

23 March 2010

Sector: IT

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## Infotech Enterprises (Rs354)

*'Engineered for growth'*

BUY

Target Price: Rs450

Infotech Enterprises' strong domain expertise in engineering services and relationships with marquee clients are expected to drive 19% revenue CAGR in this segment over FY09-12E. Key clients such as UTC have seen recovery in key financial metrics and are expected to return to growth going forward, a key positive given 60% revenue contribution from top-10 clients. In the UTG segment, Infotech has an addressable market of US\$ 6.5-7 bn and serves key clients like Tele Atlas, and the US and UK governments. Recent deal wins from the government could be good reference points for future orders. We forecast 15% and 29% CAGRs in top-line and net profit over FY09-12E. At the CMP, the stock trades at 9.9x FY12E EPS (8.4x adjusted for cash). **We Initiate Coverage on the stock with a 'Buy' recommendation and 12-month target price of Rs 450, implying a P/E of 12.5x FY12E EPS.**

- Strong client relationships, the key to sustaining growth:** Infotech Enterprises enjoys strong long-term strategic relationships with its top clients, which we believe is a key factor that has enabled the company to record strong growth in its engineering services business. The company counts marquee names as clients such as United Technologies, Bombardier, Boeing and Airbus. The combined revenues, R&D expenses, SG&A expenses and capex of these companies amounts to US\$ 152 bn, US\$ 12 bn, US\$ 14 bn and US\$ 5 bn, respectively. A recovery has been seen in key financial metrics of these clients and going forward, a return to growth is forecast as per consensus estimates taken from Bloomberg. This we believe is a key positive for Infotech, given its significant dependence on these clients for growth (60% revenue contribution from top-10 clients). We believe there is significant potential for growth and expansion of the scope of work done by Infotech with these clients and the recovery we expect will drive volumes for the company.
- Significant growth opportunity in engineering services:** As per the NASSCOM Booz-Allen Hamilton Report 2004, Indian engineering service revenues have the potential to grow to US\$ 40 bn by 2020. Infotech provides a broad array of service offerings in its engineering services business such as mechanical design, electronic design, technical publications, engineering software development and product lifecycle management to clients across verticals like aerospace, automotive, energy and hi-tech. The company appears well-positioned to leverage the significant growth opportunity. We forecast 19% revenue CAGR in this segment over FY09-12E.
- UTG segment - Smaller but significant opportunities:** The market for GIS services stands at US\$ 6.5-7 bn with Infotech addressing US\$ 1.5 bn. The company counts illustrious names as its clients such as Tele Atlas, KPN Telecom and the UK & US governments. There is significant growth potential in the Indian GIS market also with opportunities in digitisation of land records, etc. Infotech has already won an order from the Karnataka government for digitisation of property records, which will serve as a reference point for future deal wins.
- Reasonable valuations:** At the CMP, the stock trades at a P/E of 9.9x FY12E EPS. Adjusted for cash per share of Rs 71 and net interest income, valuations are even more attractive at 8.4x FY12E EPS. These valuations appear reasonable given the 12.4% CAGR in earnings expected over FY10-12E (13.4% CAGR adjusted for interest income) and historical P/E band of the stock. Given Infotech's positioning as a focussed engineering services player, good growth record, recent deal wins and long-term relationships built with marquee clients, we expect the company to grow at a faster-than-industry rate. **We Initiate Coverage on Infotech Enterprises with a 'BUY' recommendation and 12-month target price of Rs 450, implying a P/E of 12.5x FY12E EPS.**

Infotech Enterprises		Y/E March (Rs mn)	FY08	FY09	FY10E	FY11E	FY12E
Reuters/Bloomberg Code	INFE.BO/INFTEC@IN	Net Sales	6,741	8,898	9,676	11,464	13,538
Market Cap. (Rsbn)	20	EBITDA	1,217	1,785	2,098	2,404	2,791
Market cap. (US\$m)	428	Net Profit	856	925	1,572	1,738	1,988
Shares Outstanding (mn)	55	EPS (Rs)	15.4	16.7	28.4	31.3	35.9
52-week High/Low (Rs)	369 / 80	EPS Growth (%)	2.3	8.1	70.0	10.6	14.4
		EBITDA margin (%)	18.1	20.1	21.7	21.0	20.6
		PER (x)	22.9	21.2	12.5	11.3	9.9
Major Share Holders (%)		P/BV (x)	2.9	2.5	2.1	1.8	1.6
Promoter/Majority	23.4	Price/sales (x)	2.9	2.2	2.0	1.7	1.4
FII's	52.5	EV/EBITDA (x)	15.4	9.2	7.2	5.7	4.3
Banks/FIs/MFs	12.7	ROE (%)	17.7	12.8	18.7	17.7	17.4
Public & Others	11.4	ROCE (%)	20.8	13.6	23.1	22.3	22.4

Source: Company and Karvy Estimates

## Investment positives

### Top clients - Key to growth for Infotech; return to growth forecasts a key positive

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*The top-5 and top-10 clients contribute around 45% and 60%, respectively to Infotech's revenues*

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*The prospects of key clients like UTC we believe will be key determinants of Infotech's future prospects*

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*All major financial metrics for these companies reflect an economic upturn, a key positive for Infotech*

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Infotech Enterprises depends mainly on its top clients for growth of its business. The top-5 and top-10 clients contribute around 45% and 60%, respectively to the company's revenues, reflecting their importance. Infotech's top client, the UTC Group (United Technologies, including Pratt & Whitney, Hamilton Sundstrand and Sikorsky) contributes a fairly significant 24% to its revenues. The company is looking to bring down its exposure to its top-10 clients to around 40% over the next 3 years. However, it is quite clear that the top-10 clients account for the lion's share of revenues and remain the key to its growth going forward.

In such a case, it is apparent that the fortunes of Infotech are significantly dependent on those of its key clients. The prospects of key clients like UTC, Boeing, Bombardier and Schlumberger we believe will be key determinants of the future prospects of Infotech.

We believe going forward it will be a market share game for Infotech. As the company's key clients recover from the recession, get back to a period of growth and start making investments in growing their businesses, they will increasingly look to offshore their engineering work to players like itself, primarily owing to the strategic long-term relationships they share with it, strong domain knowledge built up by the company over the past 10 years in the engineering services business, consistent expansion of services into newer verticals and superior growth track record.

A brief overview of the sales, operating profit, R&D expenses, SG&A costs and capex of Infotech's key clients reflects a recovery from 4QCY09. All major financial metrics for these companies reflect an economic upturn, which we expect to sustain going forward. We have also taken consensus analyst forecasts and views for these companies based on Bloomberg data. Consensus estimates largely suggest a return to growth in CY11 for these clients, a major positive for Infotech. It should be noted that even during the recession, its top clients did not slash their budgets and with growth expectations from CY11, these clients are expected to increase their engineering budgets, implying greater volume of work.

### UTC Group

The UTC Group as we have mentioned is Infotech's largest client, accounting for around 24% of its revenues. Infotech works with major divisions of UTC such as Pratt & Whitney, Hamilton Sundstrand and Sikorsky in a number of areas such as engineering, maintenance, repair & overhaul (MRO), SAP and product development, reflecting the significant scope of the contract and domain expertise built up with its largest client in its business. Consequently, growth prospects of the UTC Group are undoubtedly one of the biggest factors that is likely to determine those of Infotech itself, given the group's major contribution to its revenues.

As can be seen in Exhibit 1, after a dip in 2Q and 3QCY09, revenues for Pratt & Whitney picked up in 4QCY09 in line with the recovery in the

global economy. As regards Hamilton Sundstrand and Sikorsky, revenue rose with each quarter of CY09 (with the exception of 3QCY09 for Hamilton Sundstrand, when sales were flat). For the UTC Group as a whole, order bookings remained "largely stable" and saw a recovery in key Asian economies like China. Consensus estimates suggest around 5% revenue growth in CY11 after 3.5% growth in CY10. Margins are also expected to rise by 70 bps in CY11. Thus, we believe improved prospects for the UTC Group will translate into increased order flows for Infotech. A look at the cost side also shows that SG&A expenses increased for UTC in 4QCY09 after a dip in 3QCY09, reflecting renewed initiatives to reduce costs through greater offshoring of key engineering functions to vendors like Infotech.

### **The Boeing Company**

The Boeing Company is one of the largest civil and military aircraft manufacturers in the world and is a key client of Infotech. The software company works with Boeing in the areas of cabin electronics, wing structures and in-flight entertainment. Revenues for Boeing saw a strong rebound in 4QCY09 from the previous quarter, as the global economy started moving towards a sustainable recovery. In fact, revenues for the full year CY09 came in at a record high of US\$ 68.3 bn on higher commercial deliveries and growth in defense, space and security. Consensus forecasts for CY11 imply a 4% growth in revenues, margin expansion and 7% growth in net profit. Even as the company expects to remain operationally efficient going forward, it is expected to focus on certifying and delivering the 787 and 747-8 models and further reposition its defense, space and security business, implying more engineering work such as wing design for vendors like Infotech.

### **Bombardier**

Bombardier is a leader in the global aerospace and rail transport sector, manufacturing state-of-the-art commercial and business jets and trains. Infotech works with Bombardier in the area of bogie design. The company saw its revenues get back on the growth track in 4QCY09. While growth forecasts for the next year are by and large flat, a positive implication is that its engineering budgets are likely to remain stable. Thus, it will be a market share game for Infotech going forward, as it aims to garner a greater share of its client's budgets to grow at a decent pace.

### **Schlumberger**

Schlumberger is one of the world's leading oilfield services companies that supplies technology, information solutions and project management services to customers in the oil and gas industry. The company saw an increase in revenues in 4QCY09 post declines in the previous 2 quarters, with revenues increasing in North America, Latin America and Middle East & Asia, driven by increasing deepwater rig count. Looking ahead to CY10, management believes the business outlook is dependent on the prospects for the general economy. Consensus forecasts predict that oil demand in 2010 will increase, particularly in the developing world, for the first time since 2007. Thus, management believes oil prices are likely to be sustained at current levels and customers' exploration and production

budgets will increase. Consequently, this will result in strong growth prospects and consensus forecasts prove this, with revenue growth expected to come in at 9% in CY10 and significantly accelerate to nearly 19% in CY11, along with margin expansion and strong earnings growth of 14% and 33% in CY10 and CY11, respectively. This is a strong positive for Infotech and suggests increased volume of work as Schlumberger expands its business.

