

# Sonata Software

**BUY**

## Growth momentum to continue

We maintain BUY on Sonata based on strong performance in 3QFY20. IP-led strategy, strong Microsoft partnership and expansion of Microsoft D365 offerings is driving growth and aiding margin expansion in IT services business. DPS growth momentum will continue led by Microsoft and there is scope for margin expansion. We upgrade our FY22E Rev/EPS estimate by 6.1/5.1%. Our TP of Rs 422 is based on 12x (~4% premium to 5Y avg.) Dec-21E EPS.

### HIGHLIGHTS OF THE QUARTER

- International IT services (IITS) revenue increased 3.3% QoQ (+2.9% CC) to USD 46.8mn vs. est. of USD 46.0mn. Growth was led by IP-led (25.1% of rev, +7.2% QoQ) and will remain the key growth driver.
- Sonata has invested in strengthening the Microsoft relationship, which has yielded positive results. Dynamics D365 revenue has grown at an 8qtr CQGR of 7.3%. The next phase of growth will come from expansion of Microsoft D365 related offerings to others verticals (ISV was the focus earlier).
- IITS margin stood at 25.2% up 321bps QoQ higher than our est. of 22.5%. Margin expansion was aided by higher productivity, growth in IP-led revenue and near peak utilisation (88%). The sustainable IITS margin range is 22-24%, highest in Tier-2 IT.

### Financial Summary

YE March (Rs bn)	3QFY20	3QFY19	YoY (%)	2QFY20	QoQ (%)	FY18	FY19	FY20E	FY21E	FY22E
Net Revenues	12.37	8.44	46.6	7.03	75.9	24.54	29.61	37.47	40.17	44.67
EBIT	1.01	0.97	3.8	0.81	23.7	2.19	3.23	3.58	4.14	4.76
APAT	0.76	0.64	18.7	0.72	5.0	1.93	2.49	2.93	3.28	3.77
Diluted EPS (Rs)	7.3	6.2	18.7	7.0	5.0	18.6	24.0	28.2	31.6	36.3
P/E (x)						18.7	14.5	12.3	11.0	9.6
EV / EBITDA (x)						13.8	10.1	8.2	6.9	5.8
RoE (%)						31.0	35.1	35.7	35.3	35.8

Source: Company, HDFC sec Inst Research # Consolidated

- Total Revenue was up 75.9% QoQ to Rs 12.37bn due to 128.5/61.9% QoQ/YoY surge in Domestic Product & Services (DPS) revenue. DPS performance is measured on absolute EBITDA (Rs 0.27bn, +20/38.5% QoQ/YoY).
- IP-led (25%) and Digital (37% of rev) grew by 50.7/24.5% YoY respectively. ~52% of the incremental growth is coming from IP-led (higher margin).
- Collections in the DPS business has improved, net cash now stands at Rs 4.42bn vs Rs 2.80bn in 2Q. Bad debts in DPS business is only 0.06% of revenue.

### STANCE: Sustainable growth at reasonable valuations

Sonata's platformation strategy to provide IT services around IPs is yielding results. Growth in IP-led revenues is improving employee productivity and aiding margin expansion. Sonata is expanding Microsoft D365 platform and IP-led related services to new clients across verticals and geographies, which will drive growth. We like Sonata's IP-focussed business model, high RoE (~35%) and dividend yield of ~5%. The stock trades at a P/E of 11.0x FY21E, which is at 20% discount to Tier-2 IT median valuations. We expect IITS' USD revenue to grow 11.8/11.5% with margin of 23.3/23.7% in FY21/22E. Risks include deceleration in top-account, delay in collections and slowdown in US/Europe.

INDUSTRY	IT
<b>CMP (as on 27 Jan 2020)</b>	<b>Rs 347</b>
<b>Target Price</b>	<b>Rs 422</b>
Nifty	12,119
Sensex	41,155
KEY STOCK DATA	
Bloomberg	SSOF IN
No. of Shares (mn)	105
MCap (Rs bn) / (\$ mn)	37/511
6m avg traded value (Rs mn)	33
STOCK PERFORMANCE (%)	
<b>52 Week high / low</b>	<b>Rs 364/283</b>
	3M 6M 12M
Absolute (%)	9.5 5.1 9.1
Relative (%)	4.6 (3.5) (5.1)
SHAREHOLDING PATTERN (%)	
	Sep-19 Dec-19
Promoters	28.17 28.17
FIs & Local MFs	11.61 11.85
FPIs	13.23 12.75
Public & Others	46.99 47.23
Pledged Shares	0.00 0.00

Source : BSE

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**Consolidated revenue was boosted due to one large deal in the DPS business. The large deal in DPS has EBITDA margin of ~2.5%**

**Consolidated EBIT margin was down 344bps QoQ to 8.1% due to lower margin in DPS business**

**Other income was down due to lower forex gains and absence of interest on dividend (Rs 42mn)**

**APAT stood at Rs 0.76bn up 5.0% QoQ in line with est. of Rs 0.75bn, led by EBIT growth of 23.7% QoQ offset by lower other income.**

