

Performance inline - Significant expansion in margins

Results Highlights

- ⇒ Persistent Systems posted decent set of numbers for Q3 FY12, both top line and profits came in line with our expectations while were above street's expectations.
- ⇒ The company top line grew 12.1% Q-o-Q and 37.3% Y-o-Y to Rs 2.67 bn, in line with our estimate of Rs 2.69 bn, aided by 11% rupee depreciation and higher utilization.
- ⇒ The revenue in US\$ terms grew only 0.3% Q-o-Q and 19.6% Y-o-Y to US\$ 51.7 mn, slowed down due to consolidation in some top accounts & delays in decision making due to uncertainty in the macroeconomic environment. As a result management also lowered its full year revenue guidance for FY12E to \$205-210 mn from \$220 mn.
- ⇒ Management believes that to spur top line growth it will have to grow partnership with existing clients (OPD business), "Sell with partners" for building services on technology platforms and will have to develop IPs (IP-Led Services) and focus primarily into new technological areas like cloud, mobility ,analytics and collaboration.
- ⇒ Net profit stood at Rs 406 mn up 12.0% Y-o-Y and 25.2% sequentially aided by outstanding margins performance offset by forex losses of Rs 41mn in the quarter.
- ⇒ Diluted EPS stood at Rs 10.1 inline with our estimate of Rs 10.2 for the quarter
- ⇒ EBITDA margin expanded 547 bps sequentially and 225 bps Y-o-Y to 24.2%, aided by rupee deprecation of 12.4% in the quarter, higher nonlinear revenues, higher Utilization rates and reduction in total no of employees.
- ⇒ Volumes grew only 0.7% sequentially, primarily due to lower no of working days and lower employee addition in the quarter.
- ⇒ Onsite pricing environment remained under pressure and declined 2.2% sequentially while offshore pricing remained flat sequentially. We believe pricing environment to remain stable in the coming quarters however demand uncertainty and instability in the west can put some pressure going forward.
- ⇒ Utilization excluding trainees improved 30 bps to 74.1% which we expect to improve further going forward. Attrition too improved and stood at 17.4% in Q3 FY12 vs 17.7% in the last quarter.

Higher margin IP led services to spur growth, Top 1/5/10 clients contribution decline

Persistent has strategically invested significantly in higher margin IP-led business and currently spend 6.0% of its technical man month into R&D up from 5.5% in the last quarter. Its contribution to total revenues increased 160 bps sequentially to 9.2% in Q3 FY12. Going forward we expect the company is well poised to tap the immense opportunities present in IP-led services business and thus will boost top line and provide cushion to margins. Revenue contribution from Top 1/5/10 clients declined 10/160/110 bps sequentially and stood at 15.9%/37.0%/48.3% respectively.

Outlook and Valuation

We believe that ongoing uncertainty in the west, unstable demand environment is the biggest risk present at the moment, which can delay client decisions and impact IT spending, making it difficult for the company to maintain high growth rate in FY13E. Management too is witnessing some delays in decision making from clients (specially large deals) and believes that consolidation within some large client base can impact business. However, we believe that company's ability to maintain long term relationships with large marquee clients, significant focus on non linear revenue streams and foray into new technological areas will help the company to achieve ~15% growth in US\$ terms in FY13E. We expect the company revenue and Diluted EPS to grow at 20.1% and 20.0% to Rs 12.0 bn and Rs 40.7 respectively in FY13E. For Q4 FY12E and FY13E we have assumed USD/INR rate of Rs 50. The stock currently trades at a P/E of 9.4x and 7.9x FY12E and FY13E earnings which we think is at a discount to its peers considering its high growth rate, healthy return ratios and higher margins. We maintain our "BUY" rating on the stock and give a DCF based target price of Rs 403 an upside of 25.8% from current levels.

Stock Rating

BUY	HOLD	SELL
> 15%	-5% to 15%	< -5%

Sector Outlook

Bullish

Stock

CMP (Rs)	320.6
Target Price (Rs)	370.0
BSE code	533179
NSE Symbol	PERSISTENT
Bloomberg	PSYS.IN
Reuters	PERS.BO

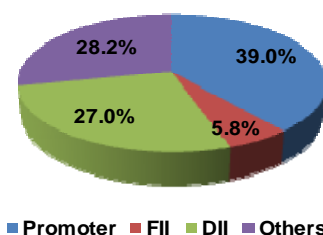
Key Data

Nifty	5,240.7
52WeekH/L(Rs)	433.8/281.0
O/s Shares (mn)	40
Market Cap (Rs bn)	12.82
Face Value (Rs)	10

