

Allsec Technologies

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Shareholding (%)

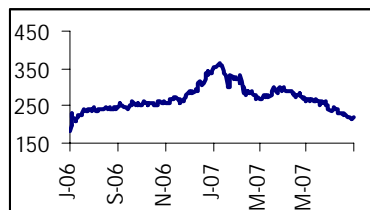
Promoters	26.8
FII's	12.6
Foreign Venture Capital	32.1
MFs	13.4
Others	15.1

Share price performance

52-week high/low (Rs)	374/183		
	-1m	-3m	-12m
Abs (%)	-6.5	-23.9	20.1
Rel* (%)	-15.0	-35.4	-31.8

*to Nifty

Stock chart



Rupee impacts profitability; maintain 'Accumulate'

Allsec Technologies Ltd's Q1FY08 revenue and net profit were impacted substantially by more than 7% due to rupee appreciation. Allsec reported sequential decline of 6% and 34.6% in revenue and net profit to Rs259mn and Rs46mn respectively. However, addition of more than 600 net employees in Q1FY08 has to an extent increased revenue visibility going forward.

Due to lower than expected results, we are lowering FY08E and FY09E EPS estimates by 26.9% and 14.6% to Rs15.7 and Rs23.1 respectively, implying a two-year EPS CAGR of 15.2%.

The stock has corrected by more than 15% in the past one quarter, on account of rupee appreciation. The stock is currently quoting at FY08E and FY09E PER of 14.1x and 9.6x respectively. Though the stock is cheaper than its peers in the offshore BPO space, we believe it should quote at a discount on account of its below industry level growth and smaller size. Therefore, we believe that the stock would be range bound in the near term, which is why we are maintaining 'Accumulate' rating on the stock. However, we may revisit our recommendation, if we see any inorganic activity or addition of a tier-I client.

Key highlights of Q1FY08 are:

- ▲ **Appreciating rupee impacts revenue:** Allsec reported 6% sequential decrease in revenue to Rs259mn. However, in dollar terms, revenue grew by around 2%. The company added more than 600 net employees in Q1FY08 and has indicated that it would deploy 200-250 of these employees with its existing clients and the rest with its new clients.
- ▲ **EBITDA margin declines by 890bps:** The company's EBITDA margin fell by 890bps to 20.2% in Q1FY08 on account of:
 - a) Rupee appreciation of more than 7%
 - b) Addition of more than 600 net employees in Q1FY08.

Going forward, we expect EBITDA margin of Allsec to increase, as the company benefits from economies of scale and lower per capita employee cost. We expect EBITDA margin of Allsec to be 23.9% in FY08E.

Accumulate Rs221

July 24, 2007

Market cap

Rs bn 4

US\$ mn 88

Avg 3m daily volume

25,481

Avg 3m daily value

Rs mn 7

Shares outstanding (mn)

