

# ROLTA INDIA



*Creditable margin and order intake, but immediate re-rating unlikely*

## Revenue and net profit in line with expectations

Rolta India's (Rolta) Q1FY11 revenues and net profits were in line with our expectations while EBITDA margins were ahead of expectations. Revenue, at INR 4.3 bn, grew 3.8% Q-o-Q and net profit, at INR 679 mn, jumped 8.8% Q-o-Q. EBITDA margins, at 39.7% (80bps improvement over previous quarter), were credible given that salary hikes were effected during the quarter (10% offshore and 2-5% onsite). Increasing proportion of high margin solutions revenue and reducing employee base were key margin boosters.

## Charting out key positive and negatives

**Positives:** (a) Key notable for the quarter was the free cash generation that stood positive for the first time after many quarters (FCF of INR 300 mn for the quarter); (b) new order intake of INR 5.2 bn has been the highest ever for Rolta. Total order book as at quarter end stood at INR 18.8 bn (up 5.5% Q-o-Q and 13% Y-o-Y). New order booking was strongest in the GIS segment that continues to see wider acceptance of its Geospatial Fusion solution; (c) book-to-bill ratio improved significantly (see table 1 below) across all three business segments; (d) increase in IP-based revenues to ~16% of total from ~10% in the previous quarter.

**Negatives:** (a) Growth in engineering segment was flat (up 0.7% Q-o-Q) and is expected to remain so for rest of the quarter of the fiscal (growth of 8-10% in FY11 over FY10); (b) margins in the EICT segment continue to remain at 12% indicating limited success in terms of shifting work offshore from TUSC (company acquired in Jan '08); (c) debtor days continue to be high at 144; (d) though the cash flow generation has been positive, we believe FCF generation has to increase significantly for it to repay the FCCB proceeds by FY12 end, which otherwise may result in capital raising by diluting the existing equity (enabling resolution to raise up to USD 150 mn passed by the board).

## Outlook and valuations: Immediate re-rating unlikely; maintain 'BUY'

Rolta has maintained its guidance of 12-15% revenue growth and over 15% net profit growth for FY11. We see valuations at 9.8x FY11E and 8.6x FY12E undemanding. However, the 15% growth is unlikely to enthuse investors and hence immediate re-rating is unlikely. We have a 'BUY' recommendation on the stock. On relative basis the stock is rated 'Sector Performer'.

October 25, 2010

Reuters: ROLT.BO Bloomberg: RLTA IN

### EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Performer
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 169
52-week range (INR)	:	210 / 148
Share in issue (mn)	:	161.2
M cap (INR bn/USD mn)	:	27 / 613
Avg. Daily Vol. BSE/NSE ('000):	:	1,694.6

### SHARE HOLDING PATTERN (%)

Promoters*	:	41.9
MFs, FIs & Banks	:	2.6
FIIIs	:	31.9
Others	:	23.6
* Promoters pledged shares (% of share in issue)	:	2.5

### PRICE PERFORMANCE (%)

	Stock	Nifty EW Technology Index
1 month	(4.9)	1.3
3 months	(6.6)	11.5
12 months	(10.3)	21.6

## Financials

(INR mn)

Year to June	Q1FY11	Q4FY10	% Chg	Q1FY10	% Chg	FY10	FY11E
Net revenues	4,276	4,121	3.8	3,505	22.0	15,327	17,744
EBITDA	1,697	1,601	6.0	1,255	35.3	5,770	7,005
Reported net profit	679	624	8.8	484	40.3	2,403	2,795
Diluted EPS (INR)	4.2	3.8	8.9	3.0	39.5	14.8	17.2
Diluted P/E (x)						11.4	9.8
EV/EBITDA (x)						6.7	5.3
EV/Revenues (x)						2.5	2.1