**Tax rate for FY20E would be ~26-27%, evaluating shifting to newer tax structure**

### Quarterly Consolidated Financials Snapshot (Rs mn)

Particulars	3QFY20	3QFY19	YoY (%)	2QFY20	QoQ (%)
IITS Net Revenues (USD mn)	46.8	40.8	14.7	45.3	3.3
<b>Net Revenues</b>	<b>12,369</b>	<b>8,440</b>	<b>46.6</b>	<b>7,031</b>	<b>75.9</b>
Inventory Costs	8,904	5,393	65.1	3,806	133.9
Employee Costs	1,670	1,404	18.9	1,618	3.2
Other Operating Expenses	699	644	8.5	702	(0.4)
<b>EBITDA</b>	<b>1,097</b>	<b>998</b>	<b>9.9</b>	<b>905</b>	<b>21.2</b>
Depreciation	91	30	209.5	92	(0.8)
<b>EBIT</b>	<b>1,005</b>	<b>969</b>	<b>3.8</b>	<b>813</b>	<b>23.7</b>
Interest Cost	43	11	305.7	35	22.2
Other Income	86	-47	NM	208	(58.8)
<b>PBT</b>	<b>1,048</b>	<b>911</b>	<b>15.1</b>	<b>986</b>	<b>6.3</b>
Tax	290	271	6.8	264	9.8
Minority Interest	0	0	NM	0	NM
<b>RPAT</b>	<b>759</b>	<b>639</b>	<b>18.7</b>	<b>722</b>	<b>5.0</b>
E/o (adj for tax)	0	0	NM	0	NM
<b>APAT</b>	<b>759</b>	<b>639</b>	<b>18.7</b>	<b>722</b>	<b>5.0</b>

Source: Company, HDFC sec Inst Research

### Margin Analysis (%)

Particulars	3QFY20	3QFY19	YoY (bps)	2QFY20	QoQ (bps)
Inventory Cost % Net Revenue	72.0	63.9	808	54.1	1,785
Employee Cost % Net Revenue	13.5	16.6	(314)	23.0	(951)
SG&A and Other Expenses % Net Revenues	5.6	7.6	(198)	10.0	(433)
<b>EBITDA Margin (%)</b>	<b>8.9</b>	<b>11.8</b>	<b>(296)</b>	<b>12.9</b>	<b>(401)</b>
<b>EBIT Margin (%)</b>	<b>8.1</b>	<b>11.5</b>	<b>(335)</b>	<b>11.6</b>	<b>(344)</b>
Tax Rate (%)	27.6	29.8	(215)	26.7	89
<b>APAT Margin (%)</b>	<b>6.1</b>	<b>7.6</b>	<b>(144)</b>	<b>10.3</b>	<b>(414)</b>

Source: Company, HDFC sec Inst Research

**DPS business is lumpy in nature due to large deal in a particular quarter. The best way to measure its performance is on absolute EBITDA basis, which was up 38.5% YoY. In 9MFY20 DPS EBITDA was up 33.4% YoY**

**IITS EBITDA margin was up 321bps QoQ at 25.2% higher than est. of 22.5%**

**DPS EBITDA margin contracted 268bps QoQ to 3.0% due to large deal**

**OPD/Travel was down in the quarter but has grown at an eight quarter CQGR of 1.4/1.4% respectively**

**Travel was impacted this quarter due to one large travel client in Europe**

**Retail growth is strong despite cut in number of customers (91 vs. 105 QoQ)**

**Others registered strong growth due to expansion of Microsoft D365 related services**

### Segmental Revenue & EBITDA Mix

Particulars (Rs mn)	3QFY20	3QFY19	YoY (%)	2QFY20	QoQ (%)	9MFY20	9MFY19	YoY (%)
IITS Net Revenues	3,298	2,840	16.1	3,126	5.5	9,469	8,164	16.0
DPS Revenue	9,120	5,632	61.9	3,991	128.5	18,852	13,262	42.2
Inter segment	(49)	(32)	NM	(86)	NM	(175)	(173)	NM
<b>Total Revenue#</b>	<b>12,369</b>	<b>8,440</b>	<b>46.6</b>	<b>7,031</b>	<b>75.9</b>	<b>28,146</b>	<b>21,254</b>	<b>32.4</b>

EBITDA (Rs mn)	3QFY20	3QFY19	YoY (%)	2QFY20	QoQ (%)	9MFY20	9MFY19	YoY (%)
IITS *	830	807	2.8	687	20.9	2,193	1,945	12.7
DPS	270	195	38.5	225	20.0	719	539	33.4
Inter segment	(3)	(4)		(7)		(14)	(13)	
<b>Total EBITDA</b>	<b>1,097</b>	<b>998</b>	<b>9.9</b>	<b>905</b>	<b>21.2</b>	<b>2,898</b>	<b>2,472</b>	<b>17.2</b>

EBITDA Margin (%)	3QFY20	3QFY19	YoY bps	2QFY20	QoQ bps	9MFY20	9MFY19	YoY (bps)
IITS*	25.2	28.4	(326)	22.0	321	23.2	23.8	(67)
DPS	3.0	3.5	(50)	5.6	(268)	3.8	4.1	(25)
<b>Total EBITDA Margin (%)</b>	<b>8.9</b>	<b>11.8</b>	<b>(296)</b>	<b>12.9</b>	<b>(401)</b>	<b>10.3</b>	<b>11.6</b>	<b>(133)</b>

Source: Company, HDFC sec Inst Research, \*IITS EBITDA excludes other income and income tax refunds

### IITS Vertical Revenue Mix

(% Contribution)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
OPD	28.0%	28.0%	27.0%	26.0%	27.0%	28.0%	25.0%
TTL	27.0%	29.0%	28.0%	28.0%	26.0%	27.0%	25.0%
CPG & Retail	25.0%	26.0%	26.0%	27.0%	28.0%	26.0%	28.0%
Others	20.0%	17.0%	19.0%	19.0%	19.0%	19.0%	22.0%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Source: Company, HDFC Sec Inst Research

### IITS Vertical-wise Revenue Growth

(Growth % QoQ; USD)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
OPD	1.1%	3.4%	0.6%	2.7%	5.8%	6.0%	-7.8%
TTL	1.1%	11.1%	0.7%	6.6%	-5.4%	6.2%	-4.3%
CPG & Retail	1.1%	7.6%	4.3%	10.7%	5.6%	-5.0%	11.3%
Others	1.1%	-12.1%	16.6%	6.6%	1.8%	2.3%	19.6%
<b>Total</b>	<b>1.1%</b>	<b>3.4%</b>	<b>4.3%</b>	<b>6.6%</b>	<b>1.8%</b>	<b>2.3%</b>	<b>3.3%</b>

