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Parul Inamdar
91-22-6632 2243

Senior Research Analyst
ParulInamdar@PLIndia.com

In Focus

Prithvi Information Solutions

BUY

Rs 391

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Q2 FY07 Result Update – Robust performance

Prithvi Information Solutions has posted a very strong performance in Q2 FY07: robust revenue growth of 21.5% qoq (and 68.2% yoy), coupled with 320-bp qoq improvement in the EBITDA margin, led to a 20.1% qoq (and 85.6% yoy) growth in net profit, to Rs 222m. For FY07 the company increased its revenue guidance by 5% to Rs 6,000m (on the back of a healthy \$170-m order book and a \$120-m pipeline) and its net profit guidance by 2.6% to Rs 795m (implying 32.5% and 47.1% yoy growths respectively).

The company plans to recruit 700-800 people in FY07 (it has already added 356). Its 2,200-seat development centre in Hyderabad has been slightly delayed and should be completed by Jul.'07. This would serve as an offshore facility.

It is finalising plans for an overseas acquisition, for which it is considering raising about \$50m to \$70m through an FCCB issue.

Key Figures

Y/e March	FY05	FY06	FY07E	FY08E
Net Sales (Rs m)	3,052	4,527	6,000	8,100
PAT (Rs m)	289	541	850	1,336
EPS (Rs)	16.0	29.9	47.0	73.9
CEPS (Rs)	16.2	30.9	50.4	78.4
PER (x)	24.5	13.1	8.3	5.3
EV / EBIT (x)	17.5	12.6	7.1	4.6
EV / Sales (x)	1.7	1.5	1.1	0.8
RoE (%)	32.8	26.3	24.7	30.4
RoCE (%)	3.3	26.7	23.8	27.1

Vertical contribution to revenue

Prithvi's revenue arises from various verticals, 'Technology' contributing the most (40.9%). Manufacturing, Healthcare, Telecoms, Retail and BFSI contribute 13.2%, 11.2%, 16.2%, 9.8% and 6.7% respectively to revenue.

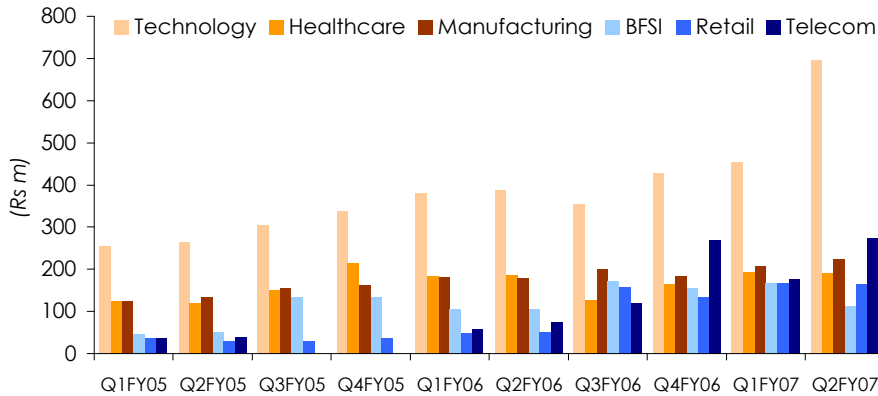
Having segmented its services into high-end and more profitable services such as Business Intelligence (BI), Networking Solutions (NS) and Knowledge-Process Outsourcing (KPO) and having gained excellent traction in them, we expect Prithvi to attain a 38.4% CAGR in revenue, accompanied by a more robust 66.6% CAGR in net profit during the period FY05 to FY08.

(Stock price as on November 1, 2006)



We believe that Prithvi’s rising offshore commitments are leading to, and would continue to lead to, expanded margins. Its offshore revenue mix in Q2 FY07 has further risen to 12.5% (11% in the previous quarter) and is much higher than the 4% of a year ago.

Vertical Contribution



Source: Company Data, PL Research

Increasing offshore revenue mix leading to better margins

In Q1 FY07, the company successfully transitioned the work of some of its top-10 clients to offshore. Further, of the 11 clients added in the quarter, four have been added offshore, and the transitioning of two more clients later in the year is a possibility. Also, the company has been increasing its revenue contribution from offshore (from 4% in a year ago to 12.5%), which has also boosted its profit margins, (gross profit margin from 21.2% a year ago to 27.6%).

