

Growth moderation in near term, pipeline continues to be strong...

About the stock: eClerx Services (eClerx) provides business process management, automation and analytics services.

- It caters to financial services, communications, retail, media, manufacturing, travel and technology companies
- OCF to EBITDA of >80%, debt free and RoCE of >20%

Q3FY23 Results: eClerx reported steady revenue growth in Q3FY23.

- Revenues increased 3.2% QoQ in CC terms
- EBITDA margins marginally declined by ~50 bps QoQ to 29.6%
- Added one client in US\$10+mn client list

What should investors do? eClerx' share price has grown by ~1.5x (adjusted bonus) over the past five years (from ~₹ 1007 in February 2018 to ~₹ 1497 in February 2023).

- We maintain **BUY** rating on the stock

Target Price and Valuation: We value eClerx at ₹ 1,735 i.e. 14x P/E on FY25E EPS.

Key triggers for future price performance:

- Traction in customer care, RPA, analytics & content development, cross sell and up sell to Personiv clients to drive growth
- Lower roll-offs, improving deal wins and revival in growth are expected to drive revenues
- Expect dollar revenues to grow at 11.6% CAGR in FY22-25E

Alternate Stock Idea: Apart from eClerx, in our IT coverage we also like Persistent.

- Key beneficiary of growth in digital technologies and exposure to growth segments like healthcare & BFSI
- BUY with a target price of ₹ 4,920

eClerx

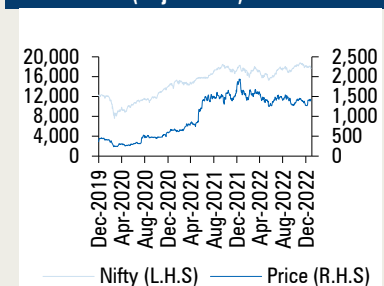
Particulars

Particular	Amount
Market Cap (₹ Crore)	7,440
Total Debt (₹ Crore)	0
Cash & Investments (₹ Crore)	688
EV (₹ Crore)	6,753
52 week H/L	1722/ 1221
Equity capital	49.6
Face value	10.0

Shareholding pattern

	Mar-22	Jun-22	Sep-22	Dec-22
Promoter	53	53	53	53
FII	14	13	12	12
DII	19	20	20	20
Public	13	13	14	15

Price Chart (adj. bonus)



Recent event & key risks

- Guides for lower end of 28-32% band for EBITDA margin in FY23
- **Key Risk:** (i) Lower-than expected revenues, (ii) Lower than expected margins

Research Analyst

Sameer Pardikar
sameer.pardikar@icicisecurities.com
Sujay Chavan
sujay.chavan@icicisecurities.com

Key Financial Summary

Key Financials	FY21	FY22	5 Year CAGR (FY17-22)	FY23E	FY24E	FY25E	3 Year CAGR (FY22-25E)
Net sales	1,564	2,160	10.2%	2,721	2,974	3,203	14.0%
EBITDA	465	697	8.3%	767	857	956	11.1%
EBITDA Margin (%)	29.7	32.3		28.2	28.8	29.8	
Net Profit	283	417	3.3%	518	550	615	13.8%
EPS (₹)	81.3	121.6		104.3	110.8	123.9	
P/E	18.4	12.3		14.4	13.5	12.1	
RoNW (%)	18.8	26.6		29.3	27.8	27.8	
RoCE (%)	23.3	34.9		36.7	35.1	35.3	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter & conference call highlights

