

KPIT Cummins Infosystems

Ashish Aggarwal

+91 22 67069925

Ashish.aggarwal@investsmartindia.com

Sanket Dalvi

+91 22 67069900

sanket.dalvi@investsmartindia.com

Shareholding (%)

Promoters	26.0
FII's	14.3
MFs / UTI	9.9
Insurance Co.	7.2
Others	42.6

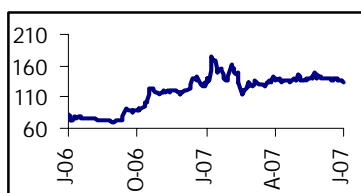
Share price performance

52-week high/low (Rs) 164/62

	-1m	-3m	-12m
Abs (%)	-3.6	-1.3	64.9
Rel* (%)	-9.5	-11.4	14.6

*to Nifty

Stock chart



Results better than expected; maintain 'Buy'

KPIT Cummins Infosystems Ltd. (KPIT) Q1FY08 results were better than expected, with sequential rupee revenue growth of 3.8% to Rs1.35bn. Though the rupee appreciated by around 7% against USD in Q1FY08, revenue growth in USD was only 5.44%. The difference was primarily on account of the company converting dollar revenue at the average realised rate of Rs43.64, instead of the average Rs/USD rate of Rs40.82 during the quarter.

The company raised its FY08 revenue guidance by 1.4% (at the lower end) to US\$145-148mn. However, on account of rupee appreciation, it reduced its profit guidance by 7% (at the lower end) to US\$15.18-16.39mn.

Due to higher than expected Q1FY08 results we are increasing our FY08E and FY09E EPS estimates by 7.5% and 3.4% to Rs8.5 and Rs12.0 respectively, implying a two-year EPS CAGR of 3.9%. We have taken Rs/USD rate of Rs40.5 for the rest of FY08E and Rs40.0 for FY09E.

Currently, the stock is quoting at FY08E and FY09E PER of 16x and 11.2x respectively. With the company expected to post two-year EPS CAGR of 33.9%, we maintain 'Buy' on the company with a price target of Rs156, 13x FY09E earnings.

Key highlights of Q1FY08 results are:

- Volume growth drives revenue growth:** KPIT reported a sequential USD revenue growth of 5.4% to US\$31mn. Revenue growth was driven by 7.9% volume growth. Though, on an average, the rupee appreciated by 7% against USD; rupee revenue grew 3.8% to Rs1.35bn. This was on account of the company converting dollar revenue at an average realised rate of Rs43.64, as against an average rate of Rs40.82. Though this did not have an impact on profitability (as the extra revenue would have come in as forex gains, if the conversion were done at average rate), revenue in INR was higher. At the average rate of Rs40.82, the company would have reported a revenue decline of 2.9% to Rs1.26bn.
- EBITDA margin expands by 10bps:** KPIT's EBITDA margin expanded by 10bps to 15.9% despite a) rupee appreciation, b) 17% offshore and 5% onsite salary hikes, c) addition of 345 employees, majority at the lateral level and d) booking of translation loss in general and administrative expenses.

BUY

Rs135

19 July 2007

Market cap

Rs bn 10

US\$ mn 218

Avg 3m daily volume

378,874

Avg 3m daily value

USD mn 1

Shares outstanding (mn)

73

Reuters

KPIT.BO/KPIT.NS

Bloomberg

KPIT IN

Sensex

15,301

Nifty

4,500

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Margin expansion was on account of a) lower sales and marketing expenses, as most of them were in USD b) higher variable commissions given in Q4FY07, not being there in Q1FY08 and c) higher offshore revenue.

We further expect EBITDA margin to expand going forward, due to:

- a) Higher offshore revenue
 - b) Lower per capita employee cost; as we expect the company to add more employees at the entry level
 - c) Benefits from economies of scale
 - d) Increasing utilisation and realisations
- ▲ **Higher depreciation impacts net income:** Net income of the company was impacted by higher depreciation, which was high on account of capitalisation of new development centre in Pune. Depreciation in Q1FY08 was Rs54mn as against Rs35mn in Q4FY07.
 - ▲ **Signs new contract with Cummins in BPO space:** KPIT has signed a new contract with Cummins in the BPO space. The company would provide F&A BPO solutions to Cummins' entities worldwide, initially for the first five years. This contract, we believe, would help the company in understanding F&A BPO business and getting new clients. KPIT plans to pay US\$5mn upfront for the contract and further pay US\$5mn at the end of the fifth year. Though Cummins has not guaranteed any revenue, KPIT expect to get US\$1mn in revenue in FY08E and expects it to grow into a US\$15mn BPO business annually in 48-60 months.
 - ▲ **Guidance:** KPIT has revised its dollar revenue guidance upwards by 1.4% (at the lower end) to US\$145-148mn. However, in lieu of appreciating rupee, it has revised its profit guidance downwards by 7% (at the lower end) to US\$15.18-16.39mn. The company expects to post revenue of Rs6,018mn-6,142mn in FY08E and net profit of Rs630-680mn. KPIT has given its guidance at Rs/USD rate of Rs41.5.
 - ▲ **Forecasts:** On account of better than expected Q1FY08, we are increasing our FY08E and FY09E EPS estimates by 7.5% and 3.4% to Rs8.5 and Rs12.0 respectively, implying a two-year EPS CAGR of 33.9%. Our estimates are based on Rs/USD rate of Rs40.5 for the rest of FY08E and Rs40.0 for FY09E.
 - ▲ **Valuation:** Currently, the stock is quoting at FY08E and FY09E PER of 16.0x and 11.2x respectively. With the company expected to post above industry average two-year (FY07-09E) EPS CAGR of 33.9%, we maintain 'Buy' on the stock with a target price of Rs156, 13x FY09E earnings.

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Table 1. Quarterly result table (consolidated)

Rs mn	Q1FY08	Q4FY07	QoQ (%)	Q1FY07	YoY (%)
Revenues	1,353	1,303	3.8%	1,023	32.3%
Software Development Expenses	842	794	6.0%	641	31.3%
Gross Profit	511	509	0.4%	382	33.9%
GPM	37.8%	39.1%		37.3%	
Selling and marketing expenses	135	153	-11.9%	107	26.7%
General and administrative expenses	162	150	7.4%	123	31.5%
EBITDA	215	206	4.4%	152	40.9%
EBITDA Margin	15.9%	15.8%		14.9%	
Depreciation	54	35	51.9%	25	113.2%
Other Income	0	4	-88.2%	1	-22.4%
Interest	20	17	17.4%	11	82.3%
PBT	141	157	-9.9%	117	21.1%
Tax	15	17	-9.0%	13	14.5%
Tax Rate	10.6%	10.5%		11.3%	
PAT before minority interest	126	141	-10.0%	104	21.9%
Minority Interest	(0)	(0)		0	
PAT after Minority Interest	127	141	-9.8%	103	22.5%
NPM	9.4%	10.8%		10.1%	

Source: IISL research, company

Table 2. Estimates

Rs mn	FY06	FY07	FY08E	FY09E
Revenues	3,182	4,637	5,916	7,730
% change	-	45.7%	27.6%	30.7%
EBITDA	462	715	1,026	1,361
% change	-	54.8%	43.4%	32.7%
Net Profit	328	501	645	915
% change	-	52.6%	28.8%	41.9%
EPS	4.4	6.7	8.5	12.0
PE(x)	30.8	20.2	16.0	11.2
ROCE (%)	20.3%	21.5%	23.3%	28.3%
ROE (%)	26.5%	29.4%	28.2%	30.4%

Source: IISL research, company

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