

Buy

Results inline, qualitative wins fortify acceleration hopes

- OFSS reported inline results with a revenue growth of 3% YoY at Rs 11.9bn (below DE at Rs12.5bn). OPM for the quarter stood at 46% up 360bps YoY (down on QoQ basis), as cost efficiency gets further deep. EBIT and PAT were in line at Rs 5.5bn (DE Rs5.5) and Rs3.9bn (DE 3.9bn).
- OFSS signed new Licences worth US\$13.4mn in line with our estimates (\$12mn in Q2FY20) that included 13 new deals across including 4 in developed markets (refer Exhibit 6) and also witnessed 18 go-lives in Q2.
- Improved deal momentum led by Digital acceleration theme (Banks investing both on creating digital channels as well as towards innovative credit initiatives across globe), significant savings on cost due to remote operations (H1 EBIT margins up 338bps) could extend the overall earnings momentum significantly hereon.
- Global leadership in underpenetrated CBS business, unmatched access, superior technology, integrated & reliable offering would ensure that OFSS emerge as most preferred vendor in the segment. Superior pricing and brand appeal would mean stronger profitability, improved cash generation (FCF Yield 5%+) and generous pay-outs. We continue to maintain OFSS as our preferred pick with Buy rating on the stock with DCF based TP of Rs 4,000 (implies 17x on FY23E PER).

Signed \$13.4mn in Licences; won 13 comprehensive new deals

OFSS added 13 new deals that included 41 different product modules being sold across Geographies (3 deals in UK – includes a Fintech as well as Underwriter Group) and product offerings – 10 Universal Banking, 8 Digital Experience and 17 Enterprise/Payments deals. The demand for Implementation (down 2.2% in H1) continued to slide as it completed go-lives on some 18 projects during the quarter. While AMC were up 13% on YoY (2.6% QoQ), contributing about ~32% of revenues. Overall Product revenues were up 4% on YoY basis at Rs10.6bn (88% of revenues), while services business witnessed revenue degrowth of about 2% YoY. OFSS reported overall EBIT margins at 46% for the quarter led by sustained cost actions as it was able to optimize by 230bps on SG&A. Gross margin declined in line with lower licence signings for the quarter (down about \$16mn on QoQ basis). We expect profitability to sustain at current levels in near future and may see some downward pressure in FY22E on cost normalisations.

Q2FY21 Result (Rs Mn)

Particulars	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)
Revenue	11,974	11,625	3.0	13,373	(10.5)
Total Expense	6,195	6,441	(3.8)	6,472	(4.3)
EBITDA	5,778	5,184	11.5	6,901	(16.3)
Depreciation	272	256	6.3	266	2.4
EBIT	5,506	4,928	11.7	6,635	(17.0)
Other Income	123	435	(71.7)	435	(71.6)
Interest	0	0		0	
EBT	5,630	5,363	5.0	7,070	(20.4)
Tax	1,709	1,775	(3.7)	2,272	(24.8)
RPAT	3,921	3,588	9.3	4,798	(18.3)
APAT	3,921	3,588	9.3	4,798	(18.3)
			(bps)		(bps)
Gross Margin (%)	53.5	54.4	(91)	59.2	(569)
EBITDA Margin (%)	48.3	44.6	366	51.6	(334)
NPM (%)	32.7	30.9	187	35.9	(314)
Tax Rate (%)	30.4	33.1	(274)	32.1	(178)
EBIT Margin (%)	46.0	42.4	359	49.6	(363)

CMP	Rs 3,145
Target / Upside	Rs 4,000 / 27%
NIFTY	11,669

Scrip Details

Equity / FV	Rs 429mn / Rs 5
Market Cap	Rs 271bn
	USD 4bn
52-week High/Low	Rs 3,400/ 1,506
Avg. Volume (no)	91,124
Bloom Code	OFSS IN

Price Performance	1M	3M	12M
Absolute (%)	3	7	(1)
Rel to NIFTY (%)	1	(1)	0

Shareholding Pattern

	Mar'20	Jun'20	Sep'20
Promoters	73.4	73.4	73.3
MF/Banks/FIs	6.3	6.4	7.0
FIIIs	13.5	13.2	12.4
Public / Others	6.8	7.0	7.3

