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SYSTEMHOUSE

The monthly review of the financial performance of the UK software and IT services industry

OFFSHORING INTEREST ACCELERATES IN THE UK

By John O'Brien

John O'Brien
Analyst

UK Government's attitude is changing

In our report, *The use of offshore IT and business services by the UK public sector*, Georgina O'Toole and I explored the opportunities for delivering offshore software and IT services (S/ITS) to the UK public sector, and the degree to which UK Government would alter its attitude to offshoring over the next few years.

We discovered that attitudes have been changing over the last few years and that there is already a sizeable degree of offshoring activity across central government departments, the NHS, local government and the transport sector.

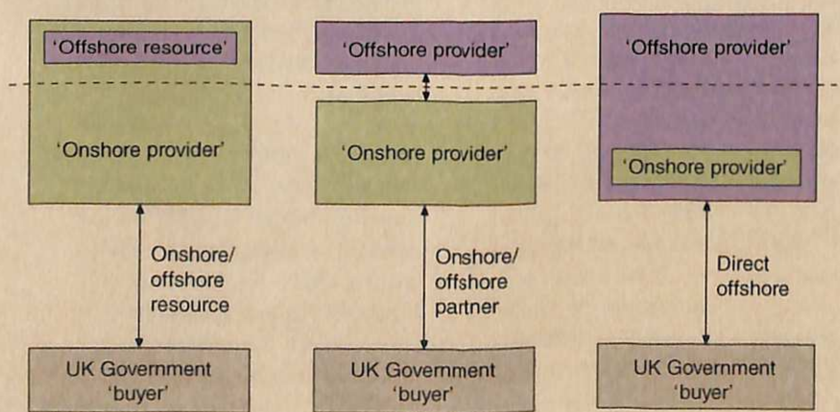
Offshoring is being driven not so much by any specific policy change by government, but rather tough budgetary constraints, compacted by the Government's Comprehensive Spending Review (CSR07). This is set to place even more financial pressure on public sector organisations over the next few years, and will lead them to consider how to deliver 'more for less'; and in turn likely open the door further to offshoring.

Cost-cutting - the driver

The majority of projects to date are ad-hoc subcontracting work, predominantly in areas such as application development and management and support. For example, BT is subcontracting Mastek to perform critical systems development for its national data spine contract on the National Programme for IT (NPfIT) in the NHS, meanwhile Fujitsu subcontracts application testing work to TCS and Capita subcontracts Mastek for development work on the London Congestion Charging scheme.

The use of offshoring as a strategic cost-cutting tool in government BPO contracts is also growing. For example, Xansa now

Figure 1 **Three types of arrangement used by UK Government**



Source: Ovum

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INDICES
(changes in March 2008)

Ovum S/ITS Index	**-3.27%**	**5245**
FTSE IT (SCS)	**-2.25%**	**485**
techMARK 100	**-3.10%**	**1512**

New broader coverage

From 1 May 2008, you will receive even more in your SystemHouse publication. Based on customer feedback, we have broadened our coverage to include global markets and players. You will still receive your current news and opinion but in a new improved publication called 'Straight Talk', which will be delivered in both a daily and monthly format. In order to support our green policy, we will no longer produce hard copy monthly publications; instead we will email a PDF copy. We actively encourage feedback from our customers, so if you have any comments or questions then please contact us at **StraightTalk@ovum.com.**

[continued from front page]

administers approximately 60% of its finance and accounting (F&A) shared services contract for the NHS from India. In these cases offshore sourcing is being used by the suppliers to help deliver against their committed cost savings.

Barriers to offshoring

There are barriers to the evolution of offshore IT services in UK Government. In our conversations with John Suffolk UK Government CIO, he believes S/ITS suppliers should treat Government in the same way they treat their private sector clients, assuming there are no security considerations. However, these views have yet to fully penetrate through to the decision makers at the front-line who make decisions on the use of offshore resource on a project-by-project and contract-by-contract basis.

Suffolk does not advocate a prescriptive approach by Government to offshore sourcing, so it is up to decision makers to choose which route is best for them. This is a big challenge given the political sensitivities around the issue, which are driven predominantly by a fear of job losses, a concern about the impact on the UK economy and a lack of confidence in the quality of service delivered from low-cost locations.

Suppliers making a splash

Offshore suppliers are attempting to mitigate some of the negative associations of offshoring by subcontracting to established onshore providers (onshore/offshore partner); likewise onshore providers are either partnering with offshore providers, or looking to use their own internal offshore resource to help meet contractual targets. To date there is very little direct offshoring taking place in which an offshore provider primes a relationship with the public sector customer. We suspect this will remain the case for some time.

Of the traditional onshore suppliers, four companies - Steria/Xansa, Capita, Capgemini and Siemens - stand out as being most confident in opening up the debate around offshore delivery in UK Government. We believe, due largely to the type of work they undertake, that they also deliver a higher proportion of their public sector contracts from offshore locations. These companies stand to benefit as offshore becomes more acceptable and they can highlight successful reference sites.

In terms of offshore IT services companies, there are currently four (all Indian-headquartered) that are making noise in the sector - Wipro, Infosys, Tata Consultancy Services and Mastek. While they might hope to benefit from direct relationships with UK Government clients, we think this will be some time coming and they must instead concentrate on building strong alliances with the onshore service providers while slowly building their own onshore presence.

Recommendations for IT services suppliers

There are a number of things suppliers can do to ensure that they benefit from the shift to offshoring over the next few years.

