

L&T TECHNOLOGY SERVICES

IT - SERVICES

BUY

Target Price: Rs 1,305

Setting base for stronger FY19

LTTs reported strong Q3 revenue growth, ahead of estimates, up 8.4% QoQ led by strong show in Telecom-Hitech vertical (28% of rev; up 24.8% QoQ). Despite wage impact, EBITDA margin (at 15.3%) was flat QoQ led by strong cost control (employee cost down 280 bps QoQ).

Outlook – confident of 18% revenue growth in FY18 and double-digit growth in FY19: LTTs continues the strong run in FY18 and has laid the foundation for a strong FY19 as well. It has won several multi-million dollar deals across segments, which lend visibility on growth. Further, demand pipeline is healthy across key verticals of Transportation, Industrials and Telecom with positive client interactions. The T30 strategy (Top 30 clients: 67% of revenue) is seeing good momentum and outlook is healthy across these clients.

CMP : Rs 1,014
Potential Upside : 29%

MARKET DATA

No. of Shares : 102 mn
Free Float : 10%
Market Cap : Rs 104 bn
52-week High / Low : Rs 1,150 / Rs 671
Avg. Daily vol. (6mth) : 34,919 shares
Bloomberg Code : LTTs IB Equity
Promoters Holding : 90%
FII / DII : 3% / 1%

Multiple margin levers: Q3FY18 EBITDA margin at 15.3% was flat QoQ despite wage impact (~100 bps impact due to 6-7% offshore hike and 1-2% onsite). Margin headwinds exist in form of currency appreciation and lower utilization level. However, management highlighted margin levers exist in form of employee pyramid management, higher offshore mix, SG&A leverage and better pricing (client specific).

IP monetization: LTTs has 7-8 key mature solutions such as UBIQWeise™, iBEMS™, WAGES, UBIQ Data etc. in emerging technology areas, which would drive higher IP revenue. In Q3FY18, LTTs added 13 patents, taking the tally to 300, of which 228 are co-authored with clients and 72 are filed by LTTs.

T-30 strategy: LTTs has created a dedicated team to mine its Top 30 accounts, where sales and delivery teams focus on moving clients up the pyramid.

Financial summary (Consolidated)

Y/E March	FY17	FY18E	FY19E	FY20E
Sales (Rs mn)	32,483	37,114	45,423	52,862
Adj PAT (Rs mn)	4,250	4,789	5,535	6,861
Con. EPS* (Rs)	-	42	50	57
EPS (Rs)	40	46	53	65
Change YOY (%)	-	14.9	15.6	24.0
P/E (x)	25.6	22.3	19.3	15.5
RoE (%)	33.3	29.9	29.7	31.1
RoCE (%)	40.7	39.7	40.2	42.6
EV/E (x)	17.8	17.8	13.8	11.0
DPS (Rs)	7	15	17	22

Source: *Consensus broker estimates, Company, Axis Capital

Key drivers

	FY17	FY18E	FY19E	FY20E
USD rev (mn)	484	575	685	797
YoY % growth	3%	19%	19%	16%
EBITDA margin	18%	15%	16%	18%

