

## Growth levers on track

We maintain BUY on Sonata based on inline revenue but slight miss on margins in 2QFY20. IP-led strategy is driving IITS growth (+9.1% 8qtr CQGR) and is aiding margin expansion (+133 bps YoY). We downgrade P/E multiple to 12x from 14x to factor in rising receivables in the DPS business. Our TP of Rs 395 is based on 12x Sep-21E EPS.

### HIGHLIGHTS OF THE QUARTER

- International IT services (IITS) revenue increased 2.3% QoQ (+3.0% CC) to USD 45.3mn vs. est. of USD 45.2mn. Growth was led by IP-led (24.2% of rev, +5.0% QoQ) and will remain the key growth driver.
- Sonata has invested in the Microsoft relationship which has yielded results, Dynamics 365 has grown at 8qtr CQGR of 6.9%. The next phase of growth will come from entry into other growth areas (Data & Cloud) within Microsoft account.
- IITS margin stood at 22.0% down 24bps QoQ slightly below est. of 22.5%. Margin was impacted due to muted performance of acquired entity (Sopris) offset by higher utilisation (+180bps QoQ). We expect gradual expansion in IITS margin led by IP-led, desired range is 22-24%, higher than peers.
- Total Revenue was down 19.6% QoQ to Rs 7.03bn due to 30.5% QoQ decline in Domestic Product & Services

### Financial Summary

YE March (Rs bn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	FY18	FY19	FY20E	FY21E	FY22E
Net Revenues	7.03	5.93	18.5	8.75	(19.6)	24.54	29.61	34.50	38.24	42.50
EBIT	0.81	0.71	14.3	0.81	0.8	2.19	3.23	3.46	4.00	4.57
APAT	0.72	0.62	16.2	0.67	7.7	1.93	2.49	2.80	3.19	3.61
Diluted EPS (Rs)	7.0	6.0	16.2	6.5	7.7	18.6	24.0	27.0	30.7	34.8
P/E (x)						16.9	13.0	11.6	10.2	9.0
EV / EBITDA (x)						12.3	9.1	7.5	6.4	5.4
RoE (%)						31.0	35.1	34.3	34.5	34.6

Source: Company, HDFC sec Inst Research # Consolidated

(DPS) revenue. DPS performance is measured on absolute EBITDA (Rs 0.23bn, +0.4/27.1% QoQ/YoY).

- IP-led and Digital (37% of rev) grew by 55.8/22.5% YoY. ~65% of the incremental growth is coming from IP-led revenue (higher margin).
- Receivable was down to Rs 7.12bn in 1HFY20 vs Rs 8.11bn in FY19, but still has increased substantially in the last two years. Domestic slowdown is impacting DPS collections, which is a concern.

### STANCE: Sustainable growth at reasonable valuations

Sonata's platformation strategy to provide IT services around IPs like Rezopia, Halosys, Brick & Click and Retina, is yielding results. Growth in IP-led revenues is improving employee productivity and aiding margin expansion. Sonata's strategy to venture into different areas within the top-account will aid growth and reduce dependency on a single platform. We like Sonata's IP-focussed business model, high RoE (~35%) and dividend yield of ~4%. The stock trades at a P/E of 10.2x FY21E, which is inexpensive but will command higher multiple only with better receivables management. We expect IITS' USD revenue to grow 13.8/11.1% with margin of 22.6/23.0% in FY20/21E. Risks include deceleration in top-account, delay in collections and slowdown in US/Europe.

INDUSTRY	IT
<b>CMP (as on 31 Oct 2019)</b>	<b>Rs 313</b>
<b>Target Price</b>	<b>Rs 395</b>
Nifty	11,877
Sensex	40,129
KEY STOCK DATA	
Bloomberg	SSOF IN
No. of Shares (mn)	105
MCap (Rs bn) / (\$ mn)	33/464
6m avg traded value (Rs mn)	32
STOCK PERFORMANCE (%)	
<b>52 Week high / low</b>	<b>Rs 364/283</b>
	3M 6M 12M
Absolute (%)	(2.5) (5.5) 1.4
Relative (%)	(9.6) (8.3) (15.1)
SHAREHOLDING PATTERN (%)	
	Jun-19 Sep-19
Promoters	28.17 28.17
FIs & Local MFs	9.88 11.61
FPIs	13.96 13.23
Public & Others	47.99 46.99
Pledged Shares	0.00 0.00

Source : BSE

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**IITS' revenue grew 2.3% QoQ and was impacted by de growth in Sopris. Acquired entities will take two quarters to settle down and grow**

**IITS' EBITDA% was impacted due to Sopris and Retail slowdown, will remain in the range of 22-24%**

**Consolidated EBIT margin was up 234bps QoQ to 11.6% but was below our est. of 12.0% due to lower margin in IITS business**