For onshore companies:

- Always embark on open and honest discussions with clients and potential clients about the use of offshore services early on in the competitive process. Departments and agencies will not always be explicit about their propensity for low-cost service delivery so it is important to gain an understanding of local policies.

- Opt to use internal offshore resource over partnering with offshore companies where possible. The use of offshore resource owned by traditional onshore companies is less visible than partnering with Indian players. Therefore, in the short term, the existence of political sensitivities, particularly in areas such as local government, means this 'captive' offshore approach is preferable.

- Demonstrate the protection of UK jobs where possible. Innovative suppliers will understand how to use offshore capability while transferring onshore resources into higher value-add service areas.

- Don't underestimate the traditional offshore service companies. The likes of TCS, Wipro, Infosys and Mastek are growing their onshore presence and aim to be seen as global delivery companies akin to their traditional onshore competitors.

- Use onshore advantage to compete with the offshore players. Traditional offshore players are at present some way from having the same UK-based presence as the traditional onshore public sector S/ITS suppliers.

Rules for offshore players:

- Be clear about the role your organisation can play in the UK public sector, and do not attempt to be all things to all people.

- Consider recruiting senior onshore staff in specific target areas to develop contacts and build domain knowledge of target clients.

- Expect tactical, point solutions and services to be offshored. Don't expect Government to select an offshore provider to prime an IT outsourcing or BPO project for a long time.

- Concentrate on key delivery areas such as application development, application management and support, as these are the areas UK Government is most comfortable offshoring.

- Offer at least equivalent or better capability than the established onshore provider to develop credibility in the sector.

PHOENIX: TACKLING MID-MARKET IT SERVICES

Kate Hanaghan
Analyst

Phoenix IT services has been changing. The UK firm has shifted from the partner-only model it so rigidly stuck to for many years, with the completion of several acquisitions meaning it now sells directly to the end customer too. In fact, acquisition has really changed the 'shape' of Phoenix, which was once firmly focused on the corporate end of the market via partners such as Logica, Atos and BT. It is now structured into three units: its core business still serves those large corporate customers through partnerships with other IT services providers; it also has a business continuity (BC) unit; and it sells IT services directly to customers through its mid-market unit.

The new structure of Phoenix is logical. It can protect its core business in the corporate market, while pushing further into BC (where it has some good assets and is experiencing healthy revenue growth) and exploiting the relatively strong prospects in the mid-market. With these three fronts into the IT services market, Phoenix is better positioned than some of its typical competitors.

Phoenix IT: The new business structure

IT services to corporates via partners	Business continuity services	IT services sold directly to the mid - market

Servo: the mid-market unit

Neil Lloyd is running what is now the mid-market unit. Some readers will recognise him as the ex-CEO of Netstore, the managed services firm. For the time being, the unit will retain the Servo name. As well as carrying out standard IT services around supporting and managing infrastructure, Servo has a technical consulting capability. While quite small, it's growing healthily, reflecting a broader trend we're seeing in the market. This kind of consulting is a far cry from the high-end business consulting carried out by Accenture et al, and typically refers to consulting services around systems design and systems assessment. Through 2008, we think those suppliers who can market their services tactically should find pockets of good growth. For example, tuning-in to current interests around governance, green IT and, of course, the need to cut IT running costs.

Vertical wrap

We have said for some time that even infrastructure services firms who provide what are essentially horizontal services need to think more closely about how they can 'verticalise' those services. In other words, how do you make an outsourcing service more applicable/attractive to a retail customer, for example? This 'verticalisation' should not be an extensive restructuring of the portfolio. What we are really talking about is marketing around those existing services in order to help customers understand the benefits for their business. There is also an element of providing reassurance by proving at least some understanding of the customer's specific challenges.

We have more recently started to see some infrastructure services firms looking to do this; Getronics, for example, is starting to do this. Likewise, Servo is going to add more specialisation and verticalisation of certain services. This is particularly interesting given it is already focused on the mid-market. We think this will serve to heighten its appeal to customers who are looking for providers that understand their technology challenges very closely.

A mid-market champion?

Ovum's research into the UK mid-market for IT services shows that there are a range of growth opportunities for certain players – particularly, players that have significant, existing relationships with customers in this segment of the market.

Repeatedly, established mid-market players highlight that it is the similarities (for example, the number of staff, layers of management or level of turnover) between their businesses and their mid-market customers' businesses that is a key winning factor. Given this, we think there is an opportunity for an IT services firm to make a name for itself as a mid-market specialist - to become THE name in mid-market IT services. But they need to be able to offer the full range of services. It's a cliché, but the concept of a "one-stop-shop" is very appealing to mid-market buyers who don't want to deal with the added complexities of having multiple suppliers. And it is exactly this position we think Servo should aspire to assume.

0%
050p

PARITY IMPROVES PERFORMANCE IN 2007

Parity, the staffing, services and training firm, has announced 2007 results with revenues from continuing operations up 2% to £160m. Across its three businesses: resources (after three years of revenue growth) declined 4% to £110.3m; Solutions grew 30% to £31.0m; and training revenues were flat at £18.6m. Overall operating margin (before exceptionals) was 2.5%, up from 0.9%.

Comment: The resources business (69% of revenues) has slipped back in the year in terms of revenues. But we're not too concerned about this (provided this is only a short-term trend), given Parity's (rightful) desire to steer away from low-margin contracts. Margin improvement is a key priority for management in 2008, and profits here remained steady year-on-year at 2.4%. Behind the scenes, its margin improved from 2.0% in the first half of 2007 to 2.8% in the second half.

