

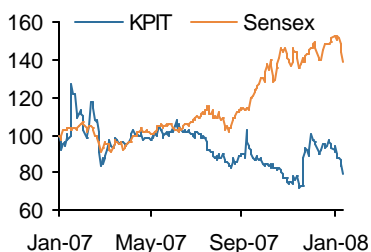
# KPIT Cummins Infosystems Ltd (Q3 FY08)

**January 21, 2008**
**Stock data**

Sensex:	19,014
CMP (Rs):	107
Target price (Rs):	-
Upside (%):	-
52 Week h/l (Rs):	181/97
Market cap (Rs cr)	1,498
6m Avg vol BSE&NSE ('000 nos):	392
No of o/s shares (mn):	76
FV (Rs):	2
Bloomberg code:	KPIT IN
Reuters code:	KPIT.BO
BSE code:	532400
NSE code	KPIT

**Shareholding pattern**

<b>September 2007</b>	<b>(%)</b>
Promoters	25.0
FIs	9.0
Indian institutions	18.0
Public & others	48.0

**Share price trend**

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- ⤴ Dollar revenue growth of 4.3% qoq was below expectations; hit by sharp decline in onsite pricing.
- ⤴ Strong growth witnessed in niche offerings of ATS and GBS and amongst non-Cummins star customers especially outside Top 10.
- ⤴ EBITDA margin and net profit were flat qoq further deteriorating the performance.
- ⤴ Despite a dull Q3 FY08, company maintains annual FY08 profit guidance – which we feel would be extremely difficult to achieve.
- ⤴ The actual non-achievement of guidance could be a further dampener on the stock price and would seriously impact management credibility - maintain negative stance.

**Result table**

Period	Q2 FY08	Q3 FY08	QoQ	YoY
(Rs mn)	(3)	(3)	(%)	(%)
Net sales	1,492	1,512	1.3	29.1
Total Expenditure	(1,258)	(1,274)	1.3	28.4
EBIDTA	235	238	1.3	33.0
EBITDA margin (%)	15.7	15.7	-	-
Depreciation	(57)	(59)	2.7	93.6
Interest	(19)	(20)	4.9	110.4
Other income	0	4	-	-
PBT	159	163	2.6	16.8
Tax	(18)	(22)	20.9	825.7
PAT	141	142	0.2	2.9
Number of shares (Mn)	152.6	152.6	-	-
EPS (Rs) - Quarterly	1.9	1.9	0.2	2.9

Source: Company, India Infoline Research

**Dollar revenue growth below expectations; hit by sharp decline in onsite pricing**

In dollar terms, revenue grew by 4.3% qoq made-up of 5.9% volume growth and 1.5% reduction in blended pricing. The growth was solely driven by a strong 10.1% qoq increase in offshore revenues comprising 7.1% volume growth and 2.8% billing rate improvement. Onsite revenues declined by 1.9% qoq with flat volume growth and a sharp 2.7% reduction in billing rates. As a result onsite:offshore revenue mix shifted significantly towards the latter by 290 bps qoq to 54.6%. In rupee terms, the revenue growth was far more disappointing at 1.3% qoq, impacted by 2.9% decline in rupee rate realized - Rs40.74 v/s Rs41.95 in Q2 FY08.

**Strong growth in non-Cummins star customers especially outside Top 10**

Non-Cummins star customer witnessed a robust growth of 8.8% qoq. However, growth seemed to be driven by smaller star customers as revenues from the Top 10 clients were flat qoq. Revenues from Cummins de-grew by 1.6% qoq after recording strong growth in the last three quarters. There was an addition of two customers in the star customer category.

**Growth continues to be driven by niche offerings of ATS and GBS**

The revenue share of Advanced Technology Solutions (ATS) increased by a substantial 330 bps qoq to 33.4% as its components - auto electronics and semiconductor - grew by 18.7% and 8.8% respectively on qoq basis. Global business solutions offerings (BPO + KPO arm) also registered a robust growth of 35.6% qoq. Revenues from the US geography were flattish, primarily impacted by higher holidays.

**EBITDA margin and net profit was flat qoq**

EBITDA margin remained flat at 15.7% qoq as the benefit of substantial offshore shift was offset by the appreciation of rupee and lower onsite pricing and utilization. Net profit was also flat qoq as company made higher tax provisions, which offset higher other income.

**Company maintains FY08 guidance – which we feel would be extremely difficult to achieve especially after a dull Q3 FY08**

Management re-assured that the company can still achieve the lower end of annual profit guidance (Rs630-680mn implying 25-35% yoy growth) given that it has negotiated 12-15% higher rates on some existing contracts which will be effective from January 1<sup>st</sup> 2008. On a blended basis, company expects a 4% qoq billing rate improvement in Q4 FY08.

On the contrary, we feel that it would be extremely difficult for the company to achieve the guidance which calls for a 56% qoq jump in bottomline in Q4 FY08. Achievement of the guidance means at least 12% billing rate improvement over existing for 35-40% of revenues and the benefits of the same following through the EBITDA line and expanding the margin by 350-400 bps in the last quarter.

**Maintain negative stance on the company**

Our view of KPIT having a serious threat of not achieving its annual profit guidance in the visit note dated December 2007 gets more credence in the light of a poor show by the company in Q3 FY08. Though our call has had an impact with market price correcting by 16% to Rs107 since then, we still maintain our negative stance as the actual non-achievement (will be known in 3 months) could be a further dampener on the stock price and could seriously impact management credibility.

**Projected financials**

y/e Mar (Rs mn)	FY06	FY07	FY08E	FY09E	FY10E
Revenues	3,182	4,637	6,020	7,711	9,570
yoy growth (%)	26.0	45.7	29.8	28.1	24.1
EBITDA	462	708	995	1,306	1,520
EBITDA margin (%)	14.5	15.3	16.5	16.9	15.9
Pre-exceptional PAT	326	505	607	819	823
yoy growth (%)	14.7	55.0	20.2	34.9	0.6
EPS (Rs)	22.4	6.8	8.0	10.7	10.8
P/E (x)	4.8	15.9	13.4	10.0	9.9
P/BV (x)	1.1	4.0	3.2	2.5	2.0
EV/EBITDA (x)	4.4	12.1	8.8	6.9	6.1
ROE (%)	23.0	25.4	23.9	25.1	20.7
ROCE (%)	16.4	18.6	20.4	22.6	22.3

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