

L&T Technology Services Limited

Issue competitively priced - Subscribe

Company background: L&T Technology Services Limited (LTTS) is subsidiary of Engineering giant, L&T and was incorporated in Jun-2012. Post transfer of Product Engineering Services (PES) and Integrated Engineering Services (IES) division and 2 acquisitions in 2014-15, LTTS emerged as leading pure play Engineering Research & Development (ER&D) player. Zinnov recognizes LTTS in "leadership zone" in 8 Industry verticals (Industrial Automation, Construction and Heavy Machinery, Medical Devices, Aerospace, Automotive, Rail and Marine, Telecom, Energy and Utilities) & 2 horizontal offerings (Embedded Systems and Mechanical). LTTS has 12 Global Delivery Centres (GDCs), 27 sales offices globally and 31 Labs in India. As of Jun-2016, LTTS has 9,419 Engineers from 9 nationalities serving 200+ customers, including >50 of Fortune 500 customers.

Positives: (1) LTTS, a leading global pure-play ER&D company is likely to benefit from (a) under-penetration, (b) expected increase in India's market share in outsourced ER&D space, and (c) strong 13% industry CAGR during FY2015-20E, (2) pursue multi-pronged growth strategy, which includes (a) Focus on key Segments, Verticals and Geographies, (b) mine existing customers and add new customers, (c) Focus on Solutions-oriented Engineering services, (d) continued investment towards innovation labs, (e) pursue selective acquisitions, (f) Attract and retain employees, and (3) Operational levers (improvement in Utilization, better onshore-offshore mix) to aid margin expansion, and (4) strong historical financial performance.

Risks & Concerns: (1) LTTS could lose business volumes if large clients set-up their own captive R&D centers, (2) LTTS is dependent to large extent on limited clients. Loss of a major client could impact the revenues of LTTS.

Valuation: LTTS trades at 21.0x FY2016 EPS at upper-end of issue price band. On considering (1) strong growth potential of LTTS, which is ahead of some of the industry peers, coupled with (2) 38%+ RoE levels in FY2016, (3) FY2015-16 average cash flow from operations of ₹446cr, (4) strong ~64% dividend payout (translating to ~4% dividend yield), we are of view that LTTS stock has the potential to trade at premium to the peers. However, if we consider the average of the 3 peers, then LTTS stock has been priced at 19% discount. **Given that the LTTS IPO has been priced at discount, we advise SUBSCRIBE.**

Key Financial

Y/E March (₹ cr)	FY15	FY16
Net Sales	2,619	3,067
% chg		17.1
Net Profit	311	417
% chg		33.8
EBITDA (%)	15.2	17.0
EPS (₹)	31	41
P/E (x)	28.1	21.0
P/BV (x)	8.3	8.0
RoE (%)	29.6	38.9
RoCE (%)	33.3	42.2
EV/Sales (x)	1.8	2.2
EV/EBITDA (x)	11.6	12.8

Source: Company, Angel Research; Note: Considered Upper price band of ₹860/share; For EPS and other valuation purposes, we have considered 10.2cr shares o/s

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Issue Open: September 12, 2016
 Issue Close: September 15, 2016

Issue Details

Face Value: ₹2

Present Eq. Paid up Capital: ₹20.3cr

Fresh Issue: 0.0cr Shares

Offer for Sale: 1.04cr Shares

Post Eq. Paid up Capital: ₹20.3cr

Issue size (amount): ₹884-894.4cr

Price Band: ₹850-860

Lot Size: 16 shares and in multiple there-of

Post-issue implied mkt. cap:
 ₹8,643.7cr- 8,745.4cr

Promoters holding Pre-Issue: 100.0%

Promoters holding Post-Issue: 89.8%

Book Building

QIBs	50% of issue
Non-Institutional	15% of issue
Retail	35% of issue

Post Issue Shareholding Pattern

Promoters Group	89.8
DII's/FII's/Public & Others	10.2

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Issue Details

LTTS is offering 1.04cr equity shares of ₹2 each via book building route in price band of ₹850-860/share, entirely comprising offer for sale by current promoters L&T.

Exhibit 1: Shareholding Pattern

Particulars	Pre-Issue		Post-Issue	
	No. of Shares	(%)	No. of Shares	(%)
Promoter Group	101,690,392	100.0	91,290,392	89.8
Retail & HNI Investors	0	0.0	5,200,000	5.1
Institutional Investors	0	0.0	5,200,000	5.1

