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KPIT Technologies Ltd.

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Gaining competency to provide scale

KPIT Technologies (KPIT) is focused on providing IT consulting and product engineering solutions & services to automotive, manufacturing, energy & utilities and life sciences companies. It has a strong workforce of more than 10,500 employees across the globe. The company has a wide geographical presence with 10 development centers and 34 offices across 16 countries.

Investment Rationale

Traction in automotive engineering; key to growth: In the automotive industry, there is a growing demand for connected mobility and digital technologies. This has triggered huge investment in the internet of things (IoT) space. It is estimated that by 2030, up to 15% of the new cars will be fully autonomous and this will trigger demand for advanced driver assistance solutions (ADAS) technology. Given, KPIT's dominance in the automotive engineering space with more than 25 patents in the ADAS and powertrain space will augur well for the company. Further, to meet the growing demand for connected mobility, KPIT has invested in enterprise cost management (ECM) and advanced simulation areas in mechanical engineering, which are fast gaining traction and resulting in deal wins. It is also investing in enhancing its core competencies across offerings such as connectivity, cybersecurity, IoT/mobility services and analytics.

Gaining competence in the digital technology: KPIT is gaining traction in the digital technology space with the contribution of the total digital revenue increasing to 15% in FY16 from 12% in FY15. KPIT's digital transformation solutions are focused on cloud, social, big data & analytics and IoT/machine to machine communication (m2m). To cater to the growing demand for digital technologies, the company is building capabilities in new technologies with special emphasis on IoT. We expect the company to benefit owing to its ongoing investments in this space which provides us confidence of continued traction in large deals going ahead.

Traction in SAP SBU to drive further growth: SAP SBU (strategic business unit) contributed ~23% to the overall revenue in FY16. To further strengthen its position in SAP, the company has expanded its offerings to include cloud based technologies like SuccessFactors, CEC, Hybris, CPQ and other emerging technologies like HANA, Hadoop and IoT. This is already yielding results with the company delivering 15% revenue growth in FY16 as against a degrowth in FY15. Further, this has provided the company with the first mover advantage and has resulted in deal wins in this space. It has a robust pipeline in SuccessFactors. With the company's continuous focus on strengthening its position in the business through technological advancements, we expect robust revenue growth from SAP SBU going ahead.

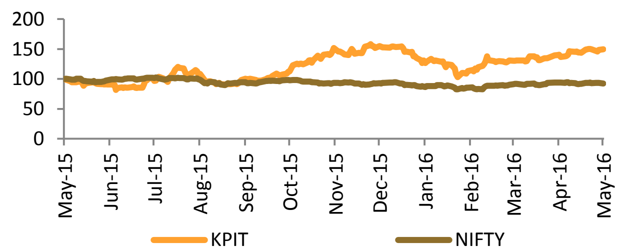
Valuation: The huge investment towards building technologies and solutions in the automotive and manufacturing space, will aid growth and provide scalability to KPIT. We expect revenue and Adj. PAT to grow at a CAGR of ~10% and ~12% over FY16-18E. We initiate coverage on the stock with a BUY rating with a target price of Rs. 189 (based on FY18E P/E of ~9.6x), implies a potential upside of ~15% over the next 1 year.

Market Data	
Rating	**BUY**
CMP (Rs.)	164
Target (Rs.)	**189**
Potential Upside	~15%
Duration	Long Term
Face Value (Rs.)	2
52 week H/L (Rs.)	175.8/85.1
Adj. all time High (Rs.)	175.8
Decline from 52WH (%)	6.7
Rise from 52WL (%)	92.7
Beta	0.5
Mkt. Cap (Rs.Cr)	3,236

Fiscal Year Ended

Y/E	FY15	FY16	FY17E	FY18E
Revenue (Rs.Cr)	2,990	3,224	3,517	3,876
Adj. Net profit (Rs.Cr)	237	293	325	368
Adj. EPS (Rs.)	12.3	15.6	17.2	19.6
Adj. P/E (x)	13.3	10.5	9.5	8.4
P/BV (x)	2.4	2.2	1.8	1.5
ROE (%)	18.4	21.9	21.2	19.9

One year Price Chart



Shareholding Pattern	Mar-16	Dec-15	Chg.
Promoters (%)	16.8	17.2	(0.4)
Public (%)	78.3	77.8	0.5
Others (%)	4.9	-	-

KPIT Technologies Ltd: Business overview

The company caters to various industries viz; automotive, manufacturing (life science, medical devices, industrial manufacturing), energy & utilities, hi-tech, government & defense.

