

BUY

Price	Rs48
Target Price	Rs57
Investment Period	12 months

Stock Info

Sector	IT
Market Cap (Rs cr)	624
Beta	0.98
52 WK High / Low	140 / 25
Avg Daily Volume	267944
Face Value (Rs)	10
BSE Sensex	11,953
Nifty	3,625
BSE Code	532628
NSE Code	3IINFOTECH
Reuters Code	TIIN.BO
Bloomberg Code	III@IN

Shareholding Pattern (%)

Promoters	39.5
MF/Banks/Indian FIs	16.2
FII/ NRIs/ OCBs	7.9
Indian Public/ Others	36.4

Abs.	3m	1yr	3yr
Sensex (%)	28.5	(31.2)	(3.3)
3i Infotech (%)	38.5	(63.7)	(52.7)

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Performance Highlights

■ **Poor performance in IT Services segment leads to lower Top-line:** 3i posted a 0.3% qoq contraction in 4QFY009 Top-line. This quarter, the IT Services segment recorded a poor performance, clocking a 10.7% qoq contraction in its Top-line. The global economic turmoil has taken its toll on this business. On the other hand, Software Products recorded a 3.1% qoq increase in Revenues, while Transaction Services posted the best performance, growing 6.2% qoq. On a yoy basis, Top-line increased 73.4%, with 49.4% of the growth coming from inorganic initiatives, while the balance came from organic pursuits. Segment-wise, the Transaction Services Business was the key contributor to growth, with the business spiking by as much as 462.4% yoy. The Software Products Business grew by 16.4% yoy, while IT Services posted a 34.6% yoy growth. Transaction Services contributed over 70% of the incremental growth to Top-line on a yoy basis.

In the Software Products Business, 3i Infotech witnessed no growth in the Insurance and Banking sub-segment qoq, while Capital Markets bounced back, growing 11.1% qoq (17.2% qoq fall in 3QFY2009). On a yoy basis, Insurance grew 12.2%, Banking 39.7% and Capital Markets 9.1%. ERP saw no qoq growth, while yoy a 12.7% de-growth was recorded. 3i's order book registered just 1.8% qoq growth to Rs1,445cr (Rs1,419cr last quarter).

■ **Margins soar on lower Salary costs, higher Product Margins:** 3i Infotech saw expansion of 155bp qoq in EBITDA Margins in 4QFY2009 due to lower Employee costs (down 170bp qoq as percentage of Sales). Segment-wise, Product Business Gross Margins saw expansion of 268bp qoq. Given that this business is more profitable (54.8% gross margins as compared with 36.3% in IT Services and 28.4% in Transaction Services), this drove Margin expansion. On yoy basis, EBITDA Margins fell by 168bp due to higher Employee costs (up 323bp yoy as a percentage of Sales).

■ **Higher Interest, Depreciation and lower Other Income impact Bottom-line:** Despite the higher Margins, 3i's Bottom-line for the quarter saw no growth (0% excluding one-time items) due to higher Interest, higher Depreciation and lower Other Income. On yoy basis, Bottom-line after Minority Interest grew 32.2% (excluding one-time items). This quarter, 3i Infotech bought back and cancelled FCCBs of €4mn and US \$25.1mn equivalent to Rs153cr at a discount. On a net basis, a sum of Rs26cr has been shown as a one-time gain, including which Bottom-line grew by 40.3% qoq and by 85.4% yoy.

Key Financials (Consolidated)

Y/E March (Rs cr)	FY2008	FY2009	FY2010E	FY2011E
Net Sales	1,205	2,286	2,403	2,814
% chg	83.9	89.6	5.1	17.1
Net Profit*	169	275	195	214
% chg	75.3	62.3	(29.0)	9.5
EBITDA Margin (%)	21.2	19.0	18.0	17.5
FDEPS (Rs)	12.3	19.9	14.1	15.5
P/E (x)	3.9	2.4	3.4	3.1
P/BV (x)	0.9	0.6	0.5	0.5
RoE (%)	27.3	30.8	17.4	16.4
RoCE (%)	15.8	14.6	10.4	10.4
EV/Sales (x)	1.3	1.1	1.0	0.9
EV/EBITDA (x)	6.4	5.8	5.7	5.0

Source: Company, Angel Research; *Adjusted for Preference dividend

Transaction Services drives FY2009 Top-line

3i Infotech recorded a strong 89.6% yoy growth in FY2009 Top-line to Rs2,286cr. Of this growth, 38.7% came from the company's organic initiatives, while the balance growth came from inorganic pursuits. It was the Transaction Services Business that contributed the maximum to the company's growth in FY2009. This business soared by as much as 400% yoy, led by the acquisition of Regulus, which recorded Rs550cr in Top-line for the year. The Transaction Services Business contributed to 53.8% of the incremental Top-line growth for the fiscal, reflecting 3i's increased focus on this high-volume, low-margin segment. On the other hand, the IT Services and Software Products Businesses grew by 61.3% yoy and 36.1% yoy, respectively.

