WILLIAM O'NEIL INDIA

IT SECTOR
REPORT

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JULY
2020

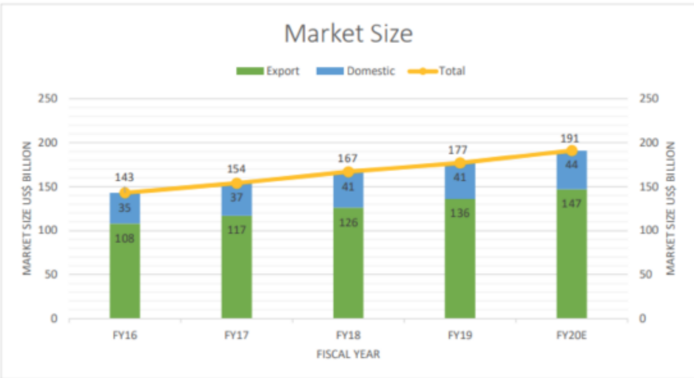
williamoneilindia.com
marketsmithindia.com
swingtraderindia.com

A4, Technomark Television,
1st Floor, NGEF Industrial Estate,
Graphite India Road, Mahadevapura,
Bengaluru, Karnataka 560048

www.williamoneilindia.com

Overview: Indian IT Sector

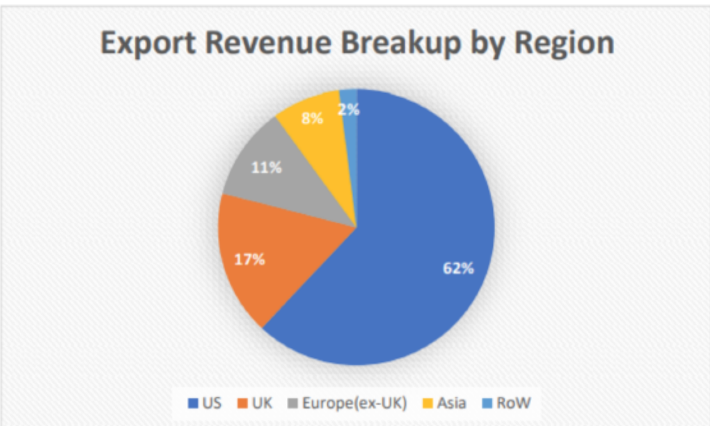
In this ever-growing age of digitization and automation, Indian IT firms are one of the favorite investment destinations. According to NASSCOM, the industry generated more than $200B in revenue in FY20. E-commerce witnessed the highest growth rate of 26% y/y in FY20. Revenue from digital constituted 28% of the IT industry revenue, clocking 23% y/y growth. According to consensus, the market size of India's IT-BPM sector is likely to reach $350B by 2025. The cloud market is forecast to see the highest growth. It is expected to grow three-fold to $7.1B by 2022 as the adoption of big data, analytics, artificial intelligence, and the Internet of Things (IoT) is poised to increase. India's digital economy is estimated to reach US$ 1T by 2025. The transition to 5G is expected to bring excellent growth for network, infrastructure, and equipment vendors.



Source: NASSCOM, Gartner

Uncertainty in growth due to the pandemic

In the last two to three weeks of March, the impact of COVID-19 was significant. Also, there was no clarity on how things will play out in terms of COVID-19. India's leading IT firms had activated business continuity plans. During the Q4 FY20 earnings call, most of the firms informed that more than 90% of their employees were working remotely. Also, the consensus was that the efficiency was maintained, and clients were mostly satisfied. IT firms did not provide any growth guidance due to uncertainty. India's IT firms generate more than 85% of their revenue from the U.S. and Europe region.



Source: NASSCOM

According to the recent growth forecast from the International Monetary Fund, for 2020, the growth rate of the U.S. is expected to be -5.9%, whereas the eurozone's growth is likely to fall to -7.5%. Lower growth in these regions can hurt a significant pie of revenue for India's IT firms.

(real GDP, annual percent change)	2019	2020	2021
World Output	2.9	-3.0	5.8
Advanced Economies	1.7	-6.1	4.5
United States	2.3	-5.9	4.7
Euro Area	1.2	-7.5	4.7
Germany	0.6	-7.0	5.2
France	1.3	-7.2	4.5
Italy	0.3	-9.1	4.8
Spain	2.0	-8.0	4.3
Japan	0.7	-5.2	3.0
United Kingdom	1.4	-6.5	4.0
Canada	1.6	-6.2	4.2
Other Advanced Economies	1.7	-4.6	4.5
Emerging Markets and Developing Economies	3.7	-1.0	6.6
Emerging and Developing Asia	5.5	1.0	8.5
China	6.1	1.2	9.2
India	4.2	1.9	7.4
ASEAN-5	4.8	-0.6	7.8

India's IT firms generates more than 85% of revenue from U.S. and Euro Area

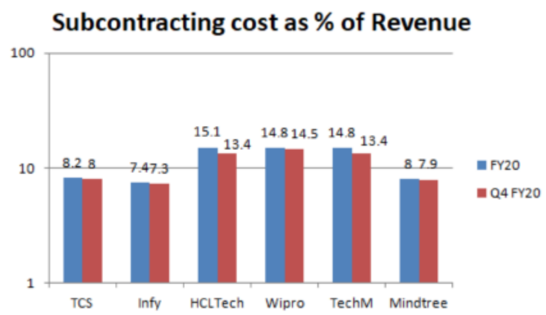
Lower growth due to the pandemic can significantly impact global IT spending. According to consensus, spending can be 12–15% lower on y/y basis. If the pandemic situation does not improve, spending may drop further.

Source: Gartner, Inc. and Bloomberg

There will be an adverse impact on the business environment across all sets of industries. However, there will be a long-term opportunity as the focus on digital and core transformation accelerates cloud, virtualization, workforce transformation, and cost-reduction programs. Near-term weakness will be more evident in discretionary spending.

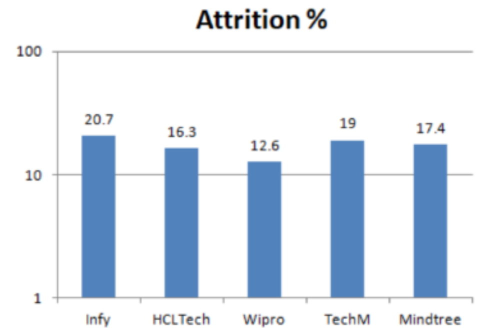
Sub-Contracting Cost to Remain low

In their Q4 FY20 earnings call, management of most Indian IT services companies announced initiatives to reduce dependence on subcontractors to control costs, as FY21 could bring along slow new deal flow and pressure on margins. On average, subcontracting forms about 10–15% of total employee costs. The fall in subcontracting cost was visible in Q4 FY20 as well and is expected to continue over the next few months.

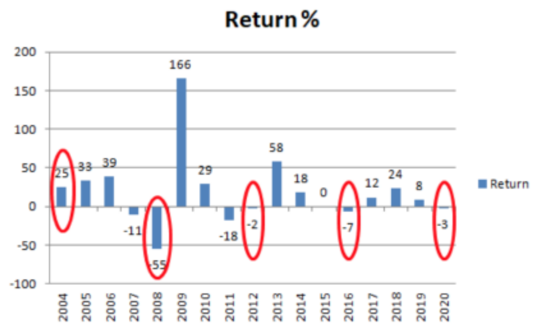


Attrition Rate

Due to hiring freeze/low hiring, attrition rates are trending downwards.



U.S. election year and Nifty IT performance



During the last couple of U.S. election years, the performance of Nifty IT was muted. 2008 was the year of financial crises, and 2020 is bearing the impact of the pandemic. If we look at two years after the election, Nifty IT has performed well, and it can be attributed to the decline in uncertainty and an increase in IT spending.

Sector-wise Impact and Opportunities

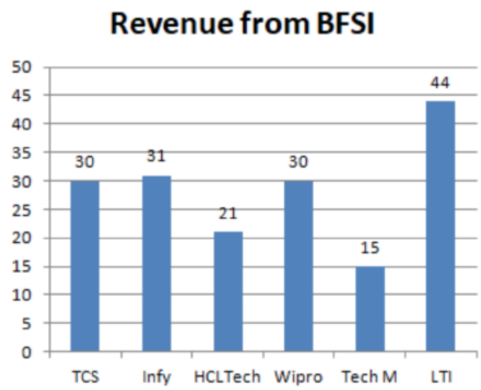
BFSI

The Financial Services sector, contributing more than 30% to revenue of TCS, Infosys, and Wipro, can have an adverse impact from the decline in interest rate across the developed and emerging economies as net interest margin is severely compressed. The banks are also expected to see an increase in loan losses over the next two to three quarters, which will have an impact on their profits. Insurance may also see increased pressure due to higher claims. Global banks had poor Q1 and consensus expects that the next couple of quarters may remain weak.

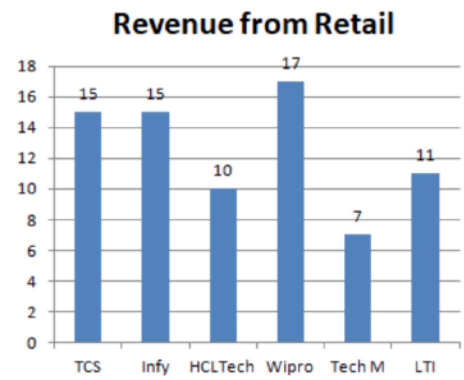
Banks	Q1 y/y Earnings	Miss Consensus
JPM	-70%	-60%
BoA	-43%	-18%
GS	-50%	-15%
WFC	-89%	-97%
MS	-30%	-11%

Short-term pain due to BFSI, but long-term gains visible

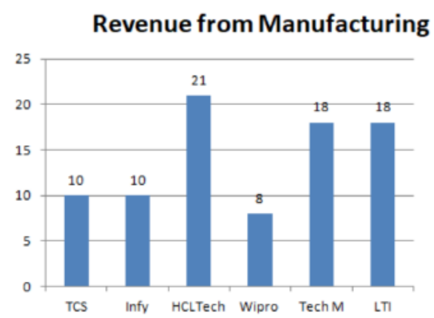
Though the new order flow may remain low in 2020, post-pandemic technology development can prove a silver lining for India's IT sector. BFSI expects a strong opportunity for cloud, data services, and new digital bank capabilities after the pandemic. In April, JP Morgan released its annual report for 2019. The company disclosed that it would increase its technology spends by 4% versus the last year, despite the pandemic. Of this, 50% would be dedicated to 'new' capabilities. The other big banks such as Bank of America and Citigroup also suggested in their annual reports that their investments in digital initiatives will increase efficiency and reduce costs.



The Retail sector, which contributes more than 15% to revenue of top IT firms, has been hit hard. Non-grocery, apparel, lifestyle and fashion, and logistics companies have taken a hit globally. In the last three to four quarters, there was a healthy deal from this segment but we expect significant pressure on spend for the segment in the coming quarters. Though the sector's deal pipeline is strong, the conversion rate is expected to slow down.



The Manufacturing sector recorded decent growth in the last few quarters. COVID-19 spread exacerbated by supply chain disruptions has resulted in a widespread closure of production facilities globally. The possibility of reduced travel in the near future will also affect the auto and aerospace industries. TCS, Infosys, and Wipro have ~10% of revenue from these sectors but HCL Tech and Tech Mahindra derive ~20% revenue from this sector.



