

# ROLTA INDIA



Revenue momentum picks up with better profitability

## ■ Performance in line with expectations; uptick seen across segments

Rolta's Q1 results clearly indicate the improving traction across its three business segments. The engineering segment has seen stability with marginal revenue growth after two successive quarters of decline, while the GIS segment continued to deliver profitable growth. The GIS division posted top line growth of 7.2% Q-o-Q and EBITDA margin expansion of 280bps to 46.8%. Company level operating profit margin improved 200bps to 35.6% Q-o-Q driven by cost rationalisation and better utilisation. Rolta's order accretion remained healthy with INR 4 bn worth of new orders, taking the company's total order book to INR 16.6 bn (up 3% Q-o-Q). However, despite better profitability during the quarter (vis-à-vis our expectation) higher depreciation and tax rate dragged down the net profit in line with our expectation.

## ■ GIS business segment drives performance

The company, with its unique solutions, has created a strong niche in the GIS market. With leadership in the Indian defence geospatial market and high exposure to the government its GIS business has more than offset the impact of slowdown in the engineering segment. Further, as its Fusion solution has gone live, profitability of the segment has increased to 47% at the EBITDA level during the quarter. We expect this business segment to grow ahead of the company's growth rate.

## ■ Equity raising could be in the offing

Rolta has passed an enabling resolution to raise funds up to USD 250 mn through instruments like ADRs/GDRs/FCCBs/QIPs/Warrants or private placements of any other form of securities convertible into equity shares. Though the company has indicated that it has no plans currently to raise equity, we understand it could be particularly targeted to deleverage the balance sheet (current net debt of ~INR 8 bn, i.e., USD 172 mn). Though an option, the company is not pursuing any acquisitions actively currently. In case of full USD 250 mn being raised, equity will be diluted by 28%.

## ■ Outlook and valuations: Growth momentum returning; maintain 'BUY'

Past two quarters have seen sharp increase in Rolta's order intake, the impact of which in terms of better growth rates will be seen in the P/L during forthcoming quarters. We maintain our estimate of revenue growth of 12% and EPS estimate of INR 16 for FY10. At CMP of INR 187, the stock is trading at P/E of 11.7x FY10E and 9.7x FY11E earnings. We maintain **'BUY'** recommendation. On relative return basis, the stock is rated **'Sector Outperformer'** (refer rating page for details).

### Financials

Year to June	Q110	Q409	Growth %	Q109	Growth %	FY09	FY10E
Revenue (INR mn)	3,505	3,327	5.3	3,461	1.3	13,728	15,339
Gross profit (INR mn)	1,659	1,584	4.7	1,552	6.9	6,274	7,225
EBITDA (INR mn)	1,255	1,125	11.6	1,185	5.9	4,685	5,307
Net profit (INR mn)	484	947	(48.9)	136	256.2	2,814	2,585
Diluted EPS (INR)	3.0	5.9	(49.1)	0.8	259.2	17.5	16.0
Diluted P/E (x)						10.7	11.7
EV/EBITDA (x)						6.9	6.0
EV/Revenues (x)						2.4	2.1

October 22, 2009

Reuters : ROLT.BO      Bloomberg : RLTA IN

### EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperformer
Risk Rating Relative to Sector	High
Sector Relative to Market	Equalweight

Note:  
Please refer last page of the report for rating explanation

### MARKET DATA

CMP	:	INR 187
52-week range (INR)	:	206 / 40
Share in issue (mn)	:	161.0
M cap (INR bn/USD mn)	:	30.1 / 643.3
Avg. Daily Vol. BSE ('000)	:	8,113.6

### SHARE HOLDING PATTERN (%)

Promoters*	:	42.0
MFs, FIs & Banks	:	3.4
FIIIs	:	29.2
Others	:	25.4
* Promoters pledged shares (% of share in issue)	:	2.5

### RELATIVE PERFORMANCE (%)

	Sensex	Stock	Stock over Sensex
1 month	2.0	4.8	2.8
3 months	14.3	38.0	23.6
12 months	61.2	10.2	(51.1)