Exhibit 1: Segment-wise Revenue break-up - Transaction Services powers growth

(Rs cr)	FY2008	FY2009	% chg
Software Products			
Revenues	596	811	36.1
Gross profit	327	439	34.3
Gross margins (%)	54.8	54.1	(71 bps)
IT Services			
Revenues	464	748	61.3
Gross profit	189	271	43.2
Gross margins (%)	40.8	36.2	(459 bps)
Transaction Services			
Revenues	145	726	400.0
Gross profit	44	210	380.5
Gross margins (%)	30.1	28.9	(117 bps)
Total			
Revenues	1,205	2,286	89.6
Gross profit	560	920	64.3
Gross margins (%)	46.4	40.2	(620 bps)

Source: Company, Angel Research

Margins contract on higher Staff Costs, investments in newer initiatives

3i Infotech recorded a 214bp yoy contraction in its EBITDA Margins in FY2009. This was primarily on account of higher Staff Costs, which rose as a percentage of Sales by 322bp yoy. The company also invested in newer initiatives like Taxsmile, Kiosks and Elegon, which had an impact of 200bp on Margins.

Lower Margins, higher Interest and Depreciation impact Bottom-line growth

On account of lower Margins, higher Interest Costs (up 88% yoy) and Depreciation Charges (up by as much as 187.1% yoy), Bottom-line growth for the fiscal, while decent at 45% yoy (excluding one-time items), trailed Top-line and EBITDA growth. Including the one-time gains accrued on account of the FCCBs cancelled, Bottom-line grew by 59.7% yoy.

Outlook and Valuation

Going ahead, we expect 3i Infotech to record a CAGR of 11% in Top-line over FY2009-11E, while Bottom-line is expected to record a compounded de-growth of 7.3% over the same period (excluding one-time items). At the CMP, the stock is trading at a P/E of 3.4x FY2010E EPS. Management has not given any guidance for FY2010, given the poor business visibility. Nonetheless, we believe the company could continue to buy back its FCCBs at a discount, which we believe is a key catalyst for a stock re-rating. Improvement in the quality of the Balance Sheet is also another key factor that the company will need to focus on, given that Goodwill accounts for a significant 164% of FY2009 Net Worth. **We believe at current levels, the stock is reasonably attractive from a valuation standpoint and maintain a Buy with a Target Price of Rs57.**

Exhibit 2: FY2009 Consolidated Financial Performance

Y/E March (Rs Cr)	FY2009 4Q	FY2009 3Q	% chg (qoq)	FY2008 4Q	% chg (yoy)	FY2009	FY2008	% chg
Total Revenue	607	609	(0.3)	350	73.4	2,286	1,205	89.6
Operating Costs	488	499	(2.2)	275	77.1	1,851	950	94.8
EBITDA	119	110	8.2	75	59.8	434	255	70.4
Interest	28	25	10.2	14	96.8	95	51	88.0
Depreciation & Amortisation	23	20	19.3	8	191.8	70	24	187.1
Other Income / (Expense)	4	7	(43.2)	2	75.0	19	18	4.2
Income before Income Taxes	72	72	(0.4)	55	31.4	288	198	45.5
Income Taxes	5	2	133.5	4	15.4	22	15	45.9
Net Income before Minority Interest	67	70	(4.4)	50	32.7	266	183	45.4
Exceptional Items	26	-		-		26	-	
Min. Interest & Share of Ass. Profits	2	5		1		10	7	
Profit after Tax	90	65	40.3	49	85.4	282	177	59.7
Diluted EPS (Rs)	6.8	4.8	41.5	3.5	95.4	21.0	12.7	66.1
EBITDA Margin (%)	19.6	18.1		21.3		19.0	21.1	
Net Profit Margin (%)	14.9	10.6		14.0		12.3	14.6	
Effective Tax Rate (%)	6.9	3.0		7.9		7.6	7.6	

Source: Company, Angel Research



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Ratings (Returns) : Buy (Upside > 15%)
 Reduce (Downside upto 15%)

 Accumulate (Upside upto 15%)
 Sell (Downside > 15%)

Neutral (5 to -5%)