#### **KPN Telecom**

KPN is a leading telecom service provider in The Netherlands offering wireline and wireless telephony, internet, TV and ICT services to consumers and business. The company after a dip in revenues in 3QCY10 recorded a rebound in 4QCY10. SG&A costs and capex also witnessed a rise, reflecting an improving business environment. Consensus forecasts suggest around 2% revenue growth in CY10 and CY11, thus showing stability. Given that KPN is a key client for Infotech's UTG business, this implies that business volumes are likely to be stable with incremental volumes likely to come in at lower rates.

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*We believe Infotech's top clients are likely to witness stability in their respective businesses in CY10 followed by accelerated growth in CY11*

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Overall, we believe Infotech's top clients are likely to witness stability in their respective businesses in CY10 followed by accelerated growth in CY11 as the global recovery sustains. This in turn implies increasing business volumes for the software company going forward, as it aims to not only garner additional business from these clients but also gain market share from other vendors, something that has already been seen in the case of British Telecom. Thus, this is the biggest factor giving us confidence that Infotech will be able to sustain good volume growth going forward.

**Exhibit 1: Key financials, consensus forecasts for Infotech's key clients**

Company	1QCY09	2QCY09	3QCY09	4QCY09	CY09	CY10E	CY11E	% chg
<b>Pratt &amp; Whitney (US\$ mn)*</b>								
Sales	3,180	3,111	<b>3,031</b>	<b>3,255</b>	12,577	<b>54,791</b>	<b>57,448</b>	<b>4.8</b>
Operating profit	436	467	444	488	1,835	<b>7,521</b>	<b>8,288</b>	<b>10.2</b>
R&D expenses	409	384	344	421	1,558	NA	NA	
SG&A expenses	1,483	1,574	<b>1,424</b>	<b>1,555</b>	7,594	NA	NA	
Capex	167	173	161	325	826	NA	NA	
<b>Hamilton Sundstrand (US\$ mn)*</b>								
Sales	1,381	1,402	<b>1,400</b>	<b>1,416</b>	5,599	<b>54,791</b>	<b>57,448</b>	<b>4.8</b>
Operating profit	192	187	247	231	857	<b>7,521</b>	<b>8,288</b>	<b>10.2</b>
R&D expenses	409	384	344	421	1,558	NA	NA	
SG&A expenses	1,483	1,574	<b>1,424</b>	<b>1,555</b>	7,594	NA	NA	
Capex	167	173	161	325	826	NA	NA	
<b>Sikorsky (US\$ mn)*</b>								
Sales	1,334	1,389	<b>1,648</b>	<b>1,947</b>	6,318	<b>54,791</b>	<b>57,448</b>	<b>4.8</b>
Operating profit	116	133	157	202	608	<b>7,521</b>	<b>8,288</b>	<b>10.2</b>
R&D expenses	409	384	344	421	1,558	NA	NA	
SG&A expenses	1,483	1,574	<b>1,424</b>	<b>1,555</b>	7,594	NA	NA	
Capex	167	173	161	325	826	NA	NA	
<b>Schlumberger (US\$ mn)</b>								
Sales	6,000	5,528	<b>5,430</b>	<b>5,744</b>	22,702	<b>24,701</b>	<b>29,375</b>	<b>18.9</b>
Operating profit	1,171	768	960	983	4,120	<b>4,579</b>	<b>6,133</b>	<b>33.9</b>
Net income	938	613	787	795	3,134	<b>3,585</b>	<b>4,784</b>	<b>33.4</b>
R&D expenses	190	197	198	217	802			
SG&A expenses	341	351	<b>348</b>	<b>383</b>	1,425			
Capex	748	504	467	676	2,395			
<b>The Boeing Company (US\$ mn)</b>								
Sales	16,502	17,154	<b>16,688</b>	<b>17,937</b>	68,281	<b>64,911</b>	<b>67,693</b>	<b>4.3</b>
Operating profit	1,028	1,532	(2,150)	1,710	2,120	<b>4,854</b>	<b>5,100</b>	<b>5.1</b>
Net income	610	998	(1,564)	1,268	1,312	<b>2,929</b>	<b>3,129</b>	<b>6.8</b>
R&D expenses	970	960	3,574	1,002	6,506	NA	NA	
SG&A expenses	791	925	868	780	3,364	NA	NA	
Capex	442	296	227	221	1,186	NA	NA	
<b>Bombardier (US\$ mn)**</b>								
Sales	4,789	4,932	<b>4,571</b>	<b>5,429</b>	19,721	19,189	19,094	<i>(0.5)</i>
Operating profit	446	252	313	251	1,388	1,132	1,142	<i>0.9</i>
Net income	226	246	245	291	1,008	735	727	<i>(1.1)</i>
R&D expenses	40	47	34	50	171	NA	NA	
SG&A expenses	365	404	402	387	1,558	NA	NA	
Capex	255	169	162	189	775	NA	NA	
<b>KPN Telecom (Euros mn)</b>								
Sales	3,388	3,408	<b>3,307</b>	<b>3,371</b>	13,415	<b>13,612</b>	<b>13,826</b>	<b>1.6</b>
Operating profit	632	742	752	724	2,850	<b>3,045</b>	<b>3,114</b>	<b>2.3</b>
Net income	317	371	398	1,092	2,178	<b>1,810</b>	<b>1,865</b>	<b>3.0</b>
SG&A expenses	2,764	2,669	<b>2,579</b>	<b>2,647</b>	10,659	NA	NA	
Capex	456	386	360	565	1,767	NA	NA	

Source: Respective companies, Bloomberg, KSBL Research;

\* For Pratt & Whitney, Hamilton Sundstrand and Sikorsky, projections are taken for the entire UTC Group;

\*\* Bombardier's fiscal year ends in January, thus CY09=year ended January 31, 2009

**Engineering services - Significant opportunity for growth; expected to record US\$ 40 bn in revenues by 2020, implying more than 15% CAGR over next 10-12 years**

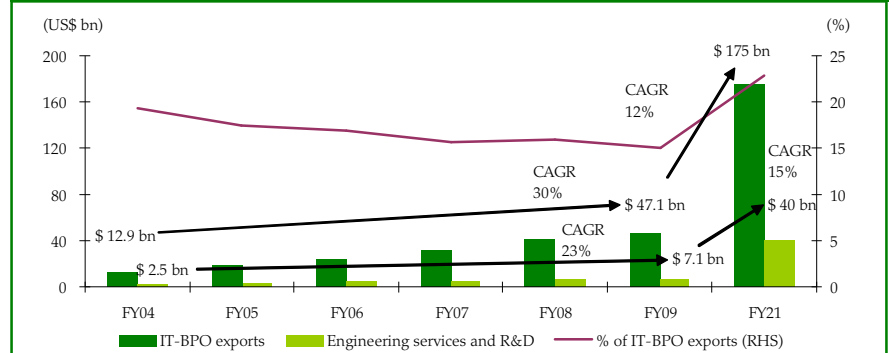
*As per the NASSCOM Booz-Allen Hamilton Report 2004, Indian engineering services revenues have the potential to grow to US\$ 40 bn by 2020, translating into over 15% CAGR over the next 10-12 years*

*NASSCOM has said that IT exports are expected to grow by 13-15% to US\$ 56-57 bn in FY11 indicating a strong recovery and is a reflection that the industry including engineering services is back on the growth path*

As per the NASSCOM Booz-Allen Hamilton Report 2004, the Indian IT industry has the potential to grow to US\$ 40 bn in offshore engineering service revenues by 2020. This implies a nearly six-fold increase from US\$ 7 bn revenues clocked by the research and development (R&D) and engineering services segments in FY09, translating into an over 15% CAGR over the next 10-12 years. The expected growth rate in engineering services is higher than the expected growth in overall IT-BPO exports, which stands at around 12% as per NASSCOM-McKinsey Perspectives 2020 (May 2009). Indian IT-BPO exports could potentially hit US\$ 175 bn by 2020 (US\$ 47.1 bn in FY09). Thus, engineering services as a percentage of IT-BPO exports are expected to rise from 15% in FY09 to nearly 23% over the next 10-12 years.

It should be noted that despite the recession, engineering revenues have continued to witness growth, increasing by 11% yoy in FY09. NASSCOM estimates IT-BPO exports to grow by just 5.5% in FY10 to US\$ 49.7 bn after 16.6% yoy growth in FY09 owing to the global economic recession. However, in its forecasts for FY11 the software association has said that IT-BPO exports are expected to grow by 13-15% yoy to US\$ 56-57 bn, indicating a strong recovery from the slower growth expected in FY10. Thus, the Indian IT industry including engineering services is expected to be back on the growth path in FY11.

**Exhibit 2: Engineering services - Significant scope for growth**



Source: NASSCOM Booz-Allen Hamilton Report 2004, NASSCOM-McKinsey 2020 Perspectives (May 2009), KSBL Research

### What is engineering services outsourcing?

Engineering services outsourcing (parts of which are also referred to as engineering BPO) is the practice of sourcing some or all of a company's design and engineering requirements from external service providers. Over the years, for instance outsourced product engineering (mechanical) services have graduated from basic drawing conversions and CAD migration assignments, through 2D - 3D modeling and digital mock-ups, conceptual design, analysis and validation; complete design outsourcing, manufacturing coordination, CPC / PDM; overall process quality improvement, e-engineering solutions, remote monitoring and system architecture development.

In the past, engineering services have been aggregated either under IT services (as R&D services) or under ITES-BPO (as engineering BPO). However, the evolution of market demand and increasing maturity of the vendor landscape for engineering services has highlighted the need for examining this as a separate segment.

The following table outlines the key differences between IT services and engineering services outsourcing.

