

# KPIT Cummins Infosystems Ltd (Q1 FY09)

July 21, 2008

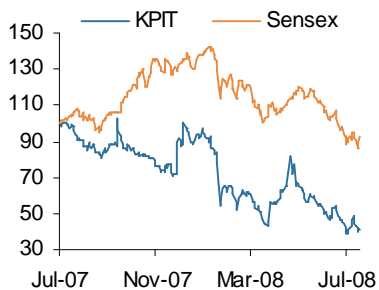
## Stock data

Sensex:	13,635
CMP (Rs):	56
Target price (Rs):	61
Upside (%):	8.3
52 Week h/l (Rs):	144/52
Market cap (Rs cr)	440
6m Avg vol BSE&NSE ('000 nos):	416
No of o/s shares (mn):	78
FV (Rs):	2
Bloomberg code:	KPIT IN
Reuters code:	KPIT.BO
BSE code:	532400
NSE code:	KPIT

## Shareholding pattern

<b>March 2008</b>	<b>(%)</b>
Promoters	24.6
FII's	8.3
Indian institutions	18.0
Public & others	49.1

## Share price trend



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- ↗ Dollar revenue growth modest; rupee growth restricted by hedges
- ↗ Growth driven by ATS vertical and Cummins and other star customers
- ↗ Gross margin improves by 100bps but OPM declines by 130bps
- ↗ Lower interest and depreciation push profit growth to 25% qoq
- ↗ Likely to miss FY09 earnings guidance; maintain Market Performer with price target Rs61

## Result table

Period	Q4 FY08	Q1 FY09	QoQ	YoY
(Rs mn)	(3)	(3)	(%)	(%)
Net sales	1,648	1,737	5.4	28.4
Total Expenditure	(1,413)	(1,511)	6.9	32.7
EBIDTA	236	226	(4.0)	5.4
<i>EBITDA margin (%)</i>	14.3	13.0	-	-
Depreciation	(85)	(66)	(22.4)	23.3
Interest	(17)	(10)	(39.6)	(48.6)
Other income	4	(1)	-	-
PBT	137	149	8.6	5.4
Tax	(20)	(20)	0.6	35.1
PAT	117	129	9.9	1.9
Exceptionals	(13)	1	-	-
APAT	104	130	24.7	2.5
Number of shares (Mn)	155.8	156.1	-	-
EPS (Rs) – Quarterly	1.3	1.7	24.5	2.0

Source: Company, India Infoline Research

## Dollar revenue growth modest; Rupee growth restricted by hedges

In dollar terms, revenues for Q1 FY08 grew by 3.4% qoq. In rupee terms the growth was 5.4% aided by 1.8% qoq higher realization of Re/\$. KPIT realized a lower Re/\$ rate as compared to other companies as it has covered ~85% of the net dollar inflows for FY09 at Rs40.25. This huge forex cover will continue to haunt the company in the H2 FY09 marginalizing any benefits from rupee depreciation. A forex loss of Rs23mn was included in the revenue line. With the onsite revenues (up 7.6% qoq) growing faster than offshore revenues (up 3.4% qoq), the revenue mix shifted onsite by 100bps qoq.

## Growth driven by ATS vertical and Cummins and other star customers

Revenues from the ATS vertical (Auto Electronics + Semiconductor Solutions) grew 8.3% qoq with its revenue share increasing from 32.5% to 33.4%. Growth was especially strong for Semiconductor Solutions that grew 28% qoq. Amongst customers, growth was seen in all star customers including Cummins, the top client. Cummins and other star customers grew by 6.8% and 7.9% qoq respectively. The US and Europe region registered above-company growth of 7.4% and 13.8% qoq respectively.

**Gross margin improves by 100bps but OPM declines by 130bps**

Gross margin improved 100bps qoq to 38.7% despite salary hikes (Onsite-<5% & Offshore->10%) for more than 50% of employees due to lower variable payments sequentially. Company had distributed significant variable payments in Q4 FY08, being the last quarter of the fiscal. However, OPM declined 130bps qoq to 13% due to higher S&M (up 14% qoq) and G&A (up 17% qoq) expenses. Higher S&M resulted from increase in headcount and salary hikes for marketing people. G&A was boosted by forex loss of Rs27mn and salary hikes.

**Lower interest and depreciation push profit growth to 25% qoq**

Depreciation was significantly lower qoq as previous quarter included ~Rs22mn amortization component with respect to payment made for taking over Cummins Business Services. Interest was also lower by 40% qoq. Aided by this, net profit jumped 25% qoq despite a 4% qoq decline in operating profit.

**Likely to miss FY09 earnings guidance; maintain Market Performer with price target Rs61**

Despite a sub-standard Q1 FY09, management refrained from changing the FY09 earnings guidance for the time-being saying that there is business unclarity in the near-term. Such statement from a management is astonishing and conveys negative signals. We believe that KPIT would significantly underperform its full-year earnings guidance of 27-31% yoy growth and the management is likely to revise it downward anytime. We rate KPIT as Market Performer with one-year target price of Rs61.

**Projected financials**

y/e Mar (Rs mn)	FY06	FY07	FY08E	FY09E	FY10E
Revenues	3,182	4,637	6,005	7,467	8,927
yoy growth (%)	26.0	45.7	29.5	24.3	19.6
Operating profit	462	708	923	1,029	1,223
OPM (%)	14.5	15.3	15.4	13.8	13.7
Pre-exceptional PAT	326	505	513	618	733
yoy growth (%)	14.7	55.0	1.6	20.5	18.6
EPS (Rs)	22.4	6.8	6.6	7.9	9.4
P/E (x)	2.5	8.3	8.6	7.1	6.0
P/BV (x)	0.6	2.1	1.8	1.5	1.2
EV/EBITDA (x)	2.8	6.8	5.4	5.1	4.4
ROE (%)	23.0	25.4	21.0	20.8	20.4
ROCE (%)	16.4	18.6	18.4	17.9	18.5

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