Performance in the solutions business has been driven in part by activity in the public sector, specifically in portals and knowledge management in mid-sized organisations. The affordability of tools is making these kinds of projects do-able, without the need for full-blown content management rollouts. The size of these deals is in the £300k-£1.5m range - so not huge. However, Parity seems to have found itself in a good position where there is a fairly regular supply of these deals. Moreover, Parity's pipeline indicates that this area of the public sector is likely to remain solid.

As well as focusing on margin improvement in the resources business, Parity's management is (wisely) seeking to be 'fleet of foot' in order to anticipate any changes in client sentiment against the backdrop of a gloomy economic outlook. This partly means keeping a tight and cautious hold on costs, but also looking out for any signs that customers are pulling back - and diversifying accordingly.
Kate Hanaghan

-4%
173p

COMPUTACENTER RETURNS TO GROWTH

Computacenter announced its 2007 financial results. Group revenues increased 4.8% to £2.38bn – the first time Group revenue has grown since 2003. Operating profit (before exceptional items) was £43.1m, which generated a margin of 1.8%.

UK revenues grew by 5.9% to £1.36bn, and were driven by "strong" sales in data centre services and an improvement in product revenues. UK services revenues, excluding the effect of acquisitions, declined 3.5%, with professional services growth partially compensating for a decline in contractual revenues.

Computacenter has been buying back shares for cancellation. This programme began in November and by the close of the financial year 1.5 million shares (0.9% of the issued share capital) had been purchased.

Comment: Computacenter Services delivers a range of offerings around outsourcing, support and professional services. The purchase of Digica in January 2007 demonstrated a broadening towards data centre services. And the purchase of Allnet, a network integration and cabling company, in April signified Computacenter's move into network-oriented services. However, the final UK Services numbers for FY07 are poor. H2 saw something of a recovery, which brought a "small contract base increase", which we hope will continue into 2008.

Computacenter says that its increased use of shared service facilities, tools and repeatable processes is proving to be attractive to customers. Indeed, the company claims it was these that helped it to secure the £19m/five-year managed services contract with Marks & Spencer. Additionally, Computacenter has made internal changes to aid growth and profitability in the services business. They include improving how it is aligned with customer business strategies and objectives. Computacenter blames the loss of some important contracts in 2006 (which impacted the H1 2007 numbers) on a lack of alignment here.

Germany, which accounts for almost a third of Group revenues, turned in its best profit performance since Computacenter acquired the CompuNet business from GE in 2003. The business was lifted partly by a healthy market and partly by a reduction in losses from two data centre services contracts. Computacenter's investment in the services business has certainly paid-off - particularly in managed services and consulting - with growth hitting 13%. Let's hope we see a similar scenario emerge in the UK.
Kate Hanaghan

0%
211p

NCIPHER POSTS ENCOURAGING RESULTS AGAIN

nCipher posted results for the year to December 2007. Revenue was up by 15% (20% at constant currency) to £24.2m, while profit before tax was £3.4m, compared to a loss of £4.7m in 2006.

During the year it acquired NeoScale, which will help it to develop its core key management capability. The acquisition, in December 2007, came too late to have a material effect on the numbers.

Comment: nCipher remains a technologically-oriented player, as exemplified by its commitment to growing R&D expenditure at a time when many companies are drawing in their horns in the face of the impending storm. It raised substantial funds during the dotcom era but did not spend them in the way that most dotcoms did, and later it decided to return a large portion to the investors. This year it has completed this process with a further return of £34m through a tender offer.

nCipher's core competence is encryption and while encryption has recently gained a high profile due to numerous cases of the loss of sensitive data, encryption in itself is well understood and of little commercial value. nCipher has recognised this and focuses on key management where there is a major challenge for enterprises, along with providing a secure hardware environment where this is needed. nCipher is well set up to ride the tide in meeting this fundamental business need.

The Abridean story is less cheerful. At the time of its purchase, nCipher hoped to profit from the second wave of identity management. Ovum recently commented on the difficulties of finding financial success in the identity management market in the context of HP's retrenchment, and a similar message would be even more relevant here, as nCipher lacks HP's market presence. nCipher has now decided that identity management is not strategic to its aims and we can expect a disposal in the near future.

Graham Titterington

-17%
020p

RESTRUCTURING COSTS PUSH NETSTORE INTO LOSSES

Netstore, provider of IT managed services and IT security, released its results for the six months to end December 2007. Revenue declined from £20.0m to £19.7m. Excluding exceptionals (mostly restructuring costs), the operating margin was 6.2% in the six-month period - compared with 7.0% in 2006. Including exceptionals, the company made a small operating loss of £88,000, versus a small profit of £116,000 in the comparable period last year.

The company has been undertaking a review of its accounting procedures following the discovery of certain irregularities following the installation of a new management team. Netstore is currently in discussions with a number of potential buyers for the firm.

Comment: Despite the move into losses and the decline in revenue, we see some positives - notably in managed services, which continues to be a healthy market, particularly in the mid-market. We see this trend continuing and believe the opportunities for growth are there for Netstore. In addition, its Security business has seen 'significant new contract activity' - which again bodes well.

But what we really need to evaluate Netstore against is its strategy to simplify its processes (including sales) to bring costs down and cross-sales up. We support this strategy and believe it is worth the pain in the short-term. It's worth noting that while undertaking this (and of course dealing with the accounting issues in parallel) the firm has grown its Security and Managed Service revenue streams. In other words, it hasn't been distracted. We will, however, need to wait a little longer to see just how effective the measures taken by the management team are.

