

Sonata Software Limited



Sonata Software Limited.
Continued investments showed tailwind in deal wins especially in annuity;

CMP INR 501	Target INR 587	Potential Upside ~17.2%	Market Cap (INR Mn) INR 70,345	Recommendation BUY	Sector Internet Software & Services
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Synopsis:

Sonata Software Ltd (SSOF) Q2FY23 performance was marginally higher than our estimate. Rupee revenue grew by ~55% YoY to INR 14,960Mn (KRChoksey est. INR 12,122Mn). Reported operating margin stood at to 9.4% and reported net profit grew by 4.6% QoQ to INR 1,127Mn (KRChoksey est. INR 1,021Mn) with margin of 7.5%. DPS posted a strong quarter(+38% YoY), supported by growth in cloud license and higher annuity revenue. In Q2FY23, IITS EBITDA margin stood at 27.4% and DPS EBITDA margin stood at 3.75% and consolidated EBITDA margin stood at 10.5%. The company has declared an interim dividend of INR 7. Growth was mainly driven on the back of Top 20 clients and has successfully added 12 new clients in Q2 & has added 19 new USD Mn clients this quarter. Management has indicated that pipeline continues to be healthy and strong through multiple new digital wins from existing and new customers. Our target price of INR 587 is based on 17x Mar-24E EPS with EPS CAGR of 13.4% over FY22-24E.

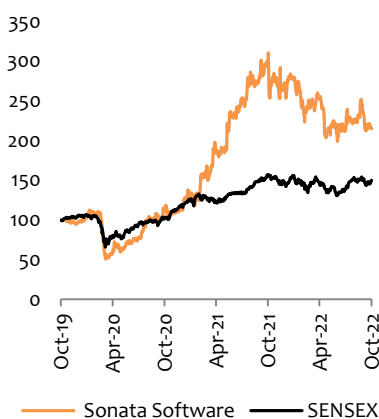
MARKET DATA

Shares outs (Mn)	140
Mkt Cap (INR Mn)	70,345
52 Wk H/L (INR)	772.5/457.5
Volume Avg (3m K)	268.4
Face Value (INR)	1
Bloomberg Code	SSOF IN

KEY FINANCIALS

(INR Mn)	Q2FY23A	Q1FY23A	Q2FY22A	QoQ	YoY	KRChoksey Est.	Variance (%)
USD IITS Revenue	57.8	57	49	1.4%	18.0%	58	-0.3%
Revenue	14,960	17,789	9,632	-15.9%	55.3%	12,122	23.4%
EBIT	1,410	1,287	1,114	9.6%	26.6%	1,311	7.6%
PAT	1,127	1,078	912	4.6%	23.6%	1,021	10.4%
OPM (%)	9.4%	7.2%	11.6%	219 bps	-214 bps	10.8%	-139 bps
NPM(%)	7.5%	6.1%	9.5%	147 bps	-193 bps	8.4%	-89 bps

Source: Company, KRChoksey Research

SHARE PRICE PERFORMANCE

Robust growth across board

Sonata Software (SSOF) Q2FY23 performance was marginally lower than our estimates. For Q2FY23, company reported rupee revenue growth of 55.3%YoY to INR 14,960Mn. IITS revenue stood at USD 57.8mn with +18% QoQ growth (USD 57mn in Q1FY23). Digital/platform revenue contributed 73/24% to IITS revenue. Among the verticals, ISV grew +3% QoQ while travel/retail were down -9.4/-1.1% QoQ due to cross-currency impact. The sell to Microsoft portfolio (ISV, +3.0% QoQ) was driving the growth & management remains optimistic about the Microsoft opportunity (product Engg + dynamics 365) and expects to deliver 15-20% YoY growth in the medium term. The management has a target of doubling its IITS revenue in the next four years.

Strong deal wins to drive growth across geographies

Company is prioritizing on platformation & alliance led growth for International services. Company continues to strengthen its revenue through deeper client mining, new client acquisition & strong pipeline. Management is also hiring sales personnel for acquiring new clients. Higher customer retention/large deals, strategic shift towards cloud, new strategic business lines for expansion, sales of multi year annuity licenses are likely to help domestic business to grow in the near future. Company continues to focus on large annuity-based managed services contracts; the recent two large deal wins (USD 10mn+) will start contributing from Q4FY23E.

Hiring strategy helped expand the margin in Q2

IITS EBITDA margin stood at 23.5% (+110bps QoQ) while DPS EBITDA margin stood at 4.5% (-120bps QoQ). Sequential decline in Domestic business led the de-growth in revenue mainly due to seasonality impact. The company added 403 headcounts in Q2 (290 fresher added in H1) and plans to add around 600 fresher in FY23E to tackle supply side concerns. The next wage hike and sales investments will come in Q4, the target margin range for IITS is 22-23%.