- Revenue in CC & US\$ term grew 3.2% QoQ to US\$85.1 million (mn) while in rupee terms, revenue grew 5.6% QoQ to ₹ 686.7 crore
- The company reported that its offshore revenue (81.2% of mix) increased 4.3% QoQ while onshore revenue (19.8% of mix) declined 1.1% QoQ. BPaas (managed services) revenue (26% of mix) increased 3.2% QoQ
- Geography wise Europe (20.4% of mix) reported growth of 5.2% QoQ while US (71.1% of mix) reported growth of 2.2% QoQ
- EBITDA margin declined ~50 bps QoQ to 29.6%. eClerx indicated that margins declined due to higher sub-contractor cost & higher SG&A expenses
- The company reported other income of ₹ 17.8 crore during the quarter and PAT of ₹ 131 crore, up 4.1% QoQ with corresponding PAT margin of 19.1%
- Top five (40% of mix) & Top 10 (59% of mix) customers declined 2.9% & 0.6% QoQ while YoY the growth moderated to 2.6% & 12.6%, respectively. Emerging clients reported strong growth of 9.1% QoQ & 21.5% YoY
- The company during the quarter added one client in US\$10+mn revenue bucket taking the total clients to eight
- eClerx, during the quarter, added 535 net new employees taking the total employee count to 16,804. The company's attrition during the quarter declined 480 bps QoQ to 32.3% while its utilisation improved marginally by 90 bps to 74.7%
- The company added that it is expecting some moderation in the CY23 performance due to softness seen in the near term. eClerx mentioned that it normally has a visibility for the next three to six months and its assessment is for a similar time period while the long term demand outlook is stable. The company added that the demand pipeline remained robust for its offerings but it is seeing slower decision making from clients, which is likely have an impact on revenue conversion. eClerx also indicated that this slowness is broad based and not specific to any client, geography or vertical. The company also indicated there are certain cost pressures the clients are facing. As a result of the same, decision making has been on the slower side
- The company also added that though its offering, especially on the offshore side, can help in automation as well cost savings for clients, the situation could be a little more dampener this time. eClerx also mentioned its growth depends on the US and Europe geographies and since the clients are growing through stress there, the clients are reviewing their spends. eClerx also indicated that on a YTD basis, its revenue growth in FY23 is in the range of 18-19%, which is already a deceleration compared to the same period for FY22 numbers. IT may see some moderation. The company also indicated that earlier it guided for 3-4% QoQ growth for the medium term but that number could be lower at least for the few quarters. eClerx also mentioned that services that it provides in terms of analytics, consulting are valuable to the clients since they have been delivered in the most cost-effective manner. Hence, it does not see quarterly growth to be much below the indicated range of 3-4%
- The company also mentioned it is open to M&A opportunity for growth as valuation correction is visible currently and it is evaluating a few options. eClerx also indicated that its preference for the targeted entity would be on offshore side of the business supporting European & North America geography
- The company indicated that to tackle the visible softness, it is working on: i) it will continue to make investments in capabilities such as KYC, logistics, analytics, marketing automation, etc, ii) it will continue to make investment in talent especially in sales, consulting and onsite capabilities, iii) it will strengthen its delivery team, iv) make some tuck in acquisitions for enhancing capabilities and accelerating growth
- As far as top 10 clients are concerned, the company mentioned that it has seen a cut down of spends by a couple of clients due to high inflation scenario on the onshore side. eClerx also mentioned that impact of this pullback was 1% of revenue for Q3 and it is in active conversation with the clients. It is confident of recouping the same in the next quarter and expects a steady performance from top 10 clients in CY23. The company also said it

is seeing normal roll offs in CY23 and not seeing anything abnormal at this moment. The impact of the same is already baked in the outlook

- The company indicated that SG&A expenses for the quarter were higher partly due to Personiv payout, which falls under SG&A expenses. eClerx indicated that it is largely done with the payout for the year including ₹ 21 crore paid in Q1 and it does not anticipate any major payout in Q4 except some top up, if required. The company indicated that it is likely to be at lower end of their EBITDA margin guidance of 28-32% in FY23. eClerx also indicated that other income for Q3 also includes ₹ 5.46 crore of one-time income coming from re-assessment of lease agreement for its offices in Airoli (where the company had offices in two buildings, now it has vacated the old building and taken additional two floors apart from existing three floors in the new building). The company also mentioned that margins in Q4 will be higher despite i) one-time other income gain going away in Q4 (the company include other income in EBITDA margin calculation); ii) some increase in marketing and travel expenses due to the tailwinds of: i) lower sub-contractor's costs, which was elevated in Q3 due to subcontractors hired in the quarter for the Europe region due to demand in high luxury segment ii) utilisation improvement. The company also indicated that it does not see any major benefit from rupee depreciation since currency realisation is based on the hedge rate and not spot rate. The company also added that current SEZ regulation are valid till December 2023. Currently, 45% of its employees are working from office. Any change in this regulation i.e. more working from office is likely to increase housekeeping and facility expenses