Average volume

3 months	14,802
6 months	20,098
1 year	35,389

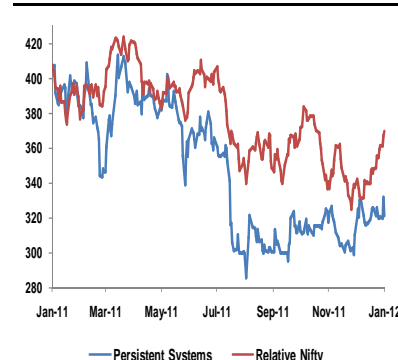
Share Holding Pattern (%)



Key Financials					
YE March (Rs. mn)	FY09	FY10	FY11	FY12E	FY13E
Net Sales	5,938	6,012	7,758	9,991	11,995
Sales Growth (Y-o-Y)	39.8%	1.2%	29.1%	28.8%	20.1%
EBIDTA	914	1,464	1,583	2,092	2,550
EBIDTA Growth (Y-o-Y)	1.5%	60.2%	8.2%	32.1%	21.9%
Net Profit	661	1,150	1,397	1,358	1,630
Net Profit Growth (Y-o-Y)	(20.5%)	74.0%	21.5%	(2.8%)	20.0%
Diluted EPS	18.8	32.1	34.9	34.0	40.7
Diluted EPS Growth (Y-o-Y)	-22.1%	70.1%	8.8%	-2.7%	20.0%
Key Ratios					
EBIDTA (%)	15.4%	24.3%	20.4%	20.9%	21.3%
NPM (%)	11.1%	19.1%	18.0%	13.6%	13.6%
RoE (%)	18.6%	22.0%	19.8%	16.4%	16.8%
RoCE (%)	18.6%	21.9%	19.7%	16.4%	16.7%
Book Value Per share (Rs.)	110.1	178.1	186.8	219.1	258.2
Valuation Ratios					
P/E (x)			9.2x	9.4x	7.9x
EV/EBITDA (x)			7.0x	5.3x	4.0x
P/BV (x)			1.7x	1.5x	1.2x
Market Cap./ Sales (x)			1.6x	1.2x	1.0x

Source: Company, BP Equities Research

Relative Price Chart



Research Analyst

Amit Chandra

amitchandra@bpwealth.com

022-61596411

Quarterly Result Analysis (Consolidated)

YE March (Rs. mn)	Q3 FY12	Q2 FY12	Q-o-Q change %	Q3 FY11	Y-o-Y change %	Q3 FY12 BP Esti- mates	Deviation%
Net Sales	2,677	2,382	12.4%	1,949	37.3%	2,696	(0.7%)
Less:							
Personnel expenses	1,643	1,632	0.7%	1,270	29.4%	1,716	(4.2%)
Operating and other expenses	386	304	27.0%	252	53.5%	351	10.2%
Total Expenditure	2,030	1,936	4.9%	1,522	33.4%	2,067	(1.8%)
EBIDTA	648	446	45.2%	428	51.4%	630	2.8%
Less: Depreciation	159	140	14.0%	106	49.6%	144	10.8%
EBIT	489	307	59.4%	321	52.0%	486	0.5%
Less: Interest	0	0	NA	0	NA		NA
Add: Other income	76	145	(47.5%)	73	3.4%	94	(19.5%)
Less: Extraordinary Expense (net)	0	0	NA	0	NA		NA
Profit before tax	565	451	25.2%	395	43.0%	581	(2.8%)
Adjusted Profit before Tax	565	451	25.2%	395	43.0%	581	(2.8%)
Less: Total Tax	159	127	25.0%	32	389.2%	174	(8.8%)
Profit After Tax	406	324	25.2%	362	12.0%	406	(0.2%)
Adjusted Profit After Tax	406	324	25.2%	362	12.0%	406	(0.2%)
Diluted EPS (Rs.)	10.1	8.1	25.2%	9.1	12.0%	10.2	(0.2%)
Adjusted Diluted EPS	10.1	8.1	25.2%	9.1	12.0%	10.2	(0.2%)
Diluted No of Share (mn)	40.0	40.0		40.0		40.0	
Margin Analysis %			Change in bps		Change in bps		Change in bps
EBIDTA Margin %	24.2%	18.7%	547	21.9%	225	23.4%	83
EBIT Margin %	18.3%	12.9%	538	16.5%	176	18.0%	22
NPM %	15.2%	13.6%	155	18.6%	(343)	15.1%	8
Effective Tax Rate %	28.1%	28.2%	(3)	8.2%	1,991	30.0%	(187)
Cost Analysis %			Change in bps		Change in bps		Change in bps
Personnel expenses	61.4%	68.5%	(712)	65.1%	(377)	63.6%	(226)
Operating and other expenses	14.4%	12.8%	166	12.9%	152	13.0%	142

