

Ebix: Building a Wide Moat

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Ebix ([EBIX](#)) began operations in 1976 as Delphi Information Systems, a supplier of agency management software primarily to the property & casualty industry. Unable to maintain a profitable business, the company went through a succession of CEOs in the 90s. Finally, with its very existence at stake, the company transitioned to a new management under Robin Raina in the year 2002. This new management aggressively cut costs, moved product development to India to take advantage of lower cost base and focussed on growing revenues. In addition, the management made a deliberate decision to expand its product offerings to include - infrastructure software such as exchanges that could be used by insurance carriers to connect with the brokers and agents, carrier backend systems and broker backend systems to handle the entire life cycle of insurance policies. Today, EBIX has grown to become a leading provider of end-to-end solutions to the Insurance industry around the world.

To be an airport or an airline?

Recall how we can choose an airline to fly with but the airport is not really a choice. There is typically only one in a city. Ebix aims to be that airport by providing exchange infrastructure that power insurance transactions. Therein lies the company's moat. Exchanges are like landgrabs with strong resistance to entry of late entrants in the market. Ebix moved in early and capitalized on the opportunities in life insurance exchange, annuities exchange in the US and P&C exchanges in Australia. Today, Ebix operates data exchanges in the areas of life insurance, annuities, employee health benefits and P&C insurance. Ebix's life exchange processes close to 16 million transactions every year in the US. Ebix's annuity exchange powers in excess of 40 billion in premiums every year in the US. Ebix Exchange in Australia powers the majority of P&C insurance transactions.



Exchange revenue is primarily derived from transaction fees charged for each data transaction processed on EBIX Exchange. Hence, this revenue is recurring in nature and provides a stable, predictable cash flow. Ebix Exchange family of products currently generate about 70% of total Ebix's revenues and will continue to be the most important piece of Ebix.

Ebix back-end carrier and broker system platforms generate revenues under a subscription or license based model. Unlike Ebix Exchange, these products are somewhat exposed to internal spending cycles and budget allocations within the industry. These products account for ~ 20% of Ebix's revenues.

The remaining 10% is made up by the business process outsourcing (BPO) services which include insurance certificate origination, certificate tracking, claims adjustment call center and back office support.

Swinging at fat pitches or rash acquisition spree?

It is true that Ebix has grown by acquiring companies in related product categories. In 2009, Ebix acquired E-Z data Inc (insurance industry customer management software), Peak Performance Solutions (software provider for workers compensation claims processing, managed care tracking), Fact Services Inc (software provider for healthcare claims processing, employee benefits and managed care). Similarly, in 2008, Ebix acquired four companies. Noteworthy among them is the Telestra acquisition. According to Robin, this was a "extremely accretive" deal. It is a monopoly business with highly predictable revenue stream. The main product of this acquisition, Sunrise Exchange, enables

insurers and brokers in Australia to process insurance policies electronically.

This is the engine brokers use in the Australian P&C insurance market and it boasts of ~ 90% market share. Note that Ebix has never over-paid for its acquisitions, preferred to use internally generated cashflow and avoided using its shares to pay for the transaction. All acquisitions are required to be accretive to Ebix's earnings right away. A key criterion for a acquisition candidate is the chance of dominance in that area of business. In essence, Ebix only acquires companies that deliver convergence with its technology and existing platforms and provide opportunities for cross selling.

By being aggressive yet disciplined in the recent turmoil, the management has shown itself to be opportunistic and willing to take advantage of market situations.

Valuation

Ebix revenue have increased from 29.25 million in 2006, 42.84 million in 2007, 74.75 million in 2008 to 97.72 million in 2009. Net Income has increased from 6 million in 2006, 12.7 million in 2007, 27.3 million in 2008 to 39 million in 2009. 2010 Q1 revenue was 32 million with net income coming in at 12.4 million. Ebix generated 34 million in free cash flow in 2009 and expects to generate at least 50 million in cash flow in the current year. With no net debt and enterprise value of ~ 500 million, EBIX trades at an attractive 10% cash flow yield. In addition, the management (who is very conservative and rarely gives guidance) has stated that they are targeting 200 million annual run rate of revenue by 4Q of 2011 with ~40% in operating margin.

Additional Points to take note of

1. Robin Raina, CEO & Chairman of the board, is primarily the key decision maker. He has been the architect of the turn-around and it is his strategic direction that has led the company back to profitability. He owns ~11% of the shares outstanding and is the second largest shareholder of the company. To a large extent, Ebix does depend on his vision and leadership.
2. Recent account signings at Ebix Exchange include Bank of America ([BAC](#)), Wells Fargo ([WFC](#)), Fidelity, US Bank, Ameriprise ([AMP](#)), John Hancock, Genworth ([GNW](#)), etc. Such large accounts should help strengthen the growth of Ebix Exchange systems in the US. Network effect in action.
3. Management has stated the intention to build on its success and deploy new exchanges across the world. Specifically, Ebix has stated plans to grow its presence in Latin America and Asia. With its ability to save significant costs via end-to-end software solutions versus the legacy paper-based processes, Ebix can continue to win markets in its niche - the insurance sector.

Disclosure: Long EBIX

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