AXIS SECURITIES

Result Update
10th Aug 2022

Zensar Technologies (ZENSAR)
IT Services

BUY
Target Price
255

Revenue Growth in-line albeit With Below-Estimates Margins; Superior Outlook

Zensar Q1FY23 performance beat our expectations on the revenue front. Revenue for the quarter stood at Rs 1,203 Cr, up 4.3% QoQ and 28.5% YoY. However, the company's Operating Margins reported a de-growth of 3% and stood at 11.3%. Net income de-grew 42.2% QoQ and stood at Rs 75 Cr. The company has reported strong recovery from its existing clients and its new clients' addition helped to gain traction. Total deal wins for the quarter remained strong at $165.6 Mn, which reported a robust growth of 32% QoQ. Zensar continues to build competency and scale in the focused strategic growth opportunities (SGOs) such as Experience Services, Advanced Engineering, and Data Analytics in addition to core services. Zensar management expects to report strong revenue growth momentum in the next 3-7 quarters owing to better deal pipeline and execution strategies. Its clients continue to see it as a reliable and future-driven partner as it brings in world-class processes and learnings.

We recommend a BUY on Zensar, aided by strong revenue growth momentum and better recovery. We assign a 10x P/E multiple to its FY24E earnings of Rs 24.3 per share to arrive at a TP of Rs 255/share, implying an upside of 12% from the CMP.

Strong vertical performance

On the vertical front, the HI-Tech vertical de-grew 0.8% QoQ owing to strong demand across geographies. Banking grew by 10.6% QoQ, Insurance by 5.6% QoQ, and Consumer Services de-grew by 0.4% QoQ. The Manufacturing segment also witnessed strong growth of 3.3% QoQ. Emerging services reported better recovery at 5.1% growth QoQ.

On a geographical front, North America (70% of revenue) exhibited a robust recovery with 2.5% QoQ growth, Europe (11% of revenue) also showcased a strong growth of 3.5% QoQ, Africa region (11% of the revenue) showed strong growth of 6% QoQ. Zensar management is expecting robust demand backed by better deal wins across geographies.

Outlook & Valuation

We believe Zensar Technology has been witnessing strong demand across key verticals such as Hi-tech and Banking backed by healthy deal wins spread across verticals. While higher onsite expenses and rising employee expenses may impact its operating margins temporarily, they will likely expand with strong volume growth moving forward. **We recommend a BUY on Zensar, aided by strong revenue growth momentum and better recovery. We assign a 10x P/E multiple to its FY24E earnings of Rs 24.25 per share to arrive at a TP of Rs 255/share, implying an upside of 12% from the CMP.**

Key Financials (Consolidated)

(Rs Cr)	FY21E	FY22E	FY23E	FY24E
Net Sales	3,781	4,244	5,044	5,851
EBITDA	1,208	678	792	919
Net Profit	303	416	469	550
EPS (Rs)	13.31	17.63	20.86	24.45
PER (x)	30.43	22.98	19.41	16.57
EV/EBITDA (x)	7.5	13.6	11.8	10.3
P/BV (x)	3.8	3.5	3.1	2.8
ROE (%)	18%	19%	20%	21%

Source: Company, Axis Research

(CMP as of Aug 08, 2022)

CMP (Rs)	228
Upside /(Downside (%)	12%
High/Low (Rs)	587/243
Market cap (Cr)	Rs 5,602
Avg. daily vol. (6m) Shrs.	3,65,286
No. of shares (Cr)	22.54

Shareholding (%)

	Dec-21	Mar-22	Jun-22
Promoter	49.1	49.1	49.2
FIIs	17.8	16.6	16.0
MFs / UTI	13.6	12.9	12.6
Banks / FIs	0.0	0.0	0.0
Others	19.5	21.4	22.3

Financial & Valuations

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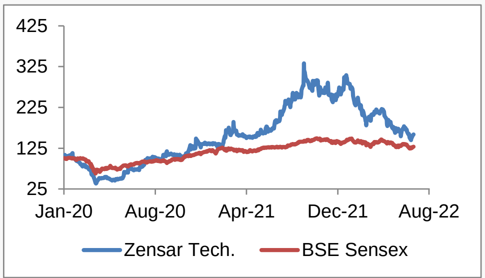
ESG disclosure Score**

