

Quick Heal Technologies

IPO Note

Quick Heal Technologies (QHTL) is a dominant player in the growing Retail IT Security software market in India with a market share of 30% and an active license user base of 7.13mn. ~87% of its customers are retail clients while the balance is made up of enterprises and government institutions. The company has laid the foundation in terms of product development, creating infrastructure for distribution and built a brand to further grow its overall business.

Leadership position in growing Retail IT Security market: The Indian IT Security software market is estimated to be at ₹1,500-1,800cr in 2015, of which, the retail market accounts for ~₹600-800cr. The retail market has grown from ~₹400-600cr in 2013 and is expected to post a CAGR of 20-25% over 2015-17E on the back of growing number of internet users. QHTL is best placed to benefit from the growing industry on the back of its brand visibility along with its wide distribution reach.

Strong distribution network with good brand equity: Despite facing competition from international as well as domestic players in India, QHTL has been able to successfully grow its business and establish a strong position across India on the back of its 19,000 retail channel partners. QHTL has also built support systems that include mobile, enterprise and government channel partners. The company has historically spent ~10% of its top-line on advertisement and is expected to allocate ~₹111cr from the IPO proceeds (over three years) to further improve its visibility, which in turn, will aid growth.

Debt free with healthy Cash Flow generation for future R&D needs: QHTL has a debt-free balance sheet and cash balance of ~₹107cr as of 1HFY2016. Over the past five years, QHTL is generating strong operating cash flows which have grown from ~₹49cr in FY2012 to ~₹77 in FY2015. We believe that the company generates sufficient cash flows to cover for R&D and technology up-gradation related expenses.

Outlook Valuation: QHTL has shown significant growth over FY2012-15, posting a revenue CAGR of 16.9% while its profitability has declined from ₹68cr in FY2012 to ₹54cr in FY2015 as the company was in an investment phase. Investments were incurred towards new product development for its Enterprise business and brand building.

On the valuation front, at the upper end of the price band, the pre-issue P/E works out to 41.2x its 1HFY2016 annualized earnings which we consider decent taking into account the company's brand image. Further, the company is confident of it being able to sustain its growth trajectory owing to its strong distribution network. Additionally, there is a two-year lead-lag on product development for the Enterprise business of which the company will reap benefits in future. **Thus, we recommend a Subscribe on the issue from a longer term perspective.**

Key Financial

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	1HFY2016
Net Sales	179	205	243	286	148
% chg	-	14.5	18.5	17.8	-
Net Profit	68	77	58	54	24
% chg	-	12.8	(24.1)	(7.8)	-
OPM (%)	53.5	51.3	43.0	32.1	29.7
EPS (₹)	11.0	12.4	9.4	8.6	3.9
P/E (x)	29.3	26.0	34.2	37.1	-
P/BV (x)	9.5	7.0	6.0	6.0	-
RoE (%)	32.4	27.0	17.6	16.2	-
RoCE (%)	44.5	35.3	28.2	21.6	-
EV/Sales (x)	10.6	9.0	7.6	6.5	-
EV/EBITDA (x)	19.8	17.6	17.8	20.2	-

Source: Company, Angel Research; Note: Valuation ratios based on pre-issue outstanding shares and at upper end of the price band

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Issue Open: February 8, 2016
 Issue Close: February 10, 2016

Issue Details

Face Value: ₹10

Present Eq. Paid up Capital: ₹62.2cr

Fresh Issue**: 0.78cr Shares

Offer for sale: 0.63cr Shares

Post Eq. Paid up Capital: ₹70cr

Market Lot: 45 Shares

Fresh Issue (amount): ₹250cr

Price Band: ₹311-321

Post-issue implied mkt. cap ₹2,186cr* - 2,248cr**

Note:*at Lower price band and **Upper price band

Book Building

QIBs	50%
Non-Institutional	15%
Retail	35%

Post Issue Shareholding Pattern(%)

