

REDUCE

TP: Rs 950 | ▼ 4%

ECLERX SERVICES

| IT Services

| 29 January 2021

Upbeat quarter led by organic growth

eClerx (ECLX) reported a substantial topline beat in Q3FY21 backed partly by Personiv revenues flowing in and robust CLX business. Dollar revenue grew 9.9% QoQ, ahead of our estimate led by growth in managed services. We raise FY21/FY22/FY23 EPS by 27%/15%/8% to factor in the upbeat Q3 performance. On rollover, we have a new Dec'21 TP of Rs 950 (vs. Rs 800). Maintain REDUCE as we see limited growth potential beyond FY22 despite faster CLX recovery and synergy from the Personiv acquisition.

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Strong organic growth: Dollar revenue at US\$ 53.3mn (US\$ 49mn est.) increased 9.9% QoQ and 9.5% CC (1.1% CC contributed by Personiv at ~US\$ 0.5mn). Demand recovery has also been faster than management expected, driven by (1) improvement in CLX and managed services business, and (2) increased utilisation (+210bps QoQ to 81.2%) post stabilisation in the 'work-from-home' environment. EBIT margin at 24.7% (23.7% est.) was up 20bps QoQ as offshoring increased 9% QoQ and efficiency improved across other levers. A full wage hike was carried out in Q3.

CLX recovery continues: CLX business had recovered sharply last quarter following a 20-30% QoQ drop in Q1FY21. During Q3, Europe grew 9.9% QoQ as CLX business continued to revive. Management does not expect the current restrictions in Europe to affect operations as these are mostly for discretionary activities. Nevertheless, we remain wary of the volatile nature of the CLX business.

Margins guided to decline: Management expects the current EBIT margin of ~24% to decline as some of the costs e.g. non-people SG&A costs, travel and facilities cost start to normalize. We expect FY21 margin levels to remain high as revenue shoots up following the Personiv acquisition.

Ticker/Price	ECLX IN/Rs 988
Market cap	US\$ 510.1mn
Shares o/s	38mn
3M ADV	US\$ 1.7mn
52wk high/low	Rs 1,034/Rs 320
Promoter/FPI/DII	50%/25%/25%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	14,305	14,376	16,626	23,048	23,866
EBITDA (Rs mn)	3,092	3,249	4,810	5,915	6,350
Adj. net profit (Rs mn)	2,283	2,087	2,963	3,658	3,963
Adj. EPS (Rs)	60.1	55.5	86.6	106.9	115.8
Adj. EPS growth (%)	(19.4)	(7.7)	56.2	23.5	8.3
Adj. ROAE (%)	20.2	17.5	21.2	24.0	23.6
Adj. P/E (x)	16.5	17.8	11.4	9.2	8.5
EV/EBITDA (x)	10.8	10.6	7.2	5.7	5.4

Source: Company, BOBCAPS Research

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FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
Revenues (US\$ mn)	53.3	51.8	2.9	48.5	9.9	142.9	152.8	(6.5)
Revenue	3,943	3,755	5.0	3,608	9.3	10,673.0	10,866.7	(1.8)
Operating Expenditure	2,767	2,723	1.6	2,527	9.5	7,829.0	8,394.3	(6.7)
Cost of revenues	1,950	1,891	3.1	1,793	8.8	5,568.0	5,724.4	(2.7)
as % of sales	49.5	50.4	-	49.7	-	52.2	52.7	-
SG&A expenses	817	832	(1.8)	734	11.3	2,261.0	2,669.9	(15.3)
as % of sales	20.7	22.2	-	20.3	-	21.2	24.6	-
EBITDA	1,176	1,032	14.0	1,081	8.8	2,844.0	2,472.4	15.0
Depreciation	202	176	14.8	196	3.0	548.0	524.7	4.4
EBIT	974	856	13.8	885	10.1	2,296.0	1,947.7	17.9
Other Income	33	115	-	(4)	-	263.7	284.1	-
Interest	48	48	-	49	-	146.9	138.9	-
PBT	959	922	3.9	832	15.3	2,412.8	2,093.0	15.3
Total Tax	247	222	11.5	217	13.9	664.5	558.6	19.0
Adjusted PAT	711	700	1.6	615	15.8	1,748.4	1,534.4	13.9
(Profit)/loss from JV's/Ass/MI	-	-	-	-	-	0.0	0.0	-
APAT after MI	711	700	1.6	615	15.8	1,748.4	1,534.4	13.9
Extra ordinary items	0	0	-	0	-	0.0	0.0	-
Reported PAT	711	700	1.6	615	15.8	1,748.4	1,534.4	13.9
Reported EPS	20.8	18.6	11.7	17.7	17.4	49.5	40.8	21.4
Margins (%)			(bps)		(bps)			(bps)
EBITDA	29.8	27.5	230	30.0	(10)	26.6	22.8	390
EBIT	24.7	22.8	190	24.5	20	21.5	17.9	360
EBT	24.3	24.6	(20)	23.0	130	22.6	19.3	330
PAT	18.0	18.7	(60)	17.0	100	16.4	14.1	230
Effective Tax rate	25.8	24.1	170	26.1	(30)	27.5	26.7	80

