

Persistent Systems

BUY
Volatile market condition impacts dollar growth
CMP: Rs324
Target Price: Rs410

Persistent reported 6.4% qoq revenue growth in Q2FY12 to Rs2,832mn, in line with expectation. Earnings grew 17.6% qoq, ahead of expected 3.2% qoq, driven by EBITDA margin expansion of 110bps qoq, despite impact of wage hike and total employee growth. Dollar revenue was weaker with 3.1% growth qoq to US\$51.5mn (v/s expected 4.4% qoq growth).

FY12 revenue guidance of US\$220mn at risk: Management is maintaining revenue guidance for FY12 at US\$220mn due to strong deal pipeline despite volatile market, and believes if one of the large deals close quickly H2FY12 may see strong growth over H1FY12. We estimate FY12 dollar revenue to be at US\$211 and believe the company may miss its full year guidance of US\$220 as H1FY12 US\$101.5mn revenue implies revenue growth of 16.7% in H2FY12 over H1FY12, which looks stretched under current conditions.

Increased market volatility impacts deal closure rate: Persistent management indicated that though technology spend remains robust at present and deal pipeline is witnessing lot of activity (better than previous quarters), heightened volatility in market is delaying closure of large deals.

Sales and marketing cost may remain volatile for a few quarters: The company is carrying out sales team re-alignment to (1) take advantage of Persistent's alliances, and (2) bring sales pitch in line with focus areas of cloud, analytics, collaboration, and mobility. Persistent maintains these steps may lead to volatility in sales cost (as % of total sales) over next 1-2 quarters.

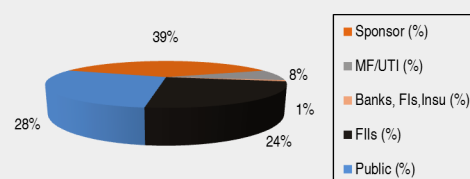
Revise estimates upwards: We revise FY12/FY13 earnings estimates upwards by 21.2% and 18.3% respectively, driven by strong earnings growth in Q2FY12, SGnA cost rationalisation, and favourable currency tailwind. We have rebased revenue estimates on Rs/US\$ rate of 48.98 leading to upwards revision in revenue estimate by 1.8% for FY12 and 7.6% for FY13.

Outlook and valuation: The stock trades at P/E of 8.9x FY12E and 7.9x FY13E earnings. Maintain Buy with target price of Rs410 (10x target P/E multiple on FY13 earnings, earlier price target Rs450) based on (1) traction in strength areas of cloud enablement, mobility, analytics and collaboration, (2) ability to protect margin despite wage hike pressure, and (3) better deal pipeline than previous quarters. We have reduced target multiple to 10x from 11x earlier (in line with de-rating of other IT stocks in our coverage universe), due to weak market sentiment and positive earnings revision driven by currency effect.

KEY DATA

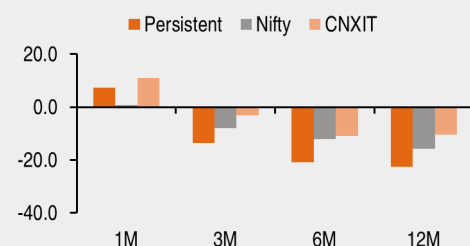
Bloomberg	PSYS IN
Reuters	PERS.BO
52-wk H/L (Rs)	465/281
6-m avg trd value	US\$0.2mn
Market cap	Rs12.9bn/US\$0.3bn
Shares o/s	40mn
Face value	Rs10

Source: Bloomberg

SHAREHOLDING (%)


Source: CMIE

As of 30 September 2011

RELATIVE PRICE PERFORMANCE


Source: Bloomberg

Key financials

(Rs mn)

Y/E Mar	FY12E	FY13E	FY14E
Sales	9,908	11,716	13,267
EBITDA	2,171	2,659	2,794
EBITDA %	21.9	22.7	21.1
Net profit	1,456	1,651	1,688
FDEPS (Rs)	36.4	41.3	42.2
EPS growth (%)	4.3	13.4	2.3
P/E (x)	8.9	7.9	7.7
RoE (%)	16.0	15.0	13.4

Source: Company, BRICS Research

Sushil Sharma

+91 22 66360073

sushil.sharma@bricssecurities.com

Rahul Dholam

+91 22 66360029

rahul.dholam@bricssecurities.com

September 2011 quarter performance							(Rs mn)	
Particulars	Sep 11 actual	Sep 11 estimate	Difference %	Sep 10	yoy %	Jun 11	qoq %	
Sales	2,382	2,389	-0.3	1,870	27.4	2,238	6.4	
EBITDA	454	412	10.1	430	5.4	401	13.1	
EBITDA %	19.0	17.2		23.0		17.9		
Depreciation	140	117	19.7	101	38.6	126	10.3	
Other income	137	105	30.2	59	131.0	126	9.1	
PBT	451	401	12.6	389	16.0	400	12.7	
Tax	127	116	9.3	31		125		
PAT	324	284	13.9	358	(9.5)	276	17.6	

