

# Sonata Software Limited



**Sonata Software Limited.**
**Strong growth across all accounts**

CMP <b>INR 862</b>	Target <b>INR 1,087</b>	Potential Upside <b>26.1%</b>	Market Cap (INR Mn) <b>INR 90,663</b>	Recommendation <b>BUY</b>	Sector <b>Internet Software &amp; Services</b>
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**Synopsis:**

Sonata Software Ltd (SSOF) Q3FY22 performance was higher than our estimate. Dollar Revenue was up materially by 9% QoQ to USD 53.4Mn (KRChoksey est. USD 52Mn). Rupee revenue grew by ~33% YoY to INR 18,580Mn (KRChoksey est. INR 17,136Mn). Reported operating margin stood at 6.4% and reported net profit grew by 7.1% QoQ to INR 977Mn (KRChoksey est. INR 994Mn) with margin of 5.3%. In Q3FY22, domestic business performed well, up 33% YoY basis. International IT services witnessed a strong growth momentum (+31% YoY) backed by strong execution in platform, IP and alliance led businesses. Growth was broad based across the US (+11% QoQ), Europe(+2.5% QoQ) and RoW (+2.3% QoQ), mainly driven by ISV (+31.4%), Retail Essential (+9%), Distribution & Manufacturing (+20%) and Travel (+9.4%). The deal pipeline continues to be healthy and strong through multiple new digital wins from existing and new customers. Our target price of INR 1,087 is based on 26x Mar-24E EPS with EPS CAGR of 17.5% over FY22-24E.

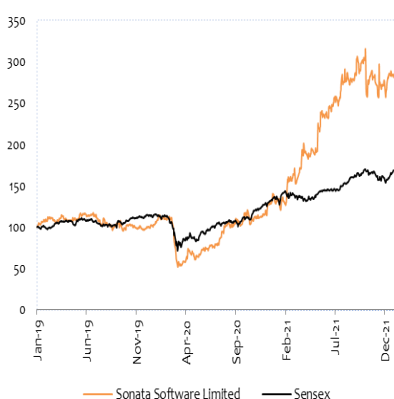
**MARKET DATA**

Shares outs (Mn)	104
Mkt Cap (INR Mn)	90663
52 Wk H/L (INR)	1030/353.95
Volume Avg (3m K)	334
Face Value (INR)	1
Bloomberg Code	SSOF:IN

**KEY FINANCIALS**

(INR Mn)	Q3FY22A	Q2FY22A	Q3FY21A	QoQ	YoY	KRChoksey Est.	Variance (%)
USD Revenue	53	49	41	9.0%	30.2%	52	2.7%
Revenue	18,580	9,632	13,962	92.9%	33.1%	17,136	8.4%
EBIT	1,190	1,114	1,017	6.8%	17.0%	1,241	-4.1%
PAT	977	912	768	7.1%	27.2%	994	-1.7%
OPM (%)	6.4%	11.6%	7.3%	-516bps	-88bps	7.2%	-84bps
NPM(%)	5.3%	9.5%	5.5%	-421bps	-24bps	5.8%	-54bps

Source: Company, KRChoksey Research

**SHARE PRICE PERFORMANCE**

**Robust growth across board**

Sonata Software (SSOF) Q3FY22 performance is higher than our estimates. For Q3FY22, company reported dollar revenue growth of 30.2% YoY (up 9% QoQ) USD 53.4Mn. In Rupee terms, revenue was up by 33.1%YoY to INR 18,580Mn. International IT services witnessed a strong growth momentum backed by strong execution through platform led growth, IP led growth and alliance led growth. With successful acquisition of new clients, SSOF has created strong pipeline & deeper revenue through client mining and new deal wins. Again, domestic business has taken steps to change with their strategy in business lines through expansion (shift to cloud) and has successfully managed to win very large deals, led by expanded market share, strong customer retention & multi-year annuity license sales. Growth was broad based across the US (+11% QoQ), Europe(+2.5% QoQ) and RoW (+2.3% QoQ), mainly driven by Data & Analytics (+12% QoQ), Managed Cloud Services (+16.1% QoQ), Microsoft Digital Platform Services (+8% QoQ) and Microsoft Dynamics Services (+10.4% QoQ). In Q3FY22, domestic business grew by +33 YoY basis to INR 14,642Mn.

