

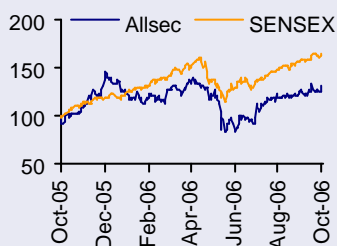
Allsec Technologies Ltd Q2 FY07 - Investment Update

Recommendation:	BUY
CMP:	Rs255
Target Price:	Rs309
Upside:	21.1%
52 Wk H/L:	Rs305/142
Market Cap:	Rs3.88bn
Face Value:	Rs10
BSE Code:	532633
NSE Code:	ALLSEC

Share holding pattern

Sep '06	(%)
Promoters	30.2
Institutions	58.3
Public	7.9
Others	3.6

Share price chart



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Allsec posted strong performance in the quarter with revenues and earnings growing sequentially by 11.5% and 9.2% respectively. Though the revenue growth was slightly above our expectation, the earnings growth was in line with our estimate. The quarter was marked by two key positives, qoq OPM expansion by 120bps and highest-ever 5 client additions. The only worry was material sequential de-growth in Top client's (CompuCredit) revenues. Most importantly, management has guided for continuance of strong growth in remaining quarters of the fiscal.

Financial highlights

Period (Rs mn)	09/06 (3)	06/06 (3)	Growth (%) qoq	09/05 (3)	Growth (%) yoy
Sales	308	277	11.5	240	28.7
Expenditure	(219)	(200)	9.7	(170)	29.3
Operating profit	89	77	16.4	70	27.2
OPM (%)	28.9	27.7	-	29.2	-
Other income	6	11	(43.0)	1	622.1
Interest	(0)	(0)	-	(2)	(84.7)
Depreciation	(20)	(20)	1.0	(18)	9.8
PBT	75	67	11.5	51	46.8
Tax	(1)	1	(181.3)	7	-
PAT	74	68	9.2	58	27.1
NPM (%)	24.0	24.5	-	24.3	-
Equity	152.3	120.8	-	120.6	-
EPS (Rs) Annualized	19.5	22.5	-	19.3	-
P/E (x) at CMP Rs255	13.1	-	-	-	-

- √ Company records the best in the last four quarters sequential topline growth of 11.5%. Revenues in the quarter were mainly driven by strong growth witnessed in the second and third largest accounts. Despite CompuCredit (the Top client) revenues de-growing 16.4% qoq, the Top 5 clients revenue contribution remained stable sequentially at about 65%. Average realizations were between 11.5-12\$/hr, similar to previous quarter.
- √ CompuCredit revenue contribution declined from 40% in Q1 FY07 to 30% Q2 FY07. For H1 FY07, it stood at near 35% compared to 40% in full year FY06. Company classifies the sequential de-growth in the quarter as an aberration and expects growth resumption in coming quarters. None of the jobs/processes run for CompuCredit was terminated during the quarter.
- √ There was a marginal shift in voice/non-voice revenue mix on sequential basis from 81/19 to 80/20 implying that growth was all-round covering both the main service segments.
- √ Company added highest-ever 5 clients in the quarter (compared to 1 in Q1 FY07) constituting 2 for voice services and 3 for non-voice service offerings. The 2 voice clients added are based in US whereas of the 3 non-voice clients (all added for HR processing services), 2 are domestic and 1 is international. Most importantly, none of the client addition was from Carlyle's reference in any way. At the end of the quarter company had about 26-27 active relationships.

- √ Quarter ending manpower stood at 2,744 on stand-alone basis and about 3,000 on consolidated basis (including B2K). The consolidated seat utilization was near 1.3x (3,000 people/2,300 seats) at the end of the quarter. Net 166 and gross 804 people were added in the quarter. Hefty 638 people left the company but this was in line with the seasonal and traditional pattern as per the company. Of the 2,744 people on stand-alone basis about 2,184 were billable.
- √ OPM improved by 120bps on sequential basis to 28.9% despite distribution of incentives for employees (staff cost up 17.1% qoq) during the quarter. The adverse impact of the above was more than compensated by containing connectivity costs and SG&A expenses both of which remained flat sequentially in absolute terms. Operating profit growth was relatively higher at 16.4% qoq.
- √ Net profit growth at 9.2% qoq was less than proportional due to lower other income and higher tax outflow.
- √ B2K achieved cash break-even and made a loss of about Rs6-6.5mn in the quarter. Company reiterated target of achieving overall break-even for the recently acquired entity by the end of the year. At the end of the quarter, B2K employed around 260 people on 600 seats implying a utilization of 0.43x.
- √ Cash and cash equivalent (C&CE) at the end of the quarter stood at about Rs900mn. Company intends to acquire 2-3 companies from the above money. New vertical/service expertise, new geography, established client base and good profitability to be the key rationale/criteria behind the inorganic growth strategy. Company keen on establishing presence in the US region and expects to close one transaction before the end of the year.
- √ Management is confident of maintaining 10-11% qoq revenue growth and current profitability margins in the remaining quarters of the fiscal.

