

Estimate change



TP change



Rating change



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Bloomberg	ZENT IN
Equity Shares (m)	226
M.Cap.(INRb)/(USD\$b)	32.5 / 0.4
52-Week Range (INR)	230 / 64
1, 6, 12 Rel. Per (%)	0/-9/-34
12M Avg Val (INR M)	21

Financials & Valuations (INR b)

Y/E Mar	2020	2021E	2022E
Sales	41.8	40.7	44.6
EBIT Margin (%)	8.5	10.3	10.5
PAT	2.7	3.2	3.6
EPS (INR)	11.9	14.1	16.0
EPS Gr. (%)	-17.2	18.5	13.4
BV/Sh. (INR)	92.7	104.2	116.6

Ratios

RoE (%)	13.3	14.3	14.5
RoCE (%)	15.1	15.5	15.8
Payout (%)	23.6	16.0	19.2

Valuations

P/E (x)	12.2	10.3	9.0
P/BV (x)	1.6	1.4	1.2
EV/EBITDA (x)	5.4	3.8	2.9
Div Yield (%)	1.9	1.6	2.1

Shareholding pattern (%)

As On	Jun-20	Mar-20	Jun-19
Promoter	49.2	49.2	48.9
DII	24.5	24.7	25.3
FII	16.0	17.7	17.0
Others	10.2	8.5	8.9

FII Includes depository receipts

CMP: INR144
TP: INR164 (+14%)
Neutral
Encouraging performance; Decent outlook!
Multiples should remain stable

- Zensar's better-than-expected revenue and EBIT margin in 1Q were encouraging. This was led by stronger-than-expected growth in the Hi-Tech vertical and aggressive cost rationalization. The company shared a cautiously optimistic outlook for a stable 2Q and growth in 2HFY21. Commentary around defending margins, healthy deal wins (USD150m), and a robust pipeline are other key positives.
- We upgrade our EPS estimate for FY21/FY22E by 5%/0% as we adjust our revenue growth assumptions and margin trajectory post the beat during the quarter. Maintain **Neutral**.

Better-than-expected revenue and profitability

- In 1QFY21, revenue (USD) / EBIT (INR) / PAT decreased by 15%/13%/7% YoY v/s our estimate of 17%/32%/30% YoY.
- Revenue decline of 4.8% QoQ (CC) was lower than our expectations. This was led by stronger-than-expected performance in Hi-Tech (+3.5%).
- While the Manufacturing vertical declined (4.3% QoQ, CC) in line with overall revenue, other verticals reported sharp declines.
- Across geographies, Africa remained resilient with near-flattish revenue as the US / Europe declined ~5%/8% QoQ (CC).
- Among service lines, Cloud and Infrastructure Services delivered strong growth (+8.5% QoQ, CC), led by remote work enablement, etc.
- The Top-5 (+0.9% QoQ, USD) and Top 6–10 accounts (+5.4% QoQ, USD) remained very resilient.
- The EBIT margin expanded 20bp QoQ v/s our expectation of a 180bp contraction. The optimization of direct costs (+240bp impact), SG&A expenses (+20bp impact), and INR depreciation (+40bp impact) were the key margin tailwinds. A drop in volume and utilization (-190bp impact) was the key headwind.
- Cash conversion improved, with DSO coming down by 12 days sequentially. The company's debt also came down by ~USD15m.
- The Total Contract Value of deals signed during the quarter was ~USD150m, hardly ~10% lower than the last six-quarter average run-rate.

Key highlights from management commentary

- 1Q revenue was impacted as clients ramped-down some projects as part of their immediate cost-control initiatives in response to COVID-19. Decline was pronounced in legacy/traditional projects.
- Revenue reached the trough level and is expected to stabilize in 2QFY21 and would be followed by growth in 2HFY21.
- Guidance of 15% for the EBITDA margin by 2HFY21 remains unchanged. Increased offshoring, pyramid correction, automation, and aggressive cost rationalization should be the key tailwinds.
- The USD1.5b deal pipeline (v/s USD1b in 4QFY20) remains healthy, with robust demand in Cloud and Infrastructure Services and Digital Application Services.

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

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- Across verticals, Retail is expected to stabilize by 2QFY21 and grow in 2HFY21. Zensar is reworking its value proposition within BFSI. The deal pipeline in Hi-Tech remains healthy.