Source: Company, Angel Research

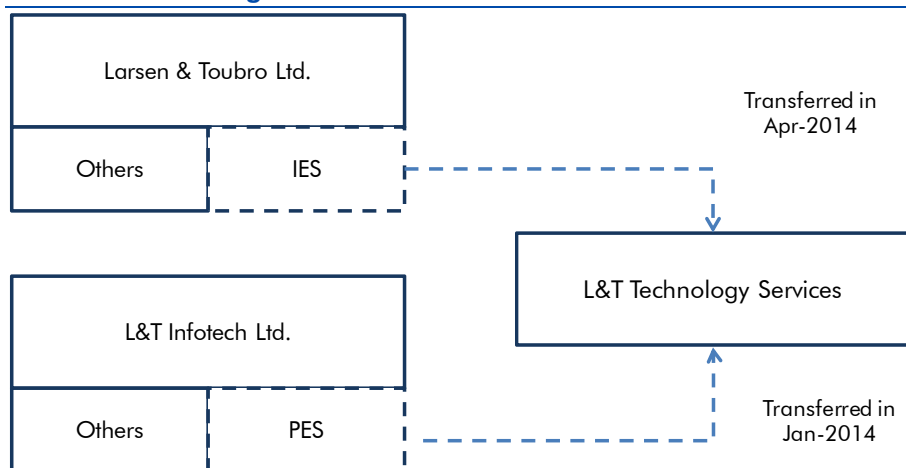
Objects of the Offer

- Objects of the Offer are to achieve benefits of listing equity shares on stock exchanges and to carry out the offer for sale. Listing of equity shares will enhance LTTS's brand name and provide liquidity to existing shareholders. The listing will also provide a public market for the equity shares in India.

About the Company

LTTS, subsidiary of Engineering giant, L&T was incorporated in Jun-2012. Thereafter in Jan-2014, Product Engineering Services (PES) division was transferred from L&T Infotech (LTIL) to LTTS. In Apr-2014, Integrated Engineering Services (IES) division was transferred from the parent to LTTS. As part of restructuring, LTTS brought together engineers with domain expertise in product and process industry from IES and PES to create specialized talent pool in ER&D services. In FY2015, LTTS acquired majority of equity of TSIPL, a company engaged in the business of, software development, IT consulting, software evaluation, design, implementation, research and training in relation to computer software. Further, in FY2015, LTTS also acquired certain of assets and liabilities of Dell Product and Process Innovation Services, Engineering services division of Dell U.S.A., and also acquired its operations in India from Dell India.

Exhibit 2: L&T Background



Source: Company, Angel Research

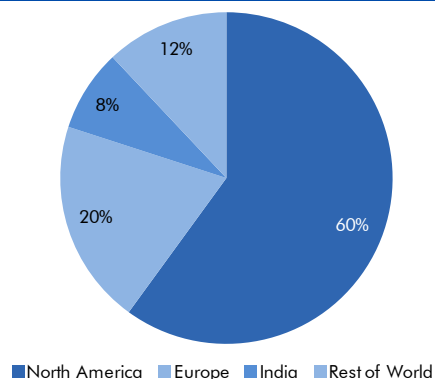
If we look at FY2016 region-wise revenue split then 80% of LTTS revenues were from North America and Europe (NA- 60%, Europe- 20%), 2 large regions of corporate ER&D spend. These 2 regions a/c'ed for 73+% of \$1,007bn corporate ER&D services spend in 2015.

Notably, Top 100 spenders contributed 66% of G500 ER&D spend and LTTS' key global customers include 43 of the top 100 global ER&D spenders.

LTTS mainly operates in 5 key Industry segments, namely, Transportation, Industrial Products, Telecom and Hi-tech, Process Industry and Medical Devices, each represent significant component of G500 ER&D spend.

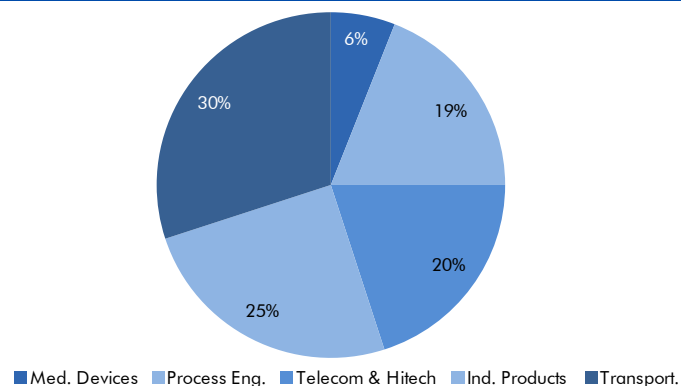
50% of FY2016 revenues were derived from Industrial Products, Process Industry and Medical Devices. These segments represent \$205bn of the G500 ER&D spend and have low penetration by India based third-party ER&D service providers, which gives LTTS competitive advantage.

Exhibit 3: Segment-wise FY2016 revenue mix



Source: Company, Angel Research

Exhibit 4: Industry-wise FY2016 revenue mix



Source: Company, Angel Research

LTTS is considered as one of the world’s leading global pure play ER&D Services Company. As an ER&D service provider, LTTS offers design, development solutions throughout product development chain, provides solutions in areas of Mechanical and Manufacturing Engineering, Embedded Systems, Software Engineering and Process Engineering. For “new” technologies, LTTS provides services and solutions in areas of Product Lifecycle Management (PLM), Engineering Analytics, Power Electronics, M2M connectivity and IoT.

LTTS has invested in IoT, digital technologies (smart products, smart services, smart manufacturing, smart operations) and Lab Infrastructure to strengthen its position in these areas. Key decision makers of LTTS customers belong to Engineering/Product Development/ R&D departments, which tend to have distinct budgets, where industry domain knowledge and focus on R&D is highly critical in the choice of outsourcing ER&D service provider. LTTS is of the view that customers value it as pure-play services provider focused solely on ER&D services, giving them edge over generalist IT service providers who also provide ER&D services.

