

BUY

TP: Rs 5,530 | ▲ 17%

COFORGE

| IT Services

| 29 July 2021

Yet another positive surprise; maintain BUY

- Q1 strong with 16% QoQ USD revenue growth led by BFSI. EBIT margin in line at 12.6% (-107bps QoQ)
- Organic revenue growth guidance raised to 19%+ YoY CC, backed by highest-ever organic executable order book of US\$ 560mn
- We raise FY23 EPS, upgrade our target P/E to 30x and move to a Jun'22 TP of Rs 5,530 (from Rs 4,080) – BUY

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Growth surprise continues: Coforge's sequential growth continued to outperform our/consensus estimates, in line with the Q1FY22 trend across the sector. Reported dollar revenue increased 16% QoQ (11.4% est.) and included two months of revenue consolidation from the SLK Global acquisition. Organic revenue growth came as a positive surprise at 7.6% QoQ USD. Growth was led by a secular uptick across verticals, including travel (+15% QoQ) and BFSI (+44% due to revenues from SLK Global). Geography-wise, North America/RoW grew the most.

EBIT margin in line: EBIT margin declined 107bps QoQ to 12.6% (12.8% est.) due to wage hikes and large-deal transition costs. Employee cost increased 200bps QoQ. Coforge continued to use offshoring as a lever and it now forms 40% share of quarterly revenue (vs. 39% in Q4FY21).

Record executable order book: The executable order book for the next 12 months was at a record US\$ 560mn (+8% QoQ, +20% YoY) plus US\$ 80mn from SLK Global. A total of 11 new logos were signed in Q1. Coforge won three large deals including a US\$ 105mn engagement for enterprise core transformation and hybrid cloud management. The company bagged a three-year US\$ 20mn+ contract in insure-tech, marking its largest deal for the 'Advantage Go' platform.

Supply-side pressure: Coforge's total headcount stood at 20,491 in Q1FY22 as it added ~8,100 employees during the quarter, its highest ever (including 6,962 employees rebadged from SLK Global). Attrition stood at an eight-quarter high of 12.6%, up 210bps QoQ, though lower than many peers. Utilisation dropped 400bps to 77% on increased hiring and employee intake from SLK Global. Management expects utilisation to normalise as large-deal transitions take place.

Maintain BUY: Following the strong Q1 results and FY22 guidance of at least 19% CC organic growth, we raise FY23 EPS by 7%. We also upgrade our FY23E P/E to 30x (from 25x), in line with our multiple for LTI, backed by steady earnings upgrades, an upbeat growth outlook, record executable order book and timely revenue diversification. On rollover, we move to a Jun'22 TP of Rs 5,530 (vs. Rs 4,080). BUY.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	COFORGE IN/Rs 4,743
Market cap	US\$ 4.0bn
Free float	43%
3M ADV	US\$ 37.7mn
52wk high/low	Rs 4,850/Rs 1,773
Promoter/FPI/DII	70%/13%/17%

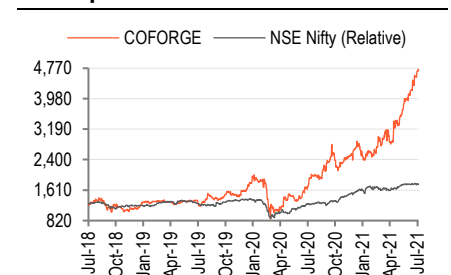
Source: NSE | Price as of 28 Jul 2021

Key financials

Y/E 31 Mar	FY21P	FY22E	FY23E
Total revenue (Rs mn)	46,628	65,007	78,938
EBITDA (Rs mn)	7,911	12,127	15,313
Adj. net profit (Rs mn)	4,556	8,002	10,583
Adj. EPS (Rs)	75.0	131.8	174.3
Consensus EPS (Rs)	75.0	109.7	133.3
Adj. ROAE (%)	17.0	25.3	28.8
Adj. P/E (x)	63.2	36.0	27.2
EV/EBITDA (x)	36.5	23.7	18.6
Adj. EPS growth (%)	2.9	75.7	32.2

