

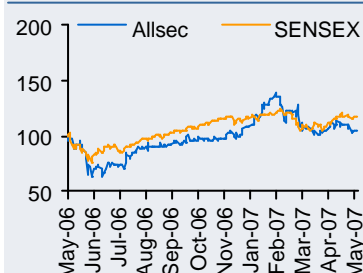
## Allsec Technologies Ltd (Q4 FY07) - Investment Update

<b>Recommendation</b>	<b>BUY</b>
CMP	Rs280
Target Price	Rs339
Upside	20.9%
52 Wk H/L	Rs366/142
Market cap	Rs4.27bn
Face value	Rs10
BSE code	532633
NSE code	ALLSEC

### Share Holding Pattern

Mar'07	(%)
Promoters	26.7
Foreign VCs/Institutions	42.4
Domestic MFs/Institutions	10.6
Indian Public	10.0
Others	10.3

### Share Price Trend



### Analyst

Rajiv Mehta  
rajivm@indiainfoline.com  
91-22-6777 0893

### Head of Research

Sachin Neema  
91-22-6749 1750

### Institutional Sales

Sandeepa Arora  
91-22-6749 1776

Allsec delivered below expected numbers for a second quarter in a row. Revenues and net profit was up just 1.2% and 0.5% respectively on qoq basis. Company continued to face manpower ramp-up issues similar to Q3 FY07 leading to a business execution shortfall. Over the last two quarters, stand alone headcount has decreased by ~573 people ie ~21%. Operating margin was maintained near the previous quarter level. For the full year on consolidated basis, revenue growth stood strong at 35.8% while profit growth was lower at 19.6% bogged down by margin contraction due to B2K losses. Management expects growth resumption from Q1 FY08 with rectification of manpower recruitment issues. Company is targeting ~4,000 people in voice segment by the end of the year.

### Financial highlights

Period	03/07	12/06	Growth	03/06	Growth	03/07	03/06	Growth	03/07*	03/06*	Growth
			(%)		(%)			(%)			(%)
(Rs mn)	(3)	(3)	qoq	(3)	yoy	(12)	(12)	yoy	(12)	(12)	yoy
Sales	276	272	1.2	259	6.3	1,133	923	22.8	1,275	939	35.8
Op Profit	80	80	0.4	73	9.4	325	267	21.8	325	262	24.2
OPM (%)	29.1	29.3	-	28.3	-	28.7	29.0	-	25.5	27.9	-
APAT	70	70	0.5	63	10.7	281	216	30.0	247	207	19.6
NPM (%)	25.4	25.6	-	24.4	-	24.8	23.5	-	19.4	22.0	-
EPS (Rs)											
Annualized	18.4	18.3	-	20.9	-	18.5	17.9	-	16.2	17.1	-
P/E @ Rs280	15.3	-	-	-	-	15.2	-	-	17.2	-	-

\* Consolidated

- ✓ Revenues grew by 1.2% sequentially and 6.3% on yoy basis to Rs276mn. The flattish qoq growth was mainly attributable to inadequacy of required manpower to execute business in the quarter. The problem is a follow-up to manpower recruitment issues faced by the company in Q3 FY07 due to failure of the new recruitment system adopted. In addition, high attrition (quarterly figure) of ~20% in Q3 FY07 and ~17% in Q4 FY07 accentuated manpower availability issues within the company. Consolidated quarter ending headcount stood at 2,491 against 2,502 at the end of Q3 FY07 and ~2,900 at the end of Q2 FY07. Rupee growth in the quarter was also impacted by the sharp Rupee appreciation against the Dollar.
- ✓ For the full year FY07, company recorded 22.8% growth in revenues to Rs1,133mn on stand-alone basis. On consolidated basis (including subsidiary Allsectech Inc and acquired entity B2K), revenues stood at Rs1,275mn representing a growth of 35.8% yoy. B2K contribution to FY07 revenues was ~Rs140mn.
- ✓ The contribution of the Top client, Compu Credit and Top 3 clients stood at 32% and 62% respectively in the quarter, similar to previous quarter levels. Average realizations were stable qoq between 11.5-12\$/hr.
- ✓ There was a significant shift in voice/non-voice revenue mix on sequential basis from 79/21 to 77/23. For the year, it stood at 80/20. In Q4 FY07, company added 5 new clients, 3 in voice segment and 2 in HR processing services.