Promoters Group	72.9
MF/Banks/Indian FIs/FIIs/Public & Others	27.1

Amarjeet S Maurya

+91 22 4000 3600 Ext: 6831

amarjeet.maurya@angelbroking.com

Milan Desai

+91 22 4000 3600 Ext: 6846

milan.desai@angelbroking.com

Company background

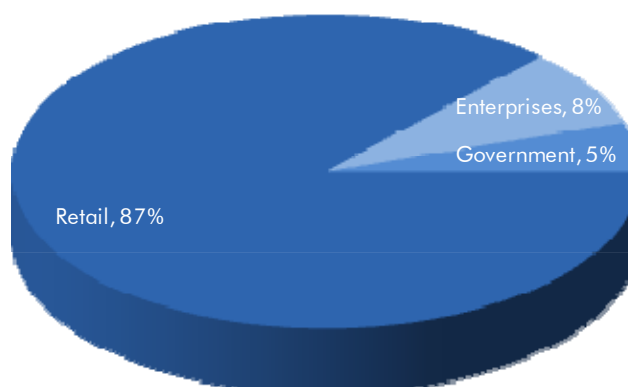
QHTL is one of the leading providers of security software products (antivirus) and solutions in India with a market share of over 30% in the retail space. Its end customers are home users, small offices and home offices, small and medium size Business units (SMB), enterprises, educational institutions, as well as government institutions. Its products are built for use across all platforms as well as devices (laptops, mobile, etc). It meets diverse user requirements which are spread across multiple price points. Its brand "Quick Heal" is well recognized (mainly for home users) and it has recently launched "Seqrite" range of solution for its Enterprise customers. As on December 31, 2015, the company had over 7.13mn active licenses spread across more than 80 countries and has installed more than 24.5mn licenses of its products. Till now, ~97% of its revenue comes from India. Retail sales account for ~87% of its overall sales, enterprises account for ~8% while government enterprises account for the balance 5% of sales. As of December 31, 2015, it has a network of over 19,000 retail channel partners, 349 enterprise channel partners, 319 government partners and 944 mobile channel partners.

Exhibit 1: Products Range

	Home Users	Enterprises
Desktops, Laptops and Tablets	Smartphones/ Mobiles	SMB, Enterprises, Educational and Government
Quick Heal Total Security	Quick Heal Mobile Security for Android	Endpoint Security
Quick Heal Internet Security	Fonetastic Free	Gateway security
Quick Heal AntiVirus Pro	Fonetastic Pro	Server security
Quick Heal Total Security for Mac	Quick Heal Gadget Security	
Quick Heal Tablet Security for Android		
Quick Heal Total Security for Android		
Quick Heal PCTuner 3.0		
Guardian NetSecure (basic antivirus solution)		

Source: RHP, Angel Research

Exhibit 2: Revenue break up (1HFY2016)



Source: Company, Angel Research

Issue details

The company is raising ₹250cr through fresh issue of equity shares in the price band of ₹311-321. In addition, the issue also consists of offer for sale of 62.7 lakh shares of which 36.8 lakh shares will be offered by the promoter entities and 25.9 lakh shares by Sequoia Capital. The fresh issue will constitute 11.1% of the post-issue paid-up equity share capital of the company assuming the issue is subscribed at the upper end of the price band.

