

Hexaware Technologies

BUY

‘Mobi’lised for growth

Hexaware has acquired Mobiquity Inc. for an all-cash consideration of USD 182mn (at 2.6x EV/rev). Mobiquity is a design and digital consulting firm (USD 70mn rev, growing at 24% CAGR) supported by strong partnerships with AWS and Backbase.

USD 131mn will be paid upfront, USD 30mn in Jan-20 and an earn-out of (upto) USD 21mn is due by Oct-20. Current cash on Hexaware’s balance sheet implies low external borrowing requirement (USD 21mn), well under annual OCF.

The acquisition fits well strategically for Hexaware, given (1) Portfolio augmentation with strong front-end capabilities across verticals (BFS, Healthcare, Retail dominant), (2) Revenue synergies/cross-sell on strong client base (most clients are net-new for Hexaware) and opportunity to increase bill-rate (Mobiquity offshore bill-rate higher than Hexaware by ~50%), (3) Backbase partnership to improve Hexaware’s BFS practice with broader inroads into banking (currently present in capital markets and mortgage segments), and (4) Access to a strong developer pool (700 globally, 225 in India) and, significantly, (5) A consulting partnership with AWS.

We increase rev estimates by 5.6/9.2% for CY19/20E factoring the acquisition and lower organic growth in CY20 (loss of a large net-new deal). Our CY20E EPS is unchanged (14.5% EPS CAGR over CY18-21E). Maintain **BUY**, with TP of 440, 16x Jun-21E EPS. Organic acceleration is expected in 2HCY19, supported by strengthening of the Adobe/Pega ecosystem and on deal momentum.

Highlights from the call and meeting with Hexaware CEO

- Mobiquity has grown at 24% CAGR over the past three years with CY18 revenue at USD 70mn. Revenue is largely project-based. However, there is high repeat business from existing clients (no change in top-10 accounts in the recent past).
- Its client base includes Amazon, Backbase, Rabobank, Vanguard, Philips, Wawa, Walmart, Nestle, Millicom, AB Inbev, Otsuka and Bank ABC. Top-20 clients contribute 89% to its revenue.
- The company has ~700 employees with 225 located in India centers of Ahmedabad/Pune with 3x growth in India headcount over the past 3 years. Attrition is 17%; ~60 employees work in design and strategy.
- Competition includes Fjord (Accenture). US-Europe revenue-mix in Mobiquity stands at 55-45%. Netherlands is the anchor location in Europe, with predominantly Backbase developers.
- Hexaware plans to retain the ‘Mobiquity’ brand and company structure. Mobiquity has gross margins of ~41%, EBITDA% in low teens and zero debt.

Financial Summary

YE March (Rs bn)	CY17	CY18	CY19E	CY20E	CY21E
Net Revenues	39.42	46.48	56.50	66.78	74.89
EBITDA	6.55	7.34	8.41	10.32	11.65
APAT	4.99	5.83	6.29	7.77	8.79
Diluted EPS (Rs)	16.8	19.6	21.1	26.1	29.5
P/E (x)	20.6	17.6	16.3	13.2	11.7
EV / EBITDA (x)	14.8	12.9	12.3	10.0	8.5
RoE (%)	26.6	26.5	24.6	26.1	25.2

Source: Company, HDFC sec Inst Research

INDUSTRY	IT
CMP (as on 14 Jun 2019)	Rs 345
Target Price	Rs 440
Nifty	11,823
Sensex	39,452

KEY STOCK DATA	HEXW IN
Bloomberg	298
No. of Shares (mn)	103/1,474
MCap (Rs bn) / (\$ mn)	427
6m avg traded value (Rs mn)	

STOCK PERFORMANCE (%)			
52 Week high / low	Rs 558/294		
	3M	6M	12M
Absolute (%)	2.6	5.2	(23.0)
Relative (%)	(1.9)	(4.5)	(33.9)

SHAREHOLDING PATTERN (%)	Dec-18	Mar-19
Promoters	62.66	62.59
FIs & Local MFs	10.97	12.35
FPIs	17.14	16.06
Public & Others	9.23	9.00
Pledged Shares	0.00	0.00

