

26 May 2016

Initiating Coverage (BUY)

KELLTON TECH SOLUTIONS

CMP

INR 198

Target Price

INR 267

Stock Details

Industry	IT Software Products
Bloomberg Code	KTSL:IN
BSE Code	519602
Face Value (Rs.)	5.00
Market Cap. (Rs. Mn)	9,257.6
52wk. High/Low (Adjusted) ((Rs.)	236.80 / 55.50

Shareholding Pattern Jun '15

Promoter (%)	62.32
FII (%)	0.00
DII (%)	0.00
Public - Other (%)	37.68
No. of Share Outstanding (mn)	46.83

Valuation Summary

	FY 14A	FY 15A	FY 16E	FY 17E
P/E (x)*	5.27	27.41	25.00	18.00
EV/EBITDA (x)	2.69	29.24	13.81	10.01
P/BV (x)	0.90	11.92	8.53	6.70

*TTM for Current Year

Based on Market Price as on 1st Apr is taken for FY14

Key Financial

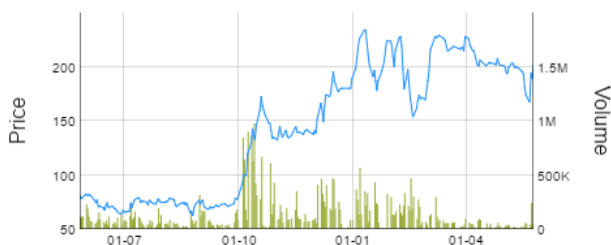
Rs. Mn	FY 14A	FY 15A	FY 16E	FY 17E
Net Sales	1,337	2,379	4,639	6,959
EBITDA	132	326	747	1,261
Net Profit	64	221	399	694
EPS (Rs.)*	1.8	5.3	8.5	14.8

*Un adjusted

Key Ratios

	FY 14A	FY 15A	FY 16E	FY 17E
EBITDA Margin (%)	9.9	13.7	16.1	18.1
EBIT Margin (%)	8.1	12.5	15.2	17.3
Net Pro. Margin (%)	4.8	9.3	8.6	10.0
Debt/Equity (x)	0.03	0.56	0.37	0.23
RoNW (%)	18.0	36.4	41.0	45.7
RoCE (%)	13.0	22.6	25.2	30.9

One Year Price / Volume



We recommend 'BUY' on Kellton Tech Solutions for a target of INR 267 - valuing the company at P/E of 18.0x FY17E Earning.

INVESTMENT RATIONALE:

- Acquired two US-based companies. VIVOS Professional Services enabled expansion in verticals of healthcare & life-sciences; ProSoft Group strengthened capabilities in ERP, EAI & BPM.
- Acquisition led growth accelerated overall growth. Successfully integrated all the acquisitions.
- Expanded global foothold. Opened and acquired new offices.
- Serving clients from startups to Fortune 500 companies.
- Kellton Tech looks forward to smaller acquisitions to fulfill its long-term strategy of offering the complete spectrum of IT offerings.
- Kellton Tech powers 30% of the 21 billion dollar eCommerce market in India through its clients.
- Sales have grown from 0.68cr to 39.90cr and NP from (minus)3.65cr(loss) to profit of 6.16cr during June 2011 to June 2015. The Company expects to do a turnover of 600cr for June '16 and targets annual revenues of 2000cr in 3 years which is highly promising and impressive.

VALUATIONS AND VIEW:

Sales have grown from 0.68cr to 39.90cr and NP from (minus)3.65cr (loss) to profit of 6.16cr during June 2011 to June 2015. Kellton Tech acquired US-based ProSoft Technology Group, a leading enterprise solutions and business integration provider. The acquisition strengthens Kellton Tech's ERP-EAI capabilities and increases its total headcount to over 1000. Thus empowered, it aims to reach revenue of Rs. 600 crore by August 2016 and targets Rs. 2000 crore annual revenue in the next three years.. We value the business at 18x FY17E EPS and recommend a BUY rating on the stock with a target price of INR 267 per share.

