

ROLTA INDIA

Poor free cash generation a key concern

India Equity Research | IT

Rolta India's (Rolta) Q1FY12 revenues were a tad below our estimates while EBITDA margins (excl. MTM losses) stood at 39.5% in line with ours and consensus estimates. While the management is seeing traction in its GIS segments (for IP based solutions) and order book remaining fairly healthy at INR 20.8 bn, the key concern for us continues to be the free cash generating ability of the business. Though the company's debt-equity ratio at 0.8 is at comfortable level, we see its high capex and acquisition led model continuing to impact the FCF generation. While the EV/EBITDA at 3.2x/2.6x FY12E/13E remains undemanding, we believe stock returns will only follow as the visibility of FCF generation improves. We cut our target price to INR 97 and maintain 'BUY'.

Profitability takes a hit due to MTM losses

Revenue at INR 4.9 bn grew 2.0% Q-o-Q versus our estimate of 3.2%. The EBITDA margin nosedived 380bps to 36.8% due to MTM losses. However, excluding MTM losses, margin at 39.5% was in line with our estimates. Net profit at INR 554 mn saw a sharp decline of 32.4% Q-o-Q largely on account of MTM losses on FCCBs and other foreign currency borrowings as well as wage hikes given during the quarter. Excluding the impact of MTM losses, net profit stood at INR 813 mn.

FCCB repayment to be refinanced through ECB

About USD 135mn of FCCB repayment is due in June 2012, which is likely to be refinanced through ECB. Thus, higher interest costs will impact not only the profitability but the FCFE as well.

Outlook and valuations: Focus on cash flow; maintain 'BUY'

While we believe the company will be able to achieve its revenue guidance of 13-15% growth for FY12, we remain cautious on the free cash generation in FY12 as it has guided for a capex of INR 2.5 bn –INR 3.0 bn (from INR 2.5bn in Q4FY11) and has a debt of INR 14.6 bn. However, at CMP of INR 82, we see the concerns being factored in. Currently the stock trades at EV/EBITDA of 3.2x and P/E of 4.4x for FY12E. We have a 'BUY /Sector Performer' rating on the stock.

Financials

Year to June	(INR mn)						
	Q1FY12	Q4FY11	% Chg	Q1FY11	% Chg	FY11	FY12E
Net revenues	4,858	4,766	2.0	4,276	13.6	18,056	20,455
EBITDA	1,790	1,934	(7.5)	1,697	5.4	7,203	7,885
Net profit	543	808	(32.8)	679	(20.1)	3,724	2,991
Diluted EPS (INR)	3.4	5.0	(32.8)	4.2	(19.6)	22.9	18.5
Diluted P/E (x)						4.9	4.4
EV/EBITDA (x)						3.7	3.2
EV/Revenues (x)						1.5	1.2

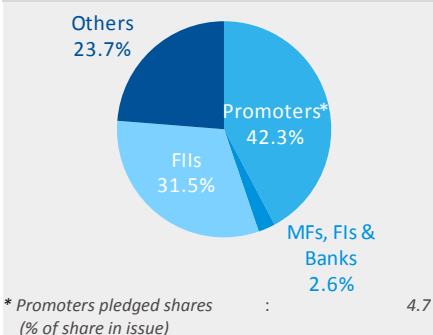
EDELWEISS 4D RATINGS

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

MARKET DATA (R: ROLT.BO, B: RLTA IN)

CMP	: INR 82
Target Price	: INR 97
52-week range (INR)	: 189 / 70
Share in issue (mn)	: 161.3
M cap (INR bn/USD mn)	: 13 / 267
Avg. Daily Vol.BSE/NSE('000)	: 711.2

SHARE HOLDING PATTERN (%)



PRICE PERFORMANCE (%)

	Stock	Nifty	EW Technology Index
1 month	(12.4)	8.4	8.3
3 months	(33.6)	(2.3)	(1.9)
12 months	(52.5)	(10.5)	3.9

