

Oracle Financial Services Software Ltd.CMP Rs. 2,117.0
HOLDResult Update
Q2FY10

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Oracle reported a very good second quarter, ended Sept 2009. On the revenues front, despite adding 12 more customers, 20 projects going live & good collections, OFSS reported a marginal decline of ~3% YoY. PAT improved significantly this quarter from Rs.934Mn for Q2FY09 to Rs.2045Mn for Q2FY10; a growth of almost 119%.

Oracle has shown tremendous margin improvement over the last year's second quarter, owing to reduction in their expenditure. As seen in the reported statement, expenditure is down by 17% compared to Q2FY09. This may be predominantly due to the overall reduction of employees & moving most of the business from on-site to offshore; which ensures better cost management. Q2FY09 shows an onsite offshore mix of 66% against 34%, whereas this quarter the mix has become 49% against 51%. This sort of cost management, moving a lot of business offshore isn't new to IT companies, forgoing a lot of premium for onsite work. It's usually favorable to have more offshore content to the revenue mix during times when clients demand pricing reductions as well as provide low volume of work.

The overall geographical growth of the company seems to be great, showing business flowing in from the US (+3%), Middle East (+4%), APAC (+2%) where as a marginal reduction in EU (-2%). It is remarkable that even in times where most of their clients haven't fully recovered from the crisis, demand seems to have improved for their products & consulting services.

Although it's interesting to see how the product revenues have panned out from a year ago. Revenue for products is mainly seen flowing from AMC (Annual Maintenance Contracts) & from their implementation work which includes product upgradation, et al. The license fee revenue has been badly hit owing to lower demand for new product installations. Therefore, we can see a marginal revenue dip year on year at the same time the revenue from other product related activities acts as a buffer. Although the first half year revenues for FY10 have shown a growth of ~4% over the last year's first half year revenue.

Valuation

OFSS trades at ~24 PE (TTM), which makes it seem to be over valued as compared to leading IT companies like Infosys, TCS & so on. In fact OFSS, as a business has not changed significantly, but has only improved compared to the past one year. Even in the down turn their business managed to report an annual revenue growth of 23% in FY09.

In spite of being a great business, it isn't a conducive pick to BUY, nevertheless a very good business to hold. The way its business is organized across a very favorable mix of consulting and product businesses & de-risking their model by moving to newer geographies, the company might get a lot business going ahead. Also its leadership status in the core banking product category (product name: Flexcube & its associated product suites) makes it a very sought after player in the banking product space.

As Philip Fisher said, the only reasons to sell a business are:

- 1) Error in the investment case
- 2) Fundamentals of the business have changed irreversibly
- 3) A better bargain is available

We recommend a HOLD for OFSS.

OFSS : Quarterly Financials

Earnings Statement								
YE March (Rs. Mn.)	Q2FY10	Q1FY10	Q-Q(%)	Q2FY09	Y-Y(%)	6MFY10	6MFY09	Y-Y(%)
Net Revenues	6,790.1	7,100.2	-4.37%	6,996.6	-2.95%	13,890.3	13,314.9	4.32%
Total Expenditure	4,796.2	4,744.1	1.10%	5,800.5	-17.31%	9,540.2	11,429.6	-16.53%
Operating Profit	1,993.9	2,356.2	-15.37%	1,196.0	66.71%	4,350.1	1,885.3	130.74%
OPM (%)	29.37%	33.18%	-11.51%	17.09%	71.78%	31.32%	14.16%	121.18%
Other Income	349.1	(204.5)		(28.7)		144.6	609.9	-76.29%
EBITDA	2,343.0	2,151.7	8.89%	1,167.3	100.71%	4,494.7	2,495.2	80.13%
Depreciation	130.6	127.3	2.60%	137.9	-5.30%	257.8	275.7	-6.49%
EBIT	2,212.4	2,024.4	9.29%	1,029.5	114.91%	4,236.8	2,219.5	90.90%
Interest	0.0	0.0	0.00%	0.0	0.00%	0.0	0.0	0.00%
PBT	2,212.4	2,024.4	9.29%	1,029.5	114.91%	4,236.8	2,219.5	90.90%
Tax	166.8	164.7	1.33%	91.1	83.22%	331.5	219.1	51.32%
PAT	2,045.6	1,859.8	9.99%	934.3	118.94%	3,905.3	2,000.4	95.23%
Equity Capital	418.9	418.8	0.00%	418.8	0.00%			
EPS	24.4	22.2	10.20%	11.2	119.01%			
Ratio Analysis								
Profitability								
YE March (Rs. Mn.)	Q2FY10	Q1FY10	Q-Q(bps)	Q2FY09	Y-Y(bps)	H1FY10	H1FY09	Y-Y(bps)
OPM (%)	29.37%	33.18%	(381.9)	17.09%	1,227.1	31.32%	14.16%	1,715.8
EBITDA (%)	34.51%	30.30%	420.2	23.39%	1,112.0	1.52%	9.44%	(792.3)
EBIT (%)	32.58%	28.51%	407.1	14.71%	1,786.9	66.37%	39.09%	2,728.9
PAT (%)	30.13%	26.19%	393.3	13.41%	1,671.4	16.53%	14.48%	204.9