KPIT Technologies (KPIT) is focused on providing IT consulting and product engineering solutions and services to automotive, manufacturing, energy & utilities and life sciences companies. Leveraging its technology and domain prowess, KPIT has long standing partnerships with 200+ global corporations. The company caters to various industries viz; automotive, manufacturing (life science, medical devices, industrial manufacturing), energy & utilities, hi-tech, government & defense. With over two decades of experience, the company has become a specialized provider of software solutions to automotive & transportation companies. Its clear focus on automotive and transportation vertical can be gauged from its patents fillings. It has filed 53 patents till date.

The company has received 23 patents globally (as on Q4FY16) largely in areas of hybrid technology along with some others in VLSI and High Performance computing. Besides, it has a strong workforce of more than 10,500 employees across the globe. The company has a wide geographical presence with 10 development centers and 34 offices across 16 countries.

KPIT's products & platforms

Tools	**K-SAR** Worlds' FIRST AUTOSAR R4.0.3 Solution Basic Software Stack Rapid Prototyping Platform | ARTOP | EUCD NOS	**In2Soft** A KPIT Cummins Company Vehicle Diagnostics Tools	medini™ Functional Safety Tool Chain
Platforms	**KIVI** KPIT In-Vehicle Infotainment	**Konnect** Connectivity: Device to Car / Device to Appliance	**KPIoT** KPIT IoT, Big Data and Analytics Platform
Products	**BMS** Battery Management Systems	**ITS** KPIT Intelligent Transport System for Smarter Mobility	**REVOLO®** hybrid solution for everyone Plug In Parallel Hybrid Solution

Source: Company

Sharp focus on automotive engineering augurs well

KPIT has long standing relationships with more than 35 leading global automotive manufacturers and 40+ prominent Tier 1 & 2 suppliers to automotive OEMs.

The automotive and transportation vertical is the largest contributor to the overall revenue at 39.7% in FY16. KPIT is the leading player in the automotive engineering space and is the largest third party vendor for automotive electronics in India. The company provides both business IT and engineering solutions for its clients. It has long standing relationships with more than 35 leading global automotive manufacturers and 40+ prominent Tier 1 & 2 suppliers to automotive OEMs. It has helped them in over 300 production programs. KPIT provides solutions in the areas of navigation, automotive infotainment, telematics, semiconductors among others.

In the automotive industry, there is a growing demand for connected mobility and digital technology. The connected car market includes infotainment, apps designed for cars, digital diagnostics, monitoring services for new drivers and enhanced navigation systems. The growing demand of connected mobility in the automotive industry has triggered huge investment in the IoT space. It is estimated that by 2030, up to 15% of the new cars are expected to be fully automated. Further, this will drive demand for advanced driver assistance solutions (ADAS) technology and safety features such as parking assistance, alert systems for approaching vehicles, people and objects, traffic congestion assistance, lane departure warning and cruise control.

The global automotive safety systems market is expected to grow at a CAGR of ~9% over the next few years. As cars become more connected, software competency will provide an edge and open huge opportunities for the service providers.

KPIT has a dominance in the automotive engineering space. Currently, the company has more than 25 patents in the ADAS and powertrain space and is planning to create more intellectual properties (IPs) in the space. In order to meet the growing demand for connected mobility, KPIT has invested in enterprise cost management (ECM) and advanced simulation areas in mechanical engineering, which are fast gaining traction and resulting in deal wins. The company is further investing in enhancing its core competencies across offerings such as connectivity, cybersecurity, IoT/mobility services and analytics. The growing demand for products engineering will augur well for the company.

Traction in performance of Revolo & ITS will be a key trigger

KPIT, over the years, has developed a product - Revolo which is a smart, plug-in (parallel hybrid solution) for automobiles that runs vehicles with batteries in tandem with the motor. This improves fuel efficiency by 35%, reduces emission by 30% and resulting in saving up to 25% of travel cost. The company has achieved a significant milestone for Revolo in FY16 as it has developed an indigenous technology for smart electric bus. It is also in talks with various OEMs and buses body builders for this product. It is also planning to sell this product outside India. However, this is yet to gain traction. Besides, the company is witnessing traction in its ITS solutions (Intelligent transport system) that offers features such as automatic vehicle location and vehicle health monitoring & diagnostics for buses. Currently, more than 5000 buses are fitted with KPIT's UBS II ITS devices. Further, the company has a robust deal pipeline of 10,000 buses for this solution. After increasing acceptance of its ITS solutions in India, the company is planning to sell its ITS solutions outside India.