Source: BOBCAPS Research

FIG 2 – OPERATING METRICS

(in US\$ terms)	Q3FY21	Growth (%)	
	(% Contr. to Revenue)	QoQ	YoY
Revenue by Geography (%)			
North America	66.0	9.9	2.9
Europe	28.0	9.9	2.9
ROW	6.0	9.9	2.9
Client Contribution to Revenue			
Top 10 (%)	64.0	5.3	9.0
Non-Top 10 client revenues	36.0	19.1	41.9
Total Employees	11,481	35	33.6
Billing Mix			
FTE	66.0	5.1	3.3
Managed Services Revenues	34.0	20.5	12.9
Onsite-Offshore Mix			
Onsite Revenues	23.0	9.9	(5.3)
Offshore Revenues	77.0	9.9	5.6
Currency Concentration			
USD	81.0	9.9	13.4
Euro	13.0	9.9	71.9
GBP	4.0	(12.1)	19.0

Source: BOBCAPS Research

Valuation methodology

Over the last three years, ECLX has witnessed a structural downward reset to operating margins led by a changing business mix in favour of onsite revenues. However, the company has demonstrated efficient cost management, helped by increased utilisation (at a four-year high of 81.2% in Q3), offshoring and reduced attrition, enabling the EBIT margin to stay above 20% for the last two quarters.

We raise FY21/FY22/FY23 EPS estimates by 27%/15%/8% factoring in the above-expected Q3 performance, higher operational efficiency, Personiv acquisition flowthrough and upbeat FY21 outlook. Rolling valuations forward, we have a revised Dec'21 target price of Rs 950 (Rs 800 earlier), set at an unchanged 8x one-year forward P/E. In our view, lower revenue productivity and an increasing mix of non-annuity business render ECLX comparable to BPO players, rather than IT services players.

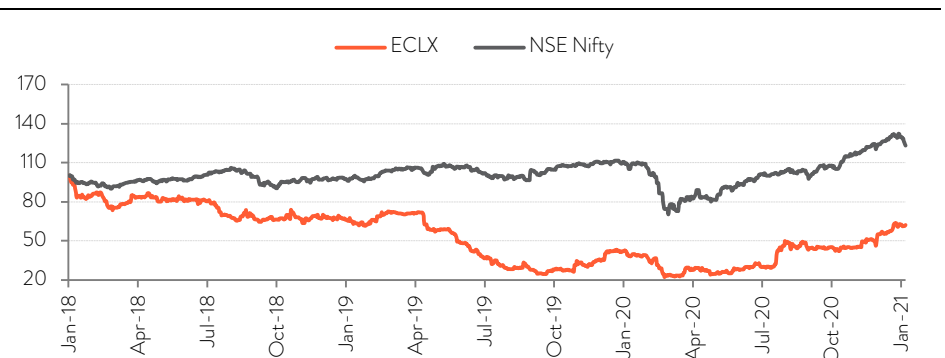
Despite the good Q3 performance, we remain wary of low long-term revenue visibility and unsustainable margins. ECLX's high top-client concentration is not encouraging, and growth beyond FY22 looks unsustainable. Reiterate REDUCE.