Environmental Disclosure Score	NA
Social Disclosure Score	NA
Governance Disclosure Score	NA
Total ESG Disclosure Score	NA

Source: Bloomberg, Scale: 0.1-100
**Note: This score measures the amount of ESG data a company reports publicly and does not measure the company's performance on any data point. All scores are based on 2020 disclosures

Relative performance



Source: Capitaline, Axis Securities

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Key Concall takeaways

1) The management will make additional investments for strengthening these service lines – both organic and inorganic (tuck-in acquisitions). It expects strategy execution to aid growth acceleration. However, it expects at least four quarters for its strategy to bear fruits.
2) Zensar's strategic focus on improving its cash management position has shown significant results in this quarter. It is now in a strong cash position, its highest ever. The company reported net cash of $ 163.5 Mn in Q1FY23.
3) The management is optimistic about the demand for digital services. Zensar continues to strengthen its go-to-market along with stated focus areas. In line with this, we completed the acquisition of M3bi, which augments and strengthens advanced engineering and data analytics capabilities. The management has indicated strong revenue growth momentum going forward.
4) Employee additions remained tepid for Q1FY23 net employee addition stood negative at 280 with total employee headcount remaining at 11,559. Attritions levels remained elevated at 28.1%, which was due to higher demand and supply-side constraints across the industry.

Client data

	Q1FY 22	Q2 FY22	Q3FY22	Q4FY22	Q1 FY23
1 Million dollar +	79	85	83	83	86
5 Million dollar +	24	26	27	27	26
10 Million dollar +	8	10	11	11	13
20 Million dollar +	3	3	4	4	4

Source: Company, Axis Research

Segment Details

	Q1FY 22	Q2 FY22	Q3FY22	Q4FY22	Q1 FY23
Revenue- top 5 clients (%)	38.4%	35.0%	34.2%	33.3%	33.0%
Revenue- top 10 clients (%)	49.4%	47.4%	47.0%	46.0%	45.0%
Revenue- top 20 clients (%)	63.7%	61.9%	61.3%	62.0%	61.0%

Source: Company, Axis Research

Segment Details

	Q1FY 22	Q2 FY22	Q3FY22	Q4FY22	Q1 FY23
Number of Employees	9,512	10,375	10,641	11,839	11,559
Utilization (In %)	80.4%	83.3%	79.9%	81.5%	80.7%

Source: Company, Axis Research

Revenue by Vertical

	Q1FY 22	Q2 FY22	Q3FY22	Q4FY22	Q1 FY23
Hi Tech	41.9%	39.0%	36.7%	36.4%	27.4%
Mfg	11.3%	10.8%	9.7%	9.5%	13.2%
Consumer Services	14.5%	15.4%	16.1%	16.1%	18.8%
Insurance	18.7%	18.8%	17.6%	17.7%	16.5%
Banking	9.9%	12.2%	14.1%	14.3%	16.7%
Emerging	3.7%	3.8%	5.8%	5.9%	7.5%

Source: Company, Axis Research

Revenue By Service Offering (as % of Revenue)

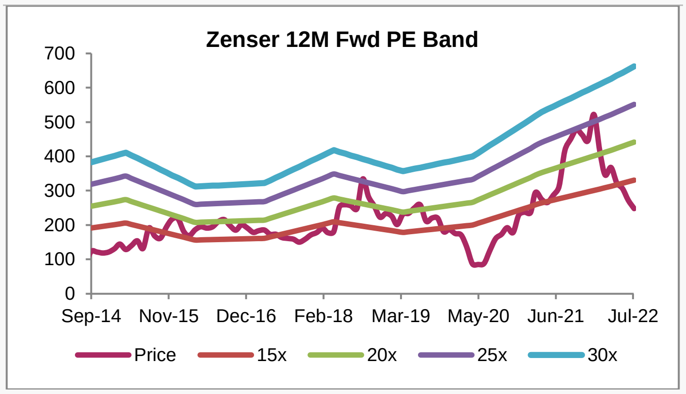
	Q1FY 22	Q2 FY22	Q3FY22	Q4FY22	Q1 FY23
Digital & Application Services (DAS)	**85.4%**	**84.8%**	**82.3%**	**81.7%**	**82.2%**
Digital Services	57.9%	61.5%	59.9%	59.8%	58.4%
Core Application Services	27.5%	23.3%	22.5%	22.0%	23.7%
Digital Foundation Services (DFS)	**14.6%**	**15.2%**	**17.7%**	**18.3%**	**17.8%**
Cloud, Digital Led next gen CIS	10.1%	9.6%	11.7%	12.2%	11.9%
Core Infrastructure Services	4.5%	5.6%	6.0%	6.1%	5.9%
Total Digital Services	**68.0%**	**71.1%**	**71.5%**	**72.0%**	**70.4%**