LTTS is recognized by Zinnov in “leadership zone” in 8 Industry verticals (Industrial Automation, Construction and Heavy Machinery, Medical Devices, Aerospace, Automotive, Rail and Marine, Telecom, Energy and Utilities) & 2 horizontal offerings (Embedded Systems and Mechanical). LTTS is ranked “high” by ARC Advisory Group for deep capabilities in Consumer IoT, Industrial IoT, and Smart Manufacturing.

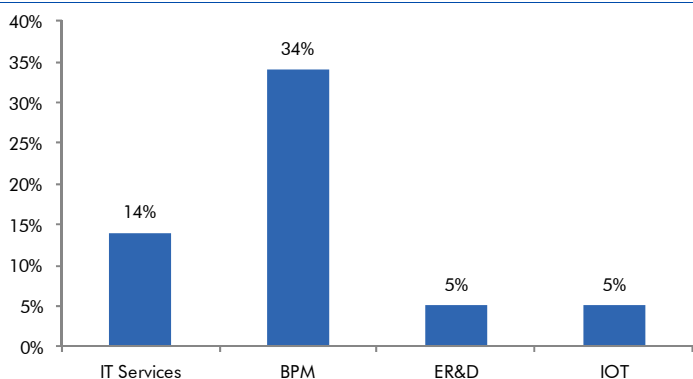
LTTS currently has 12 Global Delivery Centres (GDCs) in India and overseas, 27 Sales offices in India, North America, Europe, Middle East and Asia and 31 Labs in India. LTTS has filed 35 proprietary patents, 134 patents have been filed by our customers along with our employees. As of Jun-2016, LTTS has 9,419 Engineers from 9 nationalities serving 200+ customers, including more than 50 of the Fortune 500 customers.

Investment rationale

ER&D is a large and growing market...

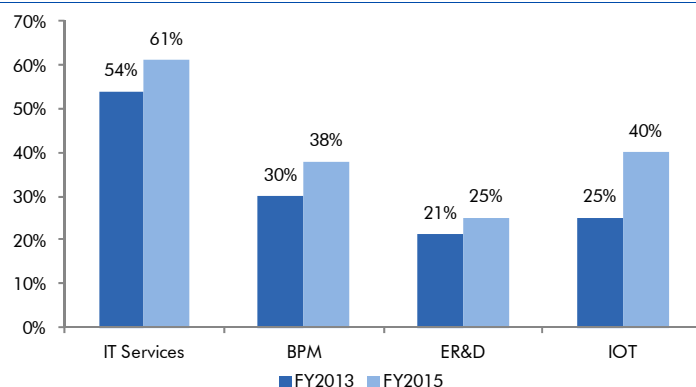
We see huge opportunity for Indian Engineering Research & Development (ER&D) business going forward, on the back of (1) under-penetration seen (as only 2% of global ER&D is outsourced against 14% in IT Services and 34% in BPM) and (2) India's 22% market share of outsourced ER&D portion (against 61% in IT Services and 38% in BPM). Zinnov Consulting highlights that India addresses 40% of the total outsourced Internet of Things (IoT) Technology market and globally the IoT market is expected to grow at 16% CAGR during FY2016-21 to \$253bn. Value addition by Indian vendors and exposure to IoT and Analytics have increased value proposition for the Indian vendors.

Exhibit 5: Share of sourcing in the global spend (%)



Source: Company, Zinnov, NASSCOM, Angel Research

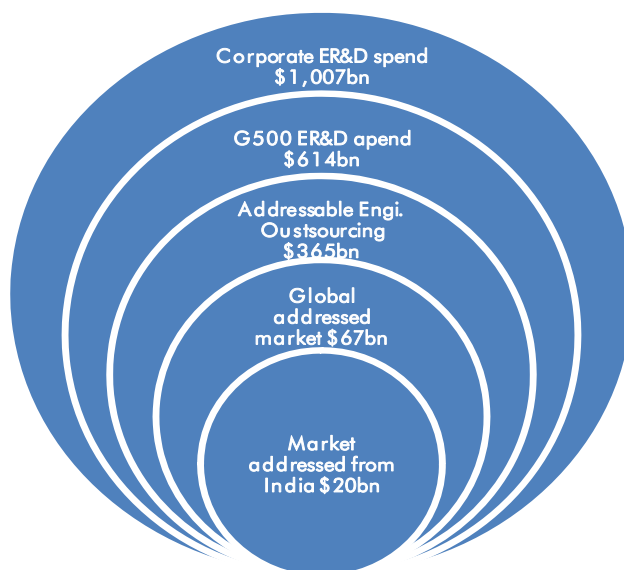
Exhibit 6: India's share in global sourcing (%)



Source: Company, Zinnov, NASSCOM, Angel Research

As per Zinnov only 2% of \$1,007bn of Corporate ER&D spend is being addressed from India, indicating huge growth potential. Zinnov identifies that of the \$365bn