Valuation (x)

	FY21E	FY22E	FY23E
P/E	15.7	14.5	13.2
EV/EBITDA	9.1	8.6	7.6
ROE (%)	26.3	28.0	29.6
RoACE (%)	24.4	26.0	27.5

Estimates (Rs mn)

	FY21E	FY22E	FY23E
Revenue	51,821	57,606	63,860
EBITDA	25,406	26,870	29,786
PAT	17,267	18,647	20,473
EPS (Rs.)	200.8	216.8	238.1

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Exhibit 1: Quarterly performance versus estimates

(Rs mn)	Actual	Estimates		% Variation		Comment
		Dolat	Consensus	Dolat	Consensus	
Revenues (Rs mn)	11,974	12,567	12,163	(4.7)	(1.6)	Weak Services revenues led to weak revenue performance
EBIT	5,506	5,446	4,811	1.1	14.5	Sustained cost actions led to further OPM gains of about 260bps ahead of our estimates.
EBIT, margin	46.0%	43.3%	39.6%	260 bps	640 bps	
PAT	3,921	3,913	3,948	0.2	(0.7)	PAT was largely inline with estimates

Source: DART, Company

Change in Estimates

Given its inline results we have kept our growth and profitability largely unchanged and on net basis upgraded our earnings estimates by 1.5%/2.9% for FY21/22E respectively. We have also introduced our FY23E estimates that factors in growth of about 11% in revenues and stable EBIT margins at 44.8% on YoY basis.

The estimates are conservative given the overall uncertainty. However, we see strong sentiments towards investments in the BFSI sector as evident from order bookings for OFSS as well as commentaries from its Software/Services peers.

Exhibit 2: Change in Estimates

(Rs mn, except EPS)	FY20A		FY21E		FY22E			FY23E
	Actual	Old	New	Change (%)	Old	New	Change (%)	New
Revenues (\$ mn)	685	708	702	(0.9)	761	758	(0.4)	840
YoY growth (%)	(2.0)	3.4	2.5		7.5	7.9		10.9
INR Revenue	48,613	52,618	51,821	(1.5)	57,865	57,606	(0.4)	63,860
EBIT	21,223	23,741	24,348	2.6	25,339	25,780	1.7	28,641
EBIT margin (%)	43.7	45.1	47.0		43.8	44.8		44.8
PAT	14,622	17,063	17,267	1.2	18,164	18,647	2.7	20,473
EPS (Rs)	169.7	198.0	200.8	1.4	210.8	216.8	2.9	238.1

Source: DART, Company

Exhibit 3: Key Assumptions in Our Estimates

(Rs mn)	FY20A	FY21E	FY22E	FY23E
Licence revenue signed (US\$ mn)	76.2	87.9	101.5	117.0
INR revenue growth (%)	(2.0)	6.6	11.2	10.9
EBIT, margin	43.7	47.0	44.8	44.8
EPS growth (%)	5.5	18.1	7.9	9.7
USD/INR	71.0	73.8	76.0	76.0