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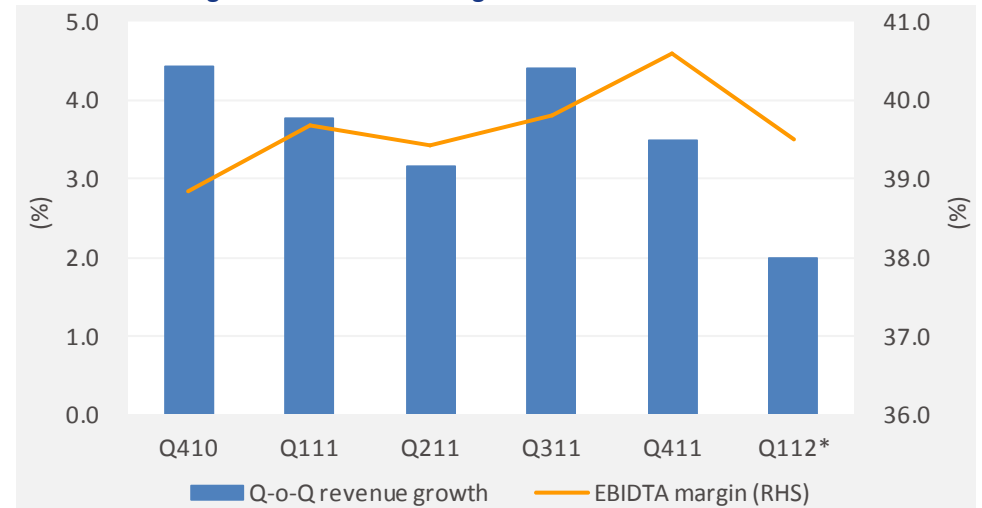
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Key highlights

- Consolidated revenue at INR 4.9 bn was marginally below our estimates and surged 2.0% Q-o-Q and 13.6% Y-o-Y. Gross profit at INR 2.4 bn declined 3.0% Q-o-Q. Gross margin dipped 250bps to 49.6%.
- EBITDA at INR 1.8 bn declined 7.5% Q-o-Q and up 5.4% Y-o-Y. EBITDA margin crashed 380bps Q-o-Q to 36.8% predominantly on account of mark-to-market losses on FCCBs and other foreign currency borrowings and wage hikes effected during the quarter. Excluding the MTM losses, EBITA margin stood at 39.5% in line with ours and consensus estimates.

Chart 1: Revenue growth and EBITDA margin trend



Note: *Q2FY11 EBITDA margin is excluding MTM losses

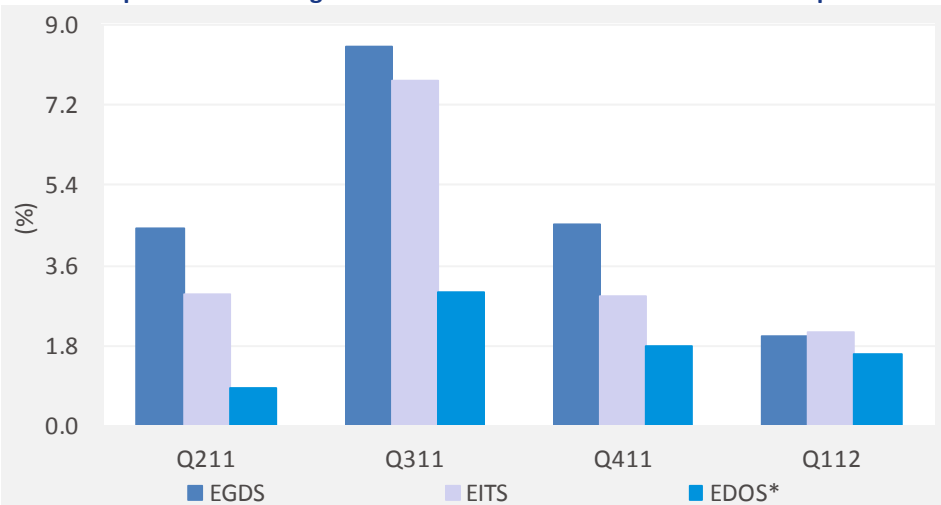
Source: Company, Edelweiss research

- Reported net profit at INR 554 mn was down 32.4% Q-o-Q and 18.4% Y-o-Y. The decline was on account of lower operating profits. Net margin for the quarter stood at 11.4% (17.2% in Q4FY11). Mark-to-market loss of INR 259 mn on FCCBs and other foreign currency borrowings were charged to the P&L Without considering this charge, the net profit for the quarter stood at INR 813 mn.

