Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Coforge Ltd

Robust quarter, maintain BUY

IT & ITeS		Sharekhan code: COFORGE	
Reco/View: Buy	⇔	CMP: Rs. 7,699	Price Target: Rs. 8,900 ↑

↑ Upgrade ⇔ Maintain ↓ Downgrade

Summary

- Coforge reported revenue of $369.4 million, up 26.8% q-o-q/32.8% y-o-y. Organic revenue stood at $309.8 million, up 5.5% q-o-q in constant currency terms, beating our estimate of $305.9 million.
- Adjusted EBITDA margin declined ~127 bps q-o-q to 16.6% owing to wage hike. The executable order book over the next 12 months jumped to $1.3 billion from $1.07 billion, up 40% y-o-y.
- The company is committed to its medium-term guidance of not only reaching the $2 billion mark but also delivering a concurrent material expansion in EBITDA.
- We maintain BUY with a revised PT of Rs. 8,900 (valued at 40x its Sep26E EPS). At CMP, the stock trades at 49.3/39/31x its FY25/26/27E EPS.

Coforge reported revenue of $369.4 million, up 26.8% q-o-q/32.8% y-o-y. Organic revenue stood at $309.8 million, up 5.5% q-o-q in constant currency terms, beating our estimates of $305.9 million. In rupee terms, the company reported revenue of Rs. 3,062 crore, up 27.6% q-o-q/34.5% y-o-y. Growth was broad-based across verticals, led by insurance, government, and others. Organic adjusted EBITDA margin declined ~127 bps q-o-q to 16.6% owing to wage hike taken during the quarter. Adjusted PAT stood at Rs. 222.3 crore, down 2.7% q-o-q/up 22.8% y-o-y. The company reported a fresh order intake of $516 million, which includes $67 million from Cigniti. The executable order book over the next 12 months jumped to $1.3 billion from $1.07 billion, up 40% y-o-y. Headcounts stood at 32,486 with net additions at 5,871 sequentially, which includes 4,430 Cigniti headcounts. The company is committed to its medium-term guidance of not only reaching the $2 billion mark but also delivering a concurrent material expansion in EBITDA. The company aims to improve Cigniti's EBITDA margin to 18% by the end of FY2025. We believe the company is well placed to see robust and sustained growth in the quarters ahead given the strengthening order book, strong large deal pipeline, second consecutive quarter of significant net headcount additions and on account of synergies with Cigniti picking up momentum. We maintain BUY with a revised price target (PT) of Rs. 8,900 (valuing at 40xSep26E EPS). At CMP, the stock trades at 49.3/39/31x its FY25/26/27E EPS.

Key positives

- Organic fresh order intake at $448 million, up 43% q-o-q.
- Excluding Cigniti, Coforge business added 1,441 people, up 5.4% q-o-q.
- Cigniti's EBITDA grew by 360 bps q-o-q to 16.2%.

Key negatives

- Adjusted EBITDA margin declined ~127 bps q-o-q to 16.6%.

Management Commentary

- The company is committed to its medium-term guidance of not only reaching the $2 billion mark but also delivering a concurrent material expansion in EBITDA.
- The company aims to improve Cigniti's EBITDA margin to 18% by the end of FY25.
- Furloughs are expected to be in line with normal trends in Q3, with no expectation of higher or lower furloughs than usual.

Revision in estimates - We have revised our earnings estimates to factor in Q2FY25 performance and Cigniti's integration.

Our Call

Valuation – Maintain BUY with a revised PT of Rs. 8,900: The company reported a robust quarter both organically and along with Cigniti's integration. Growth was broad-based across verticals and is, hence, likely to sustain going forward. Despite the margin decline during the quarter, margin performance for H1FY25 has registered a significant uptick compared to H1FY24. The 12 month executable order book and fresh order intake witnessed a sharp jump during the quarter and provides strong visibility for the quarters ahead. We believe the company is well placed to see robust and sustained growth in the quarters ahead given the strengthening of order book, strong large deal pipeline, second consecutive quarter of significant net headcount additions and on account of synergies with Cigniti picking up momentum. We expect a sales/PAT CAGR of ~23%/27% over FY2024-FY2027E. We maintain BUY with a revised PT of Rs. 8,900 (valued at 40x its Sep26E EPS). At CMP, the stock trades at 49.3/39/31x its FY25/26/27E EPS.

Key Risks

Rupee appreciation and/or adverse cross-currency movements. The contagion effect of the banking crisis, macro headwinds, and recession in the U.S can moderate the pace of technology spends.