Price performance

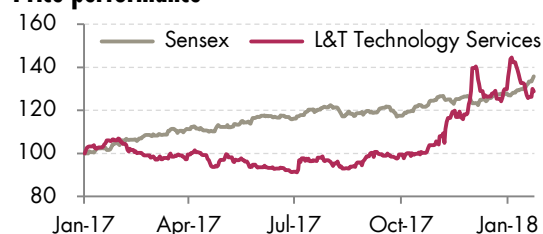


Exhibit 1: Results update

(Rs. mn)	Quarter ended					12 months ended		
	Dec-17	Dec-16	% Chg	Sep-17	% Chg	FY18E	FY17	% Chg
Net sales	9,691	8,104	19.6	9,006	7.6	37,114	32,483	14.3
EBIDTA	1,485	1,457	1.9	1,374	8.1	5,739	5,847	(1.8)
Other income	426	165	-	477	-	1,513	570	-
PBIDT	1,911	1,622	-	1,851	-	7,252	6,417	-
Depreciation	145	149	-	146	-	599	625	-
PBT	1,766	1,473	19.9	1,705	3.6	6,653	5,792	14.9
Tax	501	387	-	475	-	1,857	1,542	-
Minority Interest	3	0	-	3	-	7	0	-
Adjusted PAT	1,262	1,086	16.2	1,227	2.9	4,789	4,250	12.7
No. of shares (mn)	105	106	-	105	-	105	107	-
EBIDTA margin (%)	15.3	18.0	-	15.3	-	15.5	18.0	-
PBIDT margin (%)	19.7	20.0	-	20.6	-	19.5	19.8	-
EPS - annualized (Rs.)	48.0	41.0	17.0	46.7	2.8	45.5	39.6	14.9

Source: Company, Axis Capital

Vertical commentary

- ◆ **Transportation:** Pipeline is good driven by demand around services for autonomous vehicles and electric vehicles and growth is likely to continue in the off-highway segment as well. In aerospace, growth momentum is likely to pick up driven by good traction in in-flight entertainment and air traffic management
- ◆ **Process industry:** E&U is seeing traction aided by favorable crude prices and demand around Digitization
- ◆ **Telecom and Hi-tech:** Growth is strong led by the acquisition of Esencia which is helping LTTs participate in larger deals.

Estimates and valuation

LTTs has reported strong performance in FY18 and we expect momentum to continue driven by ramp-up of deals won during recent quarters coupled with healthy pipeline across key verticals (Transportation, Telecom-Hitech) and rebound in Process industry (momentum in CPG and favorable crude prices aiding Energy segment). We forecast ~18% USD revenue CAGR over FY18-20. EBITDA margin improvement of ~200 bps to 17.5% in FY20 will be driven by better offshore mix, employee pyramid rationalization, and operating efficiencies. **Maintain BUY** with TP of Rs 1,305 (20x FY20E), implying an upside of 29% from CMP of Rs 1,014. The stock trades at 19x/ 16x FY19E/ FY20E EPS of Rs 53/ Rs 65.

Exhibit 2: Geography performance

	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
Revenue (USD mn)	119	120	123	120	121	128	139	151
Geography Break-Up (%)								
North America	61%	64%	62%	63%	63%	65%	61%	59%
Europe	20%	20%	20%	19%	17%	17%	17%	17%
India	9%	7%	7%	8%	9%	9%	11%	12%
RoW	10%	9%	11%	10%	10%	10%	12%	13%
Revenue by Geographies								
	119	120	123	120	121	128	139	151
North America	72	76	77	75	77	82	85	89
Europe	24	24	24	23	21	21	23	26
India	11	8	9	10	11	12	15	17
RoW	11	11	13	12	12	12	17	19
QoQ change								
North America	0%	5%	0%	-2%	2%	7%	3%	5%
Europe	3%	2%	-1%	-4%	-9%	1%	9%	13%
India	18%	-26%	11%	7%	15%	7%	23%	19%
RoW	-16%	-1%	17%	-7%	1%	-1%	39%	12%

Source: Company, Axis Capital

Exhibit 3: Vertical performance

	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
Revenue (USD mn)	119	120	123	120	121	128	139	151
Vertical Break-Up (%)								
Transportation	32%	32%	33%	34%	33%	34%	32%	31%
Industrial Products	26%	26%	26%	27%	27%	26%	24%	22%
Telecom & Hi-tech	18%	19%	20%	17%	19%	20%	24%	28%
Process Industry	18%	16%	15%	16%	14%	14%	13%	13%
Medical Devices	6%	7%	7%	7%	7%	7%	7%	7%
Revenue by verticals								
	119	120	123	120	121	128	139	151
Transportation	38	39	40	41	40	43	45	47
Industrial Products	31	31	31	32	33	33	33	33
Telecom & Hi-tech	21	22	24	21	23	26	34	42
Process Industry	21	20	19	19	17	18	18	19
Medical Devices	7	8	8	8	8	9	10	10
QoQ change								
Transportation	8%	3%	5%	1%	-1%	6%	5%	4%
Industrial Products	4%	-1%	1%	2%	2%	0%	1%	0%
Telecom & Hi-tech	-11%	4%	8%	-14%	11%	12%	32%	24%
Process Industry	-4%	-7%	-5%	-1%	-8%	4%	1%	8%
Medical Devices	4%	12%	-2%	-2%	-1%	10%	11%	4%

