychological value to

> Recruitment and remuneration of senior officers just below the board level, including appointment or removal of the chief financial officer and the company secretary.

> Labour problems and their proposed solutions.

> Quarterly details of foreign exchange exposure and the steps taken by management to limit the risks of adverse exchange rate movement, if material.

The information placed before the Board of Directors includes presentations by the Chairman on the review of the business scenario, presentations by the Managing Director regarding the overview of the operations and presentations by delivery / market unit heads on the operations of respective units. The Board also deliberates and decides upon key corporate policy matters. Apart from the above, key financial and legal matters are placed before the Board.

Recommendation 8 - Listed companies with either a turnover of Rs. 100 crore or a paid-up capital of Rs. 20 crore, should set up audit committees within two years. Audit committees should consist of at least three members, all drawn from a company's non-executive directors, who should have adequate knowledge of finance, accounts and basic elements of company law. To be effective, the audit committee should have clearly defined terms of reference and its members must be willing to spend more time on the company's work vis-à-vis other non-executive directors. Audit committees should assist the board in fulfilling its function relating to corporate accounting and reporting practices, financial and accounting controls, and financial statements and proposals that accompany the public issue of any security and thus provide effective supervision of the financial reporting process. The audit committee should periodically interact with the statutory auditors and the internal auditors to ascertain the quality and veracity of the company's accounts as well as the capability of the auditors themselves. For the audit committee to discharge its fiduciary responsibilities with due diligence, it must be incumbent upon the management to ensure that members of the committee have full access to financial data of the company, its subsidiary and associated companies, including data on contingent liabilities, debt exposure, current liabilities, loans and investments. By the fiscal year 1998-99, listed companies with either a turnover of over Rs. 100 crore or a paid-up capital of Rs. 20 crore, should have in place a strong internal audit department, or an external auditor to carry out internal audits; without this, any audit committee will be toothless.

GIRISH SANDHANE
General Manager - ASTRA

"As device manufacturers build control and information availability through a plethora of everyday personal and industrial appliances, ASTRA will play a major role by offering software necessary to build these capabilities."

The Company has recently formed an audit committee of the Board consisting of two external directors and the Chairman of the Company. The Directors have adequate knowledge of financial accounts and basic elements of Company Law. The Company has also appointed a firm of Chartered Accountants to carry out internal audit. The Company is in the process of developing a guideline for the operation of internal audit committee including the nature of interaction between audit committee and the internal & statutory auditors. The Committee would meet twice in a year in the presence of internal and statutory auditors.

Recommendation 9 - Under "Additional Shareholder's Information" listed companies should give data on high and low monthly averages of share prices in a major stock exchange where the company is listed for the reporting year; greater detail on business segments upto 10% of turnover, giving their share of sales revenue, review of operations, analysis of market and future prospects.

The information regarding high and low of monthly share price at the Pune Stock Exchange are given in this report under "Shareholder's Information". The details of various business segments are also given in this report in the "Letter from the Managing Director".

Recommendation 10 - Consolidation of group accounts should be optional and subject to the financial institutions allowing companies to leverage on the basis of the group's assets and the income tax department using the group concept in assessing corporate income tax. If a company chooses to voluntarily consolidate, it should not be necessary to annex the accounts of its subsidiary companies under Section 212 of the Companies Act. However, if a company consolidates, then the definition of "group" should include the parent company and its subsidiaries (where the reporting company owns over 50% of the voting stake.)

The Company has not consolidated the books of company accounts, but has annexed the accounts of its subsidiary company as required by Section 212 of the Companies Act.

Recommendation 11 - Major Indian Stock Exchanges should gradually insist upon a compliance certificate, signed by the CEO and CFO which clearly states that, the management is responsible for the preparation, integrity and fair presentation of the financial statements and other information in the annual report, and which also suggest that the company will continue in business in the course of the following year; the accounting policies and principles confirm to standard practice, and where they do not, full disclosure has been made of any material departures; the board has overseen the company's system of internal accounting and administrative controls systems either directly or through its audit committee (for companies with a turnover of Rs. 100 crore or paid-up capital of Rs. 20 crore)

PRABODH TEREDESAI
Head - Customer Delivery Unit 2

"An increasing velocity of business is inducing end-users to opt for configurable packaged solutions over custom development. As packaged solutions pervade the whole business value chain covering plant automation at one end and Customer Relationship Management at the other, companies will face the twin challenges of application integration and information extraction and analysis for decision making."

The Stock exchanges where the shares of the Company have been listed have not insisted on compliance certificate as stated in the recommendation. The management of the Company however states that it is responsible for the preparation, integrity and fair presentation of the information contained in this report. The Accounting Policies and Principles are described in this report stating their conformance or otherwise with the standard practice.

SACHIN TIKEKAR
Head - US Operations

"The US is by far the largest market for IT and KPIT is geared to build a strong presence in this market in the next two years by forging relationships with large IT spenders looking for a competent supplier of IT services."

Recommendation 12 - For all companies with a paid-up capital of Rs. 20 crore or more, the quality and quantity of disclosure that accompanies a GDR issue should be the norm for any domestic issue.

This recommendation is not applicable to the Company.

Recommendation 13 - Government must allow far greater funding to the corporate sector against the security of shares and other paper.

This recommendation is not applicable to the Company.

Recommendation 14 - It would be desirable for financial institutions as pure creditors to rewrite their covenants to eliminate having nominee directors except in the event of serious and systematic debt default and in case of the debtor company not providing six-monthly or quarterly operational data to the concerned financial institutions.

This recommendation is not applicable to the Company.

Recommendation 15 - If any company goes to more than one credit rating agency, then it must divulge in the prospectus and issue document, the rating of all the agencies that did such an exercise. It is not enough to state the ratings. These must be given in a tabular format that shows where the company stands relative to higher and lower ranking. It makes considerable difference to an investor to know whether the rating agency or agencies placed the company in the top slots, or in the middle, or in the bottom. It is essential that we look at the quantity and quality of disclosures that accompany the issue of company bonds, debentures, and fixed deposits in the USA and Britain - if only to learn what more can be done to inspire confidence and create an environment of transparency. Finally, companies that are making foreign debt issues cannot have two sets of disclosure norms: an exhaustive one for the foreigners, and a relatively minuscule one for Indian investors.

This recommendation is not applicable to the Company.

PERVEZ DAVER
Senior Manager - Corporate Marketing

"Corporate Marketing has been entrusted with the task of creating a consistent brand identity and message that pervades all aspects of the marketing effort across regions, markets and technologies. The group will also build marketing processes and systems that incorporate business intelligence, information systems and strong customer relationships to improve the predictability and performance of the company's top and bottom lines."

Recommendation 16 - Companies that default on fixed deposits should not be permitted to accept further deposits and make inter-corporate loans or investments until the default is made good, and declare dividends until the default is made good.

This recommendation is not applicable to the Company.

ANIL PATWARDHAN
General Manager - Finance and Administration

" We are quickly learning from our experience to develop the capability and systems to anticipate and plan growth in a more predictable way so that we meet with the expectations of our Investing community."

Recommendation 17 - Reduction in the number of companies where there are nominee directors. It has been argued by Financial Institutions that there are too many companies with nominee directors on the board, and too few competent officers to do the task properly. So, in the first instance, financial institutions should take a policy decision to withdraw from boards of companies where their individual shareholding is 5% or less, or total financial institutions holding is under 10%.

This recommendation is not applicable to the Company.