Exhibit 3: Shareholding pattern

Particulars	Pre-Issue		Post-Issue	
	No. of shares	(%)	No. of shares	(%)
Promoters	5,47,10,720	87.9	5,10,30,720	72.9
Others	75,31,147	12.1	1,89,99,309	27.1
Total	6,22,41,867	100.0	7,00,30,029	100.0

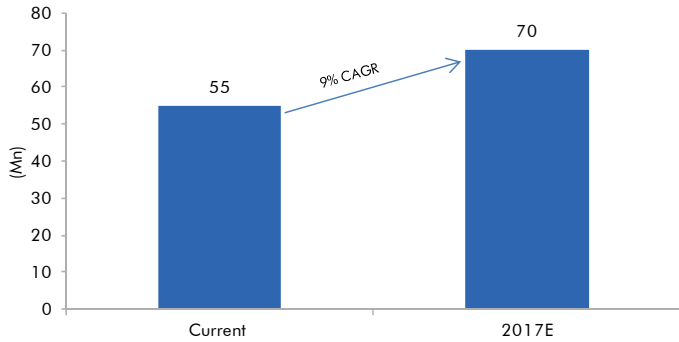
Source: Company, Angel Research

Objects of the offer

- The company estimates to use up to ₹111cr of the IPO proceeds towards advertising and sales promotion.
- It would incur capital expenditure for R&D related expenses amounting to ₹42cr.
- The company intends on utilize upto ₹28cr for purchase, development and renovation of office premises in Kolkata, Pune and New Delhi.
- The balance will be utilized for general corporate purposes.

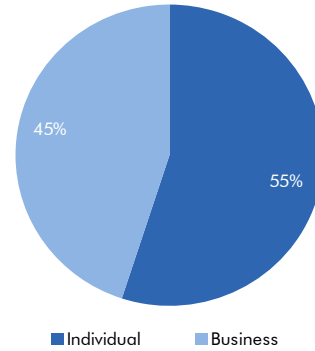
Industry story in charts

Exhibit 4: Growth in PCs installed



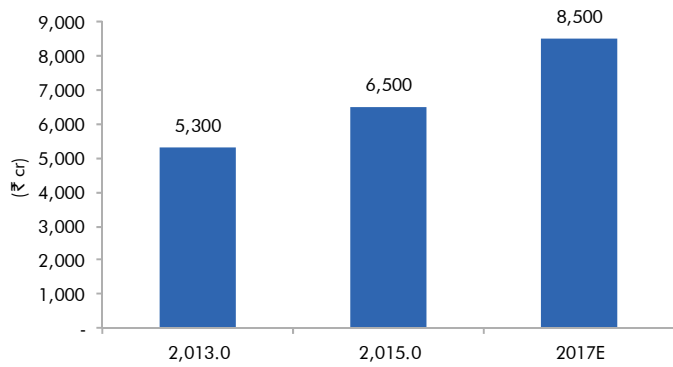
Source: Company, Angel Research

Exhibit 5: Segmental break-up



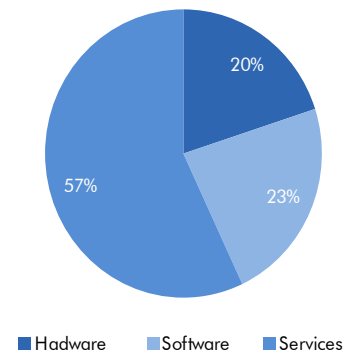
Source: Company, Angel Research

Exhibit 6: IT Security industry market size and its.....