Source: DART, Company

Exhibit 4: Quarterly and YTD Trend

Rs mn	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	YoY (%)	QoQ (%)	YTD FY20	YTD FY21	YoY (%)
Revenues(\$ mn)	183	165	163	174	181	161	(2.1)	(10.7)	348	342	(1.8)
Revenue	12,751	11,625	11,601	12,635	13,373	11,974	3.0	(10.5)	24,376	25,347	4.0
Operating Expenditure	6,563	6,441	6,339	6,983	6,472	6,195	(3.8)	(4.3)	13,003	12,667	(2.6)
Cost of revenues	5,130	5,298	5,214	5,535	5,455	5,566	5.1	2.0	10,429	11,021	5.7
as % of sales	40.2	45.6	44.9	43.8	40.8	46.5			42.8	43.5	
SG&A expenses	1,433	1,142	1,125	1,448	1,017	629	(44.9)	(38.1)	2,575	1,646	(36.1)
as % of sales	11.2	9.8	9.7	11.5	7.6	5.3			10.6	6.5	
EBITDA	6,188	5,184	5,262	5,652	6,901	5,778	11.5	(16.3)	11,372	12,679	11.5
Depreciation	265	256	268	274	266	272	6.3	2.4	521	538	3.2
EBIT	5,923	4,928	4,994	5,378	6,635	5,506	11.7	(17.0)	10,851	12,141	11.9
Other Income	293	435	596	(25)	435	123	(71.7)	(71.6)	728	558	(23.3)
PBT	6,216	5,363	5,589	5,354	7,070	5,630	5.0	(20.4)	11,579	12,699	9.7
Total Tax	2,442	1,775	1,022	2,661	2,272	1,709	(3.7)	(24.8)	4,217	3,981	(5.6)
Reported PAT	3,774	3,588	4,567	2,692	4,798	3,921	9.3	(18.3)	7,362	8,719	18.4
Reported EPS	44	42	53	31	53	45	9.1	(18.3)	85	101	18.3
Margins (%)							(bps)	(bps)			
EBIDTA	49	45	45	45	52	48	-366	-334	47	50	337
EBIT	46	42	43	43	50	46	-359	-363	45	48	338
EBT	49	46	48	42	53	47	-88	-585	48	50	260
PAT	30	31	39	21	36	33	-187	-314	30	34	419
Effective Tax rate	39	33	18	50	32	30	274	-178	36	31	-507

Source: DART, Company

What to Expect Next Quarter

We expect revenue growth momentum to continue in Q3 with 3% growth on YoY basis (QoQ basis it is expected to go up by 4%) and expect some normalization of OPM (decline) of about 84bps QoQ at 45.1%. PAT is expected to flat QoQ and expected to decline by 14% on YoY basis as it had one-time tax benefits resulting in ETR of 18% in base quarter last year, versus normal ETR of 32% in Q3FY21.

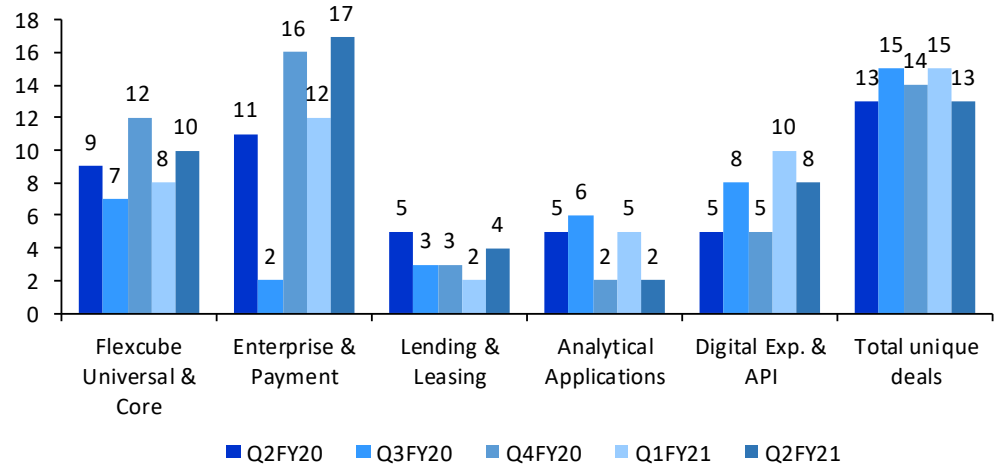
Exhibit 5: What to Expect Next Quarter

(Rs mn)	Q3FY21E	Q2FY21	Q3FY20	QoQ (%)	YoY (%)
Sales (US\$ mn)	167.7	161.4	162.9	3.9	2.9
Sales	12,329	11,974	11,601	3.0	6.3
EBIT	5,566	5,506	4,994	1.1	11.5
PAT	3,936	3,921	4,567	0.4	(13.8)
EPS (Rs)	45.8	45.4	53.2	0.7	(14.0)
EBIT Margin (%)	45.1	46.0	43.0	(84 bps)	210 bps