Gaining competence in digital technology to drive growth

KPIT's digital practice is spread across all SBUs and its digital transformation solutions are focused on cloud, social, big data & analytics and internet of things (IoT)/machine to machine communication (m2m).

KPIT continues to invest heavily in digital technology space, which is expected to drive growth in the long term. This is evident from 15%+ overall growth in digital revenue in FY16 taking the overall contribution to 15% of sales in FY16 from 12% in FY15. KPIT's digital practice is spread across all SBUs and its digital transformation solutions are focused on cloud, social, big data & analytics and internet of things (IoT)/machine to machine communication (m2m). The contribution from digital transformation (DT) SBU (erstwhile Enterprise Solutions SBU) stood at 9.7% in FY16. The primary areas driving growth in digital transformation are integrated fleet management, asset tracking and digital inventory, supply chain optimization, Big Data & Real time streaming analytics and application modernization. KPIT has collaborated with leading providers of cloud, collaboration platforms, mobile and data framework and content management systems to sale the business. Further, it has developed various products in the areas of fleet management, asset management, supply chain management, energy management and workforce analytics. **The company's investments in the digital space is bearing fruit which is visible from deal wins in this space.**

Digital transformation solutions

	Automotive	Manufacturing	E&U
Digital Customer Experience	• Social Activity Tracking & Reporting Platform • Website Click Activity Tracker	• Social Activity Tracking & Reporting Platform • Website Click Activity Tracker • Web Experience and Digital Marketing Platform • Digital Marketing Services & Staffing	• Social Activity Tracking & Reporting Platform • Website Click Activity Tracker • Web Experience and Digital Marketing Platform • Utility Customer Service & Payment Portal
Digital Operations	• Mobile Enabled Warehouse Management Solution • Stock Taking & Product Ordering • Connected Office	• Mobile Enabled Field Workforce Management • Mobile Enabled Warehouse & Inventory Management • Stock Taking & Product Ordering • SSO Reporting & Collaboration Portal • Connected Office	• Mobile Enabled Workforce Management Solution • SSO Reporting & Collaboration Portal • Connected Office • Utility Work Order Management Solution
Transformed Business	• In-Vehicle Apps (Infotainment) • Integration Platform • Device Connectivity Framework for Vehicles • Detect and Prevent Vehicle Failures • Remote Data and Diagnostics for Predictive Service	• Enterprise Content Management Solutions • Remote Data and Diagnostics for Predictive Service	• Vendor/Customer eCommerce Marketplace Solution • Remote Data and Diagnostics for Predictive Service

Source: Company

Building expertise in manufacturing space to provide scale

KPIT has a rich clientele in this vertical servicing more than 200 customers (40 among the fortune 1000 customers).

Manufacturing vertical contributed ~36% to overall revenues in FY16. It is further divided into 3 distinct sub-verticals viz; Industrial & Consumer Products, Hi Tech and Life Sciences. KPIT has a rich clientele in this vertical servicing more than 200 customers (40 among the fortune 1000 customers). The company provides technological solutions that help its customers to reduce time to market, control manufacturing operations better, and deliver superior experiences to customers.

It is expected that the global product and service market will touch USD 5.6 bn by 2019, thus providing huge growth opportunities.

The growing demand for digital technologies and IoT solutions is triggering higher usage of mobile technology in the manufacturing sector, leading to factory visibility, connected supply chain, driving automation among others. It is expected that the global product and service market will touch USD 5.6 bn by 2019, thus providing huge growth opportunities. The company has already made huge investments in this space aligned towards engineering abilities (digital transformation in product), business IT expertise (digital transformation in process), building strategic platforms, technologies and solution offerings focused on IoT, Social ERP, P2P automation etc. The company's oracle accelerate and IoT solutions for manufacturing industry is focused towards field service and mobility. This will provide the company a strong foothold and scalability.

Traction in SAP SBU to drive further growth

To further strengthen its position in SAP, KPIT has expanded its offerings to include cloud based technologies like SuccessFactors, CEC, Hybris, CPQ and other emerging technologies like HANA, Hadoop and IoT.