Exhibit 1: P&L

	Q3FY23	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	Comments
Revenue	686.7	559.2	22.8	650.3	5.6	Revenue grew by 3.2% QoQ in CC & dollar terms
Employee expenses	360.2	273.8	31.5	346.3	4.0	
Gross Profit	326.5	285.3	14.4	304.0	7.4	
Gross margin (%)	47.5	51.0	-348 bps	46.7	80 bps	
SG&A expenses	135.9	107.5	26.4	122.6	10.8	
EBITDA	208.4	182.1	14.4	202.2	3.0	
EBITDA Margin (%)	29.6	32.3	-274 bps	30.1	-55 bps	Margin impacted due to higher sub-contractor cost & higher SG&A expenses
Depreciation & amortisation	29.9	26.4	13.2	27.4	9.2	
EBIT	178.5	155.7	14.6	174.9	2.1	
EBIT Margin (%)	26.0	27.8	-185 bps	26.9	-90 bps	
Other income (less interest)	17.8	4.3	312.5	20.9	(14.8)	Other income include one time gain on re-assessment of lease agreement
PBT	173.1	144.9	19.5	169.7	2.0	
Tax paid	41.9	38.4	9.4	43.8	(4.1)	
PAT	131.0	106.6	22.9	125.8	4.1	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

₹ Crore)	FY23E			FY24E			FY25E			Comments
	Old	New	% Change	Old	New	% Change	Old	New	% Change	
Revenue	2,654	2,721	2.5	2,952	2,974	0.7	3,238	3,203	(1.1)	Re-aligning numbers on 9M performance
EBITDA	748	767	2.6	850	857	0.8	950	956	0.6	
EBITDA Margin (%)	28.2	28.2	2 bps	28.8	28.8	0 bps	29.3	29.8	49 bps	We are baking in moderation of attrition and improvement in utilisation which will aid margin expansion
PAT	492	518	5.2	523	550	5.2	585	615	5.3	
EPS (₹)	99.1	104.3	5.2	105.3	110.8	5.2	117.7	123.9	5.3	