MARKET INFO

SENSEX	58,960.6
NIFTY	17,487.0

SHARE HOLDING PATTERN (%)

Particulars	Jun-22	Mar-22	Dec-21
Promoters	28.2	28.2	28.2
FIIIs	12.9	13.7	13.9
DIIIs	14.9	14.05	15.9
Others	44.0	44.0	42.0
Total	100.0	100.0	100.0

18.5%

Revenue CAGR between FY22 and FY24E

13.4%

PAT CAGR between FY22 and FY24E

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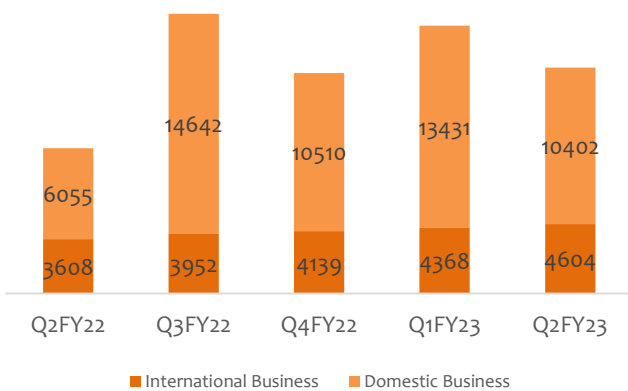
Key Concall Highlights:

(i) Sonata management has decided to scale up the BFSI and healthcare life sciences verticals through continuous investment (ii) Apart from that, company is also investing in sales and marketing across the globe e.g. USA, Europe & APAC (iii) All the recent investment activities help build robust order book/pipeline (iv) Company is investing to build capabilities in digital space (Microsoft practices) (v) Offshoring is expected to hover in the similar range of 74-76% in the medium term (vi) In spite of higher offshoring/utilization, ongoing supply side concerns to stay in the near term (vii) The company added 403 headcounts in Q2 (290 fresher added in H1) and plans to add around 600 fresher in FY23E (viii) The company declared an interim dividend of INR 7.

Valuation and view

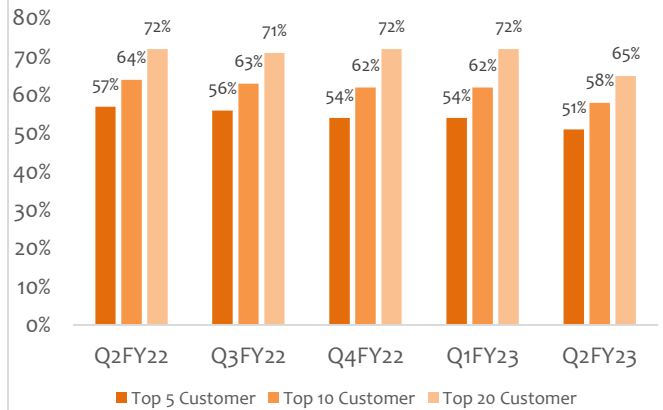
Sonata Software is currently trading at a valuation with a P/E multiple of ~17.0x/~14.5x on FY23E/FY24E earnings. We expect strong deal momentum across geographies, higher focus on ISV and Retail (Essential/Non-Essential), and tailwind in Managed Cloud Services will aid growth over the medium to long term in future and hence we are assigning a P/E multiple of 17x to the FY24 estimated EPS of INR 36.6 to arrive at an adjusted target price of INR 587 per share (Earlier Price INR 791, pre-adjustments), an upside of ~17.2% over the CMP. Accordingly, we maintain our rating to a “BUY” to the stock.

International/Domestic Business (INR Mn)