Segmental performance

- **Enterprise Geospatial and Defense Solutions (EGDS):** Consolidated revenue at INR 2.6 bn was up 2.0% Q-o-Q and 20.8% Y-o-Y. While the gross profit stood at INR 1.6 bn, gross margin surged 220bps sequentially to 60.3%. EBITDA margin took a breather declining sequentially by 460bps to stand at 49.1%. Utilisation for the quarter crashed sequentially by 380bps to 74.8%. Order book showed a sequential decline of 0.4%. On the reported basis, realisation fell 3.1% Q-o-Q.
- **Enterprise Design and Operation Solutions (EDOS):** While the consolidated revenue came in at INR 1.0 bn, EBITDA margin at 36.2% crashed by 490bps over the previous quarter. Order book grew by just 2.4% from the previous quarter.
- **Enterprise IT Solutions (EITS):** The EITS segment revenue at INR 1.2 bn grew 2.1% Q-o-Q. EBITDA margin at 11.1% dipped by 100bps from the previous quarter. Order book jumped up by 4.7% from the previous quarter.

Chart 2: Sequential revenue growth for all businesses declines over last 3 quarters



* Note: Q311 revenue growth post adjustment of share from Shaw Rolta JV
 Source: Company, Edelweiss research

- **Order book accretion disappoints:** Rolta’s order book grew by just 1.4% sequentially. Current order book stands at INR 20.8 bn. The book to bill ratio stood at 1.06x during the quarter.

Chart 3: Order book break-up segment wise

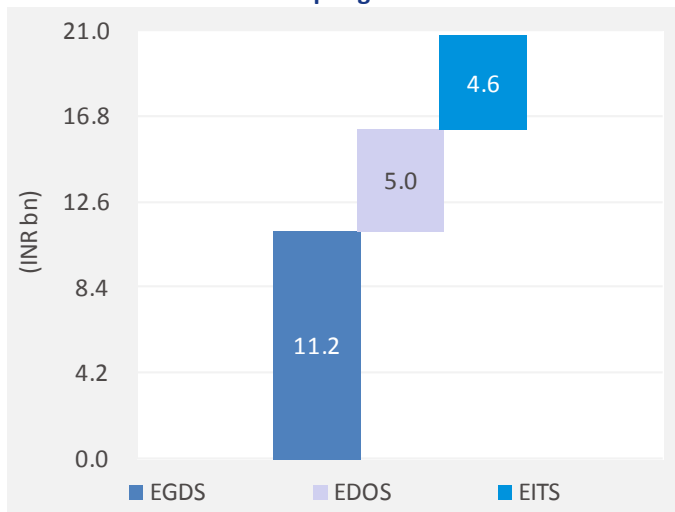
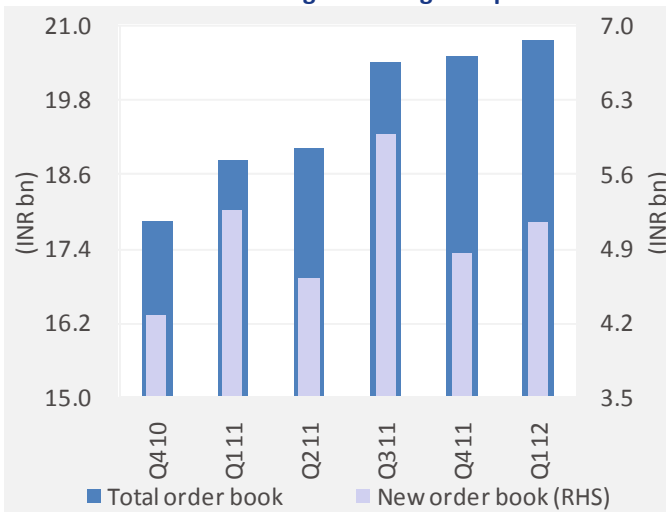


Chart 4: New order booking sees marginal uptick



Source: Company, Edelweiss research

- The management has guided for a capex of INR 2500-INR 3000 mn in FY12.
- Tax rate: Management expects FY12 tax rate to be in the 16%-17% range.