Meanwhile, the company is still in discussions with a number of third parties with regards to a possible offer. The question is whether Netstore would flourish better as it is or as part of a larger organisation that could bring additional scale. All the signs are that management are very open to taking the latter route. If Netstore gets sold in the fairly near future, we wouldn't be at all surprised or disapproving.

Kate Hanaghan

-17%
071p
statpro

STATPRO REPORTS EXCELLENT RESULTS

Statpro Group posted 2007 revenues of £24.1m, up 22% on an organic basis compared to the previous year. Operating profit went from £1.2m to £5.6m, which meant that Statpro's operating margin rose to 23% (compared to 8% in 2006).

Comment: As expected, this was an excellent performance from Statpro. On both revenues and profitability the company showed it can grow organically and successfully integrate international acquisitions (following four purchases in 2006 and 2007).

One could argue that market conditions last year were in Statpro's favour and that there's a strong risk of this changing. Mindful of this, the company provides the following outlook: 'To date there is little evidence that the problems of the credit markets are spilling over into our markets; if they do then we are confident that we are well placed to take appropriate action. In the event that conditions remain benign, then we expect to have another good year in 2008', says Chief Exec Justin Wheatley. Statpro thus joins Microgen and others in confirming that the capital markets sector has so far remained buoyant in terms of software and services spend, but also in acknowledging the downside risks in the times immediately ahead.

Phil Codling

4%
679p
CAPITA

CAPITA CEMENTS UK BPO MARKET LEADERSHIP

UK BPO player Capita released another set of stellar results, with 2007 revenue up 19% to £2.1bn. Profit before tax was up 19% to £238.4m, keeping PBT margins flat at 11.5%.

Comment: Capita is now almost twice the size of its next largest competitors in both the local government and life & pensions sectors, and at least £1.5bn in revenue ahead of second place Vertex in our UK BPO player rankings. It also swallowed up almost every mega-deal up for grabs in the UK BPO market in 2007.

The only high profile bid failures were losing the congestion charging renewal to IBM, and the Sun Life of Canada life & pensions renewal to TCS. But neither of these losses put a significant dent in Capita's growth plans. And as CEO Paul Pindar says, you can't put 100% effort behind 100% of the bids. You can't argue with that when the company's success rate is so high.

Capita is clearly in a strong position. It has managed to build significant scale across most of its target sectors. And now it is rightly focusing on the next step: generating economies of scale across its contracts by investing in integrating platforms, processes and IT systems. Capita is also accelerating its offshore resource capability, which should double in volume to 2,500 staff in India thanks to the addition of Prudential's offshore operation.

These integration and offshoring investments will boost profit margins – and just in time too. Large BPO deals incur heavy costs in their early years. And having just swallowed a series of large deals in the past two years, Capita's margin is under pressure. Indeed, we don't expect Capita to increase its margins in 2008 – and it will have done well if it can keep margins flat.

Meanwhile, Capita is exploring opening up new markets in the UK, although it is very tight-lipped about what new opportunities it expects to see. It is already expanding in the mortgage and insurance sectors, and general banking is being targeted more aggressively after the sub-prime crisis. Outside of the finance sector the company continues to expand its horizontal services offerings, particularly around human resources.

The BPO market is changing, and deals are getting smaller. Capita's own pipeline reveals this. For 2008 it is £2.5bn comprising 25 bids, whereas last year it was £2.6bn comprising 12 bids. This is a very significant shift. Having built scale, Capita will always be competitive. However, given the changing make up of deals in the market, there are still opportunities for smaller, more nimble vendors to continue to nip at Capita's heels.

Samad Masood

-4%
227p

tikit

LEGAL SECTOR CONTINUES TO SERVE TIKIT WELL

Tikit, the software resale and services firm focused on the legal sector, announced results for 2007. Group revenues increased 12% to £26.4m. Total services revenue, including consultancy and support, increased 16% to £17.6m. Operating margin improved from 11.6% in 2006 to 12.6%.

Comment: Tikit implements software for customers and provides consulting services to tailor applications to the specific needs of its predominantly legal firm client base. It also provides the ongoing support around these applications. Tikit has been moving to a subscription-based model on licence sales, which of course is impacting the way it recognises revenue. The company reports that its customers are (not surprisingly) very attracted to this model, particularly those below the 'top rung' legal firms. Going forward, this model should enable Tikit to open up more new customer opportunities among those smaller legal firms in the mid-market.

In our many conversations with the industry, numerous suppliers have told us that they are yet to feel the effect of tightening purse strings, but that they remain cautious about how the environment could change throughout the course of the year and beyond. And Tikit takes a similar view. At the moment, the legal sector is not holding back on IT spend. Nevertheless, Tikit is wisely taking a cautious view on growth for 2008. Having said that, its Document Management, CRM and Finance and Business Process Management lines of business all have the largest pipelines they have ever had. We therefore think that as long as market conditions do not alter dramatically (and we must of course not rule that out), and provided Tikit can continue to keep utilisation high, the first half of 2008 shouldn't be too bad at all for the firm.

Kate Hanaghan

-29%
398p

AXON

AXON LOOKS TO CONTINENTAL EUROPE IN 2008

SAP specialist Axon reported revenue growth of 49% to £204.5m in 2007, with organic growth at 29%. Adjusted operating profit, excluding amortization of intangibles, grew 63% to £35.5m, generating a margin of 17.4%, up from 15.9% last year.

Comment: Axon has long been a strong performer, and it is no surprise that it continues to grow aggressively on the back of its SAP-focused organic and acquisitive strategy. Over the year Axon benefited from acquisitions in the US and also in Asia Pacific, where it boosted both offshore capability (adding 150 staff) and revenues from Asian clients.