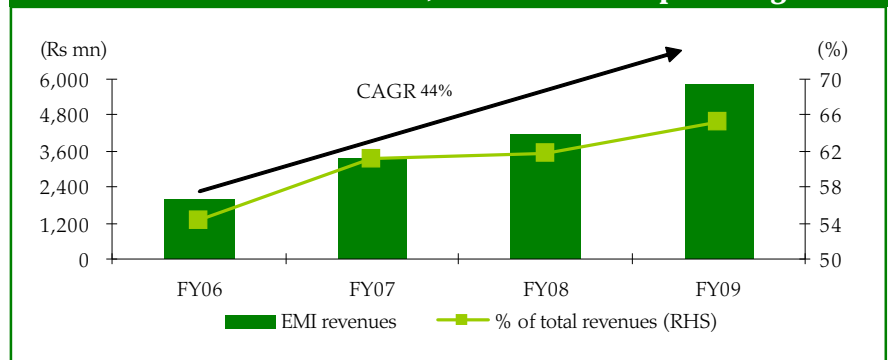
Parameter	Engineering Services	IT Services
Client sponsor	VP Engineering Engineering Program Manager	CIO IT Program Manager
Business dynamic (Vendor perspective)	Low annuity, smaller projects Change centric	High annuity, large projects Change controlled
Domain and process competencies	Industry domain skills, engineering quality processes	IT skills, software quality processes
Knowledge transfer management	High degree of knowledge transfer from client	Lower degree of core knowledge transfer from client
Switching costs (Client perspective)	Very high cost of exit due to up-front investment	Relatively lower cost of exit due to compartmentalized tasks
Value proposition	Reduction in variable cost Reduction in time to market	Reduction in fixed cost Reduction in execution time

*Infotech derives a majority of its revenues from the engineering services business (EMI, 65.3% in FY09, 64.1% in 9MFY10)*

### Infotech Enterprises - Well-positioned to tap the opportunity in engineering services

Infotech Enterprises is a focussed software company that derives a majority of its revenues from the engineering services business (EMI, 65.3% in FY09, 64.1% in 9MFY10), with the balance coming from the UTG segment (GIS services to the utilities, telecom and government segments). The company offers a wide range of services in this space in the areas of mechanical design, electronic design, technical publications, engineering software development and product lifecycle management (PLM). Infotech services marquee clients across the aerospace, automotive, energy, marine, hi-tech and rail verticals. The company's domain knowledge, technical skill sets and execution skills have enabled it to win marquee clients and grow at a strong pace.

**Exhibit 3: Infotech EMI revenues, contribution - Impressive growth**



Source: Company, KSBL Research

*Infotech has grown its engineering revenues in US dollar terms at a CAGR of 42% over FY06-09 to US\$ 126 mn in FY09 (US\$ 44 mn in FY06)*

Infotech Enterprises clocked US\$ 126 mn (Rs 5.82 bn) in EMI revenues in FY09. The company has grown its engineering revenues in US dollar terms at a CAGR of 42% over FY06-09 (US\$ 44 mn in FY06 to US\$ 126 mn in FY09). In Indian rupee terms, Infotech has reported a 44% CAGR in engineering revenues (Rs 1.97 bn in FY06 to Rs 5.82 bn in FY09). This performance is better than peers like TCS, Infosys and HCL Technologies, which have reported 23%, 38% and 29% CAGRs, respectively in revenues from this segment in dollar terms over the same period. It should be noted that the significant 134% CAGR recorded by Geometric in its engineering revenues over FY06-09 is primarily owing to its acquisition of Modern Engineering in FY07.

**Exhibit 4: Engineering revenues, CAGR - Infotech v/s peers**

(US\$ mn)	FY06	FY07	FY08	FY09	CAGR (%)
TCS	196	249	304	361	22.6
Infosys Technologies	39	49	67	103	38.4
HCL Technologies*	232	332	475	498	28.9
Geometric	3	21	46	42	134.0
<b>Infotech Enterprises</b>	<b>44</b>	<b>73</b>	<b>103</b>	<b>126</b>	<b>41.6</b>

Source: Respective companies, KSBL Research;

\* HCL Technologies has a June-ending fiscal year;

Note: Geometric's surge in engineering revenues in FY07 was owing to the acquisition of Modern Engineering.



*Infotech counts marquee names as its clients such as United Technologies Corporation, Bombardier, Boeing, Airbus and Philips in EMI, and BT, KPN Telecom and Tele Atlas in UTG*

**Strong client relationships, the key to sustaining growth; long-term relationships built with marquee names to drive revenues**

Infotech Enterprises as we have mentioned enjoys long-term strategic relationships with its top clients, which we believe is a key factor that has enabled the company to record strong growth in its engineering services business. It counts marquee names as its clients in engineering services, such as Pratt & Whitney, Hamilton Sundstrand, Sikorsky (all these companies are divisions of United Technologies Corporation - UTC, a US-based hi-tech products manufacturer and military contractor), Bombardier, Boeing, EADS Group (Airbus) and Philips. In the UTG segment also, Infotech counts well-known and reputed names such as British Telecom (BT), Swisscom, KPN Telecom, Schlumberger, Telcordia and Tele Atlas as its clients.

**Exhibit 5: Infotech Enterprises - Key clients across segments**

EMI	UTG
Pratt & Whitney	Tele Atlas
Hamilton Sundstrand	British Telecom
Sikorsky	Cox Communications
Bombardier	KPN Telecom
Boeing	Schlumberger
Airbus	Telcordia
Philips	Swisscom
Alstom	Rural Payments Agency (UK Government)
Vought Aircraft Industries, Inc.	HIS
Invensys Motor Systems	TNB Engineering Corporation

Source: Company

Infotech entered the engineering services vertical in the year 2000, with a contract from UTC. Since then, the company has recorded steady growth in this vertical through development of strong domain knowledge and expansion of services. The UTC Group is Infotech's largest client in terms of revenue contribution and the software company has over 1,100 people working on this account alone (35% of its total EMI employee base and 15% of its total employee base at the end of 3QFY10). UTC accounts for 24% of Infotech's revenues and the company provides a wide range of technical services to the group.

**Exhibit 6: EMI business - Key clients, scope of work**

Client	Scope of work	Engineers deployed	% of 3QFY10 employee base
UTC Group (Pratt & Whitney, Hamilton Sundstrand, Sikorsky)	Engineering, Maintenance, Repair & Overhaul (MRO), SAP, product development	1,100	15
Bombardier	Bogie design	400	6
Boeing + Airbus	Cabin electronics, wing structures, in-flight entertainment, mood lighting	300	4

Source: Company, KSBL Research

*Infotech's EMI clients are leaders in their respective fields with combined revenues, R&D and SG&A expenses, and capex of US\$ 152 bn, US\$ 12 bn, US\$ 14 bn and US\$ 5 bn, respectively*

The client profile of Infotech's key clients in its EMI business is fairly illustrious. All these companies are leaders in their respective fields. Combined revenues, R&D and SG&A expenses, and capex of these companies amounts to US\$ 152 bn, US\$ 12 bn, US\$ 14 bn and US\$ 5 bn, respectively (conversion of Euros to US dollars at 1 Euro = 1.35 US dollars). This reflects the significant size of these companies, their expenses on driving their operations and the significant potential for growth and expansion of the scope of work done by Infotech with these clients.

#### Exhibit 7: EMI business client profile - Illustrious lineage

Client	Industry	Revenues	Adj. profit	R&D exp.	SG&A exp.	Capex
Pratt & Whitney*	Leader in design & manufacture of aircraft engines, gas turbines	US\$ 12.6 bn	US\$ 2 bn	US\$ 1.6 bn*	US\$ 6 bn*	US\$ 826 mn*
Hamilton Sundstrand*	Leader in design & manufacture of aerospace and industrial products	US\$ 5.6 bn	US\$ 945 mn	US\$ 1.6 bn*	US\$ 6 bn*	US\$ 826 mn*
Sikorsky*	Leader in helicopter design & manufacture	US\$ 6.3 bn	US\$ 615 mn	US\$ 1.6 bn*	US\$ 6 bn*	US\$ 826 mn*
Bombardier**	Aerospace & rail transportation	US\$ 19.7 bn	US\$ 1 bn	US\$ 171 mn	US\$ 1.6 bn	US\$ 775 mn
Boeing#	Aerospace - Civil and military aircraft	US\$ 68.3 bn	US\$ 1.3 bn	US\$ 6.5 bn	US\$ 3.4 bn	US\$ 1.2 bn
Airbus\$	Aerospace - Civil and military aircraft	Euros 29 bn	Euros 1.8 bn	Euros 2.7 bn	Euros 2.3 bn	Euros 1.8 bn

Source: Respective companies, KSBL Research;

\* Pratt & Whitney, Hamilton Sundstrand and Sikorsky are all divisions of the UTC Group; figures are for CY09; adjusted profit is operating profit adjusted for restructuring expenses for each of these divisions; R&D expenses, SG&A expenses and capex are for the entire UTC Group;

\*\* Figures for Bombardier are for the year ended January 31, 2009;

# Figures for Boeing are for CY09;

\$ Figures for Airbus are for CY08; adjusted profit is EBIT; R&D expenses, SG&A expenses and capex are for the entire EADS Group of which Airbus is a part.

On the other hand, in the UTG business Infotech provides digital photogrammetry services, GIS data management, consultancy, application development, digitisation of data and asset utilisation services to its clients. The company counts Tele Atlas as its largest client. Infotech has over 1,200 people working on the Tele Atlas account (33% of its total UTG employee base and 17% of its total employee base at the end of 3QFY10). It provides street mapping for US and European cities to its largest UTG client. Apart from Tele Atlas, major telecom companies like BT and KPN Telecom are also clients of Infotech. The company also works with the UK and US governments.

#### Exhibit 8: UTG business - Key clients, scope of work

Client	Scope of work	Engineers deployed	% of 3QFY10 employee base
Tele Atlas	Street mapping for US and European cities	1,200	17
British Telecom	Data conversion solution enabling lower cost of failure and service delays	400	6
US & UK governments	Digital photogrammetry, GIS data management, consultancy and application development services	164	4

Source: Company, KSBL Research

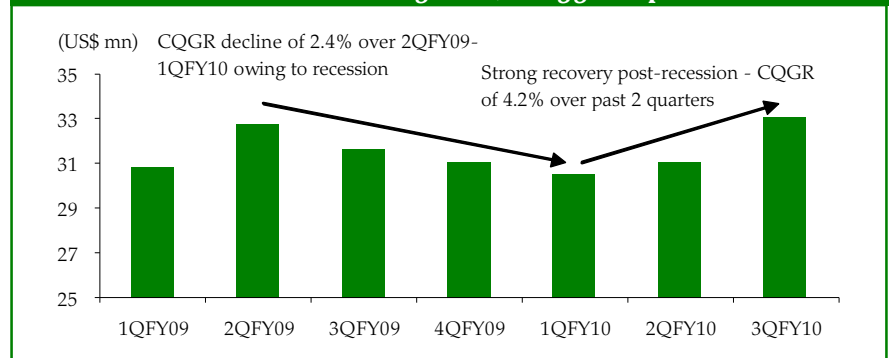
### Aerospace vertical accounts for majority of EMI revenues; 75-80% revenues annuity-based

Infotech's EMI business earns a majority of its revenues from the aerospace vertical, which contributes 60% to segment top-line. The rail segment contributes 25% to EMI revenues, with the balance revenues divided between the hi-tech and consumer electronics industries. Infotech in recent times has ventured into the marine and energy verticals as well.