Valuation and view – Multiples should remain stable

- Barring FY19 – when Zensar’s overall revenue growth (including inorganic) had come close to that of its mid-cap peers (mostly organic) – the stock has always traded at a steep discount to the sector (8–10x one-year forward P/E).
- This was largely driven by its inferior growth (organic revenue CAGR of 4% over FY15–20 v/s 12%+ for mid-cap peers), payout ratio (20%, v/s average payout of 40%), and return profile (RoE of 18% v/s 30%+ for most peers).
- On our revised estimates, the stock is trading at ~10x FY21E EPS, which is toward the higher end of its trading band. We value the stock at ~10x FY22E EPS.

Quarterly Performance

Y/E March	(INR Million)											
	FY20				FY21E				FY20	FY21E	Est.	Var.
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			1QFY21	(% / bp)
Revenue (USD m)	153	152	143	141	131	131	134	140	590	536	127	3.3
QoQ (%)	3.1	-0.7	-5.9	-1.9	-7.0	0.0	2.5	4.5	5.8	-9.1	-10.0	298bp
Revenue (INR m)	10,661	10,723	10,206	10,178	9,912	9,942	10,190	10,647	41,768	40,691	9,622	3.0
YoY (%)	20.8	13.3	-0.1	-2.8	-7.0	-7.3	-0.2	4.6	7.1	-2.6	-9.7	272bp
GPM (%)	29.4	29.1	23.6	28.9	28.8	29.0	30.0	30.0	27.8	29.5	27.8	102bp
SGA (%)	15.2	15.1	16.8	15.0	14.4	14.5	15.0	15.0	15.5	14.7	16.0	-163bp
EBITDA	1,515	1,500	696	1,416	1,430	1,442	1,527	1,602	5,127	6,001	1,133	26.2
EBITDA Margin (%)	14.2	14.0	6.8	13.9	14.4	14.5	15.0	15.0	12.3	14.7	11.8	265bp
EBIT	1,136	1,115	284	1,001	986	995	1,068	1,123	3,536	4,172	767	28.5
EBIT Margin (%)	10.7	10.4	2.8	9.8	9.9	10.0	10.5	10.5	8.5	10.3	8.0	197bp
Other income	146	181	397	161	179	215	214	215	885	822	205	-12.6
ETR (%)	28.4	28.5	25.5	27.3	26.2	26.2	26.2	26.2	27.7	26.2	27.3	
PAT	787	799	397	695	732	767	823	865	2,678	3,187	549	33.3
QoQ (%)	-9.6	1.5	-50.3	75.1	5.3	4.8	7.3	5.2			-21.0	
YoY (%)	-5.8	-16.0	-32.3	-20.1	-7.0	-4.0	107.2	24.5	-17.5	19.0	-30.2	
EPS (INR)	3.5	3.5	1.8	3.1	3.2	3.4	3.6	3.8	11.9	14.1	2.4	33.3

