

INFOTECH ENTERPRISES

INR 379

GAP takes 13% stake

BUY



Infotech Enterprises announced that the company will be raising capital of INR 3.0 bn (USD 74 mn) through preferential allotment to General Atlantic Partners (GAP) - a leading global private equity firm, and Carrier International - a wholly owned subsidiary of United Technologies. The eventual dilution on this account is 15% on the expanded capital base.

The main purpose of raising this money is acquisitions. We believe given the strong growth opportunities in the sector, an aggressive approach towards acquisitions by Infotech is warranted and will prove beneficial to investors. We are positive on the management's capability to utilize the money beneficially. We believe the acquisitions for which the money has been raised will be EPS accretive and a good quality acquisition will spread Infotech's wings wider, enabling it to build strong presence in engineering services.

* Dilution details

Capital will be raised through the following securities:

- ◆ Issue of 3.8 mn equity shares of INR 5 each at a price of INR 360 per share as underlying equity shares for the issue of ADRs.
- ◆ Issue of 2.7 mn Compulsorily Convertible Preference Shares (CCPS) of INR 360, each convertible into equal number of equity shares of INR 5 at a premium of INR 355 per share. These shares will bear a coupon rate of 1% and will be converted into shares after 18 months.
- ◆ Issue of 1.8 mn equity shares of INR 5 each at a price of INR 360 per share.

Total shares and holding post issue

- ◆ The total number of additional equity shares issued (incl. conversion of CCPS) would be 8.3 mn, taking the total outstanding shares to 55.3 mn.
- ◆ Post conversion, GAP will own 7.2 mn shares, which is 13% of the total capital of the company. Carrier International will be issued 1.1 mn shares, which will continue to maintain its 14% stake in the company.

Financials

Year to March	FY06	FY07	FY08E	FY09E
Revenues (INR mn)	3,625	5,425	7,388	9,752
Rev. growth (%)	41.0	49.7	36.2	32.0
EBITDA (INR mn)	673	1,134	1,552	2,048
Adjusted net profit (INR mn)	505	836	1,240	1,678
Shares outstanding (mn)	45.7	46.3	52.9	55.4
EPS basic (INR)	11.1	18.1	23.3	30.1
EPS growth (%)	78.6	64.1	28.5	29.2
P/E (x)	34.3	20.9	16.3	12.6
EV/EBITDA (x)	35.2	19.2	10.4	7.2
ROE (%)	27.4	32.5	23.4	20.0

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Parul Inamdar
+91-22-2286 4355
parul.inamdar@edelcap.com

Viju George
+91-22-2286 4400
viju.george@edelcap.com

Kunal Sangoi
+91-22-2286 4309
kunal.sangoi@edelcap.com

Reuters : INFE.BO
Bloomberg : INFCT IN

Market Data

52-week range (INR) : 618 / 180
Share in issue (mn) : 46.1
M cap (INR bn/USD mn) : 17.5 / 429.6
Avg. Daily Vol. BSE/NSE ('000) : 144.0

Share Holding Pattern (%)

Promoters : 28.5
MFs, FIs & Banks : 24.8
FIs : 11.0
Others : 35.7



* **Acquisition – the objective behind dilution**

Infotech's main objective behind the dilution is to utilize the funds for acquisitions. The company has earlier mentioned its intention to deepen its service offerings, especially in the engineering services space. The management has stated that the company has already identified a US-based target company on which it is currently performing due diligence. The deal size is estimated to be in the range of USD 10-12 mn with a revenue target of ~USD 8-10 mn, which values the firm attractively at ~1.2x revenues. The target company is focused on embedded engineering services and the transaction is expected to be announced by mid-July.

The remaining USD 62-64 mn is also planned to be used for the acquisitions. Infotech is looking at acquiring one more company. Our discussion with the management suggests that besides the above mentioned target, it would look at acquiring one more company or even two more companies of a larger size.

* **Impact on estimates**

We don't see any major impact on our net profit and EPS estimates on account of the dilution, as the increase in the other income will offset the dilution impact. Based on the yield of 8%, on INR 3.0 bn for 8 months in FY08 and 12 months in FY09E, the other income further increases by INR 180 mn and 240 mn for FY08 and FY09, respectively.