**Other income was boosted due to Rs 42mn interest on dividend**

**APAT stood at Rs 0.72bn up 7.7% QoQ (vs. our exp of Rs 0.69bn) due to higher other income and lower tax rate**

**Tax rate for FY20E would be ~26-27%**

### Quarterly Consolidated Financials Snapshot (Rs mn)

Particulars	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)
<b>IITS Net Revenues (USD mn)</b>	<b>45.3</b>	<b>39.1</b>	<b>15.9</b>	<b>44.3</b>	<b>2.3</b>
<b>Net Revenues</b>	<b>7,031</b>	<b>5,931</b>	<b>18.5</b>	<b>8,746</b>	<b>(19.6)</b>
Inventory Costs	3,806	3,063	24.3	5,558	(31.5)
Employee Costs	1,618	1,464	10.5	1,615	0.2
Other Operating Expenses	702	664	5.6	677	3.6
<b>EBITDA</b>	<b>905</b>	<b>740</b>	<b>22.3</b>	<b>896</b>	<b>1.0</b>
Depreciation	92	29	218.3	90	2.8
<b>EBIT</b>	<b>813</b>	<b>711</b>	<b>14.3</b>	<b>807</b>	<b>0.8</b>
Interest Cost	35	10	270.5	38	(7.9)
Other Income	208	167	24.9	168	24.2
<b>PBT</b>	<b>986</b>	<b>869</b>	<b>13.6</b>	<b>936</b>	<b>5.3</b>
Tax	264	247	6.9	266	(0.7)
Minority Interest	0	0	NM	0	NM
<b>RPAT</b>	<b>722</b>	<b>622</b>	<b>16.2</b>	<b>670</b>	<b>7.7</b>
E/o (adj for tax)	0	0	NM	0	NM
<b>APAT</b>	<b>722</b>	<b>622</b>	<b>16.2</b>	<b>670</b>	<b>7.7</b>

Source: Company, HDFC sec Inst Research

### Margin Analysis (%)

Particulars	2QFY20	2QFY19	YoY (bps)	1QFY20	QoQ (bps)
Inventory Cost % Net Revenue	54.1	51.6	250	63.6	(941)
Employee Cost % Net Revenue	23.0	24.7	(167)	18.5	455
SG&A and Other Expenses % Net Revenues	10.0	11.2	(122)	7.7	223
<b>EBITDA Margin (%)</b>	<b>12.9</b>	<b>12.5</b>	<b>39</b>	<b>10.2</b>	<b>263</b>
<b>EBIT Margin (%)</b>	<b>11.6</b>	<b>12.0</b>	<b>(43)</b>	<b>9.2</b>	<b>234</b>
Tax Rate (%)	26.7	28.4	(166)	28.4	(163)
<b>APAT Margin (%)</b>	<b>10.3</b>	<b>10.5</b>	<b>(21)</b>	<b>7.7</b>	<b>261</b>

Source: Company, HDFC sec Inst Research

*DPS business is lumpy in nature due to closure of large deal in a particular quarter. The best way to measure its performance is on absolute EBITDA basis, which was up 27.1% YoY. In 1HFY20 DPS EBITDA was up 30.5% YoY*

*IITS EBITDA% was stable at 22% in the quarter but there was a miss of 4.2% in absolute terms vs. our estimates*

*OPD/Travel has grown at an eight quarter CQGR of 2.3/2.8% respectively*

*Retail was impacted this quarter due to completion of certain projects*

*Out of the total 173 customers 105/19/12 are in Retail/OPD/Travel respectively*

### Segmental Revenue & EBITDA Mix

Particulars (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	6MFY20	6MFY19	YoY (%)
IITS Net Revenues	3,126	2,753	13.5	3,045	2.7	6,171	5,324	15.9
DPS Revenue	3,991	3,259	22.5	5,741	(30.5)	9,732	7,630	27.5
Inter segment	(86)	(81)	NM	(40)	NM	(126)	(140)	NM
<b>Total Revenue#</b>	<b>7,031</b>	<b>5,931</b>	<b>18.5</b>	<b>8,746</b>	<b>(19.6)</b>	<b>15,777</b>	<b>12,814</b>	<b>23.1</b>

EBITDA (Rs mn)	2QFY20	2QFY19	YoY (%)	1QFY20	QoQ (%)	6MFY20	6MFY19	YoY (%)
IITS *	687	568	20.9	676	1.5	1,363	1,138	19.8
DPS	225	177	27.1	224	0.4	449	344	30.5
Inter segment	(7)	(5)		(4)		(11)	(9)	
<b>Total EBITDA</b>	<b>905</b>	<b>740</b>	<b>22.3</b>	<b>896</b>	<b>1.0</b>	<b>1,801</b>	<b>1,474</b>	<b>22.2</b>

EBITDA Margin (%)	2QFY20	2QFY19	YoY bps	1QFY20	QoQ bps	6MFY20	6MFY19	YoY (bps)
IITS*	22.0	20.6	133	22.2	(24)	22.1	21.4	71
DPS	5.6	5.4	21	3.9	174	4.6	4.5	11
<b>Total EBITDA Margin (%)</b>	<b>12.9</b>	<b>12.5</b>	<b>39</b>	<b>10.2</b>	<b>263</b>	<b>11.4</b>	<b>11.5</b>	<b>(8)</b>

