

Financial Technologies

Rs1334
OUTPERFORMER

RESULT NOTE

Market Cap: Rs61.2bn; US\$1.3bn

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Result: Q4FY10

Comment: New growth avenues ahead!

Key valuation metrics

Year to March (Rs m)	Net revenues	yoy chg (%)	Adjusted net profit*	EPS* (Rs)	yoy chg (%)	EV/EBITDA (x)	PER * (x)
FY08	1,375.6	39.2	838.3	18.3	(0.2)	118.3	73.0
FY09	3,343.2	143.0	1,729.2	37.7	106.3	32.9	35.4
FY10	3,070.3	(8.2)	1,390.1	30.3	(19.6)	36.7	44.0
FY11E	3,108.2	1.2	1,341.1	29.2	(3.5)	42.7	45.6
FY12E	3,263.0	5.0	1,367.5	29.8	2.0	43.2	44.8

*Standalone financials; *excludes project divestment income*

HIGHLIGHTS OF Q4FY10 RESULTS AND OUR INTERACTION WITH THE MANAGEMENT

- Financial Technologies (FTIL) reported its Q4FY10 results. As booking of exchange solution revenues is varied across quarters, the quarterly financials are not fully comparable with previous years.
- Ahead of estimates, standalone revenues declined by 27% at Rs836m (estimates of Rs735m), EBITDA margins stood at 45.3% or Rs379m (estimates of 39.2% or Rs288m) and net profit declined by 44% at Rs438m (estimates of Rs247m).
- With regards revenues, exchange solutions is estimated to contribute ~Rs500m and trading solutions the remaining Rs334m. This is in contrast to Q4FY09, wherein ~75% of revenues (or Rs850m+) came in from exchange solutions. This explains the yoy decline in reported revenues in Q4FY10. Important to note that FTIL has booked revenues to the tune of Rs700m on account of exchange solutions in Q3FY10.
- Revenue decline coupled with the high operating leverage in the business has resulted in a sharp decline in EBITDA. While overall revenues have declined by 27%, reduction in total operating expenditure has been less than 10% yoy.
- This has resulted in EBITDA margins contracting from 56% in Q4FY09 to 45.3% in Q4FY10.
- During the quarter, FTIL has reported other income of Rs83m against Rs433m in Q4FY09. The decline in other income is on account of the following:
 - Losses on account of forex stood at Rs27m in Q4FY10 against a gain of Rs850m in Q4FY09. This led to a decline of Rs877m in other income.
 - However, part of the decline was netted off on account of expenses to the tune of Rs584m attributable to diminution of assets reported in Q4FY09, which stood at Rs14m in Q4FY10.
- FTIL has booked higher taxes in Q2FY10, hence tax expenses for Q4FY10 has been significantly lower at Rs7m (on a PBT of Rs445m). Thus, reported PAT for the quarter declined by 44%yoy at Rs438m.

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- For FY10, revenues from standalone operations came at Rs3.07bn, EBITDA stood at Rs1.42bn and reported PAT stood at Rs3.44bn (including project divestment income of Rs2.4bn).
- With regards consolidated operations, revenues for FY10 came in at Rs3.4bn, operational losses stood at Rs1.14bn and reported PAT (post minority interest and profits from associates) stood at Rs1.4bn.
- FTIL currently operates five domestic exchanges (MCX, MCX-SX, NSEL, IEX, IBS Forex) and one international exchange (DGCX). With MCX being an associate (ownership of 31.2% stake) and MCX-SX now an investment (subject to approvals), revenues from exchange ventures include the remaining three domestic exchanges and DGCX. For FY10, these exchange ventures reported revenues of Rs121m and an EBIT loss of Rs846m.
- With regards the ecosystem ventures (such as NBHC, Atom, etc) and others, revenues for FY10 stood at Rs1.7bn and the segment reported an operational profit of Rs49m.
- **MCX – Strong operational performance; IPO on cards:** MCX (associate of FTIL – 31.2% stake owned), India's largest commodity exchange garnered an 82% market share in FY10. Total turnover on MCX during the year stood at US\$1.36bn. Further, MCX is estimated to have garnered profits to the tune of Rs2.2bn in FY10. MCX has got the FMC approval for an IPO (subject to certain conditions) and is likely to file for the IPO in the next two months.
- **International exchanges opening up:** FTIL has plans to commence operations of three international exchanges in the next six months. The management has indicated plans to launch Singapore Mercantile Exchange (SMX) in August 2010, Mauritius based Global Board of Trade (GBOT) in September 2010, and Bahrain Financial Exchange (BFX) in October 2010. The performance of these exchanges will directly influence FTIL's core technology business and remains to be the key monitorable.
- As on 31st March 2010, aggregate cash and cash equivalents stands at Rs10.09bn, which includes Rs8bn invested in mutual funds.
- As on 31st March 2010, aggregate investments in group companies stands at Rs9.5bn+

MCX-SX – final verdict awaited!