Financial snapshot

(INR mn)

Year to June	Q1FY12	Q4FY11	% Change	Q1FY11	% Change	FY11	FY12E	FY13E
Net revenues	4,858	4,766	2.0	4,276	13.6	18,056	20,455	23,032
Cost of revenue	2,448	2,282	7.3	2,087	17.3	8,931	10,302	11,585
Gross profit	2,410	2,484	(3.0)	2,189	10.1	9,126	10,153	11,447
SG&A	621	549	13.0	492	26.2	1,923	2,268	2,764
EBITDA	1,790	1,934	(7.5)	1,697	5.4	7,203	7,885	8,683
Depreciation	948	886	6.9	763	24.1	3,300	3,551	4,000
EBIT	842	1,048	(19.7)	934	(9.8)	3,903	4,334	4,683
Other income	82	124	(33.9)	55	48.0	308	217	220
Interest	271	254	6.6	194	39.5	899	912	921
Profit before tax	653	918	(28.9)	795	(17.9)	3,312	3,639	3,981
Tax	110	110	0.0	115	(4.3)	625	647	717
Core profit	543	808	(32.8)	680	(20.2)	2,687	2,991	3,265
Minority interest	-	-	150.0	1	(80.0)	-	-	-
Extra ordinary item						1,036	-	-
Reported net profit	543	808	(32.8)	679	(20.1)	3,724	2,991	3,265
Diluted EPS (INR)	3.4	5.0	(32.8)	4.2	(19.6)	22.9	18.5	20.2

As % of net revenues

Gross profit	49.6	52.1		51.2		50.5	49.6	49.7
SG&A	12.8	11.5		11.5		10.6	11.1	12.0
EBITDA	36.8	40.6		39.7		39.9	38.5	37.7
Adjusted net profit	11.2	17.0		15.9		14.9	14.6	14.2
Reported net profit	11.2	17.0		15.9		20.6	14.6	14.2
Tax rate	16.8	12.0		14.5		18.9	17.8	18.0

Company Description

Rolta is one of the leading providers of GIS and engineering design and automation (EDOS) services. In GIS, the company provides and develops digital map-based solutions, servicing customers in segments like defence, environmental protection, utilities, emergency services, and public planning. In EDOS, it 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 EITS group. The company's past 12 months (TTM) revenue stood at INR 18.7 bn and it employs over 3,994 people.

Investment Theme

Outsourcing of engineering services is expected to touch USD 38-50 bn by 2020 against USD 2 bn currently, as per a Nasscom-Booz Allen Hamilton study. As one of the leading offshore engineering services firms for the manufacturing industry, Rolta is poised to grab the rising opportunities. Nevertheless, in the current environment, as capex spending has eased, the company 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 the JV with the Thales Group is also looking up. We perceive Rolta to be 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

- (a) Substantial proportion of revenue from non-annuity sources.
- (b) Slow down in GIS segment.
- (c) Inability to monetise Fusion solutions could impact profitability.
- (d) Inadequate free cash generation to repay FCCB and ECB debt.

Financial Statements

Income statement					(INR mn)
Year to June	FY09	FY10	FY11	FY12E	FY13E
Net revenue	13,728	15,327	18,056	20,455	23,032
Cost of revenues	7,455	7,914	8,931	10,302	11,585
Gross profit	6,274	7,413	9,126	10,153	11,447
Total SG&A expenses	1,588	1,643	1,923	2,268	2,764
EBITDA	4,685	5,770	7,203	7,885	8,683
Depreciation & Amortization	1,867	2,679	3,300	3,551	4,000
EBIT	2,818	3,091	3,903	4,334	4,683
Other income	903	409	308	217	220
Interest expenses	409	697	899	912	921
Profit before tax	3,312	2,803	3,312	3,639	3,981
Provision for tax	402	406	625	647	717
Core profit	2,910	2,398	2,687	2,991	3,265
Extra ordinary item	-	-	1,036	-	-
Profit after tax	2,910	2,398	3,723	2,991	3,265
Minority int. and others - paid/(recd.)	7	5	-	-	-
Profit after minority interest	2,917	2,403	3,724	2,991	3,265
Basic shares outstanding (mn)	161	161	161	161	161
Basic EPS (INR)	18.1	14.9	16.7	18.5	20.2
Diluted equity shares (mn)	161	162	161	161	161
Diluted EPS (INR)	18.1	14.8	16.7	18.5	20.2
CEPS (INR)	29.6	31.5	37.1	40.6	45.0
Dividend per share (INR)	3.0	3.2	3.5	4.0	4.0
Dividend (%)	30.0	32.5	35.0	40.0	40.0
Dividend payout (%)	19.5	25.5	17.7	25.2	23.0