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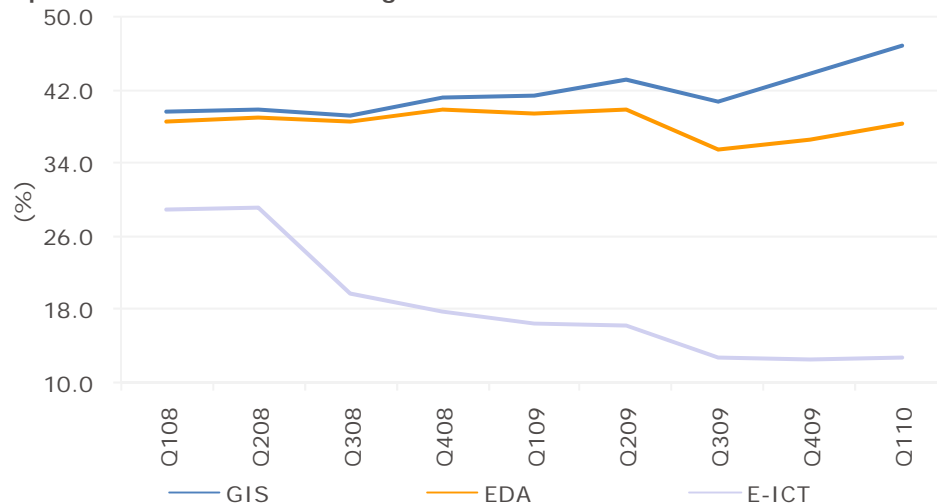
## ■ Key highlights

- Consolidated revenues, at INR 3.5 bn, were up 5.3% Q-o-Q and 1.3% Y-o-Y. Gross profits for the quarter stood at INR 1.7 bn, a sequential improvement of 4.7%. Gross margins were down marginally 30bps on account of higher material cost for the quarter.
- EBITDA stood at INR 1.25 mn, up an impressive 11.6% Q-o-Q and 5.9% Y-o-Y. EBITDA margins showed sharp improvement of 200bps Q-o-Q at 35.8%, due to cost rationalisation, lower SG&A spend, and higher utilisation.
- Net profits, at INR 484 mn, were down 49.1% Q-o-Q (on account of higher other income due to FCCB buyback gains in previous quarter), while up 259.2% Y-o-Y. Net profit margins stood at 13.8% largely in line with our estimates.
- **Guidance:** Rolta is maintaining its guidance for FY10 revenues in the range of INR 15.3 bn–15.7 bn and EBITDA margins in the 33-35% range. This implies revenue growth of 11-14% over FY09.