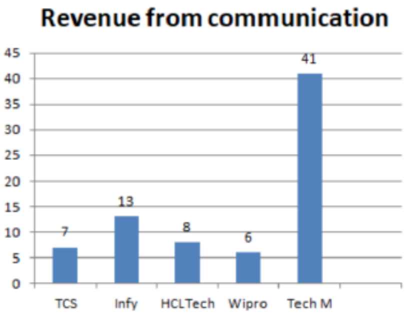
Energy and Utility will be hit hard with low energy prices and demand and supply chain issues in other sub-segments. Companies in this sector are likely to see an impact on multiple fronts, including staffing, revenue, and customer preferences. Lower crude oil prices and declining demand can hit the top-line as well as bottom-line. So, they are likely to cut spending.

Travel and Hospitality is under severe pain and is probably the worst-hit sector due to the pandemic. Countries are under lockdown and people are traveling only if it is unavoidable. There is no tourism activity. According to the International Air Transport Association (IATA), in 2020, the industry passenger revenue could be down to $252B (44% down y/y).

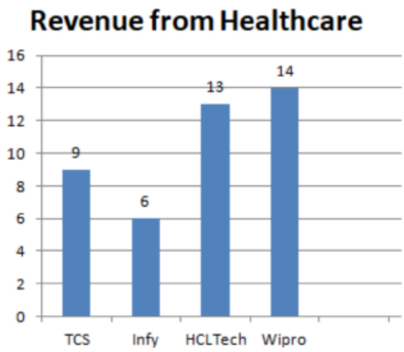
With the summer months accounting for 60–65% of their yearly business, most travel businesses have already gone into huge losses. Also, the recovery is expected to be slow as people will be hesitant to travel and tourism will be very low at least for a few more months. Midcap Indian IT firms such as Mindtree and Hexaware derive more than 10% of revenue from this sector.

Source: IATA

The Communication sector is expected to have a relatively stable performance. Spend on 5G rollout and B2B use cases of 5G may get delayed as industry players reassess capital allocation priorities. Though **revenue from this segment is relatively less for TCS and Wipro, Infosys has 12–15% revenue** from Communication, while **Tech Mahindra derives around 40% revenue** from telecom players. Tech Mahindra has a strong presence in 5G. Telecom is a relatively defensive sector in the current environment and hence telecom technology spends will be resilient. Operators across geographies have pointed to a benign impact on the low-margin handset business and on roaming charges. At the same time, the sudden shift to online sales channels and negligible customer churn due to the lockdown will aid operating margins.



Healthcare: In Life Sciences, cancellation of elective surgery can have an impact on many sub-segments such as medical devices and even certain specialty hospitals and facilities. Overall impact will not be significant on IT spending by the Healthcare sector. In the medium term, there are significant opportunities in Telemedicine services and virtual consultations.



Looking Ahead

Consensus expects margin to hold even when top-line growth is weak due to following reasons:

1) Deferral of wage hikes and lower hiring.
2) Lower sub-contracting cost
3) Lower travel cost due to international travel restrictions
4) Low marketing spend
5) INR Depreciation

The Indian tech industry has quickly cut cost by deferring salary increments and transitioned to work from home. Most companies are planning to permanently shift a substantial part of their workforce to work from home, which could help them save a lot in terms of infrastructure cost. Also, travel during the year will be minimum. In addition, companies are likely to choose digital meet over travel in the coming years. Depreciating INR can improve margin. Consensus estimates that a 1% depreciation in INR aids the EBIT margin for IT companies by 20–30bps.

Good Results by Accenture is Positive for IT Sector

Investors were worried because of the likely impact of Covid-19 driven disruption and H1B visa issues. Accenture's results for March-May quarter came above consensus. Guidance provided also did not suggest any significant deceleration in growth. Outlook for the outsourcing business was better. This is very positive for Indian IT sector. Accenture also expects spending patterns to improve, especially in areas of digital transformation initiatives. According to Accenture, impact on spending across the sectors, (barring retail, travel and manufacturing) will not have material impact.

Domestic Growth

In the Union Budget 2020, allocation toward digital India doubled to $523M. Government plans to convert 1,00,000 villages to digital villages by 2024. Government provided $845M to Bharatnet program and proposed to provide an outlay of $1.13B over a period of five years for the National Mission on Quantum Technologies and Applications.

Other benefits like Software Technology Parks of India (STPI) and Special Economic Zones (SEZ) include 100% tax holiday on exports (for the first 5 years for SEZ) and exemption from excise duties and customs. The government has also allowed 100% FDI with exemption from excise duties and customs for Export Oriented Units (EOUs).

Visa Issues May Not Have Major Impact

The U.S. has implemented temporary suspension of issuance of new H-1B visas and L-1 visas till December. It is only mildly negative for the Indian IT Services sector. This is because the suspension will not affect those already in the U.S. on visas and most of the IT firms have higher local hiring in the U.S. over the last few years. Infosys, Wipro, and HCL Tech have 60–70% of local workforce in the U.S. Also, new/initial applications form <3% of total onsite employee base.

COVID-19 has led to a major disruption within a short span of time. Due to the pandemic, India's IT sector companies had to take a prompt decision to transition to a large scale work-from-home model. India's IT companies managed the transition well. Recent management comment by leading firms indicate that only less than 10% of the revenue witnessed difficulties in the transition. Margins may remain resilient as the cost is expected to be lower due to deferral of wage hikes, lower sub-contracting cost, and INR depreciation. As leading IT firms have strong balance sheets, they will be able to digest the impact due to the pandemic.

On the business side, though the new order flow will be low during the current year, most firms already have a strong order book. In Q4 FY20, TCS had TCV of $8,900M, while Infy and Tech Mahindra had a new order flow of $1,650M and $505M, respectively. Post the pandemic, a wave of digitalization and technology upgrades are expected. India's IT firms, with their huge workforce and strong customer base, could be major beneficiaries. Though the IMF growth forecast for 2020 is weak, a sharp recovery is expected in 2021. Not only the large players, but mid-cap IT firms will also benefit due to the digitalization wave when the pandemic situation subsides.

FAANG Stocks

Facebook:

Facebook operates Facebook, Instagram, Messenger, and Whatsapp apps. It also operates Oculus, a hardware ecosystem that manufactures virtual reality products. It is the world's largest social media company with 2.3B daily active people and 2.9B monthly active people for its family of apps. Facebook Shops will help the company increase its advertiser base significantly from 8M at present. Shift in customer behavior toward online shopping due to the COVID-19 will aid growth.

- Generates revenue through Ads
- High exposure to small businesses
- Expect impact in the near term
- Well positioned due to $60B cash and STI (10% of market cap)
- Recently launched Facebook Shop

Facebook	FY19	FY20E	FY21E
Revenue	70.69	77.12	96.31
Growth % y/y		9%	25%
EBITDA	40.66	37.22	48.28
Margin %	58%	48%	50%
PAT	28.21	24.42	31.14
EPS in $	9.8	8.29	10.82
Return on Assets	16.02	15.07	16.47
Free Cash Flow	21.21	19.71	24.44

In USD Billion Bloomberg Estimate

Apple:

Apple designs Macintosh (Mac), a top-rated personal computer in the world, and leads the digital music industry with its iPods and iTunes online store. It is one of the largest players in the smartphone market in terms of sales. Its products include iPhone, iPad, iPod, and Mac computers. It globally distributes products through its retail stores, online stores, and direct sales force, as well as through third-party cellular network carriers, wholesalers, retailers, and value-added resellers. It also sells and delivers digital content and applications through its iTunes Store, App Store, iBooks Store, and Mac App Store.

- Growth drivers include services segment and 5G iPhones
- The services (~22% of revenue) segment is expected to have a 15–20% CAGR in the next few years
- Services gross margin is around 65% compared with its products segment, which has just ~30% margins
- 5G iPhone (~50% of revenue comes from iPhone sales) is expected to be launched in September
- The company can easily see 10%+ revenue growth in the next two years

Apple	FY19	FY20E	FY21E
Revenue	260.17	264.17	295.91
Growth % y/y		2%	12%
EBITDA	76.47	74.44	84.68
Margin %	29%	28%	29%
PAT	55.25	54.96	62.42
EPS in $	11.88	12.43	14.84
Return on Assets	15.69	16.79	20.48
Free Cash Flow	58.89	62.52	67.66

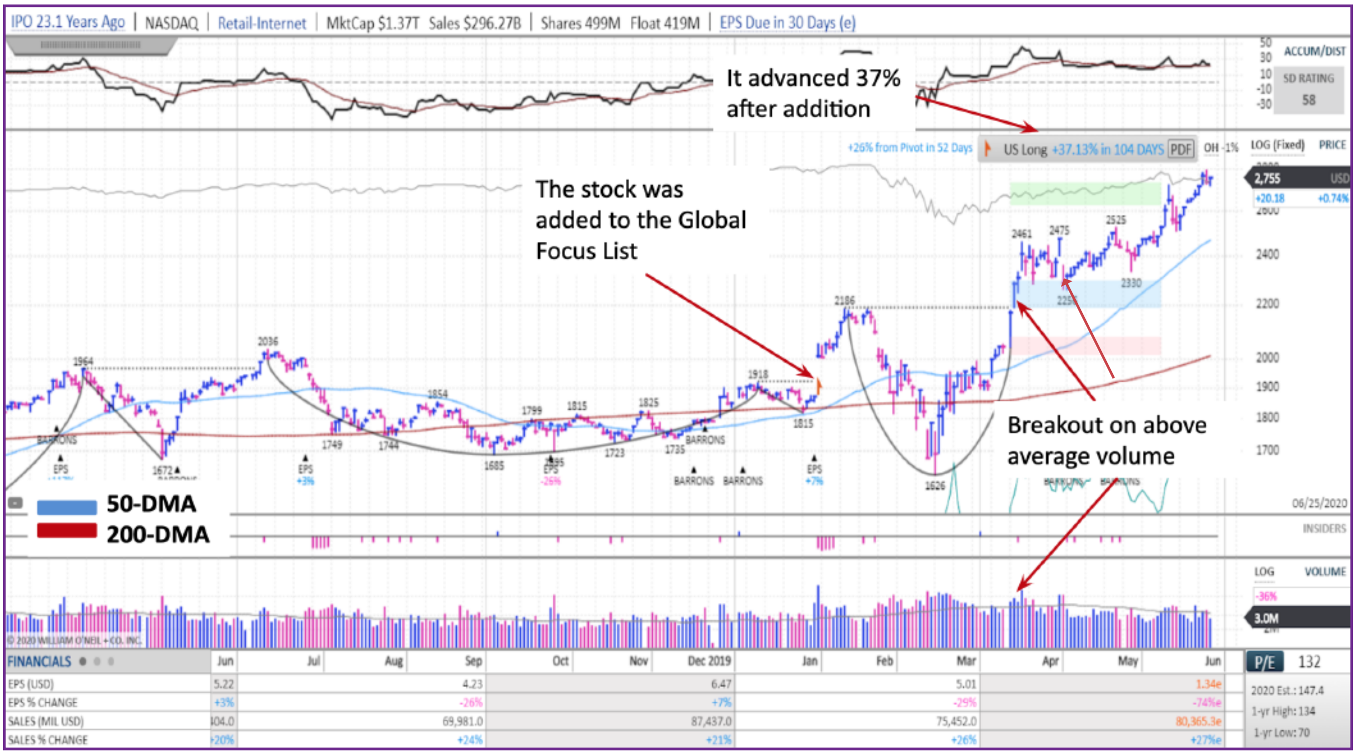
In USD Billion Bloomberg Estimate

Amazon:

Amazon offers an online retail shopping platform through its website, amazon.com, connecting vendors from more than 130 countries and buyers in 185 countries. It is the world's largest cloud computing platform and ecommerce marketplace. Its market leadership position, coupled with continued innovative initiatives, should further increase the gap with competitors.