Source : BSE

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Mobiquity's CEO was earlier CEO at Alliance Global Services (acquired by EPAM)

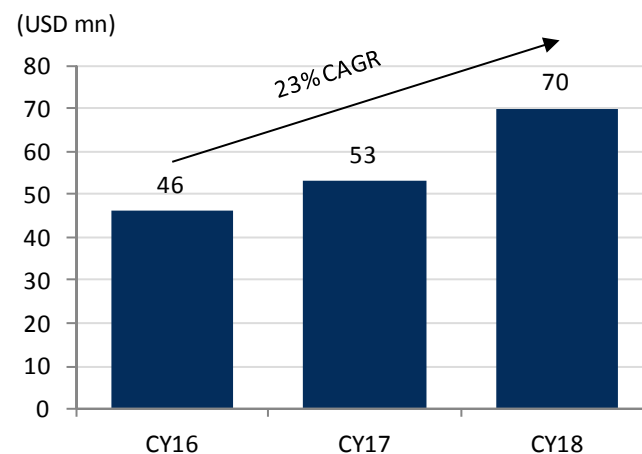
Guidance of 20% rev growth, flat EBITDA% and EPS neutral impact (ex-transaction cost) for CY19E

Hexaware has proven track record in client mining, strong scale up in USD 5-10mn band

Meeting highlights (continued...)

- Hexaware evaluated ~130 assets over the past 1.5 years and is unlikely to do another acquisition for the next 1-1.5 years. The company had earmarked USD 250-300mn for acquisitions over 2-3 years for 2/3 acquisitions.
- Mobiquity's shareholders (not a related party with Barings) included multiple financial institutions/PEs who were investors since 2011. Mobiquity employees have a low shareholding, thus lowering the risk of keyman exit post the earn-out.

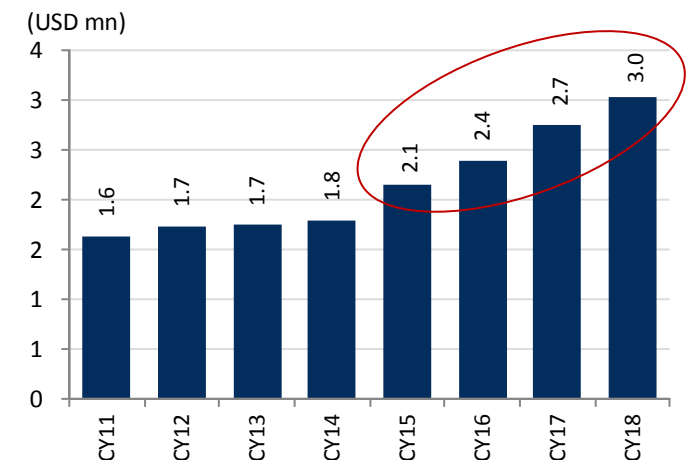
Mobiquity's Revenue Trend



Source: Company, HDFC sec Inst Research

- Post the deal, Hexaware has guided for a 20% revenue growth, flat EBITDA% and EPS-neutral impact (ex-transaction cost) for CY19E.
- Delivery/office locations in US include Boston, Florida, Philadelphia, New York and in SFO.
- Hexaware's large Nordic Net-new deal of TCV USD 100mn won in 4QCY18 has dropped off the order book due to automation plans of the client, subsequent scope expected to be lower for Hexaware. There is large growth headroom for Hexaware's IMS business as current scale only 0.2% of the entire market.

