# Zensar Technologies (ZENTE)

CMP: ₹ 290 | Target: ₹ 345 (19%) | Target Period: 12 months | BUY

June 18, 2021

## Turnaround to take four to eight quarters…

We attended the virtual analyst meet of Zensar Technologies. The key highlights of the meet were it will take four to eight quarters for a complete turnaround of the company. To achieve this, Zensar is addressing key shortages of past. In addition, the new CEO has devised a strategy to focus on experience side and build capabilities in digital engineering, data, artificial intelligence and machine learning. These technologies require 5x investment compared to the investment in experience. Further, Zensar is expanding sales capability (in pre-sales hunter, farmers) and hiring leaders to drive growth. The company is also focusing on increasing deal velocity and annuity revenues to counter deal ramp downs. In addition, Zensar plans to drive growth via tuck in acquisition. We believe all these initiatives bode well for long term growth and prompt us to be positive on the stock.

### Addressing past issues, new strategy to drive growth

Historically, the company suffered due to lower focus on core business of Oracle, unstructured verticals & sales, leakage in revenues due to project ramp downs and higher share (~55% of revenues) in commoditised business. Zensar has addressed some concerns through acquisition of experience companies like Indigo Slate & foolproof. The new CEO has also devised a new strategy to address the vertical structure by focusing on core business experience and build on digital engineering, data analytics, machine learning. Further, Zensar will invest in cloud hyperscaler and do acquisition to build capabilities. The company is investing in sales, new leaders (hired a leader in geo & salesforce) and help salesforce with focused selling to drive growth. In addition, Zensar is also focusing on improving deal velocity and annuity revenues to tackle leakage in revenues. In addition, bottoming of large clients in Hi tech, green shoots in BFSI business, improvement in cloud, retail & insurance revenues (hired a new leader) and ramp up of projects are expected to lead to healthy improvement in revenues. Hence, we expect Zensar to report improving revenue growth in the long term. In terms of margins, the company is expected to face headwinds due to investment in sales, talent, pricing pressure, wage hike and higher travel cost. However, Zensar is confident of achieving high teens margins as the pressure on margins is expected to be offset by higher offshoring, automation and pyramid rationalisation.

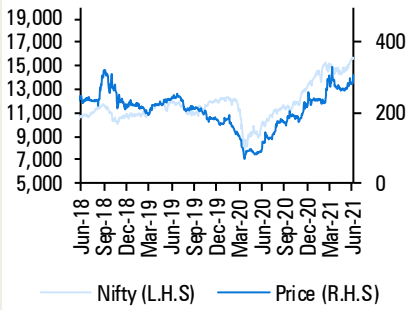
### Valuation & Outlook

The new CEO is addressing past challenges and has identified key focus areas of the company. The company's focus on driving deal momentum, annuity revenues, increasing investment in sales & talent, leadership and tuck in acquisition to build capability bodes well for long term revenue growth. In addition, healthy margins prompt us to be positive on the stock. Hence, we maintain **BUY** rating on the stock with a revised target price of ₹ 345 (15x PE on FY23E EPS, earlier target price ₹ 315).

**Particulars**

| Particular | Amount |
|---|---|
| Market Cap (₹ Crore) | 6,526.5 |
| Total Debt (₹ Crore) | - |
| Cash & Invets (₹ Crore) | 1,061.9 |
| EV (₹ Crore) | 5,464.6 |
| 52 week H/L | 347 / 121 |
| Equity capital | 45.1 |
| Face value | ₹ 2 |

**Price Performance**




**Key Risk**

- Delay in conversion of pipeline, deceleration in cloud, FS and retail may lead to lower-than-expected revenues
- In the past, the company have made acquisitions to drive revenue growth. In future, Zensar intends to acquire to boost capability. However, in the event of acquisition does not pan out as per expectations, it can adversely impact financials

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**Key Financial Summary**

| (₹ Crore) | FY19 | FY20 | FY21 | FY22E | FY23E | CAGR (FY21-23E) |
|---|---|---|---|---|---|---|
| Net Sales | 3,983 | 4,182 | 3,781 | 4,202 | 4,769 | 12.3% |
| EBITDA | 493 | 507 | 685 | 765 | 906 | 15.0% |
| EBITDA Margin (%) | 12.4 | 12.1 | 18.1 | 18.2 | 19.0 | |
| Reported PAT | 314 | 263 | 300 | 425 | 531 | 33.1% |
| EPS (₹) | 13.9 | 11.5 | 13.2 | 18.7 | 23.3 | |
| P/E | 20.8 | 25.2 | 22.0 | 15.5 | 12.4 | |
| ROE (%) | 16.1 | 12.6 | 12.8 | 16.0 | 17.5 | |
| ROCE (%) | 17.6 | 12.5 | 18.9 | 19.6 | 21.6 | |