Source: Company, HDFC Sec Inst Research

**Testing recovered after two consecutive quarters of decline**

**Growth was powered by AX which is the Microsoft Dynamics 365 offering**

**Microsoft Dynamics 365 has growth at an 8-quarter CQGR of 7.3% (company average is 2.8%). Ex-AX 8-quarter revenue CQGR is 1.5%**

**Apart from AX, ADM/BI have been fueling growth, 8 Qtr CQGR of 4.4/2.8%**

**Out of the total 167 customers 91/19/13 are in Retail/OPD/Travel respectively**

### IITS Service Line Break-up

(% Contribution)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
ADM	26.0%	25.0%	25.0%	24.0%	24.0%	27.0%	26.0%
Testing	17.0%	17.0%	17.0%	17.0%	16.0%	15.0%	15.0%
IMS	17.0%	16.0%	16.0%	16.0%	14.0%	12.0%	12.0%
AX	18.0%	20.0%	20.0%	22.0%	26.0%	26.0%	28.0%
BI	8.0%	8.0%	8.0%	8.0%	9.0%	9.0%	8.0%
E-commerce	6.0%	7.0%	6.0%	6.0%	5.0%	5.0%	5.0%
ERP	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Rezopia/Mobility/Cloud	4.0%	3.0%	4.0%	3.0%	2.0%	2.0%	2.0%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Source: Company, HDFC Sec Inst Research

### IITS Service Line Growth

(Growth %, QoQ)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
ADM	9.5%	-0.5%	4.3%	2.4%	1.8%	15.0%	-0.5%
Testing	-4.5%	3.4%	4.3%	6.6%	-4.2%	-4.1%	3.3%
IMS	-9.6%	-2.6%	4.3%	6.6%	-10.9%	-12.4%	3.3%
AX	-4.2%	14.9%	4.3%	17.3%	20.4%	2.3%	11.3%
BI	15.5%	3.4%	4.3%	6.6%	14.6%	2.3%	-8.2%
E-commerce	21.3%	20.7%	-10.6%	6.6%	-15.1%	2.3%	3.3%
ERP	-10.2%	3.4%	4.3%	6.6%	1.8%	2.3%	3.3%
Rezopia	15.5%	-22.4%	39.1%	-20.0%	-32.1%	2.3%	3.3%
<b>Total</b>	<b>1.1%</b>	<b>3.4%</b>	<b>4.3%</b>	<b>6.6%</b>	<b>1.8%</b>	<b>2.3%</b>	<b>3.3%</b>

Source: Company, HDFC Sec Inst Research

*Growth in offshore revenue has led to margin increase in IITS*

*Top 10/20 clients grew 4.9/6.1% QoQ, Non Top 10 client growth have been impressive, 8Qtr CQGR of 4.9%*

*Dependence on Top-5 clients is coming down but still high compared to peers*

### IITS Onsite-Offshore Split

IT services revenue break-up (%)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Offshore	56.0%	58.0%	58.0%	57.0%	56.0%	56.0%	58.0%
Onsite	44.0%	42.0%	42.0%	43.0%	44.0%	44.0%	42.0%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Source: Company, HDFC Sec Inst Research

### IITS Onsite-Offshore Growth

IT services revenue growth (% QoQ)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Offshore	-4.1%	7.1%	4.3%	4.8%	0.1%	2.3%	7.0%
Onsite	8.5%	-1.3%	4.3%	9.2%	4.2%	2.3%	-1.4%
<b>Total</b>	<b>1.1%</b>	<b>3.4%</b>	<b>4.3%</b>	<b>6.6%</b>	<b>1.8%</b>	<b>2.3%</b>	<b>3.3%</b>

Source: Company, HDFC Sec Inst Research

### IITS Client Concentration

Client concentration (%)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Top 5	61.0%	61.0%	61.0%	61.0%	59.0%	59.0%	57.0%
Top-10	70.0%	69.0%	69.0%	68.0%	66.0%	65.0%	66.0%
Non-top 10	30.0%	31.0%	31.0%	32.0%	34.0%	35.0%	34.0%
Top 20	80.0%	77.0%	78.0%	76.0%	75.0%	73.0%	75.0%
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>	<b>100.0%</b>

Source: Company, HDFC Sec Inst Research

### IITS Client Concentration Growth

Client concentration (% growth)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Top 5	1.1%	3.4%	4.3%	6.6%	-1.5%	2.3%	-0.2%
Top-10	2.5%	2.0%	4.3%	5.1%	-1.2%	0.7%	4.9%
Non-top 10	-2.2%	6.9%	4.3%	10.1%	8.2%	5.3%	0.4%
Top 20	2.3%	-0.4%	5.7%	3.9%	0.5%	-0.5%	6.1%
<b>Total</b>	<b>1.1%</b>	<b>3.4%</b>	<b>4.3%</b>	<b>6.6%</b>	<b>1.8%</b>	<b>2.3%</b>	<b>3.3%</b>

