

Healthy organic performance, robust guidance...

About the stock: Coforge offers system integration, apps & BPO services to BFSI, travel & healthcare verticals

- Coforge's revenues and PAT have grown at a CAGR of ~12% each over the past five years
- Healthy OCF, EBITDA (~75%) and robust return ratios (RoCE > 20%)

Q1FY22 Results: Coforge reported robust Q1FY22 results on the revenue front.

- Dollar revenues increased 16.0% QoQ of which organic was 7.6% QoQ
- EBITDA margin declined 243 bps QoQ led by wage hike
- Revised organic guidance upwards to 19.0% YoY (in CC terms) in FY22E

What should investors do? Coforge's share price has grown by ~11x over the past five years (from ~₹ 470 in July 2016 to ~₹ 5025 levels in July 2021).

- We downgrade the stock from BUY to HOLD

Target Price and Valuation: We value Coforge at ₹ 5500 i.e. 40x P/E on FY23E EPS

Key triggers for future price performance:

- Increase in deal size. Signed a US\$105 million BFS deal (for four years), Insurance US\$20 million (for three year), healthy order book to drive growth
- Bottoming out of travel vertical (in US), preferred partnership with Fortune 500 insurance & Tier 1 banking companies, recent acquisition and aggressive hiring to drive 26.5% CAGR over FY21-23E
- A 253 bps improvement in margins expected in FY21-23E due to offshoring, higher margins in acquired company, reversal of travel discount and growth

Alternate Stock Idea: Apart from Coforge, in our IT coverage we also like LTI.

- Larsen & Toubro Infotech's (LTI) ability to deliver end-to-end solutions is expected to help in registering industry leading growth
- BUY with a target price of ₹ 5,065



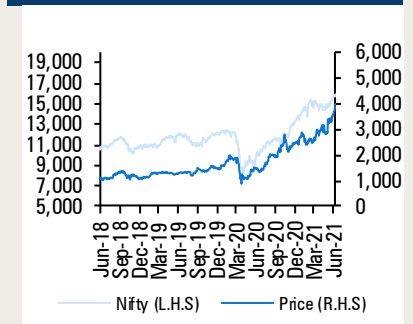
Particulars

Particular	Amount
Market Capitalisation (₹ Crore)	31,237.4
Total Debt (₹ Crore)	4.8
Cash & Investment (₹ Crore)	917.1
EV (₹ Crore)	30,325.1
52 week H/L	5057/ 1774
Equity capital	62.5
Face value	10.0

Shareholding pattern

	Sep-20	Dec-20	Mar-21	Jun-21
Promoters	70	64	64	56
FII	13	14	15	19
DII	8	12	12	15
Public	9	9	10	10

Price Chart



Recent event & key risks

- Revised organic revenue guidance upwards
- **Key Risk:** (i) Deceleration in deal pipeline, (ii) higher than expected margins

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Key Financial Summary

Financials	FY19	FY20	5 Year		FY22E	FY23E	2 year CAGR (FY21-23E)
			FY21	CAGR (FY16-21)			
Net Sales	3,676	4,184	4,663	11.7%	6,478	7,581	27.5%
EBITDA	645	720	786	11.1%	1,166	1,471	36.7%
EBITDA Margins (%)	17.6	17.2	16.9		18.0	19.4	
Net Profit	403	444	456	11.5%	661	865	37.8%
EPS (₹)	65.7	71.4	73.3		106.3	139.1	
P/E	76.5	70.4	68.6		47.3	36.1	
RoNW (%)	19.5	18.5	18.5		23.4	26.2	
RoCE (%)	25.2	23.0	23.3		26.8	29.8	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter & conference call highlights