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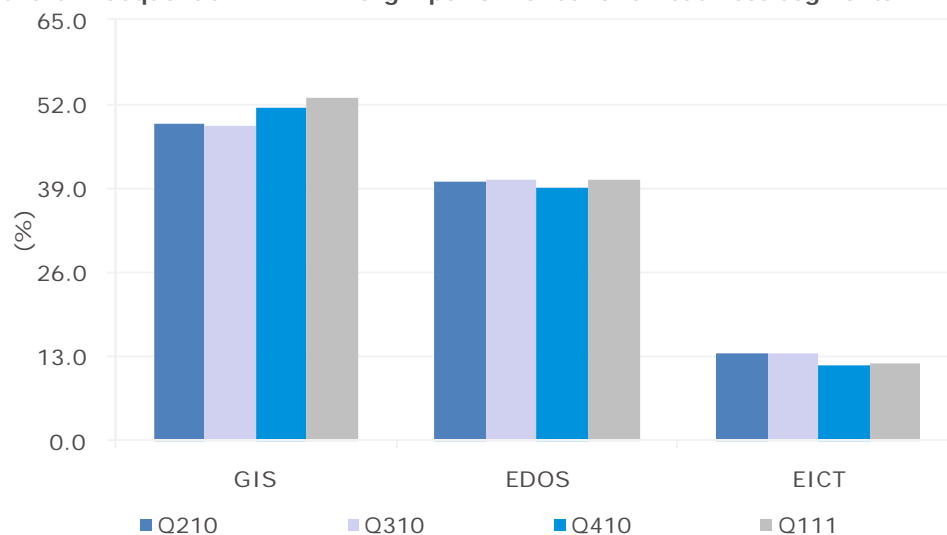
### Key highlights

- Consolidated revenues, at INR 4.3 bn, jumped 3.8% Q-o-Q and 22.0% Y-o-Y. Gross profit for the quarter stood at INR 2.2 bn, a sequential growth of 4.7%. Gross margins improved marginally by 50bps on account of higher IP-based revenue and improved realisations.
- Margin uptrend continues:** EBITDA stood at INR 1.7 bn, up 6.0% Q-o-Q and 35.3% Y-o-Y. EBITDA margins improved 80bps Q-o-Q at 39.7% in spite of a 7% overall wage hike. Increase in gross margins and lower SG&A spend resulted in this improvement. Rolta has done well in improving margins by 600bps over the past six quarters to 39.7%.
- Net profit, at INR 679 mn, was up 8.8% sequentially and 40.3% Y-o-Y on account of higher EBITDA margin and other income. Net profit margin, at 15.9%, was up 80bps Q-o-Q. Tax rate decreased during the quarter to 14.5% (15.5 % previous quarter).

### Segmental performance

- GIS:** Consolidated revenues, at INR 2.2 bn, rose 3.7% Q-o-Q and 26.0% Y-o-Y. EBITDA margin increased sequentially by 140ps and now stands at 52.9%, highest in the company's history, on account of increasing solution sales and pricing despite utilisation declining 70bps, now at 78.4%. Rolta has increased operating margins by 440bps in the past three quarters. It is witnessing strong traction in this segment for its Geospatial Fusion solution. The company's order book grew 8.1% sequentially. On reported basis, realisation posted an uptick of 3.1% Q-o-Q.
- Engineering design:** Rolta reported consolidated revenue of INR 1.1 bn, up by a meager 0.7% Q-o-Q and 22.6% Y-o-Y. EBITDA margin stood at 40.2%, an improvement of 130bps over the previous quarter.
- Enterprise information and communication technology (EICT):** The EICT segment's revenue, at INR 1,040.4 mn, grew 7.4% in the quarter. EBITDA margin, at 11.9%, was marginally up by 20bps from the previous quarter. Order book position increased 4.2% (highest in past 10 quarters) from the previous quarter.