Exhibit 7: Large untapped market



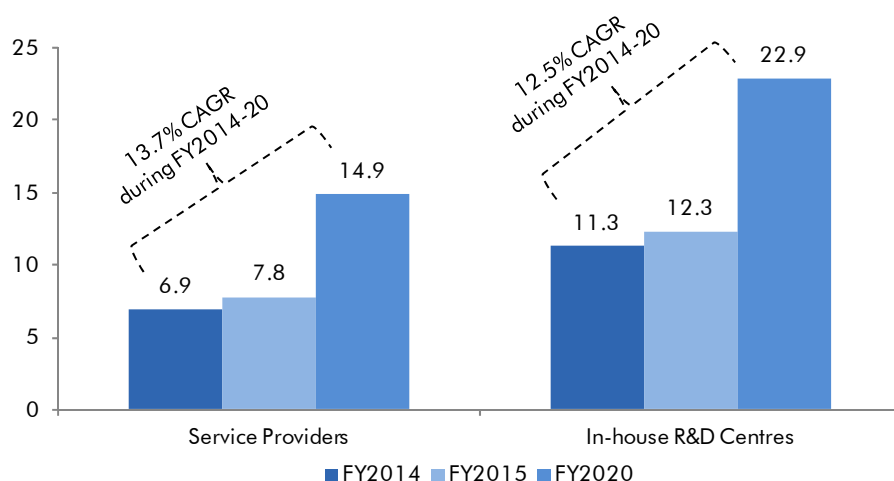
Source: Company, Zinnov, Angel Research

of addressable engineering outsourcing potential, \$215bn is from Product Eng. Services & \$150bn is from Process Eng. Services. Notably, of the \$67bn global addressable market, \$36bn is related to Service Providers and \$31bn is related to Global in-house Centres. Within the \$20bn identified Indian market opportunity, \$7.8bn is for Indian Service Providers.

Following are some of the advantages Indian Service Providers have over global peers: (1) Diversified range of service offerings across verticals (unlike European/NA/ Chinese players who are specialized in Automotive, Aerospace, Software, Internet, Telecom and Energy), (2) Skilled offering at low blended billing rates of \$40-50k/year (vs. \$70-110k/year in NA & Europe).

Indian ER&D market is expected to report 13% CAGR during FY2015-20E to \$38bn. Within Indian ER&D space, Service Providers are likely to report 13.7% CAGR during FY2014-20 to \$14.9bn, faster than 12.5% CAGR expected from In-house R&D centers during the same time period.

Exhibit 8: Service Providers to report 13.7% CAGR during FY2014-20



Source: Company, Zinnov, Angel Research

LTTS, a leading global pure-play ER&D player...

LTTS in last 3 years has emerged as one of the largest pure-play ER&D players in India with a delivery model having strong offshore presence in India. LTTS has built a global delivery model, with ~80% of its revenues booked from 2 of the largest global markets, i.e. US and Europe.

Despite having presence across diversified verticals, strong market positioning across low competitive verticals like, Industrial, Process has helped the company scale operations, which can be seen from their FY2016 turn-over of ₹3,067cr, and manpower of 9,419 Engineers who are serving 200+ customers.

Zinnov in its 2015 report, has recognized LTTS in “leadership zone” in 8 Industry verticals (Industrial Automation, Construction and Heavy Machinery, Medical Devices, Aerospace, Automotive, Rail and Marine, Telecom, Energy & Utilities) and 2 horizontal Service offerings (Embedded systems and Mechanical).

Exhibit 9: Leading global pure-play ER&D company



Source: Company, Zinnov, Angel Research

LTTS end-to-end engineering expertise backed by its parent's engineering heritage of 75+ years provides it with competitive edge over other ER&D players. Strong parentage has helped (1) LTTS in attracting and retaining quality talent (reported lower than industry attrition of 12-13%), (2) benefit from parents global network in exploring business opportunities and getting direct access to senior decision makers in potential end customers (~95% of business is repeat business).

LTTS, to pursue Multi-pronged growth strategy...

LTTS has been carved out of L&T’s IES and L&T Infotech’s PES division in 2014. If we just take segmental revenues from both entities, before LTTS was carved out, then LTTS reported 23.1% revenue CAGR during FY2013-16 to ₹3,066cr. This growth is after reducing ₹111cr of revenues in FY2016 for some non-performing accounts. LTTS is pursuing multi-pronged growth approach, which in our view could possibly drive the earnings growth, going forward.

LTTS is pursuing multi-pronged growth strategy, which includes (a) Focus on key Segments, Verticals and Geographies, (b) mine existing customers and add new customers, (c) Focus on Solutions-oriented Engineering services, (d) continued investment towards innovation labs, (e) pursue selective acquisitions, and (f) Attract and retain employees

Focus on key Segments, Verticals and Geographies

LTTS focuses to pursue growth strategies to expand its market share across key segments, verticals, geographies and solutions.

Currently LTTS is focusing on (1) Automotive (reported under Transportation) and (2) all verticals categorized under Industrial Products, Consumer Electronics and Product software (forms part of Telecom, Hi-tech) segment.