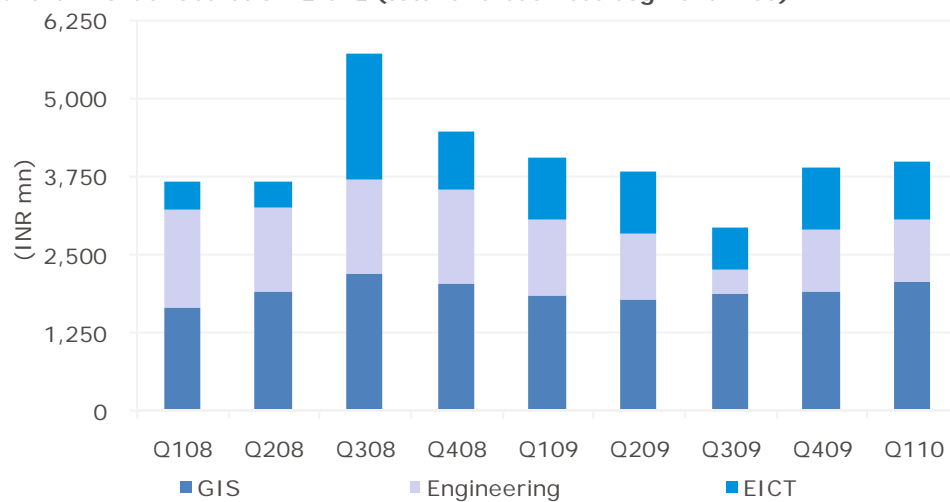
## • Segmental performance

- **GIS:** Consolidated revenues, at INR 1,709.9 mn, were up 7.2% Q-o-Q and 14.8% Y-o-Y. EBITDA margin increased sequentially over 280bps and now stands at 46.8%. Rolta has increased operating margins (~600bps) in the past two quarters. The company maintains good traction in the GIS segment which has posted yet another quarter of sequential growth in its order book by 4.6%; this was 13th successive quarter where GIS order book has reported sequential growth. On a reported basis, realisation rose 3.2% Q-o-Q as utilization improved.
- **Engineering design:** Rolta reported consolidated revenues of INR 882.4 mn, up 2.4% Q-o-Q and down 16.8% Y-o-Y. This was first quarter of growth on the back of two successive quarters of decline in revenues. EBITDA margin stood at 38.3%, an improvement of 170bps from the previous quarter. Engineering segment's performance is improving as revenue base has stabilised and order book has increased 2.5% sequentially. However, pricing was down 1.5% Q-o-Q.
- **Enterprise information and communication technology (EICT):** The EICT segment's revenue at INR 912.5 mn grew 4.8% in the quarter. EBITDA margin, at 12.8%, was marginally up 15bps from the previous quarter. Order book position and pricing were flat from the previous quarter.
- **Reduction in headcount for third successive quarter:** The company went in for stringent cost cutting to maintain margins by bringing down its headcount by 800 (by not replacing natural attrition) over the past three quarters. In fact, in Q2FY10 there was net reduction of ~225 employees which has brought down total employee cost by 3.3% sequentially (37.1% of revenues). Most of the reduction was again in the EDA segment with a decline of 175 employees.
- **Order book uptick continued:** Rolta's order book grew 3.1% sequentially. Current order book stands at INR 16.6 bn.
- Capex for the quarter was INR 900 mn; target capex for FY10 is INR 3.0 bn, of which INR 1.5-1.8 bn is attributed to the upcoming facility in Gurgaon.
- The company had INR 2.0 bn in cash and cash equivalents and debt of ~INR 10 bn, inclusive of FCCB debt at the end of the quarter, so net debt is around INR 8.0 bn.
- **DSOs decline:** Debtor days for the company dipped to 133 days (guidance of 135 days in Q4FY09) from 154 days in the previous quarter. Management is confident of bringing down DSO further to below 120 days by FY10 end.

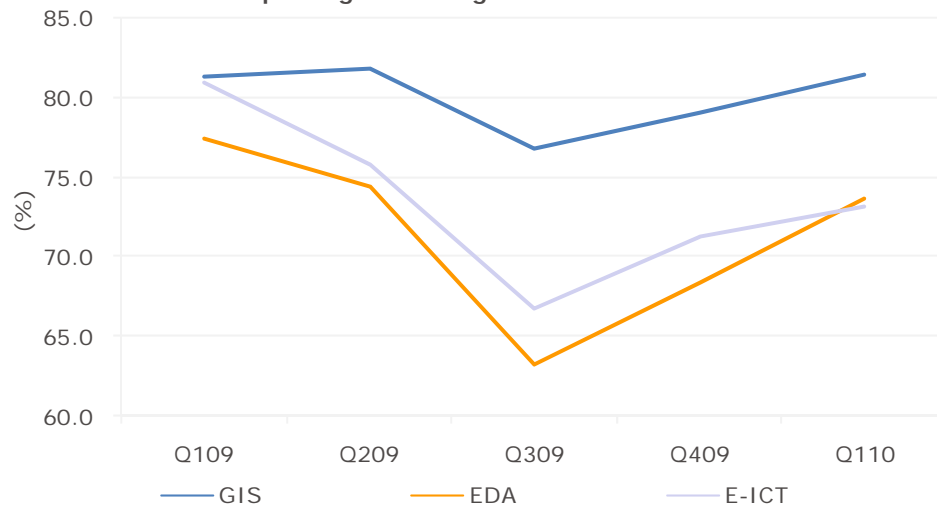
**Chart 1: Improving utilisation and cost rationalisation have driven margin improvement in GIS and EDA segment**



**Chart 2: Order accretion Q-o-Q (total and business segment wise)**



**Chart 3: Utilisation improving across segments**



Source: Company, Edelweiss research

## Financials snapshot

(INR mn)

