

# Growing visibility, Buy



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## Raising estimates; Over 25% share price upside potential

Our bullish view on Infotech (top 5 India mid-cap pick) strengthened post meeting with management. Channel checks confirm momentum in engineering services overall and ramp-up in key clients like Bombardier and Alstom. US geo-spatial operations are turning around. Raising estimates 9-15% for FY07-09.

## Key engineering services clients in ramp-up mode

Alstom starting ramping only three quarters ago and we believe presents significant potential. Senior level visits by top management of clients like Bombardier indicate increasing strategic commitment to offshore engineering services. As per NASSCOM, global engineering services spend is US\$750b p.a., with only US\$10-15b offshored and India at a mere 12% share of offshore spend.

## Geospatial solutions design (GSD) business to pick-up

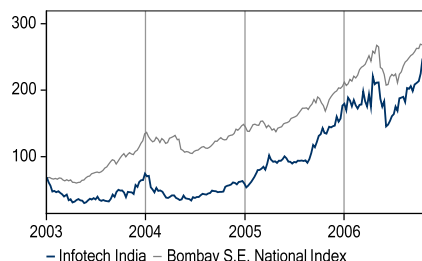
The GSD business (mapping, maintaining and analyzing location specific data) has seen two flattish quarters due to client specific issues in the US operations, which are now behind. Management indicated a strong pipeline, including several deals in the US. The company has also been working on reducing lower value added photogrammetry services in the US. European clients like Swisscom continue to ramp.

## Reiterate Buy rating for over 25% upside potential

We raise our EPS estimates by 9% for FY08 and 15% for FY09 led by higher revenue forecasts and superior mix led margin improvement (with engineering services picking up in mix). Our new PO of Rs375 (Rs285 previously) is set at 16x FY08E EPS at a 2-yr PEG of 0.65, given 25% EPS CAGR over FY07-09E, lower than the 0.7-1.2 range for peers. Key risks: Non-annuity revs in GSD, rising competition from larger Indian vendors.

## Stock Data

Price	Rs298.50
Price Objective	Rs375.00
Date Established	23-Nov-2006
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	Rs126.67-Rs318.00
Mrkt Val / Shares Out (mn)	US\$304 / 45.7
Average Daily Volume	70,566
ML Symbol / Exchange	IFKEF / BSE
Bloomberg / Reuters	INFTEC IN / INFE.BO
ROE (2007E)	33.2%
Net Dbt to Eqty (Mar-2006A)	-15.1%
Est. 5-Yr EPS / DPS Growth	24.0% / 18.0%
Free Float	NA



## Estimates (Mar)

(Rs)	2005A	2006A	2007E	2008E	2009E
Net Income (Adjusted - mn)	274	503	822	1,037	1,300
EPS	6.20	11.02	18.01	22.71	28.47
EPS Change (YoY)	201.3%	77.8%	63.4%	26.1%	25.4%
Dividend / Share	0.375	0.563	0.625	0.750	0.800
Free Cash Flow / Share	1.14	0.174	(3.33)	6.08	10.22

## Valuation (Mar)

	2005A	2006A	2007E	2008E	2009E
P/E	48.15x	27.08x	16.57x	13.14x	10.48x
Dividend Yield	0.126%	0.188%	0.209%	0.251%	0.268%
EV / EBITDA*	21.76x	15.21x	9.38x	7.16x	5.51x
Free Cash Flow Yield*	0.482%	0.076%	-1.46%	2.67%	4.48%

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 6.

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Refer to important disclosures on page 7 to 8. Analyst Certification on page 5. Price Objective Basis/Risk on page 5.

# iQprofile<sup>SM</sup> Infotech Enterprises Ltd

Key Income Statement Data (Mar)	2005A	2006A	2007E	2008E	2009E
<b>(Rs Millions)</b>					
Sales	2,571	3,625	5,367	7,230	9,600
Gross Profit	1,347	1,929	2,778	3,447	4,185
Sell General & Admin Expense	(878)	(1,257)	(1,688)	(2,019)	(2,330)
Operating Profit	302	486	843	1,146	1,494
Net Interest & Other Income	37	10	47	13	11
Associates	NA	NA	NA	NA	NA
Pretax Income	339	497	891	1,159	1,505
Tax (expense) / Benefit	(90)	(94)	(193)	(255)	(346)
Net Income (Adjusted)	274	503	822	1,037	1,300
Average Fully Diluted Shares Outstanding	44	46	46	46	46

