

Rating: HOLD | CMP: Rs366 | TP: Rs321

October 24, 2019

Q3CY19 Result Update

Change in Estimates | Target | Reco

Change in Estimates

	Current		Previous	
	CY19E	CY20E	CY19E	CY20E
Rating	HOLD		HOLD	
Target Price	321		347	
Sales (Rs. m)	55,938	65,179	56,121	67,221
% Chng.	(0.3)	(3.0)		
EBITDA (Rs. m)	9,069	9,957	9,104	10,430
% Chng.	(0.4)	(4.5)		
EPS (Rs.)	22.9	25.1	22.4	25.2
% Chng.	1.9	(0.4)		

Key Financials - Standalone

Y/e Dec	CY18	CY19E	CY20E	CY21E
Sales (Rs. m)	46,477	55,938	65,179	73,436
EBITDA (Rs. m)	7,709	9,069	9,957	11,395
Margin (%)	16.6	16.2	15.3	15.5
PAT (Rs. m)	5,833	6,796	7,458	8,615
EPS (Rs.)	19.6	22.9	25.1	29.0
Gr. (%)	16.6	16.5	9.7	15.5
DPS (Rs.)	6.9	7.8	8.8	10.1
Yield (%)	1.9	2.1	2.4	2.8
RoE (%)	26.5	26.3	24.9	24.9
RoCE (%)	32.1	31.9	31.1	30.8
EV/Sales (x)	2.2	1.7	1.4	1.2
EV/EBITDA (x)	13.0	10.6	9.2	7.6
PE (x)	18.7	16.0	14.6	12.6
P/BV (x)	4.6	3.9	3.4	2.9

Key Data

HEXT.BO | HEXW IN

52-W High / Low	Rs.456 / Rs.294
Sensex / Nifty	39,059 / 11,604
Market Cap	Rs.109bn/ \$ 1,539m
Shares Outstanding	298m
3M Avg. Daily Value	Rs.705.5m

Shareholding Pattern (%)

Promoter's	62.45
Foreign	17.85
Domestic Institution	11.58
Public & Others	8.12
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	(2.1)	5.8	3.0
Relative	(2.0)	4.5	(10.8)

Aniket Pande

aniketpande@plindia.com | 91-22-66322300

BFS weakness to weigh on growth ahead

Quick Pointers:

- Weakness in BFS & ramp down of a large financial services client led to cut in revenue guidance to 17-18% YoY CC (earlier:19% YoY).
- Unexciting order intake of USD 28mn (-22% QoQ), net new deal wins for 9MCY19 has grown by only ~6% to USD 100 mn.

Hexaware 3QCY19 reported 12.3% QoQ CC & company did not provide organic growth composition. We estimate organic growth to be at 4% QoQ CC which below our estimates of 6.5% QoQ CC. Mubiquity acquisition contributed 7.8% or US\$14.5 mn to incremental revenues. EBIT margin came 13.9% (-76bps QoQ, -156bps YoY) Q3 margin was impacted by partial impact of wage increases (full impact in Q4) offset by lack of visa costs and INR depreciation. Management highlighted that supply side constraints in US has worsened now & now it can lead to higher wage hikes as compared to last year to retain the talent. In Q4, there will be wage hike, lower number of working days & furlough which will keep the growth & margins muted.

Hexaware's BFS segment (38% of revenue) continues to face challenge due to client-specific ramp-down. Management mentioned that weakness in vertical has spread beyond the top client. Management has cut the guidance to 17-18% YoY CC from earlier 19% YoY CC. Management change in sourcing strategy impacted revenues from a large financial services client in September 2019 quarter. This impact will continue in December 2019 quarter. New TCV deal win was weak at USD28mn.

We believe key negative for Hexaware is softness in BFS (41% of revenue) mainly focused in capital markets & buy side for new deals which have longer sales cycles. We remain watchful on expanded attrition levels of ~18% along with supply side constraints. We cut revenue estimated for CY20E by 3% which led to earnings cut of 10%. We incorporate CY21E estimates & value Hexaware on Sep-21 EPS of Rs. 23 & arrive at changed target price of Rs. 321 (valued at 14x multiple) Hexaware is currently trading at 16.4X/15.6X CY20E/21E.