Key Performance Indicators

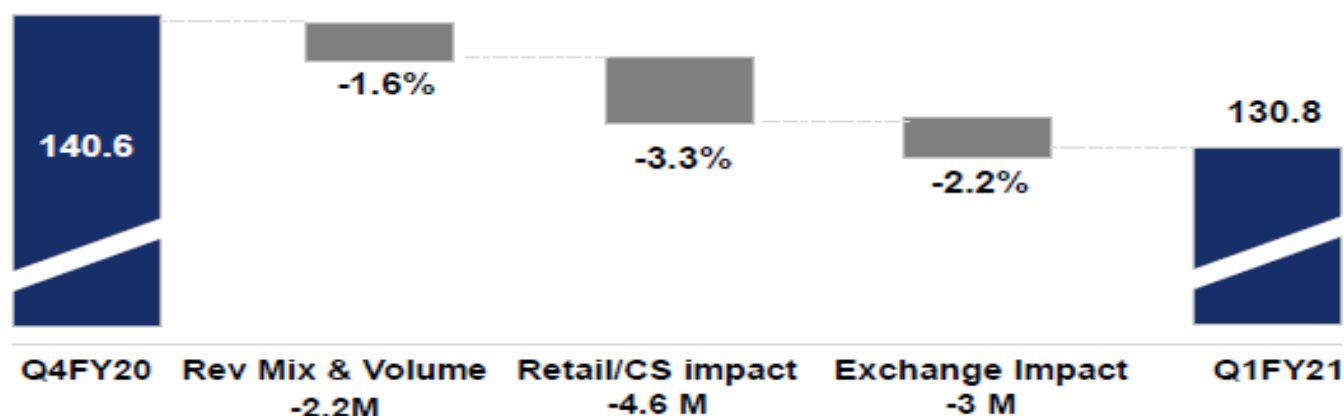
Y/E March	FY20				FY21				FY20	FY21
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q		
Revenue (QoQ CC %)	3.6	0.3	(6.4)	(1.5)	(4.8)				6.7	
Costs (% of revenue)										
COGS	70.6	70.9	76.4	71.1	71.2	71.0	70.0	70.0	72.2	70.5
Other Expenses	15.2	15.1	16.8	15.0	14.4	14.5	15.0	15.0	15.5	14.7
Margins										
Gross Margin	29.4	29.1	23.6	28.9	28.8	29.0	30.0	30.0	27.8	29.5
EBIT Margin	10.7	10.4	2.8	9.8	9.9	10.0	10.5	10.5	8.5	10.2
Net Margin	7.4	7.4	3.9	6.8	7.4	7.7	8.1	8.1	6.4	7.8
Operating metrics										
Headcount	10,166	10,219	9,951	9,524	9,027				9,524	
Attrition (%)	16.7	17.0	16.0	16.3	13.5				16.3	
Offshore Rev	31.9	33.3	32.4	35.7	35.0				35.7	
Key Verticals (YoY USD %)										
BFSI	16.5	36.4	14.5	19.2	(4.3)				21.0	
Manufacturing	23.1	14.2	9.0	0.0	(4.4)				11.0	
Retail	(11.8)	(15.3)	(31.9)	(36.3)	(45.2)				(24.0)	
Key Geographies (YoY USD %)										
North America	16.9	9.9	(2.7)	(8.6)	(15.0)				3.0	
Europe	24.1	18.0	8.6	(6.5)	(19.2)				10.0	
Africa	1.3	27.8	22.1	26.8	(4.3)				19.0	

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- The Total Contract Value of deals signed during the quarter was ~USD150m, hardly ~10% lower than the last six-quarter average run-rate.

Exhibit 1: Revenue decline led by COVID-19 impact, change in revenue mix, and exchange impact

Source: Company, MOFSL

Exhibit 2: Hi-Tech witnesses stronger-than-expected performance

Verticals	Contribution to rev (%)	Growth - QoQ (CC)
Hi-Tech	45.2	3.5
Manufacturing	12.1	-4.3
Insurance	19.4	-7.0
Banking	8.6	-12.8
Consumer Services	12.0	-20.8
Emerging	2.5	-7.5

Source: Company, MOFSL

Exhibit 3: Africa remains resilient, while US/Europe declines

Geographies	Contribution to rev (%)	Growth - QoQ (CC)
North America	73.8	-4.8
Europe	14.3	-8.1
Africa	11.9	-0.5

Source: Company, MOFSL

Exhibit 4: Strong growth in Digital Foundation Services a surprise

Verticals	Contribution to rev (%)	Growth - QoQ (CC)
Digital & Application Services (DAS)	81.6	-7.4
Digital Foundation Services (DFS)	18.4	8.5