3R MATRIX

	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)		✓	

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS	Positive	⇔	Positive
RQ	Positive	⇔	Positive
RV	Neutral	⇔	Neutral

Company details

Market cap:	Rs. 51,347 cr
52-week high/low:	Rs. 7,781/4,291
NSE volume: (No of shares)	6.2 lakh
BSE code:	532541
NSE code:	COFORGE
Free float: (No of shares)	6.7 cr

Shareholding (%)

Promoters	0
FII	42
DII	48
Others	10

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	10.0	21.5	48.2	57.2
Relative to Sensex	15.7	21.6	39.8	32.2

Sharekhan Research, Bloomberg

Valuation (Consolidated) Rs cr

Particulars	FY24	FY25E	FY26E	FY27E
Revenue	9179	12015	14866	17225
OPM (%)	16.4	15.7	16.3	17.2
Adjusted PAT	809.2	1042	1315	1655
% YoY growth	16.6	28.8	26.2	25.8
Adjusted EPS (Rs.)	129.6	156.3	197.2	248.1
P/E (x)	59.4	49.3	39.0	31.0
P/B (x)	14.2	8.6	7.5	6.5
EV/EBIDTA (x)	34.3	27.0	21.4	17.1
RoNW (%)	24.1	21.7	20.5	22.4
RoCE (%)	27.2	20.7	20.1	22.9

Source: Company; Sharekhan estimates

Key highlights

- **Revenue growth:** Coforge reported revenue of $369.4 million, up 26.8% q-o-q/32.8% y-o-y. Organic revenue stood at $310 million, up 5.5% in constant currency terms, beating our estimates of $306 million. Growth was broad based across verticals. BFS, Insurance ,Travel and Government outside India grew 5.2%/8.9%/6.2% and 6.9% q-o-q respectively
- **EBITDA margin:** Adjusted EBITDA margin declined ~127 bps q-o-q to 16.6% owing to wage hike taken during the quarter. Cigniti's EBITDA grew by 360bps q-o-q to 16.2%. The company aims to improve Cignit's EBITDA margin to 18% by the end of FY25.
- **Strong deal wins and robust deal pipeline:** The company reported a fresh order intake of $516 million, which includes $67 million from Cigniti. Executable order book over the next 12 months jumped to $1.3 billion from $1.07 billion, up 40% y-o-y. The company signed three large deals, one in continental Europe, one in North America, and one in U.K.
- **Attrition and utilisation:** Headcount stood at 32,486, with net additions at 5,871 sequentially, which includes 4,430 Cigniti headcounts. Organically, Coforge business added 1,441 people, up 5.4% q-o-q. LTM attrition, including Cigniti, stood at 11.7%. Utilisation (including trainees) rose 60 bps q-o-q to 82.2%.

Results — Rs cr

Particulars	Q2FY25	Q2FY24	Q1FY25	% YoY	% QoQ
Revenues ($ mn)	**369.4**	**278.1**	**291.4**	**32.8**	**26.8**
Revenue in Rs.	**3,062.3**	**2,276.2**	**2,400.8**	**34.5**	**27.6**
Direct expenses	2,093.6	1,537.7	1,609.7	36.2	30.1
Gross Profit	**968.7**	**738.5**	**791.1**	**31.2**	**22.5**
Selling/G&A	462.4	339.2	362.5	36.3	27.6
Acquisition-related expenses and costs of ESOPs	22.2	51.9	19.9	-57.2	11.6
EBITDA	**484.1**	**347.4**	**408.7**	**39.3**	**18.4**
Depreciation	124.3	77.2	81.5	61.0	52.5
EBIT	**359.8**	**270.2**	**327.2**	**33.2**	**10.0**
Other income	(26.2)	(29.5)	(27.2)	-11.2	-3.7
PBT	**313.5**	**240.7**	**204.7**	**30.2**	**53.2**
Tax provision	79.9	52.8	65.4	51.3	22.2
Minority Interest	31.4	6.9	6.1	355.1	414.8
Net profit	202.2	181	133.2	11.7	51.8
Adjusted PAT	**222.3**	**181**	**228.5**	**22.8**	**-2.7**
EPS (Rs.)	**38.3**	**29.6**	**35.9**	**29.4**	**6.7**
Margin (%)					
EBITDA	15.8	15.3	17.0	55	-122
EBIT	11.7	11.9	13.6	-12	-188
NPM	7.3	8.0	9.5	-69	-226

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Macro headwinds bottoming out coupled with better earnings visibility

We anticipate growth momentum to return in FY25 aided by lower base coupled with easing sector headwinds. Though the IT sector has already outperformed Nifty last year, we expect overall outperformance in CY24 as well drivenby receding headwinds and better earnings visibility.

