

## Company Flash

9 April 2007 | 7 pages

# Sasken Communication Technologies (SKCT.BO)

## Buy: Lenovo Signed as First E-Series Customer

- First E-Series customer** — Sasken Application Framework has been chosen by Lenovo as its Application Solution of choice for development of feature phones based on the OMAP-Vox platform from Texas Instruments.
- Feature-rich product** — Sasken Application Framework offers an advanced solution for rich media phones with features such as video record and play, audio-video streaming, Bluetooth stereo headsets, touchpad with handwriting recognition, as well as messaging solutions and HTML browser.
- Roadmap for E-Series** — In our past interactions, management indicated that it should take 6-9 months to go from "design in" to "design win" stage. We expect the first product on E-Series to be launched in 3Q FY08.
- Product roadmap encouraging** — At end-3Q FY07, Sasken expected 7 design-wins in FY08. With Lenovo also potentially being launched in FY08, the product roadmap looks encouraging.
- Reiterate Buy/Medium risk** — The stock trades at 15.4x FY08E EPS. Even if one values the product business at zero, the services business at ~10.5x FY08E EV/EBITDA is in line with other mid-cap stocks under our coverage. We value the product business at 3x FY08E revenues. With 70%+ EPS CAGR over FY06-FY09E, our Buy/Medium Risk rating is maintained.

<b>Buy/Medium Risk</b>	<b>1M</b>
Price (09 Apr 07)	Rs480.25
Target price	Rs653.00
Expected share price return	36.0%
Expected dividend yield	0.6%
<b>Expected total return</b>	<b>36.6%</b>
Market Cap	Rs13,687M US\$321M

### Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2005A	228	13.53	na	35.5	5.5	na	0.6
2006A	229	8.09	-40.2	59.4	3.5	8.7	0.6
2007E	495	17.29	113.8	27.8	3.2	12.2	0.6
2008E	903	31.23	80.6	15.4	2.7	19.5	1.0
2009E	1,229	42.11	34.8	11.4	2.3	22.6	2.1

Source: Powered by dataCentral

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<sup>1</sup>Citigroup Global Market India Private Limited

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Figure 1. Indian IT Sector Valuation Table

Company	RIC Code	Rating	Mkt cap (US\$ m)	Share price	Target price	P/E (x)		EV/EBITDA (x)	
						FY07E	FY08E	FY07E	FY08E
Infosys	INFY.BO	1L	26,016	1,992	2,660	30.4	23.5	24.2	18.5
TCS	TCS.BO	1L	27,348	1,194	1,560	28.2	22.1	22.9	17.7
Wipro	WIPR.BO	1L	18,823	551	730	28.2	22.0	22.4	17.2
Satyam	SATY.BO	1M	7,114	456	582	22.3	18.1	17.6	13.7
HCL Tech	HCLT.BO	1M	4,467	288	385	18.8	15.7	13.6	10.9
Patni*	PTNI.BO	1M	1,314	401	463	21.0	13.5	9.0	7.8
I-Flex	IFLX.BO	3M	4,117	2,112	1,850	53.0	40.1	40.9	28.6
Hexaware*	HEXT.BO	1M	518	167	214	18.5	14.8	15.9	9.9
NIIT	NIIT.BO	1M	322	697	690	28.8	16.5	17.1	12.1
Sasken	SKCT.BO	1M	321	482	653	27.9	15.4	15.3	10.7
KPIT	KPIT.BO	1M	225	129	173	23.8	14.4	13.4	10.2

Source: Company Reports and Citigroup Investment Research estimates; \*Using CY06E and CY07E for these companies (31-Dec year-ending).

## Sasken Communication Technologies

### Company description

Bangalore-based Sasken was established in 1989 and initially worked on electronic design automation projects. It now offers embedded software services to network equipment manufacturers, device manufacturers and service providers in the wireless and broadband space, and semiconductor vendors. Key clients include large tier-one vendors such as Nokia and Nortel. Sasken has also been investing in a products business.

### Investment thesis

We rate Sasken as Buy/Medium Risk (1M). Increasing competition is driving telecoms vendors to outsourcing software and services to countries such as India. R&D services are being outsourced from India. Sasken, with a strong focus on the telecoms and embedded space, is benefiting from this trend. We expect Sasken's services business to record a 42% CAGR over FY06-09. The acquisition of Botnia has helped in accelerating growth. The products business is in investment mode, but the number of design-ins is encouraging. We expect a ramp-up and a turnaround in the products business in FY08; we forecast a 52% CAGR in revenues over FY06-09 and see the business turning around from losses to a 30%-plus margin in FY09.

### Valuation

Our 12-month target price of Rs653 is based on a sum-of-the-parts valuation for the services business and the loss-making products business. We apply an FY08E EV/EBITDA target of 12x for Sasken's services business, which is supported by the valuations of comparable mid-caps. We value Sasken's products business at 3x EV/Sales, similar to the valuation Motorola paid for Sasken's largest competitor, TTPCom, and is supported by our forecast 30%-plus margin in FY09. Our target price implies a P/E of 20.5x FY08E EPS — a premium to the sector, which we think is justified by Sasken's strong growth rates, better margin leverage and a sharp improvement in return ratios.

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### Risks

Our quantitative risk rating system, which tracks 260-day historical share price volatility, rates Sasken as Medium Risk. Risks that could impede the stock from reaching our target price include: (1) high client concentration; (2) slowdown in the telecoms industry; (3) delays in the handset launches in which Sasken is involved, or poor customer response to the handsets; (4) technology obsolescence; (5) wage inflation and currency appreciation; and (6) volatility in QoQ revenues, as investors are used to more linear models of growth for most Indian IT services companies.

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## Appendix A-1

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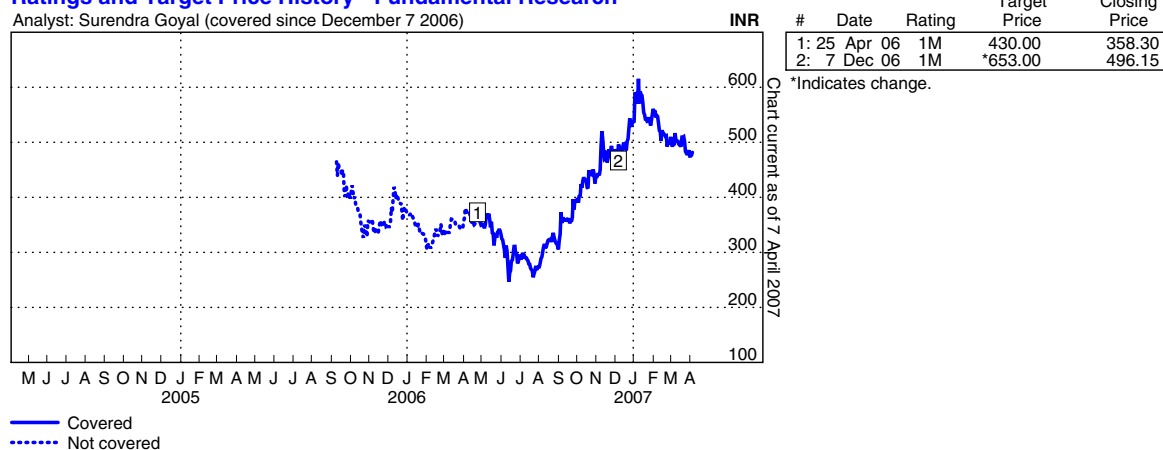
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##### Ratings and Target Price History - Fundamental Research

Analyst: Surendra Goyal (covered since December 7 2006)



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