- Inline revenue performance, miss on margins:** Revenue grew 11.7% QoQ to USD 210.5 mn (Ple/Cons: USD 212.3 mn/ 212.3 mn), while EBIT margin eroded 76 bps to 13.9% (Ple/Cons: 13.9%/ 14.9%). Q3 margin was impacted by partial impact of wage increases (full impact in Q4) offset by lack of visa costs and INR depreciation. Management highlighted that supply side constraints in US has worsened now & now it can lead to higher wage hikes as compared to last year to retain the talent. EBIT margin will decline on a sequential basis in the next quarter due to seasonality.
- Growth was led by manufacturing & consumer vertical:** Growth was led by strong growth in manufacturing & consumer (+19.4% QoQ), travel & transportation (+12.4% QoQ) and healthcare & insurance (11.9% QoQ). Growth was weak in financial services (8.4% QoQ). In geographic terms, Europe grew at a strong 32.3% QoQ while Americas grew 9.7% QoQ. From a service line perspective, revenue growth was led by ADM (+26.6% QoQ) and BPO (+13.1% QoQ).

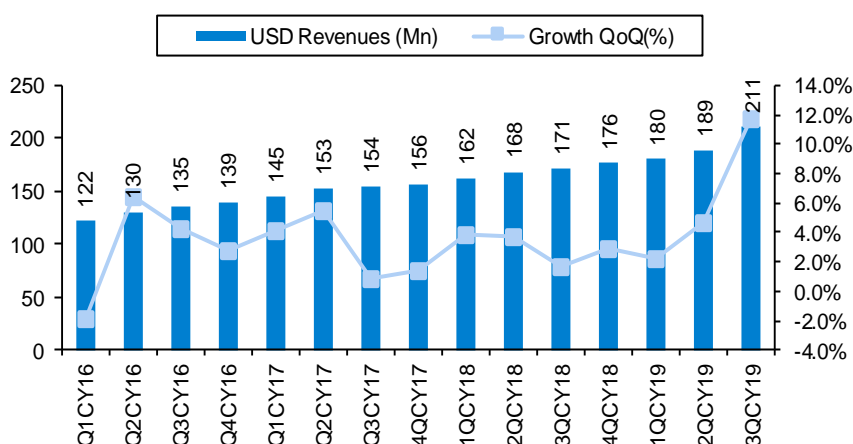
Exhibit 1: Q3CY19: Quick view on results

Y/e March (Rs mn)	Q3CY19	Q2CY19	QoQ gr.	Q3CY18	YoY gr.	PL Estimates	Variance (Actual vs Ple)
Revenues (USD mn)	210.5	189	11.7%	171	23.0%	212.7	-1.0%
Revenues (INR mn)	14,813	13,083	13.2%	12,096	22.5%	14,996	-1.2%
EBITDA	2,440	2,158	13.0%	2,117	15.2%	2,474	-1.4%
EBITDA Margins	16.5%	16.5%	-3 bps	17.5%	-103 bps	16.5%	-3 bps
EBIT	2,052	1,912	7.3%	1,864	10.1%	2,179	-5.8%
EBIT Margins	13.9%	14.6%	-76 bps	15.4%	-156 bps	14.5%	-68 bps
PAT	1,836	1,513	21.3%	1,722	6.6%	1,778	3.3%
EPS	5.0	5.0	0.0%	5.7	-12.1%	5.9	-14.9%

Source: Company, PL

Revenues came at \$210mn up 12% QoQ/23% YoY and inline with our estimates.