- Gartner forecasts global IT spending to decline 8% y/y in 2020 due to the COVID-19 impact. However, cloud services will be a bright spot, growing at 19%

- Themes working currently are cloud, cybersecurity, and gaming



Amazon	FY19	FY20E	FY21E
Revenue	280.52	346.1	407.44
Growth % y/y		23%	18%
EBITDA	43.35	44.66	61.06
Margin %	15%	13%	15%
PAT	17.01	15.63	25.83
EPS in $	33.75	33.75	52.1
Return on Assets	5.97	5.25	7.49
Free Cash Flow	21.65	26.03	40.49

In USD Billion Bloomberg Estimate

Google:

Alphabet Inc, the parent company of Google, manages the world's largest Internet search engine, Google.com. The cloud and mobile businesses will be its main growth drivers. Alphabet provides online search, internet content services, and web-based and desktop software applications. It dominates the online search market with an estimated market share of 95% in mobile and 60% in PC. Q3 2018 revenues by segment: Google, 99%; other, 1%. Its Google segment includes primary internet products such as Search, YouTube, Android, Cloud, Maps, and hardware such as Chromecast, Nexus, and Chromebooks.

- YouTube and Cloud business are the major growth drivers for the company
- Ad business has matured. Not much upside there
- In cloud business, it expects to become No. 1 by 2023
- Currently AWS is No. 1 in $200B cloud market followed by Azure
- Google Cloud is at the third position. YouTube is under monetized as it concentrates on making platform brand safe

Google	FY19	FY20E	FY21E
Revenue	131.76	137.74	166.41
Growth % y/y		5%	21%
EBITDA	56.01	56.86	70.65
Margin %	43%	41%	42%
PAT	31.67	37.8	48.41
EPS in $	45.33	52.7	66.68
Return on Assets	13.5	11.12	14.48
Free Cash Flow	30.97	30.67	42.17

In USD Billion Bloomberg Estimate

Netflix:

Netflix offers subscription-based video streaming services for TV shows, documentaries, and movies to more than 183M members in over 190 countries. It is the largest online streaming service provider. The company's vast content library and sufficient ready-to-release original content for 2020 gives it an edge over its competitors.

- The stock was lagging in 2019 due to entry of competitors
- Disney Plus and Apple TV Plus launched in November 2019, Peacock (from Comcast) in April, and HBO Max in May.
- The stock started shooting up as home confinement due to COVID-19 accelerated shift to streaming
- Underlying theme: Competition, high debt took a back seat due to COVID 19 benefit

Netflix	FY19	FY20E	FY21E
Revenue	20.15	24.78	29.29
Growth % y/y		23%	18%
EBITDA	3.13	4.56	6.07
Margin %	16%	18%	21%
PAT	2.18	3.22	4.36
EPS in $	4.84	6.84	9.15
Return on Assets	6.22	8.53	9.61
Free Cash Flow	-3.14	-1.18	-2.04

In USD Billion Bloomberg Estimate

Indian IT Stocks

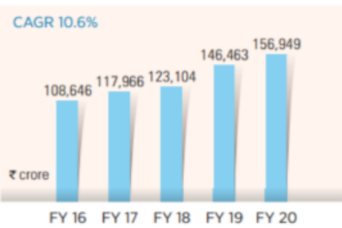
TCS

The company provides various business services such as computer programming, consulting, and related activities. It is the global leader in IT services and digital and business solutions. The company has 4,48,464 employees across 46 countries. The company's geographic footprint covers North America, Latin America, the United Kingdom, Continental Europe, Asia- Pacific, India, and Middle-East and Africa. TCS considers industry verticals as its go-to-market business segments. The five key vertical clusters are: Banking, Financial Services & Insurance (BFSI), Retail and Consumer Business, Communications, Media and Technology (CMT), Manufacturing and Others. The last category includes Life Sciences and Healthcare, Energy, Resources and Utilities, Public Services and others.

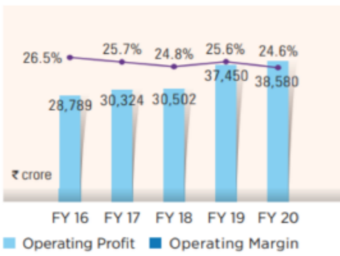
Financial Performance

In Q4, net sales advanced 5.1% y/y to Rs 39,946 crore. Further, EBIT margins improved 10bps q/q to 25.1%, led by operational efficiency. Net margin for the quarter stood at 20.2%. Cash flow from operations came in at 109.4% of net profit. The company won a deal worth $8.9B with $2.4B from BFSI and $3.1B from the retail segment ($1.7B was from Walgreen Boots deal). North America witnessed deals worth $5.3B. For the full-year, the company grew at 7.1% in constant currency, 7.2% in terms of the rupee, and 5.3% in terms of the dollar and recorded revenue of $22,031M. Net income stood at Rs 3, 23,400M with net margin of 20.6%.

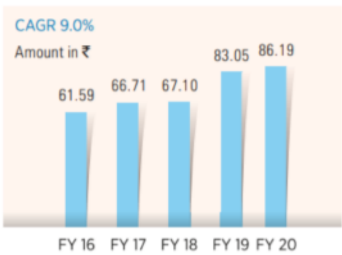
Revenue Trend



Operating Profit Trend

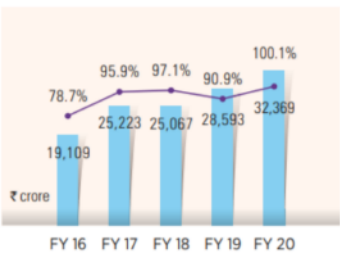


Earning Per Share*



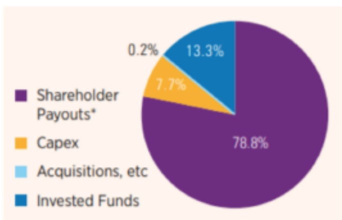
* Earnings per share is adjusted for bonus issue

OCF# and Cash Conversion



Operating Cash Flow

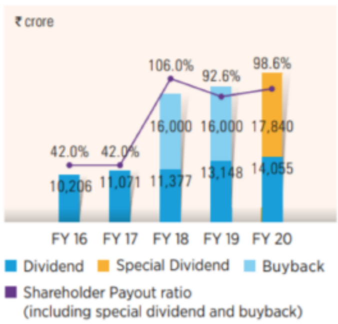
Cash Usage



(FY 16 to FY 20)

* including final dividend for FY 2020

Shareholder Payouts



Source: Company presentation

Sector-wise and Geography-wise Performance

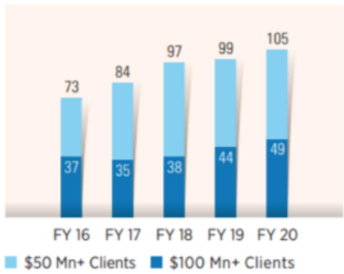
Life Science and Health Care sectors witnessed double-digit growth of 16.2%, which is the highest gain recorded among all sectors. Similarly, Communication & Media grew 9.3% y/y. Manufacturing grew 7.0% y/y, Retail & CPG grew 4.2% y/y, and Technology & Services grew 3.5% y/y. However, the BFSI vertical witnessed a degrowth of 1.3% y/y. A large part of revenue leakage was due to supply-side impact arising out of delays in or inability to activate remote access for a few offshore teams due to regulatory concerns. All growth numbers are in constant currency terms.

Geography-wise, Europe continues to outperform, growing 11.9% while the U.K. grew 5.4%. North America was flattish at 0.2%. Among the emerging markets, Latin America and APAC grew 3.9% and 3.5%, respectively, while MEA grew 1.3% and India declined 1.9%.

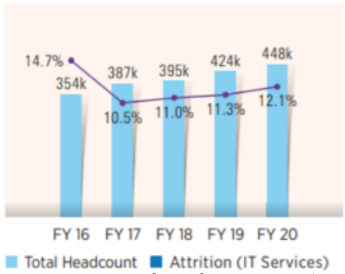
Client Metrics

The company added five more clients in the $100M+ band, taking the total count to 49; six more in the $50M+ band, bringing the total to 105; 25 in the $20M+ band, taking the total count to 240; 20 clients in the $10M+ band, bringing the total to 391; 33 clients in the $5M+ band, bringing the total to 565; and 64 clients in the $1M+ band, taking the total to 1,072.

Client Metrics



Employee Metrics



Source: Company presentation

Impact Due to COVID-19

Management expects the impact in revenue to occur in Q1 FY21E, primarily due to demand constraints (~80%) rather than supply constraints. In Q4 FY20, sectors such as BFSI witnessed supply-side constraints as few clients were unable to move BPO functions to WFH delivery due to security and regulatory requirements. On the positive side, management is hopeful about consulting services gaining momentum in the coming quarters as clients will be interested to migrate to the cloud.

Outlook

Management expects demand-side constraints to remain in the short-to-medium term. Margins are likely to be maintained at 25% and management has reiterated that margin guidance of 26–28% remains intact in the long term and is expected to be achieved in FY22E.

O'Neil Methodology and Technical Viewpoint:

The stock has made a stage-one consolidation base. Fresh positions can be initiated once the stock breaks out of the base on above average volume.

Price strength is at 52, with an RS line moving sideways.

Its buyer demand rating stands at B+, which is considered good.

There has been consistent growth in sales and earnings over the last five quarters, leading to EPS Rank of 74, which indicates a fair fundamental profile.

The number of fund holdings has increased 1% y/y in the recent quarter.

TCS	FY20	FY21E	FY22E
Revenue	156,900	159,000	173,200
Growth % y/y		1%	9%
EBITDA		41,857	46,511
Margin %		26%	27%
PAT	32340	31475	35384
EPS in Rs	86.2	84.2	94.9
Return on Assets	26.9	24	24.9
Free Cash Flow	32334	29452	31039

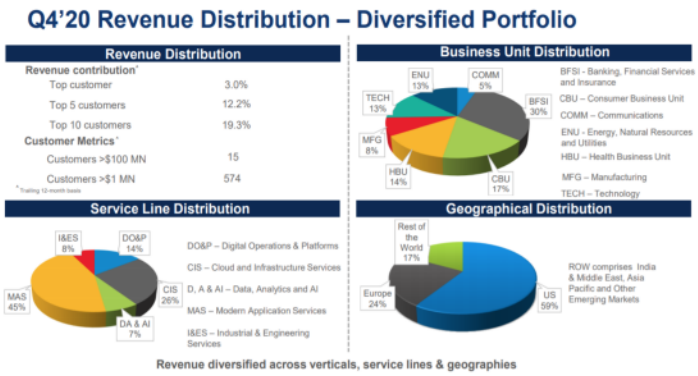
In INR Crore Bloomberg Estimate

WIPRO

The company operates in the field of information technology, consulting, and business process. It offers services through two segments: IT services and IT products. The company's IT Services business provides a range of IT and IT-enabled services. The IT products segment provides a range of third-party IT products, which allows it to offer IT system integration services. The company has over 175,000 dedicated employees serving clients across six continents. It has close partnerships with Global 2000 companies.

Recent Quarter Performance

The company posted revenue of Rs 15,750 crore (+2% q/q; +3.8% y/y) in Q4 FY20. IT services revenue grew 1% q/q in constant currency terms. Digital revenue is 41.2% (+140bps q/q) of total revenue for Q4 FY20. EBIT margin contracted to 16.1% (-101bps) this quarter due to an increase in employee expenses (+100bps). IT services operating margin was at 17.6%, down 0.8% q/q and 0.4% y/y. Net income posted a 5.3% q/q decline to Rs 2,326 crore. Operating profit witnessed a decline of 3.1% q/q to Rs 2,638.9 crore during the quarter. However, EPS grew in double digits by 11.2% y/y for the year. During Q4 FY20, the company added five accounts to the >$100M+ bucket. Further, voluntary attrition on an LTM basis has reduced to 14.7%. FPP mix stood at 63.2% for Q4 FY20, whereas the offshore mix stood at 48.2% for the quarter.



