Sonata Software (SONSOF)

CMP: ₹ 375 | Target: ₹ 440 (17%) | Target Period: 12 months | BUY

August 1, 2025

Expect gradual recovery ahead...

About the stock: Sonata Software (Sonata) provides IT services and product licensing services to its clients in BFSI, HLS (Healthcare & Lifesciences), R&M (Retail & Manufacturing) and TMT (Technology, Media and Telecom) segments.

Q1FY26 Performance: International IT services (IITS) revenue came at US$ 81.8 mn, down 0.9% QoQ/ 2.4% YoY in CC terms. IITS EBITDA margin at 16.6%, was up ~10 bps QoQ. Consol revenue came at US$ 346.5 mn, up 15% QoQ with EBITDA margin of 5.4%, down ~120 bps QoQ. PAT stood at ₹109.3 crore, up 1.7% QoQ.

Investment Rationale

- **Strong large deal momentum amid macro and client-specific headwinds:** Sonata displayed strong execution by securing 3 large deals worth US$136 mn across TMT, Healthcare, and Tech verticals. Growth was led by the ramp-up of a US$73 mn TMT deal and continued strength in HLS, which grew 15% and 17.4% QoQ, respectively, driving a healthy book-to-bill ratio of 1.28x. However, BFSI (-12.5% QoQ) and Retail (-3% QoQ) remained soft due to budget cuts at 2 key clients (1 each in BFSI & Hi-tech) & near-term risks from Microsoft's evolving GTM strategy favoring direct enterprise engagement with large enterprises. **Despite these challenges, management remains confident of achieving positive IITS revenue growth & top quartile growth overall in FY26, supported by US$105 mn in deal wins and a diversified pipeline of 30 large deals. We have baked in IT services growth CAGR of 7% over FY25-27E in US$ terms.**
- **Margins likely to improve:** IITS EBITDA margin improved by ~10bps QoQ to 16.6%, with **management targeting ~20% by FY26-end, driven by better utilization, pyramid rationalization, & increased offshoring.** While overall margins contracted ~120 bps QoQ to 5.4% due to weak domestic performance & unfavorable mix, the company's commitment to quarterly dividends (₹1.25/share announced for Q1) & continued leadership hires across key verticals reflect long-term strategic focus. **At the consolidated level, we model EBITDA margin of 6.5%/7.3% for FY26E/FY27E, as we expect a gradual margin recovery.**
- **AI-first strategy and platform-led differentiation offer long-term leverage:** Sonata is actively scaling its AI-first, modernization-led delivery model, **targeting 20% of revenue from AI-enabled services over the next three years.** Proprietary platforms like **Harmoni.AI, IntellQA, & AgentBridge** position Sonata among the few mid-tier firms offering enterprise-grade GenAI solutions. **With 95% of its workforce trained in AI $ a US$46 mn pipeline in place, the company is well-placed to drive productivity-led growth and differentiation.**

Rating and Target Price

- **Given the increasing traction in platform-led & AI-driven offerings, we expect gradual revenue and margin recovery over FY26 & FY27. Thus, we maintain our BUY rating, albeit at a reduced multiple of 21x P/E on FY27E EPS (vs 22x earlier), with lower target price of ₹440 (vs ₹580 earlier).**

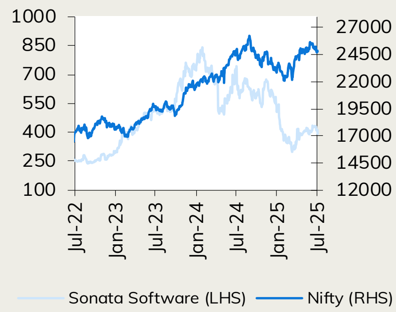
Particulars

Particulars	Amount
Market Cap (₹ Crore)	10,424
Total Debt (₹ Crore)	442
Cash and Invts (₹ Crore)	695
EV (₹ Crore)	10,171
52 week H/L	760 / 286
Equity capital (₹ Crore)	27.8
Face value	1.0