FIG 3 – REVISED ESTIMATES

(Rs mn)	FY21E			FY22E			FY23E		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Revenues (US\$ mn)	202.9	222.6	9.7	266.5	300.2	12.6	277.9	305.9	10.1
YoY growth (%)	1.2	11.0	-	31.3	34.8	-	4.3	1.9	-
Revenues	15,249	16,626	9.0	20,779	23,048	10.9	21,682	23,866	10.1
EBIT	3,142	4,011	27.6	4,283	4,895	14.3	4,972	5,287	6.3
EBIT margins (%)	20.6	24.1	-	20.6	21.2	-	22.9	22.2	-
Net Profits	2,358	2,963	25.6	3,214	3,658	13.8	3,738	3,963	6.0
EPS (Rs)	68.0	86.6	27.4	92.6	106.9	15.4	107.7	115.8	7.5

Source: BOBCAPS Research

FIG 4 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Upside risks to our estimates include:

- sharper recovery in demand, especially for the offshore business,
- stronger revival in CLX business,
- above-expected traction in large accounts, and
- better synergy from the acquisition.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	14,305	14,376	16,626	23,048	23,866
EBITDA	3,092	3,249	4,810	5,915	6,350
Depreciation	447	710	799	1,021	1,064
EBIT	2,645	2,539	4,011	4,895	5,287
Net interest income/(expenses)	0	(188)	(197)	(200)	(200)
Other income/(expenses)	469	452	236	316	342
Exceptional items	0	0	0	0	0
EBT	3,114	2,803	4,050	5,011	5,428
Income taxes	832	715	1,087	1,353	1,466
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	2,283	2,087	2,963	3,658	3,963
Adjustments	0	0	0	0	0
Adjusted net profit	2,283	2,087	2,963	3,658	3,963

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	0	0	0	0	0
Other current liabilities	1,960	1,969	2,278	3,157	3,269
Provisions	78	79	91	126	131
Debt funds	63	63	63	63	63
Other liabilities	152	152	152	152	152
Equity capital	384	384	384	384	384
Reserves & surplus	10,120	12,971	14,151	15,608	17,186
Shareholders' fund	10,505	13,355	14,535	15,992	17,570
Total liabilities and equities	12,758	15,619	17,120	19,492	21,186
Cash and cash eq.	1,256	4,357	2,838	3,294	5,008
Accounts receivables	2,352	2,363	2,733	3,789	3,923
Inventories	0	0	0	0	0
Other current assets	2,547	2,560	2,961	4,104	4,250
Investments	2,916	2,916	5,432	5,432	5,432
Net fixed assets	1,346	1,082	815	531	232
CWIP	150	150	150	150	150
Intangible assets	2,220	2,220	2,220	2,220	2,220
Deferred tax assets, net	121	121	121	121	121
Other assets	0	0	0	0	0
Total assets	12,758	15,619	17,120	19,492	21,186

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	3,562	2,797	3,762	4,679	5,026
Interest expenses	(257)	(264)	(39)	(116)	(142)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(300)	(14)	(450)	(1,284)	(163)
Other operating cash flows	(943)	809	0	0	0
Cash flow from operations	2,062	3,328	3,274	3,278	4,721
Capital expenditures	(520)	(446)	(532)	(738)	(764)
Change in investments	(1,210)	0	(2,516)	0	0
Other investing cash flows	(567)	264	39	116	142
Cash flow from investing	(2,297)	(182)	(3,010)	(621)	(622)
Equities issued/Others	53	0	0	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	(554)	0	0	0	0
Dividends paid	(38)	(45)	(1,783)	(2,201)	(2,385)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(539)	(45)	(1,783)	(2,201)	(2,385)
Changes in cash and cash eq.	(774)	3,101	(1,519)	455	1,714
Closing cash and cash eq.	1,256	4,357	2,838	3,294	5,008