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE



Earnings call highlights

- Management has guided for FY22 organic revenue growth of at least 19% YoY CC, up from the 17% guidance in Q4FY21. Though the outlook is robust, we believe it is on the conservative side. EBITDA margin guidance (pre-RSU including SLK Global) is intact at 19%, the same as last quarter.
- Revenue growth tailwinds for Coforge are as follows: (1) strong 12-month organic order book, (2) accelerated demand growth, (3) declining top client concentration, (4) upfront resource hiring, (5) increased recognition of its product engineering capabilities, and (6) foray into newer verticals over the last four quarters.
- Top-5 client concentration continued to decline and stood at 24.6% in Q1.
- Hi-tech, retail & healthcare, and government outside India formed 8.9%, 8.1% and 7% of Q1 revenue respectively (under the 'other' vertical).
- The travel vertical has been growing well and has recovered to pre-Covid levels in North America and APAC.
- DSO stood at 71 days during the quarter, up from 70 in Q4FY21.
- The board has recommended interim dividend of Rs 13/sh.

Fig 1 – Quarterly performance

(Rs mn)	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)	FY21	FY20	YoY (%)
Revenue (US\$ mn)	199.7	139.6	43.0	172.1	16.0	666.3	578.1	15.3
Revenue	14,616	10,570.0	38.3	12,615	15.9	49,338.0	41,316.0	19.4
Operating Expenditure	12,257	8,884.5	38.0	10,447	17.3	41,077.5	34,403.5	19.4
Cost of revenues	10,250	7,240.5	41.6	8,580	19.5	33,846.5	27,479.5	23.2
as % of sales	70.1	68.5	-	68.0	-	68.6	66.5	-
SG&A expenses	2,007	1,644.0	22.1	1,867	7.5	7,231.0	6,924.0	4.4
as % of sales	13.7	15.6	-	14.8	-	14.7	16.8	-
EBITDA	2,359	1,685.6	40.0	2,168	8.8	8,260.6	6,912.6	19.5
Depreciation	524	465.0	12.7	449	16.7	1,898.0	1,762.0	7.7
EBIT	1,835	1,220.6	50.3	1,719	6.7	6,362.6	5,150.6	23.5
Other Income	(44)	48.0	-	63	-	4.0	426.0	-
PBT	1,791	1,088.6	64.5	1,782	0.5	6,186.6	5,453.6	13.4
Total Tax	320	260.0	23.1	408	(21.6)	1,291.0	1,190.0	8.5
Adjusted PAT	1,471	828.5	77.5	1,374	7.1	4,895.6	4,263.6	14.8
(Profit)/loss from JV's/Ass/MI	76.0	30.0	-	44.0	-	165.0	160.0	-
APAT after MI	1,395	798.5	74.7	1,330	4.9	4,730.6	4,103.6	15.3
Extra ordinary items	96	180.0	-	46	-	322.0	237.0	-
Reported PAT	1,491	978.5	52.4	1,376	8.4	5,052.6	4,340.6	16.4
Reported EPS	20.4	12.8	58.7	21.9	(7.1)	74.5	65.2	14.1
Margins (%)			(bps)		(bps)			(bps)
EBITDA	16.1	15.9	19	17.2	(105)	16.7	16.7	1
EBIT	12.6	11.5	101	13.6	(107)	12.9	12.5	43
EBT	12.3	10.3	196	14.1	(187)	12.5	13.2	(66)
PAT	10.2	9.3	94	10.9	(71)	9.6	9.9	(34)
Effective Tax rate	17.9	23.9	(602)	22.9	(503)	20.9	21.8	(95)