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

### IITS Vertical Revenue Mix

(% Contribution)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
OPD	28.0%	28.0%	28.0%	27.0%	26.0%	27.0%	28.0%
TTL	27.0%	27.0%	29.0%	28.0%	28.0%	26.0%	27.0%
CPG & Retail	25.0%	25.0%	26.0%	26.0%	27.0%	28.0%	26.0%
Others	20.0%	20.0%	17.0%	19.0%	19.0%	19.0%	19.0%
<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)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
OPD	0.0%	1.1%	3.4%	0.6%	2.7%	5.8%	6.0%
TTL	-3.6%	1.1%	11.1%	0.7%	6.6%	-5.4%	6.2%
CPG & Retail	-7.4%	1.1%	7.6%	4.3%	10.7%	5.6%	-5.0%
Others	17.6%	1.1%	-12.1%	16.6%	6.6%	1.8%	2.3%
<b>Total</b>	<b>0.0%</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>

Source: Company, HDFC Sec Inst Research

**Testing was down for two consecutive quarters**

**IMS is impacted due to shift to cloud, down at a 8 qtr CQGR of 1.6%**

**Growth was powered by AX which is the Microsoft 365 offering. ADM was up 15% QoQ due to work related to platform engineering**

**Microsoft Dynamics 365 has growth at an 8-quarter CQGR of 6.9% (company average is 2.8%). Ex-AX 8-quarter revenue CQGR is 1.6%**

**Apart from AX, ADM/BI have been fueling growth, 8 Qtr CQGR of 4.8/6.0%**

### IITS Service Line Break-up

(% Contribution)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
ADM	24.0%	26.0%	25.0%	25.0%	24.0%	24.0%	27.0%
Testing	18.0%	17.0%	17.0%	17.0%	17.0%	16.0%	15.0%
IMS	19.0%	17.0%	16.0%	16.0%	16.0%	14.0%	12.0%
AX	19.0%	18.0%	20.0%	20.0%	22.0%	26.0%	26.0%
BI	7.0%	8.0%	8.0%	8.0%	8.0%	9.0%	9.0%
E-commerce	5.0%	6.0%	7.0%	6.0%	6.0%	5.0%	5.0%
ERP	4.5%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Rezopia/Mobility/Cloud	3.5%	4.0%	3.0%	4.0%	3.0%	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)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
ADM	4.3%	9.5%	-0.5%	4.3%	2.4%	1.8%	15.0%
Testing	-5.3%	-4.5%	3.4%	4.3%	6.6%	-4.2%	-4.1%
IMS	11.8%	-9.6%	-2.6%	4.3%	6.6%	-10.9%	-12.4%
AX	-5.0%	-4.2%	14.9%	4.3%	17.3%	20.4%	2.3%
BI	-12.5%	15.5%	3.4%	4.3%	6.6%	14.6%	2.3%
E-commerce	0.0%	21.3%	20.7%	-10.6%	6.6%	-15.1%	2.3%
ERP	12.5%	-10.2%	3.4%	4.3%	6.6%	1.8%	2.3%
Rezopia	-12.5%	15.5%	-22.4%	39.1%	-20.0%	-32.1%	2.3%
<b>Total</b>	<b>0.0%</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>

Source: Company, HDFC Sec Inst Research

*Growth was led by Europe and Row while US was weak led by Sopris*

*Onsite offshore ratio remains the same, focus is to improve margins through off shoring as utilisation is at peak level*

### IITS Geographic Revenue Mix

(% Contribution)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
USA	58.0%	60.0%	58.0%	56.0%	55.0%	56.0%	53.0%
Europe	28.0%	29.0%	30.0%	32.0%	32.0%	30.0%	30.0%
RoW	14.0%	11.0%	12.0%	12.0%	13.0%	14.0%	17.0%
<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 Geographic Revenue Growth

(% QoQ)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
USA	-1.7%	4.6%	0.0%	0.7%	4.7%	3.7%	-3.2%
Europe	3.7%	4.7%	7.0%	11.3%	6.6%	-4.5%	2.3%
RoW	0.0%	-20.6%	12.8%	4.3%	15.5%	9.7%	24.2%
<b>Total</b>	<b>0.0%</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>

Source: Company, HDFC Sec Inst Research

### IITS Onsite-Offshore Split

IT services revenue break-up (%)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
Offshore	59.0%	56.0%	58.0%	58.0%	57.0%	56.0%	56.0%
Onsite	41.0%	44.0%	42.0%	42.0%	43.0%	44.0%	44.0%
<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)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
Offshore	7.3%	-4.1%	7.1%	4.3%	4.8%	0.1%	2.3%
Onsite	-8.9%	8.5%	-1.3%	4.3%	9.2%	4.2%	2.3%
<b>Total</b>	<b>0.0%</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>

Source: Company, HDFC Sec Inst Research

### IITS Client Concentration

Client concentration (%)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
Top 5	61.0%	61.0%	61.0%	61.0%	61.0%	59.0%	59.0%
Top-10	69.0%	70.0%	69.0%	69.0%	68.0%	66.0%	65.0%
Non-top 10	31.0%	30.0%	31.0%	31.0%	32.0%	34.0%	35.0%
Top 20	79.0%	80.0%	77.0%	78.0%	76.0%	75.0%	73.0%
<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)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
Top 5	-1.6%	1.1%	3.4%	4.3%	6.6%	-1.5%	2.3%
Top-10	-2.8%	2.5%	2.0%	4.3%	5.1%	-1.2%	0.7%
Non-top 10	6.9%	-2.2%	6.9%	4.3%	10.1%	8.2%	5.3%
Top 20	0.0%	2.3%	-0.4%	5.7%	3.9%	0.5%	-0.5%
<b>Total</b>	<b>0.0%</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>