Q1FY22 Earnings Conference Call highlights

- Organic revenues increased 7.6% QoQ to US\$185.8 million led by 10.1% QoQ growth in insurance vertical (32% of revenues), BFS up 3.2% (16% of revenues), travel up 15.8% QoQ (20% of revenues) and others up 2.1% of revenues. Top 5 on organic basis grew 3.9% QoQ and top 10 5.6% QoQ
- In the quarter, the company has acquired 11 new logos, three large deals one in BFS & insurance and one in Cloud & Infra. Coforge expects BFS to lead growth in coming quarters followed by insurance & travel. In BFS, the company is seeing traction in innovation & compliance while in travel it expects further ramp up in Europe. Travel is expected to see healthy growth led by cloud, touchless travel and automated self-services. Travel has fully recovered in the US
- This, coupled with 18% increase in headcount, normalisation in utilisation (due to ramp up of projects of large deal won) and hi Tech & Manufacturing (9% of revenues), retail & health (~9% of revenues) is expected to drive growth in coming quarters. Hence, we expect Coforge to substantially surpass its organic growth guidance of 19% YoY and expect 25% YoY organic growth in FY22E
- In terms of margins, the current quarter was impacted by wage hike (200 bps), lower utilisation and 100 bps due to deferral of license revenue sale and visa cost. Going forward, Coforge expects Q2FY22E margins to improve at least 200 bps and has reiterated 19% EBITDA margin guidance (pre-RSU)
- We believe the company has many margin levers like automation offshoring, reversal of travel discount, higher utilisation, absence of visa cost in subsequent quarters, license revenues and revenue growth to drive margins. Hence, we expect margins to improve on a QoQ basis
- In the other segment, retail & healthcare accounts for ~9% of revenues, hi tech & manufacturing - 9% of revenues and 7% government business outside India. The company plans to utilise the recent approval to raise ₹ 375 core via the ADR route along with secondary sales
- Fresh order intake was at US\$318 million, up 58% QoQ (including inorganic order). The executable order book over the next 12 months on an organic basis grew 7.7% QoQ to US\$560 million. Overall order book increased 24% QoQ to US\$645 million
- The company's top five and Top 6-10 clients increased 15.8% QoQ each, respectively
- DSO days increased by one day QoQ to 71 days
- The company has added 8100 employees in the quarter of which 1138 added were on an organic basis while the rest were inorganic. Utilisation declined 400 bps QoQ to 77.0% while attrition increased 210 bps QoQ to 12.6%

Exhibit 1: Variance Analysis

	Q1FY22	Q1FY22E	Q1FY21 YoY (%)	Q4FY21 loQ (%)		Comments	
Revenue	1,461.6	1,400.0	1,057.0	38.3	1,261.5	15.9	The company's revenue grew 16.0% QoQ of which 7.6% QoQ was organic growth. The growth was led by BFS, Insurance & Travel vertical
Employee expenses	1,025.0	957.6	724.1	41.6	858.0	19.5	
Gross Margin	436.6	442.4	332.9	31.2	403.5	8.2	
Gross margin (%)	29.9	31.6	31.5	-162 bps	32.0	-211 bps	
SG&A expenses	226.2	212.8	164.3	37.7	191.3	18.2	
EBITDA	210.4	229.6	168.6	24.8	212.2	-0.8	
EBITDA Margin (%)	14.4	16.4	16.0	-156 bps	16.8	-243 bps	EBITDA margin declined 243 bps QoQ to 14.4% (below our estimate of 16.4%) mainly led by wage hikes, higher visa costs and transition cost
Depreciation & amortisation	52.4	60.3	46.5	12.7	44.9	16.7	
EBIT	158.0	169.3	122.1	29.4	167.3	-5.6	
EBIT Margin (%)	10.8	12.1	11.6	-74 bps	13.3	-245 bps	
Other income (less interest)	5.2	-3.0	4.8	8.3	10.9	-52.3	
PBT	163.2	166.3	126.9	28.6	178.2	-8.4	
Tax paid	32.0	38.2	26.0	23.1	40.8	-21.6	
PAT	123.6	114.7	79.9	54.7	133.0	-7.1	PAT was higher than our expectation due to lower tax rate

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY22E			FY23E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	6,108	6,478	6.1	7,168.0	7,581	5.8	Healthy deal pipeline, inorganic acquisition and the company's robust guidance prompt us to revise our estimates upwards
EBITDA	1,173	1,166	-0.6	1,391.0	1,471	5.7	
EBITDA Margin (%)	19.2	18.0	-120 bps	19.4	19.4	-1 bps	Margins to stabilise at 19.4% in FY23E
PAT	677	661	-2.4	815.0	865	6.1	
EPS (₹)	108.9	106.3	-2.4	131.1	139.1	6.1	

Source: Company, ICICI Direct Research

Key Metrics

Exhibit 3: Geography-wise break-up

	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22
<u>Revenue by geography (%)</u>					
America	47.0	48.0	49.0	46.0	52.0
EMEA	36.0	36.0	36.0	40.0	35.0
RoW	17.0	16.0	15.0	14.0	13.0
<u>Growth QoQ (%)</u>					
America	-7.4	12.8	6.0	0.7	30.9
EMEA	-18.5	10.5	3.8	19.1	1.4
RoW	10.0	4.0	-2.7	0.1	7.6