- √ OPM declined marginally by 20bps to 29.1%. Full year consolidated OPM declined significantly yoy by 240bps to 25.5% as B2K just managed to operationally break-even for the entire year. Stand-alone OPM for the year stood far higher at 28.7%.
- √ Other Income continued to remain higher at Rs10mn in the quarter. At the end of the year, company had C&CE balance of Rs1.1bn comprising Rs723mn in form of liquid investments and balance in bank.
- √ The seat utilization (no of people/no of seats) stood at 1.1x on consolidated basis segregated into 1.3x on stand-alone basis and 0.5x for B2K.
- √ Company is setting up new centres in Trichy, India and Manila, Philippines. The Trichy centre is expected to be operational in the next two months and would have a capacity of 200 seats to start off with. Recruitment for this centre has already started. In Manila, company is still to finalize out of 2-3 locations, the seating capacity of which would be about 500 people. Company expects this centre to start operations before the end of Q2 FY08.
- √ Company has earmarked US\$30mn for acquisitions. New vertical/service expertise, new geography, established client base and good profitability are the key rationale/criteria behind company's inorganic growth strategy. To start off, management is keen on acquiring a company in non-voice space in the US region.
- √ Carlyle's stake in the company stands at ~27.5% with high commitment towards company's growth as reflected in Mr. Daniel A. D'Aniello, co-founder of The Carlyle Group and Mr. Shankar Narayanan, Managing Director - Asia Growth Capital Fund, presence on the company's board. Through Carlyle, company has been introduced to 6 large prospects with potential annual business opportunity of ~US\$5-6mn from each of them. As the typical sales cycle is 9-12 months, company expects to close couple of these accounts by the end of the current year.
- √ With regards Q1 FY08, management expects resumption in sequential growth having added about gross 415 people in first 45 days of the quarter. Also traditionally Q1 and Q2 have been stronger quarters for the company. For FY08, company expects strong growth in topline and bottomline with a target of reaching 4,000 people in voice business by the end of the period. B2K profitability turnaround would enable company in improving or maintaining operating margin on consolidated basis.

**Negligible downside from current levels, Revise to 'BUY'**

On the back of significant underperformance in FY07 (actual EPS at Rs16.2 v/s expected EPS of Rs17), we are revising downwards our FY08 EPS forecast by 12.7% to Rs22.6. However, we are upgrading our view on the stock from 'Hold' to 'Buy' as Allsec has underperformed its peers and the market in the last three months declining by 23.5%. We see negligible downside from current levels but rather a likely upside of 20-30% in the next 6-8 months. We expect strong sequential growth in Q1 and Q2 of FY08.