Source: Company, ICICI Direct Research

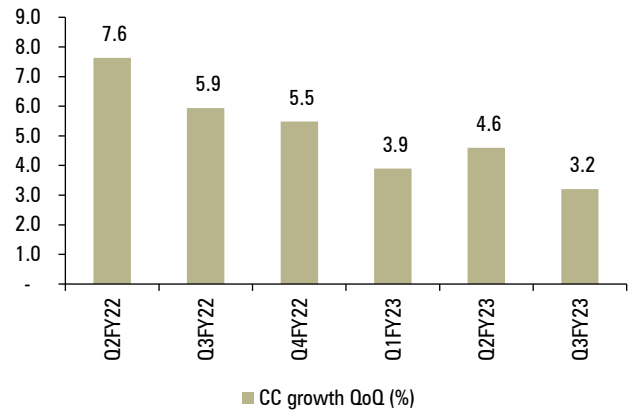
Key Metrics

Exhibit 3: Dollar QoQ revenue growth trend



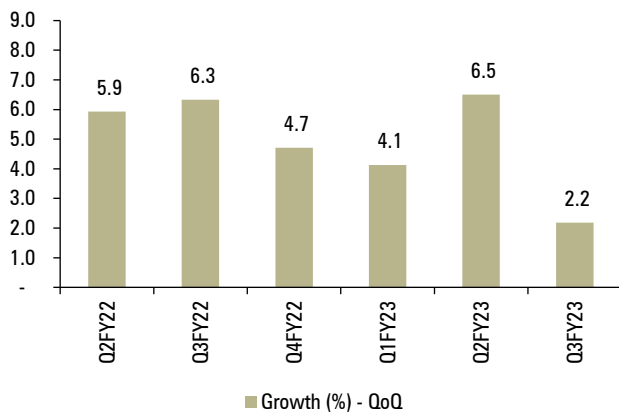
Source: Company, ICICI Direct Research

Exhibit 4: CC QoQ growth trend



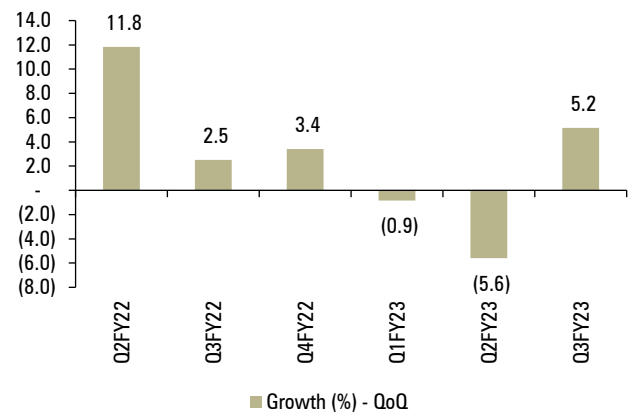
Source: Company, ICICI Direct Research

Exhibit 5: US region growth moderated in Q3



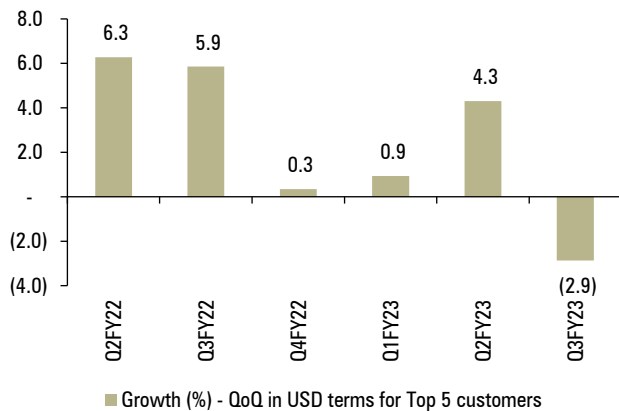
Source: Company, ICICI Direct Research

Exhibit 6: While Europe rebounds



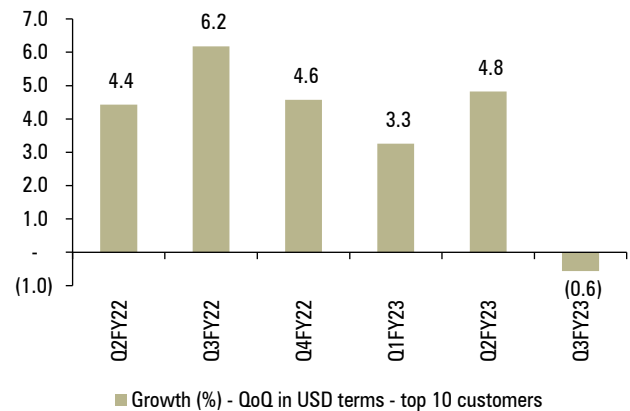
Source: Company, ICICI Direct Research

Exhibit 7: Couple of top clients cut down spend



Source: Company, ICICI Direct Research

Exhibit 8: Top 10 client growth trend



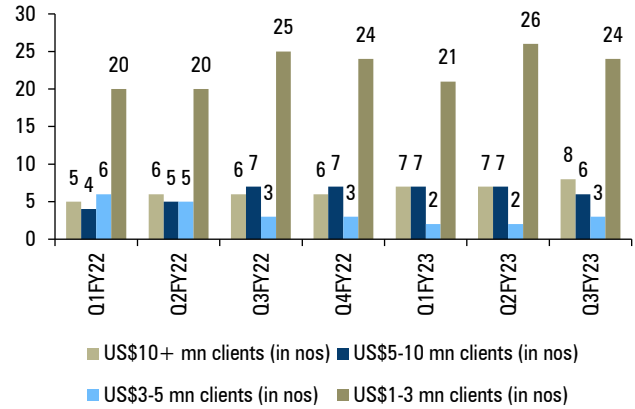
Source: Company, ICICI Direct Research

Exhibit 9: Total clients trend



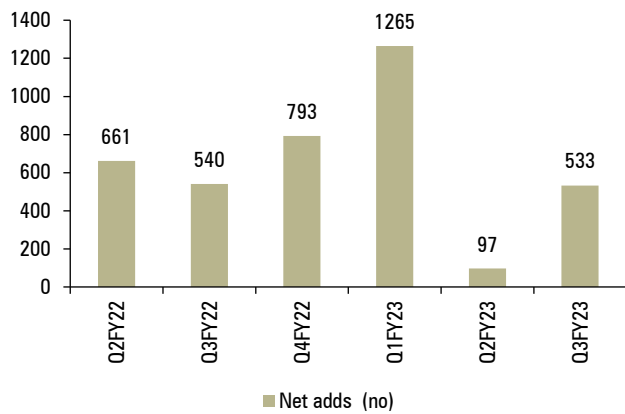
Source: Company, ICICI Direct Research

Exhibit 10: 1mn+ client count down by 1 QoQ



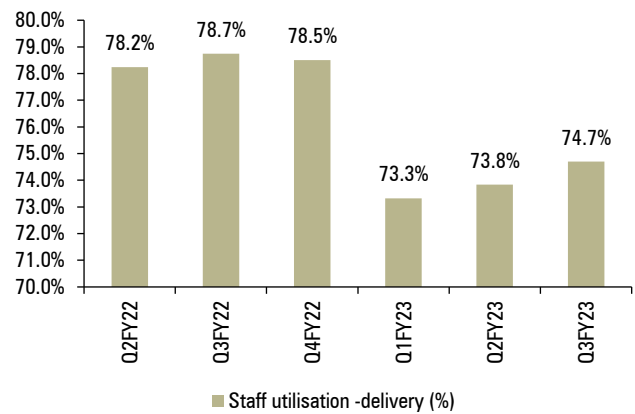
Source: Company, ICICI Direct Research

Exhibit 11: Net additions pick up in Q3



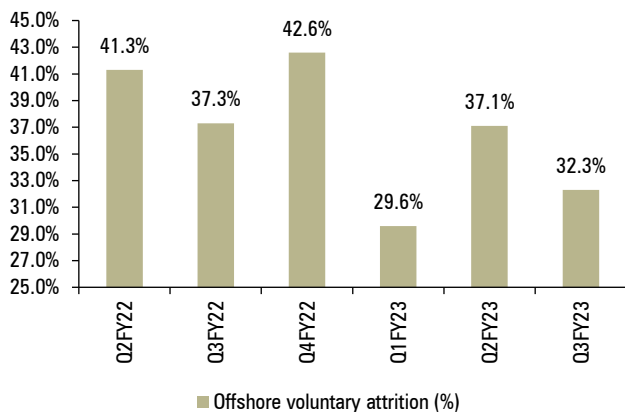