Source: Company, ICICI Direct Research

America led growth in the quarter

Exhibit 4: Vertical wise break-up

	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22
<u>Revenue by verticals (%)</u>					
Banking & financial services	17.0	17.0	18.0	17.0	21.0
Insurance	33.0	34.0	32.0	31.0	31.0
Transport	19.0	19.0	20.0	19.0	19.0
Others	30.0	30.0	30.0	33.0	29.0
<u>Growth QoQ (%)</u>					
Banking & financial services	2.7	10.5	9.9	1.3	43.1
Insurance	-3.6	13.8	-2.3	3.9	15.8
Transport	-36.2	10.5	9.3	1.9	15.8
Others	0.7	10.5	3.8	17.9	1.8

Source: Company, ICICI Direct Research

The growth was led by BFS, Insurance and Transport

Exhibit 5: Client & human resource matrix

	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22
<u>Client metrics</u>					
Between 1 to 5 million	81	83	87	88	95
Between 5 to 10 million	15	16	17	16	20
Above 10 million	11	10	11	11	15
<u>Headcount, Utilization, Attrition</u>					
Total Employees	10,598	11,162	11,424	12,391	20,491
Utilization	77	81	78.9	81.0	77.0
Attrition	11.8	10.5	10.4	10.5	12.6

Source: Company, ICICI Direct Research

Utilisation decreased in the quarter. Attrition has risen as seen other peer companies

Financial summary

Exhibit 6: Profit and loss statement				
	₹ crore			
	FY20	FY21	FY22E	FY23E
Total operating Income	4,184	4,663	6,478	7,581
Growth (%)	13.8	11.4	38.9	17.0
COGS (employee expenses)	2,753	3,169	4,327	4,988
S,G&A expenses	711	707	985	1,122
Total Operating Expenditure	3,464	3,876	5,312	6,111
EBITDA	720	786	1,166	1,471
Growth (%)	11.6	9.3	48.3	26.1
Depreciation	173	184	253	296
Other Income (net)	56	11	(7)	(7)
PBT	603	614	906	1,168
Total Tax	128	130	199	253
Adjusted 'PAT	444	456	661	865
Growth (%)	10	3	45	31
Adjusted EPS (₹)	71.4	73.3	106.3	139.1
Growth (%)	8.7	2.6	45.0	30.8

Source: Company, ICICI Direct Research

Exhibit 7: Cash flow statement				
	₹ crore			
	FY20	FY21	FY22E	FY23E
Profit before Tax	603	614	906	1,168
Add: Depreciation	173	184	253	296
(Inc)/dec in Current Assets	(362)	(160)	(501)	(302)
Inc/(dec) in CL and Provisions	-	-	444	225
Taxes paid	(181)	(168)	(199)	(253)
CF from operating activities	297	762	903	1,133
(Inc)/dec in Investments	(679)	-	-	-
(Inc)/dec in Fixed Assets	(73)	(78)	(1,101)	(144)
Others	7	7	(7)	(7)
CF from investing activities	112	(235)	(1,108)	(151)
Issue/(Buy back) of Equity	28	-	-	-
Inc/(dec) in loan funds	(5)	(62)	-	-
Dividend paid & dividend tax	(147)	(69)	(297)	(389)
CF from financing activities	(133)	(553)	(107)	(539)
Net Cash flow	300	(26)	(313)	443
Exchange difference	11	-	-	-
Opening Cash	558	826	812	500
Closing Cash	903	812	500	943

Source: Company, ICICI Direct Research

Exhibit 8: Balance sheet				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Liabilities				
Equity Capital	63	61	61	61
Reserve and Surplus	2,334	2,406	2,769	3,244
Total Shareholders funds	2,397	2,466	2,830	3,305
Total Debt	5	1	341	341
Provisions	59	70	70	70
Minority Interest / Other non	164	102	148	198
Total Liabilities	2,625	2,638	3,388	3,914
Assets				
Net Block	670	598	1,597	1,595
Capital WIP	0	0	0	0
Total Fixed Assets	671	598	1,597	1,595
Goodwill	409	423	423	423
Deferred tax assets	130	155	155	155
Debtors	857	890	1,236	1,446
Other Current Assets	377	415	577	675
Cash	903	812	500	943
Current Investments	14	12	12	12
Total Current Assets	2,151	2,130	2,325	3,077
Trade payables	284	372	517	605
Other current liabilities	498	480	771	902
Short term provisions	33	23	31	37
Total Current Liabilities	815	875	1,319	1,544
Net Current Assets	1,336	1,255	1,006	1,533
Application of Funds	2,625	2,638	3,388	3,914

