

FIRST LIGHT

28 November 2018

RESEARCH

eClerx Services | Target: Rs 1,080 | +0% | REDUCE

Operating margin outlook still cloudy

SUMMARY

eClerx Services

eClerx (ECLX), in a recent management meet, reiterated its strategy of onsite presence ramp-up in a bid to move closer to clients. Management indicated possible double-digit growth in FY20 on receding client-specific challenges and healthy deal wins. Operating margin uncertainty persists despite levers such as potential price hikes in top 10 accounts and favourable hedge positions (from H2FY20). Given the clouded margin outlook, we reiterate REDUCE with an unchanged Sep'19 target price of Rs 1,080.

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TOP PICKS

LARGE-CAP IDEAS

Company	Rating	Target
Axis Bank	Buy	750
Cipla	Buy	615
GAIL	Buy	525
Reliance Industries	Buy	1,340
TCS	Buy	2,360

MID-CAP IDEAS

Company	Rating	Target
Greenply Industries	Buy	250
L&T Infotech	Buy	2,070
Laurus Labs	Buy	495
Mayur Uniquoters	Buy	565
Mphasis	Buy	1,360

Source: BOBCAPS Research

DAILY MACRO INDICATORS

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	3.05	1bps	(2bps)	71bps
India 10Y yield (%)	7.73	2bps	(15bps)	72bps
USD/INR	70.87	(0.2)	3.5	(9.5)
Brent Crude (US\$/bbl)	60.48	2.9	(22.1)	(5.3)
Dow	24,640	1.5	(0.2)	4.6
Shanghai	2,576	(0.1)	(0.9)	(23.2)
Sensex	35,354	1.1	6.0	5.0
India FII (US\$ mn)	22 Nov	MTD	CYTD	FYTD
FII-D	149.7	1,025.0	(7,436.3)	(7,682.2)
FII-E	237.8	281.5	(5,476.7)	(7,602.2)

Source: Bank of Baroda Economics Research

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REDUCE

TP: Rs 1,080 | ▲ 0%

ECLERX SERVICES

| IT Services

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Possibility of double-digit growth in FY20E: After three years of weak growth through FY17 to FY19, management alluded to possible double-digit growth in FY20 on receding client-specific challenges and healthy deal wins. We estimate US\$ revenue growth of 2.7%/11.5%/12.6% for FY19/FY20/FY21.

Onsite revenue mix to trend up: In bid to move closer to clients, ECLX continues to invest in enhancing onsite delivery capabilities. Over the last 12 months, its onsite revenues increased by ~50% YoY vs. a 3.6% YoY decline in offshore revenues. Amid a fluid demand environment and onsite delivery scale-up, we expect a steady increase in the company's onsite revenue mix (from 22% in H1FY19), altering the operating margin profile of the business.

Operating margins in flux: With an increasing mix of onsite revenues (a relatively lower-margin business), a higher managed service mix (mostly encompasses upfront productivity sharing), and lingering challenges in the legacy business, the outlook on operating margins stays cloudy. Management is hopeful that potential price hikes in some top 10 accounts (after a gap of two years) and a favourable hedge book (from H2FY20) will support margins. We model for modest EBIT margin gains of ~140bps to 22.6% over FY19-FY21 as revenue growth recovers.

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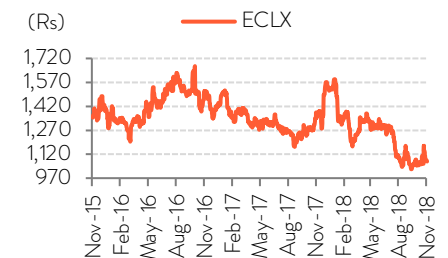
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Ticker/Price	ECLX IN/Rs 1,076
Market cap	US\$ 589.1mn
Shares o/s	39mn
3M ADV	US\$ 0.4mn
52wk high/low	Rs 1,368/Rs 1,015
Promoter/FPI/DII	50%/25%/25%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY17A	FY18A	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	3,541	2,887	2,612	2,910	3,247
Adj. EPS (Rs)	88.4	74.5	67.5	75.2	83.9
Adj. EPS growth (%)	0.5	(15.7)	(9.4)	11.4	11.6
Adj. ROAE (%)	30.8	23.6	20.3	20.8	21.4
Adj. P/E (x)	12.2	14.4	15.9	14.3	12.8
EV/EBITDA (x)	8.2	10.4	10.9	8.9	7.9

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)

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