

Zensar delivered strong results for the quarter with revenues and earnings growing far above expectations at 15.8% and 30.1% respectively. Even after excluding inorganic impact of Thought Digital, the organic revenue growth stood strong at ~10.8% qoq despite Rupee appreciation. Operating margin improved significantly by 170 bps led by sharp improvements in profitability of EAS and BPO segments. Higher other income offset the impact of sequentially higher tax payout there enabling 30.1% profit growth. Management has guided for a strong FY08 with revenues and earnings in excess of Rs8.5bn and Rs850mn respectively.

Financial Highlights

Period	03/07	12/06	Growth (%)	03/06	Growth (%)	03/07	03/06	Growth (%)
Rs mn	(3)	(3)	qoq	(3)	yoy	(3)	(3)	yoy
Sales	1,714	1,480	15.8	1,252	36.8	6,059	4,288	41.3
Operating Profit	243	185	31.5	218	11.8	828	541	53.1
OPM (%)	14.2	12.5	-	17.4	-	13.7	12.6	-
PAT	172	132	30.1	172	0.0	572	339	68.6
NPM (%)	10.0	8.9	-	13.7	-	9.4	7.9	-
EPS (Rs) Annualized	28.8	22.3	-	28.8	-	23.9	14.5	-
P/E (x) at CMP Rs300	10.4	-	-	-	-	12.5	-	-

- ✓ Revenues in the quarter grew by 15.8% on qoq basis and 36.8% on yoy basis. During the quarter, company acquired Thought Digital, a US based Oracle ERP lifecycle services company. Thought Digital financials were integrated for the last 5 weeks of the quarter adding ~Rs85mn to the topline. Even after excluding this, the pure organic growth stood strong at 10.8% qoq despite the 1.7% negative impact of Rupee appreciation. The growth in the quarter was volume led with pricing being stable sequentially. For the full year FY07, revenues were Rs6.06bn, higher than company's guidance of Rs5.8bn, representing a growth of 41.3%.
- ✓ In terms of service offerings, enterprise applications services (EAS) witnessed exceptional growth of 36.9% qoq with inclusion of Thought Digital revenues here. The organic growth in this segment of 14.6% qoq was far higher than that of the company. Other segments viz APM, ITS, BPO and Consulting also registered healthy growth rates of 8.8%, 9.6%, 8.3% and 5.5% respectively.
- ✓ In terms of clients, the large 5 clients led growth in the quarter. Top client, Cisco, grew 20% qoq while the next four clients grew by 12.2% qoq. Amongst verticals, manufacturing witnessed sharp de-growth of 31.8% qoq while utilities recorded significant growth of 48.8% qoq.
- ✓ The operating margin improved significantly by 170 bps qoq to 14.2% despite negative impacts of Rupee appreciation and Thought Digital integration (lower margin here due to ongoing restructuring) for five weeks. Company was helped by sharp improvements in profitability of EAS (from 5% to 17.5% qoq) and BPO (from 1.5% to 25.5% qoq) segments. For FY07 also, OPM showed improvement yoy by 110 bps to 13.7%.
- ✓ Forex gains boosted other income by 119.2% qoq to Rs38mn while higher provisions led to higher tax rate of 22.2% against 18.4% in the previous quarter. Quarterly net profit increased by phenomenal 30% qoq. For FY07, net profit was Rs572mn, higher than guided Rs550mn, representing 68.6% yoy growth.
- ✓ Company added about 452 people in the quarter including about 120 joining from Thought Digital. There was sharp sequential improvement in manpower utilization (including trainees) from 72% to 84%.
- ✓ For FY08, management expects revenues and earnings in excess of Rs8.5bn (>40% growth yoy) and Rs850mn (>48% growth yoy) respectively even after factoring the current Re/\$ scenario. It expects EAS to lead growth (driven by full year integration of Thought Digital) followed by ITS, BPO and APM. Company is confident about Cisco account growing >50% yoy and three of other large accounts growing >40% yoy in the year. Annual operating margin is expected to be near 14%.

Company's guidance for FY08 appears achievable given the fact that full year Thought Digital integration would add close to US\$27mn (similar to CY06 revenues) at least in the year thereby leaving a yoy growth requirement of 24% for organic revenues against 40% achieved in FY07. Further, profitability turnaround in ITS segment or even break-even here would act as a big margin lever enabling in sustaining operating margin on yoy basis. Management's earnings guidance translates into an EPS of Rs35.5 and reflects attractive P/E valuation of 8.5x on FY08 basis.

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