Shareholding pattern

	Sep-24	Dec-24	Mar-25	Jun-25
Promoters	28.2	28.2	28.2	28.2
FII	12.1	12.3	10.8	9.7
DII	23.4	24.3	25.9	25.6
Other	36.3	35.2	35.2	36.6

Price Chart



Key risks

- Delay in ramp up of large deals due to elongated deal cycles;
- Slower than expected recovery in revenue and margins

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Result Update

ICICI Securities – Retail Equity Research

Key Financial Summary

(₹ Crore)	FY23	FY24	FY25	5 year CAGR (FY20-25)	FY26E	FY27E	2 year CAGR (FY25-27E)
Net Sales	7,449	8,613	10,157	22.1%	11,163	12,124	9.3%
EBITDA	604	727	690	0.7%	723	881	13.0%
EBITDA Margin (%)	8.1	8.4	6.8		6.5	7.3	
PAT	452	308	425		473	580	
Adjusted PAT	452	483	425	4.8%	473	580	16.8%
EPS (Rs.)	32.6	11.1	15.3		17.0	20.9	
P/E (x)	12	22	25		22	18	
RoNW (%)	34.7	21.9	24.9		23.5	24.3	
RoCE (%)	25.9	31.4	27.4		25.1	26.9	

Source: Company, ICICI Direct Research

Performance highlights and outlook

- **Revenue Performance:** International IT services (IITS) revenue in Q1 stood at US$ 81.8 mn, down 0.9% QoQ/ 2.4% YoY in CC terms. This was mainly driven by the ramp-up of a large USD 73mn TMT deal, strong traction in healthcare and BFSI, and rising AI-led deal momentum. However, the company is facing headwinds from softness in the retail and manufacturing sectors due to tariff-related uncertainty, discretionary budget cuts at two large clients (one BFSI and one high-tech), and potential risks from change in Microsoft strategy (prioritizing direct sales to large enterprise clients). Domestic Products and Services reported revenues of US$ 265.8 mn, up 20% QoQ. At the company level for the quarter, the revenue stood at US$ 346.5 mn, up 15% QoQ.
- **Geography performance**: Geography wise on a QoQ basis, the growth was led by Europe (17% of the mix), up 44.4%, while, RoW (9% of the mix) and USA (74% of the mix) declined by 23.5% and 11.3%.
- **Margin performance**: IITS EBITDA margin at 16.6%, was up ~10 bps QoQ. Domestic products & services margin came at 1.9%, down 100 bps QoQ. At the company level EBITDA margin came at 5.4%, down ~120 bps QoQ.
- **Segment performance:** Segment wise on a QoQ basis, Healthcare (14% of the mix) and TMT (32% of the mix) grew by 17% and 15%. While, Emerging (4% of the mix), BFSI (20% of the mix) and Retail (30% of the mix) declined by 33%, 12.5% and 3%.
  - **BFSI & HLS**: Together, the BFSI and HLS segments now form over 30% of total revenues, a sharp increase from 13% three years ago. The company anticipates these verticals could scale up to US$250 mn over the next 2–5 years. Despite budgetary constraints at a key client, BFSI showed steady progress, while Healthcare stayed resilient, benefiting from AI-led solutions across pharma and health tech sub-verticals.
  - **Retail and manufacturing:** Sonata continues to face challenges in its retail and manufacturing segments due to macro uncertainties, including tariff-related concerns
- **TCV, Deal Wins and pipeline:** Sonata bagged **3 large deals** during the quarter—one with a BFSI client to modernize a cloud lending platform, another with a TMT firm that expanded its existing partnership, and a second BFSI client focused on modernizing its data and application landscape. **The company's GenAI pipeline has reached US$46 mn across over 100 clients, and management reiterated its ambition to drive 20% of revenue from AI-enabled services over the next 3 years. Additionally, its Microsoft Fabric-related pipeline now stands at US$39 mn.**
- **Headcount/Attrition:** Total employees for the IITS business stood at 6,393 employees, a net increase of 24 employees QoQ. Attrition for the quarter stood at 16%, up 200 bps QoQ. Moreover, 97% of the company's workforce is GenAI trained.
- **Wage hike:** The company is rolling out its annual salary revisions in 2 stages—effective August 1 for junior and mid-level employees, and from October 1 for senior leadership. Management stated that the impact on margins will remain in line with past wage increment cycles.
- **GenAI:** Sonata is delivering its AI strategy across three core areas—engineering, industry-specific solutions, and internal efficiency. Key initiatives include embedding AI via **Harmoni.AI and IntellQA,** launching enterprise-grade offerings like **AgentBridge,** and deploying internal tools such as **Sonata GPT** and productivity bots.
- **Guidance/Aspiration:** While refraining from issuing numerical revenue guidance, management reiterated its **aspiration to maintain top-quartile**