Source: Company, Axis Capital

Exhibit 4: Clientele metrics

	Q3FY17	Q2FY18	Q3FY18
Revenue (USD mn)	120	139	151
Clientele dependence			
Top 5 Clients	23.4%	26.8%	28.8%
Top 10 Clients	35.5%	39.8%	41.2%
Top 20 Clients	51.7%	54.9%	56.4%
Remaining Clients	48.3%	45.1%	43.6%
Revenue by clients			
Top 5 Clients	28	37	43
Top 6-10 clients	15	18	19
Top 11-20 clients	19	21	23
Remaining clients	58	63	66
Total	120	139	151
Client Profile			
Active Clients	217	233	233
40 Million dollar +	0	0	1
30 Million dollar +	1	2	3
20 Million dollar +	4	4	4
10 Million dollar +	11	12	12
5 Million dollar +	29	28	30
1 Million dollar +	82	79	79

Source: Company, Axis Capital

Financial summary (Consolidated)

Profit & loss (Rs mn)

Y/E March	FY17	FY18E	FY19E	FY20E
Net sales	32,483	37,114	45,423	52,862
Other operating income	-	-	-	-
Total operating income	32,483	37,114	45,423	52,862
Total operating expenses	(5,678)	(6,910)	(8,630)	(9,779)
EBITDA	5,847	5,739	7,417	9,270
<i>EBITDA margin (%)</i>	<i>18</i>	<i>15</i>	<i>16</i>	<i>18</i>
Depreciation	(625)	(599)	(818)	(952)
EBIT	5,222	5,140	6,599	8,319
Net interest	-	-	-	-
Other income	570	1,513	1,000	1,080
Profit before tax	5,792	6,653	7,599	9,399
Total taxation	(1,542)	(1,857)	(2,052)	(2,538)
<i>Tax rate (%)</i>	<i>27</i>	<i>28</i>	<i>27</i>	<i>27</i>
Profit after tax	4,250	4,796	5,547	6,861
Minorities	-	(7)	(12)	-
Profit/ Loss associate co(s)	-	-	-	-
Adjusted net profit	4,250	4,789	5,535	6,861
<i>Adj. PAT margin (%)</i>	<i>13</i>	<i>13</i>	<i>12</i>	<i>13</i>
Net non-recurring items	-	-	-	-
Reported net profit	4,250	4,789	5,535	6,861

Balance sheet (Rs mn)

Y/E March	FY17	FY18E	FY19E	FY20E
Paid-up capital	203	203	203	203
Reserves & surplus	14,649	16,937	19,969	23,799
Net worth	14,852	17,140	20,172	24,002
Borrowing	1,019	519	-	-
Other non-current liabilities	-	-	-	-
Total liabilities	15,871	17,659	20,172	24,002
Gross fixed assets	6,138	7,649	9,153	10,907
Less: Depreciation	-	-	-	-
Net fixed assets	6,138	7,649	9,153	10,907
Add: Capital WIP	23	30	35	40
Total fixed assets	6,161	7,679	9,188	10,947
Total Investment	-	-	-	-
Debtors	7,108	8,134	9,956	11,586
Cash & bank	672	1,805	975	1,355
Loans & advances	3,555	4,067	4,978	5,793
Current liabilities	5,654	6,120	7,028	7,793
Net current assets	9,064	9,335	10,339	12,409
Other non-current assets	646	646	646	646
Total assets	15,871	17,659	20,172	24,002
-	-	-	-	-

Source: Company, Axis Capital

Cash flow (Rs mn)