Source: Company, BOBCAPS Research

Fig 2 – Operating metrics

(in INR terms)	Q1FY22 (% Contr. to Revenue)	Growth	
		QoQ (%)	YoY (%)
Revenue by Geography			
North America	52	30.0	51.8
Europe	35	2.2	35.6
RoW	13	8.4	6.6
Revenue by Vertical			
Banking and Financial Services	21	43.8	71.6
Insurance	31	15.1	29.1
Transportation	19	15.3	37.6
Other	29	2.5	34.6
Revenue Offshore-Onsite Mix			
Offshore	40	19.1	45.9
Onsite	60	13.8	33.6
Client Concentration			
Top 5	25	14.0	30.8
Non-Top 5 client	75	16.5	40.9
Top 10	36	15.5	30.6
Operational Metrics			
	Q1FY22	QoQ chg	YoY chg
Number of employees	20,500	8,109	9,902
Attrition (%)	12.6	210bps	76bps
Utilisation (%)	77	(400bps)	0bps
DSO (days)	71	1 day	0 days
Customer Acquisition			
	Q1FY22	Q4FY21	Q1FY21
Significant New Customer Addition			
USA	6	4	5
Europe	4	5	5
ROW	1	2	0
Total	11	11	10
Fresh Order Intake (US\$ mn)			
USA	46	119	85
Europe	227	65	70
ROW	46	17	31
Total	319	201	186
Executable Orders Over Next 12M (US\$ mn)			
	560	520	465

Source: Company, BOBCAPS Research

Valuation methodology

Coforge has guided for at least 19% CC organic revenue growth in FY22, backed by a ~20% YoY increase in the organic executable order book and three large deal wins in Q1FY22. Following the strong Q1 results and robust FY22 guidance, we raise our FY23 EPS estimate by 7%.

We also upgrade our target FY23E P/E multiple to 30x (from 25x), in line with our multiple for L&T Infotech (LTI), backed by steady earnings upgrades, an upbeat growth outlook, record executable order book and timely revenue diversification. On rolling valuations forward, we move to a higher Jun'22 TP of Rs 5,530 (from Rs 4,080). Reiterate BUY.

Fig 3 – Revised estimates

(Rs mn)	New			Old		Change (%)	
	FY22E	FY23E	FY24E	FY22E	FY23E	FY22E	FY23E
Revenues (US\$ mn)	857	1,009	1197	820	953	4.5	5.9
YoY growth (%)	36.6	17.7	18.7	30.7	16.2	-	-
Revenues	65,007	78,938	93,710	62,726	74,551	3.6	5.9
EBITDA (post RSU)	12,127	15,313	18,454	11,733	14,283	3.4	7.2
EBITDA margin (%)	18.7	19.4	19.7	18.7	19.2	-	-
Net Profits	8,002	10,583	13,306	8,023	9,909	(0.3)	6.8
EPS (Rs)	131.8	174.3	219.1	132.1	163.2	(0.3)	6.8

Source: BOBCAPS Research

Fig 4 – Key assumptions

Parameter	FY21	FY22E	FY23E	FY24E
USD growth YoY (%)	5.8	36.6	17.7	18.7
Cost of revenues (% of total revenue)	68.0	67.7	67.1	67.1
EBIT Margin (%)	13.0	15.5	16.6	17.2

Source: Company, BOBCAPS Research

Fig 5 – Peer comparison

Ticker	CMP (Rs)	Mkt Cap (in US\$ bn)	Rating	Target Price (Rs)	US\$ revenue CAGR FY21-23E (%)	EPS (Rs)		P/E (x)		ROE (%)	
						FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
TCS IN	3,198	160.6	BUY	3,890	15.1	109.8	127.0	29.1	25.2	41.4	43.1
INFO IN	1,606	91.5	BUY	1,860	14.3	54.1	61.1	29.7	26.3	33.8	33.8
WPRO IN	591	43.7	HOLD	590	18.4	23.5	27.1	25.1	21.8	7.1	7.5
HCLT IN	985	35.8	BUY	1,260	11.3	52.2	59.0	18.9	16.7	31.9	38.4
TECHM IN	1,128	13.2	BUY	1,190	14.7	63.4	75.7	17.8	14.9	20.9	22.2
LTI IN	4,371	10.3	BUY	4,990	18.7	134.1	158.4	32.6	27.6	37.1	42.6
MPHL IN	2,578	6.4	HOLD	2,500	14.0	82.0	95.7	31.4	26.9	22.3	25.5
MTCL IN	2,725	6.0	SELL	2,270	15.8	87.7	93.9	31.1	29.0	50.5	55.7
PSYS IN	3,130	3.4	HOLD	2,920	21.0	74.0	91.4	42.3	34.2	19.6	22.5
COFORGE IN	4,749	4.0	BUY	5,530	26.8	131.8	174.3	36.3	27.4	25.3	28.8

Source: BOBCAPS Research

Key risks

Key downside risks to our estimates are:

- challenges at the company's top clients,
- recovery taking longer to materialise in the travel vertical, and
- impact of a potential Covid third wave.