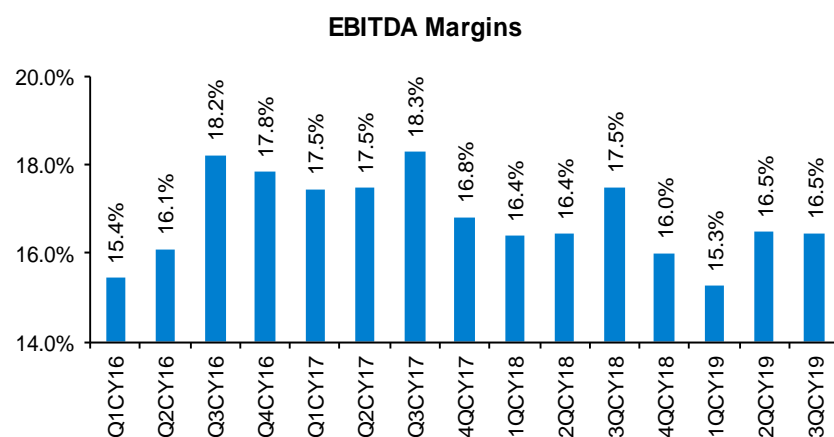
Exhibit 2: Revenue growth inline with estimates



Source: Company, PL

EBIDTA margin (excluding ESOP cost) for the quarter came at 16.5%.