## Key Cash Flow Statement Data

Net Income (Reported)	274	503	822	1,037	1,300
Depreciation & Amortization	167	186	247	282	362
Change in Working Capital	(112)	(288)	(487)	(543)	(701)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	(42)	(36)	(80)	2	6
Cash Flow from Operations	287	365	502	778	967
Capital Expenditure	(237)	(357)	(654)	(500)	(500)
(Acquisition) / Disposal of Investments	3	0	0	0	0
Other Cash Inflow / (Outflow)	(69)	(79)	54	(25)	0
Cash Flow from Investing	(303)	(436)	(600)	(525)	(500)
Shares Issue / (Repurchase)	11	100	0	0	0
Cost of Dividends Paid	(20)	(26)	(24)	(27)	(28)
Cash Flow from Financing	(23)	114	(86)	(41)	(48)
Free Cash Flow	50	8	(152)	278	467
Net Debt	(326)	(321)	(183)	(393)	(811)
Change in Net Debt	24	5	137	(209)	(419)

## Key Balance Sheet Data

Property, Plant & Equipment	327	683	1,093	1,333	1,493
Other Non-Current Assets	390	312	261	264	242
Trade Receivables	872	1,223	1,823	2,456	3,261
Cash & Equivalents	340	385	201	413	831
Other Current Assets	114	266	139	155	155
Total Assets	2,044	2,869	3,518	4,621	5,983
Long-Term Debt	14	65	18	20	20
Other Non-Current Liabilities	NA	NA	NA	NA	NA
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	465	680	667	773	876
Total Liabilities	479	745	685	793	896
Total Equity	1,564	2,123	2,833	3,828	5,087
Total Equity & Liabilities	2,044	2,868	3,518	4,621	5,983

## iQmethod<sup>SM</sup> - Bus Performance\*

Return On Capital Employed	13.7%	18.9%	24.2%	25.1%	24.5%
Return On Equity	19.1%	27.3%	33.2%	31.1%	29.2%
Operating Margin	11.8%	13.4%	15.7%	15.8%	15.6%
EBITDA Margin	18.3%	18.5%	20.3%	19.7%	19.3%

## iQmethod<sup>SM</sup> - Quality of Earnings\*

Cash Realization Ratio	1.0x	0.7x	0.6x	0.8x	0.7x
Asset Replacement Ratio	1.4x	1.9x	2.7x	1.8x	1.4x
Tax Rate (Reported)	26.5%	18.9%	21.6%	22.0%	23.0%
Net Debt-to-Equity Ratio	-20.8%	-15.1%	-6.5%	-10.3%	-16.0%
Interest Cover	NM	44.2x	NM	NM	NM

## Key Metrics

Sales Growth	37.2%	41.0%	48.1%	34.7%	32.8%
EBITDA GROWTH	60.9%	43.1%	62.2%	31.0%	30.0%
EBIT Growth	254.9%	60.8%	73.4%	35.9%	30.4%
Net Income Growth	204.3%	83.8%	63.4%	26.1%	25.4%

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 6.

## Company Description

Infotech is a mid-tier Indian IT services company providing geographical information system (GSI) services to utility, transportation, & government (UTG) segments, engineering design services to engineering, manufacturing, & industrial (EMI) product segments, & software services to both these segments. It has leadership positions in offshore GIS data conversion services for UTG segment & offshore mechanical design services for the EMI segment.

## Stock Data

Price to Book Value 3.7x

## Financial tables

**Table 1: Estimates revision table**

	New			Old			Change		
	FY07	FY08	FY09	FY07	FY08	FY09	FY07	FY08	FY09
Revenue	5,367.3	7,230.2	9,600.2	5,342.0	6,864.0	8,628.0	0.5%	5.3%	11.3%
EBITDA	1,090.0	1,427.8	1,855.4	1,067.1	1,301.4	1,623.6	2.1%	9.7%	14.3%
EBITDA Margin	20.3%	19.7%	19.3%	20.0%	19.0%	18.8%	33bps	79bps	51bps
PAT	822.3	1,036.9	1,300.0	813.0	948.0	1,128.0	1.1%	9.4%	15.2%
EPS	18.0	22.7	28.5	17.8	20.8	24.7	1.2%	9.2%	15.3%