## Quarterly Trend (Stand-alone)

Period (Rs mn)	Q2 FY05	Q3 FY05	Q4 FY05	Q1 FY06	Q2 FY06	Q3 FY06	Q4 FY06	Q1 FY07	Q2 FY07	Q3 FY07	Q4 FY07
Sales	152	139	161	183	240	241	259	277	308	272	276
% qoq growth	22.3	(8.3)	15.9	13.7	30.9	0.5	7.7	6.6	11.5	(11.7)	1.2
Expenditure	(107)	(103)	(117)	(131)	(170)	(169)	(186)	(200)	(219)	(192)	(195)
Operating profit	45	36	44	53	70	72	74	77	89	80	80
% qoq growth	28.2	(20.9)	22.8	20.1	33.3	2.7	2.2	4.1	16.4	10.3	0.4
OPM (%)	29.7	25.6	27.1	28.7	29.2	29.9	28.3	27.7	28.9	29.3	29.1
Other income	(1)	0	0	0	1	1	9	11	6	11	10
Interest	(4)	(3)	(3)	(2)	(2)	(1)	(0)	(0)	(0)	(1)	(2)
Depreciation	(10)	(11)	(10)	(10)	(18)	(16)	(17)	(20)	(20)	(20)	(19)
PBT	30	21	31	41	51	56	65	67	75	70	69
Tax	0	8	6	(1)	7	(1)	(1)	1	(1)	(0)	1
ETR (%)	-	(38.5)	(18.9)	1.6	(14.4)	1.2	2.0	(1.2)	0.9	0.4	(1.1)
PAT	30	29	37	40	58	56	63	68	74	70	70
% qoq growth	33.7	(3.1)	26.3	8.5	45.4	(4.7)	13.9	7.2	9.2	(6.1)	0.5
NPM (%)	19.9	21.1	23.0	21.9	24.3	23.1	24.4	24.5	24.0	25.6	25.4
Equity	43.5	43.5	88.2	119.6	120.6	120.6	120.8	120.8	152.3	152.3	152.4
EPS (Rs) Annualized	27.8	26.9	16.8	13.4	19.3	18.4	21.0	22.5	19.5	18.3	18.4

## Financials

### Projected Income Statement

Period (Rs mn)	FY04 (12)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
Net sales	251	578	939	1,275	1,714
Operating expenses	(352)	(406)	(677)	(950)	(1,253)
Operating profit	(102)	172	262	325	461
Other income	0	0	15	38	40
PBIDT	(102)	172	276	363	501
Interest	(15)	(14)	(5)	(4)	(8)
Depreciation	(49)	(41)	(68)	(111)	(125)
Def rev exp w/off	(7)	(1)	(0)	0	0
Profit before tax	(173)	115	203	248	368
Tax	3	10	4	(0)	(3)
Profit after tax	(170)	125	207	247	365

### Projected Balance Sheet

Period (Rs mn)	FY04 (12)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
<b>Sources</b>					
Equity Share Capital	177	88	121	152	162
Pref Share Capital	0	0	49	49	49
Share Premium	0	124	461	1,261	1,488
Other reserves	(152)	(23)	117	277	514
Net Worth	25	190	699	1,691	2,164
Loan Funds	115	72	2	0	0
<b>Total</b>	<b>140</b>	<b>262</b>	<b>749</b>	<b>1,740</b>	<b>2,213</b>
<b>Uses</b>					
Gross Block	238	257	599	627	877
Accd Depreciation	(78)	(119)	(209)	(320)	(445)
Net Block	159	138	389	307	432
Capital WIP	0	16	2	0	0
Total Fixed Assets	159	154	391	307	432
Goodwill	0	0	48	48	48
Investments	0	0	0	723	1,000
Total Current Assets	79	151	466	875	1,034
Total Current Liabilities	(104)	(68)	(178)	(235)	(323)
Net Working Capital	(25)	83	288	640	711
Miscellaneous exp	2	10	0	0	0
Def Tax assets	3	15	22	22	22
<b>Total</b>	<b>140</b>	<b>261</b>	<b>749</b>	<b>1,740</b>	<b>2,213</b>