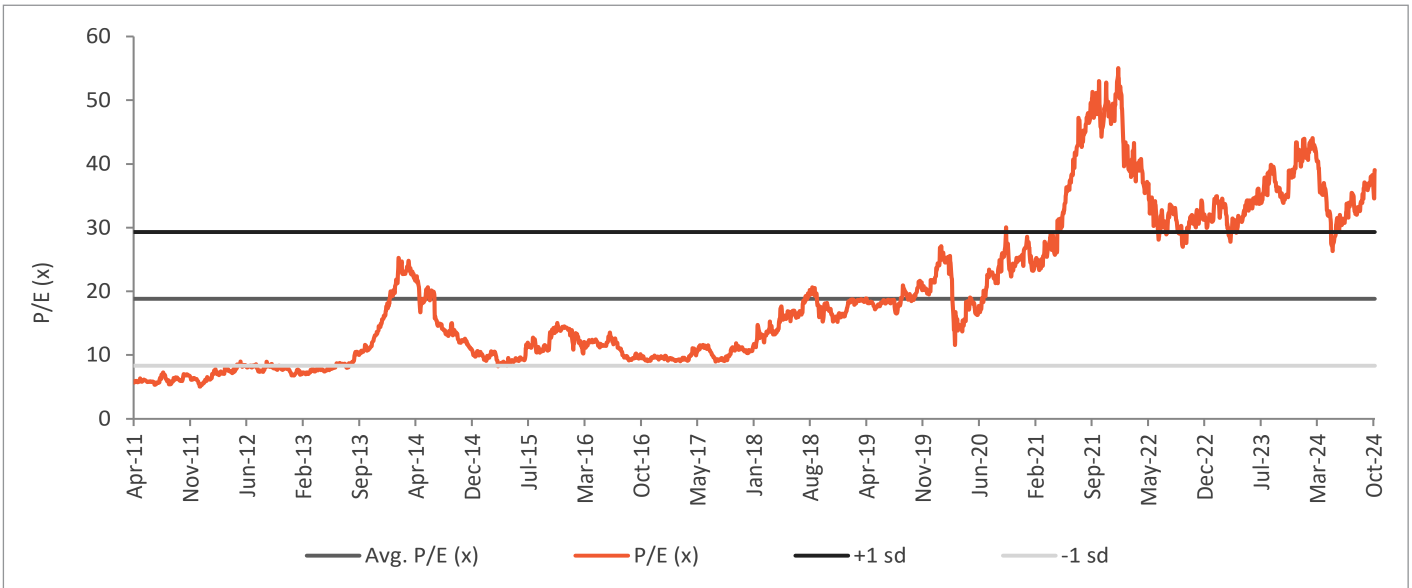
■ Company outlook - Well-prepared for next leg of growth

Coforge has successfully transformed and re-organised itself into one of the fastest-growing mid-sized IT services provider under a revamped management in the past few years. Strong leadership, deep domain capability in select verticals, improved capability and marquee client base would help the company to sustain growth momentum. Further, strategic focus on diversifying the business into emerging verticals, improvement in client metrics, strong executable orders and sharp recovery in travel segment would further aid growth. Strong growth, better digital mix and operating efficiencies should drive margin expansion in the next two years.

■ Valuation - Maintain Buy with revised PT of Rs. 8,900

The company reported a robust quarter both organically and along with Cigniti's integration. Growth was broad-based across verticals and is, hence, likely to sustain going forward. Despite the margin decline during the quarter, margin performance for H1FY25 has registered a significant uptick compared to H1FY24. The 12month executable order book and fresh order intake witnessed a sharp jump during the quarter and provides strong visibility for the quarters ahead. We believe the company is well placed to see robust and sustained growth in the quarters ahead given the strengthening of order book, strong large deal pipeline, second consecutive quarter of significant net headcount additions and on account of synergies with Cigniti picking up momentum. We expect a sales/PAT CAGR of ~23%/27% over FY2024-FY2027E. We maintain BUY with a revised PT of Rs. 8,900 (valued at 40x its Sep26E EPS). At CMP, the stock trades at 49.3/39/31x its FY25/26/27E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Established in 1981, Coforge is one of the leading mid-sized Indian IT services company, engaged in providing services in cloud, managed services, data & analytics, automation, application development & maintenance and Business Process Management. The company focuses on three key industries such as insurance, travel, transportation & hospitality and BFS. The company has started focusing on other industries such as manufacturing, healthcare, hi-tech, public sector to capture the opportunity. Digital technologies revenue, including product engineering, intelligent automation, data, integration and cloud, stood around 71% of total revenue. Coforge has over 22,000 professionals serving customers in North America, Europe, Asia and Australia.

Investment theme

Coforge's deep-domain expertise in select industry verticals and sub-verticals with heavy investments on technology, proprietary products and resources position it to participate in customers' transformation journey. Further, the company has reinvested its excess profitability in enhancing the technical capabilities by adding management/sales bandwidth. The company has also started scaling up the sub-segments such as healthcare within other verticals to drive its growth. We believe the company's differentiated positioning in select verticals, strong leadership, robust executable orders and mining of strategic accounts would position the company to deliver strong revenue growth going ahead.

Key Risks

1) Rupee appreciation and/or adverse cross-currency movements

2) Contagion effect of banking crisis, macro headwinds and possible recession in the US can moderate the pace of technology spends.

Additional Data

Key management personnel

Sudhir Singh	Chief Executive Officer & ED
Saurabh Goel	Chief Financial Officer
Madan Mohan	EVP & Global Head - TTH
Gautam Samanta	EVP & Global Head - BFS
Rajeev Batra	EVP & Global Head - Insurance

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Capital Group Cos Inc/The	7.7
2	Axis Asset Management Co Ltd/India	6.0
3	Life Insurance Corp of India	5.9
4	HDFC Asset Management Co Ltd	5.8
5	Motilal Oswal Asset Management Co	5.2
6	DSP Investment Managers Pvt Ltd	4.2
7	SBI Funds Management Ltd	3.8
8	Vanguard Group Inc/The	3.7
9	UTI Asset Management Co Ltd	3.0
10	New World Fund Inc	2.8

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/ weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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