Source: Company, ICICI Direct Research

Exhibit 12: Utilisation gradually improving



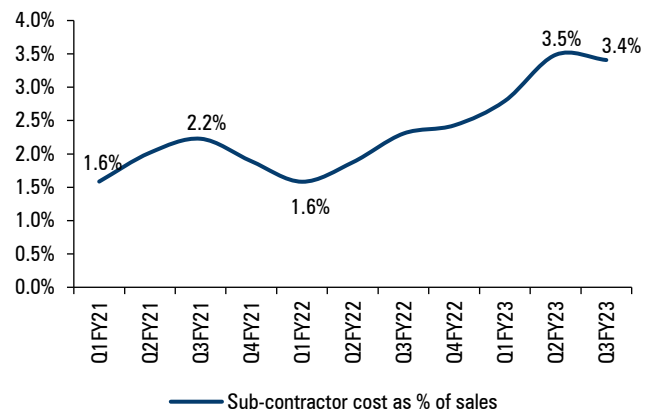
Source: Company, ICICI Direct Research

Exhibit 13: Attrition declines in Q3



Source: Company, ICICI Direct Research

Exhibit 14: Sub-contractor cost still elevated



Source: Company, ICICI Direct Research

Financial summary

Exhibit 15: Profit and loss statement					₹ crore
	FY22	FY23E	FY24E	FY25E	
Total Revenues	2,160	2,721	2,974	3,203	
Growth (%)	38.1	25.9	9.3	7.7	
Employee expenses	1,079	1,394	1,496	1,582	
Other Expenditure	409	494	580	626	
EBITDA	697	767	857	956	
Growth (%)	50.0	10.1	11.6	11.6	
Depreciation	103	111	132	142	
Other Income	24	66	41	40	
Interest expense	22	22	22	22	
PBT before Exceptional Items	560	700	744	832	
Growth (%)	47.2	25.0	6.2	11.8	
Tax	143	182	193	216	
PAT before Exceptional Items	418	518	551	615	
Exceptional items	-	-	-	-	
PAT before MI	418	518	551	615	
Minority Int & Pft. from associate	0	0	0	-	
PAT	417	518	550	615	
Growth (%)	47.6	24.1	6.2	11.8	
EPS	121.6	104.3	110.8	123.9	
EPS (Growth %)	49.6	(14.2)	6.2	11.8	