OFSS : Financials

Earnings Statement					Balance Sheet				
Particulars (Rs Mn)	FY06	FY07	FY08	FY09	Particulars (Rs Mn)	FY06	FY07	FY08	FY09
Total Revenues	14,823.0	20,609.4	23,802.4	29,276.2	Equity Capital	381.4	416.4	418.7	418.8
- Growth (%)	30.2%	39.0%	15.5%	23.0%	Share app. Money	10.3	401.7	0.3	0.1
Cost of Revenues	7,794.1	11,066.1	13,040.3	14,491.6	Reserves	13,415.4	23,202.1	27,351.6	34,629.8
Gross Profit	7,028.9	9,543.3	10,762.1	14,784.6	Shareholders Funds	13,807.2	24,020.2	27,770.6	35,048.8
Operating Expenses	3,824.7	5,118.8	6,089.8	7,320.8	Minority Interest	0.0	0.0	6.3	19.2
Operating Income	3,204.2	4,424.5	4,672.3	7,463.7	Borrowed Funds	0.0	0.0	0.0	0.0
- Growth (%)	6.8%	38.1%	5.6%	59.7%	Total Liabilities	13,807.2	24,020.2	27,776.8	35,068.0
Non-Operating Income	294.6	376.9	639.7	1,789.4	Fixed Assets	3,159.0	8,941.2	9,826.7	9,705.7
Non-Operating Expenses	9.9	17.3	0.0	0.0	Investments	52.4	59.2	54.9	9.6
Depreciation & Amortization	460.4	653.0	705.9	557.9	Current Assets				
Exceptional Item				(468.9)	Sundry Debtors	5,257.9	7,494.4	8,454.0	8,402.3
EBIT	3,028.5	4,131.1	4,606.1	8,226.3	Loans & Advances	2,078.9	4,325.0	5,241.6	6,442.3
- Growth (%)	2.6%	36.4%	11.5%	78.6%	Cash & Bank Balance	6,869.4	7,197.8	8,977.5	15,489.5
Tax	560.4	416.0	441.7	835.4	Other Current Assets	309.1	1,194.6	1,137.1	1,746.9
PAT Before MI & PPI	2,468.0	3,715.2	4,164.4	7,390.9	Current Liabilities				
- Growth (%)	6.2%	50.5%	12.1%	77.5%	Other Current Liabilities	3,308.8	4,910.5	5,613.7	6,095.0
Minority Interest	2.6	0.0	(4.4)	(12.9)	Provisions	679.9	421.2	527.0	938.6
Share of Profit of assoc. Com	3.3	7.6	(4.1)	(12.6)	Net Current Assets	10,526.7	14,880.1	17,669.5	25,047.5
Income before PPI	2,473.9	3,722.8	4,155.9	7,365.4	Net Deferred Tax	69.2	139.8	225.6	305.2
Prior Period Items	97.4	0.0	0.0	0.0	Total Assets	13,807.3	24,020.3	27,776.8	35,068.0
Net Income	2,376.5	3,722.8	4,155.9	7,365.4					
Reported PAT	2,376.5	3,722.8	4,155.9	7,365.4					
- Growth (%)	2.2%	56.6%	11.6%	77.2%					

