

Healthy quarterly performance...

Hexaware Technologies (Hexaware) reported Q2CY20 numbers. US\$ revenues fell 1.2% QoQ to US\$208.1 million vs. other midcap IT companies, which, on average, reported 4% QoQ decline. The decline in revenues was due to supply side issues (primarily in BPS), pricing discount and offshoring. EBIT margins also increased 144 bps to 13.2%. Going forward, the company expects flat to small volume growth in Q3 and Q4 as one of the top three customers of the company (that was a headwind) has returned to growth in Q2. The company expects margins in CY20 to sustain H1 actuals +/- 30 bps (i.e. 16.2% EBITDA margins +/-30 bps). The company's DSO days declined five days to 77 days. The company has declared ₹ 1.5 dividend per share.

Revenue expected to improve in coming quarters

Hexaware reported healthy Q2CY20 on the back of healthy improvement in banking (3.4% QoQ), healthcare & insurance (3.5% QoQ) and hi tech & professional (2.1% QoQ) partially offset by 27.2% QoQ decline in travel & transportation vertical. We believe this improving trend will continue in coming quarters with travel being a laggard. In addition, one of the top three clients of the company has returned to growth in Q2CY20, which will further boost revenue growth in coming quarters. This coupled with healthy growth in net new deal wins (up 60% YoY in H1CY20, highest in past three years), improving deal wins in cloud and market share gain via vendor consolidation bodes well for future revenue growth. Hence, we expect dollar revenues to increase at a CAGR of 8% over CY19-21E.

Margins to improve in CY21E

EBITDA margins increased ~240 bps to 17.3% in Q2CY20 on the back of forex gain (80 bps), higher utilisation (170 bps) and other cost rationalisation partially offset by lower bill rates (50 bps) and higher visa cost (70 bps). In addition, we believe there are tailwinds of reducing travel & subcontracting cost. This, coupled with rupee depreciation, lower attrition, higher offshoring and utility cost could act as near-term tailwind. Hence, we expect margins to improve 115 bps to 16.9% in CY20E and 17.2% in CY21E.

Valuation & Outlook

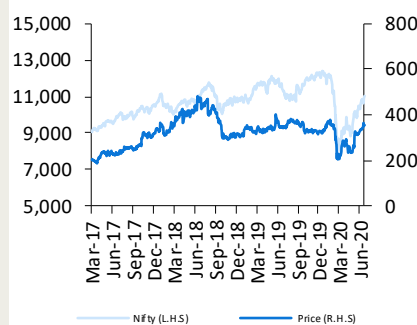
The company has seen robust deal wins in the quarter. This coupled with traction in cloud, receding supply side issue in BPO and vendor consolidation opportunity bodes well for revenue growth in coming quarters. Further, we expect margins to improve in coming quarters led by cost rationalisation and improved revenue trajectory. However, the recent run up in stock price factors in most of the positives. Hence, we maintain our **HOLD** rating on the stock with a revised target price of ₹ 415/share (16x FY22E PE).



Particulars

Particular	Amount
Market Capitalisation	₹11210 crore
Total Debt	₹143 crore
Cash and Investments	₹247 crore
EV	₹11107 crore
52 week H/L	399 / 202
Equity Capital	₹60 crore
Face Value	₹2

Price Performance



Key Highlights

- Improvement in net new deal wins and growth in top account to drive revenues
- Margins to improve gradually in coming quarters
- Maintain HOLD recommendation with revised target price of ₹ 415

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Key Financial Summary

(₹ Crore)	CY17	CY18	CY19	CY20E	CY21E	CAGR (CY19-21E)
Net Sales	3,942.0	4,647.8	5,582.5	6,299.1	6,929.0	11.4%
EBITDA	655.2	733.8	878.2	1,063.7	1,193.2	16.6%
EBITDA Margins (%)	16.6	15.8	15.7	16.9	17.2	
Net Profit	499.5	583.5	641.3	659.3	777.3	10.1%
EPS (₹)	16.6	19.3	21.2	21.8	25.7	
P/E (x)	22.1	18.9	17.2	16.8	14.2	
RoE (%)	24.9	24.4	23.2	20.4	21.0	
RoCE (%)	31.6	30.0	26.6	23.6	24.9	