*The EMI business earns a significant 75-80% as annuity revenues, a key positive feature of this business, enabling stability and predictability in revenues*

The EMI business earns a significant 75-80% as annuity revenues. This is a key positive feature of this business, enabling stability and predictability in revenues. Even when the global recession was at its worst, the fall in EMI revenues was contained to a 2.4% compounded quarterly decline over 2QFY09-1QFY10. With the global economy in recovery mode, EMI revenues have also witnessed a pick-up, having grown at an over 4% CQGR over the past 2 quarters.

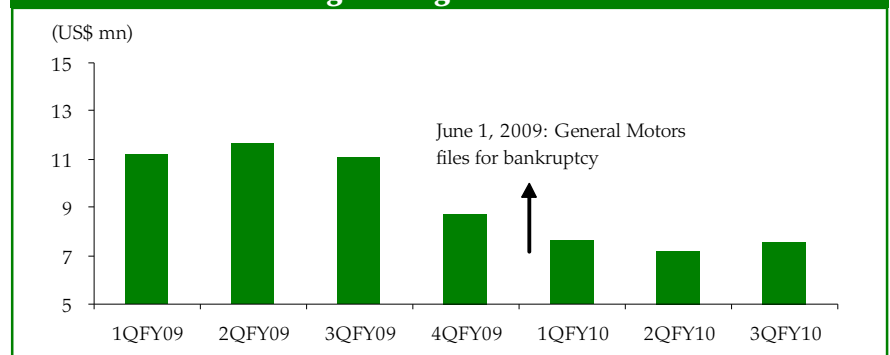
**Exhibit 9: EMI revenues - Resilience in tough times, strong growth post-recession**



Source: Company, KSBL Research

This is in stark contrast to Geometric, a company that derives most of its engineering revenues from the automotive vertical, an industry that was severely hit by the global recession, with a company like General Motors, once the largest auto maker in the world filing for bankruptcy. Geometric has over the same period (1QFY09-3QFY10), recorded a 6.3% compounded quarterly decline in its engineering revenues, from US\$ 11.2 mn in 1QFY09 to US\$ 7.6 mn in 3QFY10.

**Exhibit 10: Geometric engineering revenues - The 'auto' effect**



Source: Company, KSBL Research

*Back-of-the-envelope calculations suggest that the quarterly revenue run rate on a steady-state basis works out to around US\$ 7.2 mn, a significant 22% of 3QFY10 EMI revenues*

*Infotech has managed to restrict sequential revenue declines in dollar terms to 2 quarters amid the global recession*

### Recent agreement signed with UTC Group - To further boost growth of EMI segment

Infotech recently signed an agreement with Hamilton Sundstrand in the avionics segment. The deal envisages 400 engineers being deputed on the project over of 3 years. While the company has not given the size of the deal, back-of-the-envelope calculations suggest that, assuming a 50% onsite-offshore effort mix, the quarterly revenue run rate on a steady-state basis works out to around US\$ 7.2 mn, which is a significant 22% of 3QFY10 EMI revenues. Thus, EMI revenues could witness significant upside going forward. The fact that Infotech won the deal through a competitive bidding process is an even more heartening feature.

### Strong resilience witnessed in revenues; just 2 quarters of sequential de-growth recorded during recession

Infotech Enterprises has shown admirable resilience in its revenues even in the global recession, with the company managing to restrict sequential revenue declines in dollar terms to 2 quarters - 3Q and 4QFY09. Typically, mid-sized software companies are characterised by high client concentration and are generally more dependent on a select few clients for a majority of their revenues. Thus, in the event of such companies losing one or a few of their key clients, they will inevitably end up losing business. However, Infotech despite having client concentration levels in line with most mid-sized software companies has not suffered any major loss of revenues.

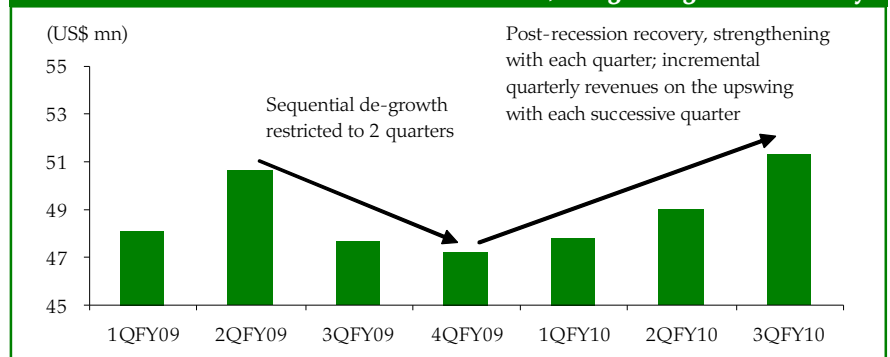
**Exhibit 11: Client concentration - Significant dependence on top clients, similar to peers...**

(% of revenues)	Infotech	Tech Mah.	Patni	KPIT	Cummins	Hexaware	Mastek	Geometric	Zensar
Top client	N.A.	46.0	11.1		30.6	10.3	N.A.	28.0	N.A.
Top-5 clients	44.7	75.0	37.0		N.A.	35.0	54.0	54.0	50.0
Top-10 clients	59.8	82.0	50.9		58.0	49.8	69.0	69.0	61.0

Source: Respective companies, KSBL Research;

Note: Client concentration data for Infotech, Tech Mahindra, KPIT, Geometric and Zensar is for 3QFY10, for Patni and Hexaware it is for 4QCY09 (December-ending fiscal years) and for Mastek it is for 2QFY10 (June-ending fiscal year).

**Exhibit 12: ...but revenues resilient amidst the downturn, strengthening with the recovery**



Source: Company, KSBL Research

*In one instance where vendor consolidation was witnessed (BT in UTG), Infotech ended up getting retained and gained the largest share of BT's budget in the scope of work it carries out*

### Vendor consolidation exercises - No impact on Infotech; emerged stronger in the few instances it has happened

During the global recession, there have been numerous examples of vendor consolidation that have been witnessed. In such cases, vendors who are retained typically end up gaining market share in that particular customer's budgets. Mid-sized software companies are generally at a disadvantage in such exercises due to their smaller size and lesser ability to scale up rapidly. In the case of Infotech, the company has been virtually unaffected by these exercises. The software company has not lost any of its key clients. This can be gauged by the fact that the top-5 and top-10 client concentration levels have remained stable. In one instance where vendor consolidation was witnessed (BT in UTG), Infotech ended up getting retained (number of vendors cut from 6 to 3) and gained the largest share of BT's budget in the scope of work it carries out.

**Exhibit 13: Infotech - Top clients remain growth drivers, showing strong resilience**

(% of revenues)	1QFY09	2QFY09	3QFY09	4QFY09	1QFY10	2QFY10	3QFY10
Top-5 clients	40.9	39.1	42.1	41.0	41.4	44.7	44.7
Top-10 clients	56.4	55.5	57.9	55.4	57.1	61.6	59.8

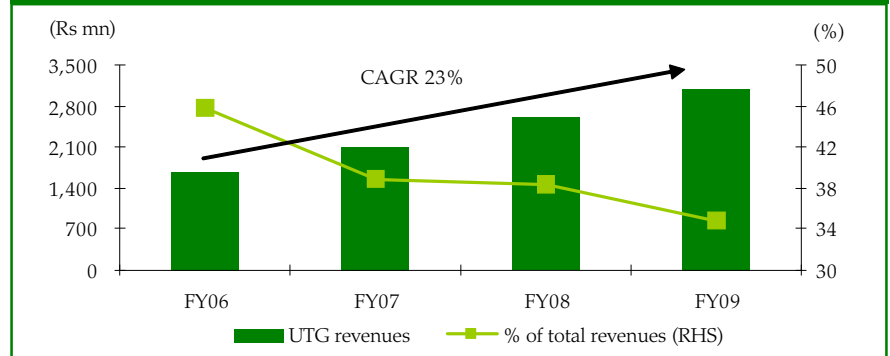
Source: Company, KSBL Research

*UTG revenues in dollar terms have grown at a CAGR of 22% over FY06-09, from US\$ 38 mn in FY06 to US\$ 67 mn in FY09*

### UTG segment - Smaller but significant global, Indian opportunities

The UTG segment accounted for 34.7% and 35.9% of company revenues in FY09 and 9MFY10, respectively. UTG revenues in dollar terms have grown at a CAGR of 22% over FY06-09, from US\$ 38 mn in FY06 to US\$ 67 mn in FY09. In rupee terms, UTG revenues have grown at a 23% CAGR over the period (Rs 1.66 bn in FY06 to Rs 3.09 bn in FY09). Thus, the segment has under-performed EMI, which has grown at nearly double the rate. Consequently, UTG revenues as a percentage of total revenues have fallen from 45.7% in FY06 to 34.7% in FY09.

**Exhibit 14: Infotech UTG revenues, contribution**



Source: Company, KSBL Research

*The market for GIS services stands at US\$ 6.5-7 bn, with Infotech addressing US\$ 1.5 bn*

The market for GIS services stands at around US\$ 6.5-7 bn, with Infotech addressing US\$ 1.5 bn of the market. The company counts illustrious names as its clients in this space, such as Tele Atlas, BT, KPN Telecom, Schlumberger, Rural Payments Agency (an executive agency of the UK

*Infotech has won an order from Government of Karnataka for the digitisation of urban property ownership records, which could serve as a reference point for future deal flows*

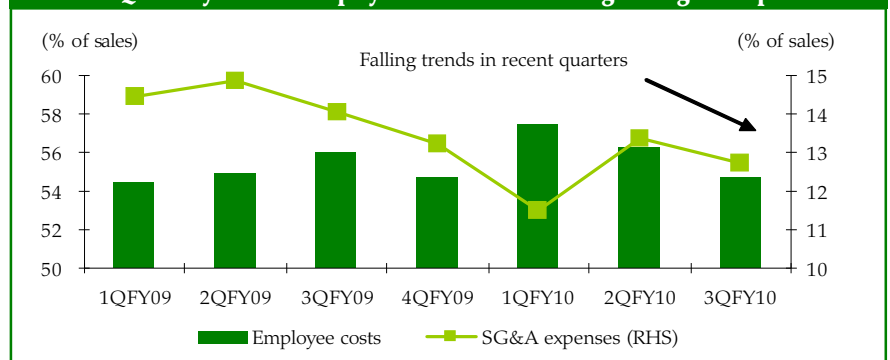
Department for Environment, Food and Rural Affairs) and IHS. A lion's share of Infotech's UTG revenues comes from global clients, with a minor share coming from domestic clients. There is significant growth potential in the Indian GIS market as well, with opportunities expected to come up in city mapping projects, e-governance and digitisation of land and property ownership records by state governments. As a matter of fact, Infotech has won an order from Government of Karnataka for the digitisation of urban property ownership records. Infotech's subsidiary, Infotech Geospatial has also won the project for one town - Shimoga. Under this project, Infotech will digitise property records of Shimoga town and will develop the software (GIS backbone) for the digitisation project. It is a seven-year order worth Rs 60 mn.