Year to June	Q110	Q409	Growth %	Q109	Growth %	FY09	FY10E	FY11E
Total revenues	3,505	3,327	5.3	3,461	1.3	13,728	15,339	17,542
Cost of revenues	1,846	1,743	5.9	1,910	(3.4)	7,455	8,114	9,315
Gross profit	1,659	1,584	4.7	1,552	6.9	6,274	7,225	8,227
SG&A	405	460	(12.0)	367	10.3	1,588	1,917	2,052
EBITDA	1,255	1,125	11.6	1,185	5.9	4,685	5,307	6,175
Depreciation	621	578	7.5	379	64.0	1,867	2,120	2,240
EBIT	634	547	15.9	806	(21.4)	2,818	3,187	3,935
Interest expense*	160	134	19.8	103		512	571	587
Other income	99	626	(84.2)	(464)	(121.4)	903	380	300
PBT	573	1,040	(44.9)	239	139.4	3,208	2,996	3,648
Tax	90	94	(4.0)	105	(14.1)	402	419	547
Adjusted net profit	482	945	(49.0)	134	259.6	2,807	2,577	3,101
Minority interest	(2)	(2)	-	(2)	-	(7)	(8)	0
Reported net profit*	484	947	(48.9)	136	256.2	2,814	2,585	3,101
EPS fully diluted (INR)	3.0	5.9	(49.1)	0.8	259.2	17.5	16.0	19.2

## as % of net revenues

Gross profit	47.3	47.6		44.8		45.7	47.1	46.9
SG&A	11.5	13.8		10.6		11.6	12.5	11.7
EBITDA	35.8	33.8		34.2		34.1	34.6	35.2
Adjusted net profit	13.8	28.4		3.9		20.4	16.8	17.7
Reported net profit	13.8	28.5		3.9		20.5	16.8	17.7
Tax rate	15.8	9.0		43.9		12.5	14.0	15.0

\* Accrued interest on FCCB taken in interest expenses and thus commensurate gain of FCCB buy-back also reversed in profit and loss account

### ■ Company Description

Rolta is one of the leading providers of GIS and engineering design and automation (EDA) services. In GIS, Rolta provides and develops digital map-based solutions, servicing customers in segments like defence, environmental protection, utilities, emergency services, and public planning. In EDA, Rolta focuses on computer-aided plant design and mechanical engineering solutions. The company provides a combination of software skills and component manufacturing services through its EDA group. It also provides security and IT infrastructure, software development, testing, and gaming services through its EICT group. The company's past twelve months (TTM) revenues stood at INR 13.8 bn (USD 294 mn) and it employs over 4,750 people.

### ■ Investment Theme

Outsourcing of engineering services is expected to reach USD 38-50 bn by 2020 against USD 2 bn currently, as per the Nasscom-Booz Allen Hamilton study. As one of the leading offshore engineering services firms for the manufacturing industry, Rolta is poised to grab the increasing opportunities. Nevertheless, in the current environment, as capex spending has eased, Rolta has seen uptick in new orders. Moreover, with increased emphasis and spending plans on upgrading defence technologies, opportunity for Rolta is significant. In addition, visibility for JVs with Shaw Group and Thales Group is also looking up. We see Rolta placed in a strong position to explore the high opportunity segments of GIS and engineering along with its focus on transitioning towards solutions approach.

### ■ Key Risks

Key risks to our investment theme include: (a) substantial proportion of revenues from non-annuity sources; (b) non pick-up of growth in other verticals of the EDA segment; and (c) inability to monetize the Fusion solutions could impact profitability.

## Financial Statements

<b>Income statement</b>		<b>(INR mn)</b>				
Year to June	FY07	FY08	FY09	FY10E	FY11E	
Revenues	7,112	10,722	13,728	15,339	17,542	
Cost of revenues	3,618	5,761	7,455	8,114	9,315	
Gross profit	3,494	4,961	6,274	7,225	8,227	
Total SG&A expenses	628	1,064	1,588	1,917	2,052	
EBITDA	2,866	3,897	4,685	5,307	6,175	
Depreciation & Amortization	1,018	1,383	1,867	2,120	2,240	
EBIT	1,848	2,515	2,818	3,187	3,935	
Interest expense	7	-	512	571	587	
Other income	103	170	952	380	300	
Profit before tax	1,943	2,685	3,258	2,996	3,648	
Tax	214	388	402	419	547	
Core profit	1,729	2,297	2,856	2,577	3,101	
Profit after tax	1,729	2,297	2,856	2,577	3,101	
Net profit after extra ord. & minority interest	1,729	2,306	2,814	2,585	3,101	
Shares outstanding (mn)	159	161	161	161	161	
EPS (INR) basic	10.9	14.2	17.5	16.0	19.2	
Diluted shares (mn)	160	163	161	161	161	
EPS (INR) diluted	10.8	14.1	17.5	16.0	19.2	
CEPS (INR)	17.3	23.0	29.6	29.1	33.2	
Dividend per share	5.0	3.1	4.0	4.5	5.0	
Dividend (%)	50.0	30.9	40.0	45.0	50.0	
Dividend pay out (%)	27.2	25.3	26.8	32.8	30.4	