Source: Company, ICICI Direct Research

Exhibit 16: Cash flow statement					₹ crore
	FY22	FY23E	FY24E	FY25E	
Net profit before Tax	560	700	744	832	
Depreciation	103	111	132	142	
(inc)/dec in Current Assets	(51)	561	263	(211)	
(inc)/dec in current Liabilities	(164)	(182)	(193)	(216)	
CF from operations	448	1,191	945	547	
Other Investments	108	-	-	-	
Other income	4	66	41	40	
(Purchase)/Sale of Fixed Asset	(61)	(61)	(67)	(73)	
CF from investing Activiti	38	5	(27)	(33)	
Inc / (Dec) in Equity Capital	(355)	(0)	(0)	(0)	
Dividend & Dividend tax	(3)	(319)	(338)	(378)	
Interest Paid on Loans	(58)	(0)	-	-	
CF from Financial Activiti	(416)	(359)	(379)	(418)	
Exchange rate differences	1	-	-	-	
Opening cash balance	491	562	1,399	1,939	
Other adjustments	-	-	-	-	
Closing cash	562	1,399	1,939	2,034	

Source: Company, ICICI Direct Research;

Exhibit 17: Balance sheet					₹ crore
	FY22	FY23E	FY24E	FY25E	
Equity	33	50	50	50	
Reserves & Surplus	1,534	1,717	1,929	2,166	
Networth	1,568	1,767	1,979	2,216	
Minority Interest	1	1	1	1	
Loans	0	0	0	0	
Other liabilities	199	199	199	199	
Source of funds	1,768	1,968	2,179	2,416	
Gross Block	531	632	739	846	
Acc.dep	319	430	562	705	
Net Block	212	201	177	142	
CWIP	2	2	2	2	
Other Intangible assets	126	126	126	126	
Other non current assets	45	137	149	159	
Investments	194	194	194	194	
Goodwill	375	375	375	375	
Debtors	329	615	428	697	
Cash & Cash equivalents	494	1,399	1,939	2,034	
Loans and advances	-	-	-	-	
Other current assets	293	634	678	714	
Trade payables	17	91	100	108	
Current liabilities	156	854	943	1,017	
Provisions	129	703	776	837	
Application of funds	1,768	1,967	2,179	2,416	

Source: Company, ICICI Direct Research

Exhibit 18: Key ratios					₹ crore
	FY22	FY23E	FY24E	FY25E	
Per share data (₹)					
EPS	121.6	104.3	110.8	123.9	
Cash EPS	151.6	126.7	137.4	152.6	
BV	456.6	355.8	398.4	446.1	
DPS	1.0	64.1	68.1	76.2	
Cash Per Share	143.8	281.7	390.4	409.6	
Operating Ratios (%)					
EBITDA Margin	32.3	28.2	28.8	29.8	
PBT Margin	25.9	25.7	25.0	26.0	
PAT Margin	19.3	19.0	18.5	19.2	
Debtor days	56	82	53	79	
Creditor days	3	12	12	12	
Return Ratios (%)					
RoE	26.6	29.3	27.8	27.8	
RoCE	34.9	36.7	35.1	35.3	
RoIC	55.0	148.8	642.3	326.2	
Valuation Ratios (x)					
P/E	12.3	14.4	13.5	12.1	
EV / EBITDA	9.7	7.6	6.2	5.5	
EV / Net Sales	3.1	2.1	1.8	1.6	
Market Cap / Sales	3.4	2.7	2.5	2.3	
Price to Book Value	3.3	4.2	3.8	3.4	
Solvency Ratios					
Debt/EBITDA	0.0	0.0	0.0	0.0	
Debt / Equity	0.0	0.0	0.0	0.0	
Current Ratio	2.1	0.8	0.6	0.7	
Quick Ratio	2.1	0.8	0.6	0.7	

Source: Company, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

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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