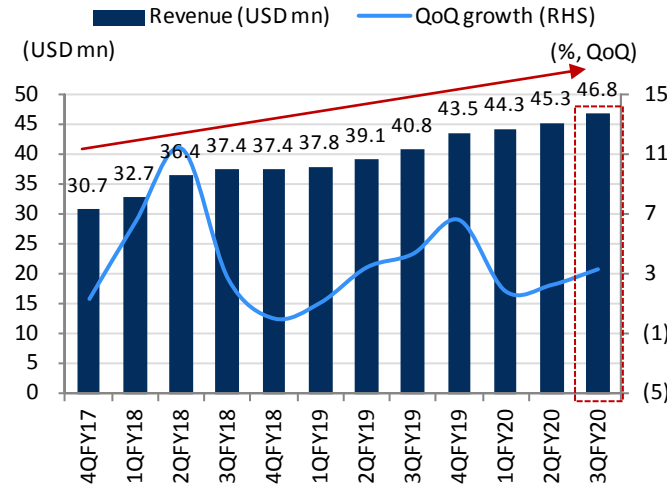
Source: Company, HDFC Sec Inst Research

**IITS revenue/EBITDA has grown at CQGR of 2.8/6.5% over the last eight quarter**

**Avg. revenue per employee in 3Q was USD 46,429, +1.2/+6.6% QoQ/YoY. There has been a steady rise in employee productivity (8-Qtr CQGR of +0.6%)**

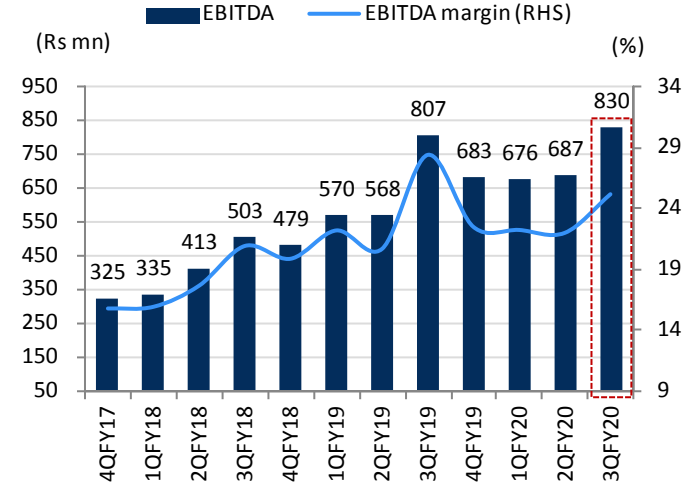
**Growth in IP led revenue is driving growth and margin in the IITS business. IP-led and Digital has grown at 8-qtr CQGR of +9.5/+5.1% respectively**