### Common size metrics - as % of revenues

Year to June	FY07	FY08	FY09	FY10E	FY11E
Cost of revenues	50.9	53.7	54.3	52.9	53.1
Gross margin	49.1	46.3	45.7	47.1	46.9
SG&A expenses	8.8	9.9	11.6	12.5	11.7
EBITDA margin	40.3	36.3	34.1	34.6	35.2
EBIT margin	26.0	23.5	20.5	20.8	22.4
Net profit margins	24.3	21.4	20.8	16.8	17.7

### Growth metrics (%)

Year to June	FY07	FY08	FY09	FY10E	FY11E
Revenues	33.0	50.8	28.0	11.7	14.4
EBITDA	28.6	36.0	20.2	13.3	16.3
EBIT	24.7	36.1	12.1	13.1	23.5
PBT	36.8	38.2	21.3	(8.0)	21.8
Net profit	35.8	32.8	24.3	(9.8)	20.3
EPS	15.1	30.1	24.2	(8.2)	20.0

<b>Balance sheet</b>					
	(INR mn)				
As on 30th June	FY07	FY08	FY09E	FY10E	FY11E
Equity share capital	801	1,609	1,610	1,610	1,610
Share premium account	4,092	2,822	2,821	2,821	2,821
Reserves	5,573	7,411	9,471	11,208	13,366
Total shareholders funds	10,466	11,841	13,902	15,638	17,797
Borrowings	6,177	6,938	9,675	10,221	10,808
Minority interest	0	15	8	0	0
Deferred tax liability	346	459	520	750	850
<b>Sources of funds</b>	<b>16,989</b>	<b>19,253</b>	<b>24,105</b>	<b>26,610</b>	<b>29,455</b>
Goodwill and other intangible asset	60	2,000	2,000	2,000	2,000
Gross fixed assets	8,283	10,583	14,835	18,170	20,537
Less: Accumulated depreciation	3,619	4,090	5,958	8,078	10,318
Net fixed assets	4,664	6,493	8,878	10,093	10,220
Capital WIP	1,463	1,729	1,500	1,150	1,200
Investments	976	2,816	3,000	3,200	4,500
Deferred tax asset	0	63	63	63	63
Cash & bank balances	6,390	2,598	4,553	5,460	6,385
Debtors	3,770	5,018	5,642	5,967	6,584
Inventories	206	215	268	349	453
Loans and advances	885	1,160	1,567	1,958	2,350
Total current assets	11,251	8,991	12,029	13,734	15,773
Sundry creditors	758	1,998	2,398	2,518	3,021
Provisions	668	841	968	1,113	1,280
Total current liabilities	1,426	2,840	3,365	3,630	4,301
Working capital	9,825	6,152	8,664	10,104	11,472
<b>Application of funds</b>	<b>16,989</b>	<b>19,253</b>	<b>24,105</b>	<b>26,610</b>	<b>29,455</b>
Book value per share (BV) (INR)	65.7	73.7	86.3	97.1	110.5
<b>Free cash flow</b>					
Year to June	FY07	FY08	FY09E	FY10E	FY11E
Net profit	1,729	2,306	2,814	2,585	3,101
Depreciation	1,018	1,383	1,867	2,120	2,240
Others	(14)	84	(336)	413	387
Gross cash flow	2,734	3,772	4,345	5,118	5,728
Less: Changes in working capital	404	180	558	533	443
Operating cash flow	2,330	3,592	3,787	4,585	5,285
Less: Capex	2,648	3,444	4,023	2,985	2,417
<b>Free cash flow</b>	<b>(318)</b>	<b>148</b>	<b>(236)</b>	<b>1,600</b>	<b>2,868</b>
<b>Cash flow statement</b>					
Year to June	FY07	FY08	FY09E	FY10E	FY11E
Cash flow from operations	2,951	4,910	4,871	5,383	6,398
Cash for working capital	(404)	(180)	(558)	(533)	(443)
Operating cashflow (A)	2,330	3,592	3,787	4,585	5,285
Net purchase of fixed assets	(2,648)	(3,444)	(4,023)	(2,985)	(2,417)
Net purchase of investments	165	(1,815)	(184)	(200)	(1,300)
Others	51	(1,633)	903	380	300
Investments cashflow (B)	(2,433)	(6,891)	(3,304)	(2,805)	(3,417)
Dividends	0	0	(753)	(848)	(942)
Proceeds from issue of equity	6,001	49	0	0	0
Proceeds from LTB/STB	(396)	(540)	2,225	(25)	0
Financing cash flow (C)	5,605	(492)	1,472	(873)	(942)
<b>Change in cash (A+B+C) + (D)</b>	<b>5,502</b>	<b>(3,791)</b>	<b>1,955</b>	<b>907</b>	<b>926</b>

