

Technology

Jun'20 Results Preview

Looking forward to normalization

	CMP(₹)	3M ret (%)	Yearly (%)
Index Returns			
Nifty	10,800	23.4	(6.5)
CNX IT	15,785	26.4	3.5
Large-Caps			
TCS	2,270	33.1	6.4
INFO	794	25.7	11.0
WPRO	225	16.6	(15.3)
HCLT	592	27.9	16.1
TECHM	587	5.0	(13.2)
Mid-Caps			
MTCL	982	34.2	27.1
MPHL	921	36.8	(2.3)
HEXW	335	34.3	(5.8)
ECLX	474	31.4	(30.1)
NITEC	1,513	37.4	15.1
CYL	270	23.3	(49.7)
PSYS	678	32.7	10.2

1QFY21E preview - We expect Indian IT companies to report sequential revenue decline in the range of -5% to -8% in cc terms for top-5 IT companies and -5% to -14% for mid-caps with a cross currency headwind of 20-80bps. The decline will be largely led by weakness in retail, banking, energy and ER&D vertical. Larger IT services companies such as Infosys and TCS are likely to report better results as the base is much more diversified with average ~5% decline. TechM will report worst set of numbers with 8% QoQ decline impacted by high portion of discretionary work around network integration and 5G related spend remains weak as well.

Spending cuts dent TechM/Wipro/Mid-caps sales more than Infosys/TCS. Larger IT services companies such as Infosys and TCS are likely to report better results as the base is much more diversified with average ~5% decline. TechM will report worst set of numbers with ~8% QoQ decline impacted by high portion of discretionary work around network integration and 5G related spend remains weak as well. Mid-caps are also likely to witness higher impact on greater proportion of discretionary work and high client concentration.

Margins unlikely to fall meaningfully on high variable cost: Indian IT services industry has a high variable proportion in total cost which allows them to adjust quickly to any immediate demand shocks, given nearly 60-70% of the costs are related to employees/quarterly performance bonuses. It's easy for them to reduce employee cost and adjust to any near-term demand slowdown. In addition, reduction in subcontractor cost and absence of travel expenses because of the lock-down are other levers which will help companies offset lower utilization and revenue decline impact. INR depreciation against USD by 4% during the quarter will also help margins.

Maintain our preference towards large caps over mid-caps: Nifty IT index has rallied 23% in past 3 months on the expectation that FY22E revenue growth will be as high as double digits on the back of spending on core transformation programs, vendor consolidation & pickup in IT spending. Infosys/ HCL Technologies remain our Top picks.

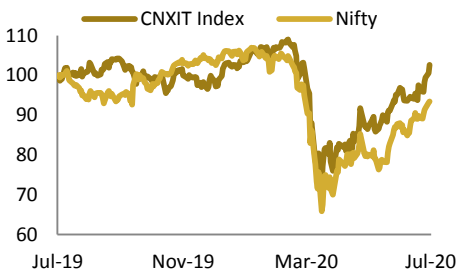
	Rating	FDEPS (₹)	
		FY21E	FY22E
TCS	Hold	83.0	90.6
INFO	Buy	37.3	41.1
WPRO	Hold	15.7	17.1
HCLT	Buy	39.2	43.3
TECHM	Buy	41.5	48.4
MTCL	Hold	47.6	55.1
MPHL	Buy	58.0	65.7
HEXW	Hold	19.9	22.8
ECLX	Buy	46.2	55.4
NITEC	Buy	75.0	86.5
CYL	Buy	24.3	28.8
PSYS	Hold	42.6	47.6

Exhibit 1: Key Financials for quarter ending Jun'20

(₹ mn)	Revenue	QoQ (%)	EBITDA	QoQ (%)	PAT	QoQ (%)
TCS	388,627	(2.7)	94,721	(5.5)	77,593	(3.6)
INFO	230,406	(1.0)	47,986	(2.6)	39,502	(8.9)
WPRO	149,787	(4.7)	23,129	(7.5)	22,287	(5.0)
HCLT	179,659	(3.4)	34,296	(11.6)	26,832	(14.9)
TECHM	89,350	(5.9)	7,659	(19.3)	7,010	(12.8)
MTCL	19,547	(4.7)	2,597	(14.4)	1,934	(6.2)
MPHL	22,958	(2.1)	3,500	(8.6)	2,833	(19.8)
HEXW	15,015	(2.6)	1,594	(16.0)	1,298	(25.8)
ECLX	3,239	(7.7)	441	(25.5)	353	(36.3)
NITEC	11,060	(0.3)	1,354	(13.0)	1,107	(13.6)
CYL	9,721	(9.5)	372	(58.8)	575	(23.6)
PSYS	9,463	2.2	792	(11.8)	711	(15.1)

Source: Trust

Nifty vs CNX IT



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Exhibit 2: Results preview for quarter ending June 2020

