

CMP: ₹ 403

Target: ₹ 505 (25%)

Target Period: 12 months

BUY

July 27, 2021

Hi Tech drives topline...

About the stock: Zensar Technologies (Zensar) offers application & IMS services to hi-tech, manufacturing, retail and BFSI.

- Zensar has grown organically and inorganically over the years
- Net debt free and healthy double digit return ratio (with RoCE of 19%)

Q1FY22 Results: Zensar reported healthy revenue growth.

- Digital revenues increased 5.8% QoQ to US\$127.2 million
- EBIT margins declined 90 bps QoQ to 13.9%
- Deal wins were at US\$96.7 million

What should investors do? Zensar's share price has grown by ~2x over the past five years (from ~₹ 201 in July 2016 to ~₹ 403 levels in July 2021).

- We continue to remain positive and retain our BUY rating on the stock

Target Price and Valuation: We value Zensar at ₹ 505 i.e. 22x P/E on FY23E

Key triggers for future price performance:

- Zensar is addressing key shortages of the past. The new CEO has devised a strategy to focus on experience side and build capabilities in digital engineering, data, artificial intelligence and machine learning
- Driving deal momentum, annuity revenues, increasing investment in sales & talent, leadership and tuck in acquisition to build capability bode well for long term revenue growth
- Expect dollar revenue CAGR of 11% over FY21-23E

Alternate Stock Idea: Apart from Zensar, in our IT coverage we also like Persistent.

- Key beneficiary of growth in digital technologies and exposure to growth segments like Healthcare & BFSI
- BUY with a target price of ₹ 3,535

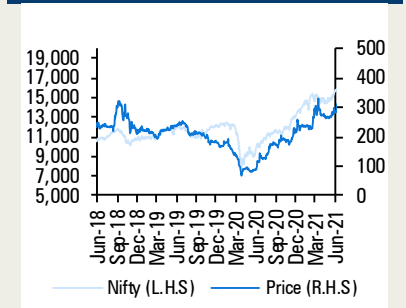
Particulars

Particular	Amount
Market Cap (₹ Crore)	9,069.5
Total Debt (₹ Crore)	-
Cash & Invets (₹ Crore)	1,061.9
EV (₹ Crore)	8,007.6
52 week H/L	424 / 139
Equity capital	45.1
Face value	₹ 2

Shareholding pattern

	Sep-20	Dec-20	Mar-21	Jun-21
Promoter	49	49	49	49
FII	16	16	16	17
DII	25	25	25	21
Public	10	10	10	13

Price Chart



Recent event & key risks

- Deal wins remain robust
- **Key Risk:** (i) Deceleration in deal pipeline, (ii) Inability to sustain cost savings.

Research Analyst

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Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	5 Year CAGR (FY16-21)	FY22E	FY23E	2 Year CAGR (FY21-23E)
Net Sales	3,983	4,182	3,781	4.9%	4,202	4,790	12.6%
EBITDA	493	507	685	9.2%	748	910	15.3%
EBITDA Margin (%)	12.4	12.1	18.1		17.8	19.0	
Reported PAT	314	263	300	-0.6%	413	534	33.4%
EPS (₹)	13.9	11.5	13.2		18.1	23.5	
P/E	28.9	35.0	30.6		22.2	17.2	
ROE (%)	16.1	12.6	12.8		15.6	17.6	
ROCE (%)	17.6	12.5	18.9		19.1	21.7	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter & conference call highlights

Q1FY22 Earnings Conference Call highlights

- The company saw healthy growth in the Hi tech vertical led by new logos, healthy demand and ramp up in existing customers. Zensar has aligned its services with client spend, which is helping drive growth. The company has also hired leadership to drive growth in the segment
- In insurance, the company has diversified from P&C to L&A and is going after larger clients. Zensar is also focussing on insurance tech companies to drive growth
- The new CEO's strategy to focus on digital app, advance engineering, digital engineering, experience and digital foundation services is seeing traction. The CEO is also focusing sales expansion, partnership, reskilling and M&A which is expected to drive long term revenues. This strategy is expected to drive long term sustainable growth. The CEO expects the strategy to fully materialise in the next seven quarters (green shoots are visible in the current quarter)
- The company is targeting large deals (via third party advisors and internal team), expanding its hunting sales (has led to one client transition to US\$20 million bucket), which will further drive growth
- This, coupled with opening of new logos, higher demand in retail & Hi Tech, healthy order booking (50% new), focus on annuity revenues, improvement in cloud, acquisition M3Bi (to start contributing from Q2FY22E), higher headcount addition and ramp up of projects are expected to lead to healthy improvement in revenues
- In terms of margins, current quarter margins were impacted by higher SG&A cost (led by higher delivery expenses) and higher onsite revenues. Going forward, the company expects margin headwinds in terms of wage hike (effective Q2FY22E), lower margins in M3Bi sales expansion and supply side constraints)
- However, the company is also trying to rationalise its pyramid, re skill & up skill its employees, rationalise amortisation (up due to higher acquisition), higher offshoring and automation to offset the margin headwinds
- Hence, although in the near term, we expect EBITDA margins to taper down by 30 bps YoY to 17.8%, we then expect them to expand 120 bps YoY to 19% in FY23E in line with Zensar's aspiration to reach high teen margins

