

**Sonata Software Limited**

CMP Rs. 60.00  
SELL

Result Update  
Q4FY10

Raunak Onkar | raunak@ppfas.com

Sonata Software reported a poor quarterly performance as well as a topline de-growth YoY. This might be a case of having issues with low scalability, when volume growth doesn't kick in soon enough and there is a downward margin pressure. The most profitable business, SSL also showed an operating margin decline of 4%. The PAT margin seems secured due to a larger than average other income, in this quarter.

An alarming thing in this quarter's disclosure, is a sudden increase in the contingent liabilities from Rs. 2.6 Crs in FY09 to Rs. 225 Crs. This is against a net worth of ~Rs. 360 Crs. An issue with small companies is that such a large liability where the probability of any outcome cannot be guessed with reasonable confidence. This can potentially wipe out several years of profits earned.

In the event of such an outcome taking place, the option to scale up their profitable business also gets jeopardized due to cash & cash equivalents draining out to meet these liabilities. The cash position as of this quarter is Rs. 73 Crs & liquid investments are at Rs. 45 Crs.

A fundamental problem with businesses where revenues are linked linearly to the number of employees deployed is that when volume growth slows down, it doesn't necessarily decrease the cost of keeping these employees. In IT businesses, companies might face margin pressure on increasing wage rates vis-a-vis a strong rupee, which can instantly dissolve any chances of sustaining the "growth year"-like margins.

Sonata Software limited might be able to achieve its growth targets in the future, but it seems unjustified to face it with a dangling sword of heavy contingent liabilities.

We recommend a Sell on Sonata Software.

**Financials >>**

## Sonata: FY10 Performance Review

Particulars (Rs. Mn)	Standalone			Consolidated		
	FY10	FY09	Y-Y Chng	FY10	FY09	Y-Y Chng
Sales & Service	2,360.4	2,435.8	-3.1%	13,804.4	15,912.7	-13.2%
Other Income	52.8	10.5	401.4%	128.5	109.5	17.3%
Total Revenues	2,413.2	2,446.3	-1.4%	13,932.9	16,022.2	-13.0%
Total Expenditure	1,718.9	1,795.7	-4.3%	12,222.0	14,394.3	-15.1%
<i>RM Consumed</i>	0.0	15.7	-100.0%	4,421.8	5,843.0	-24.3%
<i>Other Expenditure</i>	1,718.9	1,780.1	-3.4%	7,800.2	8,551.3	-8.8%
Operating Profit	694.3	650.6	6.7%	1,710.9	1,627.9	5.1%
Other Income	0.0	0.0		0.0	0.0	
EBITDA	694.3	650.6	6.7%	1,710.9	1,627.9	5.1%
Misc Write off	0.0	0.0		0.0	0.0	
Depreciation	77.7	81.3	-4.5%	491.7	435.0	13.0%
PBIT	616.6	569.2	8.3%	1,219.1	1,192.9	2.2%
Interest	0.0	3.9	-100.0%	67.0	66.9	0.1%
PBT	616.6	565.4	9.1%	1,152.1	1,126.0	2.3%
Tax	15.1	31.8	-52.5%	197.9	221.6	-10.7%
<i>Current Tax</i>	15.1	31.8	-52.5%	197.9	221.6	-10.7%
<i>FringeBenefit Tax</i>	0.0	0.0		0.0	0.0	
<i>Deferred tax</i>	0.0	0.0		0.0	0.0	
PAT before MI	601.5	533.6	12.7%	954.3	904.4	5.5%
Share in Earnings of Affiliates	0.0	0.0		-15.4	2.5	-712.3%
Minority Interest	-	-		(140.1)	(141.3)	-0.8%
PAT	601.5	533.6	12.7%	798.7	765.7	4.3%
Extra-ordinary Income	0.0	0.0		0.0	0.0	
Reported PAT	601.5	533.6	12.7%	798.7	765.7	4.3%