₹ Mn		Jun'20E	Jun'19	YoY (%)	Mar'20	QoQ (%)	Comments
TCS	Revenues (US\$)	5,127	5,485	(6.5)	5,444	(5.8)	Expect a cc revenue decline of 5.2% and cc headwind of 55 bps - Retail, Autos, T&T spending cuts to impact hard.
	Revenues	388,627	381,720	1.8	399,460	(2.7)	Bookings to be under pressure, though Phoenix Group US\$1.5 bn expanded deal will help.
	EBIT	94,721	92,200	2.7	100,250	(5.5)	Expect margin decline of 60bps, Margin headwinds are from lower utilization rate helped by INR tailwind.
	PAT	77,593	81,310	(4.6)	80,490	(3.6)	Will lookout for commentary on demand, pricing, WFH strategy and receivables.
Infosys	Revenues (US\$)	3,040	3,131	(2.9)	3,197	(4.9)	Expect a cc revenue decline of 4.6% and cc headwind of 35 bps - Retail, Autos, T&T spending cuts to impact hard.
	Revenues	230,406	218,030	5.7	232,670	(1.0)	Expect margin decline of 30bps, Margin headwinds are from lower utilization rate helped by INR tailwind.
	EBIT	47,986	44,710	7.3	49,270	(2.6)	Infosys may not resume annual guidance due to potential risks from second wave of lockdowns.
	PAT	39,502	38,020	3.9	43,350	(8.9)	Will lookout for commentary on demand, pricing, WFH strategy and receivables.
Wipro	Revenues (US\$) - IT	1,918	2,039	(5.9)	2,074	(7.5)	Expect a cc revenue decline of 7% and cc headwind of 55 bps. Decline will be on account of demand & supply side.
	Revenues	149,787	147,161	1.8	157,110	(4.7)	Capital return policy to be seen as WPRO has done last Buyback in Sept'19.
	EBIT	23,129	23,176	(0.2)	25,001	(7.5)	Expect margin decline of 40bps, Margin headwinds are from lower utilization rate helped by INR tailwind.
	PAT	22,287	24,021	(7.2)	23,451	(5.0)	Will lookout for update in the turnaround strategy, new account growth, New CEOs strategy and receivables.
HCL Tech	Revenues (US\$)	2,370	2,364	0.3	2,543	(6.8)	Expect QoQ revenue decline of 6.5% and cc headwind of 30 bps - ER&D project cancellations to make impact.
	Revenues	179,659	164,250	9.4	185,900	(3.4)	Expect margin decline of 160bps - demand & supply side challenges, lower pricing and utilization.
	EBIT	34,296	28,050	22.3	38,810	(11.6)	Company may retain its commentary of stabilization in September quarter and growth in 2HFY21.
	PAT	26,832	22,200	20.9	31,530	(14.9)	Will lookout for commentary on demand outlook, competitive intensity in IMS and profitability & WFH strategy.
Tech Mahindra	Revenues (US\$)	1,179	1,247	(5.5)	1,295	(8.9)	Expect cc revenue decline of 8.1% QoQ and cc headwind of 80 bps
	Revenues	89,350	86,530	3.3	94,902	(5.9)	Expect only 100bps contraction in margins aided by lower subcontracting cost, travel cost and INR depreciation.
	EBIT	7,659	9,928	(22.9)	9,496	(19.3)	Net profit decline will be sharper due to negligible Fx gains as compared to gains earlier.
	PAT	7,010	9,593	(26.9)	8,039	(12.8)	Update on outlook of tech spending around telecom and estimated timelines for pickup in 5G investments.
Mphasis	Revenues (US\$)	303	297	2.0	320	(5.3)	Expect DXC/HP channel continue to remain weak. Direct Core will be relatively stable helped by strategic accounts.
	Revenues	22,958	20,626	11.3	23,462	(2.1)	Expect margins to reduce by 100bps in the quarter
	EBIT	3,500	3,193	9.6	3,831	(8.6)	4QFY20 had low tax rate of 14.9% due to one-time reversal.
	PAT	2,833	2,647	7.0	3,532	(19.8)	Lookout for commentary on - HP Enterprise, HP Non-Enterprise and the Direct Channel ramp-up going forward.
Hexaware	Revenues (US\$)	198	189	5.1	211	(5.9)	Expect revenue decline of 5.5% in cc terms
	Revenues	15,015	13,083	14.8	15,418	(2.6)	Expect margins to drop by 150bps led by lower utilization; while INR depreciation, absence of travel cost to help.
	EBIT	1,594	1,953	(18.4)	1,898	(16.0)	Update around Baring offer to take the company private.
	PAT	1,298	1,513	(14.2)	1,750	(25.8)	Management commentary on (1) progress in IMS vertical, (2) deal wins and demand outlook.