Financial summary

Exhibit 1: Profit and loss statement				
	₹ crore			
	FY20	FY21	FY22E	FY23E
Total Revenues	4,182	3,781	4,202	4,790
Growth (%)	5.0	-9.6	11.1	14.0
Employee Benefit Expense	3,016.0	2,514.5	2,786.0	3,176.1
Other Expenses	658.6	582.1	668.1	704.2
EBITDA	507	685	748	910
Growth (%)	2.9	35.1	9.2	21.7
Depreciation	159.2	174.7	174.7	174.7
Other Income	88.4	25.5	34.0	41.7
Interest	60.5	53.5	40.0	40.0
PBT before Exceptional Items	375.8	482.0	567.2	737.2
Growth (%)	-15.6	28.3	17.7	30.0
Tax	104.2	126.0	147.5	195.4
PAT before Exceptional Items	271.6	356.1	419.8	541.8
Minority interest	8.2	7.0	7.2	7.8
PAT after exceptional items	263	300	413	534
Growth (%)	-16.0	13.9	37.5	29.5
Diluted EPS	11.5	13.2	18.1	23.5
EPS (Growth %)	-17.3	14.3	37.5	29.5

Source: Company, ICICI Direct Research

Exhibit 2: Cash flow statement				
	₹ crore			
	FY20	FY21	FY22E	FY23E
Profit before Tax	376	482	567	737
Depreciation	159	175	175	175
Change in working capital	235	315	(54)	(75)
Income Taxes Paid	(115)	(140)	(147)	(195)
CF from operations	686	858	539	632
Other Investments	(237)	(547)	34	42
(Purchase)/Sale of Fixed Asse	(78)	(39)	(231)	(62)
CF from investing Activities	(315)	(528)	(197)	(21)
Inc / (Dec) in Equity Capital	2	1	-	-
Inc / (Dec) in sec.loan Funds	11	(330)	-	-
Dividend & Dividend tax	(120)	(27)	(111)	(144)
Interest Paid on Loans	(12)	(4)	(40)	(40)
CF from Financial Activities	(119)	(359)	(151)	(184)
Net change in cash	252	(29)	190	427
Opening cash	326	517	699	839
Closing cash	517	699	839	1,216

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	2,598	2,988
Networth	2,090	2,342	2,643	3,033
Total debt	289	-	-	-
Minority Interest	24	29	29	29
Other liabilities	377	324	324	324
Source of funds	2,779	2,695	2,996	3,386
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	839	1,216
Inventories	94	-	-	-
Debtors	666	589	651	743
Other current assets	514	342	347	373
Trade payables	265	220	240	273
Other Current liabilities	551	518	518	539
Application of funds	2,779	2,695	2,996	3,386

Source: Company, ICICI Direct Research

Exhibit 4: Key ratios				
	₹ crore			
	FY20	FY21	FY22E	FY23E
Per share data (₹)				
Diluted EPS	11.5	13.2	18.1	23.5
BV	91.5	102.9	116.1	133.3
DPS	2.8	3.6	4.9	6.3
Cash Per Share	22.6	30.7	36.9	53.4
Operating Ratios (%)				
EBITDA Margin	12.1	18.1	17.8	19.0
PAT Margin	6.3	7.9	9.8	11.1
Debtor days	58	57	57	57
Creditor days	23	21	21	21
Return Ratios (%)				
RoE	12.6	12.8	15.6	17.6
RoCE	12.5	18.9	19.1	21.7
RoIC	17.4	31.2	32.0	40.7
Valuation Ratios (x)				
P/E	35.0	30.6	22.2	17.2
EV / EBITDA	16.9	11.7	10.5	8.2
Market Cap / Sales	2.2	2.4	2.2	1.9
Price to Book Value	4.4	3.9	3.5	3.0
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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