Source: Company, Axis Research

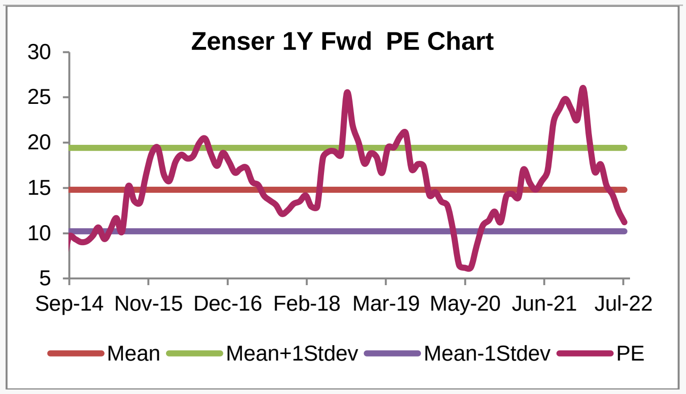
Valuation and Outlook

We believe Zensar Tech will deliver long-term sustainable growth, aided by a healthy deal pipeline and strong execution. **We recommend a BUY on Zensar, aided by strong revenue growth momentum and better recovery. We assign a 10x P/E multiple to its FY24E earnings of Rs 24.25 per share to arrive at a TP of Rs 255/share, implying an upside of 12% from the CMP.**

Zensar Tech 12M Fwd PE Band



Zensar Tech 1Y Fwd PE Chart



Source: Company, Axis Securities

Result Update (Rs Cr)

Y/E March	Q1FY23	Q4FY22	Q1FY22	(YoY)	(QoQ)
Total Revenue	**1,203**	**1,154**	**937**	**28%**	**4%**
Total Cost of Sales	883	806	611		
Gross Profit	**321**	**348**	**326**	**-2%**	**-8%**
Margin(%)	27%	30%	35%	-816	-355
Selling and marketing Expenses	74	76	60		
G&A expenses	110	108	94		
Total Operating Expenses	**184**	**184**	**153**		
EBITDA	**136**	**164**	**173**		
Margin(%)	11%	14%	18%		
Depreciation	49	48	43		
Operating Income	**87**	**116**	**130**	**-33%**	**-25%**
Margin(%)	7%	10%	14%	-665	-282
Total Other Income/(Expense)	15	48	10		
Income Before Income Taxes	**102**	**180**	**140**		
Total Taxes	27	49	37		
ETR (%)	26%	27%	26%	-8	-85
Net Profit After Taxes	**75**	**131**	**103**	-27%	-43%
Non Controlling Interest	0	1	2		
Net Income After Extraordinary Items	**75**	**130**	**101**	-26%	-42%
Margin(%)	7%	7%	7%	-	-
EPS	**2.43**	**4.18**	**3.37**	-28%	-42%

Source: Company, Axis Securities

Financials (Consolidated)

Profit & Loss (Rs Cr)

Y/E March	FY21	FY22	FY23E	FY24E
Net revenues	3,781	4,244	5,044	5,851
Other ooperating Income	0	0	0	0
Total Operating income	**3,781**	**4,244**	**5,044**	**5,851**
Employee Cost	2,153	2,922	3,380	3,920
EBITDA	**1,208**	**678**	**792**	**919**
EBITDA Margin (%)	*32%*	*16%*	*16%*	*16%*
Depreciation	175	126	146	170
Other Income	25	91	32	37
Interest (Net)	175	35	45	45
PBT	**433**	**574**	**633**	**741**
PBT Margin (%)	*11%*	*12%*	*13%*	*13%*
Tax	123	153	158	185
Adjusted PAT	307	422	475	555
Extraordinary Items	7	5	5	5
Reported PAT	**303**	**416**	**469**	**550**

Source: Company, Axis Securities

Balance Sheet (Rs Cr)

