

Technology

Earnings revisions

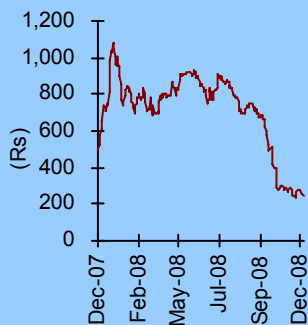
(%)	FY09E	FY10E	FY11E
Sales	↓ 2.4	↓ 13.7	↓ 21.6
EBITDA	↓ 7.0	↓ 18.2	↓ 24.7
EPS	↓ 0.2	↓ 13.1	↓ 25.2

Shareholding pattern

	Mar '08	Jun '08	Sep '08
Promoters	64.8	64.6	63.7
Institutional investors	22.0	21.8	23.0
MFs and UTI	11.9	11.9	12.8
Insurance Cos.	0.0	0.0	0.0
FII	10.1	9.9	10.2
Others	13.2	13.6	13.3

Source: www.nseindia.com

Price chart



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INDIA

Allied Digital Services

BUY

Maintained

Rs250

Better bet

Reason for report: Management meet and earnings revision

Key takeaways from our management meet with Allied Digital Services (ADSL) are: i) the company has not been significantly affected by the slowdown till date, except the complete freeze of capex IT budget by most Indian private sector banks (but significant opportunities available in PSU banks), ii) consolidation of clients creating new opportunities in migration and integration – ADSL has been positively impacted by mergers/acquisitions of Nomura-Lehman, DSPML-Blackrock & Kingfisher-Deccan, iii) increased opportunities in maintenance-system integration (SI) as clients prefer to extend current infrastructure rather than replacement, iv) increased traction in healthcare, ITES, airline for network operating centre (NOC)/security operating centre (SOC) offerings with significant deal wins in the past three months adding to the strong pipeline, v) improving revenue visibility from the recently acquired EnPointe (visibility increased to US\$57mn from US\$40mn at the time of acquisition) and vi) ADSL expects overall margins to improve 100-150bps per annum as the business mix changes in favour of RIMS offerings. We maintain BUY with revised price target of Rs525/share.

- ▶ **IMS & RIMS – Key growth drivers.** ADSL is witnessing good traction in its IMS and RIMS offerings and has added many new clients recently. Mandatory compliance requirement and significant cost savings in an uncertain environment are the prime reasons for this healthy growth. New NOC/SOC facility is expected to be operational by Q4FY09, by when (March '09) ADSL expects to manage +4,000 devices (upside risk to our FY09E & FY10E estimates of 2,100 & 3,900 devices respectively).
- ▶ **Better margins from EnPointe** The management expects EnPointe's FY10E EBITDA margin to improve from the current 10% to 20% (I-Sec 15%) via increased offshoring (over 60% of clients have agreed to offshoring).
- ▶ **Maintain BUY; we lower our price target to Rs525.** Factoring in the expected slower growth in project-based SI business, we have reduced our FY10E revenue and EPS estimates 13.7% and 13.1% respectively. Our revised target price is Rs525 at which the stock will trade at FY10E P/E of 6.8x and EV/EBITDA of 4x (Table 4). With strong earnings visibility (EPS CAGR of 54% over FY08-11E), changing business mix and improving margins, FY10E P/E of 3.2x and EV/EBITDA of 2.2x are attractive. Maintain BUY.

Market Cap	Rs4.5bn/US\$93mn
Reuters/Bloomberg	ADIS.BO/ALDS IN
Shares Outstanding (mn)	18.04
52-week Range (Rs)	1078/241
Free Float (%)	36.3
FII (%)	10.2
Daily Volume (US\$'000)	180
Absolute Return 3m (%)	(66.3)
Absolute Return 12m (%)	(49.2)
Sensex Return 3m (%)	(32.6)
Sensex Return 12m (%)	(52.4)

Year to March	FY08	FY09E	FY10E	FY11E
Revenue (Rs mn)	2,973	6,137	8,072	9,843
Net Income (Rs mn)	429	1,017	1,388	1,645
EPS (Rs)	24.8	56.4	77.0	91.2
% Chg YoY	38.3	127.0	36.5	18.5
P/E (x)	10.1	4.4	3.2	2.7
CEPS (Rs)	27.4	60.5	82.5	98.0
EV/E (x)	6.3	3.1	2.2	1.7
Dividend Yield (%)	0.5	0.5	0.5	0.5
RoCE (%)	34.1	34.8	29.3	26.4
RoE (%)	35.8	40.1	35.0	30.4

Q2FY09 results as expected

ADSL's standalone Q2FY09 revenues grew 14.8% QoQ to Rs1.03bn, in line with our expectations, backed by 15.4% growth in solutions and 13.2% surge in services. Revenues stood at Rs1.48bn, including the recent acquisition of EnPointe Global Services (only 80.5% consolidated on a *pro-rata* basis) effective July 10, '08. EnPointe reported EBITDA margins of 10.2%, resulting into consolidated EBITDA margin declining 560bps QoQ to 18.8%. With higher other income (including Rs15mn forex gain) and lower taxes (16.7% of PBT versus 26.7% in Q1FY09), consolidated PAT grew 53% QoQ to Rs241mn (I-Sec Rs220mn).