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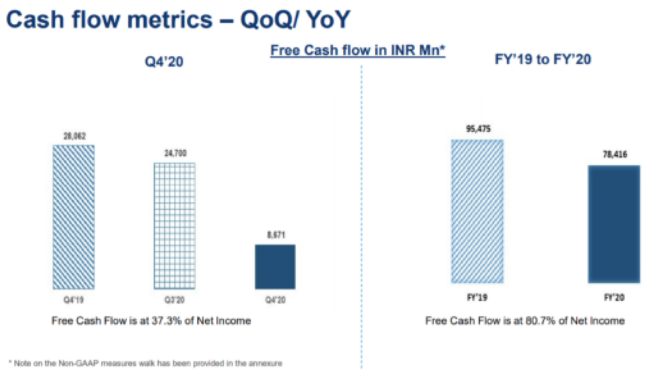

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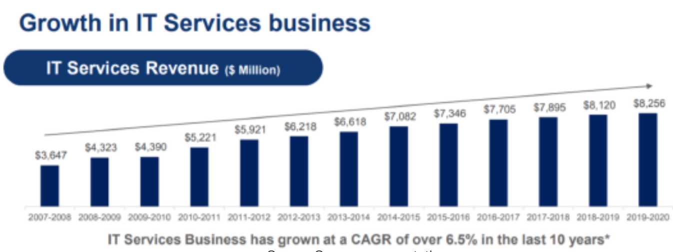


Source: Company presentation

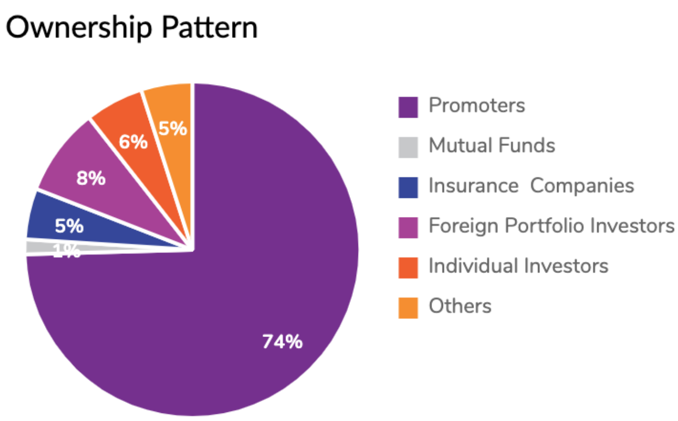
Source: Company presentation

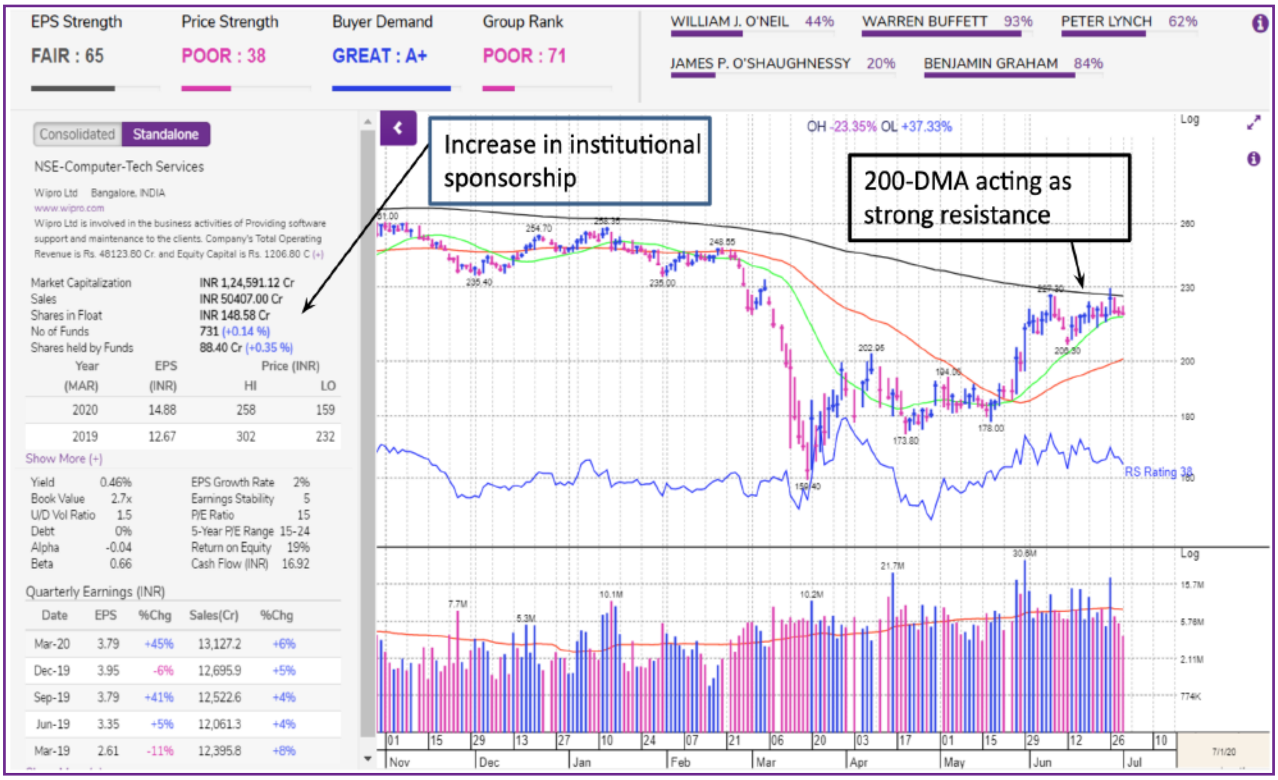
Impact of COVID -19

Geography-wise, India got impacted in terms of supply whereas the U.S. and Europe experienced an impact in demand due to the Covid-19 crisis. Management witnessed a spill-over effect on IT expenditure due to global slowdown. This can be in terms of a cut in the budget, pricing pressure, and reduction in discretionary expenditures. Major verticals that are expected to be largely impacted include travel and hospitality, aviation, oil & gas due to fluctuating oil prices, and consumer business units except for food & groceries, among others. Similarly, from the BFSI vertical perspective, volatility in interest rates could negatively impact the sector while higher refinancing activities can act in favor.

Outlook

Management decided not to provide revenue guidance for the quarter ending June 30, 2020, in light of the uncertainty around the course of the COVID-19 pandemic. Management stated that they do not have visibility into the extent to which it will disrupt the company's operations. However, management will resume providing revenue guidance when the certainty of both demand and supply-side factors increase in due course. Further, management believes that there will be demand in areas such as modernization, cloud migration, supply chain, automation, and analytics from the clients' side. The company will focus on client mining in those areas to gain market share.





O'Neil Methodology and Technical Viewpoint:

The stock has been trading in the range of Rs 200-230 for the last four weeks and finding resistance near its 200-DMA (Rs 227). It is crucial for the stock to reclaim its 200-DMA on above average volume for further upmove.

Price strength is at 38, with an RS line moving sideways.

Its buyer demand rating stands at A+, which is considered great.

EPS Rank of 65 indicates a fair fundamental profile.

The number of fund holdings and shares held by funds have increased 0.1% and 0.4%, y/y, respectively, in the recent quarter.

Wipro	FY20	FY21E	FY22E
Revenue	61,023	60,816	63,590
Growth % y/y		0%	5%
EBITDA		11,656	12,477
Margin %		19%	20%
PAT	9,722	8,831	9,620
EPS in Rs	17	15.5	17
Return on Assets	11.78	10.3	11.6
Free Cash Flow	9,674	7,062	8,479

In INR Crore Bloomberg Estimate

INFOSYS

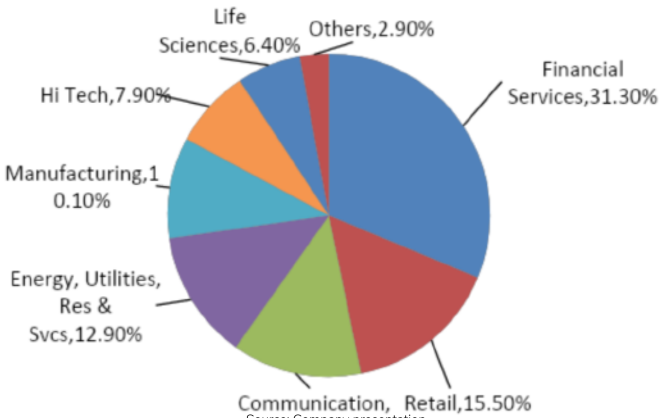
Infosys is India's second-largest provider of consulting and IT services across the globe. The company provides business consulting, application development and maintenance, and engineering services to 1,251 active clients across Banking, Financial Services, Insurance, Retail, Manufacturing, and Utilities sectors in 50 countries. The company has a proprietary core banking software, Finacle, which is used by several leading banks in India, the Middle East, Africa, and Europe.

Financial Performance

The company witnessed growth of 9.8% in constant currency and achieved 21.3% of operating margins during the financial year. Its digital revenue grew 38% in constant currency and in Q4, it became 42% of the company's overall business. It signed $9B+ of large deals for the full-year. The company's earnings per share grew at 8.3% in dollar terms. Further, the company had the highest cash collection in Q4 and indeed for the full fiscal year that has just ended.

In Q4, the company grew 6.4% in constant currency on a y/y basis and delivered 21.1% operating margins with $1.6B in large deals, some of which were in the last two weeks of March. The company also won 12 large deals: seven from America and five from Europe. The company currently has a very strong cash position of $3.6B with no debt on the balance sheet.

Revenue Breakup



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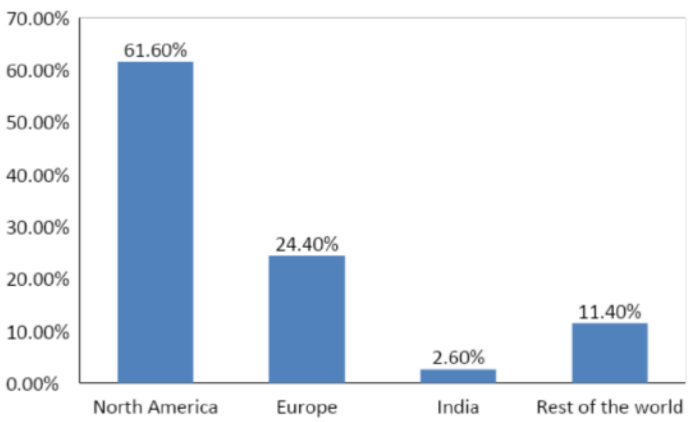


Source: Company presentation

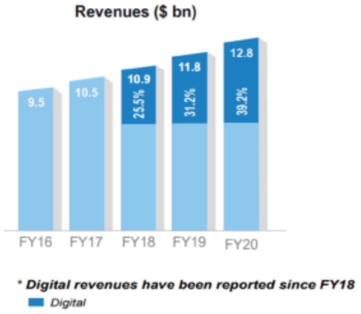
Robust balance sheet continues to remain strong

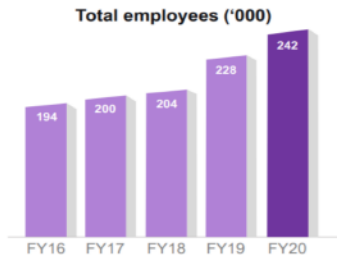
The company currently has a robust cash position of $3.6B with no debt on the balance sheet. Also, the company has a zero promoter pledge. Further, its revenue has been increasing every quarter for the past four quarters. It has the potential for generating strong cash from its core business.