Y/E March	FY21	FY22	FY23E	FY24E
Equity capital	45	45	45	45
Reserves & Surplus	2349	2576	2874	3226
Net worth	**2,394**	**2,621**	**2,919**	**3,271**
Total debt	420	420	420	420
Total Liabilities & Equity	**4,017**	**4,402**	**4,880**	**5,438**
Tangible Assets	418	452	488	527
Total fixed assets	1,280	1,477	1,708	1,978
Investments	75	75	75	75
Goodwill	861	1,025	1,220	1,451
Other Fixed Assets	-	-	-	-
Total Non-Current Assets	**263**	**303**	**349**	**403**
Debtors	1,159	1,333	1,533	1,762
Cash & bank	441	323	217	100
Loans & advances	-	-	-	-
Other Current Assets	883	1,015	1,168	1,343
Total Current Assets	**2,663**	**2,851**	**3,097**	**3,385**
Creditors	961	1,085	1,226	1,386
Provisions	163	195	235	281
Current Liab. & Prov.	**1,123**	**1,281**	**1,461**	**1,667**
Total Assets	**4,017**	**4,402**	**4,880**	**5,438**

Source: Company, Axis Securities

Cash Flow (Rs Cr)

Y/E March	FY21	FY22	FY23E	FY24E
PBT	433	536	633	741
Add: Depreciation	175	126	146	170
Other Adjustments	(10)	(10)	(10)	(10)
Chg. in working capital	(154)	(157)	(164)	(172)
Taxes paid	(123)	(134)	(158)	(185)
Extra Ordinary Items	-	-	-	-
CF from operations	**375**	**277**	**339**	**408**
Change in fixed assets	(38)	(38)	(38)	(38)
Purchase of investment	(38)	(38)	(38)	(38)
Proceeds from Invest. Sale	10	10	10	10
Other Adjustments	4	4	4	4
CF from Investing acti.	**(7)**	**(7)**	**(7)**	**(7)**
Chg. in debt	(28)	(19)	(26)	(34)
Chg. in Equity capital	-	-	-	-
Chg. in Pref. capital	-	-	-	-
Dividend & dividend tax	(50)	(50)	(50)	(50)
CF from Financing acti.	**(8)**	**(7)**	**(8)**	**(8)**
Chg. in cash	36	26	32	39
Opening cash	5	4	3	2
Closing cash	44	32	22	10

Source: Company, Axis Securities

Ratio Analysis (%)

Y/E March	FY21	FY22	FY23E	FY24E
Per Share Ratios				
Fully diluted E P S	13.31	17.63	20.86	24.45
Book Value	106.40	116.51	129.73	145.38
Dividend per share	2.90	2.90	2.90	2.90
Valuation Ratio				
P/E	30.43	22.98	19.41	16.57
P/BV	3.81	3.48	3.12	2.79
EV/EBITDA	7.53	13.58	11.76	10.27
EV/Sales	2.40	2.12	1.85	1.61
Growth Ratios				
Sales Growth	-9%	15%	16%	16%
EBITDA Growth	136%	-44%	17%	16%
Net Profit Growth	13%	31%	18%	17%
EPS Growth	12%	32%	18%	17%
Common size Ratios				
EBITDA Margin	32%	16%	16%	16%
EBIT margin	13%	13%	13%	13%
PAT margin	8%	9%	9%	9%
Employee cost	69%	67%	67%	67%
Return ratios				
RoNW	13%	15%	16%	17%
RoCE	18%	19%	20%	21%
Solvency Ratios				
Total Debt/Equity	18%	16%	14%	13%

Source: Company, Axis Securities

Zensar Technologies Price Chart and Recommendation History

Date	Reco	TP	Research
27-Jan-20	HOLD	185	Result Update
18-May-20	BUY	106	Result Update
27-Jul-20	HOLD	155	Result Update
02-Nov-20	HOLD	192	Result Update
25-Jan-21	HOLD	263	Result Update
03-May-21	HOLD	285	Result Update
17-May-21	HOLD	285	Event Update
27-Jul-21	BUY	455	Result Update
28-Oct-21	BUY	540	Result Update
11-May-22	BUY	360	Result Update
10-Aug-22	BUY	250	Result Update

Source: Axis Securities

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BUY	More than 10%
HOLD	Between 10% and -10%
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