**Strong deal wins to drive growth across geographies**

The deal pipeline continues to be healthy and strong through multiple new digital wins from existing and new customers. Approach to digitizing business using platforms played well for Sonata and has successfully added 2 new clients (>USD 2Mn) in Q3. Sonata (including Encore) has a strong presence in developed regions as the majority of the customers are from USA (98 Clients), Europe (44 Clients) & ANZ ( 39 clients). Company has successfully added 1 new Fortune 500 clients to 36 on YoY basis. Focus area continues to be Distribution & Manufacturing (60 Clients), Retail Essential/Non-Essential (31/17 Clients), ISV (30 Clients) and Healthcare (15 Clients). Major portion of the domestic business is coming from annuity business driven by multi-year annuity enterprise sales and the average run rate for domestic cloud business is around +78%. Top 81 clients contribute to ~80% of the gross margin for domestic business.

**Higher attrition to drag the EBIT margin**

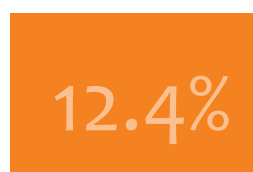
In Q2FY22, the company registered EBIT margin of 6.4%. The ongoing talent crunch led by supply side challenges, wage hikes, increasing sub-contracting costs and higher intake of fresher will keep margins under check in the near term.

**MARKET INFO**

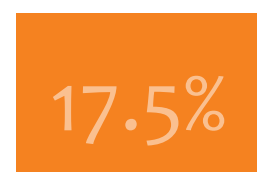
SENSEX	60,755
NIFTY	18,113

**SHARE HOLDING PATTERN (%)**

Particulars	Dec-21	Sep-21	Jun-21
Promoters	28.2	28.2	28.2
FIIIs	13.9	16.5	15.4
DIIIs	15.9	14.2	14.1
Others	42.0	41.1	42.4
Total	100.0	100.0	100.0



Revenue CAGR between FY22 and FY24E



PAT CAGR between FY22 and FY24E

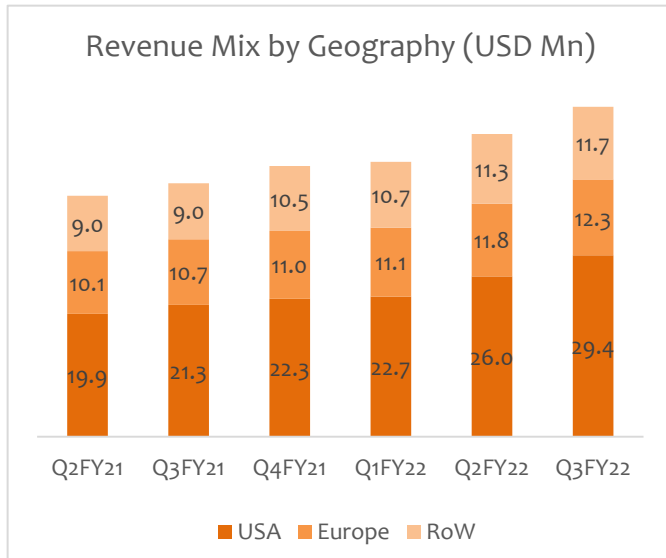
## Sonata Software Limited.