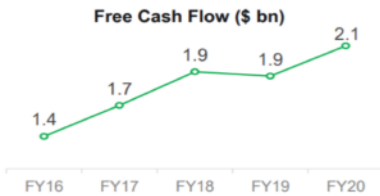
It saw improving cash flow from operations for the last two years. For FY20, operating cash flow grew 15.4% to $2.611B. Free cash flow grew 12.1% and crossed $2B for the first time. Cash flows are robust and operating cash flows have increased to Rs 17,003 crore in FY20 from Rs 14,841 crore in FY19.

Focus on R&D

The company has developed/commercialized indigenous innovative technologies through a focus on R&D. The company has established the world's first carbon dioxide to lipid pilot plant and five TPD Bio-methanation plants. Also, it has completed the commissioning of the revamped DHDS unit at Gujarat Refinery with indeDiesel Technology for BS-VI compliance. Further, the company has developed Indinaoil Innovative Additive (INNOVA) for OEM approvals for lubes.







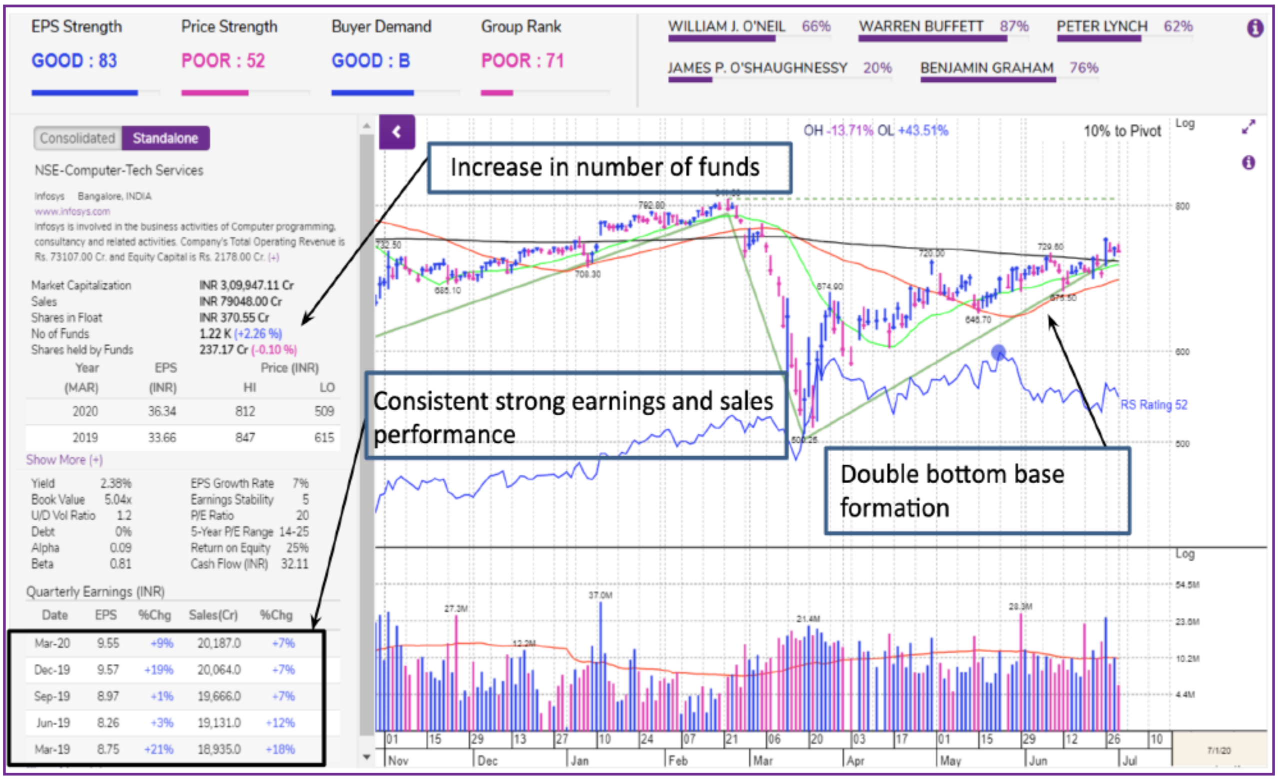
Source: Company presentation

Risk related to COVID-19

Most of its clients' business operations may be negatively impacted due to the economic downturn, resulting in postponement, termination, suspension of a few ongoing projects, and/or reduced demand for services and solutions. Some of the clients or suppliers have invoked force majeure clauses in the contracts with them, negatively impacting the business with limited recourse. Lower profitability and prolonged payment term requests from clients can impact cash flows negatively and may impact the ability to provide dividends to shareholders.

Outlook

Management decided not to provide revenue guidance for the quarter ending June 30, 2020 in light of the uncertainty around the course of the COVID-19 pandemic. Management stated that they do not have visibility into the extent to which client businesses will be marred by this volatility. Thus, it will be appropriate to provide annual guidance at this stage.



O'Neil Methodology and Technical Viewpoint:

The stock has made a stage-one double-bottom base. Fresh positions can be initiated once the stock breaks out of the base on above average volume.

Price strength is at 52, with an RS line moving sideways.

Its buyer demand rating stands at B, which is considered good.

There has been consistent growth in sales and earnings over the last five quarters, leading to EPS Rank of 83, which indicates a good fundamental profile.

The number of fund holdings has increased 2.3% y/y in the recent quarter.

Infosys	FY20	FY21E	FY22E
Revenue	90,791	92,971	101,600
Growth % y/y		2%	9%
EBITDA		22,324	25,197
Margin %		24%	25%
PAT	16,594	16,042	18,138
EPS in Rs	38.9	37.9	42.8
Return on Assets	18.7	16.6	17.9
Free Cash Flow	15,626	13,917	15,556

In INR Crore Bloomberg Estimate

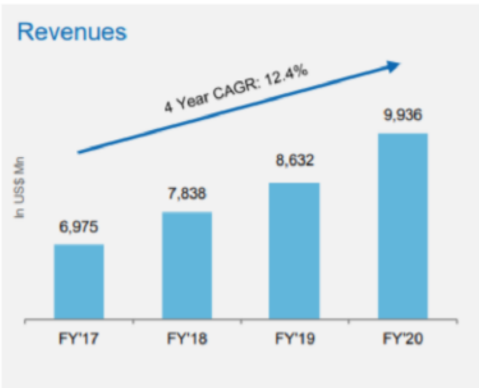
HCL TECH

he company is a leading global IT services company. It provides a range of software, infrastructure, and business process outsourcing services. HCL offers its services and products through three business units - IT and Business Services (ITBS), Engineering and R&D Services (ERS), and Products & Platforms (P&P). The company delivers solutions across Financial Services, Manufacturing, Telecommunications, Media, Publishing, Entertainment, Retail & CPG, Life Sciences & Healthcare, Oil & Gas, Energy & Utilities, Travel, Transportation & Logistics, and Government.

Financial Performance

The company continued to deliver an industry leading growth. In FY20, the y/y growth of LTM stood at 16.7% in constant currency. The company's strong growth is driven by industry leading organic growth and acceleration of its Mode 2 and Mode 3 revenue. It witnessed strong double-digit growth across all segments, geographies, and verticals. Mode 2 and Mode 3 revenues for the year now make up 33% of total revenues, increasing from 28.4% in FY19, resulting in a combined growth of 34.7% y/y in constant currency. Mode 2 grew at a solid 27.6% y/y in constant currency and Mode 3 grew at 45.3% y/y in constant currency. Revenue grew 17% y/y to Rs 70,678 crore. Net income advanced 9.3% y/y to Rs 11,062 crore. Revenue growth in constant currency stood at 16.7% on a y/y basis. EBIT margins stood at 19.6% for FY20, beating the guidance of 19.0–19.5%. ROE stood at 23.6%. Cash position remains strong with net cash at $1,359M.

In Q4 FY20, the company's revenue grew 2.5% q/q and 16.3% y/y to Rs 18,590 crore. Net income grew 3.8% q/q and 22.8% y/y to Rs 3,154 crore. Revenue in constant currency terms was up 0.8% on a q/q basis and 13.5% on a y/y basis.



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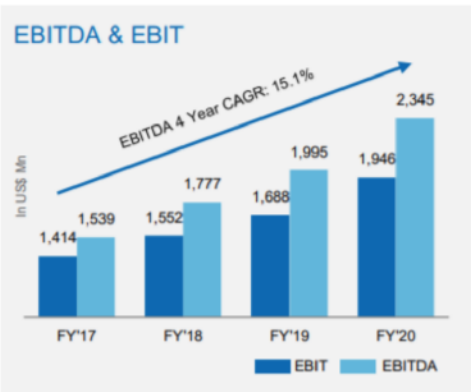

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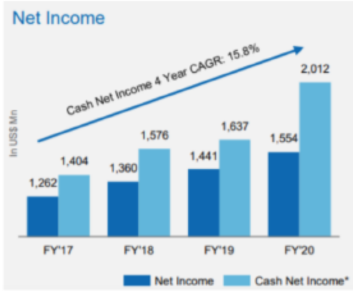
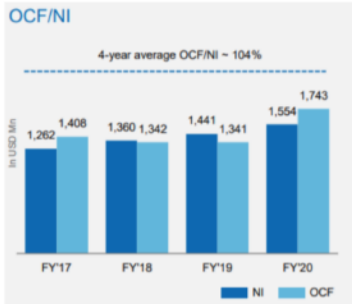
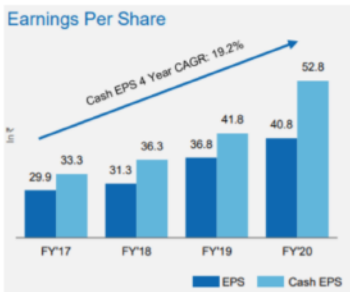






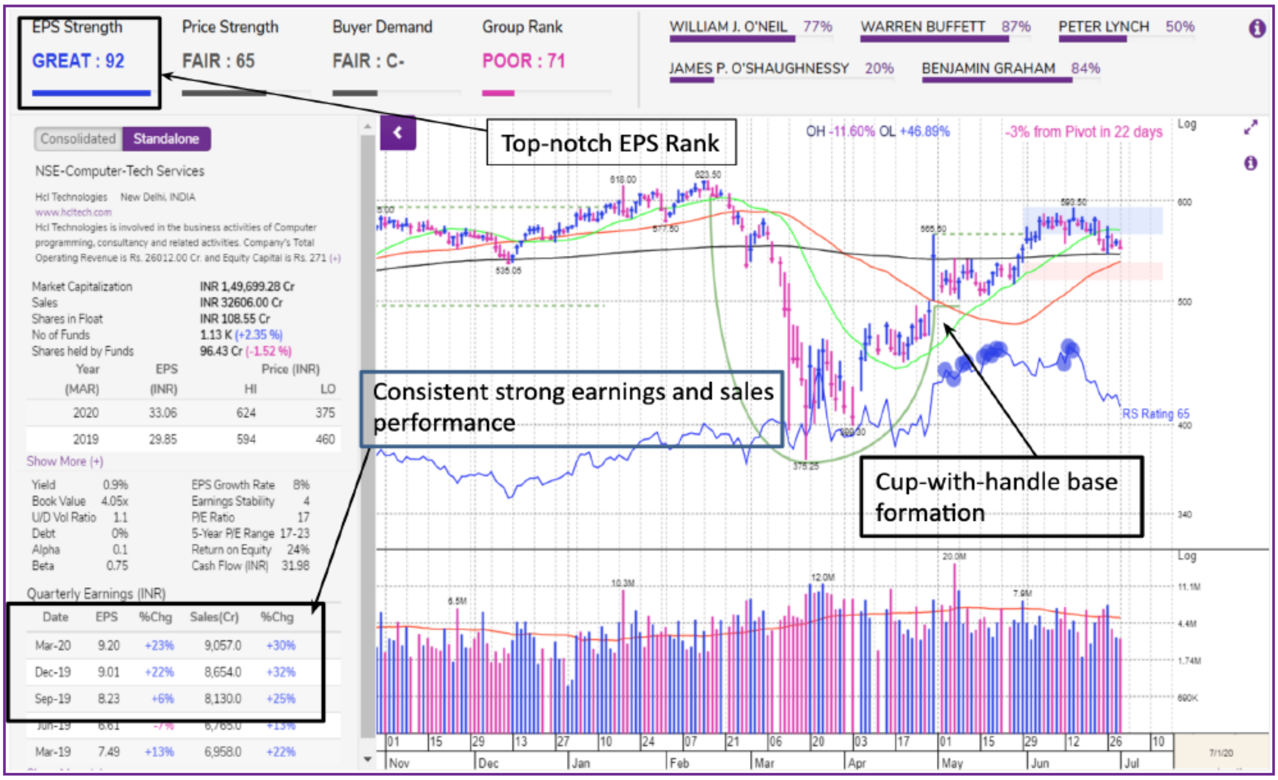
Source: Company presentation

Healthy Deal Wins

In FY20, the company's total deals stood at 53, with Q4 contributing 14 deals. Those belong to key industry sectors such as Retail & CPG, Manufacturing and Financial Services, and Hi-Tech and Telecom, among others. The deals will start aiding revenue in Q2 FY21. In Q4 FY20, most of the deals were signed in the first two months and witnessed a significant decline in March. The ramp-up of deals has already started with management not witnessing any delay as such.