KPIT provides full spectrum of SAP applications. SAP SBU contributed ~23% to the overall revenue in FY16. To further strengthen its position in SAP, the company has expanded its offerings to include cloud based technologies like SuccessFactors, CEC, Hybris, CPQ and other emerging technologies like HANA, Hadoop and IoT. This is already yielding results with the company delivering 15% revenue growth in FY16 as against a degrowth in FY15. Further, this has provided the company with the first mover advantage and has resulted in deal wins in this space. It has a robust pipeline in SuccessFactors. With the company's continuous focus on strengthening its position in the business through technological advancements, we expect robust revenue growth from SAP SBU going ahead.

Client mining strategies is expected to aid growth

The company has added 10 new customers in FY16, taking its active customers base to 218.

The client addition remains modest in FY16 as the company added 10 new customers, taking its active customers base to 218. However, KPIT's top client - Cummins continues to reel under pressure (revenue contribution declined to 14.1% in FY16 from 15% in FY15). To offset the pressure, the company is focusing on developing different offerings, which are more domain intensive. The company is developing its expertise and capabilities in new technologies mainly across engineering, digital, IoT and IMS space. This is providing traction and is resulting in deal wins. Further, the company is shifting strategy by focusing on verticals rather than services. This is a reflection of KPIT's ability to deepen its client engagements. It is also hiring more account managers to focus on its large clients.

Revenue & Adj. PAT to grow at a CAGR of ~10% and ~12% respectively over FY16-18E

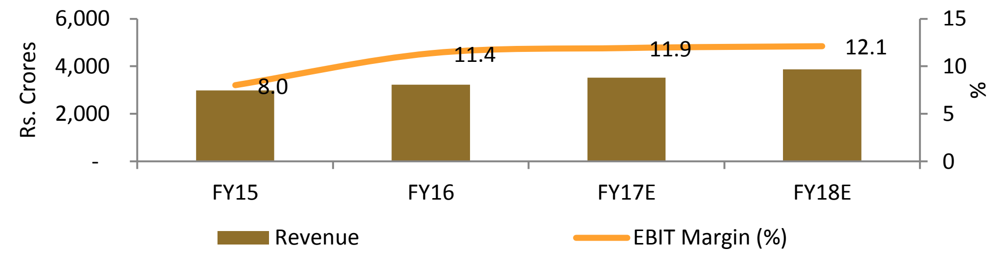
KPIT's dominance in the automotive engineering will provide traction and scalability to its business.

We expect KPIT's revenue to grow at ~10% CAGR over FY16-18E. The company's dominance in the automotive engineering will provide traction and scalability to its business. We expect EBIT margin to improve to 12.1% in FY18E from 11.4% in FY16 on the back of the company's focus on operational efficiencies (higher fresher recruits) and improvement in utilization, which will help offset higher investments on increasing account managers and business growth. Further, expected improvement in SAP's profitability will also drive margins. As a result, the net profit is projected to grow at a CAGR of ~12% over FY16-18E. While, ROE is expected to decline to 19.9% in FY18 owing to higher cash generation, ROCE on the other hand is expected to increase to 25.3% in FY18 owing to improvement in margins. The company's debt/equity has declined significantly in FY16 to 0.16x from 0.34x in FY14 due to the repayment of debt by the company. We expect the debt/equity to further slide to 0.07x in FY18.

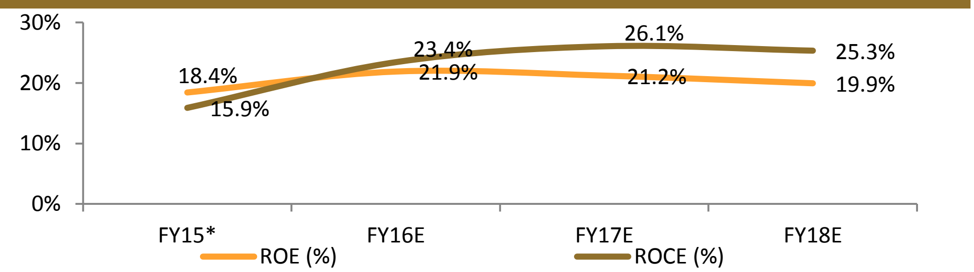
Key risks:

- Adverse currency movement could impact its performance.
- Slowdown in global IT spend.
- Failure to sustain margin improvement from SAP.

