

Coforge (COFORGE)

BUY

Strong performance despite poor macro

Summary

Coforge Ltd's Q4 USD revenue growth was better than most of its peers. The company's revenue growth guidance of 13-16% is 800-900 bps higher than its larger peer. We have considered mid-point of the guided range (i.e 14.5%) considering the macro uncertainty. We believe the flat EBITDA margin guidance was a tad disappointing, as we expected gross margin expansion to flow to EBITDA. However, considering the opportunity the company is seeing it plans to invest the same in sales expansion. This bodes well for future growth. We have revised our EPS estimates a tad downwards by 3.9% & 1.2% for FY24E and FY25E. Considering the strong sales growth (16% CAGR over FY23-FY25E) in poor macro we maintain our BUY rating on the stock with a revised target price of Rs 4,550 (23x on FY25E EPS).

Key Highlights and Investment Rationale

- Strong near term outlook despite poor macro:** The company's 12 month executable order book stood at 869 million, up 20.7% YoY. In addition the company sees strong growth in low code, no code, system integration, data and product engineering. Further the company expects 15% YoY growth across its key verticals of BFS and Insurance. In addition, the company has come out with new organisation structure to focus on US\$50-US\$100 mn clients and identified 6 services line to drive long term growth.
- Longer term margins to improve:** Coforge saw healthy expansion in gross margins (50 bps in FY23). It also expects 50 bps increase in gross margins in FY24E, however expects flat EBITDA margins. We believe the gross margin expansion will be reinvested in sales expansion and capabilities. This bodes well for longer term growth and also bodes well for longer term margin expansion. The company could expand margins by 150-300 bps in its journey to US\$2 bn revenues.

TP	Rs4,550
CMP	Rs3,948
Potential upside/downside	15%
Previous Rating	BUY

Price Performance (%)

	-1m	-3m	-12m
Absolute	6.7	(7.5)	(2.3)
Rel to Sensex	1.9	(7.7)	(7.4)

V/s Consensus

EPS (Rs)	FY24E	FY25E
IDBI Capital	157	196
Consensus	168	198
% difference	(6.7)	(1.0)

Key Stock Data

Bloomberg/Reuters	COFORGE IN / NITT.BO
Sector	IT Services
Shares o/s (mn)	61
Market cap. (Rs mn)	241,209
3-m daily avg Trd value (Rs mn)	67.9
52-week high / low	4,513/3,210
Sensex / Nifty	60,301 / 17,814

Shareholding Pattern (%)

Promoters	30.2
FII	25.4
DII	31.7
Public	12.7

Financial snapshot

Year	FY21	FY22	FY23	FY24E	FY25E
Revenue	46,628	64,320	80,146	94,339	110,564
Change (yoy, %)	11	38	25	18	17
EBITDA	7,865	11,154	14,053	16,576	20,150
Change (yoy, %)	9	42	26	18	22
EBITDA Margin(%)	16.9	17.3	17.5	17.6	18.2
Adj.PAT	4,916	6,618	6,938	9,766	12,157
EPS (Rs)	79	107	112	157	196
Change (yoy, %)	7.3	34.7	4.8	41	24
PE(x)	49.9	37.1	35.3	25	20
Dividend Yield (%)	0.6	1.3	1.6	2	2
EV/EBITDA (x)	30.1	21.9	17.3	14.4	11.5
RoE (%)	20.2	25.5	23.9	29	31
RoCE (%)	22.9	27.9	30	31	32