Table 1: Impact of the dilution on the estimates

(INR mn)	FY08E	FY09E
Earlier net profit	1,119	1,517
Add: Incr. in other inc.	180	240
(8% yeild on INR 3.0 bn)	(9 months)	(12 months)
Less: Inc. in tax	59	79
Revised net profit	1,240	1,678
Less: Pref. div	7	8
(1% coupon rate)	(8 months)	(10 months)
Adjusted net profit	1,233	1,669
New shares o/s (incl. ESOP dilution)	52.9	55.4
New EPS (INR)	23.3	30.3
Old EPS (INR)	23.7	31.6
Change in EPS (%)	(1.5)	(4.3)

Source: Edelweiss research

* **Valuations**

We expect Infotech, to grow its revenue and net profit at a CAGR of 34.1% and 41.6% over FY07-09E, respectively. At INR 379, the stock trades at a P/E of 16.3x and 12.6x and EV/EBITDA of 10.4x and 7.2x on our revised FY08E and FY09E earnings, respectively. We see the stock returns tracking the earnings growth rate going forward and continue to maintain our 'BUY' recommendation.

Company Description

Infotech Enterprises (Infotech) is a 5,100 plus employee software services company with competencies in: (a) GIS services catering to utility, transportation, and government segments, (b) engineering design services for engineering, manufacturing, and industrial products verticals, and (c) software services to clients in data and technology services, engineering design, and IT services. The company has grown its revenues and net profits at a CAGR of 45.3% and 74.8%, respectively, over FY05-07. The company's past twelve months revenues stood at INR 5.4 bn (USD 120.3 mn).

Investment Theme

Outsourcing of engineering services is expected to reach USD 38-50 bn by 2020E compared with USD 2 bn currently, as per a Nasscom, Booz Allen Hamilton study. As one of the leading offshore engineering services firm for the manufacturing industry, Infotech is poised to grab the increasing opportunities. The company has strong domain knowledge and complete solution capabilities in the GIS segment along with a healthy pipeline of deals. The company's skills in the areas of mapping and designing across diverse segments, and in a variety of end-user IT environments give it an edge over peers. We expect Infotech's revenues and net profits to grow at a CAGR of 42.7% and 50.8%, respectively, over FY06-08E.

Key Risks

- ◆ Inadequate availability of skilled manpower.
- ◆ Slowdown in engineering spend
- ◆ Significant appreciation of rupee against the USD, Euro, and GBP.

Financial Statements

Income statement

Year to March	FY05	FY06	FY07	FY08E	FY09E
Revenues	2,571	3,625	5,425	7,388	9,752
Total employee cost	1,224	1,696	2,589	3,499	4,661
Travel and conveyance	231	328	482	645	800
Purchase for resale	285	459	617	872	1,170
Gen & admin expenses	359	469	604	820	1,073
Operating expenditure	2,099	2,952	4,292	5,836	7,704
EBITDA	473	673	1,134	1,552	2,048
Depreciation	167	186	256	300	410
EBIT	305	487	878	1,252	1,638
Other exp	3	-	-	-	-
Net interest	3	11	14	13	15
Total other income	40	21	67	244	320
Profit before tax	339	498	930	1,483	1,943
Tax	90	93	187	325	445
Net profit	249	404	744	1,158	1,498
Share of profit in associate	25	101	93	82	180
Adjusted net profit	274	505	836	1,240	1,678
EPS basic (INR)	6.2	11.1	18.1	23.3	30.1
Dividend (%)	15.0	22.5	30.0	40.0	50.0
Dividend pay out (%)	8.1	6.8	9.3	10.0	9.7

Common size metrics - as % of revenues

Year to March	FY05	FY06	FY07	FY08E	FY09E
Employee cost	47.6	46.8	47.7	47.4	47.8
EBITDA margin	18.4	18.6	20.9	21.0	21.0
EBIT margin	11.9	13.4	16.2	16.9	16.8
Net profit margin	9.7	11.2	13.7	15.7	15.4
Adj. net profit margin	10.6	13.9	15.4	16.8	17.2

Growth metrics (%)

Year to March	FY05	FY06	FY07	FY08E	FY09E
Revenues	37.2	41.0	49.7	36.2	32.0
EBITDA	61.9	42.4	68.4	36.9	32.0
PBT	191.7	46.7	86.9	59.4	31.0
Net profit	176.5	62.3	83.9	55.7	29.3
Adjusted net profit	203.8	84.5	65.6	48.3	35.3

