

Strong Quarter ,But high valuation likely to cap the upside

CMP: Rs 1749

Rating: Hold

Target Price: Rs 1872

Stock Info

BSE	532541
NSE	LTTS
Bloomberg	LTTS IN
Reuters	LTECH.BO
Sector	Computers-Software
Face Value (Rs)	2
Equity Capital (Rs mn)	209
Mkt Cap (Rs mn)	183425
52w H/L (Rs)	1,879 / 995
Avg Yearly Vol (in 000')	7.84

Shareholding Pattern %

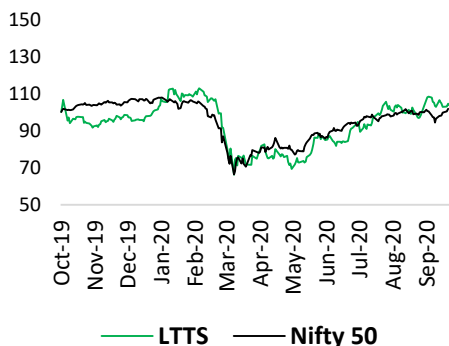
(As on September, 2020)

Promoters	74.36
FII	7.97
DII	5.83
Public & Others	11.84

Stock Performance (%)

	3m	6m	12m
LTTS	21.9	48.5	18.4
Nifty	6.8	28.1	2.6

LTTS Vs Nifty



L&T Technology Services' (LTTS) Q2FY21 earnings were mixed. Consolidated revenue stood at Rs 13,138 Mn, below our estimate of Rs 13,993 Mn, registering a de-growth of 6.3% YoY and muted growth of 1.5% QoQ. Reported EBITDA was down by 17.8% YoY but grew by 13.1% QoQ to Rs 2,328 Mn, above our estimate of Rs 1745 Mn, while EBITDA margin contracted by 248bps YoY but expanded by 182bps QoQ to 17.7% in Q2FY21. EBIT margins was up 161bps QoQ TO 13.7% in Q2FY21.. EBIT margins during the quarter improved primarily due to increase in utilization PAT for Q2FY21 declined by 19.6% YoY but rose by 41.2% QoQ to Rs 1,655 Mn, above our estimate of Rs 1407 Mn.

Business Highlights – Q2FY21

- LTTS reported constant currency revenue growth of 2.9% QoQ.in Q2FY21. All three impacted segments during Q1FY21 - Industrial Products, Transportation and Plant Engineering showed strong growth recovery in Q2 up 4.6%/4.1%/8.1% sequentially in dollar terms..
- Deal wins continue to remain strong with LTTS winning 8 multi-million dollar deals which includes 3 deals with TCV of USD15mn plus and another 3 deals with TCV of USD10mn plus.
- Company has upgraded guidance led by cross currency tailwind and improved business visibility. LTTS upgraded FY21 revenue guidance to 7-8% from 9-10% decline in USD terms; increase of 200 bps. Company expects growth momentum to continue helped by steady order bookings and a healthy pipeline across all segments.
- Revenue from top 10 clients declined by 0.8% QoQ in USD terms while revenue excluding top 20 clients increased by 7.8% QoQ. Employees count decreased by 4.4% QoQ to 15,902 Attrition reduced 60 bps QoQ to 10.8.
- All verticals except Telecom & Hi-tech (down 0.6% QoQ in USD terms) were up, Transportation (up 4.1% QoQ), Industrial Products (up 4.6%), and Plant Engineering (up 8.1%). Medical Devices continues to report healthy growth at 7.4% QoQ. Broad-based growth across geographies led by RoW, up 10.8% QoQ in USD terms followed by India (up 8.5%), Europe (up 4.1%) and North America (up 2.1%).

Outlook & Valuations

Company had a strong Q2FY21 with broad based revenue growth and an improvement in operating margin performance on QoQ basis which was in line with guidance given by company earlier. Steady order bookings and a healthy pipeline across all segments gives us confidence that the growth momentum will continue. Customers are accelerating the deployment of digital engineering projects to enable business continuity and drive scale. LTTS with its highly differentiated skillsets in Plant Engineering is thus rightly positioned to provide solutions around virtualization, 3D Modelling and digital twin, that allows it to partner with customers on transformational programs which will benefit company.. At CMP of Rs 1749, LTTS currently trades at P/E of 22x. To its FY20 EPS of Rs 78 .We like the company considering company's ability to win large deals and deep engineering expertise however high valuations is likely to cap the upside. Thus We value LTTS at P/E of 26x to its FY22E EPS , which yields target price of Rs 1872 per share and **assign Hold rating on the stock.**