Y/E March	FY17	FY18E	FY19E	FY20E
Profit before tax	5,792	6,653	7,599	9,399
Depreciation & Amortisation	625	599	818	952
<i>Chg in working capital</i>	<i>(4,387)</i>	<i>862</i>	<i>(1,833)</i>	<i>(1,690)</i>
Cash flow from operations	(82)	4,744	3,532	5,042
<i>Capital expenditure</i>	<i>(435)</i>	<i>(2,117)</i>	<i>(2,327)</i>	<i>(2,710)</i>
Cash flow from investing	(396)	(2,117)	(2,327)	(2,710)
<i>Equity raised/ (repaid)</i>	<i>697</i>	<i>(920)</i>	<i>(677)</i>	<i>(768)</i>
<i>Debt raised/ (repaid)</i>	<i>(936)</i>	<i>(500)</i>	<i>(519)</i>	-
<i>Dividend paid</i>	<i>(751)</i>	<i>(1,580)</i>	<i>(1,827)</i>	<i>(2,264)</i>
Cash flow from financing	318	(1,495)	(2,035)	(1,952)
Net chg in cash	(160)	1,133	(830)	380

Key ratios

Y/E March	FY17	FY18E	FY19E	FY20E
OPERATIONAL				
FDEPS (Rs)	40	46	53	65
CEPS (Rs)	45	51	60	74
DPS (Rs)	7	15	17	22
Dividend payout ratio (%)	18	33	33	33
GROWTH				
Net sales (%)	6	14	22	16
EBITDA (%)	13	(2)	29	25
Adj net profit (%)	2	13	16	24
FDEPS (%)	-	14.9	15.6	24.0
PERFORMANCE				
RoE (%)	33.3	29.9	29.7	31.1
RoCE (%)	40.7	39.7	40.2	42.6
EFFICIENCY				
Asset turnover (x)	2.4	2.4	2.6	2.5
Sales/ total assets (x)	1.6	1.6	1.8	1.8
Receivable days	79.9	80.0	80.0	80.0
Inventory days	-	-	-	-
Payable days	25.3	25.0	25.0	25.0
FINANCIAL STABILITY				
Total debt/ equity (x)	0.1	-	-	-
Current ratio (x)	2.6	2.5	2.5	2.6
Interest cover (x)	-	-	-	-
VALUATION				
PE (x)	25.6	22.3	19.3	15.5
EV/ EBITDA (x)	17.8	17.8	13.8	11.0
EV/ Net sales (x)	3.2	2.8	2.3	1.9
PB (x)	7.3	6.2	5.3	4.4
Dividend yield (%)	0.7	1.5	1.7	2.1

Source: Company, Axis Capital

Disclosures:

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

1. Axis Securities Ltd. (ASL) is a SEBI Registered Research Analyst having registration no. INH000000297. ASL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Depository participant services & distribution of various financial products. ASL is a subsidiary company of Axis Bank Ltd. Axis Bank Ltd. is a listed public company and one of India's largest private sector bank and has its various subsidiaries engaged in businesses of Asset management, NBFC, Merchant Banking, Trusteeship, Venture Capital, Stock Broking, the details in respect of which are available on www.axisbank.com.
2. ASL is registered with the Securities & Exchange Board of India (SEBI) for its stock broking & Depository participant business activities and with the Association of Mutual Funds of India (AMFI) for distribution of financial products and also registered with IRDA as a corporate agent for insurance business activity.
3. ASL has no material adverse disciplinary history as on the date of publication of this report.
4. I/We, authors (Research team) and the name/s subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect my/our views about the subject issuer(s) or securities. I/We also certify that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. I/we or my/our relative or ASL does not have any financial interest in the subject company. Also I/we or my/our relative or ASL or its Associates may have beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of the Research Report. Since associates of ASL are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report. I/we or my/our relative or ASL or its associates do not have any material conflict of interest. I/we have not served as director, officer or employee in the subject company.

