

BSE SENSEX 60,347  
S&P CNX 18,004

CMP: INR231 TP: INR265 (+15%) Buy



**Stock Info**

Bloomberg	ZENT IN
Equity Shares (m)	226
M.Cap.(INRb)/(USDb)	52.4 / 0.7
52-Week Range (INR)	587 / 222
1, 6, 12 Rel. Per (%)	-1/-44/-56
12M Avg Val (INR M)	640
Free float (%)	50.8

**Financials Snapshot (INR b)**

Y/E Mar	2022	2023E	2024E
Sales	42.4	49.9	55.7
EBIT Margin (%)	11.1	7.6	9.7
PAT	4.2	3.1	4.3
EPS (INR)	18.3	13.6	18.9
EPS Gr. (%)	19.7	-25.6	38.8
BV/Sh. (INR)	121.0	128.1	138.3

<b>Ratios</b>			
RoE (%)	16.3	11.1	14.3
RoCE (%)	11.9	8.8	11.9
Payout (%)	40.3	40.4	40.4

<b>Valuations</b>			
P/E (x)	12.6	16.9	12.2
P/BV (x)	1.9	1.8	1.7
EV/EBITDA (x)	6.4	6.8	4.7
Div Yield (%)	3.2	2.4	3.3

**Shareholding pattern (%)**

As On	Jun-22	Mar-22	Jun-21
Promoter	49.2	49.1	49.2
DII	13.9	13.4	21.1
FII	16.0	16.6	17.1
Others	21.0	21.0	12.6

Note: FII includes depository receipts

**Valuations offer a cushion against macro concerns**

**Targets mid-teen margin by mid-FY24**

ZENT remains cautious given the weakening demand, especially from Retail, Manufacturing, and Technology, while the same from BFSI remains good. The management, at RPG's annual investor conference, said it is aiming at mid-teen margin by 2QFY24. It also has a good M&A pipeline, with five deals on the table.

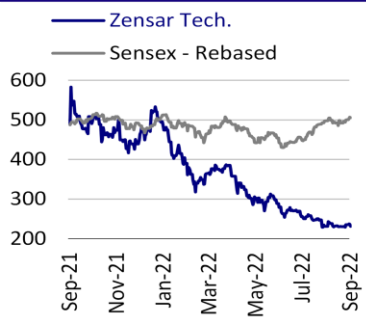
**Expect some impact on demand from a weakening macro**

- The management is seeing signs of a softening in demand from clients.
- There is a visible slowdown in Retail, Manufacturing, and Technology. Tech companies have started to lay-off employees.
- As the business at large retailers is shifting towards cost-efficiency work, ZENT aims to be selective in its approach to avoid aggressive pricing behavior.
- Demand and order book from the BFSI space remains strong, given the Fed's stance on interest rates. The management said the demand environment is similar to CY06.
- It has recently hired Mr. Manikandesh Venkatachalam (formerly with MTCL) to spearhead ZENT's five strategic growth opportunities.
- In terms of geographies, Africa remains strong, although depreciation in the currency has acted as a drag for ZENT.
- It also has a good M&A pipeline, with five deals on the table.

**Strong execution to drive margin improvements**

- Operating margin was impacted due to higher attrition, with replacement cost at 1.5-2.5x. The lack of a fresher program had an additional impact on margin.
- It hired 1,600 freshers in FY22. Higher sub-contractor costs and an increase in its bench strength, due to the training period, acted as a drag on margin.
- The management aims to push margin back to the mid-teens by 2QFY24.
- It highlighted six margin levers, led by an improvement in: 1) the service mix, 2) commercials (securing good price hikes), 3) utilization, and optimization of the 4) employee pyramid (hiring more junior staff), 5) support costs, and 6) cost of talent acquisition.
- ZENT offered its best-ever wage hike in Jul'22, which is helping cool attrition. It aims to pare down attrition to 22% over the next two-to-three quarters.
- Pressure on the supply-side will continue for some time, given the elevated industry pressure on account of: a) the drying up of supply from Eastern Europe, b) demand from captives, c) startups, and d) lack of trained supply. This is likely to delay the normalization of supply.