**Ratios**

Year to June	FY07	FY08	FY09E	FY10E	FY11E
ROAE (%)	17.4	20.7	22.5	17.4	18.5
ROACE (%)	15.0	15.5	15.0	14.3	16.3
Debtors (days)	180	150	142	138	131
Payable (days)	33	47	58	58	58
Cash conversion cycle	147	103	83	80	73
Current ratio	7.9	3.2	3.6	3.8	3.7
Debt/EBITDA	2.2	1.8	2.1	1.9	1.8
Interest cover (x)	251	NA	6	6	7
Fixed assets turnover (x)	1.7	1.9	1.8	1.6	1.7
Total asset turnover(x)	0.5	0.6	0.6	0.6	0.6
Equity turnover(x)	0.7	1.0	1.1	1.0	1.0
Debt/Equity (x)	0.6	0.6	0.7	0.7	0.6
Adjusted debt/Equity	0.6	0.6	0.7	0.7	0.6

**Valuation parameters**

Year to June	FY07	FY08	FY09E	FY10E	FY11E
Diluted EPS (INR)	10.8	14.1	17.5	16.0	19.2
<i>Y-o-Y growth (%)</i>	<i>15.1</i>	<i>30.1</i>	<i>24.2</i>	<i>(8.2)</i>	<i>20.0</i>
CEPS (INR)	17.3	23.0	29.6	29.1	33.2
Diluted PE (x)	17.3	13.3	10.7	11.7	9.7
Price/BV(x)	2.8	2.5	2.2	1.9	1.7
EV/Revenues (x)	4.0	2.9	2.4	2.1	1.7
EV/EBITDA (x)	10.0	8.1	6.9	6.0	4.9
EV/EBITDA (x)+1 yr forward	7.3	6.7	6.1	5.1	
Dividend yield (%)	2.7	1.7	2.1	2.4	2.7





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Ideas create, values protect

Company	Absolute reco	Relative reco	Relative risk
Infotech Enterprises	Buy	SO	H
Rolta India	Buy	SO	H
Tata Consultancy Services	Buy	SO	L
Mphasis	Hold	SU	M
Wipro	Buy	SP	L
Infosys Technologies	Hold	SU	L
Patni Computer Systems	Hold	SU	M
HCL Technologies	Hold	SO	H

## ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

## RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

## RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

## SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

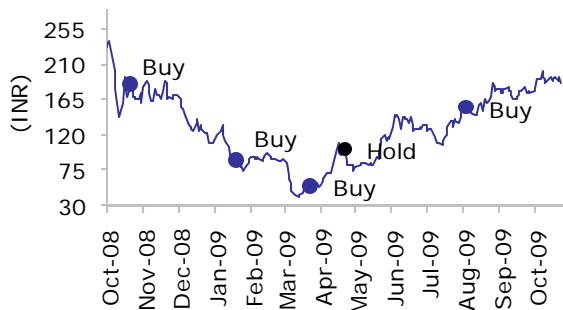
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### Coverage group(s) of stocks by primary analyst(s): Information Technology

HCL Tech, Infosys, Infotech, Mphasis, Patni, Rolta, TCS, and Wipro

#### Rolta



#### Recent Research

Date	Company	Title	Price (INR)	Recos
22-Oct-09	TCS	Uptick in momentum to sustain; <i>Result Update</i>	628	Buy
16-Oct-09	TCS	Firing on all cylinders again; <i>Result Update</i>	598	Buy
14-Oct-09	Infotech Enterprises	Stability proven, but growth awaited; <i>Result Update</i>	245	Buy
09-Oct-09	Infosys Technologies	A mixed quarter sending no signals of a swift, Decisive upturn; <i>Result Update</i>	2,178	Hold

#### Distribution of Ratings / Market Cap

##### Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	70	53	16	142

\* 3 stocks under review

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	89	38	15

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