

REDUCE

TP: Rs 1,020 | ▼ 11%

ECLERX SERVICES

IT Services

14 March 2019

Announces Rs 2.6bn buyback – a transient trigger

Event: eClerx (ECLX) has announced a buyback worth Rs 2.6bn through the tender offer route at a maximum price of Rs 1,600/sh (39.6% premium over today's closing price of Rs 1,146), translating into 1.63mn shares or 4.23% of paid up equity shares.

Financial implications: As per our calculations, this is likely to be EPS-dilutive by 0.6-0.9% but could translate into ~90bps ROE improvement.

Payout ratio: The buyback coupled with interim dividend of Re 1/sh announced in Aug'18 implies a payout ratio of ~124% (based on our estimated FY19 net profit of Rs 2.15bn) and marks an improvement over the FY18/FY17 payout ratios of ~89%/67%.

A temporary trigger: We view this development as a positive step towards efficient capital allocation. We had highlighted the possibility of a buyback as a near-term catalyst in our report '[Not out of the woods yet](#)' dated 31 Jan 2019, and the stock has already inched up ~11% in the past week in the run-up to the announcement. Nonetheless, we see this as a transient trigger in the absence of operational performance improvement (9MFY19 EBIT down 21.6% YoY).

Maintain REDUCE: We believe continued investments toward onsite delivery expansion (which has a 3-6-month lag in revenues vs. costs) and offshore revenue leakage due to roll-offs (though relatively lower than last year) will limit margin expansion, at least till H1FY20. A structural downward reset to operating margins led by a changing business mix in favour of onsite revenues precludes a constructive outlook. Reiterate REDUCE. We value the stock at an unchanged target P/E multiple of 13.5x, a 20% discount to its five-year average 12-month forward P/E due to a weaker margin and growth profile.

FIG 1 – BUYBACKS OVER FY17-FY19

Particulars	FY17	FY18	FY19
Buyback size (Rs mn)	2,340	2,580	2,620
No of equity shares (in mn)	1.17	1.29	1.63
% of equity	2.78	3.23	4.23
Buyback price (Rs per sh)	2,000	2,000	1,600
Premium over last price (%)	40.2	33.3	39.6
Date of announcement (Board meeting)	14-Oct-16	22-Dec-17	14-Mar-19

Source: Company, BOBCAPS Research

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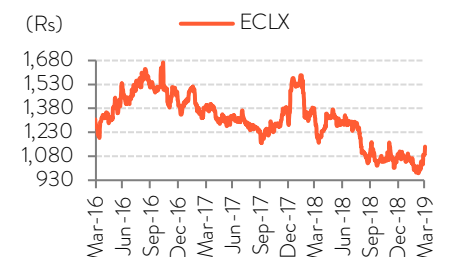
Ticker/Price	ECLX IN/Rs 1,146
Market cap	US\$ 640.3mn
Shares o/s	39mn
3M ADV	US\$ 0.3mn
52wk high/low	Rs 1,368/Rs 976
Promoter/FPI/DII	50%/25%/25%

Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19E	FY20E	FY21E
Adj. net profit (Rs mn)	2,156	2,478	2,964
Adj. EPS (Rs)	56.7	65.2	78.0
Adj. EPS growth (%)	(23.8)	14.9	19.6
Adj. ROAE (%)	16.9	18.1	20.1
Adj. P/E (x)	20.2	17.6	14.7
EV/EBITDA (x)	13.8	11.2	9.4

Source: Company, BOBCAPS Research

STOCK PERFORMANCE

Source: NSE

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

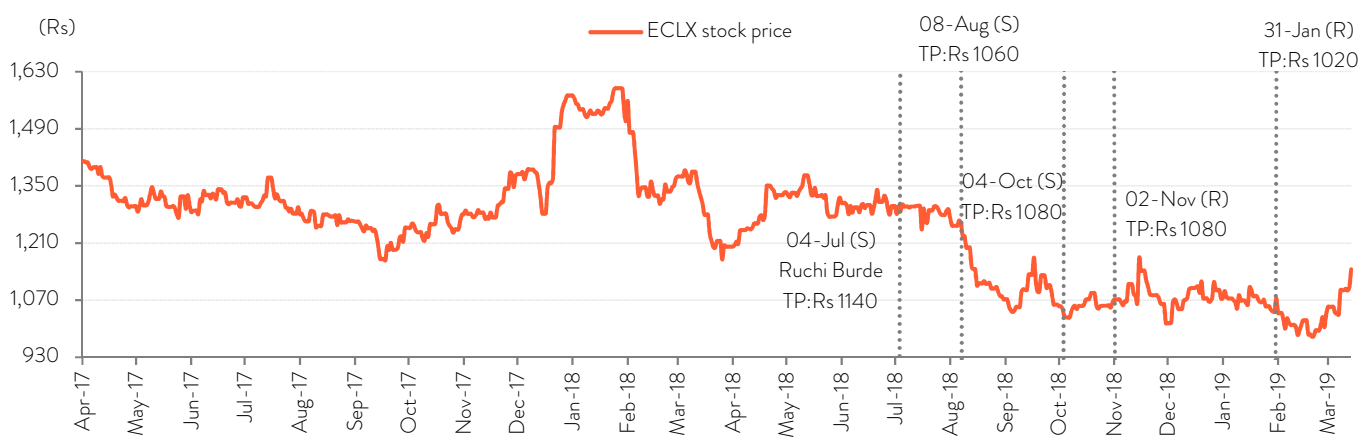
ADD – Expected return from >+5% to +15%

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)

HISTORICAL RATINGS AND TARGET PRICE: ECLERX SERVICES (ECLX IN)



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

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