**Stock's performance (one-year)**



**Valuation and view**

- ZENT's current valuation (12x FY24E EPS) is one of the lowest in our midcap coverage.
- We expect a continuation in the revenue growth momentum in FY23. The new CEO-led leadership team is in place and its growth strategy has delivered results. The management expects margin to revert to the high teens over the medium term. With strong organic growth in FY23 and a recovery in key accounts, we see potential for a significant stock re-rating as valuations catch up with its peer group. Our TP implies 14x FY24E EPS. **We maintain our Buy rating on the stock.**

**Key focus areas going forward**

The management shared five key focus areas:

- Experience and design services
- Advanced engineering and Cloud engineering services
- Data engineering and analytics
- Applications and platforms
- Foundation and infrastructure services

**Exhibit 1: Market trends, imperatives, and the focus areas for ZENT**



Source: MOFSL, Company

**Strategy on track; focus on execution continues**

The management highlighted six key areas for execution:

- Transformation in the client experience
- Tuck-in acquisitions to augment its services and vertical capabilities
- Multi-service line solutions targeting industry-specific needs
- Thrust on margin improvement
- Continued push on talent transformation
- Sustained focus on growth resilience

## Exhibit 2: ZENT's strategy



Source: MOFSL, Company

## Exhibit 3: Operating metrics

	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22	1QFY23
<b>Geographic mix (%)</b>									
USA	75	73	70	70	70	70	71	70	71
Europe	15	16	17	19	18	18	18	19	18
RoW	10	11	12	12	12	12	11	11	11
<b>Vertical mix (%)</b>									
Manufacturing	58	55	52	52	53	50	46	46	46
Retail and Consumer Services	12	14	15	15	15	15	16	16	16
Financial Services	27	29	29	30	29	31	32	32	33
Emerging	2	2	4	3	4	4	6	6	6
<b>Service mix (%)</b>									
Application Management Services	85	85	85	85	85	85	82	82	82
Infrastructure Management Services	15	15	15	15	15	15	18	18	18
<b>Project type (%)</b>									
Fixed price	60	61	61	62	64	61	60	59	58
Time and material	40	39	39	39	36	39	40	41	42
<b>Revenue by delivery (%)</b>									
Onsite	63	60	57	57	58	58	58	56	58
Offshore	37	40	43	43	42	43	42	44	42
<b>Client concentration (%)</b>									
Top five	43	40	38	37	38	35	34	33	33
Top six to 10	11	11	10	11	11	12	13	13	12
Top 10	54	51	48	48	49	47	47	46	45
Top 11-20	14	15	14	15	14	15	14	16	16
Top 20	68	66	62	63	64	62	61	62	61
<b>Number of clients (USD m)</b>									
Over USD1m	80	81	83	78	79	85	81	83	86
Over USD5m	24	23	24	24	24	26	25	27	26
Over USD10m	9	8	8	7	8	10	11	11	13
Over USD20m	2	2	2	2	3	3	4	4	4
<b>Client metrics</b>									
Number of active clients	132	134	134	134	135	143	144	147	147
<b>Employee metrics</b>									
Total headcount	8,955	8,542	8,809	9,111	9,512	10,375	10,641	11,839	11,559
Gross employees added during the period	229	394	991	1,332	1,508	1,545	1,416	2,331	1,220
Utilization	82.2	83.3	80.1	81.3	80.4	83.3	79.9	81.5	80.7
Attrition	13.5	11.7	12.9	14.8	18.1	23.2	26.7	27.9	28.1