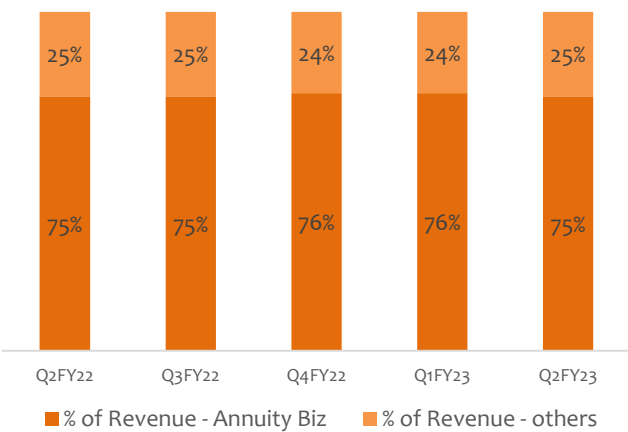
Source: Company, KRChoksey Research

Client Concentration



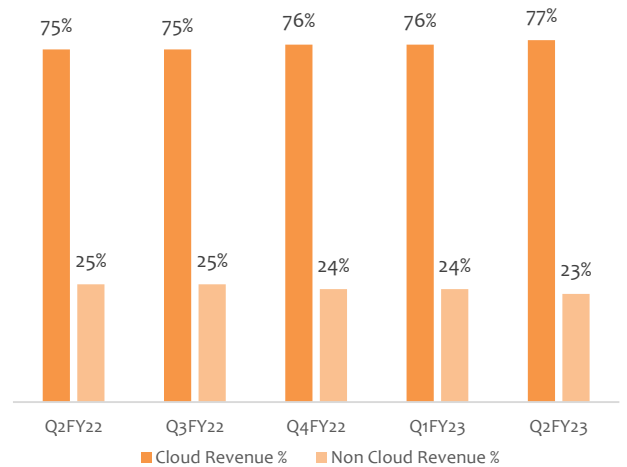
Source: Company, KRChoksey Research

Domestic Revenue (Annuity/Others)



Source: Company, KRChoksey Research

Domestic Revenue (Cloud/Non Cloud)



Source: Company, KRChoksey Research

Sonata Software Limited.

KEY FINANCIALS

Exhibit 1: Balance Sheet

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22	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
Total non current assets	2,799	2,813	4,269	4,777	4,977	5,190	5,373
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
Total current assets	9,525	12,468	11,896	14,692	16,891	19,864	23,639
Total Assets	12,324	15,281	16,165	19,469	21,868	25,054	29,012
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	6,533	7,683	6,697	9,055	10,705	12,678	15,027
Non controlling Interest	0	0	0	0	0	0	0
Total Equity	6,533	7,683	6,697	9,055	10,705	12,678	15,027
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
Total non current liabilities	314	435	1,157	1,021	1,417	1,812	2,208
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
Total Current Liabilities	5,478	7,163	8,311	9,394	9,746	10,564	11,778
Total liabilities	12,324	15,281	16,165	19,469	21,868	25,054	29,012

Source: Company, KRChoksey Research

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KEY FINANCIALS

Exhibit 2: Profit & Loss Statement

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Revenue	24,539	29,609	37,433	42,281	55,534	67,522	77,976
Total operating Expenses	22,230	26,253	33,705	38,487	50,896	62,277	71,759
EBITDA	2,310	3,356	3,728	3,794	4,638	5,245	6,217
Depreciation	124	127	365	396	473	512	547
EBIT	2,186	3,229	3,363	3,398	4,164	4,733	5,670
Other income, net	455	273	584	278	1,020	1,070	1,120
Finance costs	48	34	152	154	181	211	251
(Less)/ Add: (Extraordinary Item) Interest Income	12	28	0	0	0	0	0
Pre-tax Income	2,604	3,495	3,795	3,521	5,004	5,592	6,539
Income tax expense	682	1,006	1,026	1,082	1,239	1,454	1,700
Net profit Before MI	1,921	2,489	2,769	2,440	3,764	4,138	4,839
Minority Interest	4	4	0	0	0	0	0
Net profit After MI	1,925	2,493	2,769	2,440	3,764	4,138	4,839
Adj. diluted EPS (INR)	13.8	17.8	19.8	17.4	26.9	29.6	34.6
Shares in Million	140	140	140	140	140	140	140

Source: Company, KRChoksey Research

Exhibit 3: Free Cash Flow Analysis

Particulars (INR Mn)	FY18	FY19	FY20	FY21	FY22	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	FY22	FY23E	FY24E
EBIT Margin (%)	8.9%	10.9%	9.0%	8.0%	7.5%	7.0%	7.3%
Tax rate (%)	26.2%	28.8%	27.0%	30.7%	24.8%	26.0%	26.0%
Net Profit Margin (%)	7.8%	8.4%	7.4%	5.8%	6.8%	6.1%	6.2%
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)	13.8	17.8	19.8	17.4	26.9	29.6	34.6

Source: Company, KRChoksey Research

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Sonata Software Limited				Rating Legend (Expected over a 12-month period)	
Date	CMP (INR)	TP(INR)	Recommendation	Our Rating	Upside
19-Oct-22	501	587	BUY	Buy	More than 15%
26-July-22	684	791	BUY	Accumulate	5% – 15%
02-May-22	736	931	BUY	Hold	0 – 5%
				Reduce	-5% – 0
				Sell	Less than – 5%

ANALYST CERTIFICATION:

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