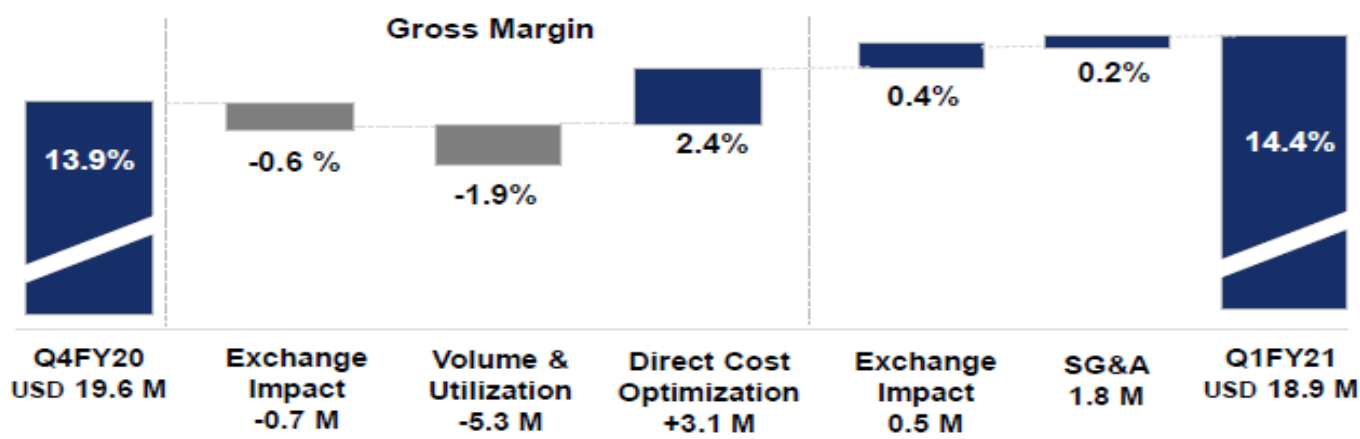
Source: Company, MOFSL

Exhibit 5: Top 5 clients flattish, but Top 6-10 drive growth

Verticals	Contribution to rev (%)	Growth - QoQ (USD)
Revenue- top 5 clients	41.2	0.9
Revenue- top 6-10 clients	10.2	5.4
Revenue- top 11-20 clients	13.8	-4.2

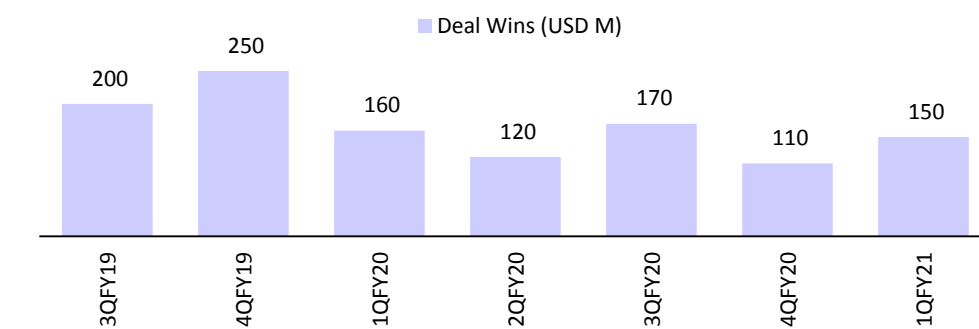
Source: Company, MOFSL

Exhibit 6: Expansion in margins largely due to cost optimization, offset by volume decline



Source: Company, MOFSL

Exhibit 7: Deal wins ~10% lower than last six-quarter average run-rate

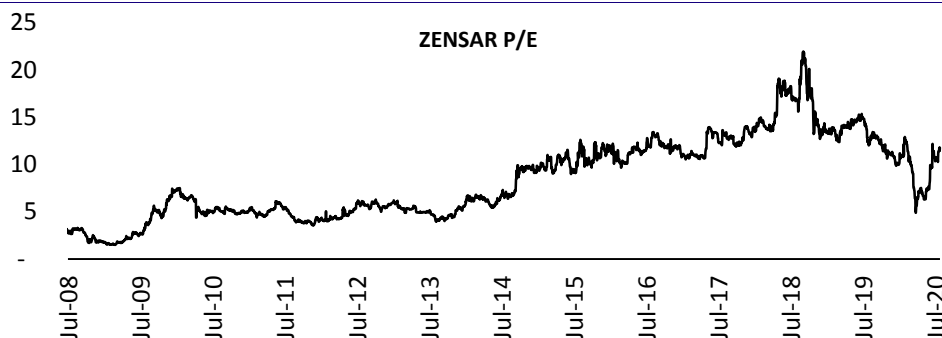


Source: Company, MOFSL

Valuation and view – Multiples should remain stable

- Barring FY19 – when Zensar’s overall revenue growth (including inorganic) had come close to that of its mid-cap peers (mostly organic) – the stock has always traded at a steep discount to the sector (8–10x one-year forward P/E).
- This was largely driven by its inferior growth (organic revenue CAGR of 4% over FY15–20 v/s 12%+ for mid-cap peers), payout ratio (20%, v/s average payout of 40%), and return profile (RoE of 18% v/s 30%+ for most peers).
- On our revised estimates, the stock is trading at ~10x FY21E EPS, which is toward the higher end of its trading band. We value the stock at ~10x FY22E EPS.