Outlook

Per management's commentary, there will be a reduction in Q1 FY21 revenue. Revenue is expected to stabilize in Q2 FY21 and then grow in H2 FY21. Taking the worst-case scenario, there may be a decline in revenue Q3 FY21 after the stability in Q2 FY21 due to the resurgence of the COVID-19 outbreak. The company is well positioned in the digital space and has maintained a healthy partnership with its clients.



O'Neil Methodology and Technical Viewpoint:

The stock has made a stage-one cup-with-handle base. Fresh positions can be initiated once the stock breaks out of the base on above average volume.

Price strength is at 65, with an RS line moving downwards.

Its buyer demand rating stands at C-, which is considered poor.

EPS Rank of 92 indicates a strong fundamental profile.

The number of fund holdings have increased 2.4% y/y in the recent quarter.

HCL	FY20	FY21E	FY22E
Revenue	70686	74092	60064
Growth % y/y		5%	-19%
EBITDA		17,427	18,997
Margin %		24%	32%
PAT	11058	10967	12271
EPS in Rs	40.7	40.5	45.4
Return on Assets	15.9	13.3	13.7
Free Cash Flow	10652	6561	10473

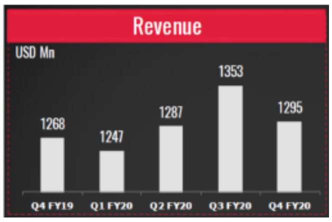
In INR Crore Bloomberg Estimate

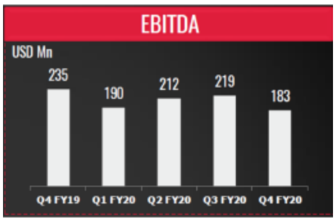
TECH MAHINDRA

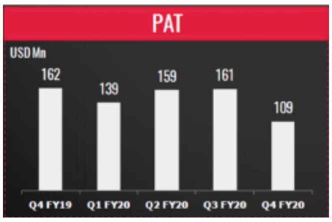
The company offers computer programming, consultancy, and related services. Its segments include Information Technology (IT) Services and Business Processing Outsourcing (BPO). The company operates in various sectors, including telecom and enterprise solutions. The telecom business provides consulting-led integrated portfolio services to customers, which include telecom equipment manufacturers and service providers.

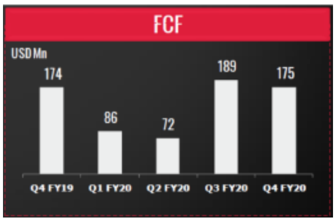
Financial Performance

During Q4 FY20, the company posted a 3.3% decline in revenue in constant currency terms. In rupee terms, the company witnessed a -1.7%/6.7% q/q & y/y growth in revenue to Rs 95B. The Communications sector, contributing to ~41% of revenue, declined the most (-6% q/q). On a similar front, BFSI vertical also declined ~14% q/q. PAT witnessed a decline of 29.8% q/q to Rs. 8.0B on the back of a one-off, i.e., impairment of goodwill of Rs. 2.2B. EBIT moderated by 19.4% q/q to Rs. 9.5B and EBIT margin for the quarter posted deteriorated 220bps q/q to 10.0%. This includes 100bps cost impact due to CSR, per management. Further, a transition cost impact in AT&T deal and a few large deals won in Q3 FY20, together with the COVID-19 impact led to a reduction in volume by 100bps.





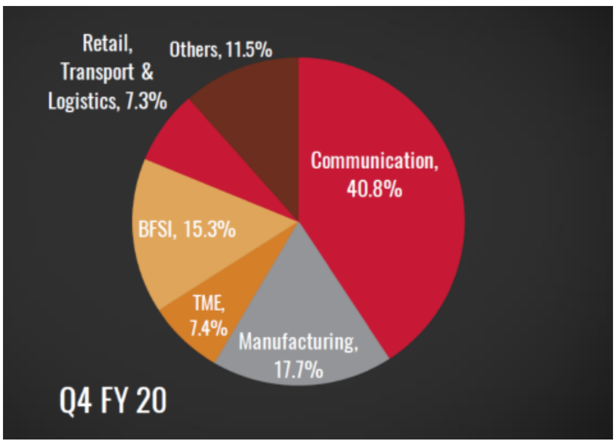




Source: Company presentation

Geography-wise Performance

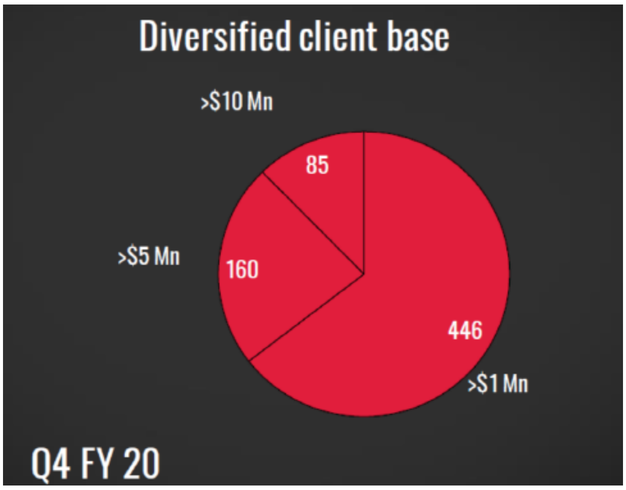
The U.S. business, which contributes 48% to revenue, witnessed a decline of 3.1% q/q and Europe, which accounts for 27% of the total revenue, saw a degrowth of 3.5% q/q. On the other hand, the rest of world saw growth of 3.1% q/q. The decline in revenue in the U.S. and Europe was primarily driven by the fall in demand. This is expected to continue in Q1 FY21 as well. Lower transition business led to a fall in revenue in the U.S., whereas revenue from the Europe business was down due to currency fall.



Source: Company presentation

Diversified Client Base and Robust Deal Wins

The company has 85 clients in the $10M+ band and 160 clients in the $5M+ band. In addition, more than 440 clients belong to the $1M+ band. The company has announced ~$1.3B of deal wins; $900M came from a BFSI client, where the company would be working together with the client on managed services and digital transformation.

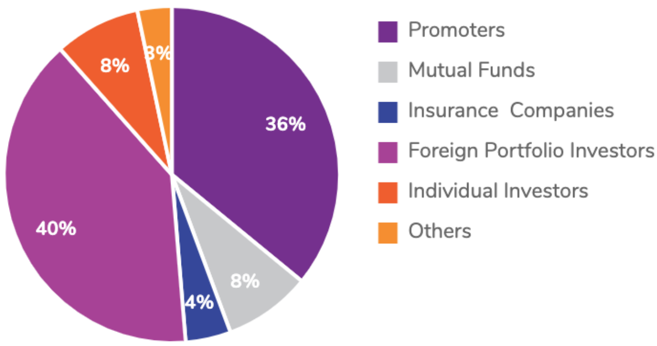


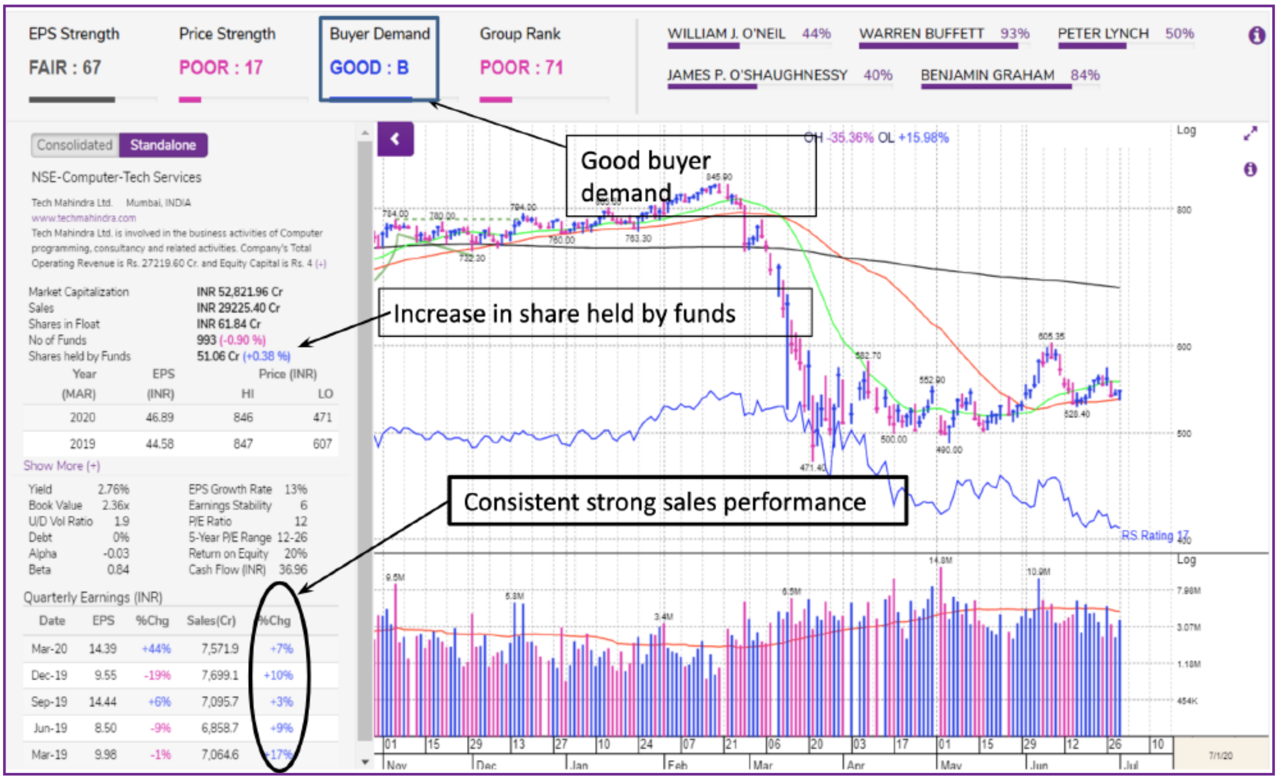
Source: Company presentation

Outlook

Management anticipates short-term impact in revenue and decided not to provide revenue guidance for the quarter ending June 30, 2020, in light of the uncertainty around the course of the COVID-19 pandemic. Management commented that margins can be built up by building momentum in revenue growth. In Q1 FY21E, demand-side pressure can impact revenue and margins rather than supply constraints, which are expected to come down in Q1 FY21. Management will focus on cost savings around sub-contracting and travel. Further, management stated that they will plan accurately once a base EBIT margin is achieved, and going forward, it will be able to mitigate risk further.