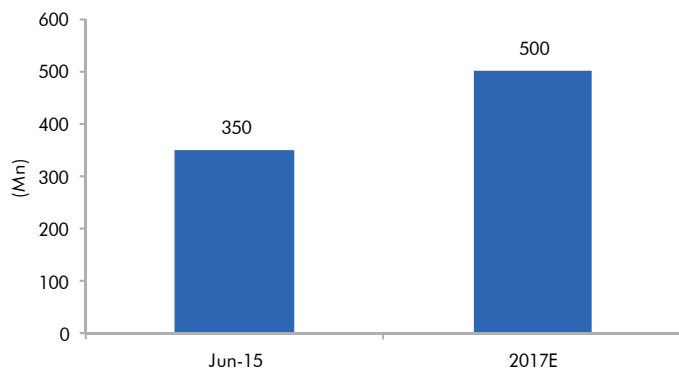
Source: RHP, Angel Research

Exhibit 7:.....Split by segment



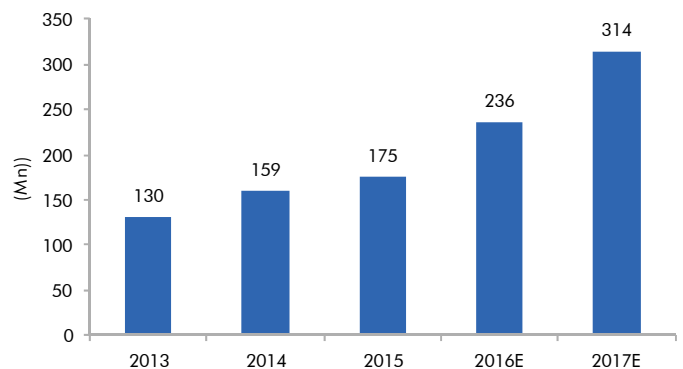
Source: RHP, Angel Research

Exhibit 8: Expected growth in no. of internet users



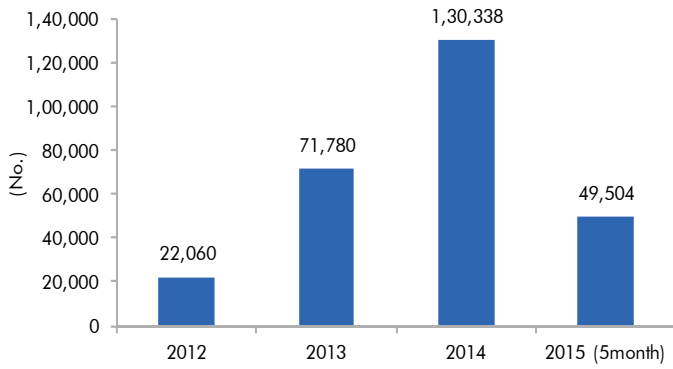
Source: Company, Angel Research

Exhibit 9: No. of mobile internet users in India



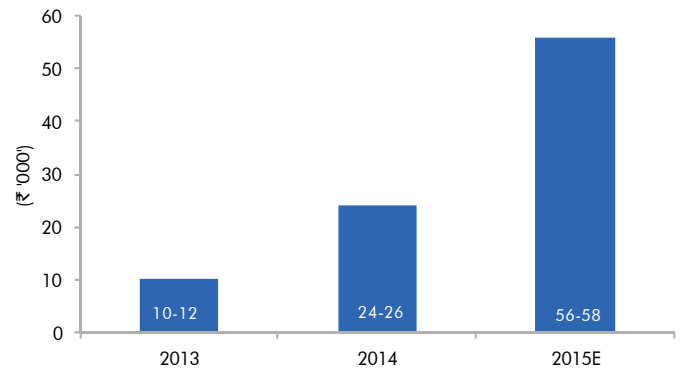
Source: Company, Angel Research

Exhibit 10: Historical data of Cyber attacks in India



Source: Company, Angel Research

Exhibit 11: Avg. Cost suffered per attack in India



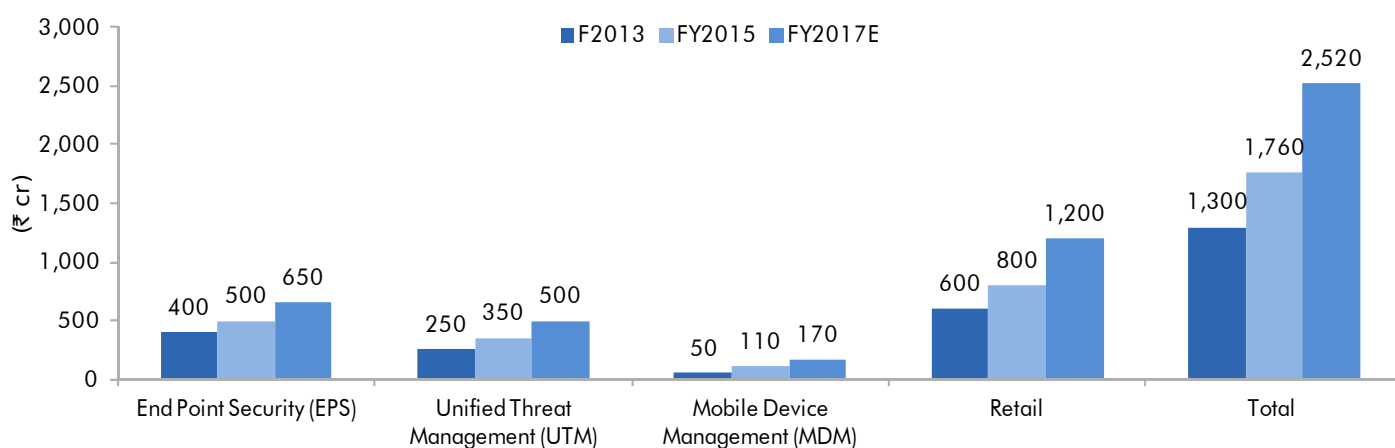
Source: Company, Angel Research

Investment rationale

Leadership position in a growing IT Security market

Currently, the IT Security software market in India is estimated to be at ~₹1500-1800cr which comprises of Retail, End Point Security (EPS), Unified Threat Management (UTM) and Mobile Device Management (MDM). Going forward, the overall industry is expected to grow to ~₹2,000-2,500cr by 2017E. Of the overall market, the retail segment forms the major portion and is currently estimated to be at ~₹600-800cr and is expected to post a CAGR of 20-25% over 2015-17E on the back of growing number of internet users.