Source: DART, Company

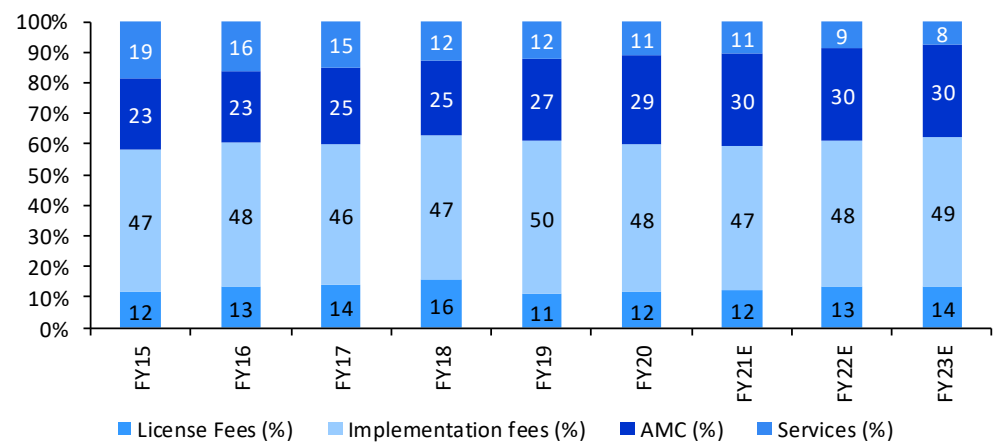
Story in Charts

Exhibit 6: Product and module sales quarterly



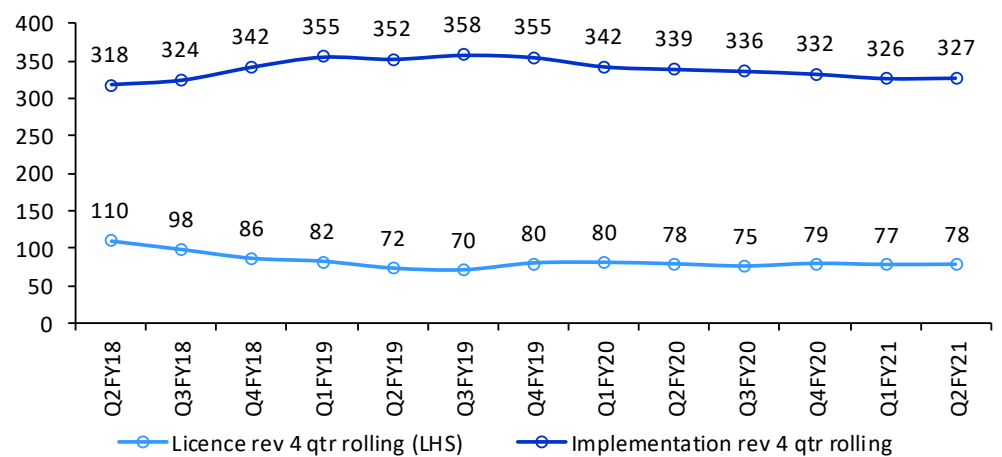
Source: DART, Company

Exhibit 7: Revenue Mix Trends



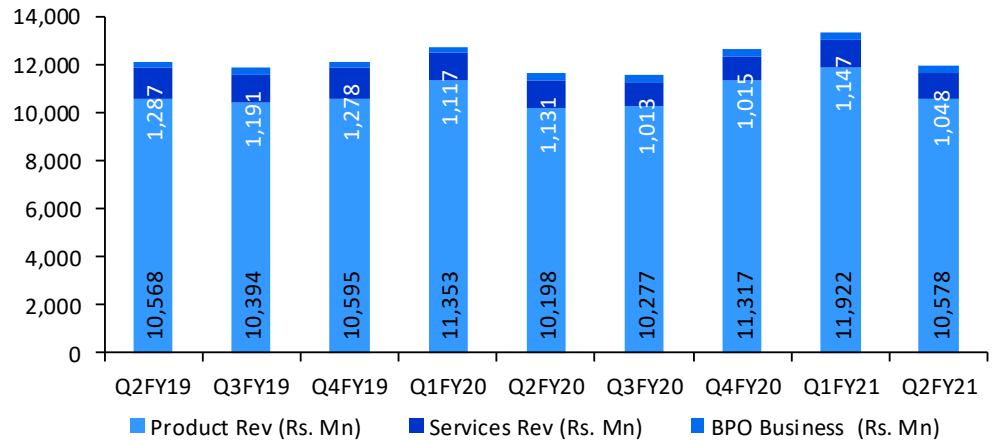
Source: DART, Company

Exhibit 8: License and Implementation Revenue on 4-Qtr Rolling basis



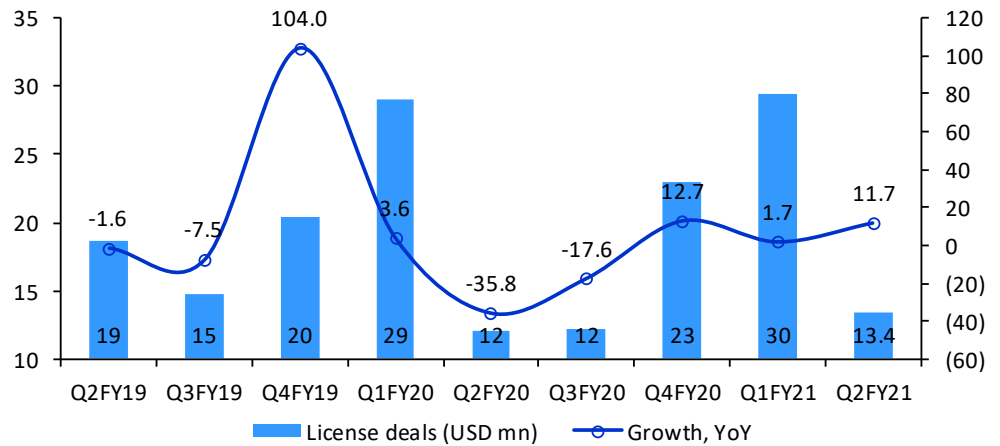
Source: DART, Company

Exhibit 9: Revenue Breakup in Product, Services and BPO Business



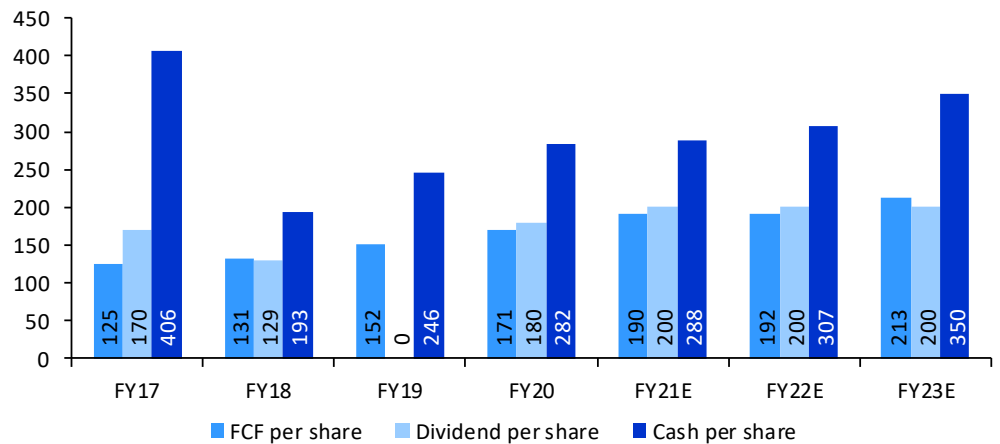
Source: DART, Company

Exhibit 10: License Wins Trend



Source: DART, Company

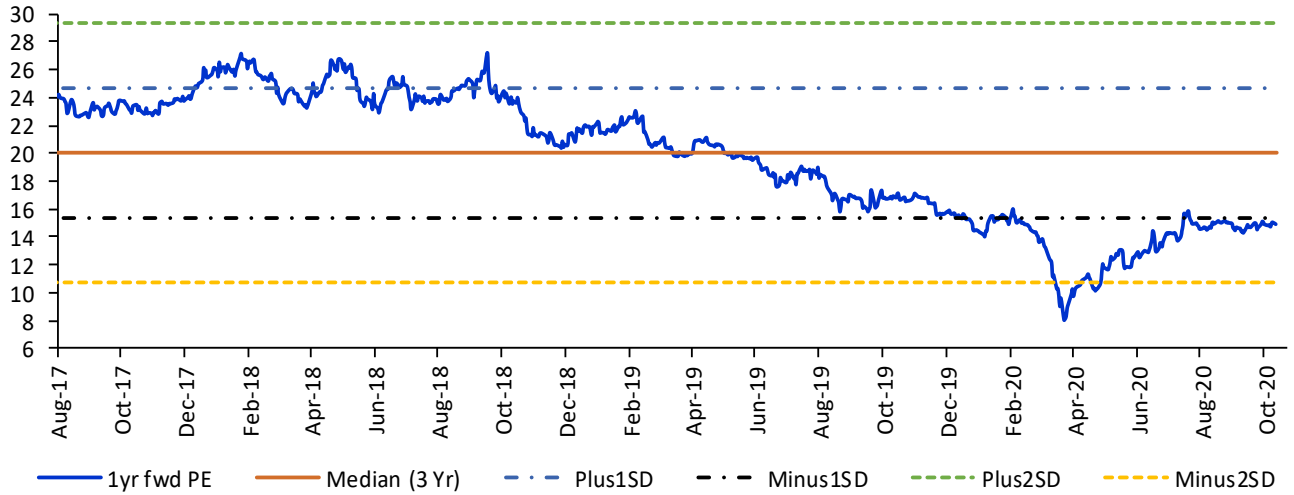
Exhibit 11: Dividend Payout to get revived as robust FCF Generation continues



Source: DART, Company

Band Chart

Exhibit 12: OFSS PE Band Chart: Valuation is recovering as growth is improving over the quarters.