Chart 1: Sequential EBITDA margin performance for all business segments



Source: Company, Edelweiss research

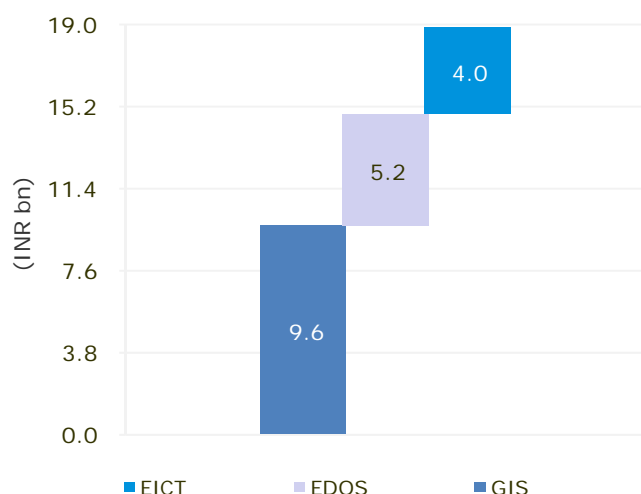
- **Headcount addition declines for second consecutive quarter:** The headcount reduced by 55 during the quarter; this was on the back of net reduction of 103 employees in previous quarter. Total employee count now stands at 4,651. As the solution proportion increases going forward, revenues will de-link with manpower growth, thus headcount addition should not be looked upon as a lead indicator unlike tier I players where hiring guidance has been revised upwards and strong net addition reported in the quarter.
- **Order book uptick continued:** Rolta's order book grew 5.5% sequentially (highest in the past nine quarters). Current order book stands at INR 18.8 bn.

**Table 1: Book-to-bill trend across all three business segments has shown a marked improvement**

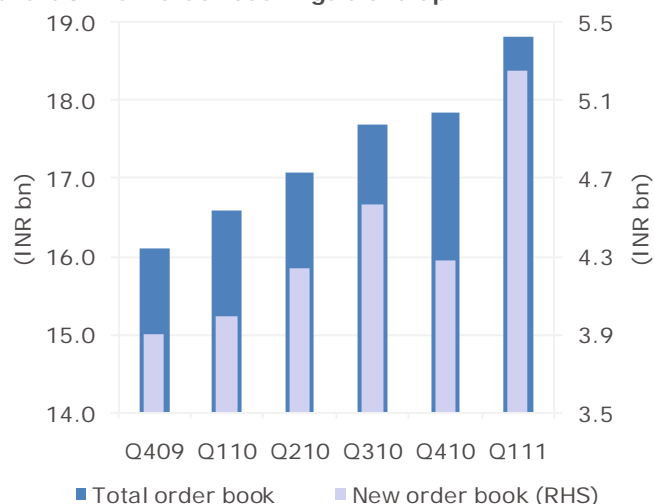
Book-to-bill ratio	Q109	Q209	Q309	Q409	Q110	Q210	Q310	Q410	Q111
GIS	1.2	1.2	1.2	1.2	1.2	1.1	1.2	1.1	1.3
EDOS	1.2	0.9	0.4	1.1	1.1	1.4	1.1	0.9	1.1
EICT	1.1	1.0	0.8	1.2	1.0	0.9	1.1	1.1	1.2
<b>Total</b>	<b>0.9</b>	<b>0.9</b>	<b>0.7</b>	<b>1.3</b>	<b>1.0</b>	<b>1.1</b>	<b>1.1</b>	<b>0.9</b>	<b>1.2</b>

Source: Company, Edelweiss research

**Chart 2: Order book break-up segment wise**



**Chart 3: New order bookings trend up**



Source: Company, Edelweiss research

- The company had INR 1 bn in cash and cash equivalents and debt of INR 12.3 bn. The net cash flow from operations stood at INR 1.05 bn and FCF of INR 300 mn for the quarter.
- **DSOs decline:** Debtor days stand at 144 days vis-à-vis 148 in the previous quarter.
- The company's board also passed an enabling resolution to raise up to USD 150 mn through GDR/ ADR/ FCCB/ QIP, among other options.