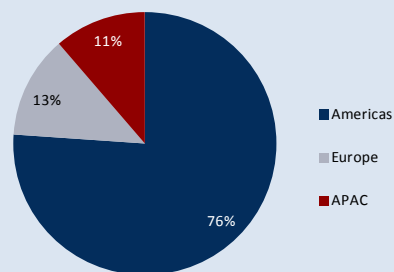
Hexaware's Strong Account Mining: Revenue/Client (USD mn)



Source: Company, HDFC sec Inst Research

Hexaware's growth has been led by Mfg/Consumer and Healthcare/Insurance verticals

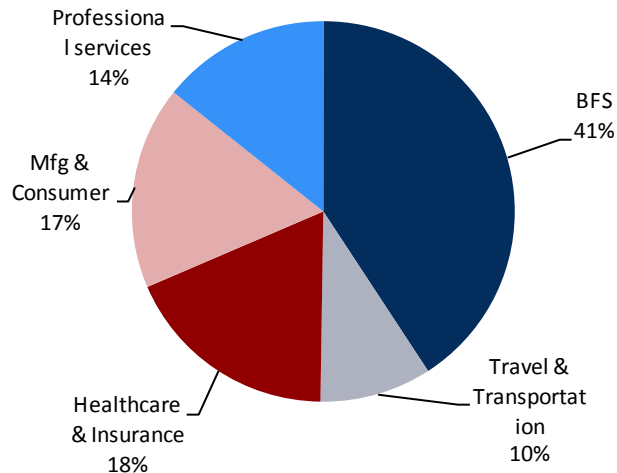
Revenue Mix by Geographies (%)



Source: Company, HDFC sec Inst Research, 1QCY19

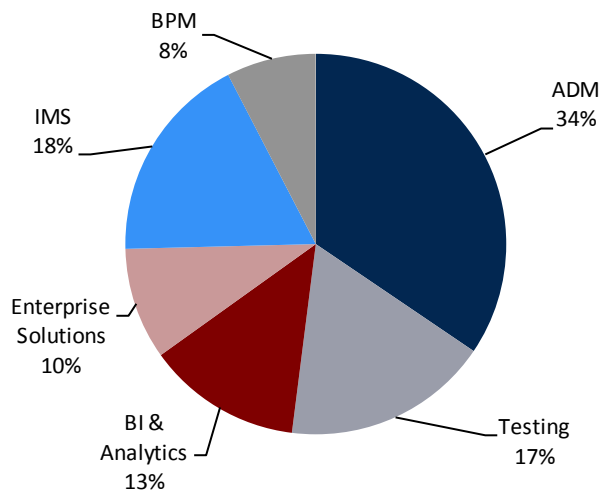
IMS and BPM led growth within services-lines

Revenue Mix by Verticals (%)



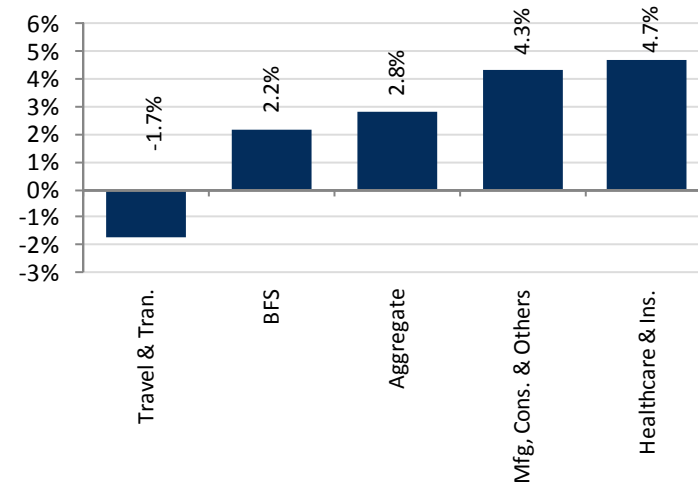
Source: Company, HDFC sec Inst Research, 1QCY19

Revenue Mix by Service-Lines (%)