Source: Company, BP Equities Research

Results Highlights

- ⇒ In Q3 FY12, Persistent revenue grew 37.3% Y-o-Y and 12.4% sequentially in INR terms to Rs.2,677 mn, driven by rupee depreciation and expansion in utilization rate
- ⇒ In US Dollar terms, the company's revenue grew 0.3% Q-o-Q and 19.6% Y-o-Y to US\$ 51.7 mn, which was below expectations due to lower volumes growth
- ⇒ The tax rate for the quarter stood at 28.1%, as against 28.2% in Q2 FY12. Tax rate for the full year is expected to be at 28-30%
- ⇒ At the end of the quarter, company had cash & cash equivalents amounting to Rs.1,518 mn on its balance sheet as against Rs 903 mn in the same quarter last year, which the company will use for acquisitions
- ⇒ DSO stood at 68 in the quarter as compared to 66 in the last quarter
- ⇒ The total number of employees reduced by 194 in the quarter and stood at 6,706.
- ⇒ The company added 20 clients in the quarter which were primarily small client of size up to \$1mn.
- ⇒ Life science segment contributed 12.5% against 10.6% in the last quarter due to contribution from French life science business and we expect this to a strong revenue driver for the company

Persistent Systems Ltd.

Q3 FY12 Result Update

Income Statement

YE March (Rs. mn)	FY09	FY10	FY11	FY12E	FY13E
Net Sales	5,938	6,012	7,758	9,991	11,995
Growth %	39.8%	1.2%	29.1%	28.8%	20.1%
Total Revenue	5,938	6,012	7,758	9,991	11,995
Less:					
Personnel Expenses	3,324	3,687	5,123	6,491	7,825
Operating & Other expenses	1,701	860	1,052	1,408	1,619
Total Operating Expenditure	5,025	4,548	6,175	7,899	9,445
EBIDTA	914	1,464	1,583	2,092	2,550
Growth %	1.5%	60.2%	8.2%	32.1%	21.9%
Less: Depreciation	297	335	424	592	691
EBIT	617	1,128	1,159	1,500	1,859
Growth %	-0.5%	83.0%	2.7%	29.4%	23.9%
Non-operating Income	69	112	344	437	420
Extraordinary Income	(15)	0	2	0	0
Extraordinary Expense	0	0	0	0	0
Profit Before tax	671	1,241	1,505	1,937	2,279
Tax	10	91	108	579	650
Minority Interest	0	0	0	0	0
Net Profit	661	1,150	1,397	1,358	1,630
Adjusted Profit	676	1,150	1,396	1,358	1,630
Reported Diluted EPS Rs	18.4	32.1	34.9	34.0	40.7
Growth %	-20.5%	73.9%	9.0%	-2.8%	20.0%
Adjusted Diluted EPS Rs	18.8	32.1	34.9	34.0	40.7
Growth %	-22.1%	70.1%	8.8%	-2.7%	20.0%

Source: Company, BP Equities Research

Balance Sheet

YE March (Rs. mn)	FY09	FY10	FY11	FY12E	FY13E
Liabilities					
Equity Capital	359	400	400	407	407
Reserves & Surplus	3,589	5,990	7,071	8,357	9,920
Equity	3,948	6,390	7,471	8,764	10,327
Preference Share Capital	0	0	0	0	0
Net Worth	3,948	6,390	7,471	8,764	10,327
Net Deferred tax liability/(Asset)	0	45	30	29	32
Total Loans	0	0	0	0	0
Capital Employed	3,948	6,435	7,501	8,793	10,359
Assets					
Gross Block	3,372	3,715	4,543	5,743	6,643
Less: Depreciation	1,573	1,881	2,281	2,873	3,564
Net Block	1,800	1,834	2,261	2,870	3,079
Capital WIP	377	485	605	649	696
Investments	880	1,562	2,500	2,598	2,639
Others - A	20	7	60	60	60
Current Assets					
Sundry Debtors	1,034	1,363	1,582	2,053	2,465
Cash and Bank Balance	211	1,918	1,000	1,207	2,173
Loans and Advances	408	723	869	1,079	1,295
Other Current Assets	130	340	226	310	372
Total Current Assets	1,784	4,344	3,677	4,649	6,305
Less: Current Liabilities & Provisions					
Sundry Creditors	140	398	465	606	725
Provisions	170	317	396	478	555
Other Current Liabilities	604	1,080	741	949	1,140
Total Current Liabilities & Provisions	914	1,796	1,602	2,033	2,419
Capital Applied	3,948	6,435	7,501	8,793	10,359