growth among mid-tier peers over the long term. Sonata remains focused on improving IITS margins and aims to reach ~20% EBITDA by FY26-end.

- **Dividend:** The company declared an interim dividend of ₹1.25 per share.
- **Strengthening Microsoft-led momentum:** Sonata continues to benefit from its strong partnership with Microsoft, contributing over 50% of revenues. The company is expanding its Microsoft-focused offerings, especially in areas like Azure, Dynamics 365, and Power Platform, which remain in demand despite macro softness. With 7 Microsoft specializations and strong execution capabilities, Sonata is well-positioned to capture digital transformation spends from enterprise clients globally. This strategic focus provides resilience and consistent growth visibility in its core ISV and enterprise segments.

Quarter Performance

	Q1FY26	Q1FY25	YoY (%)	Q4FY25	QoQ (%)	Comments
Revenue	2,965	2,527	17.3	2,617	13.3	International IT services (IITS) revenue in Q1 stood at US$ 81.8 mn, down 0.9% QoQ/ 2.4% YoY in CC terms. Domestic Products and Services reported revenues of US$ 265.8 mn, up 20% QoQ.
Employee expenses	418	369	13.2	419	(0.3)	
Purchase of stock-in trade	2,209	1,787	23.6	1,863	18.5	
Gross Margin	339	371	(8.7)	335	1.2	
Gross margin (%)	11.4	14.7	-326 bps	12.8	-137 bps	
Other expenses	179	195	(8.1)	162	10.5	
EBITDA	160	176	(9.4)	173	(7.5)	
EBITDA Margin (%)	5.4	7.0	-159 bps	6.6	-121 bps	IITS EBITDA margin at 16.6%, was up ~10 bps QoQ. Domestic products & services margin came at 1.9%, down 100 bps QoQ.
Depreciation & amortisation	26	33	(21.6)	23	13.2	
EBIT	134	143	(6.5)	150	(10.7)	
EBIT Margin (%)	4.5	5.7	-115 bps	5.7	-121 bps	
Other income (less interest)	19	(1)	(1,764.3)	1	1,608.9	
PBT	153	142	7.7	151	1.3	
Tax paid	43	36	20.1	43	0.3	
PAT	109	106	3.5	108	1.7	

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 1: Profit and loss statement ₹ crore

(Year-end March)	FY24	FY25	FY26E	FY27E
Total Revenues	**8,613**	**10,157**	**11,163**	**12,124**
Growth (%)	15.6	17.9	9.9	8.6
Total Op Expenditure	7,886	9,468	10,440	11,243
EBITDA	**727**	**690**	**723**	**881**
Growth (%)	20.4	(5.2)	4.8	21.9
Depr & Amortization	132	121	116	121
Other Income	126	71	57	53
Interest costs	85	65	35	50
PBT before Excep Items	636	574	628	763
Growth (%)	6.5	(9.8)	9.5	21.4
Tax	153	149	155	183
PAT before Excep Items	483	425	473	580
Exceptional items	(175)	-	-	-
PAT before MI	308	425	473	580
Minority Int & Pft. from associates	-	-	-	-
PAT	**308**	**425**	**473**	**580**
Growth (%)	(32)	38	11	23
EPS	11.1	15.3	17.0	20.9
EPS (Growth %)	(66)	38	11	23