Sector recommendation snapshot

Stock	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Coforge	COFORGE IN	4	4,743	5,530	BUY
HCL Technologies	HCLT IN	36	983	1,260	BUY
Info Edge	INFOE IN	9	5,255	2,880	SELL
Infosys	INFO IN	92	1,606	1,860	BUY
L&T Infotech	LTI IN	10	4,357	4,990	BUY
Mindtree	MTCL IN	6	2,709	2,270	SELL
Mphasis	MPHL IN	6	2,588	2,500	HOLD
Persistent Systems	PSYS IN	3	3,098	2,920	HOLD
Tata Consultancy Services	TCS IN	161	3,198	3,890	BUY
Tech Mahindra	TECHM IN	13	1,120	1,190	BUY
Wipro	WPRO IN	44	592	590	HOLD

Source: BOBCAPS Research, NSE | Price as of 28 Jul 2021

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21P	FY22E	FY23E	FY24E
Total revenue	41,839	46,628	65,007	78,938	93,680
EBITDA	7,431	7,911	12,127	15,313	18,454
Depreciation	1,730	1,836	2,060	2,199	2,351
EBIT	5,701	6,075	10,067	13,114	16,103
Net interest inc./(exp.)	0	0	0	0	0
Other inc./(exp.)	462	113	579	1,077	1,535
Exceptional items	0	0	0	0	0
EBT	5,978	5,962	10,646	14,191	17,638
Income taxes	1,203	1,302	2,159	2,980	3,704
Extraordinary items	185	226	0	0	0
Min. int./Inc. from assoc.	236	104	485	628	628
Reported net profit	4,539	4,556	8,002	10,583	13,306
Adjustments	0	0	0	0	0
Adjusted net profit	4,539	4,556	8,002	10,583	13,306

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21P	FY22E	FY23E	FY24E
Accounts payables	0	0	0	0	0
Other current liabilities	7,526	8,637	11,809	14,214	16,758
Provisions	922	4,599	6,412	7,786	9,240
Debt funds	0	0	0	0	0
Other liabilities	387	387	387	387	387
Equity capital	625	625	625	625	625
Reserves & surplus	23,340	28,911	33,061	39,178	46,706
Shareholders' fund	23,965	29,536	33,686	39,803	47,331
Total liab. and equities	32,800	43,159	52,294	62,189	73,716
Cash and cash eq.	8,195	8,063	12,920	19,969	28,566
Accounts receivables	5,672	9,326	13,001	15,788	18,736
Inventories	3	3	3	3	3
Other current assets	3,976	5,432	7,093	8,353	9,686
Investments	3,651	3,651	3,651	3,651	3,651
Net fixed assets	10,001	15,137	14,077	12,878	11,527
CWIP	0	0	0	0	0
Intangible assets	0	0	0	0	0
Deferred tax assets, net	1,302	1,548	1,548	1,548	1,548
Other assets	0	0	0	0	0
Total assets	32,800	43,159	52,294	62,189	73,716

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21P	FY22E	FY23E	FY24E
Cash flow from operations	2,279	4,850	9,130	12,066	14,467
Capital expenditures	(1,657)	(1,000)	(1,000)	(1,000)	(1,000)
Change in investments	0	0	0	0	0
Other investing cash flows	3,807	958	579	1,077	1,535
Cash flow from investing	2,150	(42)	(421)	77	535
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(1,328)	(4,940)	(3,852)	(5,094)	(6,405)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(1,328)	(4,940)	(3,852)	(5,094)	(6,405)
Chg in cash & cash eq.	3,101	(132)	4,857	7,049	8,597
Closing cash & cash eq.	8,195	8,063	12,920	19,969	28,566

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21P	FY22E	FY23E	FY24E
Reported EPS	72.9	75.0	131.8	174.3	219.1
Adjusted EPS	72.9	75.0	131.8	174.3	219.1
Dividend per share	10.0	24.8	52.7	69.7	87.6
Book value per share	384.8	474.3	540.9	639.2	760.1