Common size metrics - as % of net revenues

Year to June	FY09	FY10	FY11	FY12E	FY13E
Cost of revenues	54.3	51.6	49.5	50.4	50.3
Gross margin	45.7	48.4	50.5	49.6	49.7
SG&A expenses	11.6	10.7	10.6	11.1	12.0
EBITDA margins	34.1	37.6	39.9	38.5	37.7
EBIT margins	20.5	20.2	21.6	21.2	20.3
Net profit margins	21.2	15.6	14.9	14.6	14.2

Growth ratios (%)

Year to June	FY09	FY10	FY11	FY12E	FY13E
Revenues	28.0	11.6	17.8	13.3	12.6
EBITDA	20.2	23.2	24.8	9.5	10.1
EBIT	12.1	9.7	26.3	11.1	8.0
PBT	23.4	(15.4)	18.1	9.9	9.4
Net profit	26.7	(17.6)	12.1	11.3	9.1
EPS	28.8	(18.3)	12.5	11.3	9.2

Balance sheet					(INR mn)
As on 30th June	FY09	FY10	FY11	FY12E	FY13E
Equity capital	1,610	1,612	1,613	1,613	1,613
Share premium account	2,577	2,355	2,403	2,403	2,403
Reserves & surplus	10,054	12,080	14,969	17,273	19,785
Shareholders funds	14,242	16,047	18,985	21,289	23,802
Minority interest (BS)	8	3	2	2	2
Borrowings	9,967	12,588	14,636	12,725	10,421
Deferred tax liability	479	424	446	520	520
Sources of funds	24,696	29,061	34,069	34,536	34,745
Gross block	16,518	21,594	29,985	32,985	35,985
Accumulated depreciation	4,047	5,014	8,314	11,865	15,865
Net block	12,471	16,580	21,670	21,119	20,119
Capital work in progress	2,793	2,428	1,800	1,350	1,200
Deferred tax asset	72	71	67	67	67
Goodwill	3,010	2,961	2,849	2,849	2,849
Investments	354	551	961	400	500
Inventories	105	39	-	-	-
Sundry debtors	5,951	6,248	6,926	8,294	9,150
Cash and equivalents	1,376	504	451	705	871
Loans and advances	1,305	2,031	1,758	2,286	2,971
Total current assets	8,736	8,821	9,135	11,285	12,992
Sundry creditors and others	1,794	1,246	1,308	1,373	1,648
Provisions	946	1,105	1,105	1,161	1,335
Total current liabilities & provisions	2,740	2,351	2,413	2,533	2,982
Net current assets	5,996	6,470	6,722	8,751	10,010
Uses of funds	24,696	29,061	34,069	34,536	34,745
Book value per share (INR)	88.5	99.6	117.7	132.0	147.5

Free cash flow					(INR mn)
Year to June	FY09	FY10	FY11E	FY12E	FY13E
Net profit	2,917	2,403	3,724	2,991	3,265
Depreciation	1,867	2,679	3,300	3,551	4,000
Others	(30)	673	617	769	701
Gross cash flow	4,754	5,755	7,641	7,311	7,966
Less: Changes in WC	1,151	1,706	304	1,775	1,092
Operating cash flow	3,603	4,049	7,337	5,536	6,874
Less: Capex	7,635	4,684	7,762	2,550	2,850
Free cash flow	(4,032)	(635)	(425)	2,986	4,024

Cash flow metrics

Year to June	FY09	FY10	FY11E	FY12E	FY13E
Cash flow from operations	3,515	5,168	7,703	7,432	8,415
Cash for working capital	(1,151)	(1,706)	(304)	(1,775)	(1,092)
Operating cash flow	3,603	4,049	7,337	5,536	6,874
Net purchase of fixed assets	(7,635)	(4,684)	(7,762)	(2,550)	(2,850)
Net purchase of investments	2,467	(196)	(410)	561	(100)
Others in Cash Flow Metrics	(1,234)	(1,746)	308	217	220
Investing cash flow	(6,402)	(6,626)	(7,864)	(1,772)	(2,730)
Dividends	(576)	(573)	(658)	(752)	(752)
Proceeds from issue of equity	8	13	49	-	-
Proceeds from LTB/STB	3,846	3,317	1,149	(2,823)	(3,225)
Financing cash flow	1,577	1,705	540	(3,575)	(3,978)
Net cash flow	(1,223)	(872)	13	188	166