Source: Merrill Lynch Research Estimates

**Table 2: Profit and loss statement**

Year to March, Rs mn	FY05	FY06	FY07E	FY08E	FY09E
<b>Revenues</b>	<b>2,571.3</b>	<b>3,625.0</b>	<b>5,367.3</b>	<b>7,230.2</b>	<b>9,600.2</b>
Personnel Expenses	1,223.9	1,696.5	2,589.1	3,783.6	5,415.2
Operating & Admin Expenses	877.7	1,256.5	1,688.1	2,018.8	2,329.5
Total operating expenses	2,102	2,953	4,277	5,802	7,745
<b>EBIDTA</b>	<b>469.7</b>	<b>672.0</b>	<b>1,090.0</b>	<b>1,427.8</b>	<b>1,855.4</b>
Other Income	39.5	21.3	62.1	29.1	31.2
Interest expense, net	2.5	11.0	14.8	16.0	20.0
Depreciation & Amortization	167.3	185.7	246.7	281.9	361.8
<b>EBIT</b>	<b>302.4</b>	<b>486.3</b>	<b>843.3</b>	<b>1,145.8</b>	<b>1,493.6</b>
<b>Profit before Tax</b>	<b>339</b>	<b>497</b>	<b>891</b>	<b>1,159</b>	<b>1,505</b>
Provision for Tax	90.1	94.0	192.7	255.0	346.1
<b>Profit after tax</b>	<b>249.3</b>	<b>402.6</b>	<b>697.9</b>	<b>904.0</b>	<b>1,158.8</b>
Share of IASI profit	25	101	124	133	141
<b>Profit after tax incl share above</b>	<b>274</b>	<b>503</b>	<b>822</b>	<b>1,037</b>	<b>1,300</b>

Source: Company, Merrill Lynch Research Estimates

**Table 3: Balance Sheet**

As at 31st March, Rs mn	FY05	FY06	FY07E	FY08E	FY09E
Share Capital	147	152	228	228	228
Reserves & Surplus	1,417	1,971	2,604	3,600	4,859
<b>Shareholders funds</b>	<b>1,564</b>	<b>2,123</b>	<b>2,833</b>	<b>3,828</b>	<b>5,087</b>
Debt	14	65	18	20	20
<b>Source of funds</b>	<b>1,578</b>	<b>2,188</b>	<b>2,851</b>	<b>3,848</b>	<b>5,107</b>
Gross Fixed Assets	1,324	1,811	2,446	2,946	3,446
Accumulated depreciation	860	1,014	1,260	1,542	1,904
Net Fixed Assets	463	798	1,186	1,404	1,542
Capital WIP	141	11	30	30	30
Investments	100	179	125	150	150
<i>Current Assets:</i>					
Inventories	2	1	4	5	5
Sundry Debtors	872	1,223	1,823	2,456	3,261
Cash & Cash equivalents	340	385	201	413	831
Loans & Advances	112	265	135	150	150
<i>Current Liabilities</i>	358	525	400	425	425
<i>Provisions</i>	108	156	267	348	451
<b>Working Capital</b>	<b>861</b>	<b>1,194</b>	<b>1,497</b>	<b>2,251</b>	<b>3,371</b>
Deferred Tax asset	13	8	13	13	13
<b>Application of funds</b>	<b>1,578</b>	<b>2,189</b>	<b>2,851</b>	<b>3,848</b>	<b>5,107</b>

Source: Company, Merrill Lynch Research Estimates

**Table 4: Cash Flow statement**

Year to March, Rs mn	FY05	FY06E	FY07E	FY08E	FY09E
PAT	273.9	503.3	822.3	1,036.9	1,300.0
Depreciation	167.3	185.7	246.7	281.9	361.8
Interest	2.5	11.0	14.8	16.0	20.0
(Inc) / Dec in Working capital	(111.8)	(287.6)	(486.6)	(543.4)	(701.4)
Others	(44.9)	(47.1)	(94.9)	(13.7)	(13.9)
<b>Net cash from operations</b>	<b>287.0</b>	<b>365.2</b>	<b>502.4</b>	<b>777.7</b>	<b>966.5</b>
Investments	(68.9)	(79.0)	53.8	(25.0)	-
Capital expenditure	(236.9)	(357.3)	(654.3)	(500.0)	(500.0)
Acquisitions / JV	3.0				
Others					
<b>Net cash from investing</b>	<b>(302.7)</b>	<b>(436.3)</b>	<b>(600.4)</b>	<b>(525.0)</b>	<b>(500.0)</b>
Free Cash Flow	50.2	8.0	(151.9)	277.7	466.5
Issue of equity	10.7	99.8	-	-	-
Inc / (Dec) in Debt	(11.7)	50.6	(46.6)	2.0	-
Dividends	(19.9)	(25.6)	(24.5)	(27.5)	(27.7)
Interest	(2.5)	(11.0)	(14.8)	(16.0)	(20.0)
Others					
<b>Net cash from financing</b>	<b>(23.4)</b>	<b>113.8</b>	<b>(85.9)</b>	<b>(41.5)</b>	<b>(47.7)</b>
Exchange differences	3.9	2.9	-	-	-
<b>(Dec) / Inc in cash</b>	<b>(35.2)</b>	<b>45.6</b>	<b>(183.9)</b>	<b>211.3</b>	<b>418.8</b>
Cash balance at the beginning	374.8	339.6	385.2	201.3	412.5
Cash balance at the end	339.6	385.2	201.3	412.5	831.4