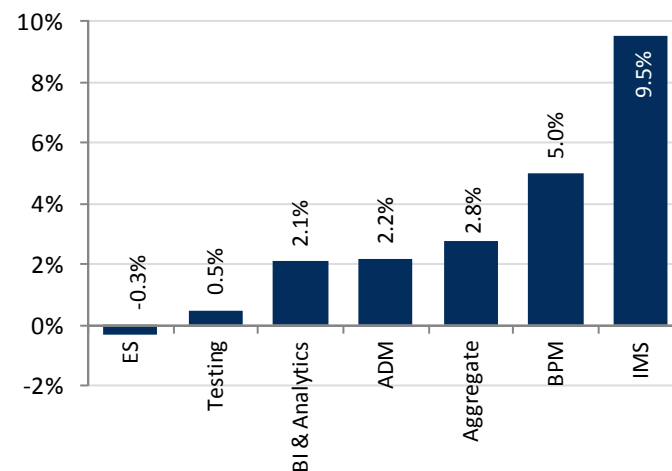
Source: Company, HDFC sec Inst Research, 1QCY19

Growth by Verticals (8-qtr CQGR%)



Source: Company, HDFC sec Inst Research, *includes Professional services & others

Growth by Service-Lines (8-qtr CQGR%)



Source: Company, HDFC sec Inst Research

We have lowered organic growth est. for CY20, factored upfront payment of Rs 9.17bn and deferred consideration of Rs 3.57bn (in CY20E) towards acquisition

USD rev growth of 19.0% and 18.3% for CY19/20E includes 6% and 7% inorganic impact, respectively

Factored EBITDA% at 14.9/15.5/15.6% for CY19/20/21E

Change In Estimates

Particulars	OLD	NEW	% change
CY19E			
Revenue (USD mn)	764	806	5.6
Revenue (Rs bn)	53.50	56.50	5.6
EBITDA (Rs bn)	8.26	8.41	1.8
EBITDA margin (%)	15.4	14.9	(56)bps
EPS (Rs)	21.4	21.1	(1.0)
CY20E			
Revenue (USD mn)	874	954	9.2
Revenue (Rs bn)	61.16	66.78	9.2
EBITDA (Rs bn)	9.57	10.32	7.9
EBITDA margin (%)	15.6	15.5	(18)bps
EPS (Rs)	26.1	26.1	0.1
CY21E			
Revenue (USD mn)	980	1,070	9.2
Revenue (Rs bn)	68.59	74.89	9.2
EBITDA (Rs bn)	10.79	11.65	7.9
EBITDA margin (%)	15.7	15.6	(18)bps
EPS (Rs)	29.4	29.5	0.5