Profitability & efficiency ratios

Year to June	FY09	FY10	FY11	FY12E	FY13E
ROAE (%)	22.3	15.8	15.3	14.9	14.5
ROACE (%)	13.8	11.7	12.7	12.9	13.7
Debtors days	146	145	133	136	138
Payable days	50	36	26	24	24
Cash conversion cycle (days)	95	109	107	112	114
Current ratio	3.2	3.8	3.8	4.5	4.4
Debt/EBITDA	2.1	2.2	2.0	1.6	1.2
Debt/Equity	0.7	0.8	0.8	0.6	0.4
Adjusted debt/equity	0.7	0.8	0.8	0.6	0.4
Interest coverage	6.9	4.4	4.3	4.8	5.1

Operating ratios

Year to June	FY09	FY10	FY11	FY12E	FY13E
Total asset turnover	0.6	0.6	0.6	0.6	0.7
Fixed asset turnover	1.4	1.1	0.9	1.0	1.1
Equity turnover	1.1	1.0	1.0	1.0	1.0

Valuation parameters

Year to June	FY09	FY10	FY11	FY12E	FY13E
Diluted EPS (INR)	18.1	14.8	16.7	18.5	20.2
Y-o-Y growth (%)	28.8	(18.3)	12.5	11.3	9.2
CEPS (INR)	29.6	31.5	37.1	40.6	45.0
Diluted PE (x)	4.5	5.5	4.9	4.4	4.0
Price/BV (x)	0.9	0.8	0.7	0.6	0.6
EV/Sales (x)	1.6	1.6	1.5	1.2	1.0
EV/EBITDA (x)	4.6	4.3	3.7	3.2	2.6
EV/EBITDA (x)+1 yr forward	3.7	3.4	3.4	2.9	-
Dividend yield (%)	3.7	4.0	4.3	4.9	4.9

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
ECLERX SERVICES	BUY	SO	M	HCL Technologies	BUY	SO	H
Hexaware Technologies	BUY	SO	M	Info Edge	REDUCE	SU	M
Infosys	HOLD	SP	L	Infotech Enterprises	BUY	SO	H
Mphasis	REDUCE	SU	M	Patni Computer Systems	HOLD	SU	M
Rohta 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
	Stock return < 1.25 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

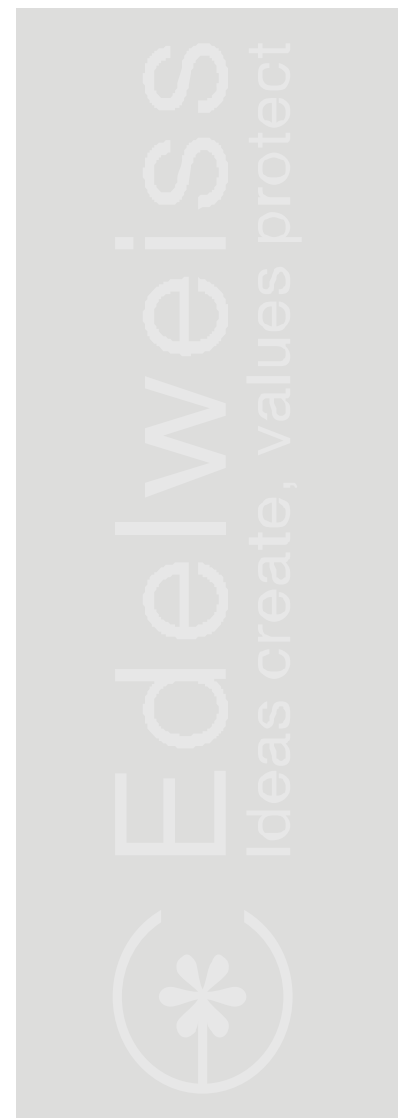
RELATIVE RISK RATING

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
	Sector return < 1.25 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): IT

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

Recent Research

Date	Company	Title	Price (INR)	Recos
31-Oct-11	Wipro	Gradual progression; <i>Result Update</i>	367	Hold
20-Oct-11	Info Edge	Moderating hiring outlook ; <i>Result Update</i>	704	Reduce
20-Oct-11	Hexaware Technologies	Delivering consistently; <i>Result Update</i>	89	Buy

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	119	47	15	184
* 3 stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	111	57	16	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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