With stand-alone revenues of Rs585mn and earnings of Rs142mn in H1 FY07 and management's strong comments on remaining quarters, we believe that company would meet our FY07 consolidated (including B2K) revenue and earnings estimates of Rs1.51bn and Rs313mn (given in our September 2006 report) respectively. Improvement in seat utilization from the current level to near 1.6x by the end of the year would remain a major margin defense for the company. We still do not factor the prospective acquisitions in our estimates without any enhanced information on the same. We maintain 'BUY' with our August 2007 price target of Rs309 based on 5.5x FY08 EV/EBITDA.

Quarterly Trends (Stand-alone)

Period (Rs mn)	Q1 FY05	Q2 FY05	Q3 FY05	Q4 FY05	Q1 FY06	Q2 FY06	Q3 FY06	Q4 FY06	Q1 FY07	Q2 FY07
Sales	124	152	139	161	183	240	241	259	277	308
% qoq growth	-	22.3	(8.3)	15.9	13.7	30.9	0.5	7.7	6.6	11.5
Expenditure	(89)	(107)	(103)	(117)	(131)	(170)	(169)	(186)	(200)	(219)
Operating profit	35	45	36	44	53	70	72	74	77	89
% qoq growth	-	28.2	(20.9)	22.8	20.1	33.3	2.7	2.2	4.1	16.4
OPM (%)	28.3	29.7	25.6	27.1	28.7	29.2	29.9	28.3	27.7	28.9
Other income	1	(1)	0	0	0	1	1	9	11	6
Interest	(4)	(4)	(3)	(3)	(2)	(2)	(1)	(0)	(0)	(0)
Depreciation	(10)	(10)	(11)	(10)	(10)	(18)	(16)	(17)	(20)	(20)
PBT	23	30	21	31	41	51	56	65	67	75
Tax	0	0	8	6	(1)	7	(1)	(1)	1	(1)
ETR (%)	-	-	(38.5)	(18.9)	1.6	(14.4)	1.2	2.0	(1.2)	0.9
PAT	23	30	29	37	40	58	56	63	68	74
% qoq growth	-	33.7	(3.1)	26.3	8.5	45.4	(4.7)	13.9	7.2	9.2
NPM (%)	18.2	19.9	21.1	23.0	21.9	24.3	23.1	24.4	24.5	24.0
Equity	43.5	43.5	43.5	88.2	119.6	120.6	120.6	120.8	120.8	152.3
EPS (Rs) Annualized	20.8	27.8	26.9	16.8	13.4	19.3	18.4	21.0	22.5	19.5

Financials

Projected Income statement

Period (Rs mn)	FY04 (12)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
Net sales	251	578	939	1,515	2,089
Operating expenses	(352)	(406)	(677)	(1,124)	(1,539)
Operating profit	(102)	172	262	391	549
Other income	0	0	15	50	65
PBIDT	(102)	172	276	441	614
Interest	(15)	(14)	(5)	0	0
Depreciation	(49)	(41)	(68)	(115)	(140)
Def rev exp w/off	(7)	(1)	(0)	0	0
Profit before tax	(173)	115	203	326	474
Tax	3	10	4	(13)	(19)
Profit after tax	(170)	125	207	313	455
Adjusted profit after tax	(170)	125	207	313	455