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Q2 FY21 - Quarterly Performance (Consolidated)

Particulars (in Rs million)	Q2FY21	Q1FY21	Q2FY20	Y-o-Y	Q-o-Q
Revenue (USD)	178	171	198	-10.0%	4.1%
Net Revenue	13,138	12,947	14,021	-6.3%	1.5%
Employee cost	8,161	8,337	8,228	-0.8%	-2.1%
Other Expenses	2,649	2,551	2,961	-10.5%	3.8%
EBITDA	2,328	2,059	2,832	-17.8%	13.1%
<i>EBITDA margin %</i>	<i>17.7%</i>	<i>15.9%</i>	<i>20.2%</i>	<i>-248bps</i>	<i>182bps</i>
Other Income	566	137	469	20.7%	313.1%
Depreciation	527	492	444	18.7%	7.1%
EBIT	1,801	1,567	2,388	-24.6%	14.9%
<i>EBIT margin %</i>	<i>13.7%</i>	<i>12.1%</i>	<i>17.0%</i>	<i>-332bps</i>	<i>161bps</i>
Finance costs	109	107	91	19.8%	1.9%
PBT	2,258	1,597	2,766	-18.4%	41.4%
Tax Expense	595	417	704	-15.5%	42.7%
<i>Effective tax rate %</i>	<i>26.4%</i>	<i>26.1%</i>	<i>25.5%</i>	<i>90bps</i>	<i>24bps</i>
PAT	1,663	1,180	2,062	-19.4%	40.9%
Extraordinary Items (Net of tax expense)	-	-	-		
Reported PAT	1,663	1,180	2,062	-19.4%	40.9%
<i>PAT margin %</i>	<i>12.7%</i>	<i>9.1%</i>	<i>14.7%</i>	<i>-205bps</i>	<i>354bps</i>
<i>Minority Interest</i>	<i>-8</i>	<i>-8</i>	<i>-4</i>		
PAT (After MI)	1,655	1,172	2,058	-19.6%	41.2%
EPS (Rs)	15.7	11.1	19.5		

Source: Arianth Research, Company Filings, Ace Equity, Bloomberg

Q2FY21 Concall Highlights

- Utilization including trainees bounced back to 75.4%, up 450bps QoQ. Cash Flow and EPS growth was aided by INR400mn export incentives from the government. The YTD FCF stood at Rs 634 crores in Q2FY21 which is 224% of Net Income.
- Company has declared an interim dividend of INR7.5/share
- Billed DSO reduced from 74days in Q1FY21 to 72 days in Q2FY21. Whereas the unbilled DSO reduced from 22 days in Q1 to 20 days in Q2. Combined DSO stands at 92 days which was below their target range of 95 days which shows an improvement in DSO.
- Company now owns 8 deals across all segments out of which 3 deals are of 15 million plus and 3 deals are of 10 millions plus.
- It has been a tough quarter for the telecom sector mainly due to the delay in decision making. However, Company see a good pickup in growth for the Q3FY21.
- 49% share of revenue is from leading technology and digital engineering.
- Segment wise : In the transportation sector, company has opened a deal with a European tier 1 company, 2 deals with 2 different north American companies, Company is also working on additional convergence across this stage on 6 deals. In the industrial product sector, they've closed one OEM and are opening on 2 other OEM's with the digitalization of their product. Continued growth is expected. In the high-tech sector, large deals are awaited. In the plant and engineering sector, they've closed 3 new deals in speciality chemicals, oil & gas and CPG program. In the medical sector, they've closed 2 deals in area of digital health.
- Client program showed an improvement in the 20m+ category from 4 to 5. And in the 1m+ category from 113 to 116 on YOY basis.
- At the end of the second quarter, the patents portfolio of L&T Technology Services stood at 550, out of which 404 are co-authored with its customers and the rest are filed by LTTS.

Key Financials

Income Statement (Rs Mn)

Year End-March	FY19	FY20	FY21E	FY22E
Revenue (CC Terms) (Mn USD)	723	786	716	773
Growth (%)	24.6%	8.7%	-8.9%	7.9%
Revenues	50,783	56,191	54,927	61,325
<i>Change (%)</i>	35.5%	10.6%	-2.2%	11.6%
Employee Costs	30,318	32,916	34,891	36,984
Other Expenses	11,307	12,170	11,974	13,369
Total Expenses	41,625	45,086	46,865	50,353
EBITDA	9,158	11,105	8,062	10,972
Other Income	2,228	2,091	2,133	2,175
Depreciation	1,042	1,829	2,060	2,557
Interest	19	365	150	157
PBT	10,325	11,002	7,986	10,433
Tax	2,630	2,778	2,008	2,624
<i>Rate (%)</i>	25.5%	25.3%	25.2%	25.2%
PAT	7,695	8,224	5,977	7,809
Consolidated PAT	7,695	8,224	5,977	7,809
<i>Change (%)</i>	50.3%	6.9%	-27.3%	30.6%