Source: HDFC sec Inst Research

Peer Set Comparison

Company	MCap (Rs bn)	CMP (Rs)	TP (Rs)	RECO	EPS (Rs)				P/E (x)				RoE (%)			
					FY18	FY19	FY20E	FY21E	FY18	FY19	FY20E	FY21E	FY18	FY19	FY20E	FY21E
TCS	8,460	2,255	2,410	BUY	68.8	83.9	91.1	101.3	32.8	26.9	24.7	22.2	30.1	36.1	37.2	38.9
Infosys	3,221	740	755	NEU	33.8	36.4	37.5	41.9	21.9	20.4	19.7	17.7	24.5	23.7	23.2	23.6
Wipro	1,703	299	250	SELL	14.0	15.8	16.5	17.9	21.3	18.9	18.1	16.7	16.5	17.3	16.9	17.0
HCL Tech	1,513	1,087	1,250	BUY	64.7	74.6	77.3	89.1	16.8	14.6	14.1	12.2	25.3	26.0	23.8	24.2
TechM	651	740	652	SELL	43.2	48.9	49.6	54.3	17.1	15.2	14.9	13.6	21.5	22.0	21.1	21.0
Tier-1 IT Median									21.3	18.9	18.1	16.7	24.5	23.7	23.2	23.6
LTI	308	1,772	2,095	BUY	66.9	87.3	93.0	104.6	26.5	20.3	19.1	16.9	33.2	34.6	30.1	28.6
Mphasis	178	958	1,330	BUY	45.4	57.7	62.0	73.8	21.1	16.6	15.4	13.0	14.6	20.0	20.8	21.8
LTTS	181	1,736	1,860	BUY	45.5	68.0	71.4	93.0	38.1	25.5	24.3	18.7	27.7	32.0	27.5	30.0
Mindtree	159	971	1,040	NEU	32.3	44.2	51.6	57.8	30.0	22.0	18.8	16.8	21.4	24.9	24.9	25.0
Hexaware *	102	345	440	BUY	16.8	19.6	21.1	26.1	20.6	17.6	16.3	13.2	26.6	26.5	24.6	26.1
Cyient	60	536	595	NEU	38.6	43.6	47.2	51.6	13.9	12.3	11.3	10.4	18.1	19.5	19.5	19.0
Tata Elxsi	54	861	945	NR	38.5	46.6	46.0	52.4	22.3	18.5	18.7	16.4	37.0	34.5	27.7	26.5
Zensar	58	256	305	BUY	10.6	13.8	16.0	19.1	24.1	18.5	16.0	13.4	15.1	17.0	17.1	17.8
Persistent	50	630	645	NEU	40.6	45.9	44.1	49.5	15.5	13.7	14.3	12.7	16.0	15.7	14.2	14.7
eClerx	34	891	815	SELL	74.1	61.7	67.8	74.1	12.0	14.4	13.1	12.0	24.1	18.1	18.2	19.6
Sonata	37	357	480	BUY	18.6	24.0	26.9	29.9	19.2	14.9	13.3	11.9	31.0	35.1	34.2	33.8
Intellect	34	275	313	BUY	3.7	8.1	11.0	15.9	NM	34.0	25.0	17.2	6.7	11.1	12.6	15.9
Majesco	14	491	715	BUY	(1.5)	18.3	26.4	34.8	NM	26.8	18.6	14.1	NM	8.4	10.4	12.4
HGS	13	638	770	NR	96.5	72.5	86.4	96.4	6.6	8.8	7.4	6.6	14.3	9.8	10.7	10.9
Mastek	11	473	657	BUY	27.8	40.6	44.7	52.2	17.0	11.7	10.6	9.1	13.7	16.1	14.8	15.4
Tier-2 IT Median									20.6	17.6	16.0	13.2	19.8	19.5	19.5	19.6

Company	MCap (USD bn)	CMP USD	TP	RECO	EPS (USD)				P/E (x)				RoE (%)			
					FY18	FY19E	FY20E	FY21E	FY18	FY19E	FY20E	FY21E	FY18	FY19E	FY20E	FY21E
Accenture	124	185	NA	NR	5.6	6.5	7.3	8.0	33.3	28.6	25.3	23.2	41.7	42.0	39.9	36.7
Cognizant	35	62	NA	NR	2.5	3.6	3.9	4.3	24.4	17.2	15.8	14.4	14.1	19.0	18.2	19.1
Capgemini^	18	97	NA	NR	4.9	4.4	6.5	7.2	19.9	22.2	14.8	13.5	11.5	10.1	13.3	13.5
Global IT Median									24.4	22.2	15.8	14.4	14.1	19.0	18.2	19.1

Source: HDFC sec Inst Research, Bloomberg, *Dec YE, ^CMP and EPS in EUR terms

Consolidated Income Statement

YE December (Rs bn)	CY17	CY18	CY19E	CY20E	CY21E
Net Sales (USD mn)	607	678	806	954	1,070
Growth (%)	15.6	11.6	19.0	18.3	12.1
Net Sales	39.42	46.48	56.50	66.78	74.89
Growth (%)	11.5	17.9	21.6	18.2	12.1
Employee Expenses	21.43	24.80	30.11	34.09	38.16
Other Operating Expenses	11.44	14.34	17.97	22.37	25.09
EBITDA	6.55	7.34	8.41	10.32	11.65
EBITDA (%)	16.6	15.8	14.9	15.5	15.6
EBITDA Growth (%)	13.3	12.0	14.6	22.7	12.8
Depreciation	0.63	0.65	0.87	1.02	1.12
EBIT	5.92	6.69	7.54	9.30	10.52
Other Income	0.49	0.58	0.32	0.48	0.52
Interest	0.00	0.00	0.07	0.13	0.13
PBT	6.40	7.27	7.80	9.66	10.92
Tax (incl deferred)	1.41	1.43	1.50	1.88	2.13
RPAT	4.99	5.83	6.29	7.77	8.79
APAT	4.99	5.83	6.29	7.77	8.79
APAT Growth (%)	18.9	16.9	7.9	23.5	13.1
EPS	16.8	19.6	21.1	26.1	29.5
EPS Growth (%)	18.9	16.9	7.9	23.5	13.1