Source: Company, HDFC Sec Inst Research

*Top 5/10 clients grew 2.3/0.7% QoQ, Non Top 10 client growth have been impressive, 8Qtr CQGR of 4.3%*

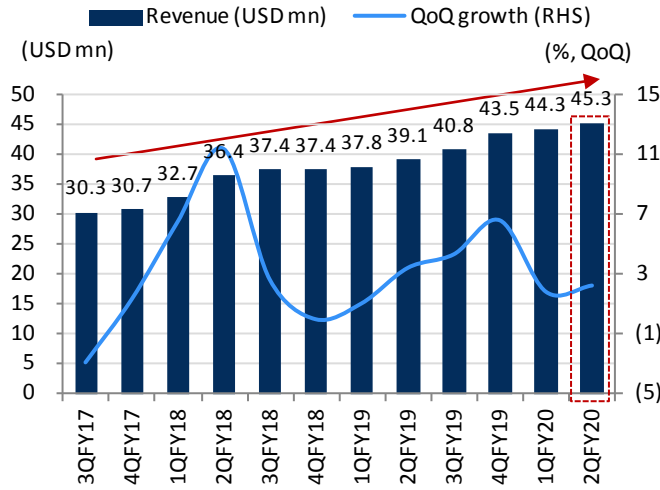
*Dependence on Top-10 clients is coming down but still high compared to peers*

**IITS revenue/EBITDA has grown at CQGR of 2.8/6.6% over the last eight quarter**

**Avg. revenue per employee in 2Q was USD 45,879, +0.3/+4.6% QoQ/YoY. There has been a steady rise in employee productivity (8-Qtr CQGR of 1.0%)**

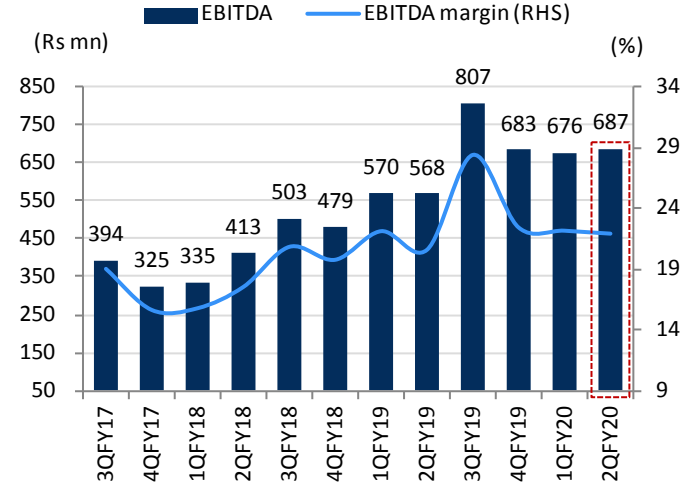
**IITS debtor days are among the lowest in the industry at 40-42 days**