## Sonata: Financials

### Q3FY10 Standalone Reported

Standalone (Rs. Mn)	Mar 10	Dec 09	Q-Q Chng	Mar 09	Y-Y Chng
Sales & Service	587.7	605.2	-2.9%	589.3	-0.3%
Other Income	39.2	4.3	808.8%	1.2	3166.6%
Total Revenues	627.0	609.5	2.9%	590.5	6.2%
Total Expenditure	458.2	420.6	8.9%	440.2	4.1%
<i>RM Consumed</i>	0.0	0.0		3.9	-100.0%
<i>Staff Cost</i>	315.0	294.9		296.6	
<i>Other Expenditure</i>	143.2	125.7	13.9%	139.7	2.5%
Operating Profit	168.8	188.9	-10.7%	150.3	12.3%
Other Income	0.0	0.0		0.0	
EBITDA	168.8	188.9	-10.7%	150.3	12.3%
Misc Write off	0.0	0.0		0.0	
Depreciation	20.3	19.8	2.5%	18.0	13.0%
PBIT	148.5	169.1	-12.2%	132.3	12.2%
Interest	0.0	0.0		0.0	
PBT	148.5	169.1	-12.2%	132.3	12.2%
Tax	-9.4	5.4	-273.2%	3.6	-362.2%
PAT	157.9	163.7	-3.5%	128.7	22.6%
Extra-ordinary Income	0.0	0.0		0.0	
Reported PAT	157.9	163.7	-3.5%	128.7	22.6%

### Q3FY10 Consolidated Reported

Consolidated (Rs. Mn)	Mar 10	Dec 09	Q-Q Chng	Mar 09	Y-Y Chng
Sales & Service	3,191.0	3,360.4	-5.0%	3,683.8	-13.4%
Other Income	73.8	18.1	308.0%	25.5	189.7%
Total Revenues	3,264.8	3,378.4	-3.4%	3,709.2	-12.0%
Total Expenditure	2,865.6	2,913.9	-1.7%	3,348.9	-14.4%
<i>RM Consumed</i>	958.1	950.3	0.8%	1,356.6	-29.4%
<i>Other Expenditure</i>	1,907.6	1,963.6	-2.9%	1,992.3	-4.3%
Operating Profit	399.1	464.5	-14.1%	360.3	10.8%
Other Income	0.0	0.0		0.0	
EBITDA	399.1	464.5	-14.1%	360.3	10.8%
Misc Write off	0.0	0.0		0.0	
Depreciation	120.0	125.2	-4.2%	107.7	11.4%
PBIT	279.1	339.3	-17.7%	252.6	10.5%
Interest	16.9	16.4	3.1%	16.6	1.5%
PBT	262.2	322.9	-18.8%	235.9	11.1%
Tax	32.0	61.0	-47.6%	39.3	-18.7%
PAT before MI	230.3	261.9	-12.1%	196.6	17.1%
Share in Earnings of Affiliates	-15.4	0.0		2.7	
Minority Interest	(27.1)	(41.8)	-35.2%	(27.1)	
PAT	187.8	220.1	-14.7%	172.2	9.1%
Extra-ordinary Income	0.0	0.0		0.0	
Reported PAT	187.8	220.1	-14.7%	172.2	9.1%

