In 1994, there were 74 IPOs in one week. Only a handful of them are currently listed and traceable. The others have all just DISAPPEARED. We believe that the situation today is similar – the economy is in shambles, stock markets are in doldrums and companies are coming out with IPOs when it is logically one of the worst times for public offerings. As per our information, around 25 IPOs are lined-up over the next two months. To substantiate our point, the Government has delayed the IPOs of a few public sector undertakings (PSUs) due to poor market conditions. We wonder what the managements, investment bankers and stock brokers think of all those companies that are coming out with their IPOs. Most of these companies have absolutely amazing financials, which are just too good to be true. We believe that in almost all cases, they are! These numbers are fudged and companies have resorted to various window dressing techniques to show a healthy financial position, to get a valuation from the market and subsequently burn investors' cash. Hence, we recommend investors to generally stay away from the IPOs that are lined-up in the coming months.

IPO note - Taksheel Solutions Price band Rs130-150 2nd Oct'2011

Taksheel Solutions

Taksheel solution is a provider of software and telecommunication services. The company primarily focuses on the wealth management section within the financial services vertical. The company has footprints in data warehousing and business intelligence as well. It has taken baby steps in the telecom space with a few telecom products. In FY2011, the company had a turnover of Rs14.7cr, both through direct client engagement with its own resources and subcontracting to third parties.

Key Strengths:

- Management's ability to leverage opportunities by subcontracting instead of direct employment.

As per the company, the current number of employees stands at 70 (as of March 31, 2011 this number was 40 employees). This implies that most of the revenues have been generated at a relatively low employee base. Most of the profits are earned from commission cuts through subcontracting. But this very strength itself may prove to be their bane, as discussed later.

Key Risks

- High bench strength is a pre-requisite to maintain strong growth in the software services business. The company does not seem to have this.

- The company has no wealth management products of its own. Thus it is difficult to be a niche player in the wealth management space.

- The company is not a primary vendor for any of its clients. Typically in the wealth management industry, primary vendors are preferred vendors for any software spending in terms of budget allocation for new and existing projects. Therefore such vendors can have better visibility in terms of revenue targets and resource requirement. For Taksheel solutions revenue growth becomes abrupt and prone to sudden fluctuations.

- Marketing of their telecom products is in its nascent stage and the company's entry into the telecom vertical is fairly recent.

- Again during discussions with the management, we gather that for its single largest client it provides $4 million worth of services. But there is no guarantee of repeat business because of the company's predominantly subcontracting model, which has a very high attrition risk attached to it.

In short the company has no unique differentiating factor, except for the management's capability to have a profitable sub-contracting model which does not seem sustainable.

Understanding the software services business

The software services typically fall under industry and service vertical.

The industry vertical is typically the industry which the company services such as:

banking & financial services, energy, resources & utilities, government, life sciences, healthcare, high tech, insurance, manufacturing, media & information services, retail & consumer products, telecom, travel, transportation & hospitality. These can again be sub-divided into sub-verticals.

The service vertical is the kind of services the company provides such as:

IT services, IT infrastructure services, enterprise solutions, consulting, business process outsourcing, business intelligence & performance management.

The company's growth prospects depend on the number of industry and service verticals the company is in –more the number of verticals, lesser the risk and more chances of growth.

The other way of growing is being a pioneer in products of a particular service or industry practice.

e.g. being a banking product specialist.

Taksheel solutions in the services arena:

The company operates in two industry verticals - finance and telecom (recently started). One clearly mentioned service vertical in which it has managed to make footprints is in business intelligence and data warehousing.

In none of these verticals does it offer any unique services, nor does it have the bench strength or the experience to execute large projects (100 and above resources in a single project), or even a medium size projects (20 and above resources in a single project)

The telecom product has not developed into a recognizable revenue generating model yet and is largely untested.

SOA architecture implementation is neither a unique nor a recent development. Taksheel is one the many companies which involves itself in SOA implementation.

Current Industry Scenario

The BFSI industry is in turmoil. This will certainly affected the body-shopping companies and small time contractors who form the bulk of resources laid off during cost cutting measures.

Valuation & recommendation:

The software services business is primarily a commodity business. In the absence of any strong products, the simplest performance measure is the growth in the billable employees/resources in the company.

Considering that the company has started in 1999. As per the company's numbers, on an average the company has added roughly *seven* resources annually. But what is remarkable is that as of March 2011 the company had 40 employees (CARE report). So the company claims to have almost doubled its employee base in a few months.

Pre-IPO share capital of the company is Rs16.3cr. Through the IPO the company plans to issue 55,00,000 new shares in the price range of Rs130 to Rs150. This will constitute 25.17% of the fully diluted post-issue paid up capital of the company.

Rs cr	2007	2008	2009	2010	2011
Revenue	12	32	33	50	147
PAT	8	14	2	8	27

At the IPO price of Rs130-150, the stock would trade at 10-12x its FY2011 earnings as against its peers like Sonata, Geometric and Datamatics trading in range of 3-8x their respective FY2011 earnings.

In our opinion, undertaking an IPO with little foothold in the industry (in terms of resource presence) is unwarranted and premature. This IPO is an AVOID.

Sageraj Bariya

Ramprakash S