**IITS Rev Growth Trend**



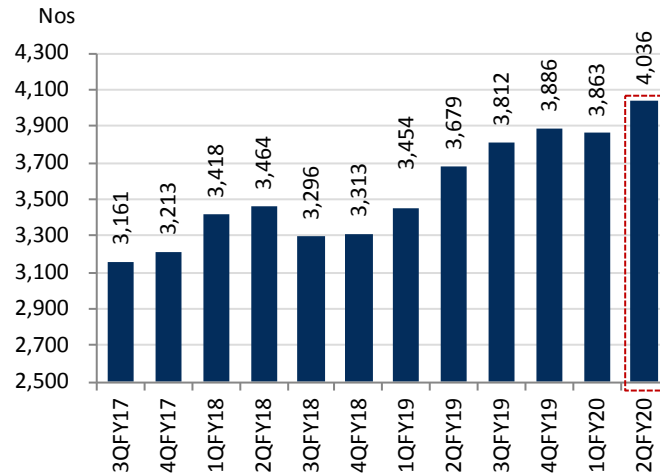
Source: Company, HDFC sec Inst Research

**IITS EBITDA, Margin Trend**



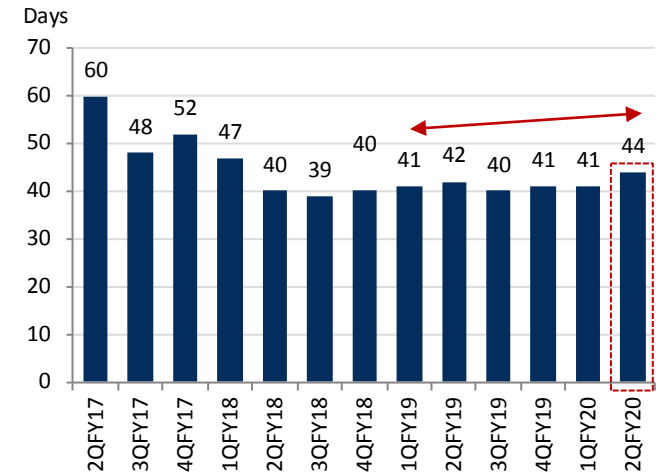
Source: Company, HDFC sec Inst Research

**IITS Headcount**



Source: Company, HDFC sec Inst Research

**IITS Debtor Days**



Source: Company, HDFC sec Inst Research

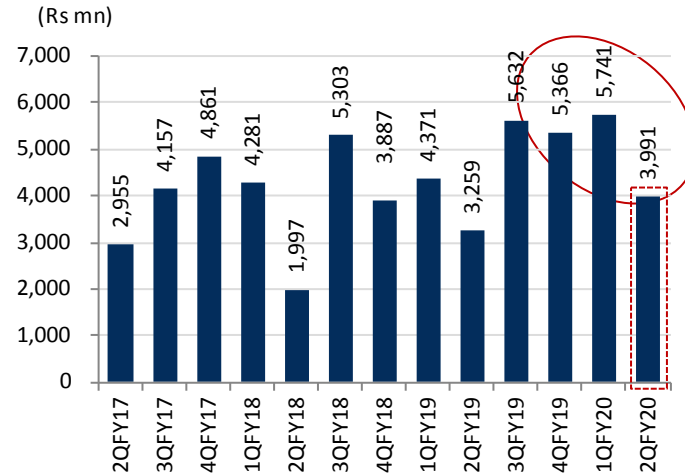
**DPS Revenue/EBITDA has grown at a CQGR of 9.0/6.1% over the last eight quarter**

**DPS employee headcount is consistently coming down**

**DPS' debtor days have increased to 43 days. There is a mismatch between the calculated consolidated DSO days and the reported DSO days in the presentation**

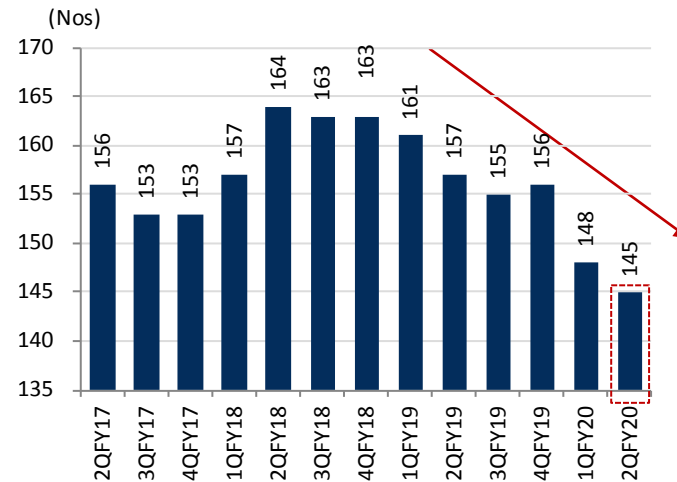
**Receivables has increased significantly in the last two years and is a cause of concern**

**DPS Quarterly Revenue Trend**



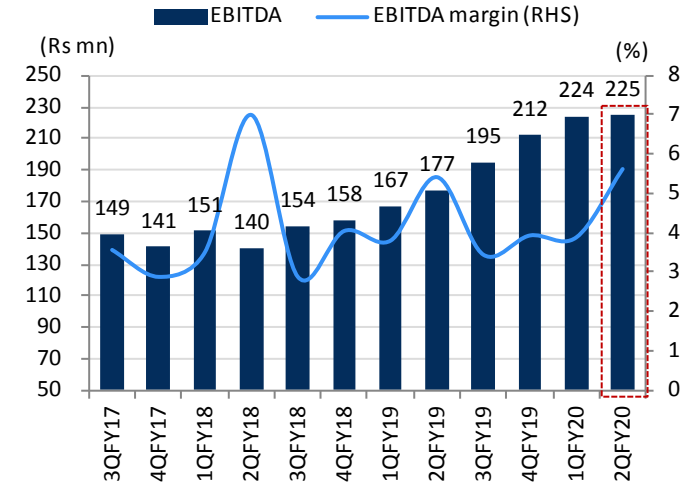
Source: Company, HDFC sec Inst Research

**DPS' Headcount**



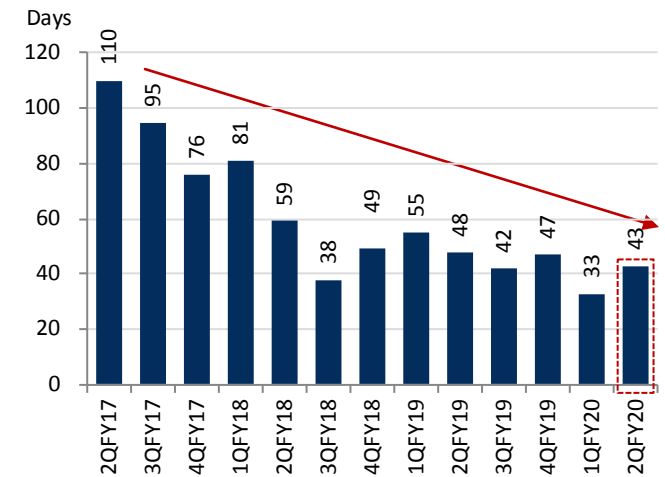
Source: Company, HDFC sec Inst Research

**DPS EBITDA Margin Trend**



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	183.4	203.8	227.2
% Growth	18.6	12.0	13.8	11.1	11.5
Revenue	9,285	11,205	12,784	14,573	16,584
% Growth	13.0	20.7	14.1	14.0	13.8
EBITDA	1,730	2,629	2,884	3,352	3,864
EBITDA Margin (%)	18.6	23.5	22.6	23.0	23.3