Exhibit 12: Product Segments - IT Security market



Source: Company, Angel Research

Exhibit 13: IT Security Market (Product Segments) expected growth

	CAGR			
	EPS	UTM	MDM	Retail
FY2013-15	10-15%	15-20%	45-50%	10-15%
FY2015-17E	10-15%	15-20%	25-30%	20-25%

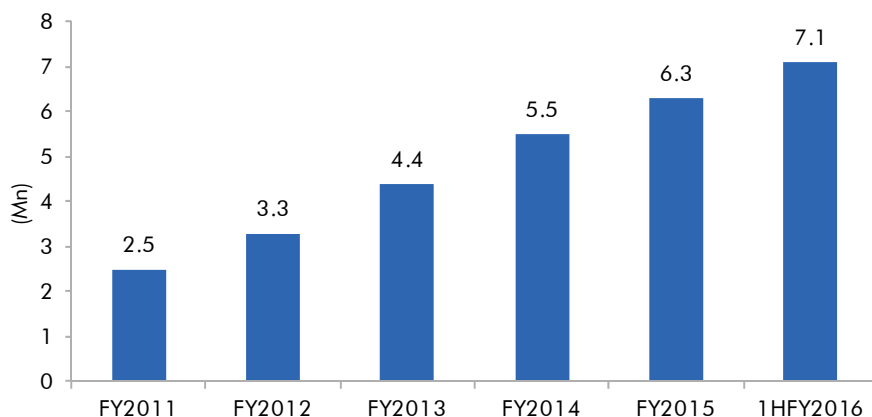
Source: Company, Angel Research

Quick Heal had over 7.13mn active licenses as on December 31, 2015 spread across India as well as outside of India

Currently the company is one of the leading providers of security software solutions in India with a market share of ~30% in the retail segment. It has over 7.13mn active licenses as of December 31, 2015 spread across India as well as outside India. Over the last four years the company has reported a ~26% CAGR in terms of active users. Going forward, we expect the growth momentum to continue as QHTL is best placed to benefit from the growing industry on the back of its brand visibility and its wide distribution reach.