In Automotive vertical, LTTS would focus on software-based engineering solutions, which will supplement its traditional strength in Auto-mechanics area. Area which LTTS intends to expand in Automotive space include, Telematics, Advance driver assist systems, V2X communication (includes vehicle-to-vehicle and vehicle-to-infrastructure intelligent control and connectivity systems), Green Technologies (hybrid vehicles, battery management systems), Infotainment and Body electronics.

In Industrial products segment, LTTS plans to expand its offerings in IoT-enabled smart products, Renewable Energy space with focus on storage, Grid connectivity, Energy efficiency for Buildings. In Customer Electronics vertical, LTTS would focus on Wearables, Connected Homes (Smart Homes), Camera and Security devices.

Geographically LTTS would continue to focus on North America and Europe, which happen to be the 2 largest markets. Also, LTTS is working on setting-up Labs/ Development Centres in close proximity to its customers' offices. LTTS is keen to focus on Austria, Switzerland markets and also establish a Delivery centre at East Europe. LTTS is also keen to expand its operations in Japan, as number of its existing and prospective Automotive customers are based in Japan.

Mine existing customers, develop new Customer relationships

Top 20 customers of LTTS contributed ~54% of FY2016 revenues (vs. ~56% in FY2015). LTTS boasts to serve 43 of top 100 global ER&D spenders, representing 66% of G500 ER&D corporate spending budget (Source: Zinnov). This indicates huge opportunity awaiting for the pure play ER&D companies.

Exhibit 10: Sourcing share in global spend (%)

Customer Revenue (\$ mn)	No. of Customers- FY2016	No. of Customers- FY2015
20+	3	2
10-20	8	8
5-10	17	16
>1-5	44	41

Source: Company, Zinnov. NASSCOM, Angel Research

Exhibit 11: Customer Concentration details...

Customer Concentration	FY2016	FY2015
New customers added	36	8
Revenue from new customers (%)	5.4	1.3
Repeat business (%)	94.6	98.7

Source: Company, Zinnov. NASSCOM, Angel Research

Over the next few years, Top 100 ER&D spending is expected to grow in to a large market opportunity for LTTS. With majority of LTTS clients belonging to the sub-\$5mn category (61% of the clients as of FY16), there exists scope for increase in client mining, which could contribute to the long-term growth of LTTS. Also, 36 of these total 72 clients added in FY2016, contributed only 5.4% of the total FY2016 revenues of ₹3,067cr.

LTTS is implementing a "T30:A3" model, whereby top customer a/c's (contributing in \$10mn revenue bracket) have been identified under T30 model and are developing relationships with adjacent customers, which are identified under A3 model (those with potential to be scaled to \$5mn of yearly revenues). Here, LTTS is identifying potential opportunities from within the same verticals and engage them in cross-selling of solutions. Further, LTTS seeks to provide value-added solutions by leveraging its in-depth industry expertise and then expanding the breadth of services offered to them beyond those in the initial engagement.

Also LTTS aims to leverage its employee's domain expertise in different services to offer their customers multiple services and solutions under single engagement. For example, one of their strategies is to structure large, long term deals with customers, with defined time periods for execution. These deals would help the company to improve their productivity and provide better revenue visibility.

Focus on Solutions-oriented Engineering services...

Based on its experience of having served clients in Digital Engineering, Mobile Internet, IoT (IIoT, mBioT), Knowledge Automation, Advanced Robotics, Autonomous and near-autonomous Vehicles, Energy efficiency and Imaging and Video solutions space, the company as a natural progression is building its portfolio of Solutions-Oriented Engineering Services across verticals.

A logical extension of their strategy in our view is to develop industry-specific use cases and then customize these solutions as per specific individual customer requirements. In order to achieve this goal, LTTS is already in the process of building and strengthening its alliances with the technology companies.

Higher investment towards Innovation labs...

LTTS has been continuously investing in innovation labs since its establishment and currently has 31 such labs (located in Bengaluru, Mumbai, Mysore, Vadodara and Chennai). LTTS also intends increase the scope of its existing labs by adding space/ equipment to its existing labs to broaden their capabilities and address customer needs. LTTS has highlighted that it would continue to invest towards the innovation labs, which would help them provide competitive advantage to its peers.

Expand business through selective acquisitions...

LTTS has pursued the inorganic growth strategy to grow its business. To-date it has done 2 acquisitions. In Jun-2014, LTTS acquired 74% stake in TSIPL (Indian subsidiary of Thales) to further strengthen its expertise in Transportation segment, especially in the embedded avionics. Thereafter in Jul-2014, LTTS acquired certain assets and liabilities of Dell India and in Nov-2014, acquired certain assets and liabilities of Dell USA, which added 3 delivery centers in US to LTTS's portfolio. These acquisitions strengthened LTTS's global ER&D position in Transportation segment, widened the reach through local delivery centers and enhanced the talent pool with addition of 200+ engineers to the workforce.

LTTS has further indicated that it would pursue selective acquisitions, strategic alliances that provide it access to better infrastructure, industry knowledge, technology expertise, geographical reach and allows it to expand to their vertical offerings and customer base.

LTTS also intends to pursue acquisitions outside India in order to expand their global footprint by leveraging low cost offshore delivery model and move greater portion of their work offshore to India.