Source: Company, HDFC sec Inst Research

### DPS' Segment Estimates

DPS (Rs million)	FY18	FY19	FY20E	FY21E	FY22E
Revenue	15,468	18,628	21,717	23,672	25,921
% Growth	(1.9)	20.4	16.6	9.0	9.5
EBITDA	603	751	946	1,048	1,140
EBITDA Margin (%)	3.9	4.0	4.4	4.4	4.4

Source: Company, HDFC sec Inst Research

### Change In Estimates

Particulars	Earlier estimates	Revised estimates	% change
<b>FY20E</b>			
Revenue (Rs mn)	34,301	34,501	0.6
EBIT (Rs mn)	3,456	3,465	0.3
EBIT margin (%)	10.1	10.0	-3
APAT	2,751	2,802	1.8
<b>FY21E</b>			
Revenue (Rs mn)	37,637	38,244	1.6
EBIT (Rs mn)	3,916	4,003	2.2
EBIT margin (%)	10.4	10.5	6
APAT	3,107	3,186	2.5
<b>FY22E</b>			
Revenue (Rs mn)	41,393	42,504	2.7
EBIT (Rs mn)	4,474	4,567	2.1
EBIT margin (%)	10.8	10.7	-6
APAT	3,542	3,615	2.0

Source: Company, HDFC sec Inst Research

**We have increased IITS USD revenue estimate by only 0.2/0.3% for FY20/21E while the increase in revenue is consolidated revenue is due to DPS**

**We increase APAT by 1.8/2.5% for FY20/21E due to higher DPS revenue and lower tax rate.**

**We cut multiple to 12x due to concerns arising due to rising receivables**

**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	8,517	2,270	1,975	NEU	68.8	83.9	85.5	92.9	33.0	27.1	26.5	24.4	30.1	36.1	35.3	37.1
Infosys	2,918	686	835	NEU	34.6	37.2	37.9	43.7	19.8	18.4	18.1	15.7	22.0	24.4	25.4	28.5
Wipro	1,542	259	230	NEU	13.5	15.1	16.8	18.0	19.3	17.1	15.4	14.4	16.5	17.3	17.8	17.7
HCL Tech	1,577	1,163	1,250	BUY	64.7	74.6	74.0	83.0	18.0	15.6	15.7	14.0	25.3	26.0	22.2	21.7
TechM	650	739	650	NEU	43.2	48.9	45.4	51.0	17.1	15.1	16.3	14.5	21.5	22.0	19.4	20.0
<b>Tier-1 IT Median</b>									<b>19.3</b>	<b>17.1</b>	<b>16.3</b>	<b>14.5</b>	<b>22.0</b>	<b>24.4</b>	<b>22.2</b>	<b>21.7</b>
LTI	299	1,722	1,845	BUY	66.9	87.3	83.7	95.5	25.7	19.7	20.6	18.0	33.2	34.6	27.5	27.1
Mphasis	177	950	1,180	BUY	45.4	57.6	58.3	69.1	20.9	16.5	16.3	13.8	14.6	20.0	19.7	20.9
LTTS	156	1,504	1,705	BUY	45.5	68.0	74.0	88.4	33.0	22.1	20.3	17.0	27.7	32.0	28.4	28.5
Mindtree	117	713	760	NEU	32.3	44.1	36.4	47.9	22.0	16.2	19.6	14.9	21.4	24.9	17.3	22.9
Hexaware *	99	333	445	BUY	16.7	19.6	21.4	24.5	19.9	17.0	15.6	13.6	26.6	26.5	24.5	24.2
Cyient	46	407	485	NEU	38.6	43.6	39.8	42.7	10.5	9.3	10.2	9.5	18.1	19.5	16.6	16.2
Zensar	41	178	240	BUY	10.6	14.3	15.5	18.1	16.8	12.5	11.5	9.9	15.1	17.6	16.6	17.0
Persistent	48	620	655	BUY	42.0	47.5	43.3	47.5	14.8	13.0	14.3	13.0	16.0	15.7	13.8	14.7
Tata Elxsi	51	819	680	NR	38.5	46.6	38.6	45.1	21.2	17.6	21.2	18.2	37.0	34.5	23.7	24.0
Sonata	33	313	395	BUY	18.6	24.0	27.0	30.7	16.9	13.0	11.6	10.2	31.0	35.1	34.3	34.5
Intellect	25	191	315	BUY	3.5	7.7	7.6	11.7	NM	24.9	25.3	16.4	6.7	11.1	9.3	12.8
eClerx	17	452	460	NEU	74.0	61.7	50.1	51.2	6.1	7.3	9.0	8.8	24.1	17.6	13.8	14.1
Majesco	12	425	700	BUY	(1.5)	18.3	20.9	31.1	NM	23.2	20.4	13.7	NM	8.4	8.3	11.4
HGS	12	576	760	NR	96.5	84.6	85.3	101.2	6.0	6.8	6.7	5.7	10.5	8.5	11.2	11.8
Mastek	8	344	505	BUY	27.7	40.4	38.3	42.7	12.4	8.5	9.0	8.1	13.7	16.1	12.9	13.0
<b>Tier-2 IT AVG</b>									<b>16.9</b>	<b>16.2</b>	<b>15.6</b>	<b>13.6</b>	<b>19.8</b>	<b>19.5</b>	<b>16.6</b>	<b>17.0</b>