### Key Concall Highlights:

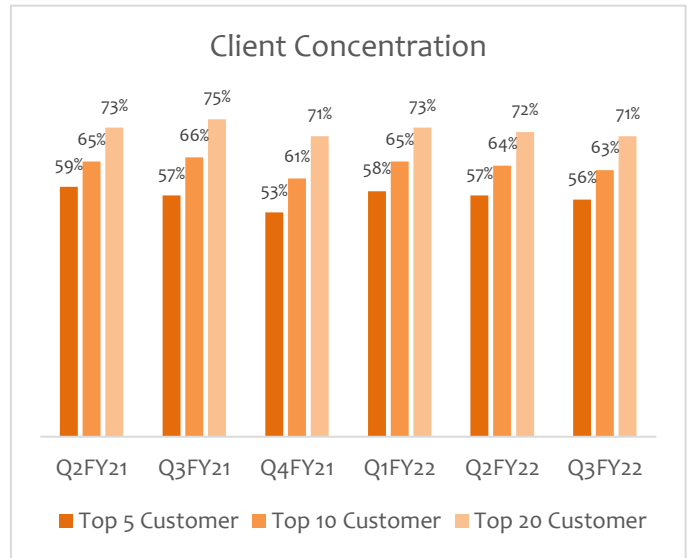
(i) Softness in the margin was due to the correction in the compensation in Q3(ii) Travel to increase starting from March/ April (iii) Pipeline in the domestic business in growing with quality & we may see further improvement in profitability (iv) Pan India business is gradually shifting towards cloud (v) management has planned to increase their onshore base in Ireland & in Canada by hiring talents (vi) Company is investing to build capabilities in digital (Microsoft practices) (vii) Sub-contracting cost for the International IT services was USD 4.5Mn (viii) Offshoring is expected to increase in medium term (ix) DSO is coming down every quarter.

### Valuation and view

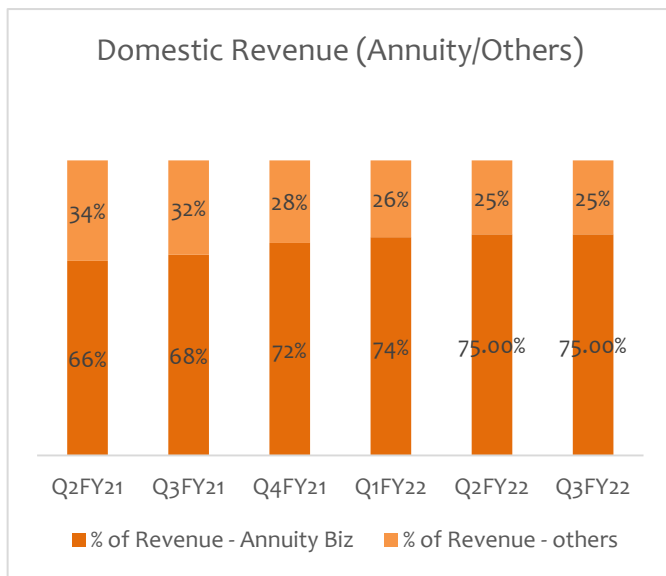
Sonata Software is currently trading at a valuation with a P/E multiple of 23.3x/20.6x on FY23E/FY24E earnings. We expect strong deal momentum across geographies, higher focus on ISV and Retail (Essential/Non-Essential), and tailwind in Managed Cloud Services will aid growth over the medium to long term in future and hence we are assigning a P/E multiple of 26x to the FY24 estimated EPS of INR 41.8 to arrive at a target price of INR 1,087 per share, an upside of 26% over the CMP. Accordingly, we upgrade our rating to an “BUY” from “ACCUMULATE” to the stock.



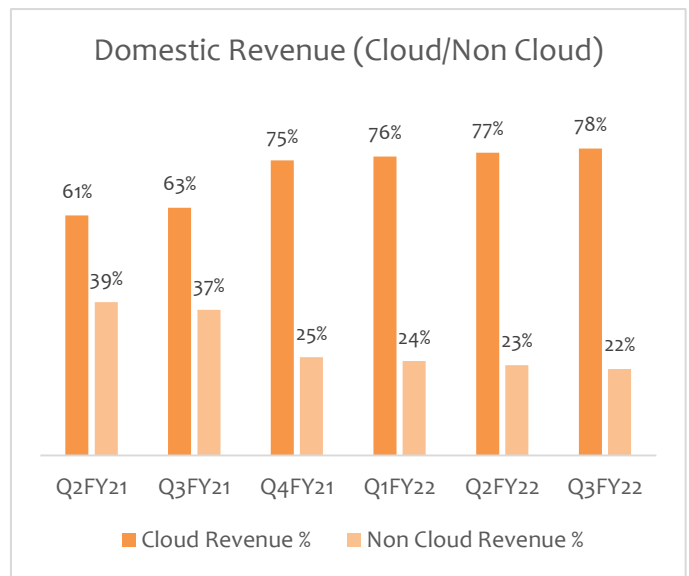
Source: Company, KRChoksey Research



Source: Company, KRChoksey Research



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## Sonata Software Limited.