Further, other segments like EPS, UTM and MDM are also growing at a healthy pace and we expect QHTL to benefit from its growing presence in the above mentioned categories.

Exhibit 14: Active license user trend

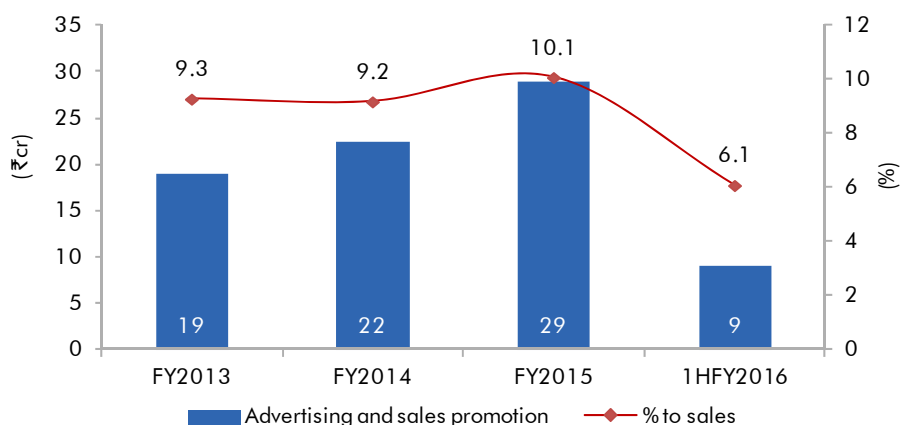


Source: Company, Angel Research

Strong distribution network with good brand equity

Despite facing competition from international as well as domestic players in India, QHTL has been able to successfully grow its business and establish a strong position across India on the back of its 19,000 retail channel partners, 349 enterprise channel partners, 319 government partners and 944 mobile channel partners, who act as distributors and resellers of its solutions. Further, QHTL conducts sales and marketing activities out of 64 offices and warehouses across 36 cities in India. As of December 31, 2015, the company had a sales & marketing team comprised of 400 employees who work closely with the company's channel partners.

Exhibit 15: Historical ad spend by QHTL



Source: Company, Angel Research

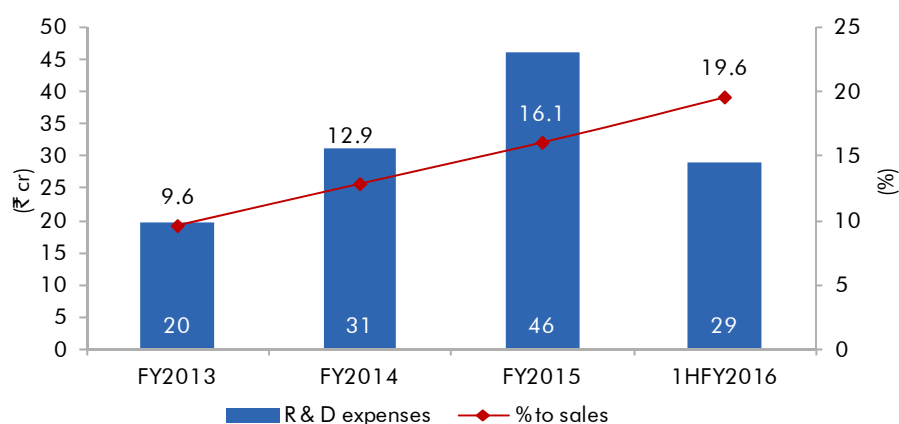
QHTL continuously does major marketing exercises for expanding dealer and retailer network. The company's media presence spans newspapers, magazines, news and entertainment TV channels, and FM radio channels in India. The company has historically spent ~10% of its top-line on advertisement and is expected to further spend ~₹111cr from IPO proceeds (over three years) to further improve its visibility which will aid growth.

Significant R&D and technology capabilities

As of December 31, 2015, the company had 1,396 employees, including 547 employees who comprise the R&D team.