Thus, the order size in relation to total UTG revenues is quite small (2% of FY09 UTG revenues). However, Infotech is looking to implement such projects and sell the software (GIS backbone) to other towns as well, with a potential addressable size of 1,000 towns. The company believes it can earn Rs 30 mn per town, thus putting the total potential market size of such opportunities at Rs 30 bn. Infotech sees good potential in states like Gujarat, Maharashtra and Rajasthan.

### Impressive margin profile among mid-sized IT firms

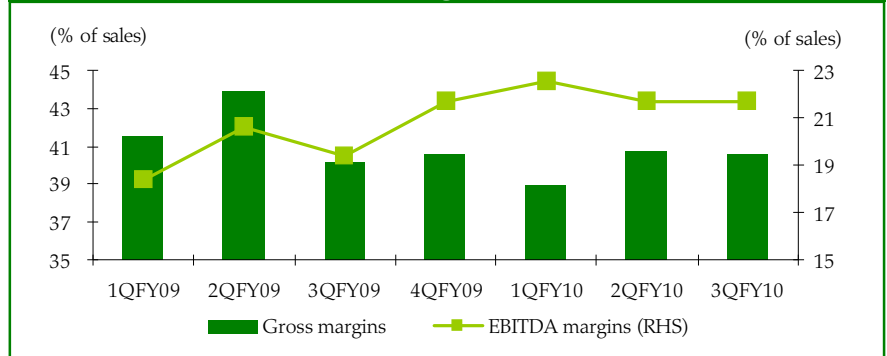
Infotech Enterprises has amongst the best margin profiles in the mid-sized IT space. Already in 9MFY10, Infotech has recorded EBITDA margins of 22%, it's highest-ever in any such period. This is higher by 246 bps yoy over 9MFY09 and EBITDA in absolute terms is higher by an impressive 22% yoy over the same period. The company has been highly disciplined in its cost management. In 9MFY10, it has significantly tightened its SG&A costs (12.5% of sales, lower by 192 bps yoy). Even in absolute terms, SG&A costs for the period are lower by 6% yoy. Infotech has also rationalised its employees, which at the end of 3QFY10 were lower by 454 as compared with the start of the fiscal. Thus, the company has focussed on operational efficiency over this period to tide over the recession. The impressive performance on this front reflects Infotech's ability to maintain and enhance profitability amidst a highly challenging operating environment.

**Exhibit 15: Quarterly trends in employee and SG&A costs - Tightening the ship...**



Source: Company, KSBL Research

### Exhibit 16: ...powers EBITDA margin performance



Source: Company, KSBL Research

*Infotech compares favourably against other mid-sized IT firms in terms of EBITDA margins and earned the third-highest margins among the companies we have compared it with*

Infotech compares favourably when viewed against other mid-sized software companies in terms of EBITDA margins, as can be seen from Exhibit 17. It earned the third-highest margins among all the 7 companies we have compared it with in FY09, while in 3QFY10 it earned the second-highest margins in the sample taken. Thus, this is a key positive factor for Infotech. Only Tech Mahindra and KPIT Cummins Infosystems enjoyed higher margins than Infotech in FY09, with only Tech Mahindra recording higher margins in 3QFY10.

### Exhibit 17: EBITDA margin comparison - Infotech compares favourably

(EBITDA margins, %)	FY09	3QFY10
<b>Infotech Enterprises</b>	<b>20.1</b>	<b>21.7</b>
Tech Mahindra	28.7	23.6
Patni Computer Systems*	19.6	21.4
KPIT Cummins Infosystems	23.1	21.3
Hexaware Technologies*	19.5	17.9
Mastek**	16.9	12.9
Geometric	13.1	17.6
Zensar Technologies	13.9	18.1

Source: Respective companies, KSBL Research;

\* For Patni and Hexaware, FY09=CY09 and 3QFY10=4QCY09 (December-ending fiscal years);

\*\* For Mastek, 3QFY10=2QFY10 (June-ending fiscal year)

### Recent acquisitions - To provide strong domain knowledge in newer verticals, marquee client base; financed through equity dilution to GA Global Investments and Carrier International

*Infotech considers numerous parameters for acquisitions including domain expertise and skill sets, entry into a newer geography, marquee customer relationships and ability to scale*

Infotech Enterprises has done its share of acquisitions in the recent past. The company considers numerous parameters before going ahead with any acquisition. These include, among others, gaining domain expertise in a newer vertical, acquiring skill sets in a particular segment, gaining an entry into a newer geography, long-term marquee customer relationships of the target company and ability to scale. Infotech had in June 2007 raised funds to the tune of nearly Rs 3 bn through a preferential issue of shares made to General Atlantic (GA) Global Investments (4.42 mn shares) and Carrier International (1.16 mn shares) at a premium of Rs 355 per share. The company also issued compulsorily convertible preference shares to GA Global Investments amounting to 2.72 mn equity shares on conversion

at a premium of Rs 355 per share. Thus, Infotech diluted its equity share capital by around 18%. The funds were raised primarily for the purpose of furthering its acquisition strategy.

**Exhibit 18: Infotech equity dilution post GA and Carrier International transactions**

Particulars	(Mn shares)
<b>Equity capital pre-dilution</b>	<b>46.2</b>
Preferential issue to General Atlantic (GA) Global Investments	4.4
Preferential issue to Carrier International Mauritius	1.2
Compulsorily convertible preference shares issued to GA, converted to equity	2.7
<b>Equity shares post-dilution</b>	<b>54.5</b>
<b>Equity dilution (%)</b>	<b>18.0</b>

Source: Company, KSBL Research

In May 2007, Infotech acquired a majority stake (74%) in Hyderabad-based Geospatial Integrated Solutions (Geospatial Integra) for a consideration of Rs 30 mn. This acquisition was a move to address geospatial business opportunities in India and the Middle East. In September 2008 the company acquired Time To Market (TTM), a California-based provider of ASIC (application-specific integrated circuit) design and embedded software solutions. This acquisition gave Infotech an entry into the hi-tech segment. As per the NASSCOM Booz-Allen Hamilton Report on engineering services, global engineering spend on hi-tech design services is estimated to reach US\$ 300 bn by 2020, with potential for offshoring estimated in excess of US\$ 15 bn. Currently, Infotech through TTM earns around US\$ 1.2 mn per quarter on ASIC design services, which has the potential to more-than-double to US\$ 2.5 mn per quarter in FY11.

More recently, in January 2010 Infotech acquired Illinois-based Daxcon Engineering in an all-cash deal. Daxcon is an engineering services company focussed on the heavy equipment engineering and commercial vehicles segment. The company has over 150 people on its rolls and a marquee customer base, with Caterpillar, one of the world's leading manufacturers of construction and mining equipment as its key client. Daxcon has annualised revenues of around US\$ 13.5-14 mn and will be consolidated with effect from January 15, 2010. The acquisition gives Infotech access to strong domain expertise in a newer market segment and access to long-term relationships with large engineering end-customers. In terms of addressable market size, the NASSCOM Booz-Allen Hamilton Report projects global engineering spend in the heavy equipment engineering and commercial vehicle segments at US\$ 100 bn with offshorable spend estimated at US\$ 9 bn by 2020.

Infotech also entered into an agreement with IDT Inc., a US-based entity engaged in design and sale of semiconductor products. The company acquired the operational assets of IDT's Hyderabad office and around 15 employees from IDT will be transitioned to Infotech. Thus, this can be defined as a small-sized asset and employee transfer deal, with a commitment to expand the relationship to a more strategic level from a tactical one.



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*Infotech has significant resources to further its acquisition plans, with cash and cash equivalents less debt to the tune of nearly Rs 4 bn on its books*

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Infotech at the end of 3QFY10 had total cash and cash equivalents adjusting for debt to the tune of nearly Rs 4 bn, implying a per-share value of Rs 71, which could provide some downside cushion to stock price movements. Thus, the company has significant resources to further its acquisition plans going forward. It is likely to make focussed acquisitions in areas such as automotive and embedded systems. Another area that Infotech could look at could be companies offering GIS services with a strong presence in government business.

## Investment Risks

### High client concentration

As is the case with most mid-sized software companies, Infotech's client concentration levels are quite high. The company's top client, the UTC Group contributes 24% to revenues, while the top-5 and top-10 clients cumulatively contribute 45% and 60%, respectively to revenues. Infotech is looking to bring down its exposure to its top-10 clients to around 40% over the next 3 years. However, the company remains dependent primarily on its top-10 clients for business.

### A focussed company, could lead to more difficulty in hiring for specialised skills

Infotech is a focussed mid-sized software company. It should be noted that the company has a target to scale up to a size of US\$ 1 bn over the next 4-5 years from US\$ 194 mn in FY09 and US\$ 204 mn in FY10 (KSBL estimates). However, in order to scale up so significantly it is necessary to recruit the right talent from the market. Given the specialised nature of Infotech's business, it may not be easy for it to find quality specialised talent in the market place. The presence of larger competitors such as TCS, Infosys, Wipro and HCL Technologies who might offer better compensation packages to employees could also affect the company's ability to hire talent at reasonable prices. It is the availability of skills and domain knowledge, and equally importantly the cost of such talent that will determine the company's ability to scale going forward.

### Currency risks

As is the case with most export-oriented software companies, Infotech is subject to currency risks, with rupee appreciation against the US dollar likely to negatively impact the company's operating performance. Apart from the movement of the rupee against the dollar, Infotech's operations are also impacted by the rupee movement against the Euro and British Pound, given its significant exposure to Europe (44.5% of consolidated revenues in 3QFY10). The company has taken forward cover of US\$ 25 mn until 3QFY11 to manage rupee movements against the US dollar. In terms of rupee movements against the Euro, the company has taken Euros 3 mn cover, while in British Pound terms cover of £ 1.2 mn has been taken (Refer Exhibit 19).