Source: Company, ICICI Direct Research

Exhibit 9: Key ratios				
	₹ crore			
(Year-end March)	FY20	FY21	FY22E	FY23E
Per share data (₹)				
Adjusted EPS (Diluted)	71.4	73.3	106.3	139.1
DPS	31	24	49	64
Cash per Share	145.2	130.7	80.4	151.7
BV per share (Diluted)	385.3	396.7	455.2	531.7
Operating Ratios (%)				
EBITDA Margin	17.2	16.9	18.0	19.4
PBT Margin	14.4	13.2	14.0	15.4
PAT Margin	10.6	9.8	10.2	11.4
Debtor days	75	70	70	70
Creditor days	25	29	29	29
Return Ratios (%)				
RoE	18.5	18.5	23.4	26.2
RoCE	23.0	23.3	26.8	29.8
RoC	32.0	33.2	31.8	39.7
Valuation Ratios (x)				
P/E (Adjusted)	70.4	68.6	47.3	36.1
EV / EBITDA	42.1	38.7	26.6	20.8
EV / Net Sales	7.2	6.5	4.8	4.0
Market Cap / Sales	7.5	6.7	4.8	4.1
Price to Book Value	13.0	12.7	11.0	9.5
Solvency Ratios				
Debt/EBITDA	0.0	0.0	0.3	0.2
Debt / Equity	0.0	0.0	0.1	0.1
Current Ratio	1.5	1.5	1.4	1.4
Quick Ratio	1.5	1.5	1.4	1.4

Source: Company, ICICI Direct Research

Exhibit 10: ICICI Direct coverage universe (IT)

Company	Cmp (₹)	TP (₹)	Rating	Mcap (₹ Cr)	EPS (₹)				P/E (x)				RoCE (%)				RoE (%)			
					FY20	FY21	FY22E	FY23E	FY20	FY21	FY22 E	FY23 E	FY20	FY21	FY22E	FY23E	FY20	FY21	FY22E	FY23E
HCL Tech (HCLTEC)	1,001	1,110	Hold	2,66,425	40.8	45.8	50.6	60.9	25	22	20	16	23.0	23.5	24.1	25.7	21.6	20.8	20.5	21.4
Infosys (INFTEC)	1,614	1,825	Buy	6,87,497	38.9	45.5	54.8	64.3	41	35	29	25	30.8	31.7	34.0	37.0	25.2	25.2	27.8	30.3
TCS (TCS)	3,217	3,800	Buy	11,90,290	86.2	86.7	108.3	127.2	37	37	30	25	44.4	45.9	50.9	54.0	38.4	37.5	43.0	45.3
Tech M (TECMAH)	1,133	1,120	Buy	1,09,614	59.5	50.2	60.1	70.2	19	23	19	16	18.3	19.8	21.2	22.5	17.5	17.8	19.1	19.9
Wipro (WIPRO)	596	670	Hold	3,26,730	16.6	19.1	21.1	25.7	36	31	28	23	19.3	21.3	22.8	27.5	17.4	19.5	21.6	26.3
Mindtree (MINCON)	2,768	3,065	Buy	45,621	38.3	67.4	81.1	95.8	72	41	34	29	23.0	32.5	33.1	33.1	20.0	25.7	25.9	25.7
LTI (LTINFC)	4,508	5,065	Buy	78,764	86.6	110.3	125.4	145.5	52	41	36	31	30.7	31.9	30.9	30.6	28.1	26.5	25.7	25.4
Coforge (NIITEC)	5,025	5,500	Hold	31,237	71.4	73.3	106.3	139.1	70	69	47	36	23.0	23.3	26.8	29.8	18.5	18.5	23.4	26.2
Infoedge (INFEDG)	5,265	5,740	Buy	67,699	26.8	21.2	33.3	47.1	197	248	158	112	18.0	7.7	12.4	16.2	13.5	6.0	9.3	12.2
Teamlease (TEASER)	3,940	4,550	Buy	6,736	20.5	45.3	68.9	100.3	193	87	57	39	15.0	14.2	16.4	19.8	6.5	11.6	15.8	18.6

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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