Source: Company, BP Equities Research

Key Ratios

YE March (Rs. mn)	FY09	FY10	FY11	FY12E	FY13E
Key Operating Ratios					
EBITDA Margin (%)	15.4%	24.3%	20.4%	20.9%	21.3%
Tax / PBT (%)	1.4%	7.3%	7.2%	29.9%	28.5%
Net Profit Margin (%)	11.1%	19.1%	18.0%	13.6%	13.6%
RoE (%)	18.6%	22.0%	19.8%	16.4%	16.8%
RoCE (%)	18.6%	21.9%	19.7%	16.4%	16.7%
Current Ratio (x)	2.0x	2.4x	2.3x	2.3x	2.6x
Dividend Payout (%)	6.3%	10.0%	18.4%	20.7%	20.1%
BV Per Share (Rs.)	110.1	178.1	186.8	219.1	258.2
Financial Leverage Ratios					
Debt/ Equity (x)	0.1x	0.1x	0.1x	0.0x	0.0x
Interest Coverage (x)	NA	NA	NA	NA	NA
Interest / Debt (%)	NA	NA	NA	NA	NA
Growth Indicators %					
Gross Block Growth (%)	15.2%	10.2%	22.3%	26.4%	15.7%
Sales Growth (%)	39.8%	1.2%	29.1%	28.8%	20.1%
EBITDA Growth (%)	1.5%	60.2%	8.2%	32.1%	21.9%
Net Profit Growth (%)	(20.5%)	74.0%	21.5%	(2.8%)	20.0%
Diluted EPS Growth (%)	(20.5%)	73.9%	9.0%	(2.8%)	20.0%
Turnover Ratios					
Debtors days	64	83	74	75	75
Creditors days	10	32	27	28	28

Source: Company, BP Equities Research

Valuation Ratios

YE March (Rs. mn)	FY09	FY10	FY11	FY12E	FY13E
P/E (x)			9.2x	9.4x	7.9x
P/BV (x)			1.7x	1.5x	1.2x
EV/EBIDTA (x)			7.0x	5.3x	4.0x
EV/Sales			1.4x	1.1x	0.8x
Market Cap./ Sales (x)			1.6x	1.2x	1.0x
Dividend Yield (%)			1.8%	2.0%	2.3%

Source: Company, BP Equities Research

Cash Flow Analysis

YE March (Rs. mn)	FY09	FY10	FY11	FY12E	FY13E
EBITDA	617	1,128	1,159	1,500	1,859
Less: Adjusted Taxes	9	82	83	448	530
NOPLAT	608	1,046	1,076	1,052	1,329
Plus: Depreciation	297	335	424	592	691
Less: Increase in Working Capital	416	(269)	721	350	370
Operating Cash flow	489	1,650	779	1,293	1,650
Less: Net Capex	501	476	971	1,245	946
Less: Increase in Net Other Assets	(105)	183	(173)	29	(29)
FCF From Operation	93	991	(19)	19	733
Less: Inc./(Dec.) in Investment	9	(9)	0	0	0
FCF after Investment	84	1,000	(19)	19	733
Plus: Gain/(loss) on Extraordinary Items	(15)	0	2	0	0
Total FCF	70	1,000	(17)	19	733
Financing Cash Flow					
Interest Exp/(inc) After Tax, Net	(68)	(104)	(320)	(306)	(300)
Inc/(dec) in Excess Cash and Marketable Securities	138	2,396	(14)	260	967
Dec/(Inc) in Debt	0	0	0	0	0
Dividends	42	115	257	281	328
Share Repurchase/(Issues)	(43)	(1,406)	60	(215)	(261)
Total Financing Flow	70	1,000	(17)	19	733

Source: Company, BP Equities Research



BP WEALTH

Research Desk

Tel: +91 22 61596464

Institutional Sales Desk

Tel: +91 22 61596403/04/05

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Corporate Office:**4th Floor, Rustom Bldg, 29, Veer Nariman Road, Fort, Mumbai – 400001****Phone- +91 22 61596161 Website- www.bpwealth.com**