LTTS at FY2016-end is sitting on Debt of ₹195.5cr, reflecting Debt/Equity ratio of 0.2x. During FY2015-16, LTTS generated ₹822cr of Cash flow from operations. Considering BS strength, cash generating potential from the current business, LTTS

is well positioned to pursue mid to small size acquisitions, without putting much of stress on the balance sheet.

Attract, retain highly-skilled employees...

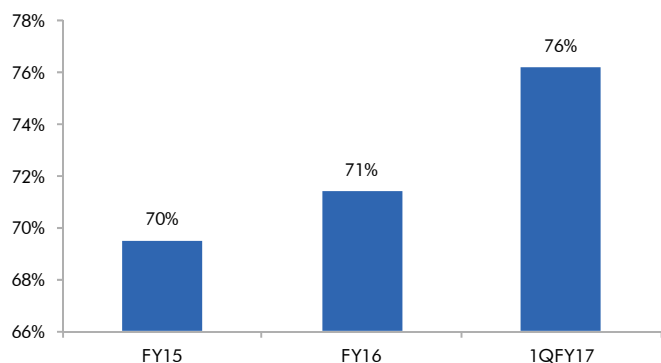
As of Jun-2016, LTTS has 9,419 Engineers with average age of 31 years, serving 200+ customers. LTTS runs various programs and has been proactive in attracting, retaining quality talent (reported lower than industry attrition of 12-13%).

Company pursuing multi-pronged growth strategy augurs well for its long-term growth prospects.

Operational levers to aid Margin expansion...

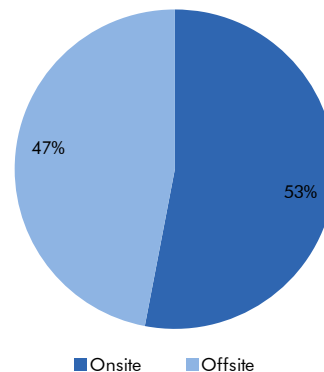
We sense LTTS has multiple operating levers, which could aid its margin expansion, going forward.

Exhibit 12: Utilization rates on uptrend...



Source: Company, Angel Research

Exhibit 13: Onshore-Offshore mix to improve...



Source: Company, Angel Research

Revenues from 36 clients added contributed just 5.4% to FY2016 revenues, indicating that there exists possibility for further client mining from these newly acquired customers. As a result, we expect Utilization rates in next few quarters to improve from the 76% reported in 1QFY2017.

At FY2016-end, LTTS reported onshore-offshore mix of 53%:47%. With company focusing on more of client mining, and maturity in the processes to be attained going forward from these projects, there again exists possibility of favourable movement in the onshore-offshore mix.

Further, LTTS has drawn strategy to focus on Solutions Oriented Engineering services approach. As a result, it could focus on cross-selling existing offerings to newer customers with some customization (as per requirement). This strategy in the long-run would aid in gradual margin expansion.

Another margin expansion lever, LTTS has in its kitty is focus on the fast growing, low competition verticals, like Industrial Products, Process Engineering, and Medical Devices. Usually billing rates across these segment tend to stand higher than other verticals, where more competition exists. Favourable shift in the mix towards high billing and margin business could aid LTTS's margin expansion strategy in the long-run.

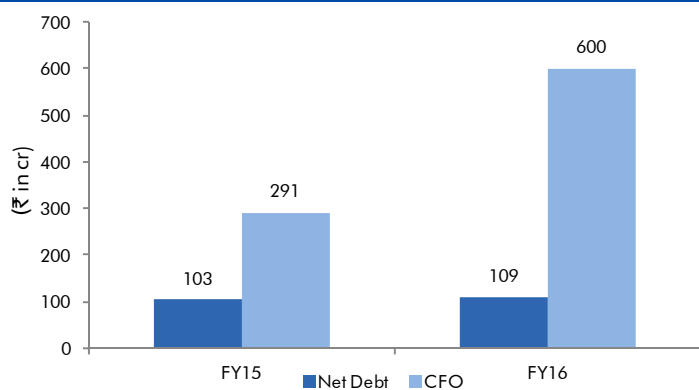
Strong Financials and Balance Sheet Strength...

LTTS reported 17.1% yoy top-line growth in FY2016, driven by higher repeat business. Shift in business mix (higher contribution from the high margin business), improvement in yoy utilization rates (from 69.5% in FY2015 to 71.4% in FY2016) and better onshore-offshore mix (from 48%:52% in FY2015 to 47%:53% in FY2016) helped the company report 174 bps improvement in its EBITDA margins to 17% in FY2016.

We expect such strong performance to continue on the back of LTTS's leadership position in the higher growth ER&D verticals, and operating levers to continue to aid the margin expansion.