Source: Company, ICICI Direct Research

Financial summary

Exhibit 1: Profit and loss statement					₹ crore
(Year-end March)	CY18	CY19	CY20E	CY21E	
Total operating Income	4,648	5,583	6,299	6,929	
Growth (%)	17.9	20.1	12.8	10.0	
COGS (employee expenses)	2,480	3,028	3,787	4,038	
S,G&A expenses	1,434	1,680	1,449	1,698	
Total Operating Expenditure	3,914	4,708	5,235	5,736	
EBITDA	734	874	1,064	1,193	
Growth (%)	12.0	19.1	21.7	12.2	
Depreciation	65	103	240	265	
Other Income less interest	58	4	-5	37	
PBT	727	775	819	966	
Total Tax	143	138	160	188	
Minority Interest	0	0	0	0	
Exceptional Item	0	0	0	0	
PAT before exceptional item	583	637	659	777	
Growth (%)	16.8	9.2	3.4	17.9	
Reported EPS (₹)	19.7	21.5	22.1	26.1	
PAT after exceptional item	583	637	659	777	
Adjusted EPS (₹)	19.3	21.2	21.8	25.7	

Source: Company, ICICI Direct Research

Exhibit 2: Cash flow statement					₹ crore
(Year-end March)	CY18	CY19	CY20E	CY21E	
Profit before Tax	727	779	819	966	
Add: Depreciation	65	103	240	265	
(Inc)/dec in Current Assets	-305	-294	-237	-203	
Inc/(dec) in CL and Provision	204	134	97	60	
Taxes paid	-143	-138	-160	-188	
CF from operations	605	596	753	936	
(Inc)/dec in Investments	-49	10	5	-37	
(Inc)/dec in Fixed Assets	-66	-1,044	-542	-173	
Others					
CF from investing	-115	-1,034	-537	-210	
Inc/(dec) in loan funds	0	143	51	-83	
Dividend paid & dividend tax	-251	-305	-198	-307	
Others	52	26	0	0	
CF from financing	-199	-136	-147	-390	
Net Cash flow	291	-574	70	336	
Exchange difference	-0	1	0	0	
Opening Cash	515	805	232	301	
Closing Cash	805	232	301	637	

Source: Company, ICICI Direct Research

Exhibit 3: Balance sheet					₹ crore
(Year-end March)	CY18	CY19	CY20E	CY21E	
Liabilities					
Equity Capital	59	60	60	60	
Reserve and Surplus	2,332	2,706	3,167	3,638	
Share Premium					
Total Shareholders funds	2,392	2,765	3,227	3,697	
Total debt	0	143	194	111	
Other liabilities & Provisions	31	47	57	62	
Total Liabilities	2,422	2,956	3,477	3,871	
Assets					
Net assets & CWIP	618	948	1,250	1,158	
Goodwill	181	1,176	1,176	1,176	
Other non current assets	348	320	368	405	
Debtors	1,076	1,333	1,503	1,654	
Other financial assets	20	47	50	55	
Other Current Assets	60	98	113	125	
Current Investments	10	0	0	0	
Cash	805	232	301	637	
Bank Balance	15	15	15	15	
Trade Payable	330	395	446	490	
OCL & Provisions	381	818	854	864	
Application of Funds	2,422	2,956	3,477	3,871	

Source: Company, ICICI Direct Research

Exhibit 4: Key ratios					₹ crore
(Year-end March)	CY18	CY19	CY20E	CY21E	
Per share data (₹)					
Adjusted EPS (Diluted)	19.3	21.2	21.8	25.7	
BV per share	80.6	92.8	108.3	124.1	
DPS	8.4	10.2	6.6	10.3	
Cash Per Share	27.6	8.3	10.6	21.9	
Operating Ratios (%)					
EBIT margins	14.4	13.9	13.1	13.4	
PBT Margins	15.6	13.9	13.0	13.9	
PAT Margin	12.6	11.5	10.5	11.2	
Debtor days	63	64	64	64	
Creditor days	26	26	26	26	
Return Ratios (%)					
RoE	24.4	23.2	20.4	21.0	
RoCE	30.0	26.6	23.6	24.9	
RoIC	48.9	29.5	26.1	28.8	
Valuation Ratios (x)					
P/E	18.9	17.2	16.8	14.2	
EV / Net Sales	2.2	2.0	1.8	1.5	
Market Cap / Sales	2.4	2.0	1.8	1.6	
Solvency Ratios					
Debt / EBITDA	0.0	0.2	0.2	0.1	
Debt / Equity	0.0	0.1	0.1	0.03	
Current Ratio	1.6	1.2	1.3	1.4	
Quick Ratio	1.2	0.9	1.0	1.0	

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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