Source: Company, MOFSL

## Financials and valuations

Income Statement								(INR m)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
<b>Sales</b>	<b>30,556</b>	<b>30,058</b>	<b>38,988</b>	<b>40,102</b>	<b>36,681</b>	<b>42,437</b>	<b>49,924</b>	<b>55,708</b>
Change (%)	4.0	(1.6)	29.7	2.9	(8.5)	15.7	17.6	11.6
Cost of Services	21,603	21,220	27,626	28,756	24,417	29,214	36,397	39,248
SG&A Expenses	5,087	5,254	6,283	6,310	5,422	6,659	7,780	8,858
<b>EBITDA</b>	<b>3,866</b>	<b>3,583</b>	<b>5,079</b>	<b>5,037</b>	<b>6,842</b>	<b>6,564</b>	<b>5,748</b>	<b>7,602</b>
As a percentage of Net Sales	12.7	11.9	13.0	12.6	18.7	15.5	11.5	13.6
Depreciation	486	651	894	1,567	1,732	1,849	1,967	2,173
Interest	88	227	373	605	536	354	253	279
Other Income	172	202	502	435	367	907	608	724
Forex	21	463	291	449	-113	470	98	0
<b>PBT</b>	<b>3,486</b>	<b>3,370</b>	<b>4,604</b>	<b>3,749</b>	<b>4,828</b>	<b>5,738</b>	<b>4,233</b>	<b>5,875</b>
Tax	1,103	1,013	1,310	1,038	1,261	1,525	1,120	1,557
Rate (%)	31.6	30.1	28.5	27.7	26.1	26.6	26.5	26.5
Minority Interest	35	50	51	82	70	53	0	0
<b>Net Income</b>	<b>2,348</b>	<b>2,306</b>	<b>3,243</b>	<b>2,629</b>	<b>3,497</b>	<b>4,160</b>	<b>3,112</b>	<b>4,318</b>
Change (%)	-18.9	-1.8	40.6	-18.9	33.0	19.0	-25.2	38.8

Balance Sheet								(INR m)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Share Capital	449	450	450	451	451	452	452	452
Reserves	14,267	16,239	18,973	20,900	23,423	26,869	28,525	30,822
<b>Net Worth</b>	<b>14,716</b>	<b>16,689</b>	<b>19,424</b>	<b>21,351</b>	<b>23,874</b>	<b>27,321</b>	<b>28,977</b>	<b>31,274</b>
Loans	1,306	60	2,578	2,886	-	0	0	0
Other liabilities	535	906	924	4,008	3,526	3,544	3,544	3,544
<b>Capital Employed</b>	<b>16,556</b>	<b>17,655</b>	<b>22,925</b>	<b>28,244</b>	<b>27,401</b>	<b>30,865</b>	<b>32,521</b>	<b>34,818</b>
<b>Net Block</b>	<b>4,495</b>	<b>5,976</b>	<b>9,617</b>	<b>13,340</b>	<b>11,330</b>	<b>12,858</b>	<b>11,691</b>	<b>10,318</b>
Other LT Assets	1,897	2,356	1,898	2,039	3,076	3,226	3,467	3,653
<b>Curr. Assets</b>	<b>14,657</b>	<b>14,624</b>	<b>19,360</b>	<b>20,576</b>	<b>19,928</b>	<b>22,628</b>	<b>26,815</b>	<b>31,246</b>
Current Investments	1,467	1,302	454	2,670	7,410	5,141	7,141	9,141
Inventories	1,127	1,060	985	941	0	0	0	0
Debtors	5,332	6,423	8,762	6,656	5,888	7,967	8,207	9,158
Cash and Bank Balance	5,996	5,137	3,259	5,258	3,492	5,054	6,213	7,085
Other Current Assets	736	702	5,901	5,051	3,138	4,466	5,254	5,863
<b>Current Liab. and Prov.</b>	<b>4,493</b>	<b>5,301</b>	<b>7,951</b>	<b>7,711</b>	<b>6,933</b>	<b>7,847</b>	<b>9,451</b>	<b>10,398</b>
Trade payables	1,753	1,839	3,010	2,650	2,201	3,164	3,942	4,251
Other liabilities	2,740	3,461	4,941	5,061	4,732	4,683	5,509	6,147
<b>Net Current Assets</b>	<b>10,164</b>	<b>9,323</b>	<b>11,409</b>	<b>12,865</b>	<b>12,994</b>	<b>14,781</b>	<b>17,363</b>	<b>20,847</b>
<b>Application of Funds</b>	<b>16,556</b>	<b>17,655</b>	<b>22,925</b>	<b>28,245</b>	<b>27,400</b>	<b>30,865</b>	<b>32,521</b>	<b>34,818</b>