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	125	186	NA	NR	5.6	6.5	7.8	8.6	33.5	28.8	23.8	21.7	41.7	42.0	34.9	35.0
Cognizant	34	62	NA	NR	2.5	3.6	4.0	4.3	24.2	17.1	15.6	14.3	14.1	19.0	19.0	20.4
Capgemini^	19	102	NA	NR	4.9	4.4	6.5	7.2	20.8	23.3	15.5	14.2	11.5	10.1	13.4	13.6
<b>Global IT Median</b>									<b>24.2</b>	<b>23.3</b>	<b>15.6</b>	<b>14.3</b>	<b>14.1</b>	<b>19.0</b>	<b>19.0</b>	<b>20.4</b>

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

### 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>183.4</b>	<b>203.8</b>	<b>227.2</b>
<b>Growth (%)</b>	<b>18.6</b>	<b>12.0</b>	<b>13.8</b>	<b>11.1</b>	<b>11.5</b>
<b>Net Revenues</b>	<b>24.54</b>	<b>29.61</b>	<b>34.50</b>	<b>38.24</b>	<b>42.50</b>
<b>Growth (%)</b>	<b>3.5</b>	<b>20.7</b>	<b>16.5</b>	<b>10.9</b>	<b>11.1</b>
Total Operating Expenses	22.23	26.25	30.67	33.84	37.50
<b>EBITDA</b>	<b>2.31</b>	<b>3.36</b>	<b>3.83</b>	<b>4.40</b>	<b>5.00</b>
<b>EBITDA (%)</b>	<b>9.4</b>	<b>11.3</b>	<b>11.1</b>	<b>11.5</b>	<b>11.8</b>
<b>EBITDA Growth (%)</b>	<b>20.6</b>	<b>45.3</b>	<b>14.1</b>	<b>14.9</b>	<b>13.7</b>
Depreciation	0.12	0.13	0.37	0.40	0.44
<b>EBIT</b>	<b>2.19</b>	<b>3.23</b>	<b>3.46</b>	<b>4.00</b>	<b>4.57</b>
<b>EBIT (%)</b>	<b>8.9</b>	<b>10.9</b>	<b>10.0</b>	<b>10.5</b>	<b>10.7</b>
<b>EBIT Growth (%)</b>	<b>21.0</b>	<b>47.7</b>	<b>7.3</b>	<b>15.5</b>	<b>14.1</b>
Other Income	0.47	0.30	0.51	0.45	0.46
Interest	0.05	0.03	0.15	0.15	0.15
<b>PBT</b>	<b>2.60</b>	<b>3.49</b>	<b>3.83</b>	<b>4.30</b>	<b>4.88</b>
Tax (incl deferred)	0.68	1.01	1.03	1.12	1.27
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>2.80</b>	<b>3.19</b>	<b>3.61</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>2.80</b>	<b>3.19</b>	<b>3.61</b>
<b>APAT Growth (%)</b>	<b>28.8</b>	<b>28.8</b>	<b>13.7</b>	<b>13.7</b>	<b>13.5</b>
<b>EPS</b>	<b>18.4</b>	<b>23.7</b>	<b>27.0</b>	<b>30.7</b>	<b>34.8</b>
<b>EPS Growth (%)</b>	<b>28.8</b>	<b>28.6</b>	<b>13.7</b>	<b>13.7</b>	<b>13.5</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	8.57	9.69	10.97
<b>Total Shareholders' Funds</b>	<b>6.53</b>	<b>7.68</b>	<b>8.67</b>	<b>9.80</b>	<b>11.07</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>9.18</b>	<b>10.31</b>	<b>11.58</b>
<b>APPLICATION OF FUNDS</b>					
Net Block	0.33	0.54	0.35	0.14	(0.08)
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>2.52</b>	<b>2.42</b>	<b>2.30</b>
Inventories	0.00	0.00	0.00	0.00	0.00
Debtors	3.96	8.11	8.03	8.91	9.90
Cash & Equivalents	5.46	3.46	5.02	5.95	7.00
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>14.16</b>	<b>16.13</b>	<b>18.36</b>
Creditors	4.32	5.87	6.30	6.95	7.71
Other Current Liabilities & Provns	0.96	1.09	1.20	1.28	1.37
<b>Total Current Liabilities</b>	<b>5.29</b>	<b>6.97</b>	<b>7.50</b>	<b>8.24</b>	<b>9.08</b>
Net Current Assets	4.94	5.56	6.66	7.89	9.28
<b>TOTAL APPLICATION OF FUNDS</b>	<b>6.93</b>	<b>8.19</b>	<b>9.18</b>	<b>10.31</b>	<b>11.58</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	3.83	4.30	4.88
Non-operating & EO items	(0.15)	(0.50)	(0.51)	(0.45)	(0.46)
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)	0.38	(0.40)	(0.45)
Tax paid	(0.55)	(0.87)	(1.03)	(1.12)	(1.27)
<b>OPERATING CASH FLOW ( a )</b>	<b>2.98</b>	<b>(0.06)</b>	<b>3.18</b>	<b>2.88</b>	<b>3.28</b>
Capex	(0.06)	(0.46)	(0.17)	(0.19)	(0.21)
Free cash flow (FCF)	2.91	(0.52)	3.01	2.69	3.07
Investments	0.00	0.00	0.00	0.00	0.00
Non-operating income	0.10	0.05	0.51	0.45	0.46
<b>INVESTING CASH FLOW ( b )</b>	<b>0.03</b>	<b>(0.41)</b>	<b>0.34</b>	<b>0.26</b>	<b>0.25</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)	2.86	2.54	2.92
Share capital Issuance	0.00	0.00	0.00	0.00	0.00
Dividend	(1.15)	(1.43)	(1.81)	(2.06)	(2.33)
<b>FINANCING CASH FLOW ( c )</b>	<b>(1.40)</b>	<b>(1.66)</b>	<b>(1.96)</b>	<b>(2.21)</b>	<b>(2.49)</b>
<b>NET CASH FLOW (a+b+c)</b>	<b>1.61</b>	<b>(2.14)</b>	<b>1.57</b>	<b>0.93</b>	<b>1.05</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	5.95	7.00