**Exhibit 19: Infotech forex cover, period**

Forex cover	Period	Millions	Rate
INR-USD	4QFY10	US\$ 12	US\$ 19 mn at Rs 40.43, US\$ 6 mn at Rs 47.995
	1QFY11	US\$ 6	
	2QFY11	US\$ 6	
	3QFY11	US\$ 1	
INR-EUR	4QFY10	Euros 3	Euros 3 mn at Rs 70.986
INR-GBP	4QFY10	£ 1.2	£ 1.2 mn at Rs 80.8063

Source: Company

**Protectionism rhetoric**

With the US economy in a nascent recovery, unemployment rates have not fallen as yet (9.7% in February 2010). In a clear attempt to address this issue, US President Barack Obama has said that tax breaks for companies that "ship jobs overseas" would be slashed and given to companies that create jobs in the US. This statement could be perceived as an indirect reference to companies that outsource their IT operations to low-cost locations like India. However, we do not believe this is the case and are of the view that this relates more to US companies operating in regions where they get tax benefits and the objective is to ensure that such companies pay more tax in the US, which would also benefit the fiscal situation of the world's largest economy to some extent. Of greater concern to us is the 'indirect protectionism' inherent in such measures. We do not believe this measure will impact business for Indian IT firms.

## Financial Outlook and Key Assumptions

### Revenues

*We expect Infotech to record a 15% CAGR in top-line in rupee terms over FY09-12E, while in dollar terms we forecast a 17.3% CAGR over the same period*

We expect Infotech to record a 15% CAGR in top-line in rupee terms over FY09-12E, while in dollar terms we forecast a 17.3% CAGR over the same period. We expect the EMI segment to be the key growth driver for the company (segment revenues in dollar terms estimated to grow at a 20% CAGR over FY09-12E, 17.3% in rupee terms). The EMI segment is expected to account for a significant 76% of Infotech's incremental revenues over the period. Excluding Daxcon, EMI revenues are expected to clock a 16.7% CAGR over the period in dollar terms. We estimate Daxcon to add US\$ 3 mn in revenues in 4QFY10, US\$ 14 mn in FY11 and US\$ 16 mn in FY12.

#### Exhibit 20: Gross revenue projections - EMI to be the key growth driver

Business segment	FY09	FY10E	FY11E	FY12E	CAGR (%)
(US\$ mn)					
EMI	126.3	132.3	174.4	216.7	19.7
UTG	67.4	71.8	81.2	96.3	12.6
<b>Total</b>	<b>193.7</b>	<b>204.0</b>	<b>255.6</b>	<b>313.0</b>	<b>17.3</b>
(Rs mn)					
EMI	5,824	6,293	7,840	9,394	17.3
UTG	3,094	3,407	3,652	4,177	10.5
<b>Total</b>	<b>8,918</b>	<b>9,700</b>	<b>11,492</b>	<b>13,571</b>	<b>15.0</b>
<b>INR-USD rate</b>	<b>45.96</b>	<b>47.40</b>	<b>44.86</b>	<b>43.25</b>	<b>(2.0)</b>

Source: Company, KSBL Research

*We expect the EMI and UTG segments to clock 20% and 12.6% CAGRs, respectively in US dollar terms over FY09-12E (17.3% and 10.5% CAGRs, respectively in rupee terms)*

On the other hand, the UTG business is expected to grow at a CAGR of 12.6% in dollar terms and 10.5% in rupee terms over the period. Going forward, we believe growth in this segment can accelerate on the back of opportunities coming up in the government business (e-governance), the APDRP (Accelerated Power Development and Reforms Programme) project, the unique identification project and a possible acquisition.

In terms of volumes, we expect the EMI segment to clock a 24.8% CAGR over FY10-12E, while UTG volumes are expected to clock a 15.3% CAGR over the same period. We expect pricing to remain largely stable. We have forecast a steadily appreciating rupee against the dollar over the period. In terms of employees, Infotech expects to hire around 700-750 employees in FY11 after a decline in FY10, a key indicator that the deal pipeline has improved.

**Exhibit 21: Segment-wise quarterly gross revenue projections**

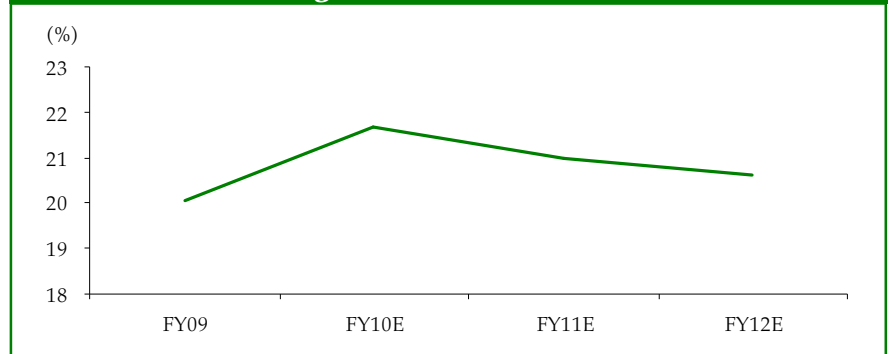
Business segment	4QFY10E	1QFY11E	2QFY11E	3QFY11E	4QFY11E	1QFY12E	2QFY12E	3QFY12E	4QFY12E
<b>(US\$ mn)</b>									
EMI	37.6	40.2	42.4	44.7	47.2	50.0	52.6	55.5	58.6
% chg qoq	13.5	6.9	5.5	5.5	5.5	6.1	5.0	5.5	5.6
UTG	18.5	19.1	19.8	20.7	21.5	22.5	23.5	24.6	25.7
% chg qoq	2.0	3.5	3.8	4.5	4.0	4.5	4.5	4.5	4.5
<b>Total</b>	<b>56.0</b>	<b>59.3</b>	<b>62.2</b>	<b>65.4</b>	<b>68.7</b>	<b>72.6</b>	<b>76.1</b>	<b>80.1</b>	<b>84.3</b>
<b>% chg qoq</b>	<b>9.2</b>	<b>5.7</b>	<b>4.9</b>	<b>5.2</b>	<b>5.0</b>	<b>5.6</b>	<b>4.9</b>	<b>5.2</b>	<b>5.2</b>
<b>(Rs mn)</b>									
EMI	1,738	1,837	1,917	2,000	2,087	2,190	2,287	2,399	2,518
% chg qoq	12.1	5.7	4.3	4.3	4.4	4.9	4.4	4.9	5.0
UTG	854	874	897	927	954	985	1,024	1,064	1,105
% chg qoq	1.0	2.4	2.6	3.4	2.8	3.3	3.9	3.9	3.9
<b>Total</b>	<b>2,592</b>	<b>2,711</b>	<b>2,814</b>	<b>2,927</b>	<b>3,040</b>	<b>3,175</b>	<b>3,310</b>	<b>3,463</b>	<b>3,623</b>
<b>% chg qoq</b>	<b>8.2</b>	<b>4.6</b>	<b>3.8</b>	<b>4.0</b>	<b>3.9</b>	<b>4.4</b>	<b>4.3</b>	<b>4.6</b>	<b>4.6</b>
INR-USD rate	46.25	45.75	45.25	44.75	44.25	43.75	43.50	43.25	43.00
% chg qoq	(1.0)	(1.1)	(1.1)	(1.1)	(1.1)	(1.1)	(0.6)	(0.6)	(0.6)

Source: KSBL Research

*We expect Infotech to record a 162 bps improvement in margins in FY10 on account of cost rationalisation measures, while in FY11 and FY12 we expect margins to decline 72 bps and 35 bps, respectively owing to numerous headwinds*

**Margins**

We forecast declining margins over FY10-12E after a strong surge in FY10E. We expect Infotech to record a 162 bps yoy improvement in margins in FY10 on account of cost rationalisation measures undertaken by the company. On account of this, Infotech is on track to achieve all-time high EBITDA margins in FY10 (21.7% as per our estimates). However, going forward, owing to factors like rupee appreciation, an expected hike in salaries in FY11 (after no hike in FY10), an increase in SG&A expenses and lower margins of acquired companies like Daxcon, we expect margins to trend downwards. We expect margins to decline 72 bps in FY11 and 35 bps in FY12.

**Exhibit 22: EBITDA margin forecasts**


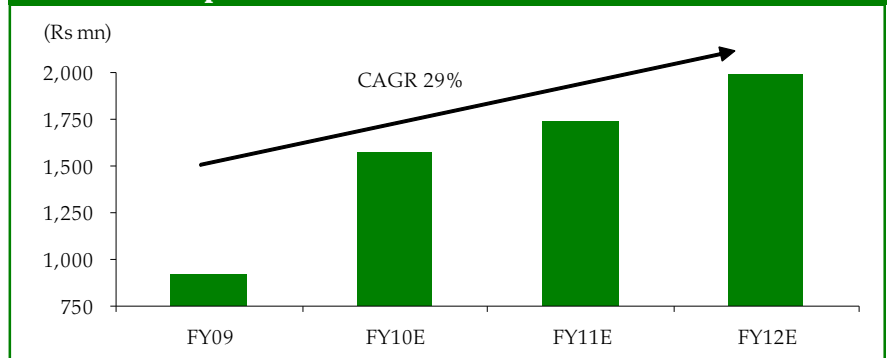
Source: Company, KSBL Research

*We forecast a net profit CAGR of 29% over FY09-12E for Infotech*

## Net profit

We forecast a net profit CAGR of 29% over FY09-12E for Infotech. It should be noted that the company had booked significant forex losses to the tune of Rs 515 mn in FY09 on account of mark-to-market forex losses on its forward contracts. This has led to a low base in FY09 and subsequently superlative net profit growth of 70% estimated in FY10.