QHTL has strong R&D capability that enables it to be competitive in an industry where technology forms the core competency. It has steadily increased its R&D expense from 9.6% of sales in FY2013 to 19.6% of sales as of 1HFY2016 and would be utilizing ₹42cr of the IPO proceeds to further invest in R&D. As of December 31, 2015, QHTL had 1,396 employees, of which 547 employees were part of its R&D team.

Exhibit 16: Historical R&D spend by QHTL



Source: Company, Angel Research

Debt free with healthy Cash Flow generation

QHTL has a debt free balance sheet and cash balance of ~₹107cr as on 1HFY2016. Over the past 5 years, QHTL is generating strong operating cash flows which have grown from ~₹49cr in FY2012 to ~₹77cr in FY2015. We believe that the company generates sufficient cash flows to cover for technology upgradation related expenses.

Valuation

Outlook Valuation: QHTL has shown significant growth over FY2012-15, posting a revenue CAGR of 16.9% while its profitability has declined from ₹68cr in FY2012 to ₹54cr in FY2015 as the company was in an investment phase. Investments were incurred towards new product development for its Enterprise business and brand building.

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Exhibit 17: Comparative Valuation

		P/E	P/BV	ROE	EV/Sales	EV/EBITDA
		(x)	(x)	(%)	(x)	(x)
Pre issue valuation ^						
QHTL*	FY2016	41.2	5.1	12.7%	6.4	21.5
Symantec Corporation*	FY2016	23.8	2.1	8.9%	1.9	12.3

Source: RHP, Note: *based on 1HFY16 annualised numbers; ^ based on price at upper band

Risks

Intense competition and lack of pricing power: QHTL faces stiff competition from both international and Indian companies like Symantec, Trend, Micro, Kaspersky, McAfee and others. This could levy pressure on the company's operating margin and lead to lower profitability.

Changes in technology: The IT security industry is subject to rapid changes in technology. Any change in technology or better technology adoption by other competitors could negatively affect the company's revenue.

Profit & Loss (consolidated)

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	1HFY16
Total operating income	179	205	243	286	148
% chg		14.5	18.5	17.8	-
Total Expenditure	83	100	138	194	104
Raw Material	9	10	11	16	8
Employee Cost	21	29	43	64	42
Other Expenses	54	62	84	114	55
EBITDA	96	105	104	92	44
% chg		9.9	(0.7)	(12.0)	
(% of Net Sales)	53.5	51.3	43.0	32.1	29.7
Depreciation & Amortisation	2	4	11	20	11
EBIT	94	101	94	72	33
% chg		7.7	(7.1)	(23.5)	
(% of Net Sales)	52.3	49.1	38.5	25.0	22.0
Interest & other Charges	-	-	-	-	-
Other Income	6	10	10	8	4
(% of PBT)	5.7	8.8	9.5	10.3	11.1
Recurring PBT	99	110	103	80	37
% chg		11.3	(6.4)	(22.8)	
Exceptional Exp/(inc)	-	-	17	-	-
PBT (reported)	99	110	86	80	37
Tax	31	34	28	26	13
(% of PBT)	31.3	30.4	32.1	32.6	34.1
PAT Reported	68	77	58	54	24
% chg		12.8	(24.1)	(7.8)	
(% of Net Sales)	38.1	37.5	24.0	18.8	16.3
Basic EPS (₹)	11.0	12.4	9.4	8.6	3.9
Fully Diluted EPS (₹)	11.0	12.4	9.4	8.6	3.9
% chg		12.8	(24.1)	(7.8)	(55.0)

Balance Sheet (consolidated)