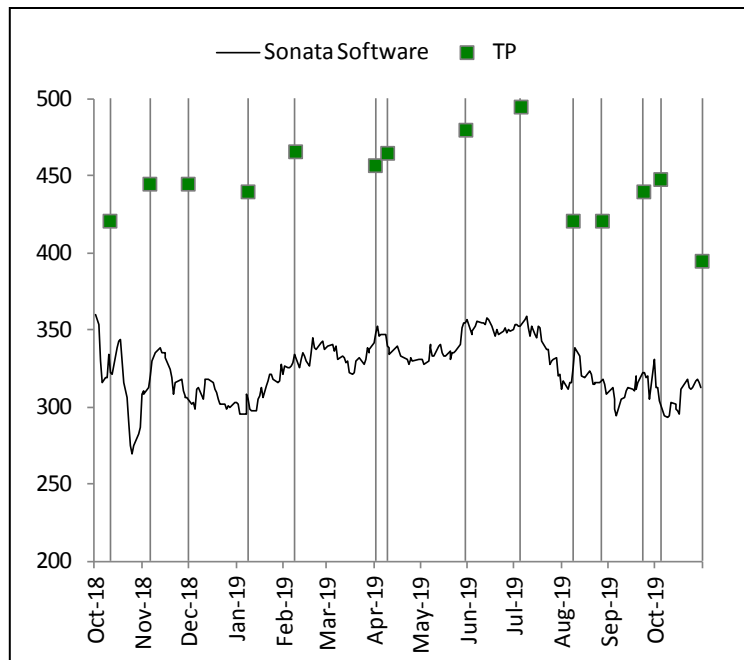
Source: Company, HDFC sec Inst Research

### Key Ratios

	FY18	FY19	FY20E	FY21E	FY22E
<b>PROFITABILITY (%)</b>					
EBITDA Margin	9.4	11.3	11.1	11.5	11.8
APAT Margin	7.8	8.4	8.1	8.3	8.5
RoE	31.0	35.1	34.3	34.5	34.6
RoIC or Core RoCE	109.6	48.4	60.8	67.9	73.7
RoCE	24.3	30.3	29.1	30.4	65.6
<b>EFFICIENCY</b>					
Tax Rate (%)	26.3	29.0	27.0	26.0	26.0
Fixed Asset Turnover (x)	17.0	16.6	17.7	17.8	18.0
Inventory (days)	0	0	0	0	0
Debtors (days)	59	100	85	85	85
Other Current Assets (days)	12	12	12	12	13
Payables (days)	71	82	75	75	75
Other Current Liab & Provns (days)	14	13	13	12	12
Cash Conversion Cycle (days)	-14	17	9	10	11
Net Debt/EBITDA (x)	(2.2)	(0.9)	(1.2)	(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	23.6	26.8	30.1
<b>PER SHARE DATA</b>					
EPS (Rs/sh)	18.4	23.7	27.0	30.7	34.8
CEPS (Rs/sh)	19.7	25.2	30.5	34.5	39.0
DPS (Rs/sh)	10.5	12.8	14.8	16.9	19.1
BV (Rs/sh)	63.0	74.0	83.6	94.4	106.7
<b>VALUATION</b>					
P/E	16.9	13.0	11.6	10.2	9.0
P/BV	5.0	4.2	3.7	3.3	2.9
EV/EBITDA	12.3	9.1	7.5	6.4	5.4
OCF/EV (%)	10.5	(0.2)	11.0	10.3	12.2
FCF/EV (%)	10.3	(1.7)	10.4	9.6	11.4
FCFE/mkt cap (%)	8.2	(2.3)	8.8	7.8	9.0
Dividend Yield (%)	3.4	4.1	4.7	5.4	6.1

Source: Company, HDFC sec Inst Research

**RECOMMENDATION HISTORY**



Date	CMP	Reco	Target
10-Oct-18	334	BUY	421
5-Nov-18	313	BUY	445
30-Nov-18	305	BUY	445
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

**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

## INSTITUTIONAL RESEARCH

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