16

Reuters

ALLS.BO/ALLSEC.NS

Bloomberg

ALST IN

Sensex

15,795

Nifty

4,621

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- ▲ **Share of voice revenue decreasing:** In Q1FY08, voice business contributed 74.6% to Allsec's revenue, down from 80.13% in Q4FY07. We believe that this could decrease further, as the company adds more clients in the HR-BPO space. The company added three new clients in the HR-BPO space and one in the voice space. Allsec's total clients in the HR-BPO and voice space now stand at 17 each.
- ▲ **Inorganic growth on the anvil:** In Q2FY07, Allsec raised Rs800mn through preferential allotment of three million shares to Carlyle. Allsec has indicated that it intends to utilise this money for inorganic growth. However, the company is yet to announce one. The company has also indicated that it would acquire a company by the end of this fiscal year. Allsec plans to acquire companies in order to either enter a new geographic area or a new vertical. Thus, we have not considered anticipated revenue from future acquisitions in our FY08E and FY09E estimates.
- ▲ **Plans to open new development centres:** Allsec plans to set-up new development centres in Trichy and Malaysia. The 200-seater Trichy facility is expected to start operations from Q2FY08E and 500-seater Manila facility from Q4FY08E.
- ▲ **Relationship with Carlyle likely to show results from FY09E:** Carlyle acquired 20% stake in Allsec through a preferential allotment in Q2FY07. Subsequent to this and Carlyle's open offer, its stake has increased to about 27%. Allsec has indicated that Carlyle has introduced them to large tier-I clients, of which four have no exposure to outsourcing. The company expects significant business from these clients and has indicated that it could be 300-400 seater contracts. The company expects to close a couple of deals by the end of FY08E. Hence, full benefit from Carlyle is expected to come in FY09E.
- ▲ **Forecasts:** Due to lower than expected Q1FY08 results, we are lowering FY08E and FY09E EPS estimates by 26.9% and 14.6% to Rs15.7 and Rs23.1 respectively, implying a two-year CAGR of 15.2%. However, it may be noted that we have not taken into account consolidation of B2K in our numbers, nor revenue from acquisitions in our FY08E and FY09E estimates.
- ▲ **Valuation:** Currently, the stock is quoting at FY08E and FY09E PER of 14.1x and 9.6x respectively. The stock has declined by over 15% in the last three months on account of sharp appreciation in rupee. Though Allsec is cheaper than its peers, we believe that it should quote at a discount on account of its below industry level growth and smaller size. Further, though Allsec's relationship with Carlyle is likely to bring increased revenue to the company from FY09E onwards, we believe that the current market price takes into account some upside from this expected business growth. Therefore, we maintain 'Accumulate' rating on the stock. However, we may revisit our recommendation, if there is some inorganic activity or it signs a big tier-I client.

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Table 1. Peer comparison

	EPS			PE			2 yr EPS CAGR
	CY06/FY07	CY07E/FY08E	CY08E/FY09E	CY06/FY07	CY07/FY08	CY08/FY09	
EXL (USD)	0.48	0.62	0.75	35.8	27.7	22.7	25.6%
WNS (USD)	0.78	0.77	1.10	34.2	34.7	24.1	19.0%
First Source (Rs)	2.50	3.3	4.00	32.4	24.5	20.3	26.5%
Allsec (Rs)	17.40	15.68	23.07	12.7	14.1	9.6	15.1%

Source: IISL research, Bloomberg

Table 2. Quarterly result table

Rs mn	Q1FY08	Q4FY07	QoQ (%)	Q1FY07	YoY (%)
Revenue	259	276	-6.0%	277	-6.3%
Staff cost	139	122	13.5%	115	20.8%
Operating expenditure	24	27	-11.1%	37	-34.2%
Other expenditure	43	46	-4.7%	48	-10.0%
EBITDA	52	80	-34.7%	76	-31.4%
EBITDA margin	20.2%	29.1%		27.6%	
Interest	0	2	-86.1%	0	-22.0%
Depreciation	19	19	-0.6%	20	-4.9%
Other income	11	10	8.0%	11	-0.8%
PBT	44	69	-36.5%	67	-34.4%
Tax	(2)	(1)		(1)	
Tax rate	-4.1%	-1.1%		-1.2%	
PAT	46	70	-34.6%	68	-32.5%
NPM	17.7%	25.4%		24.5%	

Source: IISL research, company

Table 3. Forecasts

Rs mn	FY06	FY07E	FY08E	FY09E
Net sales	923	1,133	1,230	1,721
% change	60.1	22.8	8.6	39.9
Net income	216	281	254	373
% change	85.0	30.0	-9.8	47.1
EPS (Rs.)	18.0	17.4	15.7	23.1
% change	36.1	-3.6	-9.8	47.1
P/E (x)	12.3	12.7	14.1	9.6
ROE (%)	32.5	23.4	14.3	18.5
ROCE (%)	30.6	20.5	11.4	15.4

Source: IISL research, company

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