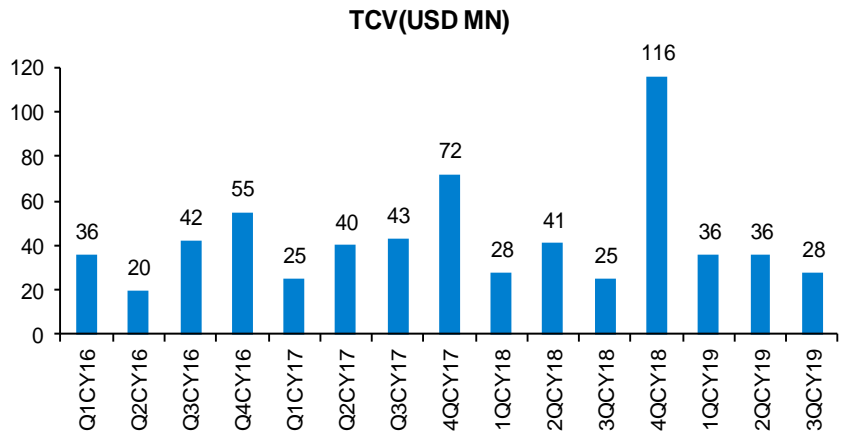
Exhibit 3: Strong beat on margins



Source: Company, PL

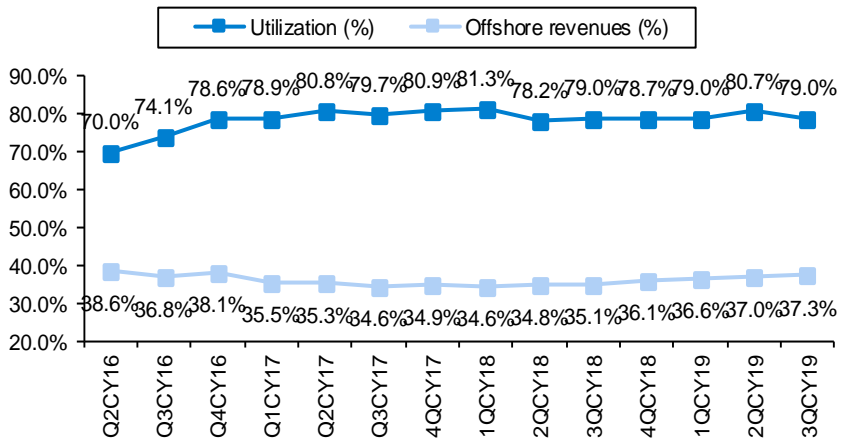
Deal signings was soft at US\$28mn

Exhibit 4: TCV back to new normal after large deal win in 4QCY18



Source: Company, PL

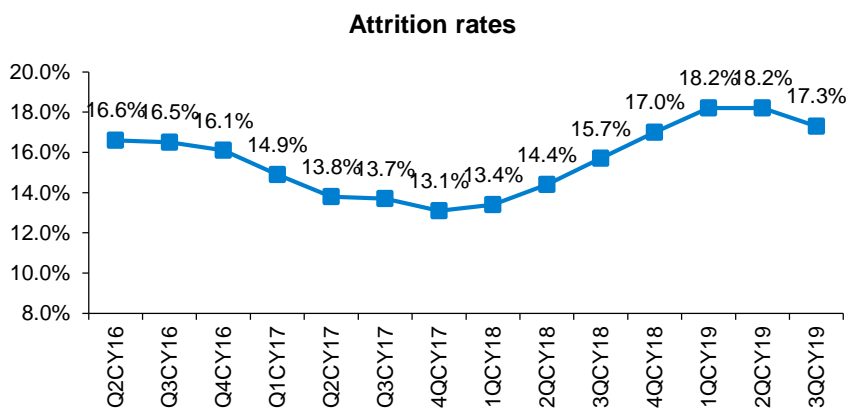
Exhibit 5: Utilization continue to remain strong



Source: Company, PL

Attrition continue to decline at 17.3%,

Exhibit 6: Attrition rate now at new normal level



Source: Company, PL

Exhibit 7: Vertical-wise revenues

USD mn	Q3CY19	Q2CY19	QoQ	Q3CY18	YoY
BFSI	81.3	75.0	8%	72.7	12%
Travel & Transportation	21.3	19.0	12%	18.0	18%
Healthcare & Insurance	40.6	36.2	12%	32.2	26%
Manufacturing, Consumer & Others	36.0	30.2	19%	25.5	41%
Professional services	31.4	28.1	12%	22.8	38%
Total	210.5	188.5	12%	171.1	23%
as a % of total					
BFSI	38.6	39.8	-120 bps	42.5	-390 bps
Travel & Transportation	10.1	10.1	0 bps	10.5	-40 bps
Healthcare & Insurance	19.3	19.2	10 bps	18.8	50 bps
Manufacturing, Consumer & Others	17.1	16.0	110 bps	14.9	220 bps
Professional services	14.9	14.9	0 bps	13.3	160 bps

Source: Company, PL

Exhibit 8: Geography-wise revenues

USD mn	Q3CY19	Q2CY19	QoQ	Q3CY18	YoY
Americas	158.7	144.8	10%	132.4	20%
Europe	34.9	26.4	32%	22.8	54%
Asia Pacific	16.8	17.3	-3%	15.9	6%
Total	210.5	188.5	0%	171.1	0%
as a % of total					
Americas	76.8	76.1	70 bps	77.0	-20 bps
Europe	14	12.6	140 bps	12.7	130 bps
Asia Pacific	9.2	11.3	-210 bps	10.3	-110 bps

Source: Company, PL

Exhibit 9: Revenue by Service-lines

USD mn	Q3CY19	Q2CY19	QoQ	Q3CY18	YoY
ADM	88.0	69.7	26%	61.6	43%
Enterprise Solutions	19.4	17.7	9%	16.6	17%
Testing / QATS (Quality)	33.0	33.4	-1%	30.3	9%
BI and Analytics	22.9	23.2	-1%	24.8	-8%
Business Process Services	17.3	15.1	14%	12.7	36%
IMS	29.9	29.4	2%	25.2	19%
Total	210.5	188.5	12%	171.1	23%
as a % of total					
ADM	41.8	37	480 bps	36	580 bps
Enterprise Solutions	9.2	9.4	-20 bps	9.7	-50 bps
Testing / QATS (Quality)	15.7	17.7	-200 bps	17.7	-200 bps
BI and Analytics	10.9	12.3	-140 bps	14.5	-360 bps
Business Process Services	8.2	8	20 bps	7.4	80 bps
IMS	14.2	15.6	-140 bps	14.7	-50 bps

Source: Company, PL

Exhibit 10: Revenue concentration from Top clients shifting

As a % of total Revenues	3QCY16	4QCY16	Q1CY17	Q2CY17	Q3CY17	Q4CY17	Q1CY18	Q2CY18	Q3CY18	Q4CY18	Q1CY19	Q2CY19	Q3CY19
Top 5 client	47.0	46.3	45.6	46.1	43.5	42.8	42.1	42.4	42.1	42.0	41.7	37.3	35.2
Top 10 clients	58.3	57.4	56.7	56.5	54.8	52.9	52.8	52.8	52.2	51.6	51.1	46.4	44.4