## Financials and valuations

### Ratios

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
<b>EPS</b>	<b>10.3</b>	<b>10.1</b>	<b>14.3</b>	<b>11.7</b>	<b>15.3</b>	<b>18.3</b>	<b>13.6</b>	<b>18.9</b>
Cash EPS	12.5	13.0	18.2	18.6	22.9	26.5	22.3	28.4
Book Value	65.6	74.2	86.3	96.3	105.7	121.0	128.1	138.3
DPS	12.0	7.0	2.8	2.8	6.4	7.4	5.5	7.6
Payout (%)	116.1	69.0	19.6	24.0	41.8	40.3	40.4	40.4
<b>Valuation (x)</b>								
P/E ratio	22.4	22.8	16.2	19.8	15.1	12.6	16.9	12.2
Cash P/E ratio	18.5	17.8	12.7	12.4	10.1	8.7	10.4	8.1
EV/EBITDA ratio	11.8	12.7	10.0	9.2	6.0	6.4	6.8	4.7
EV/Sales ratio	1.5	1.5	1.3	1.2	1.1	1.0	0.8	0.6
Price/Book Value ratio	3.5	3.1	2.7	2.4	2.2	1.9	1.8	1.7
Dividend Yield (%)	5.2	3.0	1.2	1.2	2.8	3.2	2.4	3.3
<b>Profitability Ratios (%)</b>								
RoE	17.2	14.7	18.0	12.9	15.5	16.3	11.1	14.3
RoCE	16.3	12.5	15.3	10.6	14.1	11.9	8.8	11.9
<b>Turnover Ratios</b>								
Debtors (Days)	64	78	82	61	59	69	60	60
Fixed Asset Turnover (x)	7.3	5.7	5.0	3.5	3.0	3.5	4.1	5.1

### Cash Flow Statement

(INR m)

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
CF from Operations	3,244	3,298	4,183	4,508	5,432	5,774	4,627	6,045
Cash for Working Capital	-201	-1,385	-2,622	2,354	3,148	-2,427	336	-798
<b>Net Operating CF</b>	<b>3,043</b>	<b>1,913</b>	<b>1,561</b>	<b>6,862</b>	<b>8,580</b>	<b>3,347</b>	<b>4,963</b>	<b>5,247</b>
Net Purchase of FA	-349	-515	-517	-781	-393	-373	-800	-800
<b>Free Cash Flow</b>	<b>2,694</b>	<b>1,398</b>	<b>1,043</b>	<b>6,081</b>	<b>8,187</b>	<b>2,974</b>	<b>4,163</b>	<b>4,447</b>
Net Purchase of Invest.	-1,552	-1,050	-1,894	-2,372	-4,890	400	-1,294	-1,276
<b>Net Cash from Invest.</b>	<b>-1,902</b>	<b>-1,565</b>	<b>-2,411</b>	<b>-3,153</b>	<b>-5,283</b>	<b>27</b>	<b>-2,094</b>	<b>-2,076</b>
Proc. from equity issues	46	26	14	15	15	32	0	0
Proceeds from LTB/STB	2,281	-922	-376	-502	-4,505	-1,260	-253	-279
Dividend Payments	-261	-626	-633	-1,228	-271	-881	-1,457	-2,021
<b>Cash Flow from Fin.</b>	<b>2,066</b>	<b>-1,522</b>	<b>-995</b>	<b>-1,714</b>	<b>-4,761</b>	<b>-2,109</b>	<b>-1,710</b>	<b>-2,300</b>
Exchange difference	-56	315	-32	4	-20	14	0	0
<b>Net Cash Flow</b>	<b>3,151</b>	<b>-859</b>	<b>-1,877</b>	<b>1,999</b>	<b>-1,483</b>	<b>1,279</b>	<b>1,159</b>	<b>872</b>
<b>Opening Cash Bal.</b>	<b>2,845</b>	<b>5,996</b>	<b>5,137</b>	<b>3,259</b>	<b>5,258</b>	<b>3,775</b>	<b>5,054</b>	<b>6,213</b>
Add: Net Cash	3,151	-859	-1,877	1,999	-1,483	1,279	1,159	872
<b>Closing Cash Bal.</b>	<b>5,996</b>	<b>5,137</b>	<b>3,259</b>	<b>5,258</b>	<b>3,775</b>	<b>5,054</b>	<b>6,213</b>	<b>7,084</b>

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Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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