

SIS INDIA

Minor blip; long-term story intact

India Equity Research | Business Services



SIS India (SIS) clocked robust Q1FY19 earnings with consolidated sales and EPS jumping 30% and 69% YoY, respectively. Though INR70mn one-off impact hurt domestic margin (fell to 5.0% from 6.7% in Q4FY18), management categorically termed it as non-recurring. Sales growth was robust across segments—India security, facility management (FM) and Australia up 15%, 30% and 42% YoY, respectively. This reconfirms our thesis about the sector's structural growth trajectory and SIS' competitive advantages to outperform the industry. The stock is down ~7% YTD (versus 12% dip in BSE Mid-cap index) indicating the strength in earnings. Retain 'BUY' with revised TP of INR1,500 (from INR1,532) as we marginally revise down FY19E and FY20E EPS.

Strong top-line growth; margin impact one-off

The big concern in Q1FY19 earnings was from India Security Services' EBITDA margin falling to ~5% (from normalized 6.5%). The slip was due to a mix of provisions made for some clients under NCLT and a few overheads for contracts terminated in March 2018. Management has clarified that this is a one-off, and margin should normalise and sales growth should accelerate from Q2FY19. SIS has also won contracts worth INR170mn/month in Q1FY19 and this win run rate confirms our belief that India sales can grow 18-20% annually. The Australia business jumped 42% YoY (17% organic) with steady margin, and contract wins. India FM segment's rapid pace sustained with 30% YoY surge. We estimate the segment's FY18 sales of INR6.7bn to double by FY21 with current growth pace and contract wins.

Operational moat to enable sustained industry outperformance

We reiterate our thesis that the Indian Security Services sector will grow at 16-18% value CAGR and SIS will potentially outperform the sector's growth by 2-4% driven by competitive advantages. SIS is delivering similar outperformance in FM segment and surprising positively. The Australia business also continues to outperform industry and is a strong cash flow generator (refer, *Guarding the gates*, dated April 23, 2018).

Outlook and valuations: Large opportunity; maintain 'BUY'

We value SIS on a three-stage DCF, which we believe captures the long-term opportunity much more accurately. We cut FY19/20E EPS 3-4% for one-offs and details from Annual Report. We maintain 'BUY' with INR1,500 TP. We highlight that the CMP implies ~15% EBITDA CAGR over FY20-30, which reflects ample margin of safety.

Financials

	INRmm							
Year to March	Q1FY19	Q1FY18	% change	Q4FY18	% change	FY18	FY19E	FY20E
Net rev. (INR mn)	16,114	12,435	29.6	15,922	1.2	58,334	69,303	79,063
EBITDA (INR mn)	745	670	11.1	866	(14.0)	3,120	3,647	4,408
Adj. PAT (INR mn)	399	220	81.5	333	19.5	1,629	2,309	3,008
Adj. Dil. EPS (INR)	5.3	2.9	79.7	4.5	18.3	21.9	31.6	41.1
Diluted P/E (x)							34.8	26.7
EV/EBITDA (x)							21.8	17.7
ROAE (%)							20.6	22.5

EDELWEISS RATINGS

Absolute Rating	BUY
Investment Characteristics	Growth

MARKET DATA (R: SECR BO, B: SECIS IN)

CMP	: INR 1,099
Target Price	: INR 1,500
52-week range (INR)	: 1,405 / 705
Share in issue (mn)	: 73.2
M cap (INR bn/USD mn)	: 80 / 0
Avg. Daily Vol. BSE/NSE ('000)	: 92.0

SHARE HOLDING PATTERN (%)

	Current	Q4FY18	Q3FY18
Promoters *	75.5	75.5	75.5
MF's, FI's & BKs	12.9	5.0	4.8
FII's	7.9	5.8	5.7
Others	4.5	13.8	14.0
* Promoters pledged shares (% of share in issue)	:	NIL	

PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	(4.6)	0.3	4.9
3 months	(10.6)	4.6	15.2
12 months	(1.1)	NA	NA