₹ Mn		Jun'20E	Jun'19	YoY (%)	Mar'20	QoQ (%)	Comments
MindTree	Revenues (US\$)	258	264	(2.4)	278	(7.4)	Expect sequential cc decline of 7.1% with a cross currency headwind of 35 bps
	Revenues	19,547	18,342	6.6	20,505	(4.7)	Expect margins to drop by 30bps QoQ (excluding one-off items in 4QFY20).
	EBIT	2,597	1,172	121.6	3,033	(14.4)	We expect healthy deal pipeline led by CMT and CPG verticals.
	PAT	1,934	927	108.7	2,062	(6.2)	We would lookout for 1) Growth outlook of top client, 2) margin outlook, 3) management strategy for next 2 years.
NIIT Tech	Revenues (US\$)	146	138	5.7	155	(5.7)	Expect cc revenue decline of 5.2% QoQ - expect travel vertical to get most impacted.
	Revenues	11,060	9,597	15.2	11,093	(0.3)	Expect EBIT margins to decline by 170bp impacted by lower utilization, revenue decline
	EBIT	1,354	1,005	34.7	1,555	(13.0)	Banking vertical likely to report growth in Q1.
	PAT	1,107	891	24.3	1,281	(13.6)	Commentary on demand and deals wins. Update on outlook for travel and BFSI vertical would be the key.
eClerx	Revenues (US\$)	43	51	(16.1)	48	(10.4)	Expect cc revenue decline of 10% QoQ and headwind of 40 bps in line with management commentary of a tough qtr.
	Revenues	3,239	3,547	(8.7)	3,509	(7.7)	Expect EBIT margins to come off by 250bps due to revenue pressure despite benefit from INR depreciation
	EBIT	441	476	(7.4)	592	(25.5)	Margins are also impacted by WFH enablement costs during the quarter.
	PAT	353	398	(11.3)	554	(36.3)	We will keep a look on 1) recovery in segments like CLX and US onshore business, (2) outlook on revenues/margins.
Cyient	Revenues (US\$)	128	157	(18.1)	149	(14.1)	Cyient's USD rev is estimated to decline 14% QoQ led by fall in services/DLM revenue by 12/16% QoQ.
	Revenues	9,721	10,890	(10.7)	10,736	(9.5)	Expect EBIT margins to come off by 400bps due to revenue pressure despite benefit from INR depreciation
	EBIT	372	1,003	(62.9)	904	(58.8)	Outlook for A&D vertical in a scenario where airlines globally are facing challenges.
	PAT	575	903	(36.3)	753	(23.6)	Commentary on deal pipeline, demand outlook and margin improvement needs to be seen.
Persistent Systems	Revenues (US\$)	125	120	4.4	127	(1.7)	Expect revenue decline of 1.4% in cc terms and cross currency impact of 30bps
	Revenues	9,463	8,321	13.7	9,264	2.2	Expect EBIT margins to come off by 130bps due to pressure on IP led business.
	EBIT	792	916	(13.5)	897	(11.8)	Economic impact on key verticals - BFSI, Healthcare & LS and Hi-tech & Industrial, impact on Salesforce services
	PAT	711	825	(13.8)	838	(15.1)	Impact of pricing discount/payment terms changes from key accounts; risk of financial stability of customer portfolio

Source: Company, Trust

**Exhibit 3: Depreciation of currencies against the US Dollar**

	US\$/£	US\$/Euro	¥/US\$	US\$/AU\$	Rs/US\$
31 Mar'20	1.26	1.10	109.8	0.64	73.1
30 Jun'20	1.24	1.10	107.3	0.67	75.8
% change (QoQ)	(1.8)	(0.1)	(2.3)	(3.3)	(4.0)

Source: Bloomberg

Exhibit 4: Appreciation of the Rupee against other currencies

	INR/GBP	INR/Euro	Yen/INR	INR/AUD
31 Mar'20	92.4	79.9	1.5	47.0
30 Jun'20	93.7	83.7	1.4	50.4
% change (QoQ)	(1.5)	(4.2)	(5.0)	(6.9)

Source: Bloomberg

Exhibit 5: Valuation details

	Rating	PER (x)		EV/EBITDA (x)		RoE (%)	
		FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
TCS	Hold	27.3	25.1	21.6	18.9	32.8	30.1
INFO	Buy	21.3	19.3	15.2	13.5	23.1	23.0
WPRO	Hold	14.3	13.2	10.4	8.5	15.0	14.2
HCLT	Buy	15.1	13.7	8.8	7.5	19.1	18.1
TECHM	Buy	14.1	12.1	6.2	5.0	14.1	15.1
MTCL	Hold	20.6	17.8	11.1	9.4	22.8	22.6
MPHL	Buy	15.9	14.0	12.0	10.7	17.9	18.9
HEXW	Hold	16.8	14.7	10.7	7.7	21.0	21.3
ECLX	Buy	10.3	8.6	2.4	1.6	11.7	12.3
NITEC	Buy	20.2	17.5	10.6	8.9	18.3	19.0
CYL	Buy	11.1	9.4	5.7	4.7	9.7	10.7
PSYS	Hold	15.9	14.2	10.1	8.6	13.1	13.4

Source: Bloomberg

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