This overseas expansion has helped to mitigate the company's mature position in the UK market, where it does not see much more headroom for growth. As well as Asia and the US, Axon is focusing on expansion in Continental Europe, again through acquisition. However, this might be a more challenging task. By Cardell's own admission, there are few 'quality' opportunities for acquisition in Continental Europe. To start with Axon is focusing on the DACH (Germany, Austria, Switzerland) region, but will favour the quality of the firm's business over its location. Whatever the result of its search, Axon must get a foothold in this market if it is to achieve its aim of becoming a leading global SAP integrator.

Like many S/ITS players, Axon says it has not seen the fears of economic downturn affect any of its business or pipeline. Nonetheless, it is being prudent in its vertical growth strategy and says it will now focus more on consolidating its gains in its core verticals (aerospace & defence, CPG, oil & gas, public sector, telcos and utilities) which represent 68% of its business, rather than investing too much in the financial services, high tech and services industries, which could be more at risk from a downturn.

Another key initiative is to focus on selling services into large BPO deals, either directly or alongside partners, such as Pearson and Capita, with which it is implementing SAP at Birmingham City Council. This strategy should also serve to mitigate the effects of any future economic downturn, given that outsourcing and BPO tend to be growth markets in these situations.

Samad Masood

Mergers and Acquisitions – March 2008

Buyer	Sun Microsystems Inc
Seller	MySQL AB
Seller Description	A Swedish-based provider of open source database products and services.
Acquiring	100%
Price	$1 billion (estimated)
Comment	MySQL had been talking about becoming public for about a year now. But in the end it preferred to play it safe, turning to an acquisition to build on the momentum it had already gathered. Sun will provide it with the resources required, not just in terms of money but also (support and channel) infrastructure, to go forward in the direction it has been following in the past two years, namely towards increasingly mission critical deployments in large multinationals. In return, via MySQL, Sun is trying to regain its status as the company at the heart of the 'Internet economy'.

Buyer	IDOX plc
Seller	Plantech Limited
Seller Description	A provider of software and solutions to local government
Acquiring	100%
Price	£5.3 million
Comment	In December last year we said that the shape of IDOX had changed considerably following its acquisition of CAPS this year. It has boosted the size of its software business from £5.2m to £13.2m. Excluding the acquisition, this division grew 15% - outperforming the Information Solutions division quite considerably. Aqcuiring Plantech positions IDOX for a further phase of growth but needs focus from management to ensure that the promise will be delivered.

Buyer	StatPro Group
Seller	Performa Consultants
Seller Description	A provider of software to the investment management industry
Acquiring	100%
Price	£7 million
Comment	Statpro posted an excellent performance in their recent results. On both revenues and profitability the company showed it can grow organically and successfully integrate international acquisitions (following four purchases in 2006 and 2007). This acquisition further builds on their scale and capabilities, to position them for further growth.

Buyer	Ascom Holding AG
Seller	Argogroup
Seller Description	A provider of software and managed services that maximize the end-user quality of experience on mobile applications and the new generation of converged services.
Acquiring	100%
Price	n/a
Comment	This acquisition strengthens Ascom's position in the global market of mobile and stationary network testing. It also gives them an increased foothold in Germany, since the deal also includes the German subsidiary Argogroup GmbH - based in Eningen near Stuttgart. The deal is an exit for 3i, the previous investors in Ascom.

Buyer	BT Group
Seller	Frontline
Seller Description	A provider of IT services in Asia
Acquiring	Majority acquisition
Price	$139.5 million (estimated)
Comment	This acquisition strengthens the BT presence in the Asian markets, giving them a stronger entry point into the rapidly expanding markets in the region.

Mergers and Acquisitions – March 2008

Buyer	Portrait Software
Seller	Million Handshakes AS
Seller Description	A provider of outbound campaign management and dialog marketing software
Acquiring	Majority acquisition
Price	n/a
Comment	The acquisition of Million Handshakes is designed to add to the existing suite of products that Portrait Software takes to market.

Buyer	EDS
Seller	Nexagent
Seller Description	A provider of hardware and software solutions for network service provisioning and advanced IP-based services
Acquiring	Asset purchase
Price	n/a
Comment	The impact of convergence is that many IT services firms, like EDS, are eyeing the telecoms market. EDS is therefore expanding its own network services offerings and Nexagent will help build these capabilities. The deal is designed to lower the cost and operational difficulties in migrating clients to the EDS Network.

Buyer	EuroConnXion Holdings PLC
Seller	DB Systems Pty., Ltd.
Seller Description	An Australian information technology consulting services company.
Acquiring	100%
Price	n/a - share swap
Comment	As well as giving the UK headquartered EuroConnXions a richer presence in Australia the deal has another rationale. The acquisition of DB Systems would complement EuroConnXion's existing SaaS and IT managed services businesses, providing additional technical skills and collateral sales opportunities. The transaction would further expand EuroConnXion's sales capabilities.

Buyer	Solarsoft Business Systems Limited
Seller	VantagePoint Systems, Inc.
Seller Description	Develops, implements and supports business software for packaging manufacturing companies
Acquiring	100%
Price	$10.1 million estimate
Comment	Solarsoft has emerged as another in a growing list of mid-market consolidators (along with the likes of 2e2 and Maxima in the UK). Its backers, Marlin Equity Partners of California, seem intent on using Solarsoft as a vehicle for a transatlantic roll-up strategy in mid-market software and IT services.