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Business Services

Table 1: Quarterly trend of key financials – Standalone and Consolidated

INR mn	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	YoY (%)	QoQ (%)	FY17	FY18	YoY (%)
Standalone (India Security segment)										
Sales	4,883	5,217	5,605	5,645	5,637	15.4	(0.1)	11,465	21,351	86.2
EBITDA	358	365	373	380	284	(20.8)	(25.3)	691	1,476	113.7
PBT	137	154	241	240	163	18.9	(31.9)	225	773	242.9
PAT	115	166	225	224	197	70.2	(12.3)	141	730	417.0
EBITDA margin (%)	7.3	7.0	6.7	6.7	5.0			6.0	6.9	
Consolidated										
Sales	12,435	14,600	15,377	15,922	16,114	29.6	1.2	31,491	58,334	85.2
EBITDA	670	741	843	866	745	11.1	(14.0)	1,523	3,120	104.8
PBT	366	624	555	447	501	37.1	12.1	824	1,992	141.9
PAT	220	596	472	333	399	81.5	19.5	533	1,620	203.8
EBITDA margin (%)	5.4	5.1	5.5	5.4	4.6			4.8	5.3	

Source: Company information

Table 2: Segment-wise sales and EBITDA

	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	YoY (%)	YoY (%)	FY17	FY18	YoY (%)
Sales										
India Security Services	4,900	5,230	5,620	5,700	5,650	15.3	(0.9)	11,370	21,450	88.7
Australia Security Services	6,000	7,730	8,050	8,410	8,500	41.7	1.1	17,540	30,190	72.1
India Facility Management	1,540	1,640	1,710	1,820	2,000	29.9	9.9	2,581	6,710	160.0
EBITDA										
India Security Services	348	372	380	374	270	(22.4)	(27.8)	697	1,474	111.5
Australia Security Services	252.91	290	368	369.81	343	35.6	(7.2)	758	1,281	69.0
India Facility Management	61	78	96	108	130	113.1	20.4	66	343	419.7
EBITDA margin (%)										
India Security Services	7.1	7.1	6.8	6.6	4.8			6.1	6.9	
Australia Security Services	4.2	3.8	4.6	4.4	4.0			4.3	4.2	
India Facility Management	4.0	4.8	5.6	5.9	6.5			2.6	5.1	

Source: Company information

Financial snapshot

(INR mn)

Year to March	Q1FY19	Q1FY18	% change	Q4FY18	% change	FY18	FY19E	FY20E
Net revenues	16,114	12,435	29.6	15,922	1.2	58,334	69,303	79,063
Employee Exp + other COGS	13,395	10,628	26.0	12,973	3.2	48,023	55,133	63,000
Gross profit	2,719	1,807	50.4	2,949	(7.8)	10,311	14,170	16,062
Other expenses	1,974	1,137	73.7	2,083	(5.2)	7,191	10,523	11,654
Total expenditure	15,369	11,765	30.6	15,056	2.1	55,214	65,656	74,655
EBITDA	745	670	11.1	866	(14.0)	3,120	3,647	4,408
Depreciation	133	111	19.1	183	(27.4)	560	505	525
EBIT	612	559	9.5	683	(10.4)	2,560	3,142	3,883
Interest	168	227	(26.0)	277	(39.3)	925	879	879
Other income	57	34	70.3	49	16.2	365	332	348
Add: Exceptional items				(8)	(100.0)			
Profit before tax	501	366	37.1	447	12.1	2,001	2,596	3,353
Provision for taxes	63	99	(36.1)	30	112.3	244	261	319
Minority interest	(4)	(4)	NA	27	NA	10	-	-
Associate profit share	(43)	(51)	NA	(57)	NA	(118)	(25)	(25)
Reported net profit	399	220	81.5	333	19.5	1,629	2,309	3,008
Adjusted Profit	399	220	81.5	333	19.5	1,629	2,309	3,008
Diluted shares (mn)	75	74		74		74	73	73
Adjusted Diluted EPS	5.3	2.9	79.7	4.5	18.3	21.9	31.6	41.1
Diluted P/E (x)							34.8	26.7
EV/EBITDA (x)							21.8	17.7
ROAE (%)							20.6	22.5

As % of net revenues

Raw material	83.1	85.5		81.5		82.3	79.6	79.7
Employee cost	16.9	14.5		18.5		17.7	20.4	20.3
Other expenses	12.3	9.1		13.1		12.3	15.2	14.7
EBITDA	4.6	5.4		5.4		5.3	5.3	5.6
Reported net profit	2.5	1.8		2.1		2.8	3.3	3.8