Key Ratios

Year End-March	FY19	FY20	FY21E	FY22E
Per Share (Rs)				
EPS	73.9	77.9	55.8	71.9
CEPS	83.9	95.2	75.0	95.4
BVPS	1193	1328	1546	1850
DPS	21.0	13.5	13.5	13.5
Valuation (x)				
P/E	24	22	31	24
P/CEPS	21	18	23	18
P/BV	7	7	6	5
EV/EBITDA	16	13	17	12
Return Ratio (%)				
EBIDTA Margin	18.0%	19.8%	14.7%	17.9%
PAT Margin	15.1%	14.6%	10.9%	12.7%
ROE	31.0%	29.6%	18.5%	20.2%
ROCE	24.3%	25.0%	13.9%	16.3%
Dividend Yield	1.5%	1.0%	1.0%	1.0%
Leverage Ratio (%)				
Net Debt/Equity (x)	-0.1	-0.1	-0.3	-0.2
Net Debt/EBITDA (x)	-0.1	-0.2	-1.1	-0.7
Turnover Ratios				
Asset Turnover (x)	37.7	31.7	24.2	23.0
Receivable Days	73	79	79	79
Payable days	13	12	12	12

Balance Sheet (Rs Mn)

Year End-March	FY19	FY20	FY21E	FY22E
Sources of Funds				
Share Capital	208	209	209	209
Reserves & Surplus	24,583	27,477	32,029	38,392
Non-controlling interest	31	69	69	69
Net Worth	24,822	27,755	32,307	38,670
Non-Current liabilities				
Lease liability		3,961	3,961	3,961
Other financial liabilities	60	1,622	44	49
Deferred tax liabilities (net)	134	0	86	112
Short-term borrowings	702	303	296	331
Trade payables	1,879	1,975	1,792	2,414
Other financial liabilities	2,750	3,059	2,739	2,712
Other current liabilities	1,899	2,376	2,323	2,593
Provisions	1,341	1,654	1,617	1,805
Current tax liabilities (net)	56	328	0	0
Total Current liabilities	8,627	9,695	8,767	9,855
Total liabilities	8,821	15,278	12,857	13,976
Total Equity and liabilities	33,643	43,033	45,164	52,647
Assets				
Non-Current assets				
Fixed Assets	7,800	11,822	11,923	12,684
Goodwill on consolidation	0	0	0	0
Investments		310		
Financial assets	1,362	827	808	903
Deferred tax assets (net)	126	311	304	339
Other non-current assets	635	661	674	688
Total Non-current Assets	9,923	13,931	13,710	14,614
Current Assets				
Investments	5,749	6,110	5,973	6,668
Trade receivables	10,643	13,807	10,300	16,615
Cash and cash equivalents	2,048	2,179	9,023	7,898
Other bank balances	3	260	66	66
Loans	0	1	1	1
Other financial assets	1,541	1,730	1,698	1,878
Other current assets	3,736	5,015	4,394	4,906
Total current assets	23,720	29,102	31,455	38,033
TOTAL ASSETS	33,643	43,033	45,164	52,647

Cash Flow Statement (Rs Mn)

Year End-March	FY19	FY20	FY21E	FY22E
Net Profit before Tax	10,314	11,002	7,986	10,433
Adjustments:				
Depreciation	1,042	1,829	2,060	2,557
Finance Costs	19	365	150	157
Interest and Dividend received	49	-934	-180	-201
Operating Profit before WC Changes	11,424	12,262	10,015	12,946
Adjustments to WC				
Operating Profit after WC Changes	10,870	8,500	13,340	7,253
Direct Taxes Paid & Exceptional Items	-2,808	-2,119	-2,008	-2,624
Cash Flow from Operating Activities	8,062	6,381	11,331	4,629
Cash Flow from Investing Activities	-5,093	-2,222	-2,859	-4,186
Cash Flow from Financing Activities	-2,454	-4,060	-1,582	-1,568
Net Change in Cash & Cash Equivalents	515	99	6,890	-1,125
Opening Cash & Cash Equivalents	1,519	2,034	2,133	9,023
Closing Cash & Cash Equivalents	2034	2133	9023	7898

Source: Arihant Research, Company Filings, Ace Equity, Bloomberg

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Stock Rating Scale	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	-5% to -12%
SELL	<-12%

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