Revenue to grow at ~10% CAGR over FY16-18E



Return ratios trend



Source: Company, In-house research

Profit & Loss Account (Consolidated)

Y/E (Rs.Cr)	FY15	FY16	FY17E	FY18E
Total operating Income	2,990	3,224	3,517	3,876
Raw Material cost	85	13	28	31
Employee cost	1,742	1,933	2,068	2,275
Other operating expenses	838	843	913	999
EBITDA	**324**	**435**	**507**	**571**
Depreciation	85	69	88	102
EBIT	**239**	**366**	**419**	**469**
Interest cost	26	15	7	7
Other Income	35	25	27	36
Profit before tax	248	376	439	498
Tax	11	83	114	129
Profit after tax	**237**	**293**	**325**	**368**
Minority Interests	-	-	-	-
P/L from Associates	-	-	-	-
Adjusted PAT	**237**	**293**	**325**	**368**
E/o income / (Expense)	-	(11)	-	-
Reported PAT	**237**	**282**	**325**	**368**

Balance Sheet (Consolidated)

Y/E (Rs.Cr)	FY15	FY16	FY17E	FY18E
Paid up capital	38	38	38	38
Reserves and Surplus	1,258	1,343	1,640	1,978
Net worth	**1,296**	**1,381**	**1,678**	**2,016**
Minority Interest	-	-	-	-
Total Debt	446	217	147	147
Other non-current liabilities	42	52	57	62
Total Liabilities	**1,784**	**1,649**	**1,882**	**2,225**
Net fixed assets	229	280	322	350
Capital WIP	3	5	5	5
Goodwill	509	402	402	402
Investments	82	12	12	12
Total Net Current Assets	770	732	907	1,205
-Net CA	406	337	401	459
-Cash	364	395	506	746
Deferred tax assets (Net)	52	62	62	62
Other non-current assets	139	156	172	189
Total Assets	**1,784**	**1,649**	**1,882**	**2,225**

Cash Flow Statement (Consolidated)

Y/E (Rs.Cr)	FY15	FY16	FY17E	FY18E
Pre tax profit	248	376	439	498
Depreciation	86	69	88	102
Chg in Working Capital	37	42	(75)	(69)
Others	(4)	(10)	(20)	(29)
Tax paid	(78)	(83)	(114)	(129)
Cash flow from operating activities	**289**	**394**	**318**	**372**
Capital expenditure	(91)	(121)	(130)	(130)
Chg in investments	(3)	70	-	-
Other investing cashflow	(19)	25	27	36
Cash flow from investing activities	**(113)**	**(27)**	**(103)**	**(94)**
Equity raised/(repaid)	11	(1)	-	-
Debt raised/(repaid)	(10)	(229)	(70)	-
Dividend paid	(24)	(26)	(27)	(31)
Other financing activities	(17)	(15)	(7)	(7)
Cash flow from financing activities	**(40)**	**(271)**	**(105)**	**(38)**
Net chg in cash	136	97	111	240

Key Ratios (Consolidated)

Y/E	FY15	FY16	FY17E	FY18E
Valuation(x)				
P/E	13.3	10.5	9.5	8.4
EV/EBITDA	10.0	6.7	5.4	4.4
EV/Net Sales	1.1	0.9	0.8	0.6
P/B	2.4	2.2	1.8	1.5
Per share data				
EPS	12.3	15.6	17.2	19.6
DPS	1.1	1.2	1.2	1.4
BVPS	67.5	73.4	89.2	107.1
Growth (%)				
Net Sales	11.0	7.8	9.1	10.2
EBITDA	(14.1)	34.2	16.5	12.5
Net profit	0.0	23.8	10.7	13.5
Operating Ratios				
EBITDA Margin (%)	10.9	13.5	14.4	14.7
EBIT Margin (%)	8.0	11.4	11.9	12.1
PAT Margin (%)	7.9	9.1	9.2	9.5
Return Ratios (%)				
RoE	18.4	21.9	21.2	19.9
RoCE	15.9	23.4	26.1	25.3
Turnover Ratios (x)				
Sales/Total Assets	1.4	1.4	1.5	1.5
Sales/Working Capital	7.3	8.7	9.5	9.0
Liquidity and Solvency Ratios (x)				
Current Ratio	2.6	2.3	2.5	2.9
Interest Coverage Ratio	9.2	24.1	56.9	63.7
Debt/Equity	0.3	0.2	0.1	0.1

Rating criteria

Large Cap.	Return	Mid/Small Cap.	Return
Buy	More than equal to 10%	**Buy**	More than equal to 15%
Hold	Upside or downside is less than 10%	**Accumulate***	Upside between 10% & 15%
Reduce	Less than equal to -10%	**Hold**	Between 0% & 10%
		Reduce/sell	Less than 0%

* To satisfy regulatory requirements, we attribute 'Accumulate' as Buy and 'Reduce' as Sell.

* KPIT is a small cap company

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