Exhibit 8: Barring FY19, stock trades at steep discount to sector and mid-cap peers



Source: Bloomberg, MOFSL

Operating metrics

Exhibit 9: Operating metrics

	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	1QFY21
Geographic Mix - %									
USA	76	76	77	77	76	74	74	74	76
Europe	14	15	15	15	15	15	16	15	14
ROW	10	9	8	8	9	11	10	11	10
Vertical Mix - %									
Manufacturing	49	52	51	51	52	53	55	54	59
Retail and consumer services	25	22	20	22	19	16	13	15	12
Financial services	24	23	26	23	24	28	29	29	27
Emerging	2	3	4	4	5	3	3	3	3
Service Mix - %									
Application Management Services	85	85	83	85	83	86	84	84	81
Infrastructure Management Services	15	15	17	15	17	14	16	16	19
Maintenance	5	5	5	4	4	4	4	4	4
Services	10	10	13	11	10	10	10	11	13
Project Type - %									
Fixed price	52	53	53	54	57	57	58	59	61
Time & material	48	47	47	46	43	43	43	41	39
Revenue by delivery - %									
Onsite	64	66	67	67	68	67	68	64	65
Offshore	36	34	33	33	32	33	32	36	35
Client concentration - %									
Top 5	38	38	39	37	38	38	40	38	41
Top 6-10	8	9	10	11	11	10	10	9	10
Top 10	46	47	50	48	49	48	49	47	51
Top 11-20	11	11	11	11	12	15	14	13	14
Top 20	57	58	60	59	61	63	64	60	65
Number of million-dollar clients									
1 Million dollar +	86	94	96	90	91	93	92	87	85
5 Million dollar +	19	20	20	19	20	23	24	24	24
10 Million dollar +	5	7	7	9	9	9	10	10	9
20 Million dollar +	2	2	2	2	2	2	2	2	2
Client metrics									
Number of active clients	246	280	279	285	308	309	308	283	252
Employee metrics									
Total headcount	8,790	9,138	9,456	9,748	10,166	10,219	9,951	9,524	9,027
Gross employees added during the period	724	906	1,045	10	1,279	977	608	463	229
Net employees added during the period	(115)	348	318	292	418	471	(215)	(695)	(497)
Utilization	84	86	83	82	83	83	82	84	81
Attrition	19	17	17	16	17	17	16	16	14

Source: Company, MOFSL

Financials and valuations

Income Statement							(INR m)	
Y/E March	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
Sales	26,277	29,643	30,556	30,058	38,988	41,768	40,691	44,555
Change (%)	13.5	12.8	3.1	(1.6)	29.7	7.1	(2.6)	9.5
Cost of Services	18,329	20,366	21,603	21,220	27,626	30,160	28,699	31,410
SG&A Expenses	4,307	5,015	5,135	5,254	6,283	6,481	5,991	6,460
EBITDA	3,641	4,262	3,819	3,583	5,079	5,127	6,001	6,685
% of Net Sales	13.9	14.4	12.5	11.9	13.0	12.3	14.7	15.0
Depreciation	415	454	486	651	894	1,591	1,829	2,005
Interest	112	106	88	227	373	605	592	613
Other Income	364	181	220	202	503	436	450	484
Forex	181	407	21	463	290	449	372	428
PBT	3,659	4,289	3,487	3,370	4,605	3,816	4,403	4,979
Tax	1,013	1,169	1,103	1,013	1,310	1,057	1,152	1,303
Rate (%)	27.7	27.3	31.6	30.1	28.5	27.7	26.2	26.2
Minority Interest	-1	-26	-35	-50	-51	-81	-64	-64
PAT	2,646	3,094	2,349	2,306	3,244	2,678	3,187	3,613
Extraordinary	0	0	0	0	0	0	0	0
Net Income	2,646	3,094	2,349	2,306	3,244	2,678	3,187	3,613
Change (%)	11.4	17.0	-24.1	-1.8	40.6	-17.5	19.0	13.4