Buyer	RWS Holdings plc
Seller	Document Service Center Technische Uebersetzungen und Software-Lokalisierung GmbH
Seller Description	A provider of technical translations to a broad base of German and Swiss corporates.
Acquiring	100%
Price	£6.8 million
Comment	The acquisition of Document Service Center would enhance and strengthen RWS Holdings' position as translation provider.

Buyer	Nstein Technologies, Inc
Seller	Picdar
Seller Description	A provider of digital workflow and asset management (DAM) solutions to newspapers, magazine and corporate publishers.
Acquiring	100%
Price	$6.6 - 9.2 million (estimated)
Comment	This acquisition would give Nstein an opportunity to increases its market share in Europe and strengthen its position as online publishing solutions provider for the media industry.

UK software and IT services share prices and market capitalisation - March 2008

	SCS Cat.	Share Price 31-Mar-08	Capitalisation 31-Mar-08	Historic P/E	PSR Ratio Cap./Rev.	S/ITS Index 31-Mar-08	Share price move since 29-Feb-08	Share price % move in 2008
@UK plc	SP	0.04	1.42	NA	0.98	61.07	0%	-50%
Alphameric	SP	0.20	45.08	NA	0.68	91.74	-13%	-35%
Alterian	SP	1.25	54.09	22.5	3.86	625.00	0%	8%
Anite Group	CS	0.40	137.78	7.8	0.80	233.92	-7%	-25%
Ascribe	SP	0.21	24.69	NA	4.62	1,105.26	-20%	-32%
Atelis plc	SP	0.01	0.21	NA	NA	39.53	-24%	-55%
Atlantic Global	SP	0.14	3.21	61.7	1.50	474.58	-13%	0%
Autonomy Corporation	SP	8.89	1899.81	61.2	14.81	271.37	-6%	1%
Aveva Group	SP	11.10	749.44	42.2	11.37	5,550.00	12%	15%
Axon Group	CS	3.98	250.93	12.5	1.82	2,274.29	-29%	-24%
Belgravium Technologies Plc.	SP	0.09	8.96	6.3	1.72	600.00	-18%	-10%
Bond International	SP	1.21	39.49	9.0	2.30	1,861.54	2%	-26%
Brady	SP	0.40	10.95	22.2	4.50	493.83	-11%	-9%
Business Control Solutions	CS	0.03	6.45	NA	0.81	480.00	0%	0%
Business Systems	CS	0.13	10.94	NA	0.32	109.24	-13%	8%
Cantono	CS	0.04	10.59	NA	1.47	663.64	-6%	-40%
Capita Group	CS	6.79	4126.23	29.8	2.43	183,547.44	4%	-3%
Centrom	CS	0.01	1.67	NA	0.27	166.67	0%	0%
Charteris	CS	0.18	7.10	24.6	0.80	200.00	-10%	-18%
Chelford Group	CS	2.09	14.89	203.4	0.80	363.48	23%	49%
Civica	CS	2.67	168.11	14.9	1.59	1,525.31	35%	37%
Clarity Commerce	SP	0.20	6.41	NA	0.48	160.00	-26%	-26%
Clinical Computing	SP	0.03	3.19	NA	1.93	24.19	0%	0%
CODA Plc.	SP	2.05	157.60	20.3	2.95	1,265.43	0%	17%
Computacenter	R	1.73	268.20	9.5	0.12	258.21	-4%	-8%
Corero	SP	0.05	1.82	NA	0.29	66.67	-17%	-17%
Dealogic	SP	1.40	93.60	9.8	2.33	608.69	-11%	-20%
Delcam	SP	2.58	15.93	10.5	0.66	992.31	-21%	8%
Detica	CS	2.48	287.29	24.9	1.84	3,100.00	0%	13%
Dicom Group	R	1.96	162.66	16.7	1.02	600.86	4%	12%
Dillistone Group	SP	1.75	9.45	NA	NA	1,282.05	-1%	-18%
Dimension Data	R	0.50	774.75	17.8	0.56	88.81	-4%	-19%
DRS Data & Research	SP	0.24	7.68	7.4	0.62	218.18	0%	0%
eg Solutions	SP	0.12	1.64	NA	0.30	81.63	0%	-50%
ELCOM	CS	0.02	8.28	NA	23.91	400.00	0%	0%
Electronic Data Processing	SP	0.58	14.10	29.4	2.02	1,775.87	0%	-2%
FDM Group	A	1.02	23.57	8.4	0.53	1,251.53	-9%	-18%
Ffastfill	SP	0.07	26.38	NA	9.95	58.33	-13%	0%
Fidessa Group Plc.	SP	7.39	256.10	NA	2.71	4,347.06	-20%	-11%
Financial Objects	CS	0.40	17.56	6.5	0.88	173.91	-11%	-17%
Flomerics Group	SP	0.89	20.12	21.8	1.42	3,423.08	56%	62%
Focus Solutions Group	CS	0.27	8.25	4.9	0.83	138.46	-21%	-23%
GB Group	CS	0.23	19.42	NA	1.29	148.35	0%	-8%
Gladstone	SP	0.23	11.74	8.6	1.53	575.00	15%	21%
Gresham Computing	CS	0.47	24.84	57.0	1.78	505.38	-23%	-16%
Group NBT	CS	2.01	50.54	18.3	6.02	1,005.00	-12%	-1%
Harvey Nash Group	A	0.52	37.67	8.0	0.15	297.14	0%	-4%
Highams Systems Services	A	0.04	1.24	NA	0.09	111.11	0%	-20%
Horizon Technology	CS	0.79	65.24	NA	0.34	291.45	156%	7%
IBS OPENSystems	CS	1.18	44.89	9.0	2.87	773.77	8%	-28%
I S Solutions	CS	0.23	5.30	12.2	0.96	857.10	0%	5%
IDOX	SP	0.09	32.06	27.9	2.26	11.55	-18%	-25%
ILT Solutions	SP	0.02	1.48	NA	0.81	18.59	-17%	-40%
Imaginatik	SP	0.05	6.26	NA	4.47	588.24	-7%	29%
In Technology	CS	0.29	40.59	NA	0.22	1,160.00	0%	-9%
InterQuest Group	A	0.84	24.41	11.1	0.88	1,460.87	-3%	-2%
Innovation Group	SP	0.31	196.43	24.8	3.22	135.37	-3%	-9%
Intelligent Environments	SP	0.07	11.81	20.3	3.79	74.47	-13%	-22%
Intercede Group	SP	0.28	9.93	NA	5.50	466.67	-18%	-20%
Invu	SP	0.22	24.35	11.2	3.75	2,315.77	-8%	-27%