Ownership Pattern





O'Neil Methodology and Technical Viewpoint:

The stock recorded a correction in March, in line with the general market correction. Following that, the stock has been trading sideways.

Price strength is at 17, with an RS line moving downwards.

Its buyer demand rating stands at B, which is considered good.

EPS Rank of 67 indicates a fair fundamental profile.

The number of fund holdings have increased 0.4% y/y in the recent quarter.

Tech Mahindra	FY20	FY21E	FY22E
Revenue	36867	37302	40333
Growth % y/y		1%	8%
EBITDA		5,582	6,500
Margin %		15%	16%
PAT	4185	3682	4393
EPS in Rs	48	42.6	50.3
Return on Assets	11.4	9.4	10.7
Free Cash Flow	3608	3458	3792

In INR Crore Bloomberg Estimate

NIIT Technologies

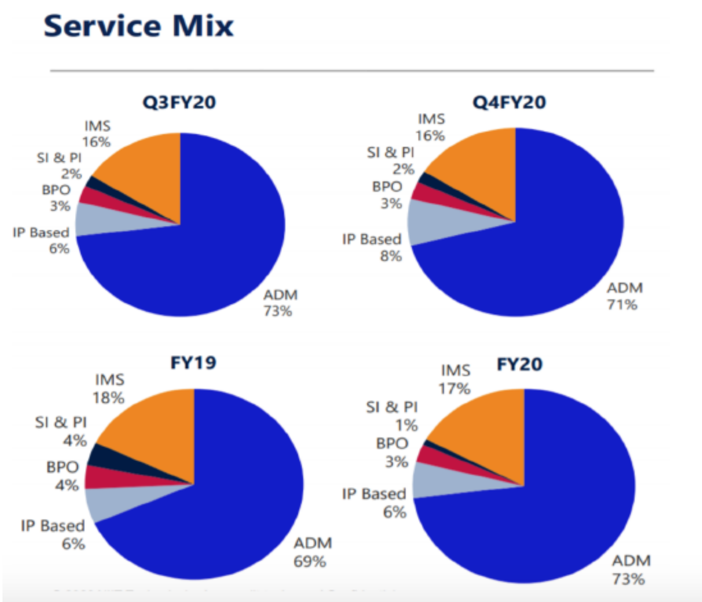
NIIT Tech is a global IT solutions company with a client base across North America, Europe, Asia, and Australia. It offers its clients the domain expertise and emerging technologies needed to move their businesses forward as smoothly as possible. This is aided by its high-end capabilities in data analytics, automation, cloud, and digital computing, among others. Its key sectors include 1) banking and financial services 2) insurance 3) travel, transportation, and hospitality.

The company has world-class development centers at New Delhi, Kolkata, Mumbai, Bangalore, Atlanta, London, and Singapore. It delivers its global services directly and through its network of subsidiaries and overseas branches. The company also has a sound business continuity plan in place that can address any natural or accidental disasters at its development and operations centers.

Financial Performance

The company's revenue grew 13.81% over the last year and averaged about 14.30% for the past three years. Revenue growth had a slight decrease mainly due to revenue softness in Q4. The q/q growth of 3.34% can be considered good especially given the major headwinds faced by the company due to the Covid-19 outbreak. Growth was up 14.10% compared with that of Q4 FY19. Net profit moderated on a q/q basis, mainly due to the increased interest and tax payments. EPS growth is strong, considering the three-year average. If we look at the quarterly EPS, it witnessed an 83% y/y growth in Q4. EBITDA margin stood at 18.1% during the quarter and at 17.9% for FY20. Its margin of 18.1% stood almost flat as compared with Q2 and Q3. In Q3, margins were flat due to the huge investment sums that went into two of the four large deals that were closed in Q3. In Q4, EBITDA margins remained flat, which is positive, due to rigorous cost-cutting measures, efficient transfer to work-from-home, and tailwinds from the large deals closed in the last two quarters.

The company targets a minimum EBITDA margin of 18% and has almost achieved it. Sales growth has been a little slow at 9.79% for the past five years and 11% for the past three years. The company has signed seven large deals in the last two quarters, which ensures good business for them in the future. The share buyback has been a positive signal as far as management's confidence is concerned. Even the promoters have increased their positions in the company to more than 70% from 36%.



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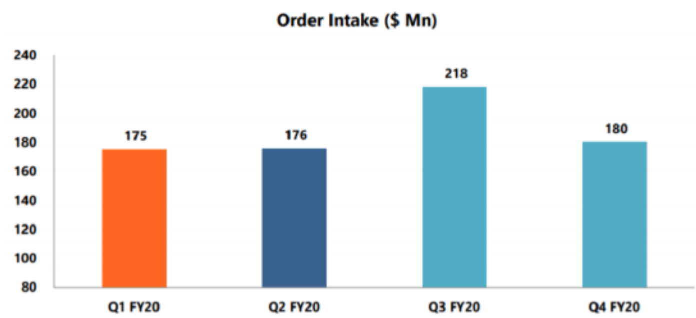
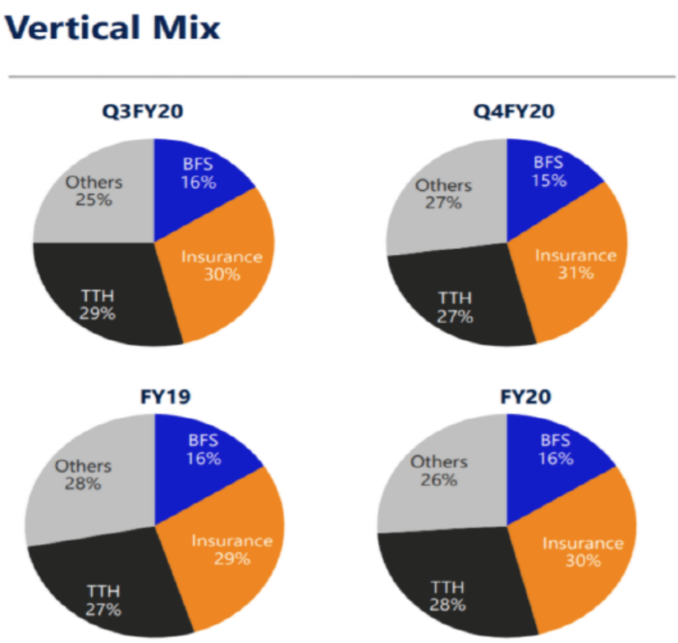


Source: Company presentation

Performance across geographical divisions and diversified client mix

The EMEA markets have performed well, even under economic pressures. The increase in revenue is due to key accounts in BFS, NITL, and Whishworks. The U.S. markets were one of the worst hit by the Covid19 crisis, which is why the U.S. orders decreased slightly, especially in the TTH sector. About 27% of the firm's revenue comes from the top five clients, and about 37% from the top 10. The multimillion dollar clients have also increased to 106.



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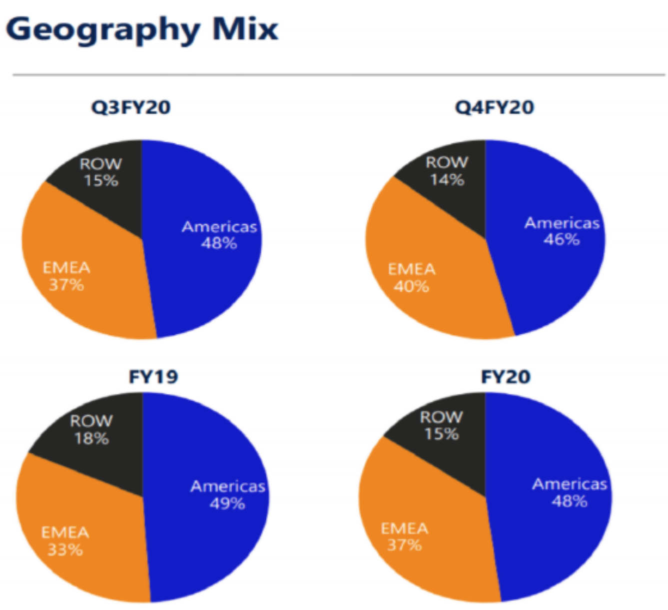

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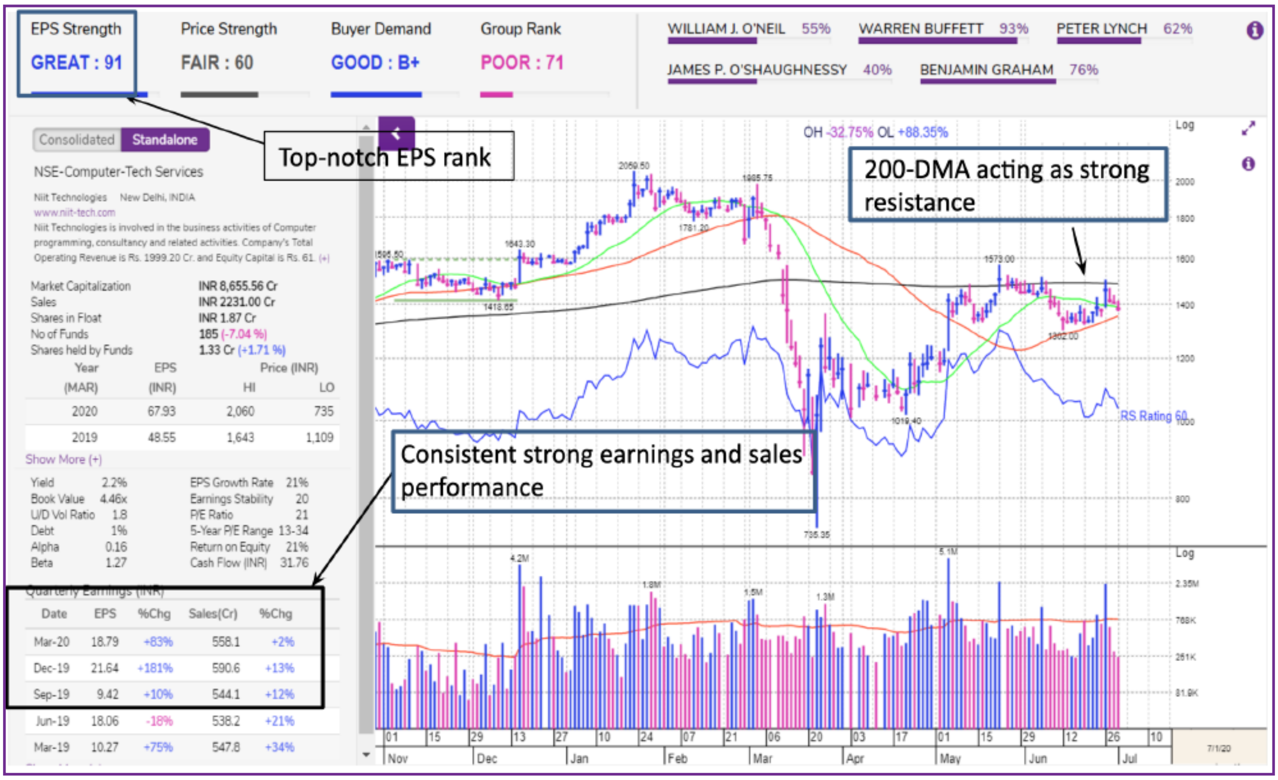

O'Neil Methodology and Technical Viewpoint:

The stock has been trading in the range of Rs 1,300-1,550 for the last four weeks and finding resistance near its 200-DMA (Rs 1,489). It is crucial for the stock to reclaim its 200-DMA on above average volume for further upmove.