Source: IDBI Capital Research

Other Key Concall Highlights

- Revenue for the quarter was up 4.7% QoQ in CC terms to \$264.4 mn. Growth was broad based across all the verticals, service lines and regions. In terms of industry verticals, BFS grew 4.5% QoQ, Insurance recorded 5% growth, travel recorded a growth of 2.4% QoQ and others grew by 6.4%.
- EBIT margin for the quarter recorded 93 bps rise QoQ to 15.5%. The improvement in margin was due to 120 bps QoQ improvement in utilization, 20 bps QoQ rise in offshore revenue and absence of furloughs.
- Fresh order intake during the quarter stood at US\$301 mn registering a sequential decline of 13%. 12 months executable order book grew 21% YoY to US\$869 mn. Company won 2 large deals during Q4FY23
- **Guidance** – Company guided revenue to grow in the range of 13%-16% in constant currency during FY24E. It expects gross margin to increase by 50 bps and adjusted EBITDA margin to be at ~18.3% which is at similar levels of FY23. Company expects growth to be driven by its 3 core verticals (BFS, Insurance and TTH). From a longer term perspective, Coforge aspires to reach \$2 bn revenue mark while expanding adj EBITDA margin by 150-300 bps from the current levels of 18.3%.
- **Outlook** – Management expects demand environment to remain challenging in FY24E. However, despite the challenging macro conditions, company is optimistic of meeting its guidance on the back of healthy order booking, large deal wins and robust 12 months executable order book. In terms of verticals, company is observing opportunities in airlines and airports in the TTH vertical and CTB in banking vertical. Company expects BFS vertical to grow by 15%-16% in FY24E which indicates significant deceleration in growth from 47% growth recorded in FY23. Insurance vertical is expected to grow by 15% in FY24E on the back of expansion in new geos and ramp up in transformational deals. In addition, management informed that it expects cloud spending to slowdown in FY24E.
- Company has put in place new organizational structure wef 1st April 23. The new structure has 6 market focused service lines which will help in scaling up \$50+mn and \$100+mn accounts. Also, Coforge will continue to invest in sales & marketing and building capabilities which will aid achieving US\$2 bn revenue.
- During the quarter, Coforge added 719 employees (~3% QoQ growth) taking the total count to 23,224. Utilization improved by 120 bps QoQ to 81.5%.

Exhibit 1: Financial snapshot

(Rs mn)

Year-end: March	Q4FY23	Q3FY23	QoQ (%)	Q4FY22	YoY (%)
Revenues (US\$ mn)	264	252	5.0	232	13.8
Revenues	21,700	20,558	5.6	17,429	24.5
COGS	14,306	13,698	4.4	11,620	23.1
Gross profit	7,394	6,860	7.8	5,809	27.3
SG&A	3,318	3,245	2.2	2,516	31.9
EBITDA	4,076	3,615	12.8	3,293	23.8
Depreciation & amortization	717	624	14.9	584	22.8
EBIT	3,359	2,991	12.3	2,709	24.0
Other income	(487)	83	(686.7)	(119)	309.2
PBT	2,872	3,074	(6.6)	2,590	10.9
Tax	379	715	(47.0)	342	10.8
Minority interest	19	77	(75.3)	171	(88.9)
Reported net profit	1,148	2,282	(50)	2,077	(45)
Exceptional items	1,326	0	n.m.	225	n.m.
Adjusted net profit	2,474	2,282	8	2,302	7
Diluted EPS (Rs)	18.5	36.9	(50)	33.6	(45)
As % of net revenue					
Gross profit	34.1	33.4		33.3	
SG&A	15.3	15.8		14.4	
EBITDA	18.8	17.6		18.9	
EBIT	15.5	14.5		15.5	
Adjusted net profit	5.3	11.1		11.9	
Tax rate	13.2	23.3		13.2	

Source: Company; IDBI Capital Research

Exhibit 2: Actual vs. estimates

Year to March	Q4FY23	Q4FY23E	Variance (%)
Revenue (US\$ mn)	264	263	0.4
Revenue (Rs mn)	21,700	21,656	0.2
EBIT (Rs mn)	3,359	3,509	(4.3)
EBIT margin (%)	15.5%	16.2%	(73)bps
PAT (Rs mn)	2,493	2,739	(9.0)
PAT margin (%)	11.5%	12.7%	(116)bps
EPS (Rs)	18.5	44.3	(58.4)

Source: Company; IDBI Capital Research

Exhibit 3: Earnings Revision

Year-end: March	FY24E			FY25E		
	New	Old	Chg (%)	New	Old	Chg (%)
Revenue (US\$ mn)	1,147	1138	0.8	1,344	1,332	0.9
Revenue (Rs bn)	94,339	93468	0.9	110,564	109,341	1.1
EBIT margin (%)	14.5%	15.0%	(59.5)	15.3%	15%	(14.0)
EPS (Rs/sh)	157.2	163.6	(3.9)	195.7	198.1	(1.2)