Source: Company, HDFC sec Inst Research

Consolidated Balance Sheet

YE December (Rs bn)	CY17	CY18	CY19E	CY20E	CY21E
SOURCES OF FUNDS					
Share Capital - Equity	0.59	0.59	0.60	0.60	0.60
Reserves	19.48	23.32	26.75	31.66	37.05
Total Shareholders' Funds	20.07	23.92	27.35	32.25	37.64
Total Debt	-	-	2.10	2.10	2.10
Net Deferred Taxes	(1.34)	(1.78)	(1.78)	(1.78)	(1.78)
Other non current liabilities	0.21	0.31	0.31	0.31	0.31
TOTAL SOURCES OF FUNDS	18.95	22.44	27.97	32.88	38.26
APPLICATION OF FUNDS					
Net Block	3.76	3.93	5.21	5.31	5.37
CWIP	2.56	2.24	2.24	2.24	2.24
Goodwill	1.66	1.81	9.45	12.50	12.50
Investments	0.02	0.03	0.03	0.03	0.03
Other non-current assets	1.58	1.67	1.67	1.67	1.67
Total Non Current Assets	9.58	9.68	18.59	21.75	21.81
Debtors	5.36	8.03	10.99	12.99	14.57
Cash & Equivalents	5.49	8.31	1.60	1.96	6.07
Other Current Assets	3.69	3.53	4.65	5.30	5.94
Total Current Assets	14.54	19.87	17.24	20.25	26.58
Creditors	2.20	3.30	3.87	4.57	5.13
Other Current Liabilities & Provns	2.97	3.81	3.99	4.55	5.00
Total Current Liabilities	5.17	7.11	7.86	9.13	10.13
Net Current Assets	9.37	12.76	9.38	11.12	16.45
TOTAL APPLICATION OF FUNDS	18.95	22.44	27.97	32.88	38.26

Source: Company, HDFC sec Inst Research

Consolidated Cash Flow

YE December (Rs bn)	CY17	CY18	CY19E	CY20E	CY21E
Reported PBT	6.40	7.27	7.80	9.66	10.92
Non-operating & EO items	0.37	0.33	(0.26)	(0.39)	(0.42)
Interest expenses	0.00	0.00	0.07	0.13	0.13
Depreciation	0.63	0.65	0.87	1.02	1.12
Working Capital Change	(0.90)	(1.17)	(3.32)	(1.39)	(1.21)
Tax paid	(1.75)	(1.59)	(1.50)	(1.88)	(2.13)
OPERATING CASH FLOW (a)	4.76	5.49	3.64	7.14	8.40
Capex	(0.95)	(0.61)	(9.78)	(4.18)	(1.18)
Free cash flow (FCF)	3.81	4.88	(6.13)	2.97	7.23
Non-operating income	0.02	0.07	0.26	0.39	0.42
INVESTING CASH FLOW (b)	(0.94)	(0.54)	(9.52)	(3.79)	(0.76)
Debt Issuance	-	-	2.10	-	-
Interest expenses	(0.00)	(0.00)	(0.07)	(0.13)	(0.13)
FCFE	3.81	4.88	(4.10)	2.84	7.10
Share capital Issuance	(0.01)	0.00	0.00	-	-
Dividend	(2.81)	(2.51)	(2.87)	(2.87)	(3.40)
FINANCING CASH FLOW (c)	(2.82)	(2.51)	(0.83)	(2.99)	(3.53)
NET CASH FLOW (a+b+c)	1.00	2.44	(6.71)	0.36	4.11
Closing Cash & Equivalents	5.49	8.31	1.60	1.96	6.07