Projected Balance Sheet

Period (Rs mn)	FY04 (12)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
Sources					
Equity Share Capital	177	88	121	162	162
Pref Share Capital	0	0	49	49	49
Share Premium	0	124	461	1,486	1,486
Other reserves	(152)	(23)	117	337	663
Net Worth	25	190	699	1,985	2,311
Loan Funds	115	72	2	0	0
Total	140	262	749	2,034	2,360
Uses					
Gross Block	238	257	599	679	919
Accd Depreciation	(78)	(119)	(209)	(324)	(464)
Net Block	159	138	389	354	454
Capital WIP	0	16	2	0	0
Total Fixed Assets	159	154	391	354	454
Goodwill	0	0	48	48	48
Investments	0	0	0	1,200	1,400
Total Current Assets	79	151	466	672	783
Total Current Liabilities	(104)	(68)	(178)	(250)	(335)
Net Working Capital	(25)	83	288	422	448
Miscellaneous exp	2	10	0	0	0
Def Tax assets	3	15	22	10	10
Total	140	261	749	2,034	2,360

Projected Cash Flow Statement

Period (Rs mn)	FY04 (15)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
Pre Tax income from operations	(173)	115	188	276	409
Depreciation	49	41	68	115	140
Expenses (deferred)/written off	(2)	(8)	9	0	0
Deferred Tax Asset/liability	(3)	(11)	(8)	12	0
Pre tax cash from operations	(128)	137	258	403	549
Other income/prior period ad	0	0	15	50	65
Net cash before tax	(128)	137	273	453	614
Tax	3	10	4	(13)	(19)
Cash profits	(125)	147	277	440	595
(Inc)/Dec in trade working capital					
-Sundry debtors	(55)	(41)	(110)	(50)	(60)
-Sundry creditors	104	(39)	39	52	45
-Others	0	3	71	21	40
Net trade working capital	49	(77)	(0)	23	25
Operating activities	(76)	70	277	463	620
(Add)/Dec in fixed assets					
(Add)/Dec in Goodwill	0	0	(48)	0	0
(Add)/Dec in Investments	0	0	0	(1,200)	(200)
(Inc)/Dec in Loans/advances	(19)	(8)	(37)	(104)	(71)
Investing activities	(228)	(44)	(390)	(1,382)	(511)
Inc/(Dec) in debt					
Inc/(Dec) in debt	115	(43)	(71)	(2)	0
Inc/(Dec) in equity/premium					
Inc/(Dec) in equity/premium	177	35	419	1,066	(0)
Direct add/(red) to reserves-Spl.item					
Direct add/(red) to reserves-Spl.item	18	16	1	0	0
Dividends					
Dividends	0	(12)	(69)	(92)	(129)
Financing activities	309	(3)	281	972	(129)
Cash generated/(utilised)					
Cash generated/(utilised)	5	23	168	54	(20)
Cash at start of the year					
Cash at start of the year	0	5	28	196	250
Cash at end of the year	5	28	196	250	230

Key Ratios

Period	FY04 (15)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
Per share ratios					
EPS (Rs)	(38.6)	14.2	17.1	19.3	28.1
Div per share (Rs)	0.0	1.2	5.0	5.0	7.0
Book value per share (Rs)	5.6	21.5	57.9	122.6	142.8
Valuation ratios					
P/E (x)	(6.6)	18.0	14.9	13.2	9.1
P/BV (x)	45.2	11.9	4.4	2.1	1.8
M Cap/Sales (x)	4.5	3.9	3.3	2.7	2.0
EV/Sales (x)	4.9	4.0	3.1	1.8	1.2
EV/EBIDTA (x)	(12.1)	13.3	10.4	6.1	4.1
Profitability ratios					
OPM (%)	(40.6)	29.7	27.9	25.8	26.3
PAT (%)	(67.7)	21.7	22.0	20.6	21.8
ROCE (%)	(113.0)	49.4	27.7	16.0	20.1
RONW (%)	(684.2)	66.1	29.6	15.8	19.7
Liquidity ratios					
Current ratio (x)	0.8	2.2	2.6	2.7	2.3
Debtors days	80.1	60.4	79.8	61.4	55.0
Net WC/Sales (%)	(9.9)	14.4	30.6	27.9	21.4
Net WC/TCE (%)	(17.8)	31.8	38.4	20.8	19.0
WC cycle (days)	(71.1)	19.7	39.7	24.1	20.1
Payout ratios					
Dividend payout (%)	0.0	8.3	29.2	25.9	24.9
Tax payout (%)	1.8	(8.5)	(2.1)	4.0	4.0
ROE De-composition					
NPM	(67.7)	21.7	22.0	20.6	21.8
TATR (S/CE)	1.8	2.2	1.3	0.7	0.9
Equity Multiplier	5.6	1.4	1.1	1.0	1.0
Du-Pont ROE	(684.2)	66.1	29.6	15.8	19.7



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