

March 27, 2020

FY22E: Year of revival...

The ongoing outbreak of Covid-19 continues to impact the economy with no respite in the very near term. As a result, IT companies, which have considerable exposure to global economies like US and Europe, could see an adverse impact from the ongoing crisis. In the near future, IT companies could feel the heat of pricing pressure, revenue loss due to lockdown (in India and many countries globally), client bankruptcy and slower client decision making led by lower discretionary spends. Further, travel restrictions across the globe could also impact new client wins, large deal closures and ability of IT companies to ramp up projects. The implications of this could be more visible on midcaps. Additionally, any scope of vendor consolidation will put midcaps on the losing front as large cap IT players are better placed with considerable exposure to a Fortune 500 client base.

With the situation surrounding Covid-19 spread and control still unclear, the managements of major companies are opting to wait for a few more days to provide a clear indication of the impact of the virus outbreak on the business. Recent commentary from the management of one of the Indian IT companies indicates a likely delay in decision making by clients and increase in receivable days (leading to higher working capital). We believe H1FY21E would be impacted in terms of lower deal wins and revenue loss. Also, new business, which contributes 3-4% of IT revenues could take a hit. Further, on the margin front, a dip in utilisation and pricing pressure are expected to play spoilsport, though lower travel cost, cut in wage hikes and currency benefit could partially provide benefit. From a year's perspective, profitability would take a back seat in FY21E with pressure in the first half of the fiscal (H1FY21E), which pertains to two strong quarters for Indian IT companies. Subsequently, a revival is only expected in FY22E.

Valuation & Outlook

It is difficult for us to accurately predict the slowdown in demand and its impact on the revenue & profitability of IT companies led by Covid-19, oil price fluctuation, banking & capital market, retail segment and travel restrictions. However, we believe there may be a gradual improvement from H2FY21E and revival in FY22E. Recent commentary from Accenture results also indicates the pain would be short-term with a gradual recovery from the second half of the fiscal. However, in the long run, higher offshoring, pick-up in digital business and improving market share will be key drivers of growth. In addition, a US\$2-trillion package would also help many struggling industries in the US, which could, in turn, improve IT spending in the long run. The recent correction in stock prices of IT companies factors in most of the negatives. Hence, as highlighted in our previous report, we continue to maintain our bullish stance on Wipro, Infosys, TechM, L&T Infotech, Sonata Software, Firstsource and Persistent. [\(Please click here for our previous update\)](#)

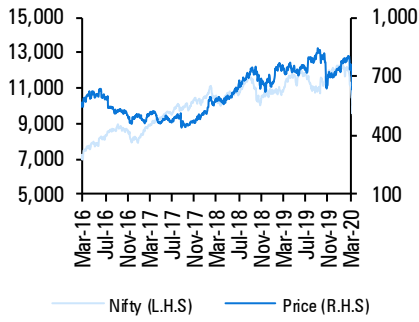
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Research Analysts

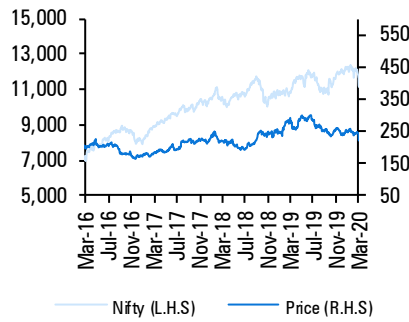
Devang Bhatt
devang.bhatt@icicisecurities.com

Deepti Tayal
deepti.tayal@icicisecurities.com

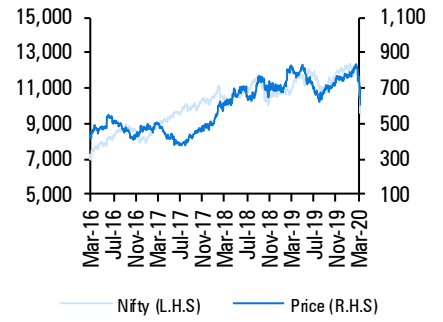
Infosys price chart



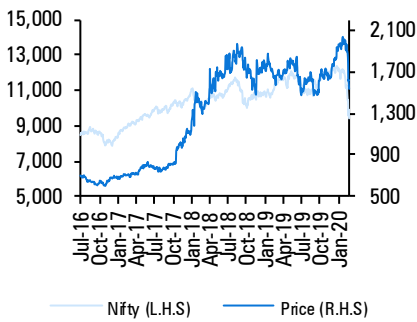
Wipro price chart



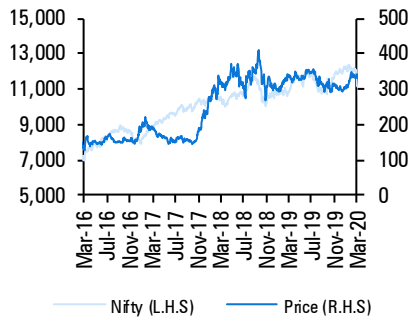
Tech Mahindra price chart



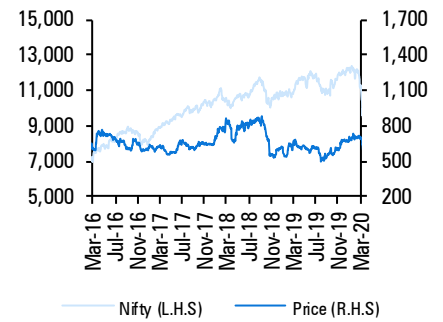
L&T Infotech price chart (Limited history)



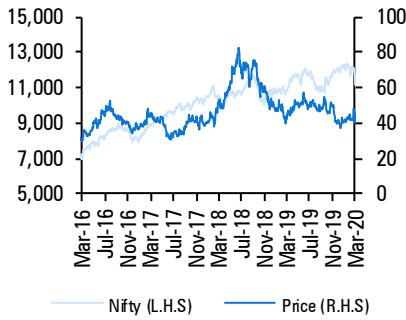
Sonata Software price chart



Persistent price chart



Firstsource price chart



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Sell: <-15%



Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

**ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com**

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