UK software and IT services share prices and market capitalisation - March 2008

	SCS Cat.	Share Price 31-Mar-08	Capitalisation 31-Mar-08	Historic P/E	PSR Ratio Cap./Rev.	S/ITS Index 31-Mar-08	Share price move since 29-Feb-08	Share price % move in 2008
K3 Business Technology	SP	1.30	31.65	12.8	1.16	993.28	-6%	-19%
Kewill	SP	0.82	66.84	45.4	1.61	1,620.55	0%	0%
Knowledge Technology Solutions	SP	0.01	3.05	NA	2.44	200.00	0%	0%
LogicaCMG	CS	1.05	1542.59	NA	0.58	1,437.96	13%	-11%
Macro 4	SP	1.42	31.34	4.9	0.95	572.58	0%	-3%
Manpower Software	SP	0.51	22.80	23.2	5.26	525.77	-11%	-6%
Maxima Holdings	CS	1.46	36.38	7.6	1.14	1,061.82	-5%	-40%
Mediasurface	SP	0.04	5.00	NA	0.52	294.12	-20%	-20%
Micro Focus	SP	1.85	370.98	15.9	4.91	0.00	-8%	-27%
Microgen	CS	0.45	46.30	11.5	1.23	192.31	0%	-4%
Minorplanet Systems	SP	0.18	6.04	4.4	0.25	367.57	-22%	-28%
Misys	SP	1.38	692.27	26.6	1.23	1,716.88	-8%	-25%
Monitise	CS	0.07	17.18	NA	0.04	45.00	-31%	-51%
Morse	R	0.58	74.80	4.1	0.20	232.00	5%	-13%
NCC Group	CS	3.33	111.82	21.0	4.40	1,994.01	-13%	-12%
Ncipher	SP	2.11	35.46	19.4	2.04	844.00	0%	-3%
Netcall	SP	0.17	11.39	15.4	3.44	343.44	-23%	-23%
Netstore	CS	0.20	36.25	23.9	1.81	133.33	-17%	-20%
Networkers International	A	0.27	24.41	11.2	1.28	843.75	-4%	-13%
Northgate Information Solutions	CS	0.95	553.35	15.7	1.57	365.38	0%	3%
NSB Retail Systems	SP	0.38	142.86	16.1	2.95	3,304.35	0%	0%
OneclickHR	SP	0.04	5.39	NA	0.91	100.00	0%	0%
OPD Group	A	1.71	45.42	5.6	1.04	777.27	-3%	-9%
Parity	A	0.50	18.82	50.2	0.12	462.96	0%	-9%
Patsystems	SP	0.25	45.16	21.7	2.95	233.65	-11%	-7%
Phoenix IT	CS	2.84	212.23	12.8	1.68	1,051.85	8%	-11%
Pilat Media Global	SP	0.38	21.02	8.8	1.62	1,900.00	-3%	-10%
Portrait Software	CS	0.11	10.18	26.3	0.71	72.22	0%	-21%
Proactis Holdings	SP	0.45	13.85	NA	7.29	927.84	-13%	-33%
Prologic	CS	0.85	8.50	9.9	1.23	1,024.10	-2%	-4%
QinetiQ Group	CS	1.91	1259.86	19.2	1.10	870.16	-4%	-3%
Qonnectis	CS	0.02	4.81	NA	43.96	533.33	0%	0%
RM	SP	2.02	187.38	19.8	0.69	5,771.43	-7%	-8%
Sage Group	SP	1.88	2457.80	NA	21.19	72,307.69	-5%	-18%
Sanderson Group	SP	0.34	14.72	11.3	0.91	680.00	-11%	-28%
SciSys	CS	0.23	6.48	4.7	0.26	178.29	-26%	-50%
SDL	CS	2.98	223.44	23.3	2.36	1,986.67	3%	9%
Serpower Technologies	SP	0.14	12.50	NA	1.57	140.00	0%	0%
SiRViS IT plc	CS	1.52	5.00	7.6	0.63	1,321.74	-4%	-13%
smartFOCUS plc	SP	0.09	8.58	15.7	0.93	972.97	-18%	-25%
Sopheon	SP	0.13	19.29	NA	3.22	187.05	-13%	-7%
Spring Group	A	0.48	78.40	12.8	0.19	533.33	-4%	-2%
SSP Holdings	SP	1.16	95.85	11.1	5.36	1,094.34	-7%	-16%
StatPro Group	SP	0.71	39.50	10.6	3.11	887.50	-17%	-18%
SThree Group plc	A	1.95	260.99	8.1	1.08	946.60	-13%	-13%
Stilo International	SP	0.02	1.62	9.3	0.70	31.00	55%	55%
Strategic Thought	CS	0.38	9.87	NA	0.86	276.75	12%	-7%
Tadpole Technology	SP	0.02	6.70	NA	1.39	48.28	0%	-33%
Tikit Group	CS	2.27	29.26	12.7	1.25	1,973.91	-4%	-13%
Total Systems	SP	0.31	3.26	NA	0.93	584.91	-6%	32%
Touchstone Group	SP	1.08	12.79	6.5	0.42	1,028.57	-6%	-22%
Triad Group	CS	0.25	3.79	NA	0.09	185.19	-4%	0%
Ultima Networks	R	0.02	3.43	43.0	1.80	40.73	67%	67%
Ultrasis Group	SP	0.01	19.95	NA	16.05	20.41	0%	0%
Universe Group	SP	0.05	6.02	NA	0.14	222.22	-17%	-17%
Vega Group	CS	2.76	56.08	15.5	0.87	2,262.30	0%	1%
Vero Software Plc.	SP	0.18	6.52	NA	0.67	350.00	-9%	11%
Xchanging	CS	2.81	603.20	29.0	NA	919.80	3%	0%
Xpertise Group	CS	0.95	5.30	3.9	0.33	3,800.00	-19%	-17%
XploITe	CS	0.40	16.80	23.7	0.57	1,230.77	-31%	-32%

