

Zensar Technologies Ltd

OUT PERFORMER

Sector: IT /Mid-Cap | Earnings Update – 2QFY22

28 October 2021

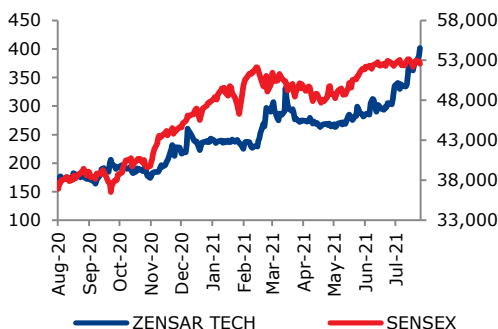
Background: Zensar is a leading digital solutions and technology services company that specialises in partnering with global organizations across industries on their Digital Transformation journey. A technology partner of choice, backed by strong track-record of innovation; credible investment in Digital solutions; assertion of commitment to client's success, Zensar's comprehensive range of digital and technology services and solutions enable its customers to achieve new thresholds of business performance. Zensar, with its experience in delivering excellence and superior client satisfaction through myriad technology solutions, is uniquely positioned to help them surpass challenges around running their existing business most efficiently, helping in their legacy transformation, and planning for business expansion and growth through innovative and digital ways.

| | |
|--------------------------|------------------|
| Sensex | 61,143 |
| Nifty | 18,210 |
| Price | ₹ 468 |
| Target Price (12 months) | ₹ 505 |
| Recommendation | OUT PERFORMER |
| 52 Week High/Low | ₹ 587/172 |
| Bloomberg / Reuters | ZENT IN /ZENT.BO |
| Equity (shares in mn) | 225.9 |
| Mkt. Cap in bn | ₹ 105.7/ \$ 1.4 |
| Avg. Daily Vol. ('000) | 1,584.4 |
| Avg. Daily Vol. (mn) | ₹ 741.9 /\$ 9.9 |

| Shareholding | Sep-20 | Jun-21 | Sep-21 |
|--------------------------------|--------|--------|--------|
| Promoters (%) | 49.2 | 49.2 | 49.1 |
| FII (%) | 16.0 | 17.1 | 15.8 |
| DII (%) | 24.5 | 21.1 | 21.0 |
| Others (%) | 10.2 | 12.6 | 14.2 |
| Pledge (% of promoter holding) | 0.0 | 0.0 | 0.0 |

| Valuation Summary (₹ bn) | | | |
|--------------------------|------|-------|-------|
| Y/E March | 2021 | 2022E | 2023E |
| Revenue | 37.8 | 41.1 | 46.1 |
| EBITDA | 6.8 | 7.0 | 8.2 |
| PAT | 3.0 | 4.2 | 5.1 |
| EPS | 13.4 | 18.6 | 22.6 |
| % growth | 13.4 | 39.0 | 21.8 |
| P/E | 35.0 | 25.2 | 20.7 |
| P/ BV | 4.5 | 4.5 | 3.8 |
| EV/EBITDA | 12.2 | 11.9 | 10.2 |
| EV/Sales | 2.2 | 2.0 | 1.8 |
| Div Yield (%) | 0.6 | 0.9 | 1.1 |
| ROE (%) | 13.7 | 17.9 | 19.9 |

| Performance(%) | 1M | 3M | 12M |
|----------------|-------|-----|-------|
| ZENSAR TECH | (3.7) | 5.4 | 155.9 |
| SENSEX | 1.8 | 8.9 | 53.2 |



Strong quarter characterized by broad based organic growth and robust deal wins; PAT was propped up by higher other income; Management retains guidance of high teen digit operating margins going forward