## Financial snapshot

(INR mn)

Year to June	Q1FY11	Q4FY10	% Change	Q1FY10	% Change	FY10	FY11E	FY12E
Net revenues	4,276	4,121	3.8	3,505	22.0	15,327	17,744	20,522
Cost of revenue	2,087	2,030	2.8	1,846	13.1	7,914	8,649	10,158
Gross profit	2,189	2,091	4.7	1,659	31.9	7,413	9,095	10,363
SG&A	492	490	0.4	405	21.5	1,643	2,090	2,545
EBITDA	1,697	1,601	6.0	1,255	35.3	5,770	7,005	7,819
Depreciation	763	716	6.7	621	22.9	2,679	3,174	3,480
EBIT	934	885	5.5	634	47.3	3,091	3,831	4,339
Other income	55	40	36.7	99	(44.3)	409	205	200
Interest*	194	187	3.5	160	21.0	697	752	724
Profit before tax	795	738	7.7	573	38.8	2,803	3,284	3,815
Tax	115	114	0.7	90	27.4	406	488	649
Core profit	680	624	8.9	482	41.0	2,398	2,796	3,167
Minority interest	1	-	-	(2)	(141.0)	(5)	-	-
Reported net profit	679	624	8.8	484	40.3	2,403	2,795	3,167
Diluted EPS (INR)	4.2	3.8	8.9	3.0	39.5	14.8	17.2	19.5

## As % of net revenues

Gross profit	51.2	50.7		47.3		48.4	51.3	50.5
SG&A	11.5	11.9		11.5		10.7	11.8	12.4
EBITDA	39.7	38.9		35.8		37.6	39.5	38.1
Adjusted net profit	15.9	15.1		13.8		15.6	15.8	15.4
Reported net profit	15.9	15.1		13.8		15.7	15.8	15.4
Tax rate	14.5	15.5		15.8		14.5	14.9	17.0

\* 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 (EDOS) 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 EDOS, 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 16.1 bn (USD 348 mn) and it employs over 4,651 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) slow down of in GIS segment; (c) inability to monetize the Fusion solutions could impact profitability; and (d) inadequate free cash generation to repay the FCCB and ECB debt.

## Financial Statements

### Income statement

(INR mn)

Year to June	FY08	FY09	FY10	FY11E	FY12E
Net revenue	10,722	13,728	15,327	17,744	20,522
Cost of revenues	5,761	7,455	7,914	8,649	10,158
Gross profit	4,961	6,274	7,413	9,095	10,363
Total SG&A expenses	1,064	1,588	1,643	2,090	2,545
EBITDA	3,897	4,685	5,770	7,005	7,819
Depreciation & Amortization	1,383	1,867	2,679	3,174	3,480
EBIT	2,515	2,818	3,091	3,831	4,339
Other income	170	952	409	205	200
Interest expenses	-	512	697	752	724
Profit before tax	2,685	3,258	2,803	3,284	3,815
Provision for tax	388	402	406	488	649
Core profit	2,297	2,856	2,398	2,796	3,167
Profit after tax	2,297	2,856	2,398	2,796	3,167
Minority int. and others - paid/(recd.)	(9)	(42)	5	-	-
Profit after minority interest	2,306	2,814	2,403	2,796	3,167
Basic shares outstanding (mn)	161	161	161	161	161
Basic EPS (INR)	14.2	17.5	14.9	17.3	19.6
Diluted equity shares (mn)	163	161	162	162	162
Diluted EPS (INR)	14.1	17.5	14.8	17.2	19.5
CEPS (INR)	23.0	29.6	31.5	37.0	41.2
Dividend per share (INR)	3.0	3.0	3.2	3.5	4.0
Dividend (%)	30.0	30.0	32.5	35.0	40.0
Dividend payout (%)	24.7	20.2	25.5	23.5	23.7

### Common size metrics

Year to June	FY08	FY09	FY10	FY11E	FY12E
Cost of revenues	53.7	54.3	51.6	48.7	49.5
Gross margin	46.3	45.7	48.4	51.3	50.5
SG&A expenses	9.9	11.6	10.7	11.8	12.4
EBITDA margins	36.3	34.1	37.6	39.5	38.1
EBIT margins	23.5	20.5	20.2	21.6	21.1
Net profit margins	21.4	20.8	15.6	15.8	15.4