- Over the last few months, MCX-SX, India's third stock exchange, has been witnessing serious headwinds on the back of its divestment process. While the exchange is less than two years into operations (currently only trades currency derivatives), launch of equity products mandated FT Group to bring down its ownership in MCX-SX to 10% (from the current 70%). The deadline for the same is 30th September, 2010. Further, the cap of 5% to be held by a single investor (with certain exceptions) implied that the FT Group needed to induct 12 investors into the exchange at a consensus valuation.
- FT Group has finally devised a smart way to achieve a break-through in equities, by complying by the required regulatory shareholding while also not trading off a desperate valuation for the exchange. MCX and FTIL, the promoters of MCX-SX, held 38.5% and 31.5% respectively in the exchange and thus in aggregate held 70%. To bring down the promoter holding to 10%, MCX-SX has cancelled 60% of the equity portion of the exchange which was held by the FT Group and in lieu of which they have issued convertible warrants. Thus the equity capital of MCX-SX has been brought down from Rs1.7bn to Rs540m.
- This effectively means that MCX-SX now meets the shareholding guidelines required by the SEBI to launch equities with FTIL and MCX each holding 5%. Further, MCX-SX has retained the ability to discover the fair value of the exchange in due course of operations as the warrants could potentially be sold to external investors at a later date.
- Previous to this, MCX-SX had divested 25% to Indian banks (at a valuation of US\$285m) and 5% to IFCI (at US\$1.2bn). With this development, the stakes owned by these entities have increased. As per the new structure, other than MCX and FTIL which own 5% each, IFCI owns 13.23%, Union Bank of India 11.5%, PNB 9.2%, IL&FS 5% and a group of sixteen banks own 51.1%.
- With shareholding guideline now met, MCX-SX is awaiting final approval from SEBI to launch the equity platform. We see this development as very positive and believe entry into equities could be a game-changer for FTIL.

FTIL has been facing serious headwinds over the last few months on the back of regulatory impediments on the way of launch of equity products on MCX-SX. However, we see things materially changing from hereon with the next six months being event packed for FTIL. With three international exchanges going live (SMX, GBOT and BFX), potential IPO for MCX (last strategic valuation of US\$1.1bn) and equity launch of MCX-SX (assuming regulatory requirements are met by way of current structure or divestment), FTIL is poised to tread a new growth path. We believe performance of international exchanges will be the key monitorable and eventually turn into value drivers for FTIL (currently valued at invested capital). With operational performance of the core technology business and exchanges (leadership across segments with market share of 80%+ in all segment except MCX-SX at 55%) imparting resilience to the business model, we see the advent of newer products/exchanges adding further momentum. With FTIL, the largest exchange conglomerate in Asia and the only listed proxy in the US\$10bn Indian Exchange space, available at US\$1.3bn, we remain bullish. Maintain Outperformer with an SoTP based price target of Rs2,000.

Consolidated segment financials

(Rs m)	FY09	FY10
Segment Revenues		
Technology solutions	3,347.1	3,115.2
yoy growth (%)	148.4	(6.9)
Exchange ventures	180.9	120.9
yoy growth (%)	(81.2)	(33.2)
Ecosystem ventures and others	1,387.0	1,706.9
yoy growth (%)	-	23.1
Total	4,915.0	4,942.9
Less: Inter-segmental revenue	1,567.7	1,544.3
Net Sales	3,347.3	3,398.6
Segment EBIT		
Technology solutions	861.5	349.8
Margin (%)	25.7	11.2
Exchange ventures	(449.4)	(845.5)
Margin (%)	-	-
Ecosystem ventures and others	164.9	49.0
Margin (%)	11.9	2.9

Source: Company, IDFC Securities Research

Quarterly results (standalone financials)

(Rs mn)	Q4FY09	FY09	Q1FY10	Q2FY10	Q3FY10	Q4FY10	FY10*	FY11E	FY12E
Net Sales	1,148.4	3,343.2	584.5	856.3	1,053.2	835.6	3,070.3	3,108.2	3,263.0
yoy growth (%)	192.4	143.0	32.8	(33.5)	53.3	(27.2)	(8.2)	1.2	5.0
EBITDA	642.6	1,646.9	188.3	481.3	630.1	378.6	1,418.3	1,270.4	1,263.9
EBITDA Margins (%)	56.0	49.3	32.2	56.2	59.8	45.3	46.2	40.9	38.7
Net interest	0.8	1.4	0.1	0.1	-	0.0	0.2	-	-
Depreciation	21.9	72.4	13.8	14.2	14.3	16.6	58.9	120.5	74.7
Other Income	432.6	1,007.8	65.0	236.6	70.7	83.3	715.5	851.8	851.8
Profit before Tax	1,052.5	2,580.9	239.5	703.6	686.6	445.3	2,074.7	2,001.7	2,041.0
yoy growth (%)	250.8	106.3	120.7	(16.5)	18.8	(57.7)	(19.6)	(3.5)	2.0
Project divestment income	-	2,067.3	-	2,397.1	-	-	2,397.1	-	-
Tax	267.5	962.2	33.9	918.4	68.9	6.8	1,028.1	660.6	673.5
Profit After Tax	785.1	3,686.0	205.6	2,182.3	617.7	438.4	3,443.8	1,341.1	1,367.5

*For FY10, quarterly revenue and EBITDA does not add up to full year because of regrouping of other income

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