- Zensar Tech reported robust revenue growth of 12.3% QoQ in cc terms to US\$141.9mn in 2QFY22 driven by strong growth across business verticals. The growth was primarily led by BFS (+20.9% QoQ USD) followed by Emerging (+14.6% QoQ USD). Organic growth >5% QoQ for two consecutive quarters shows that the new strategy is on track.
- During the quarter the company won six significant deals and reported robust deal TCV of US\$187.5mn (94%/7% QoQ/YoY). The largest deal worth US\$122mn is with City of San Diego smart city project and the management took a conservative stand by reporting only half of its maximum deal value in this quarter.
- Among business verticals, Manufacturing vertical reported 6%/1.5% QoQ/YoY USD after muted performance in the last couple of quarters indicating recovery. The company has setup a dedicated team to focus on acquiring new logos for Hi-Tech, Manufacturing and Emerging verticals. This strategy is expected to payoff in these verticals in the coming quarters.
- From a geographic perspective the topline growth in the quarter was strong across all regions. US (11.9% QoQ USD), EMEA (11.6% QoQ USD) and Africa (10% QoQ USD).
- In 2QFY22 EBITDA margins declined 308 bps sequentially to 15.3%. The decline in margins was on account of higher than normal wage hikes and increased hiring costs. However this was marginally offset by better utilization (83.3%, +290bps QoQ) and increased offshore revenue mix (42.5%, +80bps QoQ). The management expects margins to reach high teen digits levels in the next 5 quarters.
- The company has ramped up fresh hiring and intends to reduce time to billability of freshers. Strong net headcount additions of 863 QoQ (9% QOQ) in 2QFY22 resulted in an increase in headcount by 20% YoY. Meanwhile LTM Attrition increased to 23.2% (+510bps QoQ).
- Zensar has put in place strategies to manage supply side challenges such as: Upskilling and fast tracking career paths existing talent, aggressive hiring (plans to add 5x 1HFY22 freshers in 2HFY22), and rolled out hiring than normal wage hikes in July 2021.

Valuation: The Green shoots of recovery are quiet visible with the change in strategy by the company's new CEO. The topline is expected to continue its robust growth into 2HFY22 driven by recovery in clients' business. The company is investing in its sales force and offshoring which is expected to be margin accretive in the medium term. The management remains optimistic of maintaining margins in high double digits which is a positive. We believe Zensar with its proven business structure, diversified product mix and long term deal pipeline will benefit from current up cycle in technology. At CMP, the stock is trading at a P/E of 25.2x/20.7x over F22/23 EPS. We revise our target price on the stock to ₹505 and upgrade our rating on the stock to OUT PERFORMER (Earlier: MARKET PERFORMER).

Risks: Postponement/ suspension of deal pipeline, slowdown in cloud, FS and retail segment.

Results Summary 2QFY22

| Y/E March (₹ mn) | 2QFY22 | 2QFY21 | YoY Growth | 1QFY22 | QoQ Growth |
|-------------------|--------|--------|------------|--------|------------|
| Revenue | 10,506 | 9,795 | 7.3% | 9,368 | 12.1% |
| EBITDA | 1,612 | 1,842 | -12.5% | 1,726 | -6.6% |
| Depreciation | 468 | 432 | 8.3% | 426 | 9.9% |
| Other Income | 229 | -29 | NA | 184 | 24.5% |
| PBT | 1,286 | 1,249 | 3.0% | 1,395 | -7.8% |
| Tax | 328 | 329 | -0.2% | 369 | -11.1% |
| PAT | 958 | 920 | 4.1% | 1,026 | -6.6% |
| EBIDTA Margin (%) | 15.3 | 18.8 | | 18.4 | |
| Tax Incidence (%) | 25.5 | 26.3 | | 26.5 | |
| PAT Margin (%) | 9.1 | 9.4 | | 11.0 | |

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| Disclosure of Interest Statement | Update |
|--------------------------------------------|--------|
| Analyst holding in the stock | No |
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| | | |

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MARKET PERFORMER: The stock's total return is expected to be between -5% to +5% over the next 12 months.

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SELL: The stock's total return is expected to more than -15% over the next 12 months.

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