Increasing offshore employee base will prove fruitful

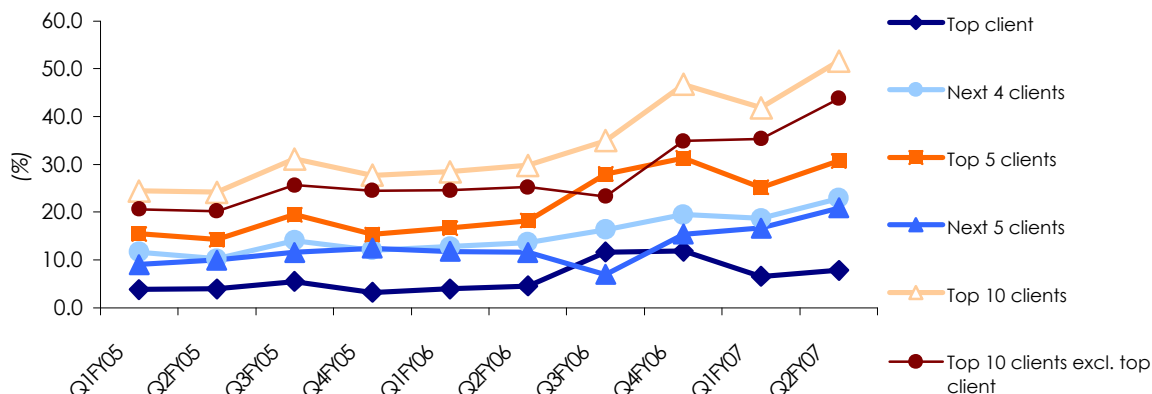
After two quarters, the company has added a larger number of people on-site (203) than offshore (58). Our discussions with the management clearly indicate that this has been largely due to the kick-off of certain new projects. Also, one must not ignore the fact that, in the past nine quarters, while the number of employees offshore has had a robust 23.1% CQGR, that onsite has grown by a mere 7.1%. Overall, the company added 261 employees in the quarter, taking the total to 1,552.

Good client traction continues

In Q3 and Q4 FY06, contribution from Prithvi’s top client increased substantially, from 4% in FY05. In Q1 FY07, we saw this normalizing to 4.7%; again in Q2, the contribution stands at 4.6%. This quarter saw a good 20%-plus growth in all its client categories – top-client, top-five and top-10 clients.



Movement in top-client accounts



Source: Company Data, PL Research

Conclusion

At the CMP of Rs 391, the stock trades at 8.3x FY07 estimates and 5.3x those of FY08. These seem undervalued from a 12-month perspective. We re-iterate our **BUY** rating, with a target price of Rs 525 (11.2x FY07 and 7.1x FY08 estimates).

Q2 FY07 Results Overview

(Rs m)

Y/e March	Q2 FY07	Q1 FY07	QoQ Gr. (%)	Q2 FY06	H1 FY07	H1 FY06	YoY Gr. (%)	FY06	FY07E	YoY Gr. (%)
Net Sales	1,699	1,398	21.5	1,010	3,097	1,992	55.4	4,527	6,000	32.5
Total Expenses	1,444	1,233	17.0	897	2,677	1,771	51.1	4,002	5,100	27.4
Software Development	1,230	983	25.1	796	2,212	1,561	41.7	3,389	4,260	25.7
Selling & Marketing	96	78	23.4	-	174	-	-	121	340	180.1
Others	118	173	(31.7)	101	291	210	38.2	492	500	1.6
Operating Profits / EBITDA	255	165	54.9	113	420	221	90.0	525	900	71.5
Depreciation	15.0	11.7	-	1.0	26.7	1.9	-	17.3	60.0	-
EBIT	240	153	57.0	112	393	219	79.5	508	840	65.5
Interest	14.3	6.6	-	2.9	20.9	5.5	-	14.1	50.0	-
EBT before Other Income	226	146	54.3	109	372	214	74.3	493	790	60.1
Other Income	(3)	40	-	11	37	8	-	50	65	31.2
PBT	223	186	19.5	120	409	222	84.3	543	855	57.4
Tax	1	2	(52.9)	-	3	-	-	2	5	106.6
<i>Tax Rate (%)</i>	<i>0.4</i>	<i>0.9</i>	<i>-</i>	<i>-</i>	<i>0.6</i>	<i>-</i>	<i>-</i>	<i>0.4</i>	<i>0.6</i>	<i>-</i>
PAT	222	185	20.1	120	407	222	83.2	541	850	57.2
Key Ratios										
<i>GPM (%)</i>	<i>27.6</i>	<i>29.7</i>	<i>(2.1)</i>	<i>21.2</i>	<i>28.6</i>	<i>21.7</i>	<i>6.9</i>	<i>25.1</i>	<i>29.0</i>	<i>3.9</i>
<i>OPM (%)</i>	<i>15.0</i>	<i>11.8</i>	<i>3.2</i>	<i>11.2</i>	<i>13.6</i>	<i>11.1</i>	<i>2.5</i>	<i>11.6</i>	<i>15.0</i>	<i>3.4</i>
<i>EBITM (%)</i>	<i>14.1</i>	<i>10.9</i>	<i>3.2</i>	<i>11.1</i>	<i>12.7</i>	<i>11.0</i>	<i>1.7</i>	<i>11.2</i>	<i>14.0</i>	<i>2.8</i>
<i>NPM (%)</i>	<i>13.1</i>	<i>13.2</i>	<i>(0.1)</i>	<i>11.8</i>	<i>13.1</i>	<i>11.1</i>	<i>2.0</i>	<i>11.9</i>	<i>14.2</i>	<i>2.2</i>
Adjusted EPS (Rs)	12.3	10.2	20.1	6.6	22.5	12.3	83.2	29.9	47.0	57.2



Notes

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