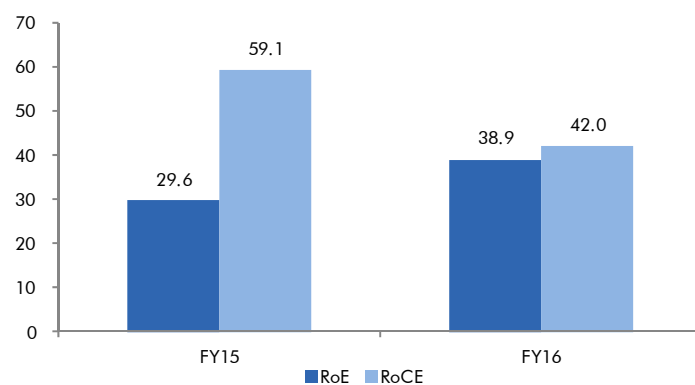
LTTS has an unlevered balance sheet as of FY2016, given their D/E ratio at 0.2x (with debt o/s at ₹195cr). LTTS in last 2 years generated cash flow from operations to the tune of ₹822cr (average for FY2015-16 at ₹411cr). Comfortable balance sheet, strong cash flow generating potential of the business suggests that LTTS could go ahead with small to mid size strategic acquisitions.

Exhibit 14: Strong Cash Flow from Operations potential



Source: Company, Angel Research

Exhibit 15: Impressive RoEs...



Source: Company, Angel Research

Risks & Concerns

1. For large clients willing to set-up their own captive R&D centers could act as a big threat to company's business. This could also lead to loss of business.
2. LTTS is dependent to large extent on limited number of customers. On loss of a major client, LTTS could see decline in the company's revenues.

Outlook and Valuation

LTTS reported 17.1% yoy top-line growth in FY2016, driven by higher repeat business. LTTS is pursuing multi-pronged growth strategy of (1) focusing on key segments, verticals and geographies, (2) mining the existing customers, add new customers, (3) Focus on Solutions-oriented engineering, (4) continued investment towards innovation labs, (5) expand business through selective acquisitions, and (6) retain skilled employees, all augur well for long-term growth prospects of the company. LTTS on the back of its leadership position in the high growth ER&D space should be able to report strong revenue growth, going forward.

Continued shift in business mix (with high contribution from high margin business), likely improvement in yoy utilization rates, better onshore-offshore mix should help LTTS continue to report EBITDA margin expansion.

For comparison purposes, we have considered Tata Elxsi, Geometric, and Cyient.

Tata Elxsi generates >70% of revenues from Embedded product development and the remaining from Systems Integration, Industrial design, Visual Effects and Animation business (this segment's contribution to the total revenues over the years has been declining). Tata Elxsi is highly dependent on Transportation vertical, especially Automotives segment. During FY2014-16, Tata Elxsi reported 18.0% top-line CAGR to ₹1,075cr. High contribution from high margin Embedded product development segment, better onshore-offshore mix helped the company report 210bps EBITDA margin improvement during the same period to 23.0% and 46.4% PAT CAGR to ₹155cr.

Exhibit 16: Peer group comparison

	Sales		Adj. PAT		Rev. CAGR (FY14-16)	PAT CAGR (FY14-16)	EBITDA %		PAT %		RoE %		P/E FY16
	FY15	FY16	FY15	FY16			FY15	FY16	FY15	FY16	FY15	FY16	
LTTS	2,619	3,067	311	417	20.0%	NA	15.2	17.0	11.9	13.6	29.6	38.9	21.0
Tata Elxsi	849	1,075	102	155	18.0%	46.4%	20.9	23.0	12.0	14.4	36.0	40.1	46.9
Geometric	1,105	1,234	55	105	6.1%	51.0%	12.1	14.3	5.0	8.5	13.5	22.2	14.4
Cyient	2,736	3,096	353	333	18.4%	11.9%	13.9	13.3	12.9	10.8	19.2	17.4	16.2
Average							15.6	16.9	10.0	11.2	22.9	26.6	25.8

Source: Company, Angel Research; Note: NA – Not available

Geometric offers a portfolio of Global Engineering Services, Product Lifecycle Management (PLM) Solutions, Embedded System Solutions, and Digital Technology Solutions. Software services a/c for >60% of revenues, with remaining from Engineering Services. Geometric is pre-dominantly focused on 3 verticals namely, Automotive, Industrial Heavy Equipment and Aerospace and Defense. During FY2014-16, Geometric reported 6.1% top-line CAGR to ₹1,234cr. Shift in business mix towards high realization areas, improvement in utilization, helped Geometric report 224bps EBITDA margin expansion during the same period to 14.3% and report 51% PAT CAGR to ₹105cr.

Cyient, one of the closest competitor to LTTS is the market leader in Engineering Services space (accounted for >60% of revenues), especially in Aerospace and

Railways verticals. Data Transformation, Network & Operations (DNO) for Communication Service Providers and Utilities account for remaining revenues. During FY2014-16, Cyient reported 18.4% top-line CAGR during to ₹3,096cr, led by 3 acquisitions. Revenue growth from organic business has been flat owing to client specific issues. Pricing pressure, shift in business mix (towards low margin business), re-investment in restructuring, acquisition of low margin business led to 61bps EBITDA margin decline during the same period to 13.3% and just 11.9% PAT CAGR to ₹333cr.