Source: Company, ICICI Direct Research

Exhibit 2: Cash flow statement ₹ crore

(Year-end March)	FY24	FY25	FY26E	FY27E
Net profit before Tax	**461**	**574**	**628**	**763**
Depreciation & Amortization	132	121	116	121
WC changes	(209)	103	8	7
Other non cash adju.	159	10	(22)	(3)
Income taxes paid	(262)	(164)	(155)	(183)
CF from Operations	**281**	**644**	**575**	**705**
Capital expenditure	0	(68)	(39)	(42)
Δ in investments	(88)	(389)	-	-
Other investing cash flow	33	21	57	53
CF from Investing Activities	**(54)**	**(436)**	**18**	**11**
Issue of equity	14	0	-	-
Δ in debt funds/lease liablities	139	(276)	(24)	(24)
Dividends paid	(215)	(119)	(166)	(203)
Other financing cash flow	(46)	(38)	(35)	(50)
CF from Financial Activities	**(109)**	**(433)**	**(225)**	**(277)**
Δ in cash & cash bank balance	118	(225)	368	439
Effect of exchange rate changes	1	(1)	-	-
Opening cash	417	536	449	818
Closing cash	**865**	**449**	**818**	**1,257**

Source: Company, ICICI Direct Research

Exhibit 3: Balance Sheet ₹ crore

(Year-end March)	FY24	FY25	FY26E	FY27E
Equity	28	28	28	28
Reserves & Surplus	1,379	1,678	1,986	2,363
Networth	1,406	1,706	2,013	2,390
Minority Interest	-	-	-	-
LT liabilties & provisions	219	187	187	187
Total Debt	674	442	442	442
Source of funds	**2,299**	**2,334**	**2,642**	**3,019**
Assets				
Net fixed assets	558	490	437	382
Goodwill	1,113	1,140	1,140	1,140
Long term loans	-	-	-	-
Other non current assets	403	394	424	453
Loans and advances	-	-	-	-
Inventories	98	47	52	56
Current Investments	232	245	245	245
Debtors	1,605	1,741	1,913	2,078
Cash & Cash equivalents	865	449	818	1,257
Other current assets	275	249	274	297
Current liabilities	2,813	2,378	2,613	2,839
Provisions	37	43	47	51
Net current assets	226	311	641	1,044
Application of funds	**2,299**	**2,334**	**2,642**	**3,019**

Source: Company, ICICI Direct Research

Exhibit 4: Key ratios

(Year-end March)	FY24	FY25	FY26E	FY27E
Per share data (₹)				
EPS-diluted	11.1	15.3	17.0	20.9
Cash per share	31.1	16.2	29.4	45.2
BV	50.6	61.4	72.4	86.0
DPS	7.9	6.7	6.0	7.3
Operating Ratios (%)				
EBITDA Margin	8.4	6.8	6.5	7.3
Adjusted PBT Margin	7.4	5.6	5.6	6.3
Adjusted PAT Margin	3.6	4.2	4.2	4.8
Return Ratios (%)				
RoNW	21.9	24.9	23.5	24.3
RoCE	31.4	27.4	25.1	26.9
RoIC	49.5	34.6	38.4	50.1
Valuation Ratios (x)				
P/E	21.6	24.5	22.0	18.0
EV / EBITDA	13.7	14.7	13.6	10.6
Price to Book Value	7.4	6.1	5.2	4.4
EV/Total Revenues	1.2	1.0	0.9	0.8
MCap/Total Revenues	1.2	1.0	0.9	0.9
Turnover Ratios				
Debtor days	68	63	63	63
Creditors days	60	56	56	56
Solvency Ratios				
Debt/EBITDA	0.9	0.6	0.6	0.5
Total Debt / Equity	0.5	0.3	0.2	0.2
Current Ratio	1.1	1.1	1.2	1.4
Quick Ratio	1.0	1.1	1.2	1.3
Debt / EBITDA	0.9	0.6	0.6	0.5

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%

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