### KEY FINANCIALS

#### Exhibit 1: Balance Sheet

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
Property, Plant and Equipment	234	226	213	152	352	566	748
Right-of-use Asset	0	0	973	849	849	849	849
Intangible Assets	101	322	238	477	477	477	477
Goodwill on consolidation	807	1,452	1,558	1,759	1,759	1,759	1,759
Non-current Investments	685	62	87	106	106	106	106
Deffered tax assets	124	119	244	189	189	189	189
Other non current assets	848	632	956	1,245	1,245	1,245	1,245
<b>Total non current assets</b>	<b>2,799</b>	<b>2,813</b>	<b>4,269</b>	<b>4,777</b>	<b>4,977</b>	<b>5,190</b>	<b>5,373</b>
Cash & equivalent	3474	1992	3964	6771	7927	9672	12171
Trade Receivables	3,964	8,111	7,000	6,158	7,085	8,102	9,287
Current Investments	1,300	1,402	48	654	654	654	654
Unbilled Revenues	412	447	408	408	523	735	827
Other Current Assets	376	516	476	701	701	701	701
<b>Total current assets</b>	<b>9,525</b>	<b>12,468</b>	<b>11,896</b>	<b>14,692</b>	<b>16,891</b>	<b>19,864</b>	<b>23,639</b>
<b>Total Assets</b>	<b>12,324</b>	<b>15,281</b>	<b>16,165</b>	<b>19,469</b>	<b>21,868</b>	<b>25,054</b>	<b>29,012</b>
Equity Share Capital	104	104	104	104	104	104	104
Other Equity	6,429	7,579	6,593	8,951	10,601	12,574	14,923
Equity Attributable to Owners of the Company	<b>6,533</b>	<b>7,683</b>	<b>6,697</b>	<b>9,055</b>	<b>10,705</b>	<b>12,678</b>	<b>15,027</b>
Non controlling Interest	0	0	0	0	0	0	0
<b>Total Equity</b>	<b>6,533</b>	<b>7,683</b>	<b>6,697</b>	<b>9,055</b>	<b>10,705</b>	<b>12,678</b>	<b>15,027</b>
Long term Debts	187	0	0	0	0	0	0
Other Long TermLiabilities	127	435	1,157	1,021	1,417	1,812	2,208
<b>Total non current liabilities</b>	<b>314</b>	<b>435</b>	<b>1,157</b>	<b>1,021</b>	<b>1,417</b>	<b>1,812</b>	<b>2,208</b>
Trade Payables	4,323	5,873	5,619	6,510	7,257	7,980	9,125
ST-Term Borrowings	0	156	860	897	516	516	516
Other Current Liabilities	162	75	683	990	990	990	990
Others	60	133	0	0	0	0	0
Other Payables	391	316	560	282	282	282	282
Provision	543	611	589	715	701	796	864
<b>Total Current Liabilities</b>	<b>5,478</b>	<b>7,163</b>	<b>8,311</b>	<b>9,394</b>	<b>9,746</b>	<b>10,564</b>	<b>11,778</b>
<b>Total liabilities</b>	<b>12,324</b>	<b>15,281</b>	<b>16,165</b>	<b>19,469</b>	<b>21,868</b>	<b>25,054</b>	<b>29,012</b>