RISK & CONCERNS:

- **Technology Obsolesces:** There is a tendency to rush towards latest fads in technology, and by the time a company equips itself with the necessary specific expertise, the fad may no longer be in vogue. Technology being highly volatile, there is a need to be able to cater to newly developed markets in quick notice and capitalise on the opportunities they offer. However, companies risk being caught off-guard if after all the efforts they put in, the market need has evolved or moved on. Therefore, Kellton Tech has dual focus on both meeting the immediate requirements in contemporary market while keeping the long-range customer needs in mind.
- **Highly Competitive Market that may impact pricing power**

COMPANY BACKGROUND:

Kellton Tech Solutions Limited is a software development company. The Company offers information technology (IT) solutions, strategic technology consulting and product development services in Web; social, mobile, analytics, cloud (SMAC); enterprise resource planning (ERP)-business process management (BPM), and Internet of things (IoT) space. Its product includes KLGAME, which is a gamification, analytics and messaging engine that provides backend system. It offers services, such as offshore product development, research and development, IT consulting services, analytics and information management, resourcing, Internet marketing services and managed services. The Company serves clients across a range of verticals, including retail; travel; e-commerce; education; hospitality; advertising; market research; manufacturing; consumer goods; logistics; supply chain management (SCM); banking, financial services and insurance (BFSI); lifestyle, and non-profits.

Kellton Tech is steadily expanding its offerings portfolio through organic growth and synergistic acquisitions. It has strengthened its foothold in technology and through its expanded workforce it is capable of offering a diverse range of IT services and solutions.

Today, its offerings include I-SMAC (Internet of Things, Social, Mobile, Analytics, Cloud), Enterprise Resource Planning, and Enterprise Application Integration apart from its other traditional offerings.

INDUSTRY OVERVIEW:

India gave a decisive mandate for a strong government last year and the new government has since been actively working to inspire global confidence in India's growth story and IT industry has been accorded special focus in the new scheme of affairs. The recently launched Digital India Campaign would open up a plethora of opportunities for IT companies.

The vision of smart cities is a challenge that Indian IT industry is well-equipped to tackle and this is a golden opportunity to demonstrate its technological prowess while contributing to the nation-building.

Now that the tremors from Greek Crises have been absorbed, Indian IT companies can look forward to serve European customers too.

India is the topmost offshoring destination for IT companies across the world. Having proven its capabilities in delivering both on-shore and off-shore services to global clients, emerging technologies now offer an entire new gamut of opportunities for top IT firms in India. Social, mobility, analytics and cloud (SMAC) are collectively expected to offer a US\$ 1 trillion opportunity. Cloud represents the largest opportunity under SMAC, increasing at ~30% CAGR to around US\$ 650-700 billion by 2020. The social media is the second most lucrative segment for IT firms, offering a US\$ 250 billion market by 2020. The Indian e-commerce segment is US\$ 12 billion in size and is witnessing strong growth and thereby offers another attractive avenue for IT companies to develop products and services to cater high growth consumer segment.

Globalisation has made it impossible for any nation to be insulated from the economic tremors from elsewhere. This was reinforced when the news of Greek Crises and Chinese Stock market crash were received with concern globally. Thankfully, the Greek Crises appeared to be resolved for now, and Europe can look forward to future with renewed optimism.

Increasingly, the traditional advantage of English-speaking people that India earlier possessed, can no longer be solely relied upon. Many South Asian nations apparently provide a ready, cheaper alternative in this respect. However, Indian IT industry, by and large, has met this challenge by trying to realign its focus on value-added products and services. But this will require pouring more efforts and resources in the R&D endeavours.

Kellton Tech's R&D efforts (whose latest brainchild is KLGAME™) have been handsomely rewarded even as it prepares itself for the long haul.

Peer Comparison

Company	CMP (Rs)	P/E*	Mcap (Rs Cr)	Div Yld (%)	NP Qtr (Rs Cr)	Qtr Profit Var (%)	Sales Qtr (Rs Cr)	Qtr Sales Var (%)	CMP/BV
Lycos Internet	18	2.1	833.4	-	125.2	26.60	718.3	20.58	0.45
Tata Elxsi	166	20.3	659.0	0.61	41.1	37.70	294.0	27.10	5.24
Polaris Consulta	199	14.9	2,016.7	7.44	5.1	(82.15)	506.1	8.36	2.06
Aurionpro Sol.	143	4.6	314.4	1.90	14.1	(31.45)	187.3	8.82	0.60
Trigyn Techno.	108	8.2	317.7	-	13.5	195.86	173.4	27.87	1.11
Zen Technologies	74	15.0	568.3	0.48	(2.7)	3.97	4.5	(40.19)	4.82
Subex	10	13.6	497.2	-	(11.5)	40.78	89.5	(20.23)	1.86
Kellton Tech	201	27.4	9,982.5	-	10.1	108.66	116.5	156.46	11.92