LTTS fares better on all the above-mentioned metrics, given the 20.0% revenue CAGR seen during FY2014-16, and strong earnings growth. Such strong financial performance is driven by (1) new client additions, (2) mining of existing clients, and (3) improvement in the utilization and onshore-offshore mix.

Again on considering Zinnov's view of leadership position in 8 verticals, and more operating levers in place, we are optimistic about LTTS continuing to perform strongly, going forward (glimpse of it is already seen in the 1QFY2017 numbers, EBITDA/ PAT margins were at 19.3%/14.8% in 1QFY2017 vs. 17.0%/13.6% in FY2016).

On the back of strong financial performance, LTTS reported impressive RoE's of 29.6%/38.9% for FY2015/16. This is against peers FY2016 RoE's in the range of 13.5% (Geometric)-40.1% (Tata Elxsi).

LTTS trades at 21.0x FY2016 EPS at upper-end of issue price band. On considering (1) strong growth potential of LTTS, which is ahead of some of the industry peers, coupled with (2) 38%+ RoE levels in FY2016, (3) FY2015-16 average cash flow from operations of ₹446cr, (4) strong ~64% dividend payout (translating to ~4% dividend yield), we are of view that LTTS stock has the potential to trade at premium to the peers. However, if we consider the average of the 3 peers, then LTTS stock has been priced at 19% discount. **Given that the LTTS IPO has been priced at discount, we advise SUBSCRIBE.**

Profit & Loss Statement (Consolidate)

Y/E March (₹ cr)	FY15	FY16
Net Sales	2,619	3,067
% Chg		17.1
Total Expenditure	2,220	2,546
Operating Expenses	230	266
Employee benefits Expense	1,487	1,723
Other Expenses	503	557
EBITDA	399	520
% Chg		30.5
EBIDTA %	15.2	17.0
Depreciation	48	59
EBIT	350	462
% Chg		31.7
Interest and Financial Charges	3	2
Other Income	25	76
EBT & exceptional items	372	535
Exceptional Items	0	0
EBT	372	535
Tax Expenses	61	119
% of PBT	16.4	22.2
PAT	311	417
Minority Interest loss/ (Income)	(0)	0
PAT after MI	311	417
% Chg		33.8
PAT %	11.9	13.6
Diluted EPS	30.6	41.0
% Chg		33.8

Balance Sheet (Consolidate)

Y/E March (₹ cr)	FY15	FY16
Sources of Funds		
Equity Capital	1,050	1,050
Reserves & Surplus	2	43
Networth	1,052	1,093
Total Debt		
Total Debt	219	195
Deferred Tax Liabilities (net)	0	0
Other Long-term Liabilities & Prov.	7	19
Total Liabilities	1,278	1,307
Application of Funds		
Gross Block	562	628
Accumulated Depreciation	61	120
Net Block	1,064	1,160
Goodwill	8	8
Investments	0	56
Current Assets		
Inventories	175	147
Sundry Debtors	685	727
Cash and Bank Balance	115	86
Loans & Advances	232	234
Other Current Asset	0	0
Current Liabilities	537	614
Net Current Assets	671	581
Deferred Tax Assets	37	36
Total Assets	1,278	1,307

Cash Flow Statement (Consolidate)

Y/E March (₹ cr)	FY15	FY16
Profit before tax	372	535
Depreciation & Other Non-cash Charges	48	59
Change in Working Capital	(64)	151
Interest & Financial Charges	2	(1)
Direct taxes paid	(67)	(145)
Cash Flow from Operations	291	600
(Inc)/ Dec in Fixed Assets	(53)	(127)
(Inc)/ Dec in Investments & Oth. Adj.	(614)	(52)
Cash Flow from Investing	(667)	(179)
Issue/ (Buy Back) of Equity	547	0
Inc./ (Dec.) in Borrowings	170	(23)
Dividend Paid (Incl. Tax)	(250)	(358)
Interest Expenses & Oth. Adj.	(3)	(2)
Cash Flow from Financing	464	(383)
Inc./ (Dec.) in Cash & forex translation	86	(29)
Opening Cash balances	29	115
Closing Cash balances	115	86

Ratio Analysis

Y/E March	FY15	FY16
Valuation Ratio (x)		
Adj. P/E (on FDEPS)	28.1	21.0
Adj. P/CEPS	24.3	18.4
Dividend yield (%)	4.9	4.7
EV/Sales	1.8	2.2
EV/EBITDA	11.6	12.8
EV / Total Assets	0.4	0.6
Per Share Data (₹)		
Adj. EPS (fully diluted)	30.6	41.0
Cash EPS	35.4	46.8
DPS	41.8	40.3
Book Value	103	107
Returns (%)		
RoCE (Pre-tax)	33.3	42.2
Angel RoIC (Pre-tax)	27.3	35.3
RoE	29.6	38.9
Turnover ratios (x)		
Total Asset Turnover (x)	2.0	2.3
Inventory / Sales (days)	24	18
Receivables (days)	96	87
Payables (days)	75	73
WC (days)	45	31
Leverage Ratios (x)		
D/E ratio (x)	0.2	0.2

Source: Company, Angel Research; Note: Considered Upper price band of ₹860/share; For EPS and other valuation purposes, we have considered 10.2cr shares o/s

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