Source: Company, BRICS Research

Financial summary

Income statement					Balance sheet				
(Rs mn)					(Rs mn)				
Y/E 31 March	2011	2012E	2013E	2014E	Y/E 31 March	2011	2012E	2013E	2014E
Revenue	7,758	9,908	11,716	13,267	Net fixed assets	2,866	4,238	4,909	5,127
Revenue growth (%)	29.1	27.7	18.2	13.2	Investments	2,500	2,872	3,259	3,646
Operating exp	6,175	7,738	9,057	10,473	Current assets	3,677	3,997	5,241	6,288
EBITDA	1,583	2,171	2,659	2,794	Inventories	—	—	—	—
EBITDA margin (%)	20.4	21.9	22.7	21.1	Sundry debtors	1,582	1,784	2,033	2,221
Depreciation	424	549	640	722	Cash & bank balance	1,000	1,050	1,841	2,631
EBIT	1,159	1,622	2,019	2,072	Loans & advances	869	931	1,101	1,194
MTM profit / (loss)	—	—	—	—	Other current assets	226	232	266	241
Other income	344	436	339	340	Total assets	9,103	11,107	13,410	15,061
Interest paid	—	—	—	—	Net worth	7,071	8,715	10,602	12,242
PBT	1,504	2,058	2,358	2,412	Share capital	400	400	400	400
Tax	108	601	707	724	Reserves & surplus	6,671	8,315	10,202	11,842
PAT	1,396	1,456	1,651	1,688	Minority interest	—	—	—	—
Minority interest	—	—	—	—	Total debt	—	—	—	—
EO income	—	—	—	—	Secured loans	—	—	—	—
APAT	1,396	1,456	1,651	1,688	Unsecured loans	—	—	—	—
PAT growth (%)	21.3	4.3	13.4	2.3	Current liabilities & prov	1,602	1,993	2,408	2,419
Shares o/s (mn)	40	40	40	40	Current liabilities	1,206	1,496	1,827	1,747
Fully diluted o/s shrs (mn)	40	40	40	40	Provisions	396	496	581	672
FDEPS (Rs) recurring	34.9	36.4	41.3	42.2	Net deferred tax liab	—	—	—	—
					Total liabilities	9,103	11,108	13,410	15,061

Cash flow statement					Key ratios				
(Rs mn)									
Y/E 31 March	2011	2012E	2013E	2014E	Y/E 31 March	2011	2012E	2013E	2014E
PBT	1,504	2,058	2,358	2,412	Valuation ratios				
Depreciation	424	549	640	722	PE (x)	9.3	8.9	7.8	7.7
Amortisation	—	—	—	—	CEPS (Rs)	45.5	50.1	57.3	60.3
Interest paid	—	—	—	—	PCE (x)	—	—	—	—
Tax paid	(342)	(601)	(707)	(724)	BVPS (Rs)	177	83	265	306
Chg in working capital	48	121	(38)	(245)	Price/Book (x)	1.8	1.5	1.2	1.1
Int/div in other income	(142)	(71)	(80)	(92)	EV/EBITDA (x)	7.5	5.5	4.2	3.7
Other operations	84	88	83	87	EV/Revenue (x)	1.5	1.2	0.9	0.8
CF from operations (a)	1,575	2,143	2,254	2,160	Dividend yield (%)	1.2	0.7	0.9	0.9
Capital expenditure	(970)	(1,681)	(1,024)	(939)	Cash flow yield (%)	(7.4)	1.2	7.1	7.2
Chg in investments	(1,684)	(372)	(387)	(387)	Performance ratios				
Other investing act	(18)	—	—	—	Raw material to sales (%)	66.0	59.9	58.9	59.7
Int/div in other income	142	71	80	92	SGA to sales (%)	13.6	18.2	18.4	19.3
CF from investments (b)	(2,530)	(1,982)	(1,331)	(1,234)	Effective tax rate (%)	7.2	29.2	30.0	30.0
Free cash flow (a+b)	(954)	161	924	926	PAT margin (%)	18.0	14.7	14.1	12.7
Equity raised/(repaid)	(45)	—	—	—	DPS (Rs)	4.0	2.4	2.8	2.9
Debt raised/(repaid)	(15)	—	—	—	Dividend payout ratio (%)	11	7	7	7
Interest paid	—	—	—	—	Return ratios				
Dividend (incl tax)	(280)	(111)	(133)	(135)	RoE avg (%)	21.4	18.4	17.1	14.8
Other fin activities	(372)	—	—	—	RoCE avg (%)	16.6	19.5	20.1	17.5
CF from financing (c)	(712)	(111)	(133)	(135)	Fixed asset turnover (x)	3.0	2.8	2.6	2.6
Net chg in cash (a+b+c)	(1,667)	50	791	790	Working capital ratios				
Opening balance	1,896	230	279	1,070	Inventory (days)	—	—	—	—
Closing balance	230	279	1,070	1,860	Payable (days)	119	107	112	92
					Receivable (days)	74	66	63	61
					Working capital (days)	(45)	(41)	(49)	(31)
					Leverage ratios				
					Interest cost (%)	—	—	—	—
					Net debt/equity (x)	(0.1)	(0.1)	(0.2)	(0.2)
					Interest coverage (x)	—	—	—	—

BRICS RECOMMENDATION SCALE

BUY:	More than 15% upside
ADD:	Upside up to 15% (between 0% and 15%)
REDUCE:	Downside up to 15% (between 0% and –15%)
SELL:	More than 15% downside

Head Office: Sadhana House, 1st Floor, 570, P. B. Marg, Behind Mahindra Tower,
Worli, Mumbai - 400 018. Tel: (91-22) 6636 0000

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