**IITS Rev Growth Trend**



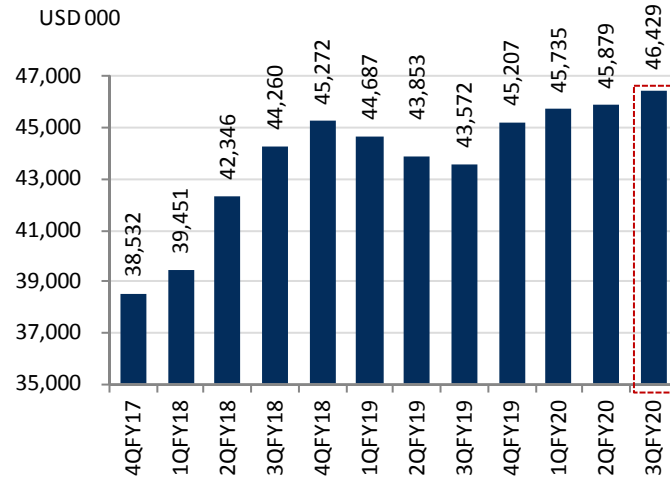
Source: Company, HDFC sec Inst Research

**IITS EBITDA, Margin Trend**



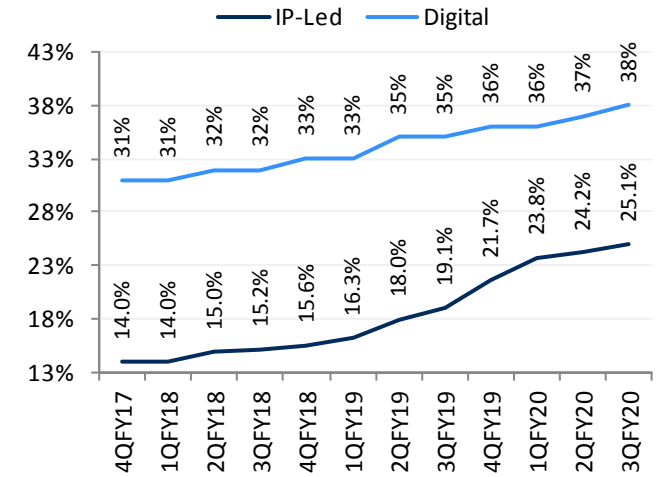
Source: Company, HDFC sec Inst Research

**IITS Employee Productivity**



Source: Company, HDFC sec Inst Research

**IP-Led & Digital Revenue %**

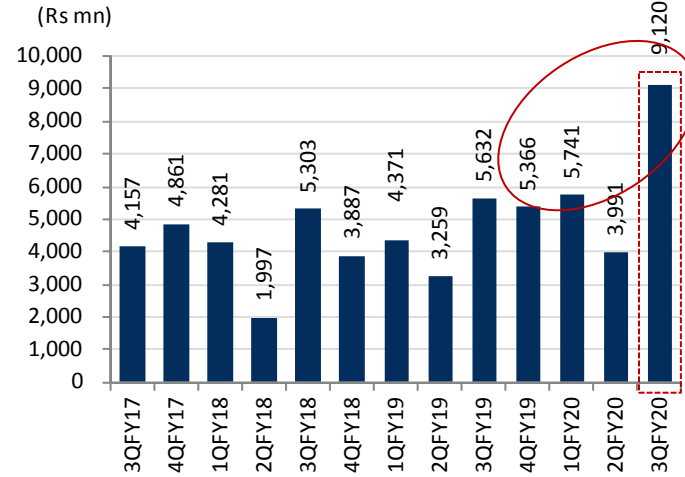


Source: Company, HDFC sec Inst Research

*DPS Revenue/EBITDA has grown at a CQGR of 7.0/7.3% over the last eight quarter*

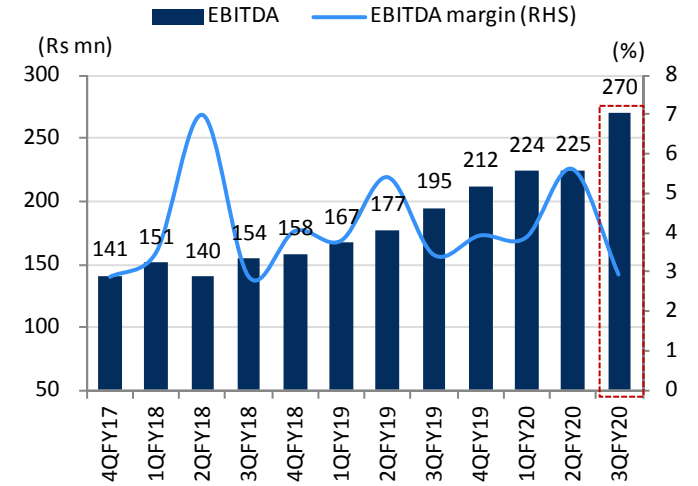
*Receivables has come down in the DPS business and bad debts is very low, less than 0.1% historically*

**DPS Quarterly Revenue Trend**



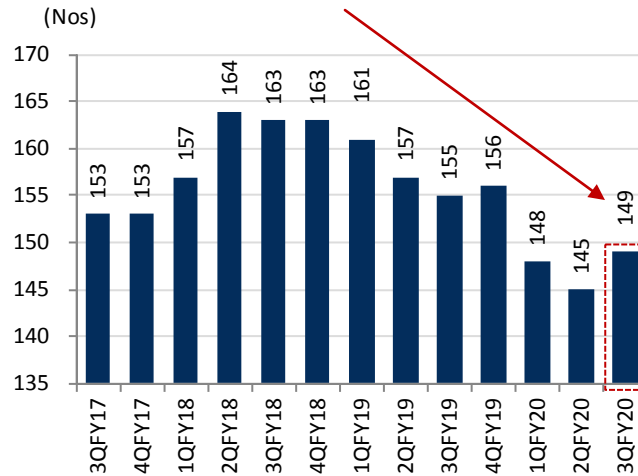
Source: Company, HDFC sec Inst Research

**DPS EBITDA Margin Trend**



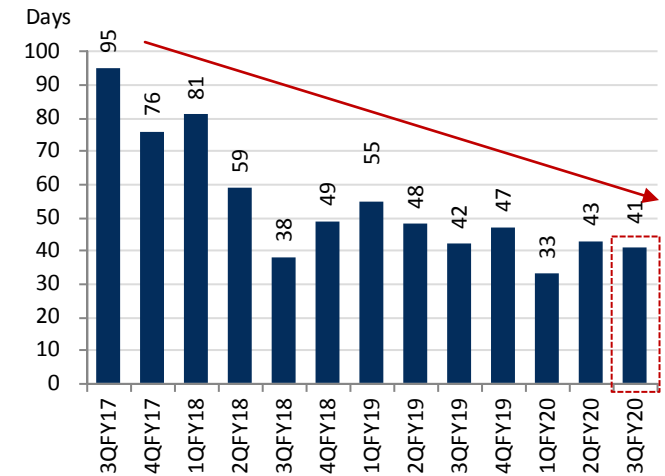
Source: Company, HDFC sec Inst Research

**DPS' Headcount**



Source: Company, HDFC sec Inst Research

**DPS' Debtor Days**



Source: Company, HDFC sec Inst Research

### IITS' Segment Estimates

IITS (Rs million)	FY18	FY19	FY20E	FY21E	FY22E
Revenue (USD million)	143.9	161.2	184.6	206.4	230.1
% Growth	18.6	12.0	14.5	11.8	11.5
Revenue	9,285	11,205	12,891	14,760	16,797
% Growth	13.0	20.7	15.1	14.5	13.8
EBITDA	1,730	2,629	2,980	3,432	3,986
EBITDA Margin (%)	18.6	23.5	23.1	23.3	23.7

Source: Company, HDFC sec Inst Research

### DPS' Segment Estimates

DPS (Rs million)	FY18	FY19	FY20E	FY21E	FY22E
Revenue	15,468	18,628	24,755	25,406	27,874
% Growth	(1.9)	20.4	32.9	2.6	9.7
EBITDA	603	751	985	1,105	1,220
EBITDA Margin (%)	3.9	4.0	4.0	4.3	4.4

Source: Company, HDFC sec Inst Research

### Change In Estimates

Particulars	Earlier estimates	Revised estimates	% change
<b>FY20E</b>			
Revenue (Rs mn)	34,261	37,471	9.4
EBIT (Rs mn)	3,441	3,581	4.0
EBIT margin (%)	10.0	9.6	-49
APAT	2,854	2,931	2.7
<b>FY21E</b>			
Revenue (Rs mn)	37,880	40,166	6.0
EBIT (Rs mn)	3,975	4,136	4.1
EBIT margin (%)	10.5	10.3	-20
APAT	3,165	3,284	3.8
<b>FY22E</b>			
Revenue (Rs mn)	42,103	44,671	6.1
EBIT (Rs mn)	4,536	4,764	5.0
EBIT margin (%)	10.8	10.7	-11
APAT	3,591	3,773	5.1

Source: Company, HDFC sec Inst Research

**We have increased IITS USD revenue estimate by only 0.9/1.8% for FY20/21E while the increase in consolidated revenue is due to DPS**