**Exhibit 23: Net profit forecasts**



Source: Company, KSBL Research

## YTD performance - 3Q and 9MFY10 update

**Exhibit 24: 3Q and 9MFY10 performance - Strong operational performance**

Rs mn	3QFY09	2QFY10	3QFY10	QoQ (%)	YoY (%)	9MFY09	9MFY10	YoY (%)
Net Sales	2,328	2,374	2,391	0.7	2.7	6,548	7,091	8.3
Operating Costs	1,877	1,859	1,873	0.7	(0.2)	5,272	5,534	5.0
EBITDA	451	515	518	0.5	14.9	1,276	1,557	22.0
EBITDA Margin (%)	19.4	21.7	21.7	(0.0)	2.3	19.5	22.0	2.5
Other Income	(166)	45	78	73.8	(146.6)	(20)	285	(1,526)
Depreciation	119	114	111	(2.6)	(7.0)	341	343	0.6
Financial Expenses	13	2	2	(37.5)	(88.5)	35	6	(81.8)
Profit before Tax	152	443	483	8.9	217.6	881	1,493	69.5
Tax	36	124	129	4.5	256.4	206	402	95.4
Tax rate (%)	23.8	27.9	26.7	(1.1)	2.9	23.4	26.9	3.6
Profit from associate company	30	33	25	(7.6)	(4.5)	65	100	53.5
Minority Interest	1	(1)	0			1	(5)	
Net Profit	145	353	379	7.3	161.9	739	1,195	61.6

Source: Company, KSBL Research

## Revenues

Infotech has recorded a strong performance in 9MFY10. Revenue growth for the period came in at 8.3% yoy over 9MFY09. This was owing to the continuing effects of the recession. However, signs of a recovery are apparent, with 3QFY10 revenues growing sequentially in dollar terms for the third consecutive quarter after 2 quarters of decline in 3Q and 4QFY09. In terms of segments, the EMI business in 9MFY10 has been flat in dollar terms (6.4% qoq growth in 3QFY10), while the UTG segment recorded 4% yoy growth over the same period (1.1% qoq growth in 3QFY10).

## EBITDA

EBITDA growth was robust at 22% yoy in 9MFY10 owing to strong cost containment. Infotech cut down on SG&A costs, which fell by 346 bps yoy as a percentage of revenues and even in absolute terms, SG&A costs fell 7% yoy over the period. The company has rationalised its employee base also, with 3QFY10 being the fourth consecutive quarter of employee declines. This also led to savings in employee costs. In 3QFY10, EBITDA margins fell by a marginal 3 bps qoq on account of a rise in SG&A expenses. Key discretionary expenses like travel costs rose by 46 bps qoq as a percentage of sales (higher in absolute terms by 8.8% qoq), signalling a steady revival in demand.

## Net Profit

Infotech recorded an impressive 61.6% yoy growth in net profit in 9MFY10 owing partly to the margin expansion witnessed as also higher other income. It should be noted that in 9MFY09, the company recorded Rs 166 mn negative other income owing to forex losses incurred. Excluding this item, net profit grew by 41% yoy in 9MFY10. In 3QFY10, on account of higher other income and lower interest costs, net profit grew 7.3% qoq.

## Comparative Analysis

### Exhibit 25: Comparative Analysis

Particulars	Infotech	Patni	KPIT	Hexaware	Mastek	Geometric	Zensar
Sales (FY09, Rs mn)	8,898	30,435	7,932	10,386	9,426	5,981	9,081
Sales (FY09, US\$ mn)	194	656	174	215	196	129	195
EBITDA Margins (FY09, %)	20.1	19.6	23.1	19.5	16.9	13.1	13.9
Net Profit (FY09, Rs mn)	925	5,558	659	1,342	1,412	69	866
Sales CAGR (FY06-09, %)	34.9	6.0	36.2	7.0	11.0	38.8	28.4
Net Profit CAGR (FY06-09, %)	22.5	28.6	26.5	2.6	26.9	(35.6)	36.6
Revenues per Employee (FY09, Rs mn)	1.21	2.11	1.75	1.93	2.41	2.15	1.98
P/E ratio (FY11E, x)	11.3	12.6	9.5	6.9	8.6	10.0	N.A.
RoE (FY09, %)	12.8	17.8	30.9	17.7	31.3	4.0	31.9
RoCE (FY09, %)	13.6	18.5	26.1	18.7	28.6	4.3	18.9
Dividend payout ratio (FY09, %)	9.0	3.8	7.1	15.0	19.0	114.2	12.5

Source: Respective companies, Bloomberg, KSBL Research;

Notes:

(1) All figures for Patni and Hexaware are for CY09, with the sales and net profit CAGRs calculated over CY06-09.

(2) P/E ratio for all companies is calculated based on FY11 consensus EPS estimates taken from Bloomberg; for Patni and Hexaware, the P/E ratio is calculated based on CY11 consensus EPS estimates.

## Outlook and Valuation

Going forward, the market for engineering services outsourcing is expected to increase significantly and could potentially touch US\$ 40 bn by the year 2020, as per the NASSCOM Booz-Allen Hamilton Report 2004. Infotech Enterprises, with its wide range of services to key verticals appears well-set to reap the benefits of this strong growth. The company's long-term strategic relationships with key clients we believe will be the key driver for it to sustain strong top-line growth in this segment. We

expect the company's EMI business to clock a 19.7% CAGR over FY09-12E in US dollar terms to touch US\$ 216.7 mn (US\$ 126 mn in FY09), whereas in rupee terms, the business is estimated to clock a 17.3% CAGR to touch Rs 9.4 bn (Rs 5.8 bn in FY09).

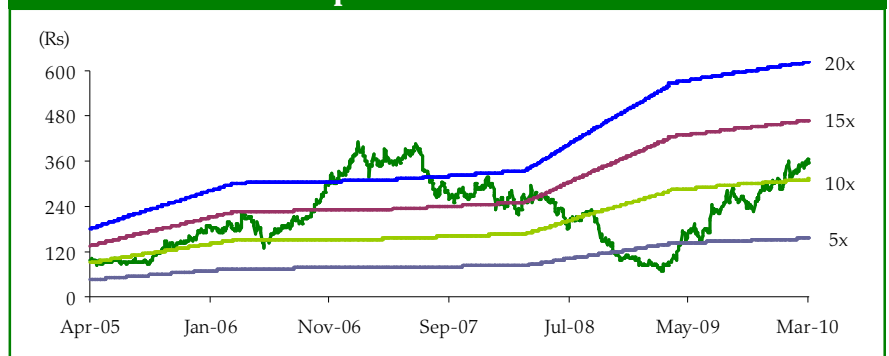
On the other hand, the market for GIS services stands at around US\$ 6.5-7 bn, with Infotech currently addressing around US\$ 1.5 bn of the market. The company counts illustrious names as its clients in this space, such as Tele Atlas, BT and the US and UK governments. There is also significant growth potential in the Indian GIS market, with opportunities expected to come up in city mapping projects, e-governance and digitisation of land and property ownership records by state governments. We expect the UTG business to clock a 12.6% CAGR in US dollar terms over FY09-12E to touch US\$ 96.3 mn (US\$ 67 mn in FY09), whereas in rupee terms the segment is expected to grow at a 10.5% CAGR to touch Rs 4.2 bn (Rs 3.1 bn in FY09).

Overall, we expect Infotech Enterprises to clock a 17.3% CAGR in top-line in dollar terms over FY09-12E to touch US\$ 313 mn, whereas in rupee terms top-line is expected to clock a 15% CAGR to touch Rs 13.6 bn. We have modeled for a 162 bps yoy increase in EBITDA margins in FY10 owing to cost containment measures and employee rationalisation, post which we estimate margins to dip by 72 bps and 35 bps yoy in FY11 and FY12, respectively owing to rupee appreciation, an expected hike in salaries in FY11, an increase in SG&A expenses and lower margins of acquired companies like Daxcon. On the net profit front, we forecast a CAGR of 29% over FY09-12E. We model for the rupee to appreciate steadily against the dollar, from an average rate of Rs 45.96 in FY09 to Rs 43.25 in FY12.

*Infotech Enterprises' stock has traded in a P/E band of 3-27x over the past five years, with an average multiple of around 13x*

In terms of historical valuations, Infotech Enterprises' stock has traded in a P/E band of 3-27x over the past five years, with an average multiple of around 13x. During periods of strong global economic growth, the stock has traded at an average P/E multiple of 18x. IT companies are characterised by strong cash flows, high levels of annuity business, decent profitability levels and good return ratios. We believe with the global economy in recovery mode, IT stocks in general and Infotech Enterprises in particular will trade at P/E ratios around their five-year average.

**Exhibit 26: Infotech Enterprises P/E band**



Source: C-line, KSBL Research

At the CMP, the stock is quoting at 9.9x FY12E EPS, which is below its five-year average and significantly lower than the average multiple it has traded at in times of strong global economic growth. Even in terms of relative valuations with other mid-sized IT companies, the stock in our view is attractively priced given its good track record, resilient performances during the global recession, better-than-average levels of profitability and strong growth expected going forward owing to strategic long-term relationships built with marquee clients.

*Infotech has net cash on its books to the tune of nearly Rs 4 bn, translating into Rs 71 per share; adjusting for this factor, valuations are even more attractive at 8.4x FY12E EPS*

The company had net cash on its books at the end of 3QFY10 of nearly Rs 4 bn (negligible debt of Rs 3.3 mn), which translates into Rs 71 on a per-share basis. If we adjust this factor and accordingly adjust our net profit and EPS forecasts for net interest income and taxes, the company's valuations turn out to be even more attractive at 8.4x FY12E EPS on an expected EPS CAGR of 13.4% over FY10-12E. Thus, we believe this is a factor that provides a downside cushion to the stock price. Given reasonable valuations, **we Initiate Coverage on Infotech Enterprises with a 'Buy' recommendation and 12-month target price of Rs 450, implying a P/E of 12.5x FY12E EPS.**

#### Exhibit 27: Net profit, EPS and P/E adjusted for cash & interest - Attractive proposition

Particulars	FY09	FY10E	FY11E	FY12E
Net profit (Rs mn)	925	1,572	1,738	1,988
EPS (Rs)	16.7	28.4	31.3	35.9
<b>P/E ratio (x)</b>	<b>21.2</b>	<b>12.5</b>	<b>11.3</b>	<b>9.9</b>
Net profit adjusted for net interest income and taxes (Rs mn)	818	1,447	1,611	1,860
EPS adjusted for net interest income and taxes (Rs)	14.7	26.1	29.1	33.5
<b>P/E ratio adjusted for cash per share (x)</b>	<b>19.1</b>	<b>10.8</b>	<b>9.7</b>	<b>8.4</b>

Source: Company, KSBL Research

#### Company Background

Infotech Enterprises is a mid-sized software company with a focus on two segments - engineering services (EMI) and geospatial information services (GIS, UTG). The company was founded in 1991 and services several verticals in its niche areas of focus. In the EMI vertical, Infotech provides services such as mechanical design, electronic design, technical publications, engineering software development and PLM to clients across the aerospace, automotive, energy, marine, hi-tech, rail and plant engineering verticals. The company counts marquee names like the UTC Group, Boeing, Airbus and Philips as its clients. The company has built long-term strategic relationships with these clients, resulting in a major portion of EMI business revenues being annuity in nature. In FY09, Infotech recorded US\$ 126 mn (Rs 5.82 bn) in revenues from the EMI business and these revenues have clocked a healthy CAGR of 42% and 44% in dollar and rupee terms, respectively over FY06-09. The EMI business accounted for a majority of Infotech's revenues at 65.3% in FY09 and 64.1% in 9MFY10.