Table 1: Earnings revision

(Rs mn)

	FY09E			FY10E			FY11E		
	New	Old	% chg	New	Old	% chg	New	Old	% chg
Revenues	6,137	6,290	(2.4)	8,072	9,356	(13.7)	9,843	12,550	(21.6)
EBIDTA	1,374	1,478	(7.0)	1,954	2,389	(18.2)	2,530	3,361	(24.7)
EPS (Rs)	56.4	56.5	(0.2)	77.0	88.6	(13.1)	91.2	121.9	(25.2)

Source: I-Sec Research

Table 2: Revenue CAGR at 27% over FY09E-11E

(Rs mn, year ending March 31)

	FY08	FY09E	FY10E	FY11E
Revenues				
Solutions	2,343	3,234	3,861	4,593
- Enterprise Solutions	2,013	2,727	3,190	3,737
- Integrated Solutions	330	507	671	856
Services	630	1,493	2,266	3,170
-T-BPO + IMS	496	682	899	1,146
-NOC + SOC	134	811	1,368	2,024
Digicomp	-	163	202	244
EnPointe	-	1,247	1,742	1,835
Total	2,973	6,137	8,072	9,843
Growth Rate (%)				
Solutions	88.5	38.0	19.4	19.0
- Enterprise Solutions	80.0	35.5	17.0	17.1
- Integrated Solutions	165.0	53.6	32.4	27.6
Services	100.9	137.1	51.9	39.9
- T-BPO + IMS	58.2	37.5	31.8	27.6
- NOC + SOC	-	506.2	68.7	47.9
Digicomp	-	-	23.8	20.9
EnPointe	-	-	39.8	5.3
Total	91.0	106.4	31.5	21.9
Revenue breakup (%)				
Solutions	78.8	52.7	47.8	46.7
- Enterprise Solutions	67.7	44.4	39.5	38.0
- Integrated Solutions	11.1	8.3	8.3	8.7
Services	21.2	24.3	28.1	32.2
- T-BPO + IMS	16.7	11.1	11.1	11.6
- NOC + SOC	4.5	13.2	16.9	20.6
Digicomp	0.0	2.7	2.5	2.5
EnPointe	0.0	20.3	21.6	18.6
Total	100.0	100.0	100.0	100.0

Source: Company, I-Sec Research

Table 3: EBITDA CAGR at 36% through FY09E-11E

	FY08	FY09E	FY10E	FY11E
EBITDA (Rs mn)				
Solutions	349	465	550	656
TBPO + IMS + Digicomp	228	353	455	547
NOC + SOC	78	406	686	992
EnPointe	0	150	262	336
Total	655	1,374	1,954	2,530
EBITDA (%)				
Solutions	14.9	14.4	14.3	14.3
TBPO + IMS + Digicomp	46.1	41.7	41.4	39.3
NOC + SOC	58.1	50.1	50.2	49.0
EnPointe	-	12.1	15.0	18.3
Total	22.1	22.4	24.2	25.7

Source: Company, I-Sec Research

Table 4: Valuations based on FY10E EV/EBITDA

(Rs mn)

Business Segments	EBITDA	% of EBITDA	Old target multiple	New target multiple	EV	% to EV
Enterprise Solutions	550	28	5	3	1,513	19
TPO + IMS + Digicomp	455	23	7	4	1,752	22
NOC + SOC	686	35	10	6	3,775	48
EnPointe	262	13	6	3	865	11
Total EV	1,954	100	7.4	4.0	7,905	100
Add Cash					2,371	
Less Debt					814	
Equity Value					9,462	
No. of Shares outstanding (mn)					18,04	
Per Share Value (Rs)					525	

Source: Company, I-Sec Research

Maintain BUY; we lower our price target to Rs525/share

Factoring in the expected slower growth in project-based SI business, we have reduced our FY10E revenue and EPS estimates 13.7% and 13.1% respectively. Our revised target price is Rs525 at which the stock will trade at FY10E P/E of 6.8x and EV/EBITDA of 4x (Table 4). With strong earnings visibility (EPS CAGR of 54% over FY08-11E), changing business mix and improving margins, FY10E P/E of 3.2x and EV/EBITDA of 2.2x are attractive. Maintain BUY.