**Consolidated EBIT margin is cut by 20/11bps for FY21/22E due to lower DPS margin**

**We increase APAT by 3.8/5.1% for FY21/22E due to higher DPS revenue, IITS traction and stable margins**



## Peer Set Comparison

Company	MCap (Rs bn)	CMP (Rs)	TP (Rs)	RECO	EPS (Rs)				P/E (x)				RoE (%)			
					FY19	FY20E	FY21E	FY22E	FY19	FY20E	FY21E	FY22E	FY19	FY20E	FY21E	FY22E
TCS	8,140	2,169	2,025	NEU	83.9	86.5	93.6	104.7	25.9	25.1	23.2	20.7	36.1	35.7	37.2	39.7
Infosys	3,304	778	850	BUY	37.1	38.2	43.5	48.1	20.9	20.4	17.9	16.2	24.3	25.4	28.2	28.3
Wipro	1,399	245	235	NEU	15.8	17.4	18.3	20.0	15.5	14.1	13.4	12.3	17.3	17.7	17.3	16.2
HCL Tech	1,639	604	665	BUY	37.3	39.0	41.7	48.2	16.2	15.5	14.5	12.5	26.0	23.2	21.0	20.7
TechM	743	791	870	BUY	48.9	47.5	52.5	59.9	16.2	16.7	15.1	13.2	22.0	20.2	20.5	20.5
<b>Tier-1 IT Median</b>									<b>16.2</b>	<b>16.7</b>	<b>15.1</b>	<b>13.2</b>	<b>24.3</b>	<b>23.2</b>	<b>21.0</b>	<b>20.7</b>
LTI	339	1,947	2,090	BUY	87.1	85.6	101.6	120.7	22.3	22.7	19.2	16.1	34.6	28.0	28.4	28.7
Mphasis	166	891	1,165	BUY	57.6	58.3	65.5	75.0	15.5	15.3	13.6	11.9	20.0	19.7	19.9	20.2
L&T Tech	181	1,739	1,790	BUY	67.8	76.0	86.6	103.7	25.7	22.9	20.1	16.8	32.0	29.4	28.4	28.5
Mindtree	146	885	830	NEU	44.1	38.5	48.0	63.3	20.1	23.0	18.5	14.0	24.9	18.3	22.7	26.0
Hexaware *	104	347	450	BUY	19.6	21.6	24.5	28.3	17.8	16.1	14.2	12.3	26.5	24.7	24.1	24.0
Cyient	55	492	490	NEU	43.6	36.3	40.9	46.0	11.3	13.6	12.0	10.7	19.5	15.3	15.9	16.2
Zensar	40	177	177	NEU	14.2	10.8	12.9	17.1	12.5	16.4	13.7	10.3	17.6	11.9	12.9	15.3
Persistent	55	722	725	BUY	47.8	45.2	48.5	57.7	15.1	16.0	14.9	12.5	15.7	14.3	14.8	15.8
Tata Elxsi	59	943	875	NR	46.6	39.4	49.5	57.0	20.2	23.9	19.0	16.5	34.5	24.2	26.1	25.4
<b>Sonata</b>	<b>36</b>	<b>347</b>	<b>422</b>	<b>BUY</b>	<b>23.7</b>	<b>28.5</b>	<b>31.6</b>	<b>36.3</b>	<b>14.6</b>	<b>12.2</b>	<b>11.0</b>	<b>9.6</b>	<b>35.1</b>	<b>36.1</b>	<b>35.3</b>	<b>35.7</b>
Intellect	22	170	255	BUY	7.7	2.6	7.3	11.2	22.2	66.5	23.3	15.1	11.1	3.3	8.7	12.1
eClerx	25	681	560	NR	61.7	52.0	53.7	57.0	11.0	13.1	12.7	11.9	17.6	14.0	14.7	14.6
Majesco	12	413	655	BUY	18.3	19.9	30.0	36.7	22.5	20.8	13.8	11.2	8.4	7.9	11.0	12.2
HGS	14	655	745	NR	84.6	100.3	110.9	129.5	7.7	6.5	5.9	5.1	8.5	13.1	13.3	13.7
Mastek	11	443	515	BUY	40.4	40.9	45.1	52.9	11.0	10.8	9.8	8.4	16.1	13.7	13.6	14.4
<b>Tier-2 IT AVG</b>									<b>15.5</b>	<b>16.1</b>	<b>13.8</b>	<b>11.9</b>	<b>19.5</b>	<b>15.3</b>	<b>15.9</b>	<b>16.2</b>