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	1HFY16
SOURCES OF FUNDS					
Equity Share Capital	8	8	61	61	61
Reserves & Surplus	203	277	271	270	295
Shareholders' Funds	210	285	332	331	356
Minority Interest	-	-	-	-	-
Total Loans	-	-	-	-	-
Long-term provisions	0.4	-	-	-	-
Deferred Tax Liability	0	1	-	-	-
Total Liabilities	211	285	332	331	356
APPLICATION OF FUNDS					
Gross Block	19	38	82	111	150
Less: Acc. Depreciation	-	-	-	-	-
Net Block	19	38	82	111	150
Capital Work in Progress	24	29	55	74	49
Investments	100	139	131	130	96
Current Assets	78	97	92	91	87
Inventories	1	2	6	8	7
Sundry Debtors	66	77	69	65	58
Cash	8	10	10	13	11
Loans & Advances	4	7	6	6	8
Other Assets	0	0	0	0	4
Current liabilities	19	29	47	97	47
Net Current Assets	59	68	44	(6)	40
Long term loans and adv.	9	11	16	17	15
Other Non Current Assets	0	0	0	0	0
Deferred Tax Asset	-	-	4	5	5
Mis. Exp. not written off	-	-	-	-	-
Total Assets	211	285	332	331	356

Cash flow statement (consolidated)

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	1HFY16
Profit before tax	99	110	86	80	37
Depreciation	2	4	11	20	11
Change in Working Capital	(19)	(10)	(5)	13	(1)
Interest / Dividend (Net)	(5)	(7)	(8)	(7)	(3)
Direct taxes paid	(29)	(30)	(41)	(30)	(10)
Others	1	0	17	1	(0)
Cash Flow from Operations	49	68	61	77	34
(Inc.)/ Dec. in Fixed Assets	(9)	(33)	(77)	(66)	(25)
(Inc.)/ Dec. in Investments	(44)	(29)	18	13	37
Cash Flow from Investing	(53)	(63)	(59)	(53)	12
Issue of Equity	-	-	-	-	-
Inc./(Dec.) in loans	-	-	-	-	-
Dividend Paid (Incl. Tax)	-	(1)	(2)	(17)	(49)
Interest / Dividend (Net)	-	-	-	-	-
Cash Flow from Financing	-	(1)	(2)	(17)	(49)
Inc./(Dec.) in Cash	(4)	4	(1)	7	(2)
Opening Cash balances	6	3	6	5	13
Effect of Foreign exchange diff.	-	-	(0)	-	-
Closing Cash balances	3	6	5	13	10

Key Ratios

Y/E March	FY2012	FY2013	FY2014	FY2015
Valuation Ratio (x)				
P/E (on FDEPS)	29.3	26.0	34.2	37.1
P/CEPS	28.4	24.6	28.9	27.0
P/BV	9.5	7.0	6.0	6.0
Dividend yield (%)	0.1	0.1	0.5	2.3
EV/Sales	10.6	9.0	7.6	6.5
EV/EBITDA	19.8	17.6	17.8	20.2
EV / Total Assets	8.2	5.9	4.9	4.3
Per Share Data (₹)				
EPS (Basic)	11.0	12.4	9.4	8.6
EPS (fully diluted)	11.0	12.4	9.4	8.6
Cash EPS	11.3	13.1	11.1	11.9
DPS	0.2	0.3	1.5	7.4
Book Value	33.8	45.8	53.4	53.3
Returns (%)				
ROCE	44.5	35.3	28.2	21.6
Angel ROIC (Pre-tax)	91.1	74.5	48.9	37.9
ROE	32.4	27.0	17.6	16.2
Turnover ratios (x)				
Asset Turnover (Gross Block)	9.5	5.3	3.0	2.6
Inventory / Sales (days)	1	4	9	10
Receivables (days)	134	138	104	83
Payables (days)	29	37	44	48
WC cycle (ex-cash) (days)	106	105	70	45

Note: Valuation ratios based on pre-issue outstanding shares and at upper end of the price band

Research Team Tel: 022 - 39357800

E-mail: research@angelbroking.com

Website: www.angelbroking.com

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