Note: We calculate PSR as market capitalisation divided by sales in the most recently announced financial year.
Main **SYSTEM**HOUSE S/ITS Index set at 1000 on 15th April 1989. Any new entrants to the Stock Exchange are allocated an index of 1000 based on the issue price. The Ovum Index is not weighted; a change in the share price of the largest company has the same effect as a similar change for the smallest company. **Category Codes: CS** = Computer Services **SP** = Software Product **R** = Reseller **A** = IT Staffing Agency

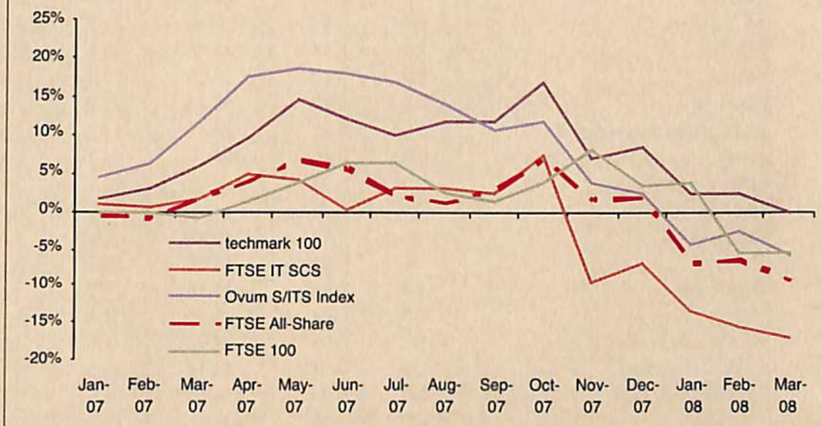
IT COULD BE WORSE!

Samad Masood
Analyst

Overall declines in share prices continued in March. The IT indices we track fell by between 1.7% (FTSE IT SCS) and 3.3% (Ovum S/ITS) in the month, which was generally in line with falls across the overall market (FTSE All-Share down by 2.9% and the FTSE 100 down by 3.1%).

But there is some evidence to contradict the doom-mongers who fear the end is nigh for IT. Since the start of the year, IT indices have fallen slightly less than the overall market (-7.8% techMark 100, -10.9% FTSE IT SCS, and -8.2% for Ovum S/ITS – compared to -10.9% and -11% for the FTSE All-Share and 100 indices respectively). It's certainly not justification to claim that IT is not hurting, but clearly, this industry is not taking much of a bigger hit than the average.

Performance of selected UK indices over January 2007 to end of March 2008



Source: Ovum

Nonetheless, in times like these, investors can be that much more jittery – and reactions to even the slightest bad news can send shares tumbling. Take Sthree for example, the staffing agency that published very strong full year numbers in February – with revenue up 32.9%. In March it released a generally positive interim management statement with a small mention that business in the financial service sector was looking soft. Shares have since tumbled 13% to £1.95, wiping £41m off the company's value, even though management do not consider the financial services sector to be a large enough part of the business to affect overall performance.

As a staffing agency, one could argue that Sthree is at the brunt of any jitters in the market. This sector is seen by many as a bellweather for the IT industry and, as such, concerns about future prospects have driven down average share prices in this segment by 4%. This compares to services companies and resellers that were generally flat on average in the month.

But it was software companies that took the biggest hit on average – down by 6.3%. Again this can be seen as due to general jitters in the market related to concerns of an economic recession. When IT budgets get cut, it is new software purchases that are the first things to get stopped. Indeed, the only software vendors that grew their share prices in the month were those that had some external interest buying up shares. That is apart from Aveva, a long standing high-performer and investor favourite.

Unsurprisingly, it is M&A interest that accounts for much of the biggest share movements across the board. Interest in Civica and Chelford Group has driven their share prices up by 35% and 23% respectively. Meanwhile Xploite, the company founded to consolidate smaller IT companies, announced that discussions with a buyer had ended – resulting in its share price falling 31% to 40 pence.

All in all, there are no signs that the feared recession is hitting IT stocks more than other industries, or that the declines are accelerating. Ultimately, the main underlying performance drivers related to M&A and organic growth remain. That said, investors are also more sensitive to bad news, and are still more likely to see the glass half empty.

SYSTEMHOUSE

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