### Growth ratios (%)

Year to June	FY08	FY09	FY10	FY11E	FY12E
Revenues	50.8	28.0	11.6	15.8	15.7
EBITDA	36.0	20.2	23.2	21.4	11.6
EBIT	36.1	12.1	9.7	23.9	13.3
PBT	38.2	21.4	(14.0)	17.2	16.2
Net profit	32.8	24.4	(16.1)	16.6	13.3
EPS	30.1	24.2	(15.3)	16.3	13.3

**Balance sheet**

(INR mn)

As on 30th June	FY08	FY09	FY10	FY11E	FY12E
Equity capital	1,609	1,610	1,612	1,612	1,612
Share premium account	2,822	2,577	2,644	2,644	2,644
Reserves & surplus	7,411	10,054	11,791	13,929	16,344
Shareholders funds	11,841	14,242	16,047	18,185	20,600
Minority interest (BS)	15	8	3	3	3
Borrowings	6,938	9,967	12,588	11,404	9,977
Deferred tax liability	459	479	424	520	520
<b>Sources of funds</b>	<b>19,253</b>	<b>24,696</b>	<b>29,061</b>	<b>30,111</b>	<b>31,100</b>
Gross block	10,583	16,518	21,594	24,594	28,094
Accumulated depreciation	4,090	4,047	5,014	8,188	11,668
Net block	6,493	12,471	16,580	16,406	16,426
Capital work in progress	1,729	2,793	2,428	1,800	1,350
Deferred tax asset	63	72	71	71	71
Goodwill	2,000	3,010	2,961	2,961	2,961
Investments	2,816	354	551	600	600
Inventories	215	105	39	58	76
Sundry debtors	5,018	5,951	6,248	7,292	7,871
Cash and equivalents	2,598	1,376	504	752	1,591
Loans and advances	1,160	1,305	2,031	2,640	3,116
Total current assets	8,991	8,736	8,821	10,742	12,654
Sundry creditors and others	1,998	1,794	2,351	2,468	2,962
Provisions	841	946	-	-	-
Total current liabilities & provisions	2,840	2,740	2,351	2,468	2,962
Net current assets	6,152	5,996	6,470	8,274	9,692
<b>Uses of funds</b>	<b>19,253</b>	<b>24,696</b>	<b>29,061</b>	<b>30,111</b>	<b>31,100</b>
Book value per share (INR)	73.7	88.5	99.6	112.8	127.8

**Free cash flow**

(INR mn)

Year to June	FY08	FY09	FY10	FY11E	FY12E
Net profit	2,306	2,814	2,403	2,796	3,167
Depreciation	1,383	1,867	2,679	3,174	3,480
Others	84	73	673	643	524
Gross cash flow	3,772	4,754	5,755	6,612	7,170
Less: Changes in WC	180	1,151	1,706	1,555	578
Operating cash flow	3,592	3,603	4,049	5,057	6,592
Less: Capex	3,444	7,635	4,684	2,372	3,050
<b>Free cash flow</b>	<b>148</b>	<b>(4,032)</b>	<b>(635)</b>	<b>2,686</b>	<b>3,542</b>

**Cash flow metrics**

Year to June	FY08	FY09	FY10	FY11E	FY12E
Cash flow from operations	4,910	3,515	5,168	6,730	7,664
Cash for working capital	(180)	(1,151)	(1,706)	(1,555)	(578)
Operating cash flow	3,592	3,603	4,049	5,057	6,592
Net purchase of fixed assets	(3,444)	(7,635)	(4,684)	(2,372)	(3,050)
Net purchase of investments	(3,448)	1,233	(1,942)	156	200
Investing cash flow	(6,891)	(6,402)	(6,626)	(2,215)	(2,850)
Dividends	-	(576)	(573)	(658)	(752)
Proceeds from issue of equity	49	8	13	-	-
Proceeds from LTB/STB	(540)	3,846	3,317	(1,936)	(2,150)
Financing cash flow	(492)	1,577	1,705	(2,594)	(2,902)
Net cash flow	(3,791)	(1,223)	(872)	248	840