Source: HDFC sec Inst Research

## Consolidated Income Statement

YE March (Rs bn)	FY18	FY19E	FY20E	FY21E	FY22E
<b>IITS USD Revenue (mn)</b>	<b>143.9</b>	<b>161.2</b>	<b>184.6</b>	<b>206.4</b>	<b>230.1</b>
<b>Growth (%)</b>	<b>18.6</b>	<b>12.0</b>	<b>14.5</b>	<b>11.8</b>	<b>11.5</b>
<b>Net Revenues</b>	<b>24.54</b>	<b>29.61</b>	<b>37.47</b>	<b>40.17</b>	<b>44.67</b>
<b>Growth (%)</b>	<b>3.5</b>	<b>20.7</b>	<b>26.6</b>	<b>7.2</b>	<b>11.2</b>
Total Operating Expenses	22.23	26.25	33.52	35.63	39.46
<b>EBITDA</b>	<b>2.31</b>	<b>3.36</b>	<b>3.95</b>	<b>4.54</b>	<b>5.21</b>
<b>EBITDA (%)</b>	<b>9.4</b>	<b>11.3</b>	<b>10.5</b>	<b>11.3</b>	<b>11.7</b>
<b>EBITDA Growth (%)</b>	<b>20.6</b>	<b>45.3</b>	<b>17.7</b>	<b>14.8</b>	<b>14.7</b>
Depreciation	0.12	0.13	0.37	0.40	0.44
<b>EBIT</b>	<b>2.19</b>	<b>3.23</b>	<b>3.58</b>	<b>4.14</b>	<b>4.76</b>
<b>EBIT (%)</b>	<b>8.9</b>	<b>10.9</b>	<b>9.6</b>	<b>10.3</b>	<b>10.7</b>
<b>EBIT Growth (%)</b>	<b>21.0</b>	<b>47.7</b>	<b>10.9</b>	<b>15.5</b>	<b>15.2</b>
Other Income	0.47	0.30	0.58	0.45	0.48
Interest	0.05	0.03	0.15	0.15	0.15
<b>PBT</b>	<b>2.60</b>	<b>3.49</b>	<b>4.01</b>	<b>4.43</b>	<b>5.09</b>
Tax (incl deferred)	0.68	1.01	1.08	1.15	1.32
Minority Int. and associate profit	0.00	0.00	0.00	0.00	0.00
<b>RPAT</b>	<b>1.93</b>	<b>2.49</b>	<b>2.93</b>	<b>3.28</b>	<b>3.77</b>
EO (Loss) / Profit (Net Of Tax)	0.01	0.03	0.00	0.00	0.00
<b>APAT</b>	<b>1.91</b>	<b>2.47</b>	<b>2.93</b>	<b>3.28</b>	<b>3.77</b>
<b>APAT Growth (%)</b>	<b>28.8</b>	<b>28.8</b>	<b>18.9</b>	<b>12.0</b>	<b>14.9</b>
<b>EPS</b>	<b>18.4</b>	<b>23.7</b>	<b>28.2</b>	<b>31.6</b>	<b>36.3</b>
<b>EPS Growth (%)</b>	<b>28.8</b>	<b>28.6</b>	<b>18.9</b>	<b>12.0</b>	<b>14.9</b>

Source: Company, HDFC sec Inst Research

## Consolidated Balance Sheet

YE March (Rs bn)	FY18	FY19	FY20E	FY21E	FY22E
<b>SOURCES OF FUNDS</b>					
Share Capital - Equity	0.10	0.10	0.10	0.10	0.10
Reserves	6.43	7.58	8.61	9.77	11.11
<b>Total Shareholders' Funds</b>	<b>6.53</b>	<b>7.68</b>	<b>8.72</b>	<b>9.88</b>	<b>11.21</b>
Minority Interest	(0.00)	0.00	0.00	0.00	0.00
<b>Total Debt</b>	<b>0.41</b>	<b>0.52</b>	<b>0.52</b>	<b>0.52</b>	<b>0.52</b>
Net Deferred Taxes	(0.12)	(0.12)	(0.12)	(0.12)	(0.12)
Long-term Provisions & Others	0.10	0.11	0.11	0.11	0.11
<b>TOTAL SOURCES OF FUNDS</b>	<b>6.93</b>	<b>8.19</b>	<b>9.23</b>	<b>10.39</b>	<b>11.72</b>
<b>APPLICATION OF FUNDS</b>					
Net Block	0.33	0.54	0.36	0.16	(0.06)
CWIP	0.00	0.01	0.01	0.01	0.01
Goodwill & Other Intangible Assets	0.81	1.45	1.45	1.45	1.45
Investments	0.00	0.00	0.00	0.00	0.00
LT Loans & Advances, Others	0.85	0.63	0.72	0.81	0.93
<b>Total Non Current Assets</b>	<b>1.99</b>	<b>2.63</b>	<b>2.53</b>	<b>2.43</b>	<b>2.32</b>
Inventories	0.00	0.00	0.00	0.00	0.00
Debtors	3.96	8.11	8.73	9.35	10.40
Cash & Equivalents	5.46	3.46	5.02	5.97	7.06
Other Current Assets	0.80	0.96	1.11	1.27	1.46
<b>Total Current Assets</b>	<b>10.22</b>	<b>12.53</b>	<b>14.85</b>	<b>16.60</b>	<b>18.92</b>
Creditors	4.32	5.87	6.89	7.32	8.11
Other Current Liabilities & Provns	0.96	1.09	1.27	1.32	1.42
<b>Total Current Liabilities</b>	<b>5.29</b>	<b>6.97</b>	<b>8.16</b>	<b>8.64</b>	<b>9.53</b>
<b>Net Current Assets</b>	<b>4.94</b>	<b>5.56</b>	<b>6.69</b>	<b>7.96</b>	<b>9.40</b>
<b>TOTAL APPLICATION OF FUNDS</b>	<b>6.93</b>	<b>8.19</b>	<b>9.23</b>	<b>10.39</b>	<b>11.72</b>