Source: DART, Company

Profit and Loss Account

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Revenue	48,613	51,821	57,606	63,860
Total Expense	26,326	26,415	30,737	34,074
COGS	21,178	23,094	26,183	28,429
Employees Cost	0	0	0	0
Other expenses	5,148	3,321	4,554	5,645
EBIDTA	22,287	25,406	26,870	29,786
Depreciation	1,064	1,058	1,090	1,145
EBIT	21,223	24,348	25,780	28,641
Interest	0	0	0	0
Other Income	1,299	1,025	1,642	1,916
Exc. / E.O. items	0	0	0	0
EBT	22,522	25,372	27,422	30,557
Tax	7,901	8,105	8,775	10,084
RPAT	14,622	17,267	18,647	20,473
Minority Interest	0	0	0	0
Profit/Loss share of associates	0	0	0	0
APAT	14,622	17,267	18,647	20,473

Balance Sheet

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Sources of Funds				
Equity Capital	429	429	430	430
Minority Interest	0	0	0	0
Reserves & Surplus	65,266	65,335	66,984	70,458
Net Worth	65,696	65,765	67,414	70,889
Total Debt	5,058	5,145	5,238	5,338
Net Deferred Tax Liability	0	0	0	0
Total Capital Employed	70,753	70,909	72,652	76,227

Applications of Funds

Net Block	18,909	18,899	18,915	18,904
CWIP	0	0	0	0
Investments	1,549	1,549	1,549	1,549
Current Assets, Loans & Advances	59,755	60,436	62,682	66,806
Inventories	0	0	0	0
Receivables	9,254	9,864	10,966	12,156
Cash and Bank Balances	13,316	13,386	14,531	17,741
Loans and Advances	0	0	0	0
Other Current Assets	5,533	5,533	5,533	5,257
Less: Current Liabilities & Provisions	9,460	9,976	10,495	11,033
Payables	355	443	502	545
Other Current Liabilities	9,105	9,533	9,993	10,488
<i>sub total</i>				
Net Current Assets	50,295	50,460	52,187	55,773
Total Assets	70,753	70,909	72,652	76,227