Source: Company, PL

Exhibit 11: Strong Capital Allocation Strategy

In Rs	3QCY16	4QCY16	Q1CY17	Q2CY17	Q3CY17	Q4CY17	Q1CY18	Q2CY18	Q3CY18	Q4CY18	Q1CY19	Q2CY19	Q3CY19
Dividend	1.0	1.0	1.0	1.0	1.0	1.0	1.0	2.5	2.5	2.5	2.5	1.5	2.0

Source: Company, PL

Exhibit 12: Client Metrics

	3QCY16	4QCY16	Q1CY17	Q2CY17	Q3CY17	Q4CY17	Q1CY18	Q2CY18	Q3CY18	Q4CY18	Q1CY19	Q2CY19	Q3CY19
1 mn	77	78	81	81	82	88	89	93	95	99	99	120	124
1 mn - 5 mn	63	64	67	66	64	71	69	71	70	72	71	85	89
5 mn - 10 mn	6	6	6	7	9	7	10	12	15	18	19	24	22
10mn -20mn	3	3	3	3	4	6	6	6	6	4	4	6	7
> USD 20 mn	5	5	5	5	5	4	4	4	4	5	5	5	6

Source: Company, PL

Exhibit 13: Headcount Metrics

Billable Personnel (IT Services +BPS)	1QCY17	2QCY17	3QCY17	4QCY17	1QCY18	2QFY18	3QCY18	4QCY18	1QCY19	2QCY19	3QCY19
Onsite	20.9%	20.9%	19.9%	19.7%	19.0%	18.8%	18.4%	19.0%	19.1%	19.2%	18.3%
Offshore	71.0%	71.2%	72.1%	72.5%	73.3%	73.7%	74.2%	73.6%	73.5%	73.2%	74.2%
Total	91.9%	92.1%	92.0%	92.2%	92.3%	92.5%	92.6%	92.6%	92.6%	92.4%	92.5%
Marketing (incl. Sales Support)	3.2%	3.3%	3.3%	3.3%	3.2%	3.0%	3.0%	3.0%	3.0%	3.0%	2.9%
Others (incl. tech Support)	4.9%	4.6%	4.7%	4.5%	4.5%	4.5%	4.4%	4.4%	4.5%	4.6%	4.6%
Grand Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.1%	100.0%	100.0%

Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Dec	CY18	CY19E	CY20E	CY21E
Net Revenues	46,477	55,938	65,179	73,436
YoY gr. (%)	17.9	20.4	16.5	12.7
Employee Cost	31,122	37,735	43,659	49,557
Gross Profit	15,355	18,203	21,520	23,879
Margin (%)	33.0	32.5	33.0	32.5
SG&A Expenses	7,646	9,134	11,563	12,484
Other Expenses	-	-	-	-
EBITDA	7,709	9,069	9,957	11,395
YoY gr. (%)	11.7	17.6	9.8	14.4
Margin (%)	16.6	16.2	15.3	15.5
Depreciation and Amortization	650	831	652	734
EBIT	7,059	8,238	9,305	10,661
Margin (%)	15.2	14.7	14.3	14.5
Net Interest	-	-	-	-
Other Income	206	31	(180)	(120)
Profit Before Tax	7,265	8,268	9,125	10,541
Margin (%)	15.6	14.8	14.0	14.4
Total Tax	1,432	1,472	1,667	1,925
Effective tax rate (%)	19.7	17.8	18.3	18.3
Profit after tax	5,833	6,796	7,458	8,615
Minority interest	-	-	-	-
Share Profit from Associate	-	-	-	-
Adjusted PAT	5,833	6,796	7,458	8,615
YoY gr. (%)	16.8	16.5	9.7	15.5
Margin (%)	12.6	12.1	11.4	11.7
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	5,833	6,796	7,458	8,615
YoY gr. (%)	16.8	16.5	9.7	15.5
Margin (%)	12.6	12.1	11.4	11.7
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	5,833	6,796	7,458	8,615
Equity Shares O/s (m)	297	297	297	297
EPS (Rs)	19.6	22.9	25.1	29.0