Source: Company, Merrill Lynch Research Estimates

**Table 5: Key ratios**

Year to 31st March	FY05	FY06E	FY07E	FY08E	FY09E
<b>EPS (Rs)</b>	<b>6.2</b>	<b>11.0</b>	<b>18.0</b>	<b>22.7</b>	<b>28.5</b>
CFPS (Rs)	10.0	15.1	23.4	28.9	36.4
BVPS (Rs)	35.4	46.5	62.0	83.9	111.4
CPS (Rs)	5.2	2.6	1.5	5.8	14.9
PER	49.2	26.8	16.4	13.0	10.4
P/ CF	30.5	19.5	12.6	10.2	8.1
P/ BV	8.3	6.3	4.8	3.5	2.6
EV/ EBIDTA	28.3	19.8	12.2	9.3	7.2
EV/ Net sales	5.2	3.7	2.5	1.8	1.4
Net Debt	(437.3)	(585.7)	(318.3)	(542.5)	(961.4)
FCF per share	1.14	0.17	(3.33)	6.08	10.22
<b>Profitability (%)</b>					
EBITDA margin	18.3	18.5	20.3	19.7	19.3
Net Profit margin	10.7	13.9	15.3	14.3	13.5
<b>Turnover (times)</b>					
Debtor days	124	123	124	124	124
Total Assets	1.6	1.7	1.9	1.9	1.9
Net fixed assets	5.5	4.5	4.5	5.2	6.2

Source: Company, Merrill Lynch Research Estimates

## Price Objective Basis & Risk

Our PO of Rs375 is set at 16x FY08E EPS at a 2-yr PEG of 0.65, given a 25% EPS CAGR over FY07-09E, lower than the 0.7-1.2 range for peers.

Key risks: 1) Non-annuity revenues in GIS, 2) Increasing competition from large Indian IT vendors, 3) Threat of captive in engineering services and 4) Rupee appreciation and industry wide wage inflation.

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I, Mitali Ghosh, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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**iQmethod<sup>SM</sup> Measures Definitions**

<b>Business Performance</b>	<b>Numerator</b>	<b>Denominator</b>
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
<b>Quality of Earnings</b>		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
<b>Valuation Toolkit</b>		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Sales} + \text{Other LT Liabilities}$	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

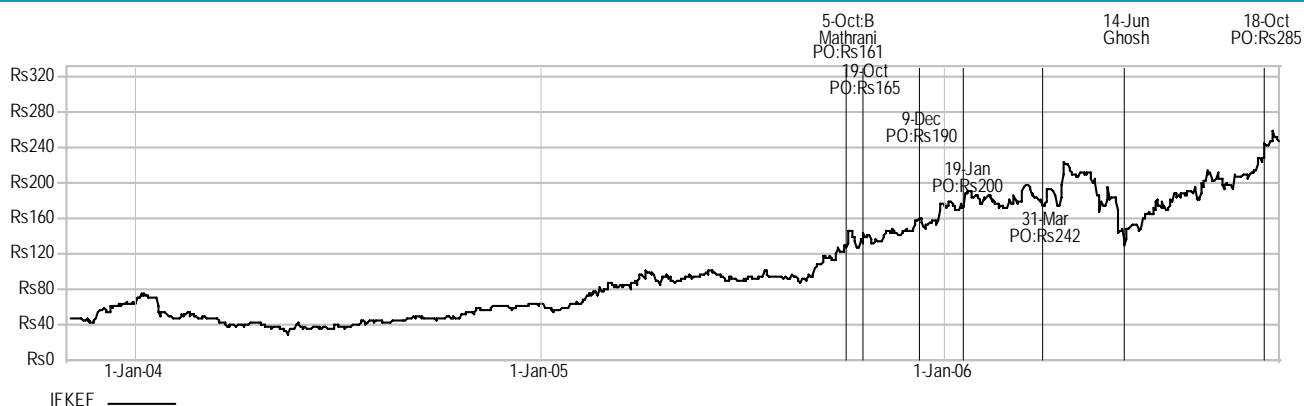
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B : Buy, N : Neutral, S : Sell, PO : Price objective, NA : No longer valid

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark Grey shading indicates the security is restricted with the opinion suspended. Light Grey shading indicates the security is under review with the opinion withdrawn. Chart current as of October 31, 2006 or such later date as indicated.

### Investment Rating Distribution: Technology Group (as of 30 Sep 2006)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	111	45.12%	Buy	21	18.92%
Neutral	126	51.22%	Neutral	21	16.67%
Sell	9	3.66%	Sell	1	11.11%

### Investment Rating Distribution: Global Group (as of 30 Sep 2006)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1325	44.76%	Buy	434	32.75%
Neutral	1420	47.97%	Neutral	412	29.01%
Sell	215	7.26%	Sell	48	22.33%

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