Balance Sheet							(INR m)	
Y/E March	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
Share Capital	2,217	2,232	2,244	450	450	451	451	451
Reserves	9,353	10,420	12,461	16,239	18,973	20,449	23,030	25,821
Net Worth	11,570	12,651	14,705	16,689	19,424	20,900	23,481	26,272
Minority Interest	12	39	74	137	170	237	237	237
Loan	1,396	1,967	2,049	838	3,353	6,657	6,657	6,657
Capital Employed	12,977	14,658	16,828	17,664	22,946	27,794	30,375	33,166
Applications								
Gross Block	8,201	1,884	2,490	2,508	3,052	4,179	5,179	6,179
Less : Depreciation	-2,728	-710	-1,175	-1,654	-1,921	-2,885	-4,714	-6,719
Net Block	5,474	1,174	1,315	854	1,131	1,294	465	-540
CWIP	14	2	10	23	56	18	18	18
Other LT Assets	617	3,653	4,970	7,305	10,433	14,067	14,119	14,171
Curr. Assets	11,240	13,861	14,732	14,782	19,278	20,576	25,090	29,642
Current Investments	931	1,078	1,467	1,302	454	2,670	2,770	2,870
Inventories	1,226	1,259	1,127	1,060	985	941	917	1,004
Debtors	4,539	5,400	5,327	6,423	8,762	6,656	6,485	7,101
Cash & Bank Balance	1,960	2,769	3,291	2,069	3,259	5,166	9,775	13,525
Loans & Advances	880	0	0	0	0	0	0	0
Other Current Assets	1,704	3,354	3,521	3,929	5,819	5,143	5,143	5,143
Current Liab. & Prov	4,368	4,032	4,199	5,301	7,951	8,162	9,318	10,126
Current Liabilities	1,305	1,826	2,061	1,839	3,010	2,650	3,049	3,328
Other liabilities	2,426	2,184	2,138	3,461	4,941	5,512	6,269	6,798
Provisions	637	22	0	0	0	0	0	0
Net Current Assets	6,872	9,829	10,533	9,481	11,327	12,414	15,772	19,516
Application of Funds	12,977	14,658	16,828	17,664	22,946	27,794	30,374	33,165

Financials and valuations

Ratios

Y/E March	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
Basic (INR)								
EPS	12.2	13.6	10.4	10.2	14.4	11.9	14.1	16.0
Cash EPS	14.1	15.6	12.6	13.1	18.3	18.9	22.3	24.9
Book Value	53.3	55.8	65.2	74.0	85.9	92.7	104.2	116.6
DPS	2.2	2.4	2.4	2.2	2.8	2.8	2.2	3.1
Payout %	18.4	17.6	23.0	21.5	19.5	23.6	16.0	19.2
Valuation (x)								
P/E	11.9	10.6	13.9	14.1	10.1	12.2	10.3	9.0
Cash P/E	10.8	8.5	6.9	9.7	8.8	4.2	2.6	2.0
EV/EBITDA	8.1	7.1	7.6	8.2	6.2	5.4	3.8	2.9
EV/Sales	1.1	1.0	1.0	1.0	0.8	0.7	0.6	0.4
Price/Book Value	2.7	2.6	2.2	2.0	1.7	1.6	1.4	1.2
Dividend Yield (%)	1.5	1.7	1.7	1.5	1.9	1.9	1.6	2.1
Profitability Ratios (%)								
RoE	25.2	25.6	17.2	14.7	18.0	13.3	14.3	14.5
RoCE	28.6	30.2	23.2	17.7	21.4	15.1	15.5	15.8
RoIC	25.1	26.5	19.9	15.6	17.9	13.1	16.3	20.0
Turnover Ratios								
Debtors (Days)	86	95	94	78	82	58	58	58
Fixed Asset Turnover (x)	4.8	25.2	23.2	30.0	38.0	32.3	87.5	(82.5)

Cash Flow Statement

Y/E March	FY15	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E
(INR m)								
CF from Operations	2,823	3,805	3,354	3,444	4,182	4,345	5,594	6,217
Cash for Working Capital	382	-1,218	-281	-1,385	-2,622	1,884	1,302	5,665
Net Operating CF	3,206	2,587	3,073	2,059	1,560	6,229	6,896	11,882
Net Purchase of FA	-372	-423	-349	-515	-524	-782	-1,000	-1,000
Free Cash Flow	2,834	2,164	2,724	1,544	1,036	5,447	5,896	10,882
Net Purchase of Invest.	-1,448	1	-1,538	-1,050	-1,887	-2,371	-104	-104
Net Cash from Invest.	-1,819	-422	-1,887	-1,565	-2,411	-3,153	-1,104	-1,104
Proc. from equity issues	62	42	46	26	14	15	0	0
Proceeds from LTB/STB	-395	-375	-286	-1,440	2,628	-152	-592	-613
Dividend Payments	-542	-969	-261	-626	-633	-1,197	-592	-808
Cash Flow from Fin.	-874	-1,302	-501	-2,040	2,009	-1,335	-1,184	-1,421
Exchange difference	0	-54	-162	148	124	4	284	-5,323
Net Cash Flow	512	809	523	-1,398	1,282	1,746	4,892	4,034
Opening Cash Bal.	1,448	1,960	2,769	3,254	1,856	3,138	4,883	9,491
Add: Net Cash	512	809	523	-1,398	1,282	1,746	4,892	4,034
Closing Cash Bal.	1,960	2,769	3,292	1,856	3,138	4,883	9,775	13,525

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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