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Dec	CY18	CY19E	CY20E	CY21E
Non-Current Assets				
Gross Block	8,383	8,383	8,433	8,483
Tangibles	7,704	7,704	7,744	7,784
Intangibles	679	679	689	699
Acc: Dep / Amortization	4,451	5,282	5,934	6,668
Tangibles	3,877	4,625	5,276	6,011
Intangibles	574	657	657	657
Net fixed assets	3,932	3,101	2,499	1,815
Tangibles	3,828	3,080	2,468	1,774
Intangibles	105	21	31	41
Capital Work In Progress	2,244	2,244	2,244	2,244
Goodwill	1,809	1,809	1,809	1,809
Non-Current Investments	412	412	412	412
Net Deferred tax assets	1,784	1,784	1,784	1,784
Other Non-Current Assets	1,283	1,383	1,483	1,583
Current Assets				
Investments	101	101	101	101
Inventories	-	-	-	-
Trade receivables	8,031	7,663	8,929	10,060
Cash & Bank Balance	8,205	12,859	16,883	21,799
Other Current Assets	636	736	836	936
Total Assets	31,335	35,544	40,976	47,023
Equity				
Equity Share Capital	595	595	595	595
Other Equity	23,324	27,158	31,474	36,458
Total Network	23,919	27,753	32,068	37,053
Non-Current Liabilities				
Long Term borrowings	-	-	-	-
Provisions	230	240	250	260
Other non current liabilities	-	-	-	-
Current Liabilities				
ST Debt / Current of LT Debt	-	-	-	-
Trade payables	3,300	3,065	3,571	4,024
Other current liabilities	3,810	4,410	5,010	5,610
Total Equity & Liabilities	31,335	35,544	40,976	47,023

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Dec	CY18	CY19E	CY20E	CY21E
PBT	7,266	8,099	9,125	10,541
Add. Depreciation	651	831	652	734
Add. Interest	0	-	-	-
Less Financial Other Income	206	31	(180)	(120)
Add. Other	328	-	-	-
Op. profit before WC changes	8,245	8,931	9,777	11,275
Net Changes-WC	(1,166)	88	(792)	(654)
Direct tax	(1,592)	(1,472)	(1,667)	(1,925)
Net cash from Op. activities	5,487	7,546	7,317	8,696
Capital expenditures	(606)	-	(50)	(50)
Interest / Dividend Income	63	-	-	-
Others	88	(100)	(100)	(100)
Net Cash from Inv. activities	(455)	(100)	(150)	(150)
Issue of share cap. / premium	4	-	-	-
Debt changes	-	-	-	-
Dividend paid	(2,506)	(2,793)	(3,143)	(3,630)
Interest paid	0	-	-	-
Others	-	-	-	-
Net cash from Fin. activities	(2,502)	(2,793)	(3,143)	(3,630)
Net change in cash	2,530	4,654	4,025	4,915
Free Cash Flow	4,878	7,546	7,267	8,646

Source: Company Data, PL Research

Key Financial Metrics

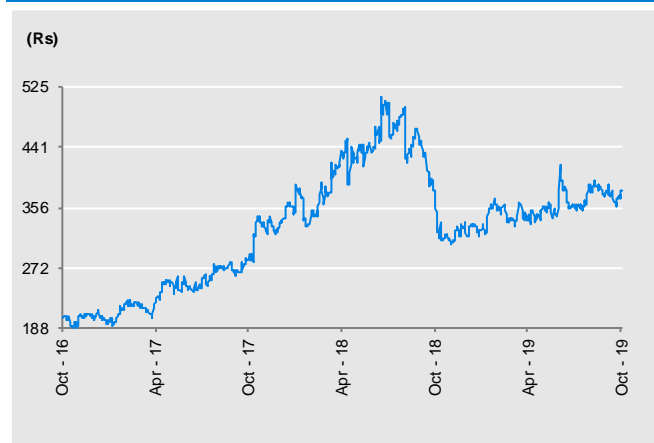
Y/e Dec	CY18	CY19E	CY20E	CY21E
Per Share(Rs)				
EPS	19.6	22.9	25.1	29.0
CEPS	21.8	25.7	27.3	31.4
BVPS	80.4	93.3	107.8	124.6
FCF	16.4	25.4	24.4	29.1
DPS	6.9	7.8	8.8	10.1
Return Ratio(%)				
RoCE	32.1	31.9	31.1	30.8
ROIC	36.3	45.8	50.4	57.5
RoE	26.5	26.3	24.9	24.9
Balance Sheet				
Net Debt : Equity (x)	(0.3)	(0.5)	(0.5)	(0.6)
Debtor (Days)	63	50	50	50
Valuation(x)				
PER	18.7	16.0	14.6	12.6
P/B	4.6	3.9	3.4	2.9
P/CEPS	16.8	14.3	13.4	11.6
EV/EBITDA	13.0	10.6	9.2	7.6
EV/Sales	2.2	1.7	1.4	1.2
Dividend Yield (%)	1.9	2.1	2.4	2.8