### 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	210	328
Depreciation	49	41	68	111	125
Expenses (deferred)/written off	(2)	(8)	9	0	0
Deferred Tax Asset/liability	(3)	(11)	(8)	0	0
Pre tax cash from operations	(128)	137	258	320	452
Other income/prior period ad	0	0	15	38	40
Net cash before tax	(128)	137	273	358	493
Tax	3	10	4	(0)	(3)
<b>Cash profits</b>	<b>(125)</b>	<b>147</b>	<b>277</b>	<b>358</b>	<b>490</b>
(Inc)/Dec in trade working capital					
-Sundry debtors	(55)	(41)	(110)	(70)	(77)
-Sundry creditors	104	(39)	39	37	48
-Others	0	3	71	21	40
Net trade working capital	49	(77)	(0)	(12)	11
<b>Operating activities</b>	<b>(76)</b>	<b>70</b>	<b>277</b>	<b>347</b>	<b>501</b>
(Add)/Dec in fixed assets					
(Add)/Dec in Goodwill	0	0	(48)	0	0
(Add)/Dec in Investments	0	0	0	(723)	(277)
(Inc)/Dec in Loans/advances	(19)	(8)	(37)	(167)	(52)
<b>Investing activities</b>	<b>(228)</b>	<b>(44)</b>	<b>(390)</b>	<b>(916)</b>	<b>(579)</b>
Inc/(Dec) in debt					
Inc/(Dec) in equity/premium	115	(43)	(71)	(2)	0
Direct add/(red) to reserves-Spl.item	177	35	419	832	237
Dividends	18	16	1	0	0
<b>Financing activities</b>	<b>309</b>	<b>(3)</b>	<b>281</b>	<b>743</b>	<b>108</b>
Cash generated/(utilized)	5	23	168	174	30
Cash at start of the year	0	5	28	196	370
<b>Cash at end of the year</b>	<b>5</b>	<b>28</b>	<b>196</b>	<b>370</b>	<b>400</b>



### Key Ratios

Period	FY04 (15)	FY05 (12)	FY06 (12)	FY07P (12)	FY08P (12)
<b>Per share ratios</b>					
EPS (Rs)	(38.6)	14.2	17.1	16.2	22.6
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	111.0	133.7
<b>Valuation ratios</b>					
P/E (x)	(7.3)	19.7	16.3	17.2	12.4
P/BV (x)	49.7	13.0	4.8	2.5	2.1
M Cap/Sales (x)	4.9	4.3	3.6	3.3	2.6
EV/Sales (x)	5.4	4.4	3.4	2.5	1.8
EV/EBIDTA (x)	(13.2)	14.6	11.5	8.7	6.3
<b>Profitability ratios</b>					
OPM (%)	(40.6)	29.7	27.9	25.5	26.9
PAT (%)	(67.7)	21.7	22.0	19.4	21.3
ROCE (%)	(113.0)	49.4	27.7	14.5	17.0
ROE (%)	(684.2)	66.1	29.6	14.6	16.9
<b>Income Generation ratios</b>					
NFATR (x)	1.6	4.2	2.4	4.2	4.0
TATR (S/CE)	1.8	2.2	1.3	0.7	0.8
ETR (x)	10.1	3.0	1.3	0.8	0.8
<b>ROE De-composition</b>					
NPM	-	21.7	22.0	19.4	21.3
TATR (S/CE)	1.8	2.2	1.3	0.7	0.8
Equity Multiplier	5.6	1.4	1.1	1.0	1.0
Du-Pont ROE	-	66.1	29.6	14.6	16.9
<b>Liquidity ratios</b>					
Current ratio (x)	0.8	2.2	2.6	3.7	3.2
Debtors days	80	60	80	79	75
Creditors days	151	41	40	40	40
Net WC/Sales (%)	(9.9)	14.4	30.6	50.2	41.5
Net WC/TCE (%)	(17.8)	31.8	38.4	36.8	32.1
WC cycle (days)	(71)	20	40	39	35
<b>Leverage ratios</b>					
Debt / Total equity (x)	4.6	0.4	0.0	0.0	0.0
<b>Debt service ratios</b>					
Interest/Sales (%)	6.0	2.4	0.5	0.3	0.5
ICR (x)	(10.1)	9.4	40.8	-	-
<b>Payout ratios</b>					
Dividend payout (%)	0.0	8.3	29.2	30.8	31.0
Tax payout (%)	1.8	(8.5)	(2.1)	0.1	0.7



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**India Infoline Ltd**, 15th Floor, P.J.Tower, Dalal Street, Mumbai -01. Tel 91-22-67491700.

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