Ratio Analysis				
Particulars	FY06	FY07	FY08	FY09
OPM (%)	21.6%	21.5%	19.6%	25.5%
PBIT (%)	20.4%	20.0%	19.4%	28.1%
PAT (%)	16.0%	18.1%	17.5%	25.2%
EPS (Rs.)	31.2	44.7	49.6	87.9
Cash Per Share (Rs.)	90.0	86.4	107.2	184.9
P/E (x)	68.0	47.4	42.7	24.1
P/BV (x)	11.7	7.3	6.4	5.1
BVPS (Rs.)	181.0	288.4	331.6	418.4
Market Cap (Rs. Mn.)	161,502.5	176,322.0	177,293.2	177,339.8
M Cap/Sales (x)	10.9	8.6	7.4	6.1
EV (Rs. Mn.)	154,633.1	169,124.2	168,315.7	161,850.3
EV/EBITDA (x)	48.3	38.2	36.0	21.7
EV/Sales (x)	10.4	8.2	7.1	5.5
ROIC (%)	22.5%	19.4%	17.8%	20.5%
ROCE (%)	21.9%	17.2%	16.6%	23.5%
RONW (%)	17.2%	15.5%	15.0%	21.0%
Debtors T/o Days	127.7	130.9	127.9	103.3
Advances T/o Days	50.5	75.5	79.3	80.0
Creditors T/o Days	80.4	85.8	84.9	85.0
Working Cap T/o Days	255.7	259.9	267.2	270.0
Fixed Assets T/o (Gross)	3.7	2.1	2.1	2.4
DPS (Rs.)	5.0	0.0	0.0	0.0
Dividend Payout (%)	16.1%	0.0%	0.0%	0.0%

Cash Flow				
Particulars (Rs Mn)	FY06	FY07	FY08	FY09
Opening Cash & Bank	6,634.8	6,869.4	7,197.754	8,977.532
Profit After Tax	2,376.5	3,722.8	4,155.9	7,365.4
Invnt Income	(294.6)	(376.9)	(639.7)	(1,789.4)
Interest Paid	0.0	0.0	0.0	0.0
Miscellaneous Exp W/Off	0.0	0.0	0.0	0.0
Depreciation	460.4	653.0	705.9	557.9
Deferred Taxation	0.0	(69.6)	(70.6)	(85.9)
Others	(893.7)	(260.0)	(170.8)	246.6
Change in Working Cap	(1,200.9)	(4,025.1)	(1,009.7)	(865.9)
CF - Operating Activities	447.8	(355.7)	2,971.0	5,428.7
Change in Fixed Assets	(1,366.7)	(6,424.0)	(1,429.6)	(664.3)
Change in Investments	8.6	(6.8)	4.2	45.4
Investment Income	294.6	376.9	639.7	1,789.4
CF - Investing Activities	(1,063.6)	(6,053.9)	(785.7)	1,170.5
Increase in Equity	414.1	6,614.1	(405.5)	(87.2)
Changes in Borrowings	0.0	0.0	0.0	0.0
Interest Paid	0.0	0.0	0.0	0.0
Dividend Paid	436.3	123.9	0.0	0.0
CF - Financing Activities	850.4	6,738.0	(405.5)	(87.2)
Net Change in Cash	234.6	328.3	1,779.8	6,512.0
Closing Cash & Bank Bal	6,869.4	7,197.8	8,977.5	15,489.5

Disclaimer

Disclosure of Interest Statement	OFSS
1. Analyst Ownership of the scrip	NO
2. PPFAS ownership of the scrip	YES
3. PMS ownership of the scrip	YES

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