Company Description

SIS is a security services company based in India and Australia with leadership in cash logistics and facility management (FM) services. The company offers solutions across service lines including security services (primarily the manned guarding business in India and Australia), wherein it has expanded operations via the acquisition of Chubb Security Personnel (later renamed and rebranded as MSS Security). SIS provides cash logistics through SIS Cash Services, a joint venture with Prosegur of Spain and the second-largest cash logistics service provider in India. The company entered FM services via an exclusive licence agreement with Service Master for the Service Master Clean brand. In FY17, SIS acquired 78.72% of the outstanding equity shares of Dusters, the fourth-largest FM provider in India by revenue.

Investment Theme

Since FY06, SIS' domestic security services segment has clocked sales CAGR of ~35%, and we expect this outperformance to sustain as the company shines on all critical success-enablers, viz: 1) scale; 2) reinvestment in core business; 3) pan-India presence; and 4) expansion to tier II-III cities. We expect SIS to emerge as the market leader in the Indian manned guarding services by FY20 with a market share of ~5%. Its market leadership in Australia is also expected to remain unchallenged. Besides, SIS' domestic FM segment may undergo a huge ramp up over the next two years. Over FY18–20E, high organic growth should drive a consolidated EPS CAGR of ~40% and RoE expansion from 20.2% to 23.5%.

Key Risks

Our estimates and target price are based on the assumption that SIS will consistently gain market share in the Indian manned guarding business over the next six-seven years. A failure thereof is the key downside risk to our estimates and target price.

In Australia, we expect sales to grow ~8% based on a headcount (security guards) growth assumption of 4-5%. Any slowdown in the Australian economy leading to lower demand for security services is a downside risk to our Australia business assumptions.

Higher-than-expected pricing intensity in the security services business, which could exert pressure on our margin assumptions, is another downside risk to our estimates.

We have assumed an annual wage hike of 7-8% over FY18-20 for security guards in India. A lower-than-expected annual hike and SIS' inability to gain from these hikes also pose a downside risk to our thesis.

Financial Statements

Key Assumptions

Year to March	FY17	FY18	FY19E	FY20E
Macro				
GDP(Y-o-Y %)	6.6	6.5	7.1	7.6
Inflation (Avg)	4.5	3.8	4.5	5.0
Repo rate (exit rate)	6.3	6.0	6.0	6.5
USD/INR (Avg)	67.1	64.5	66.0	66.0
Company				
Net borrowings (INR mn)	1,981	(67)	(875)	(2,364)
Debtor days	76	71	71	71
Inventory days	-	1	1	1
Payable days	3	5	5	5
Cash conversion cycle	73	67	67	67

Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Net revenue	43,872	58,334	69,303	79,063
Materials costs	163	363	476	590
Gross profit	6,679	10,311	14,170	16,062
Employee costs	37,030	47,660	54,657	62,410
Other Expenses	4,475	7,191	10,523	11,654
Operating expenses	4,475	7,191	10,523	11,654
Total operating expenses	4,638	7,554	10,999	12,245
EBITDA	2,204	3,120	3,647	4,408
Depreciation	358	560	505	525
EBIT	1,845	2,560	3,142	3,883
Less: Interest Expense	767	925	879	879
Add: Other income	86.74	365.44	332.22	348.36
Profit Before Tax	1,165	2,001	2,596	3,353
Less: Provision for Tax	8	244	261	319
Less: Minority Interest	(21)	10	-	-
Associate profit share	(60)	(118)	(25)	(25)
Exceptional items	-	8	-	-
Reported Profit	1,118	1,637	2,309	3,008
Exceptional Items	-	8	-	-
Adjusted Profit	1,118	1,629	2,309	3,008
Shares o/s (mn)	69	73	73	73
Adjusted Basic EPS	16.3	22.2	31.5	41.1
Diluted shares o/s (mn)	69	73	73	73
Adjusted Diluted EPS	16.3	22.2	31.5	41.1
Adjusted Cash EPS	16.5	25.1	36.1	45.0
Dividend per share (DPS)	-	3.5	5.0	6.6
Dividend Payout Ratio(%)	-	0.2	0.2	0.2

Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Gross margin	15.2	17.7	20.4	20.3
Operating expenses	10.2	12.3	15.2	14.7
Interest Expense	1.7	1.6	1.3	1.1
EBITDA margins	5.0	5.3	5.3	5.6
EBIT margins	4.2	4.4	4.5	4.9
Net Profit margins	2.5	2.8	3.3	3.8

Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	14.4	33.0	18.8	14.1
EBITDA	69.6	41.6	16.9	20.8
Adjusted Profit	158.4	45.6	41.8	30.3
EPS	156.0	36.6	41.8	30.3

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	687	732	732	732	
Reserves & Surplus	5,219	9,551	11,426	13,868	
Shareholders' funds	5,906	10,283	12,158	14,600	
Minority Interest	3	14	14	14	
Long term borrowings	3,735	3,763	3,763	3,763	
Short term borrowings	2,538	1,598	1,598	1,598	
Total Borrowings	6,273	5,361	5,361	5,361	
Long Term Liabilities	1,340	3,834	3,834	3,834	
Def. Tax Liability (net)	(895)	(1,163)	(1,163)	(1,163)	
Sources of funds	12,627	18,329	20,204	22,646	
Gross Block	1,373	1,878	2,428	2,978	
Net Block	1,088	1,267	1,312	1,337	
Capital work in progress	4	10	10	10	
Intangible Assets	2,932	5,946	5,946	5,946	
Total net fixed assets	4,024	7,223	7,267	7,293	
Non-current investments	989	921	921	921	
Cash and Equivalents	4,292	5,428	6,236	7,725	
Inventories	33	142	154	179	
Sundry Debtors	4,207	6,243	7,476	8,532	
Loans & Advances	925	1,151	1,151	1,151	
Other Current Assets	5,077	5,670	6,635	7,494	
Current Assets (ex cash)	10,241	13,206	15,416	17,357	
Trade payable	394	806	963	1,086	
Other Current Liab	6,525	7,642	8,674	9,564	
Total Current Liab	6,918	8,449	9,637	10,650	
Net Curr Assets-ex cash	3,322	4,757	5,779	6,707	
Uses of funds	12,627	18,329	20,204	22,646	
BVPS (INR)	86.0	140.4	166.0	199.4	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	1,118	1,637	2,309	3,008	
Add: Depreciation	358	560	505	525	
Interest (Net of Tax)	514	620	589	589	
Others	(1,400)	(766)	(2,086)	(1,914)	
Less: Changes in WC	(411)	(99)	(1,022)	(928)	
Operating cash flow	1,001	2,150	2,340	3,136	
Less: Capex	647	516	550	550	
Free Cash Flow	355	1,634	1,790	2,586	

Cash flow metrics		FY17	FY18	FY19E	FY20E
Year to March					
Operating cash flow		1,001	2,150	2,340	3,136
Financing cash flow		1,929	995	(1,313)	(1,445)
Investing cash flow		(2,886)	(1,164)	(218)	(202)
Net cash Flow		45	1,981	808	1,489
Capex		(647)	(516)	(550)	(550)
Dividend paid		(53)	(144)	(370)	(481)

Profitability and efficiency ratios		FY17	FY18	FY19E	FY20E
Year to March					
ROAE (%)		21.4	20.2	20.6	22.5
ROACE (%)		25.5	26.0	26.8	29.3
Inventory Days		-	1	1	1
ROA		10.8	10.5	12.0	14.0
Debtors Days		76	71	71	71
Payable Days		3	5	5	5
Cash Conversion Cycle		73	67	67	67
Current Ratio		2.1	2.2	2.2	2.4
Debt/EBITDA (x)		2.8	1.7	1.5	1.2
Adjusted Debt/Equity		1.1	0.5	0.4	0.4
Net Debt/Equity		0.3	-	(0.1)	(0.2)
Interest Coverage Ratio		2.4	2.8	3.6	4.4
LT debt /Cap empl. (%)		29.6	20.5	18.6	16.6
Debt / Cap employed (%)		49.7	29.2	26.5	23.7