Balance sheet		(INR mn)				
Year to March	FY05	FY06	FY07E	FY08E	FY09E	
Sources of funds						
Equity share capital	147	152	230	265	277	
Share premium account	463	558	606	4,011	4,153	
Reserves	954	1,413	2,179	3,289	4,796	
Borrowings	14	65	250	215	210	
Deferred tax liability	(13)	(8)	(16)	(16)	(16)	
Total sources of funds	1,565	2,180	3,250	7,763	9,421	
Application of funds						
Gross fixed assets	1,324	1,811	2,391	3,092	3,692	
Depreciation	(860)	(1,014)	(1,270)	(1,570)	(1,980)	
Net fixed assets	463	798	1,122	1,522	1,712	
Capital WIP	141	11	81	50	-	
Investments	100	178	330	450	-	
Cash & cash equivalents	340	385	675	4,395	6,019	
Debtors	872	1,223	1,605	2,065	2,565	
Loans & advances	112	265	170	213	266	
Inventories	2	1	15	25	25	
Total current assets	1,326	1,874	2,465	6,697	8,874	
Sundry creditors & other liabilities	(358)	(525)	(510)	(663)	(809)	
Provisions	(108)	(156)	(237)	(294)	(357)	
Total current liabilities	(465)	(680)	(747)	(957)	(1,166)	
Working capital	861	1,194	1,718	5,741	7,708	
Total application of funds	1,565	2,180	3,250	7,763	9,421	

Cash flow statement		(INR mn)				
Year to March	FY05	FY06	FY07E	FY08E	FY09E	
Cash flow from operations	412	492	1,014	1,471	1,923	
Cash for working capital	(143)	(180)	(273)	(348)	(383)	
Net operating cash flow (A)	269	311	740	1,123	1,540	
Net purchase of fixed assets	(274)	(338)	(650)	(670)	(550)	
Net purchase of investments	(15)	(63)	(152)	(120)	450	
Others	4	4	93	82	180	
Cash flow from investments(B)	(285)	(396)	(709)	(708)	80	
Dividends	(20)	(26)	(39)	(84)	(132)	
Proceeds from issue of equity	11	100	126	3,439	155	
Proceeds from LTB/STB	(12)	51	185	(35)	(5)	
Interest paid & other items	(3)	(9)	(14)	(13)	(15)	
Cash flow from financing (C)	(23)	116	258	3,307	3	
Exchange rate differences (D)	4	3	-	-	-	
Change in cash(A-B+C) + (D)	(35)	34	290	3,722	1,623	

Ratios

Year to March	FY05	FY06	FY07E	FY08E	FY09E
ROE (%)	19.1	27.4	32.5	23.4	20.0
ROCE (%)	18.9	27.3	31.1	22.6	19.6
Debtor days	123.8	123.1	108.0	102.0	96.0
Fixed asset T/O	5.3	5.7	5.7	5.6	6.0

Valuations

Year to March	FY05	FY06	FY07E	FY08E	FY09E
EPS (INR)	6.2	11.1	18.1	23.3	30.1
BVPS (INR)	35.4	46.5	65.5	142.3	165.8
P/E (x)	61.3	34.3	20.9	16.3	12.6
Pr/CF (x)	40.0	25.5	16.1	11.5	8.4
P/BV (x)	11.3	8.3	5.8	2.3	1.9
EV/EBITDA (x)	56.4	35.2	19.2	10.4	7.2
EV/Revenues (x)	6.7	4.8	3.2	1.8	1.2

Edelweiss Securities

14th Floor, Express Towers,
Nariman Point, Mumbai – 400 021
Board: (91-22) 2286 4400
Email: research@edelcap.com



Naresh Kothari – 2286 4246

Head, Institutional Equities

Vikas Khemani – 2286 4206

Head, Institutional Equities

INDIA RESEARCH	SECTOR	INSTITUTIONAL SALES
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Harish Sharma - 2286 4307	Infrastructure, Auto Components, Mid Caps	Balakumar V - (044) 4263 8283
Priyanko Panja - 2286 4300	Infrastructure, Engineering, Telecom	Ashish Agrawal - 2286 4301
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		Nirmal Ajmera - 2286 4258
		Ankit Doshi - 2286 4671
		Dipesh Shah - 2286 4434

Email addresses: firstname.lastname@edelcap.com

e.g. naresh.kothari@edelcap.com

unless otherwise specified

RATING INTERPRETATION

Buy	Expected to appreciate more than 20% over a 12-month period	Reduce	Expected to depreciate up to 10% over a 12-month period
Accumulate	Expected to appreciate up to 20% over a 12-month period	Sell	Expected to depreciate more than 10% over a 12-month period
Trading Buy	Expected to appreciate more than 10% over a 45-day period	Trading Sell	Expected to depreciate more than 10% over a 45-day period

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