**Profitability & efficiency ratios**

Year to June	FY08	FY09	FY10	FY11E	FY12E
ROAE (%)	20.7	22.2	15.8	16.3	16.3
ROACE (%)	15.5	13.8	11.7	13.2	14.5
Debtors days	150	146	145	139	135
Payable days	47	50	49	50	48
Cash conversion cycle (days)	103	95	96	90	87
Current ratio	3.2	3.2	3.8	4.4	4.3
Debt/EBITDA	1.8	2.1	2.2	1.6	1.3
Debt/Equity	0.6	0.7	0.8	0.6	0.5
Adjusted debt/equity	0.6	0.7	0.8	0.6	0.5
Interest coverage	-	5.5	4.4	5.1	6.0

**Operating ratios**

Year to June	FY08	FY09	FY10	FY11E	FY12E
Total asset turnover	0.6	0.6	0.6	0.6	0.7
Fixed asset turnover	1.9	1.4	1.1	1.1	1.3
Equity turnover	1.0	1.1	1.0	1.0	1.1

**Valuation parameters**

Year to June	FY08	FY09	FY10	FY11E	FY12E
Diluted EPS (INR)	14.1	17.5	14.8	17.2	19.5
<i>Y-o-Y growth (%)</i>	<i>30.1</i>	<i>24.2</i>	<i>(15.3)</i>	<i>16.3</i>	<i>13.3</i>
CEPS (INR)	23.0	29.6	31.5	37.0	41.2
Diluted PE (x)	12.0	9.6	11.4	9.8	8.6
Price/BV (x)	2.3	1.9	1.7	1.5	1.3
EV/Revenues (x)	2.7	2.6	2.5	2.1	1.7
EV/EBITDA (x)	7.3	7.6	6.7	5.3	4.5
EV/EBITDA (x) +1 yr forward	6.1	6.1	5.5	4.8	-
Dividend yield (%)	1.8	1.8	1.9	2.1	2.4





Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
HCL Technologies	HOLD	SP	H	Hexaware Technologies	BUY	SO	M
Info Edge	REDUCE	SU	M	Infosys Technologies	HOLD	SP	L
Infotech Enterprises	BUY	SO	H	Mphasis	REDUCE	SU	M
Patni Computer Systems	HOLD	SP	M	Rollta India	BUY	SP	H
Tata Consultancy Services	BUY	SO	L	Wipro	HOLD	SU	L

## 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 < 1.25 x Sector return
	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 < 1.25 x Nifty return
	Sector return < 0.75 x Nifty return

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Ideas create, values protect



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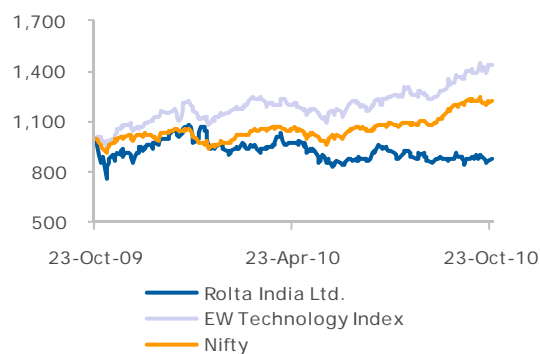
### Coverage group(s) of stocks by primary analyst(s): IT

HCL Technologies, Hexaware Technologies, Infosys Technologies, Info Edge, Infotech Enterprises, Mphasis, Patni Computer Systems, Rolta India, Tata Consultancy Services, Wipro

#### Rolta India



#### EW Indices



#### Distribution of Ratings / Market Cap

##### Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	116	45	12	176
* 3 stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	110	53	13	

#### Recent Research

Date	Company	Title	Price (INR)	Recos
23-Oct-10	<b>Info Edge</b>	Too much too soon; <i>Result Update</i>	635	Reduce
22-Oct-10	<b>Wipro</b>	Mellow quarter in a buoyant environment; <i>Result Update</i>	449	Hold
21-Oct-10	<b>TCS</b>	Picture perfect; <i>Result Update</i>	986	Buy

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