Financial Summary

Table 5: Profit and Loss Statement

(Rs mn, year ending March 31)

	FY08	FY09E	FY10E	FY11E
Operating Income (Sales)	2,973	6,137	8,072	9,843
of which Solutions	2,343	3,234	3,861	4,593
of which Others	630	2,903	4,211	5,250
Operating Expenses	2,310	4,763	6,118	7,313
EBITDA	662	1,374	1,954	2,530
% margins	22.3	22.4	24.2	25.7
Depreciation & Amortisation	33	61	81	98
Gross Interest expense	14	40	52	58
Other Income	30	53	68	93
Recurring PBT	646	1,325	1,889	2,466
Less: Taxes	217	278	453	765
Less: Minority Interest	0	30	47	57
Net Income (Reported)	429	1,017	1,388	1,645
Recurring Net Income	429	1,017	1,388	1,645

Source: Company data, I-Sec Research

Table 6: Balance Sheet

(Rs mn, year ending March 31)

	FY08	FY09E	FY10E	FY11E
Assets				
Total Current Assets	1,666	3,392	5,171	7,443
of which cash & deposits	414	1,062	2,071	3,538
Total Current Liabilities & Provisions	553	1,019	1,580	2,420
Net Current Assets	1,114	2,373	3,592	5,023
Investments	501	351	301	251
Strategic/Group	1	1	1	1
Other Marketable	500	350	300	250
Net Fixed Assets	234	1,505	1,774	2,076
Intangibles	0	920	920	920
Capital Work-in-Progress	57	72	87	102
Total Assets	1,906	4,301	5,754	7,452
of which cash and equivalents	914	1,412	2,371	3,788
Liabilities				
Borrowings	80	784	814	834
Deferred Tax Liability	12	25	44	69
Minority Interest	0	80	117	147
Equity Share Capital	173	180	180	180
Face Value per share (Rs)	10	10	10	10
Reserves & Surplus*	1,642	3,232	4,599	6,222
Net Worth	1,814	3,412	4,779	6,403
Total Liabilities	1,906	4,301	5,754	7,452

*excluding revaluation reserves

Source: Company data, I-Sec Research

Table 9: Quarterly trends

(Rs mn, year ending March 31)

	Dec-07	Mar-08	Jun-08	Sep-08
Net sales	793	820	911	1,489
% growth (YoY)	83.2	69.5	39.9	110.3
EBITDA	163	201	223	281
Margin (%)	20.6	24.6	24.5	18.8
Other income	16	9	6	31
Net profit	121	124	158	241

Source: Company data, I-Sec Research

Table 7: Cash Flow Statement

(Rs mn, year ending March 31)

	FY08	FY09E	FY10E	FY11E
Operating Cash flow before	662	1,374	1,954	2,530
Working Capital changes				
Working Capital Inflow / (Outflow)	(264)	(846)	(523)	(456)
Taxes Paid	(137)	(60)	(169)	(305)
Operating Free Cash flows	262	468	1,262	1,769
Capex	(220)	(1,347)	(365)	(415)
Changes in Traded Investments	(473)	150	50	50
Interest income	30	53	68	93
Interest Paid	(14)	(40)	(52)	(58)
Issue of Share Capital/Dividend paid	799	581	(21)	(21)
Process from Borrowings	0	784	67	49
Increase/(Decrease) in Cash	385	648	1,009	1,467

Source: Company data, I-Sec Research

Table 8: Key Ratios

(Year ending March 31)

	FY08	FY09E	FY10E	FY11E
Per Share Data (Rs)				
EPS(Basic Recurring)	24.8	56.4	77.0	91.2
Diluted Recurring EPS	24.8	56.4	77.0	91.2
Recurring Cash EPS	27.4	60.5	82.5	98.0
Dividend per share (DPS)	1.2	1.2	1.2	1.2
Book Value per share (BV)	104.9	189.2	265.0	355.0
Growth Ratios (%)				
Operating Income	91.0	106.4	31.5	21.9
EBITDA	102.9	107.5	42.2	29.5
Recurring Net Income	87.3	143.8	37.1	18.6
Diluted Recurring EPS	38.3	127.0	36.5	18.5
Diluted Recurring CEPS	50.7	120.7	36.3	18.8
Valuation Ratios (x)				
P/E	10.1	4.4	3.2	2.7
P/CEPS	9.1	4.1	3.0	2.6
P/BV	2.4	1.3	0.9	0.7
EV / EBITDA	6.3	3.1	2.2	1.7
EV / Operating Income	1.4	0.7	0.5	0.4
EV / Operating FCF (Post-Capex)	NA	17.2	NA	3.7
Operating Ratio				
Direct operating exps / Sales (%)	67.2	57.1	54.1	51.7
SG&A/Sales (%)	3.1	5.8	6.1	6.1
Other Income / PBT (%)	4.7	4.0	3.6	3.8
Effective Tax Rate (%)	33.5	21.0	24.0	31.0
NWC / Total Assets (%)	58.4	55.2	62.4	67.4
Asset Turnover (x)	12.7	4.1	4.5	4.7
Receivables (days)	110.0	105.0	103.0	100.0
Payables (days)	30.0	30.0	30.0	30.0
D/E Ratio (x)	0.0	0.2	0.2	0.1
Return/Profitability Ratio (%)				
Recurring Net Income Margins	14.4	16.6	17.2	16.7
RoCE	34.1	34.8	29.3	26.4
RoNW	35.8	40.1	35.0	30.4
Dividend Payout Ratio	4.7	2.1	1.5	1.3
Dividend Yield	0.5	0.5	0.5	0.5
EBITDA Margins	22.3	22.4	24.2	25.7

Source: Company data, I-Sec Research

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