*Source: Company, ICICI Direct Research*


Analyst Meet Update

ICICI Securities – Retail Equity Research

## Financial summary

Exhibit 1: Profit and loss statement ₹ crore

| | FY20 | FY21 | FY22E | FY23E |
|---|---|---|---|---|
| **Total Revenues** | **4,182** | **3,781** | **4,202** | **4,769** |
| Growth (%) | 5.0 | -9.6 | 11.1 | 13.5 |
| Employee Benefit Expense | 3,016.0 | 2,514.5 | 2,786.0 | 3,161.9 |
| Other Expenses | 658.6 | 582.1 | 651.3 | 701.1 |
| **EBITDA** | **507** | **685** | **765** | **906** |
| Growth (%) | 2.9 | 35.1 | 11.7 | 18.5 |
| Depreciation | 159.2 | 174.7 | 174.7 | 174.7 |
| Other Income | 88.4 | 25.5 | 34.1 | 42.0 |
| Interest | 60.5 | 53.5 | 40.0 | 40.0 |
| PBT before Exceptional Items | 375.8 | 482.0 | 584.2 | 733.5 |
| Growth (%) | -15.6 | 28.3 | 21.2 | 25.6 |
| Tax | 104.2 | 126.0 | 151.9 | 194.4 |
| PAT before Exceptional Items | 271.6 | 356.1 | 432.3 | 539.1 |
| Minority interest | 8.2 | 7.0 | 7.2 | 7.8 |
| **PAT after exceptional items** | **263** | **300** | **425** | **531** |
| Growth (%) | -16.0 | 13.9 | 41.7 | 25.0 |
| **Diluted EPS** | **11.5** | **13.2** | **18.7** | **23.3** |
| EPS (Growth %) | -17.3 | 14.3 | 41.7 | 25.0 |

*Source: Company, ICICI Direct Research*

Exhibit 2: Cash flow statement ₹ crore

| | FY20 | FY21 | FY22E | FY23E |
|---|---|---|---|---|
| **Profit before Tax** | **376** | **482** | **584** | **733** |
| Depreciation | 159 | 175 | 175 | 175 |
| Change in working capital | 235 | 315 | (54) | (73) |
| Income Taxes Paid | (115) | (140) | (152) | (194) |
| | | | | |
| **CF from operations** | **686** | **858** | **551** | **631** |
| Other Investments | (237) | (547) | 34 | 42 |
| (Purchase)/Sale of Fixed Asse | (78) | (39) | (231) | (62) |
| **CF from investing Activities** | **(315)** | **(528)** | **(197)** | **(20)** |
| Inc / (Dec) in Equity Capital | 2 | 1 | - | - |
| Inc / (Dec) in sec.loan Funds | 11 | (330) | - | - |
| Dividend & Dividend tax | (120) | (27) | (115) | (143) |
| Interest Paid on Loans | (12) | (4) | (40) | (40) |
| **CF from Financial Activities** | **(119)** | **(359)** | **(155)** | **(183)** |
| Net change in cash | 252 | (29) | 199 | 428 |
| Opening cash | 326 | 517 | 699 | 848 |
| **Closing cash** | **517** | **699** | **848** | **1,226** |

*Source: Company, ICICI Direct Research*

Exhibit 3: Balance sheet ₹ crore

| | FY20 | FY21 | FY22E | FY23E |
|---|---|---|---|---|
| Equity | 45 | 45 | 45 | 45 |
| Reserves & Surplus | 2,045 | 2,297 | 2,608 | 2,995 |
| Networth | 2,090 | 2,342 | 2,653 | 3,040 |
| Total debt | 289 | - | - | - |
| Minority Interest | 24 | 29 | 29 | 29 |
| Other liabilities | 377 | 324 | 324 | 324 |
| **Source of funds** | **2,779** | **2,695** | **3,005** | **3,393** |
| Fixed assets | 458 | 388 | 470 | 458 |
| Intangible assets | 230 | 168 | 193 | 142 |
| Goodwill | 647 | 577 | 577 | 577 |
| Non current investments | 11 | 154 | 154 | 154 |
| Other non current assets | 192 | 154 | 160 | 172 |
| Current Investments | 267 | 363 | 363 | 363 |
| Cash Balance | 517 | 699 | 848 | 1,226 |
| Inventories | 94 | - | - | - |
| Debtors | 666 | 589 | 651 | 739 |
| Other current assets | 514 | 342 | 347 | 373 |
| Trade payables | 265 | 220 | 240 | 272 |
| Other Current liabilities | 551 | 518 | 518 | 539 |
| **Application of funds** | **2,779** | **2,695** | **3,005** | **3,393** |

*Source: Company, ICICI Direct Research*

Exhibit 4: Key ratios ₹ crore

| | FY20 | FY21 | FY22E | FY22E |
|---|---|---|---|---|
| **Per share data (₹)** | | | | |
| Diluted EPS | 11.5 | 13.2 | 18.7 | 23.3 |
| BV | 91.5 | 102.9 | 116.5 | 133.6 |
| DPS | 2.8 | 3.6 | 5.0 | 6.3 |
| Cash Per Share | 22.6 | 30.7 | 37.3 | 53.9 |
| **Operating Ratios (%)** | | | | |
| EBITDA Margin | 12.1 | 18.1 | 18.2 | 19.0 |
| PAT Margin | 6.3 | 7.9 | 10.1 | 11.1 |
| Debtor days | 58 | 57 | 57 | 57 |
| Creditor days | 23 | 21 | 21 | 21 |
| **Return Ratios (%)** | | | | |
| RoE | 12.6 | 12.8 | 16.0 | 17.5 |
| RoCE | 12.5 | 18.9 | 19.6 | 21.6 |
| RoIC | 17.4 | 31.2 | 32.9 | 40.5 |
| **Valuation Ratios (x)** | | | | |
| P/E | 25.2 | 22.0 | 15.5 | 12.4 |
| EV / EBITDA | 11.9 | 8.0 | 6.9 | 5.4 |
| Market Cap / Sales | 1.6 | 1.7 | 1.6 | 1.4 |
| Price to Book Value | 3.2 | 2.8 | 2.5 | 2.2 |
| **Solvency Ratios** | | | | |
| Debt/Equity | 0.1 | - | - | - |
| Debt / EBITDA | 0.6 | - | - | - |
| Current Ratio | 1.6 | 1.3 | 1.3 | 1.4 |
| Quick Ratio | 1.4 | 1.3 | 1.3 | 1.4 |

*Source: Company, ICICI Direct Research*

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%

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