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21P	FY22E	FY23E	FY24E
EV/Sales	7.0	6.2	4.4	3.6	3.0
EV/EBITDA	39.2	36.5	23.7	18.6	15.1
Adjusted P/E	65.1	63.2	36.0	27.2	21.6
P/BV	12.3	10.0	8.8	7.4	6.2

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21P	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	75.9	76.4	75.2	74.6	75.4
Interest burden (PBT/EBIT)	104.9	98.1	105.8	108.2	109.5
EBIT margin (EBIT/Revenue)	13.6	13.0	15.5	16.6	17.2
Asset turnover (Rev./Avg TA)	138.5	122.8	136.2	137.9	137.9
Leverage (Avg TA/Avg Equity)	1.4	1.4	1.5	1.6	1.6
Adjusted ROAE	20.3	17.0	25.3	28.8	30.5

Ratio Analysis

Y/E 31 Mar	FY20A	FY21P	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	13.8	11.4	39.4	21.4	18.7
EBITDA	15.2	6.5	53.3	26.3	20.5
Adjusted EPS	10.1	2.9	75.7	32.2	25.7
Profitability & Return ratios (%)					
EBITDA margin	17.8	17.0	18.7	19.4	19.7
EBIT margin	13.6	13.0	15.5	16.6	17.2
Adjusted profit margin	10.8	9.8	12.3	13.4	14.2
Adjusted ROAE	20.3	17.0	25.3	28.8	30.5
ROCE	17.6	15.9	23.4	31.6	40.8
Working capital days (days)					
Receivables	48	59	63	67	67
Inventory	0	0	0	0	0
Payables	90	115	148	139	138
Ratios (x)					
Gross asset turnover	4.6	3.7	4.5	5.9	7.7
Current ratio	2.3	1.8	1.9	2.1	2.2
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	(0.3)	(0.3)	(0.4)	(0.5)	(0.6)

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

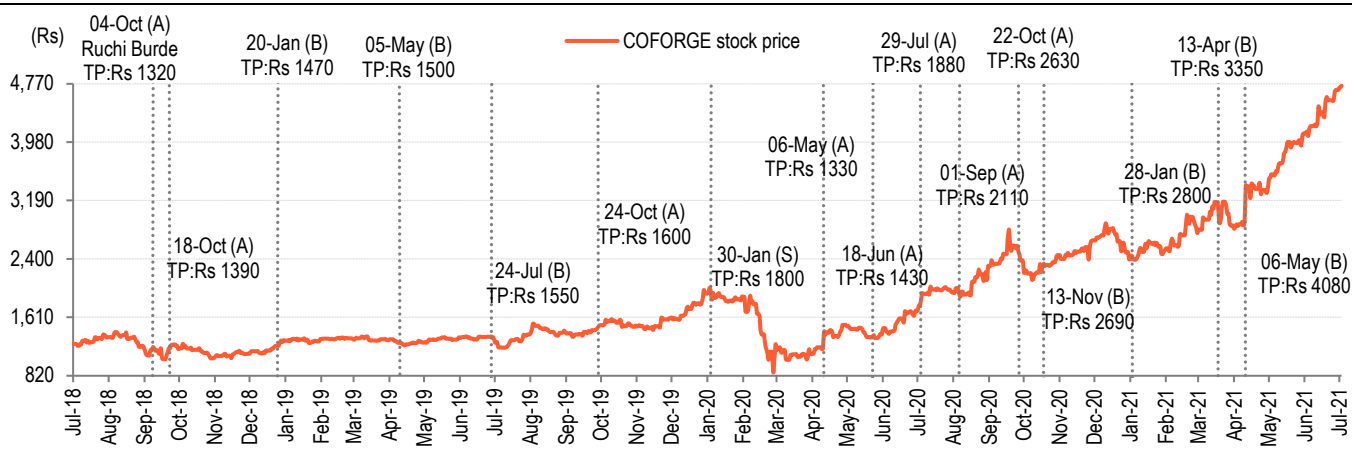
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): COFORGE (COFORGE IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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