E – Estimates

Important Ratios

Particulars	FY20A	FY21E	FY22E	FY23E
(A) Margins (%)				
Gross Profit Margin	56.4	55.4	54.5	55.5
EBIDTA Margin	45.8	49.0	46.6	46.6
EBIT Margin	43.7	47.0	44.8	44.8
Tax rate	35.1	31.9	32.0	33.0
Net Profit Margin	30.1	33.3	32.4	32.1
(B) As Percentage of Net Sales (%)				
COGS	43.6	44.6	45.5	44.5
Employee	0.0	0.0	0.0	0.0
Other	10.6	6.4	7.9	8.8
(C) Measure of Financial Status				
Gross Debt / Equity	0.1	0.1	0.1	0.1
Interest Coverage				
Inventory days	0	0	0	0
Debtors days	69	69	69	69
Average Cost of Debt	0.0	0.0	0.0	0.0
Payable days	3	3	3	3
Working Capital days	378	355	331	319
FA T/O	2.6	2.7	3.0	3.4
(D) Measures of Investment				
AEPS (Rs)	170.3	200.8	216.8	238.1
CEPS (Rs)	182.7	213.1	229.5	251.4
DPS (Rs)	180.0	199.7	200.0	200.2
Dividend Payout (%)	105.7	99.5	92.2	84.1
BVPS (Rs)	765.2	764.8	784.0	824.4
RoANW (%)	25.4	26.3	28.0	29.6
RoACE (%)	24.1	24.4	26.0	27.5
RoAIC (%)	44.0	42.4	44.6	49.1
(E) Valuation Ratios				
CMP (Rs)	3145	3145	3145	3145
P/E	18.5	15.7	14.5	13.2
Mcap (Rs Mn)	270,787	270,787	270,787	270,787
Mcap/ Sales	5.6	5.2	4.7	4.2
EV	230,876	230,893	229,842	226,731
EV/Sales	4.7	4.5	4.0	3.6
EV/EBITDA	10.4	9.1	8.6	7.6
P/BV	4.1	4.1	4.0	3.8
Dividend Yield (%)	5.7	6.4	6.4	6.4
(F) Growth Rate (%)				
Revenue	(2.0)	6.6	11.2	10.9
EBITDA	3.9	14.0	5.8	10.9
EBIT	1.5	14.7	5.9	11.1
PBT	(0.7)	12.7	8.1	11.4
APAT	5.5	18.1	8.0	9.8
EPS	5.8	17.9	8.0	9.8

Cash Flow

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
CFO	15,218	16,923	17,135	18,933
CFI	(13,841)	346	1,007	1,276
CFF	(474)	(17,198)	(16,998)	(16,998)
FCFF	14,683	16,323	16,500	18,293
Opening Cash	11,563	13,316	13,386	14,531
Closing Cash	13,316	13,386	14,531	17,741

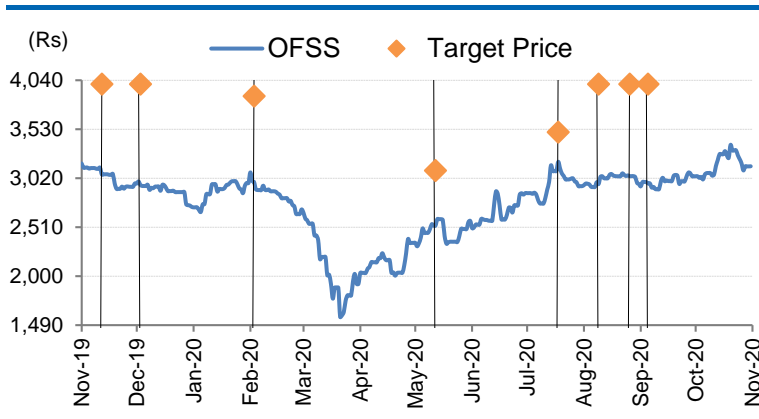
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Nov-19	Buy	4,000	3,059
Dec-19	Buy	4,000	2,951
Feb-20	Buy	3,875	2,982
May-20	Buy	3,100	2,526
Jul-20	Buy	3,500	3,191
Aug-20	Buy	4,000	2,960
Aug-20	Buy	4,000	3,042
Sep-20	Buy	4,000	2,965

*Price as on recommendation date

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