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	60.1	55.5	86.6	106.9	115.8
Adjusted EPS	60.1	55.5	86.6	106.9	115.8
Dividend per share	1.0	1.0	43.5	53.7	58.2
Book value per share	279.1	354.8	386.2	424.9	466.8

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	2.3	2.4	2.1	1.5	1.4
EV/EBITDA	10.8	10.6	7.2	5.7	5.4
Adjusted P/E	16.5	17.8	11.4	9.2	8.5
P/BV	3.5	2.8	2.6	2.3	2.1

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	73.3	74.5	73.2	73.0	73.0
Interest burden (PBT/EBIT)	117.7	110.4	101.0	102.4	102.7
EBIT margin (EBIT/Revenue)	18.5	17.7	24.1	21.2	22.2
Asset turnover (Revenue/Avg TA)	105.7	101.3	101.6	125.9	117.3
Leverage (Avg TA/Avg Equity)	1.2	1.2	1.2	1.2	1.2
Adjusted ROAE	20.2	17.5	21.2	24.0	23.6

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	4.8	0.5	15.7	38.6	3.5
EBITDA	(15.7)	5.1	48.1	23.0	7.4
Adjusted EPS	(19.4)	(7.7)	56.2	23.5	8.3
Profitability & Return ratios (%)					
EBITDA margin	21.6	22.6	28.9	25.7	26.6
EBIT margin	18.5	17.7	24.1	21.2	22.2
Adjusted profit margin	16.0	14.5	17.8	15.9	16.6
Adjusted ROAE	20.2	17.5	21.2	24.0	23.6
ROCE	30.4	27.1	37.9	39.3	41.0
Working capital days (days)					
Receivables	60	60	56	52	59
Inventory	0	0	0	0	0
Payables	64	64	66	58	67
Ratios (x)					
Gross asset turnover	11.2	11.8	17.5	34.2	62.5
Current ratio	3.0	4.5	3.6	3.4	3.9
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	(0.1)	(0.3)	(0.2)	(0.2)	(0.3)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

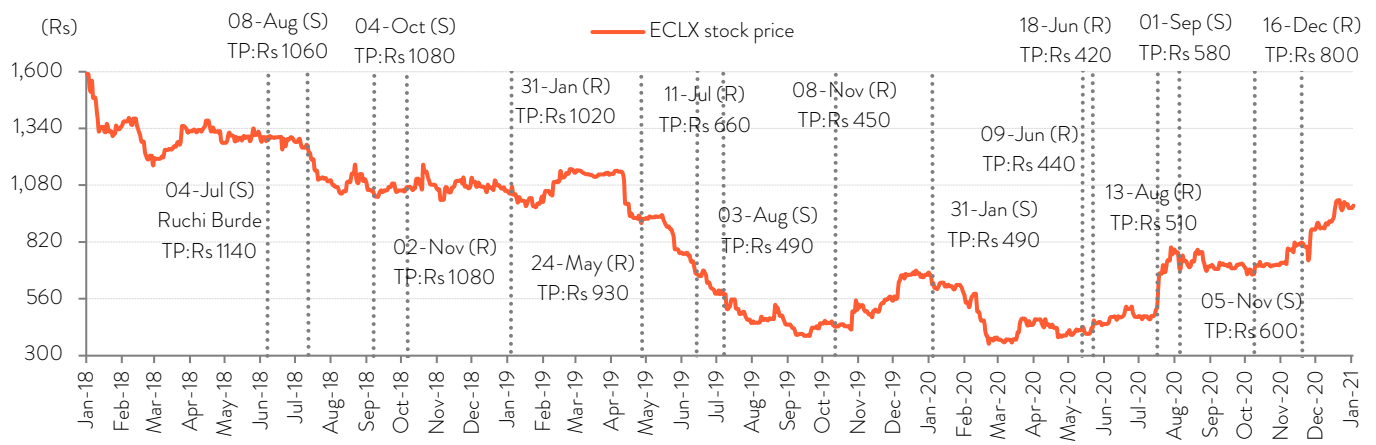
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): ECLERX SERVICES (ECLX IN)



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

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