Price strength is at 60, with an RS line moving sideways.

Its buyer demand rating stands at B+, which is considered good.

There has been consistent growth in sales and earnings over the last three quarters, leading to EPS Rank of 90, which indicates a strong fundamental profile.

Shares held by funds have increased 1.7% y/y in the recent quarter.

NIIT Technologies	FY20	FY21E	FY22E
Revenue	4,184	4,501	4,969
Growth % y/y		8%	10%
EBITDA		766	865
Margin %		17%	17%
PAT	449	468	545
EPS in Rs	71.8	76.3	88.6
Return on Assets	14.8	13.5	15.6
Free Cash Flow		403	527

In INR Crore Bloomberg Estimate

Mindtree

The company is an international IT consulting and implementation enterprise that provides business solutions through global software development. The company consists of four industry verticals – retail, CPG and manufacturing (RCM), banking, financial services and insurance (BFSI), high technology and media (Hi-tech) (erstwhile technology, media, and services-TMS) and travel and hospitality (TH). The company provides services in the fields of agile, analytics and information management, application development and maintenance, business process management, business technology consulting, cloud, digital business, independent testing, infrastructure management services, mobility, product engineering, and SAP services.

Financial Performance

For the quarter, its revenue stood at Rs 20,505M with growth of 11.48%. For the full-year, its revenue is Rs 77,643M, with growth of 10.6% on a y/y basis. The company closed FY20 with the largest-ever deal wins in its history of $1.2B and revenue growth of 9.4% in constant currency terms. Its EBITDA grew 2.4% to Rs 10,898M from Rs 10,645M in FY19 though EBITDA margin declined 120bps to 14.0% from 15.2% in FY19. Through margin improvement initiatives undertaken during the year, EBITDA margin for H2 grew to 16.4% from 11.5% in H1. Absolute EBITDA marked a CAGR of 7.3% from FY16 to FY20. PAT is Rs 6,309M for FY20 with an increase of 16.3% from Rs 7,541 in FY19. CAGR is 3.4%.

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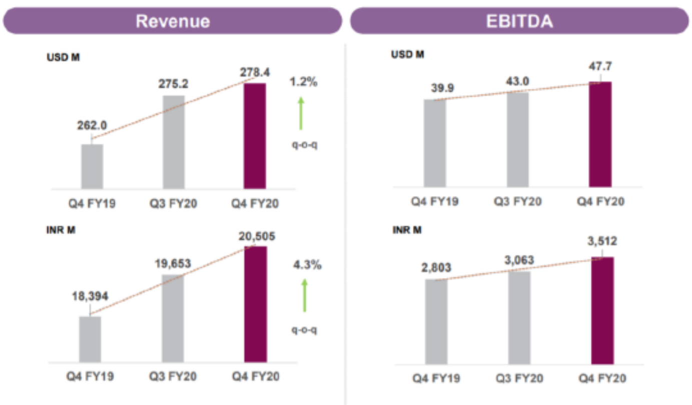
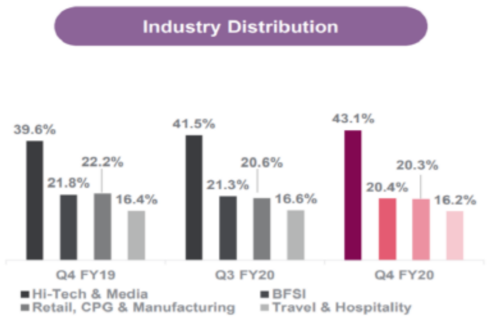
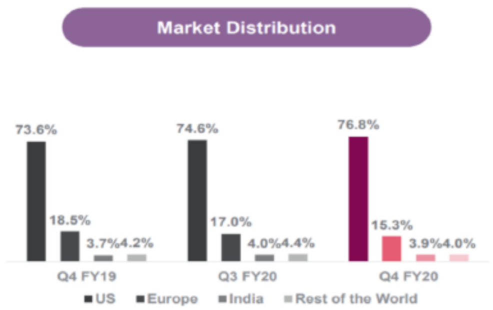


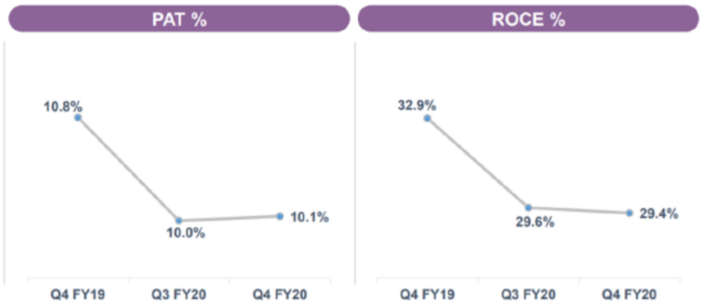




Source: Company presentation

Sound Profitability Ratios

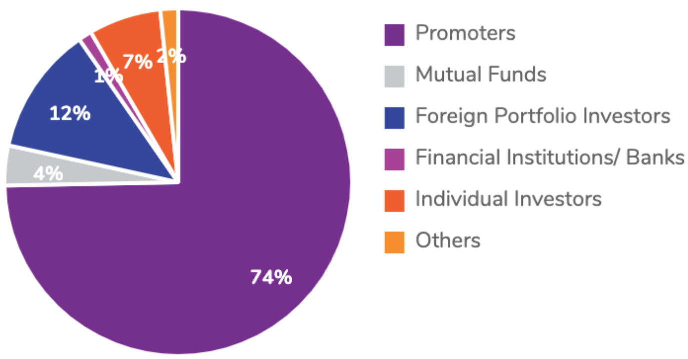
The company's return on capital employed (ROCE) strongly stood at 25.3%, despite the impact of Ind AS 116 that elevated the capital base on recognition of lease liabilities. Further, ROCE decreased to 19.5% in FY20 from 24.9% in FY19. It signifies that the company's profitability has decreased by 5.4% for those who invest their capital in the company. The ROE has been constantly been higher or the same as its ROE since 2010. When its ROE is greater than ROCE, it means that equity shareholders are being rewarded better than debt holders, which is a positive sign for equities. PAT margin dropped 2.6%, and as a percentage of revenue, decreased to 8.1% from 10.7% in FY20. Decreasing PAT margin means that the company is getting less efficient at converting sales into profits.

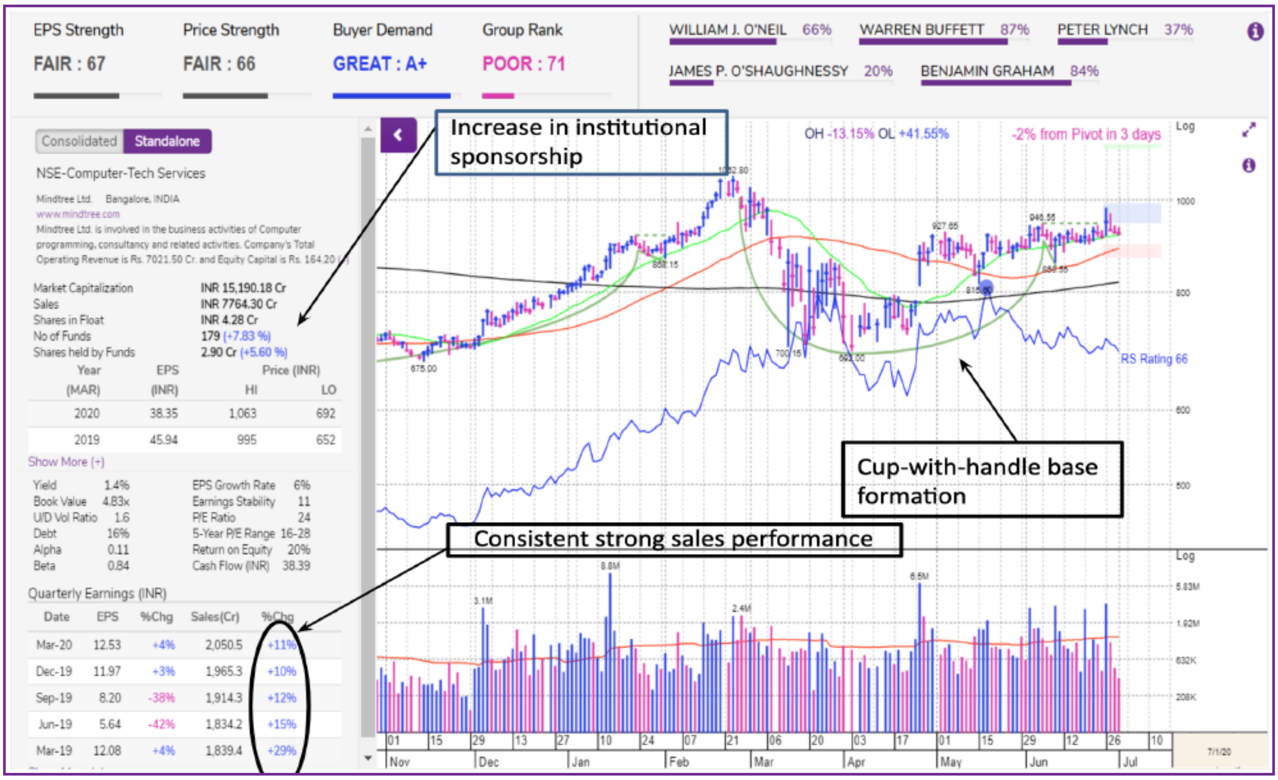


Source: Company presentation

Key risks

The COVID-19 pandemic has had an unprecedented impact on societies and economies worldwide. The company will face the impact at different levels. Risks include the impact on customers, which may lead to a reduction in customer discretionary IT spends, risk of delivery disruptions, as well as an increase in financial, compliance, and operational risks. In addition, it may increase political and macro-economic risks. The company is likely to see restrictions on outsourcing from countries such as the U.S., which are tightening their visa norms. As a significant part of its business comes from these countries, such legislation may have a huge impact on the company. This risk may get aggravated due to the economic impact of COVID-19.





O'Neil Methodology and Technical Viewpoint:

The stock has made a stage-one cup-with-handle base. Fresh positions can be initiated once the stock breaks out of the base on above average volume.

Price strength is at 66, with an RS line moving downwards.

Its buyer demand rating stands at A+, which is considered great.

EPS Rank of 67 indicates a fair fundamental profile.

The number of fund holdings and shares held by funds have increased 7.8% and 5.6%, y/y, respectively, in the recent quarter.

Mindtree	FY20	FY21E	FY22E
Revenue	7,764	7,938	8,120
Growth % y/y		2%	2%
EBITDA		1,207	1,399
Margin %		15%	17%
PAT	630	732	896
EPS in Rs	38.3	44.2	54
Return on Assets	13.5	13.4	15.4
Free Cash Flow	661	549	725

In INR Crore Bloomberg Estimate

Research Team:

Mayuresh Joshi, mayuresh.joshi@williamoneilindia.com
Kongari Rajashekar, kongari.rajashekar@williamoneilindia.com
Rushit Sejpal, rushit.sejpal@williamoneilindia.com
Satya Narayan Panda, satya.panda@williamoneilindia.com

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Disclosure of Interest Statement	Companies where there is interest
Analyst ownership of the stock	No

Registered office address: Technomark Building, A-4, NGEF Ancillary Industrial Estate, Graphite India Road, Mahadevapura, Whitefield, Bangalore 560048, Phone: + 91 80 67453802, Fax: + 91 80 6745381, Website: http://www.williamoneil.com/india/, For investor queries: queries@marketsmithindia.com For grievances: grievances@marketsmithindia.com; For compliance officer:compliance@marketsmithindia.com, Corporate Identity Number: U74999KA2012FTC066881, Investment Adviser SEBI Regn. Nos: INA200005125 valid till 11 July 2021.

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