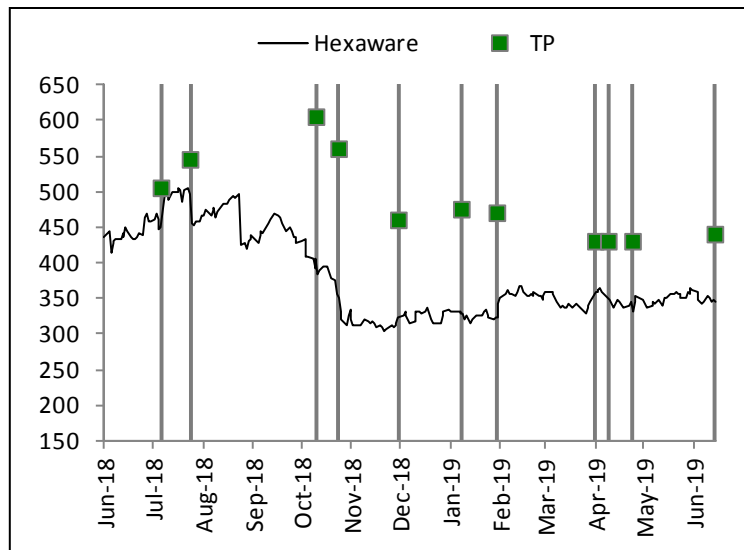
Source: Company, HDFC sec Inst Research

Key Ratios

	CY17	CY18	CY19E	CY20E	CY21E
PROFITABILITY (%)					
EBITDA Margin	16.6	15.8	14.9	15.5	15.6
APAT Margin	12.7	12.6	11.1	11.6	11.7
RoE	26.6	26.5	24.6	26.1	25.2
RoIC or Core RoCE	36.2	38.9	30.1	26.2	26.9
RoCE	28.2	28.2	25.2	25.9	25.0
EFFICIENCY					
Tax Rate (%)	22.0	19.7	19.3	19.5	19.5
Fixed Asset Turnover (x)	3.3	3.7	3.6	3.9	3.9
Debtors (days)	50	63	71	71	71
Other current assets (days)	34	28	30	29	29
Payables (days)	20	26	25	25	25
Other current liab & provn (days)	27	30	26	25	24
Cash Conversion Cycle (days)	36	35	50	50	51
Net Debt/EBITDA (x)	(0.8)	(1.1)	0.1	0.0	(0.3)
Net Debt/Equity (x)	(0.3)	(0.3)	0.0	0.0	(0.1)
Interest Coverage (x)	5,016	15,923	111	74	84
PER SHARE DATA					
EPS (Rs/sh)	16.8	19.6	21.1	26.1	29.5
CEPS (Rs/sh)	18.9	21.8	24.1	29.5	33.3
DPS (Rs/sh)	4.0	8.5	8.0	8.0	9.5
BV (Rs/sh)	67.4	80.3	91.9	108.3	126.4
VALUATION					
P/E	20.6	17.6	16.3	13.2	11.7
P/BV	5.1	4.3	3.8	3.2	2.7
EV/EBITDA	14.8	12.9	12.3	10.0	8.5
OCF/EV (%)	4.9	5.8	3.5	6.9	8.5
FCF/EV (%)	3.9	5.2	(5.9)	2.9	7.3
FCFE/mkt cap (%)	3.7	4.7	(4.0)	2.8	6.9
Dividend Yield (%)	1.2	2.5	2.3	2.3	2.8

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
6-Jul-18	450	BUY	505
25-Jul-18	496	BUY	545
10-Oct-18	404	BUY	605
25-Oct-18	351	BUY	560
30-Nov-18	315	BUY	460
8-Jan-19	329	BUY	475
31-Jan-19	323	BUY	470
1-Apr-19	345	BUY	430
9-Apr-19	351	BUY	430
25-Apr-19	333	BUY	430
17-Jun-19	345	BUY	440

Rating Definitions

BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

Disclosure:

We, **Apurva Prasad, MBA, Amit Chandra, MBA & Akshay Ramnani, CA**, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. HSL has no material adverse disciplinary history as on the date of publication of this report. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

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