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Dec	Q4CY18	Q1CY19	Q2CY19	Q3CY19
Net Revenue	12,524	12,640	13,083	14,813
YoY gr. (%)	24.6	20.5	15.1	22.5
Raw Material Expenses	8,476	8,781	8,808	9,750
Gross Profit	4,048	3,859	4,275	5,063
Margin (%)	32.3	30.5	32.7	34.2
EBITDA	1,913	1,887	2,117	2,377
YoY gr. (%)	19.7	16.1	19.4	17.5
Margin (%)	15.3	14.9	16.2	16.0
Depreciation / Depletion	158	148	205	324
EBIT	1,755	1,739	1,912	2,052
Margin (%)	14.0	13.8	14.6	13.9
Net Interest	-	-	-	-
Other Income	(215)	(42)	99	171
Profit before Tax	1,540	1,697	2,011	2,223
Margin (%)	12.3	13.4	15.4	15.0
Total Tax	306	312	329	387
Effective tax rate (%)	19.9	18.4	16.4	17.4
Profit after Tax	1,234	1,385	1,682	1,836
Minority interest	-	-	-	-
Share Profit from Associates	-	-	-	-
Adjusted PAT	1,234	1,385	1,682	1,836
YoY gr. (%)	1.9	3.1	9.6	6.6
Margin (%)	9.9	11.0	12.9	12.4
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	1,234	1,385	1,682	1,836
YoY gr. (%)	1.9	3.1	9.6	6.6
Margin (%)	9.9	11.0	12.9	12.4
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	1,234	1,385	1,682	1,836
Avg. Shares O/s (m)	302	302	302	366
EPS (Rs)	4.1	4.6	5.6	5.0

Source: Company Data, PL Research

Price Chart
Recommendation History


No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	03-Oct-19	Hold	347	369
2	08-Aug-19	Hold	347	371
3	04-Jul-19	Hold	339	373
4	17-Jun-19	HOLD	339	345
5	10-Jun-19	Reduce	325	344
6	25-Apr-19	Reduce	325	333
7	05-Apr-19	Reduce	325	360
8	31-Jan-19	Accumulate	384	323
9	07-Jan-19	Accumulate	430	332
10	25-Oct-18	Accumulate	430	351

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Cyient	Hold	507	466
2	HCL Technologies	BUY	1,258	1,095
3	Hexaware Technologies	Hold	347	369
4	Infosys	Hold	819	815
5	L&T Technology Services	Hold	1,444	1,639
6	Larsen & Toubro Infotech	Accumulate	1,825	1,500
7	Mindtree	Reduce	716	744
8	Mphasis	Accumulate	1,038	937
9	NIIT Technologies	Accumulate	1,551	1,469
10	Persistent Systems	Hold	534	560
11	Redington (India)	BUY	114	108
12	Sonata Software	Accumulate	382	313
13	Tata Consultancy Services	Hold	1,985	2,004
14	TeamLease Services	Hold	3,203	2,965
15	Tech Mahindra	Reduce	619	703
16	Wipro	Reduce	245	244
17	Zensar Technologies	Accumulate	249	211

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly



ANALYST CERTIFICATION

(Indian Clients)

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