Source: Company, KRChoksey Research

## Sonata Software Limited.

### KEY FINANCIALS

#### Exhibit 2: Profit & Loss Statement

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
Revenue	24,539	29,609	37,433	42,281	47,887	53,769	60,528
Total operating Expenses	22,230	26,253	33,705	38,487	43,421	48,542	54,600
<b>EBITDA</b>	<b>2,310</b>	<b>3,356</b>	<b>3,728</b>	<b>3,794</b>	<b>4,466</b>	<b>5,227</b>	<b>5,928</b>
Depreciation	124	127	365	396	388	344	395
<b>EBIT</b>	<b>2,186</b>	<b>3,229</b>	<b>3,363</b>	<b>3,398</b>	<b>4,078</b>	<b>4,883</b>	<b>5,533</b>
Other income, net	455	273	584	278	259	339	357
Finance costs	48	34	152	154	141	98	98
(Less)/ Add: (Extraordinary Item)							
Interest Income	12	28	0	0	0	0	0
<b>Pre-tax Income</b>	<b>2,604</b>	<b>3,495</b>	<b>3,795</b>	<b>3,521</b>	<b>4,196</b>	<b>5,124</b>	<b>5,791</b>
Income tax expense	682	1,006	1,026	1,082	1,049	1,281	1,448
<b>Net profit Before MI</b>	<b>1,921</b>	<b>2,489</b>	<b>2,769</b>	<b>2,440</b>	<b>3,147</b>	<b>3,843</b>	<b>4,344</b>
Minority Interest	4	4	0	0	0	0	0
<b>Net profit After MI</b>	<b>1,925</b>	<b>2,493</b>	<b>2,769</b>	<b>2,440</b>	<b>3,147</b>	<b>3,843</b>	<b>4,344</b>
Diluted EPS (INR)	18.31	23.70	26.65	23.48	30.29	36.99	41.81
Shares in Million	105	105	104	104	104	104	104

Source: Company, KRChoksey Research

#### Exhibit 3: Free Cash Flow Analysis

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
Net Cash Generated From Operations	3,370	708	5,014	5,758	4,274	5,057	6,124
Net Cash Flow from/(used in) Investing Activities	1,018	113	1,391	-1,141	-192	-161	-182
Net Cash Flow from Financing Activities	-215	-195	465	-181	-381	0	0
Others	-3,230	-2,108	-4,897	-1,630	-2,545	-3,151	-3,443
Net Inc/Dec in cash equivalents	943	-1,481	1,972	2,807	1,157	1,744	2,499
Opening Balance	2,530	3,474	1,992	3,964	6,771	7,927	9,672
Closing Balance Cash and Cash Equivalents	3,474	1,992	3,964	6,771	7,927	9,672	12,171

Source: Company, KRChoksey Research

#### Exhibit 4: Ratio Analysis

Key Ratio	FY18	FY19	FY20	FY21	FY22E	FY23E	FY24E
EBIT Margin (%)	8.9%	10.9%	9.0%	8.0%	8.5%	9.1%	9.1%
Tax rate (%)	26.2%	28.8%	27.0%	30.7%	25.0%	25.0%	25.0%
Net Profit Margin (%)	7.8%	8.4%	7.4%	5.8%	6.6%	7.1%	7.2%
RoE (%)	31.0%	35.1%	38.5%	31.0%	31.8%	32.9%	31.4%
RoCE (%)	24.8%	31.5%	33.8%	29.9%	31.0%	31.3%	30.0%
RoA (%)	15.6%	16.3%	17.1%	12.5%	14.4%	15.3%	15.0%
EPS (INR per share)	18.3	23.7	26.7	23.5	30.3	37.0	41.8

Source: Company, KRChoksey Research

**Sonata Software Limited.**

Sonata Software Limited				Rating Legend (Expected over a 12-month period)	
Date	CMP (INR)	TP(INR)	Recommendation	Our Rating	Upside
18-Jan-22	862	1087	BUY	Buy	More than 15%
19-Oct-21	975	1087	ACCUMULATE	Accumulate	5% – 15%
25-Aug-21	878	1001	ACCUMULATE	Hold	0 – 5%
				Reduce	-5% – 0
				Sell	Less than – 5%

**ANALYST CERTIFICATION:**

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