*TTM

FINANCIAL OVERVIEW

Q2 FY16 Performance Highlight							
(in Million)	2Q FY15	3Q FY15	4Q FY15	1Q FY16	2Q FY16	YoY (%)	QoQ (%)
Revenue	9.41	9.72	11.83	13.16	18.70	98.72%	42.10%
Other Income	0.01	0	0.49	0.06	0.01		
Total Income	9.42	9.72	12.32	13.22	18.71	98.62%	41.53%
Expenditure	-7.30	-7.46	-8.98	-9.25	-14.46		
As a % of Sales	77.58%	76.75%	75.91%	70.29%	77.33%		
Interest	-0.38	-0.4	-0.36	-0.74	-0.57	50.00%	-22.97%
PBDT	1.74	1.86	2.98	3.23	3.68		
As a % of Sales	18.49%	19.14%	25.19%	24.54%	19.68%		
Depreciation	-0.19	-0.23	-0.32	-0.34	-0.36		
PBT	1.55	1.64	2.66	2.89	3.32	114.19%	14.88%
As a % of Sales	16.47%	16.87%	22.49%	21.96%	17.75%		
Tax	-0.06	0.02	-0.84	-0.89	-0.79	1216.67%	-11.24%
Net Profit	1.49	1.65	1.82	2	2.53	69.80%	26.50%
As a % of Sales	15.83%	16.98%	15.38%	15.20%	13.53%		
Equity	20.69	21.72	21.74	21.74	21.77	5.22%	0.14%
EPS (Rs)	0.39	0.41	0.43	0.46	0.58	48.72%	26.09%
CEPS (Rs)	0.41	0.43	0.49	0.54	0.66		
OPM %	22.53	23.27	28.23	30.15	22.72		
NPM %	15.86	17.02	15.41	15.19	13.54		

Income Statement (Consolidated)

Y/E June (Rs mn)	FY 12A	FY 13A	FY 14A	FY 15A	FY 16E	FY 17E	FY 18E
Net Sales	391	486	1,337	2,379	4,639	6,959	9,742
Other Operating Income	-	-	-	-	-	-	-
Expenditure	349	426	1,205	2,053	3,921	5,742	8,039
EBITDA	41	60	132	326	718	1,217	1,703
Depreciation	9	11	23	28	44	55	64
EBIT	32	49	108	297	674	1,162	1,639
Interest Expenses	3	10	33	59	115	172	242
PBT	30	39	75	239	559	990	1,398
Tax	2	8	12	35	188	340	481
Other Income	2	5	1	17	29	44	50
Extraordinary Items	-	-	-	-	-	-	-
Net Income Before Adjustment	29	37	64	221	399	694	967
Minority Int./Income from Assoc.	-	-	-	-	-	-	-
Adjusted PAT	29	37	64	221	399	694	967

Balance Sheet (Consolidated)

Y/E June (Rs mn)	FY 12A	FY 13A	FY 14A	FY 15A	FY 16E	FY 17E	FY 18E
Equity share capita	177	177	207	217	217	217	217
Reserves & surplus	50	94	221	435	830	1,523	2,490
Share Warrants	-	-	7	124	124	124	124
Misc Expenditure	-	-	-	-	-	-	-
Net worth	227	271	436	776	1,171	1,864	2,831
Minority Interest	-	-	-	-	-	-	-
Share Application Money	-	-	-	-	-	-	-
Loan Funds	2	16	13	436	432	430	428
Net deferred tax liability	2	3	3	2	2	2	2
Other Long-term Liabilities	33	66	167	116	227	340	476
Long-term Provisions	-	-	3	4	7	11	15
Total Liabilities	263	358	622	1,337	1,840	2,650	3,755
Net block	174	218	540	1,076	1,527	1,778	2,123
Investment, Loan & Adv.	15	35	33	16	31	52	69
Total Current Assets	103	175	441	1,292	1,860	3,055	4,706
Current Liabilities & Provisions	28	71	392	1,049	1,578	2,238	3,144
Net Current Assets	75	104	49	243	281	817	1,561
Total Assets	263	358	622	1,337	1,840	2,650	3,755

Cash Flow (Consolidated)

Y/E June (Rs mn)	FY 15A	FY 16E	FY 17E	FY 18E
Operating Cash Flow	111	97	282	569
Cash Flow from Investments	(562)	(417)	(280)	(369)
Cash Flow from Financing	570	248	203	209
Net Changes in Cash	119	(71)	205	409
Opening Cash	49	168	97	301
Closing Cash Balance	168	97	301	710

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1.Analyst ownership of the stocks mentioned above	No
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