## Sonata : Financials

Earnings Statement					Balance Sheet				
YE March (Rs. Mn.)	FY07	FY08	FY09	FY10	YE March (Rs. Mn.)	FY07	FY08	FY09	FY10
Sales & Services	8,977.2	14,283.7	15,912.7	13,804.4	Equity Capital	105.2	105.2	105.2	105.2
Total Expenditure	8,189.2	13,169.0	14,394.3	12,222.0	Reserves	1,762.4	2,183.4	2,662.9	3,533.7
- Purchase of traded goods	3,764.0	5,422.2	5,843.0	4,421.8	Shareholders Funds	1,867.6	2,288.5	2,768.0	3,638.9
- Operating expenses	4,425.2	7,746.8	8,551.3	7,800.2	Minority Interest	184.9	269.1	308.1	396.7
Operating Profit	788.0	1,114.7	1,518.4	1,582.4	Borrowed Funds	581.2	283.4	33.7	299.4
Other Income	198.6	310.6	109.5	128.5	Deferred Tax Liabilities	0.6	1.1	1.0	0.1
EBITDA	986.6	1,425.3	1,627.9	1,710.9	<b>Total Liabilities</b>	<b>2,634.2</b>	<b>2,842.2</b>	<b>3,110.9</b>	<b>4,335.0</b>
Depreciation	297.4	433.5	435.0	491.7	Fixed Assets				
EBIT	689.2	991.8	1,192.9	1,219.1	Gross Block	6,922.4	7,173.7	7,474.9	7,921.6
Interest	27.7	49.6	66.9	67.0	Accumulated Depn.	5,074.8	5,410.5	5,621.3	6,078.6
PBT	661.5	942.2	1,126.0	1,152.1	Net Block	1,847.7	1,763.2	1,853.6	1,843.0
Tax	83.5	125.2	221.6	197.9	Capital WIP	49.5	74.1	56.3	4.0
PAT before MI	578.0	817.0	904.4	954.3	Investments	143.1	238.7	81.0	457.9
Minority Interest	107.3	237.8	141.3	140.1	Current Assets				
Profit from Affiliates	9.6	6.0	2.5	15.4	Inventory	56.1	144.7	54.7	147.3
PAT before EI	480.3	585.2	765.7	798.7	Sundry Debtors	1,941.9	2,386.9	2,777.5	1,939.3
Reported PAT	480.3	585.2	765.7	798.7	Loans & Advances	432.1	424.5	1,278.9	1,866.8
					Cash & Bank Balance	1,212.5	764.4	817.4	731.1
					Current Liabilities				
					Sundry Creditors	3,141.7	3,096.2	3,994.7	2,193.9
					Provisions	77.9	85.4	12.8	707.8
					Net Current Assets	423.0	539.0	921.1	1,873.6
					Deferred Tax Assets	171.0	227.2	198.9	156.6
					<b>Total Assets</b>	<b>2,634.2</b>	<b>2,842.2</b>	<b>3,110.9</b>	<b>4,335.0</b>

  

Ratio Analysis				
YE March	FY07	FY08	FY09	FY10
OPM (%)	8.8%	7.8%	9.5%	11.5%
EBITDA (%)	11.0%	10.0%	10.2%	12.4%
PBIT (%)	7.7%	6.9%	7.5%	8.8%
PAT (%)	5.3%	4.1%	4.8%	5.8%
EPS (Rs.)	4.6	5.6	7.3	7.6
P/E (x)	12.9	10.6	8.1	7.8
P/BV (x)	3.3	2.7	2.2	1.7
BVPS (Rs.)	17.8	21.8	26.3	34.6
Market Cap (Rs. Mn.)	6,204.4	6,204.4	6,204.4	6,204.4
M Cap/Sales (x)	0.7	0.4	0.4	0.4
EV (Rs. Mn.)	6,785.6	6,487.8	6,238.1	6,503.8
EV/EBITDA (x)	6.9	4.6	3.8	3.8
EV/Sales (x)	0.8	0.5	0.4	0.5
ROCE (%)	26.2%	34.9%	38.3%	28.1%
RONW (%)	25.7%	25.6%	27.7%	22.0%
Inventory T/o Days	2.3	3.7	1.3	3.9
Debtors T/o Days	79.0	61.0	63.7	51.3
Advances T/o Days	17.6	10.8	29.3	49.4
Creditors T/o Days	127.7	79.1	91.6	58.0
Working Cap T/o Days	17.2	13.8	21.1	49.5
Fixed Assets T/o (Gross)	1.3	2.0	2.1	2.1
DPS (Rs.)	1.1	1.1	1.5	-
Dividend Payout (%)	24.1%	19.8%	20.6%	0.0%
Dividend Yield (%)	1.9%	1.9%	2.5%	0.0%

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1. Analyst Ownership of the scrip
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## Sonata

- YES  
YES  
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## Contact

Raunak Onkar

Analyst - Investment Research

raunak@ppfas.com

91 22 2284 6555 Extn 323

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## Parag Parikh Financial Advisory Services Limited

130/132, Great Western Building, 1st Floor, S. B. Marg, Near Lion Gate, Fort, Mumbai - 400 001.

Tel : 91-22-2284 6555 Fax : 91-22-2284 6553, e-mail : researchcall@ppfas.com

[www.ppfas.com](http://www.ppfas.com)