Operating ratios		FY17	FY18	FY19E	FY20E
Year to March					
Total Asset Turnover		4.3	3.8	3.6	3.7
Fixed Asset Turnover		13.7	10.4	9.6	10.9
Equity Turnover		8.4	7.2	6.2	5.9

Valuation parameters		FY17	FY18	FY19E	FY20E
Year to March					
Adj. Diluted EPS (INR)		16.3	22.2	31.5	41.1
Y-o-Y growth (%)		156.0	36.6	41.8	30.3
Adjusted Cash EPS (INR)		16.5	25.1	36.1	45.0
Diluted P/E (x)		67.5	49.4	34.8	26.7
P/B (x)		12.8	7.8	6.6	5.5
EV / Sales (x)		1.8	1.4	1.1	1.0
EV / EBITDA (x)		35.2	25.8	21.8	17.7
Dividend Yield (%)		-	0.3	0.5	0.6

Additional Data

Directors Data

Ravindra Kishore Sinha	Chairman	Arun Batra	Independent Director
Rituraj Kishore Sinha	Managing Director	Amrendra Prasad Verma	Independent Director
Rita Kishore Sinha	Non-Executive Director	Jayanta Kumar Basu	Non-Executive Director
Uday Singh	Wholetime Director and CEO	T C A Ranganathan	Independent Director
Arvind Prasad	Director (Finance)	Devdas Apte	Additional Director
A K Mattoo	Independent Director		

Auditor - Saxena & Saxena

**as per last available data*

Fund holding

	Perc. Holding		Perc. Holding
Sundaram Asset Management	1.58	Tata Asset Management Ltd	0.42
BNP Paribas Asset Management Global	1.12	Credit Agricole Group	0.42
IDFC Mutual Fund	1.06	BNP Paribas Asset Management India	0.34
Reliance Capital Trustee Co Ltd	0.84	Principal Financial Group	0.27
ABSL Asset Management	0.48	Canara HSBC Oriental Bank of Commerce Fund	0.21

**as per last available data*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
10 Aug 2017	Kiduja India Ltd	Buy	500000	879.80

**as per last available data*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
No Data Available			

**as per last available data*

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Coverage group(s) of stocks by primary analyst(s): Business Services

Qess Corp Ltd, Security and Intelligence Services India Ltd, TeamLease Services Ltd

Recent Research

Date	Company	Title	Price (INR)	Recos
24-Jul-18	Teamlease Services	Upping the ante; <i>Result Update</i>	2,800	Buy
26-Jun-18	SIS India (Coffee with CEO)	Moving towards leadership; <i>Visit Note</i>	1,102	Buy
18-May-18	Qess Corp	Staffing business gains market leadership; <i>Result Update</i>	1,159	Buy

Distribution of Ratings / Market Cap

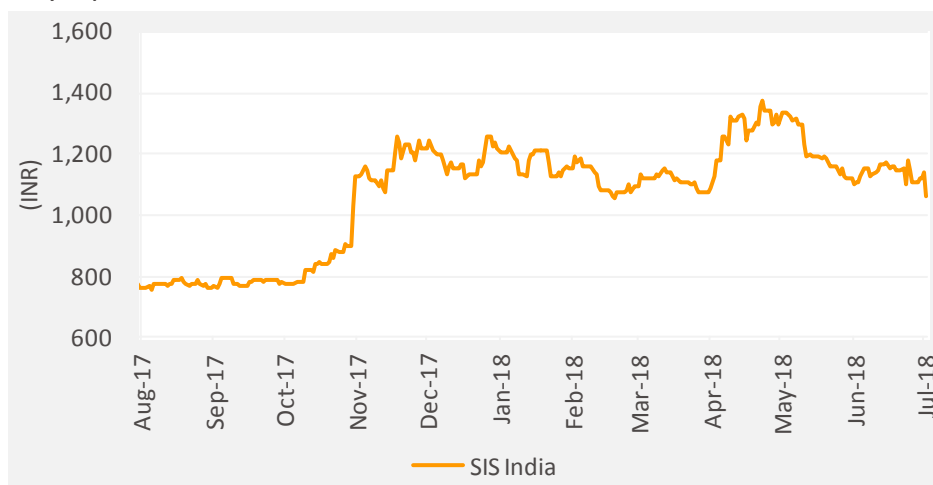
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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