Source: Company, HDFC sec Inst Research

## Consolidated Cash Flow

YE March (Rs bn)	FY18	FY19	FY20E	FY21E	FY22E
Reported PBT	2.60	3.49	4.01	4.43	5.09
Non-operating & EO items	(0.15)	(0.50)	(0.58)	(0.45)	(0.48)
Interest expenses	0.04	0.03	0.15	0.15	0.15
Depreciation	0.12	0.13	0.37	0.40	0.44
Working Capital Change	0.90	(2.35)	0.34	(0.40)	(0.47)
Tax paid	(0.55)	(0.87)	(1.08)	(1.15)	(1.32)
<b>OPERATING CASH FLOW ( a )</b>	<b>2.98</b>	<b>(0.06)</b>	<b>3.21</b>	<b>2.98</b>	<b>3.41</b>
Capex	(0.06)	(0.46)	(0.19)	(0.20)	(0.22)
Free cash flow (FCF)	2.91	(0.52)	3.02	2.78	3.19
Investments	0.00	0.00	0.00	0.00	0.00
Non-operating income	0.10	0.05	0.58	0.45	0.48
<b>INVESTING CASH FLOW ( b )</b>	<b>0.03</b>	<b>(0.41)</b>	<b>0.39</b>	<b>0.25</b>	<b>0.26</b>
Debt Issuance	(0.21)	(0.20)	0.00	0.00	0.00
Interest expenses	(0.04)	(0.03)	(0.15)	(0.15)	(0.15)
FCFE	2.66	(0.75)	2.88	2.63	3.04
Share capital Issuance	0.00	0.00	0.00	0.00	0.00
Dividend	(1.15)	(1.43)	(1.89)	(2.12)	(2.44)
<b>FINANCING CASH FLOW ( c )</b>	<b>(1.40)</b>	<b>(1.66)</b>	<b>(2.04)</b>	<b>(2.27)</b>	<b>(2.59)</b>
<b>NET CASH FLOW (a+b+c)</b>	<b>1.61</b>	<b>(2.14)</b>	<b>1.56</b>	<b>0.96</b>	<b>1.08</b>
Non-operating and EO items	0.04	0.14	0.00	0.00	0.00
Closing Cash & Equivalents	5.46	3.46	5.02	5.97	7.06

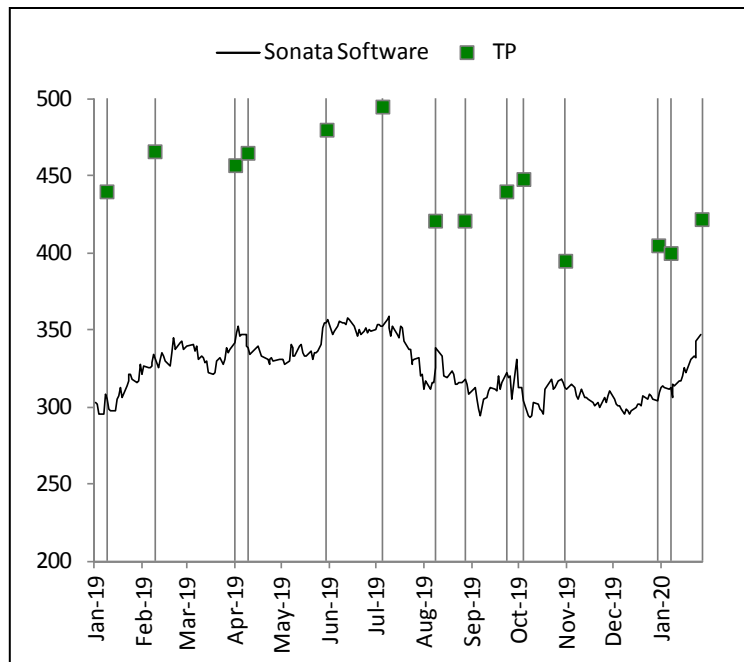
Source: Company, HDFC sec Inst Research

## Key Ratios

	FY18	FY19	FY20E	FY21E	FY22E
<b>PROFITABILITY (%)</b>					
EBITDA Margin	9.4	11.3	10.5	11.3	11.7
APAT Margin	7.8	8.4	7.8	8.2	8.4
RoE	31.0	35.1	35.7	35.3	35.8
RolC or Core RoCE	109.6	48.4	62.1	69.3	75.6
RoCE	24.3	30.3	30.0	31.2	67.9
<b>EFFICIENCY</b>					
Tax Rate (%)	26.3	29.0	27.0	26.0	26.0
Fixed Asset Turnover (x)	17.0	16.6	19.0	18.5	18.7
Inventory (days)	0	0	0	0	0
Debtors (days)	59	100	85	85	85
Other Current Assets (days)	12	12	11	12	12
Payables (days)	71	82	75	75	75
Other Current Liab & Provns (days)	14	13	12	12	12
Cash Conversion Cycle (days)	-14	17	8	10	10
Net Debt/EBITDA (x)	(2.2)	(0.9)	(1.1)	(1.2)	(1.3)
Net Debt/Equity (x)	(0.8)	(0.4)	(0.5)	(0.6)	(0.6)
Interest Coverage (x)	45.5	95.2	24.4	27.7	31.4
<b>PER SHARE DATA</b>					
EPS (Rs/sh)	18.4	23.7	28.2	31.6	36.3
CEPS (Rs/sh)	19.7	25.2	31.8	35.5	40.6
DPS (Rs/sh)	10.5	12.8	15.5	17.4	20.0
BV (Rs/sh)	63.0	74.0	84.0	95.2	108.0
<b>VALUATION</b>					
P/E	18.7	14.5	12.3	11.0	9.6
P/BV	5.5	4.7	4.1	3.7	3.2
EV/EBITDA	13.8	10.1	8.2	6.9	5.8
OCF/EV (%)	9.3	(0.2)	9.9	9.5	11.2
FCF/EV (%)	9.1	(1.5)	9.3	8.8	10.5
FCFE/mkt cap (%)	7.4	(2.1)	8.0	7.3	8.4
Dividend Yield (%)	3.0	3.7	4.5	5.0	5.7

Source: Company, HDFC sec Inst Research

**RECOMMENDATION HISTORY**



Date	CMP	Reco	Target
8-Jan-19	308	BUY	440
9-Feb-19	334	BUY	466
1-Apr-19	338	BUY	457
9-Apr-19	347	BUY	465
31-May-19	357	BUY	480
5-Jul-19	353	BUY	495
9-Aug-19	325	BUY	421
27-Aug-19	316	BUY	421
22-Sep-19	316	BUY	440
4-Oct-19	313	BUY	448
31-Oct-19	313	BUY	395
30-Dec-19	305	BUY	405
7-Jan-20	311	BUY	400
27-Jan-20	347	BUY	422

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- 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

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