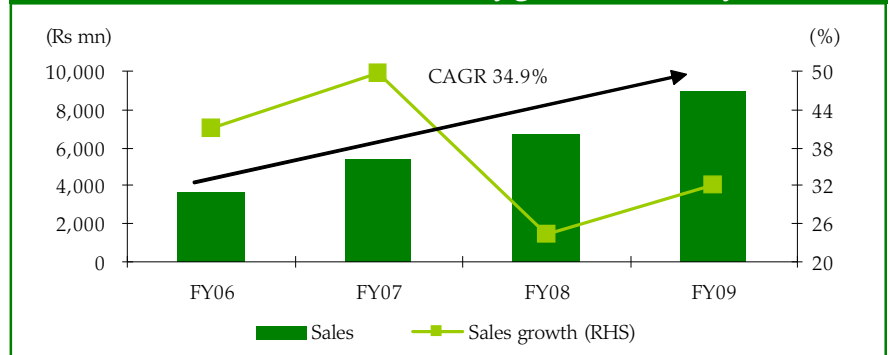
On the other hand, the company in its UTG business provides digital photogrammetry services, GIS data management, consultancy, application



development services, digitisation of data and asset utilisation services to its clients from the utilities, telecom and government verticals. The software company counts illustrious names as its clients in this business such as Tele Atlas, BT, KPN Telecom, IHS and the US and UK governments. In FY09, Infotech recorded US\$ 67 mn (Rs 3.09 bn) in revenues from the UTG business and these revenues have clocked a CAGR of 22% and 23% in dollar and rupee terms, respectively over FY06-09. The UTG business accounted for 34.7% and 35.9% of Infotech's revenues in FY09 and 9MFY10, respectively.

In terms of geographical revenue spread, Infotech earned 46.5% of its consolidated revenues from North America, 44.5% from Europe and the balance 9% from Asia and Australia in 3QFY10. Overall, Infotech Enterprises has grown its revenues at a CAGR of 33.2% and 34.9% in dollar and rupee terms, respectively over the period FY06-09, while net profits have clocked a 22.5% CAGR over the same period.

**Exhibit 28: Infotech revenues - Healthy growth over the years**



Source: Company, KSBL Research

**Exhibit 29: Infotech segment-wise key competitors**

Segment	Mechanical engineering, design	Avionics	Hi-tech	UTG (India)	UTG (Global)
Competitors	Mahindra Satyam, TCS	Wipro, HCL Technologies	Wipro, Mahindra Satyam	Rolta	Local firms

Source: Company, KSBL Research

### Profit & loss statement

(Rs mn)	FY2008	FY2009	FY2010E	FY2011E	FY2012E
Net Sales	6,741	8,898	9,676	11,464	13,538
% growth	24.3	32.0	8.8	18.5	18.1
Personnel Costs	3,561	4,895	5,422	6,357	7,539
SG&A	1,963	2,218	2,156	2,703	3,208
Total Expenditure	5,524	7,112	7,578	9,060	10,747
EBITDA	1,217	1,785	2,098	2,404	2,791
% growth	7.3	46.7	17.5	14.6	16.1
EBITDA margin (%)	18.1	20.1	21.7	21.0	20.6
Other income	227	(294)	341	328	354
Financial Expenses	37	40	8	6	4
Gross Profit	1,407	1,450	2,432	2,726	3,141
% growth	18.5	3.1	67.7	12.1	15.2
Deprn. & Amortisn.	365	466	457	515	571
Profit Before Tax	1,041	985	1,975	2,210	2,570
% growth	11.9	(5.4)	100.6	11.9	16.3
Tax	258	140	532	597	707
Effective tax rate (%)	24.7	14.2	27.0	27.0	27.5
Profit After Tax	784	845	1,442	1,613	1,863
% growth	5.3	7.8	70.8	11.8	15.5
Profit in associate company (IASI)	70	80	125	125	125
Minority Interest	(2)	(0)	(5)	0	0
Reported Net Profit	856	925	1,572	1,738	1,988
% growth	2.3	8.1	70.0	10.6	14.4
EPS (Rs)	15.4	16.7	28.4	31.3	35.9
% growth	2.3	8.1	70.0	10.6	14.4
DPS (Rs)	1.2	1.5	2.8	3.9	5.4
Payout (%)	7.3	9.0	10.0	12.5	15.0

### Ratios

(Rs mn)	FY2008	FY2009	FY2010E	FY2011E	FY2012E
ROE (%)	17.7	12.8	18.7	17.7	17.4
ROCE (%)	20.8	13.6	23.1	22.3	22.4
Personnel Costs/Sales (%)	52.8	55.0	56.0	55.4	55.7
Operating & Admin. Costs/Sales (%)	29.1	24.9	22.3	23.6	23.7
Depreciation/Gross Block excl. Land (%)	10.6	11.6	10.3	10.3	10.3
Revenue growth (%)	24.3	32.0	8.8	18.5	18.1
EBITDA margins (%)	18.1	20.1	21.7	21.0	20.6
EBITDA growth (%)	7.3	46.7	17.5	14.6	16.1
Net Profit growth (%)	2.3	8.1	70.0	10.6	14.4
EMI segment revenues (Rs mn)	4,174	5,824	6,293	7,840	9,394
EMI revenue growth (%)	25.9	39.5	8.1	24.6	19.8
EMI RPEs (Rs mn)	1.55	1.81	1.84	2.15	2.30
UTG segment revenues (Rs mn)	2,588	3,094	3,407	3,652	4,177
UTG revenue growth (%)	22.5	19.5	10.1	7.2	14.4
UTG RPEs (Rs mn)	0.80	0.78	0.86	0.92	0.97
PER (x)	22.9	21.2	12.5	11.3	9.9
P/BV (x)	2.9	2.5	2.1	1.8	1.6
Price/sales (x)	2.9	2.2	2.0	1.7	1.4
EV/EBITDA (x)	15.4	9.2	7.2	5.7	4.3
Dividend Payout (%)	7.3	9.0	10.0	12.5	15.0

### Balance sheet

(Rs mn)	FY2008	FY2009	FY2010E	FY2011E	FY2012E
Equity Capital	261	276	276	276	276
Compulsorily Convertible Preference Shares (Rs 360 FV)	981	0	0	0	0
Reserves	5,483	7,427	8,815	10,299	11,938
Net Worth	6,724	7,703	9,091	10,575	12,214
Minority Interest	3	3	(1)	(1)	(0)
Short-term Loans	140	194	147	100	54
Long-term Loans	284	1	1	1	1
Total Loans	424	195	148	101	55
<b>TOTAL LIABILITIES</b>	<b>7,152</b>	<b>7,901</b>	<b>9,238</b>	<b>10,676</b>	<b>12,268</b>
Goodwill	77	272	272	272	272
Land	25	88	88	88	88
Gross Block	3,463	4,017	4,453	5,026	5,567
Depreciation	1,582	1,954	2,410	2,926	3,497
Net Block	1,881	2,064	2,042	2,100	2,071
Capital work-in-progress	311	584	584	584	584
Investments	2,293	402	402	402	402
Deferred Tax Asset	(16)	165	165	165	165
Debtors (Net)	2,170	2,628	2,916	3,518	4,254
Cash & Bank	1,193	3,334	4,668	6,010	7,535
Loans & Advances	442	603	603	603	603
Total Current Assets	3,805	6,564	8,187	10,130	12,391
Sundry Creditors	506	822	934	1,191	1,468
Advances from customers	35	24	24	24	24
Unearned Revenue	151	6	6	6	6
Investor Education and Protection Fund - Unclaimed Dividends	1	1	1	1	1
Other Liabilities	195	993	1,058	1,265	1,500
Proposed Dividend (incl. Dividend Tax)	77	97	184	254	349
Provision for Gratuity & Leave Enhancement	260	295	295	325	357
Total Current Liabilities	1,226	2,238	2,503	3,067	3,706
Net Current Assets	2,580	4,326	5,684	7,063	8,685
<b>TOTAL ASSETS</b>	<b>7,152</b>	<b>7,901</b>	<b>9,238</b>	<b>10,676</b>	<b>12,268</b>

### Cash flow

(Rs mn)	FY2008	FY2009	FY2010E	FY2011E	FY2012E
EBIT	852	1,319	1,642	1,888	2,220
(Inc./Dec in working capital)	(460)	395	(24)	(37)	(97)
Cash flow from operations	391	1,714	1,618	1,851	2,123
Other income	227	(294)	341	328	354
Depreciation & Amortisation	365	466	457	515	571
Financial Expenses	(37)	(40)	(8)	(6)	(4)
Profit from associate company	70	80	125	125	125
Tax paid	(258)	(140)	(532)	(597)	(707)
Dividends paid	(85)	(97)	(184)	(254)	(349)
Net cash from operations	674	1,687	1,816	1,962	2,113
Capital expenditure	(1,403)	(891)	(435)	(573)	(542)
Net cash after capex	(729)	797	1,381	1,389	1,572
Inc./(Dec.) in ST borrowing	30	53	(47)	(47)	(47)
Inc./(dec.) in LT borrowing	134	(283)	0	0	0
Inc./(dec.) in borrowings	164	(229)	(47)	(47)	(47)
(Inc./Dec. in investments)	(2,035)	1,891	0	0	0
Equity issue/(Buyback)	2,993	2	0	0	0
Cash from Financial Activities	1,122	1,664	(47)	(47)	(47)
Others	65	(320)	0	0	0
Opening cash	736	1,193	3,334	4,668	6,010
Closing cash	1,193	3,334	4,668	6,010	7,535
Change in cash	457	2,141	1,334	1,342	1,525

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<b>Stock Ratings</b>	<b>Absolute Returns</b>	<b>Stock Ratings</b>	<b>Absolute Returns</b>
Buy	: > 25%	Market Performer	: 0 - 15%
Out Performer	: 16 - 25%	Under Performer	: < 0%
Sell	: <(25%)		

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