Research Team

Sr. No	Name	Designation	E-mail
1	Hiren Trivedi	Research Associate	hiren.trivedi@axissecurities.in
2	Kiran Gawle	Associate	kiran.gawle@axissecurities.in

5. ASL or its associates has not received any compensation from the subject company in the past twelve months. ASL or its Research Analysts has not been engaged in market making activity for the subject company.

6. In the last 12-month period ending on the last day of the month immediately preceding the date of publication of this research report, ASL or any of its associates may have:

- i. Received compensation for investment banking, merchant banking or stock broking services or for any other services from the subject company of this research report and / or;
- ii. Managed or co-managed public offering of the securities from the subject company of this research report and / or;
- iii. Received compensation for products or services other than investment banking, merchant banking or stock broking services from the subject company of this research report;

ASL or any of its associates have not received compensation or other benefits from the subject company of this research report or any other third-party in connection with this report

Term & Conditions:

This report has been prepared by ASL and is meant for sole use by the recipient and not for circulation. The report and information contained herein is strictly confidential and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ASL. The report is based on the facts, figures and information that are considered true, correct, reliable and accurate. The intent of this report is not recommendatory in nature. The information is obtained from publicly available media or other sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. The report is prepared solely for informational purpose and does not constitute an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments for the clients. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ASL will not treat recipients as customers by virtue of their receiving this report.

DEFINITION OF RATINGS	
Ratings	Expected absolute returns over 12-18 months
BUY	More than 10%
HOLD	Between 10% and -10%
SELL	Less than -10%

Disclaimer:

Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to the recipient's specific circumstances. The securities and strategies discussed and opinions expressed, if any, in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient.

This report may not be taken in substitution for the exercise of independent judgment by any recipient. Each recipient of this report should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this report (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. Certain transactions, including those involving futures, options and other derivatives as well as non-investment grade securities involve substantial risk and are not suitable for all investors. ASL, its directors, analysts or employees do not take any responsibility, financial or otherwise, of the losses or the damages sustained due to the investments made or any action taken on basis of this report, including but not restricted to, fluctuation in the prices of shares and bonds, changes in the currency rates, diminution in the NAVs, reduction in the dividend or income, etc. Past performance is not necessarily a guide to future performance. Investors are advised necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ASL and its affiliated companies, their directors and employees may; (a) from time to time, have long or short position(s) in, and buy or sell the securities of the company(ies) mentioned herein or (b) be engaged in any other transaction involving such securities or earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or investment banker, lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting this document.

ASL and / or its affiliates do and seek to do business including investment banking with companies covered in its research reports. As a result, the recipients of this report should be aware that ASL may have a potential conflict of interest that may affect the objectivity of this report. Compensation of Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions. ASL may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither this report nor any copy of it may be taken or transmitted into the United State (to U.S. Persons), Canada, or Japan or distributed, directly or indirectly, in the United States or Canada or distributed or redistributed in Japan or to any resident thereof. If this report is inadvertently sent or has reached any individual in such country, especially, USA, the same may be ignored and brought to the attention of the sender. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ASL to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors.

The Disclosures of Interest Statement incorporated in this document is provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. The Company reserves the right to make modifications and alternations to this document as may be required from time to time without any prior notice. The views expressed are those of the analyst(s) and the Company may or may not subscribe to all the views expressed therein.

Copyright in this document vests with Axis Securities Limited.

Axis Securities Limited, SEBI Single Reg. No.- NSE, BSE & MSEI – INZ000161633, ARN No. 64610, CDSL-IN-DP-CDSL-693-2013, SEBI-Research Analyst Reg. No. INH 000000297, SEBI Portfolio Manager Reg. No.- INP000000654, Main/Dealing off.- Unit No. 2, Phoenix Market City, 15, LBS Road, Near Kamani Junction, Kurla (west), Mumbai-400070, Tel No. – 18002100808, Reg. off.- Axis House, 8th Floor, Wadia International Centre, Pandurang Budhkar Marg, Worli, Mumbai – 400 025. Compliance Officer: Anand Shaha, E-Mail ID: compliance.officer@axisdirect.in, Tel No: 022-42671582.