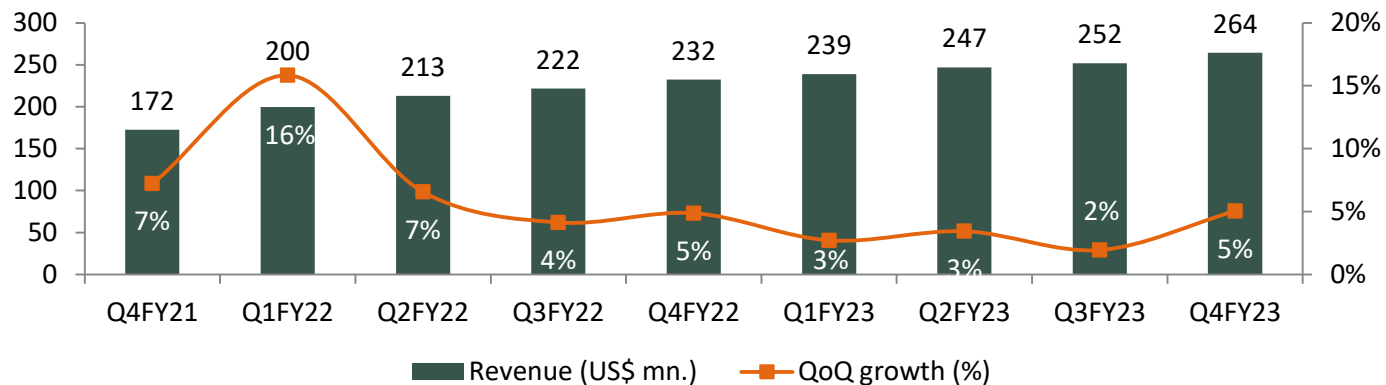
Source: Company; IDBI Capital Research

Exhibit 4: Large clients trend

No. of large clients	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23
USD1m – USD5m	88	95	92	94	100	98	97	98	101
USD5m – USD10m	16	20	22	21	19	24	26	23	23
USD10m+	11	15	16	18	18	19	19	21	21

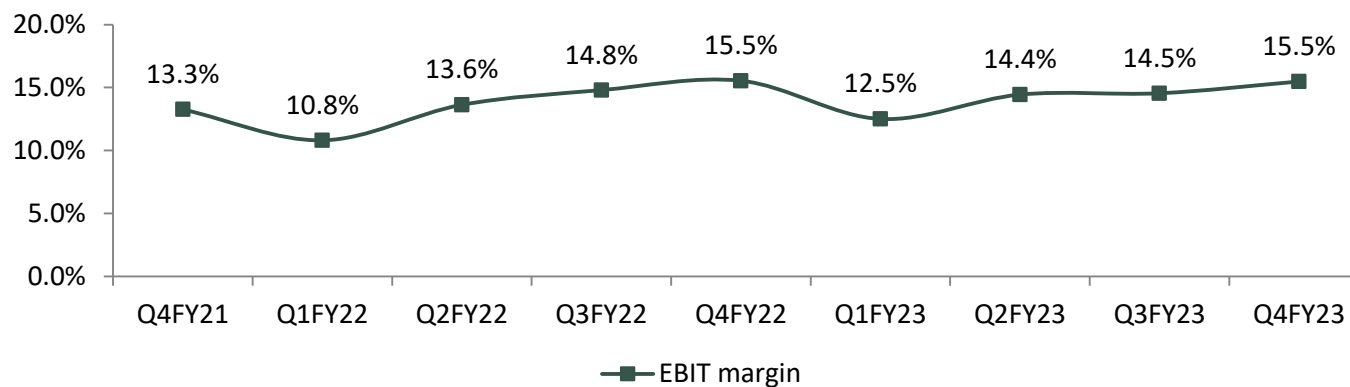
Source: Company; IDBI Capital Research

Exhibit 5: Q4FY23 revenue growth was in line with our estimates

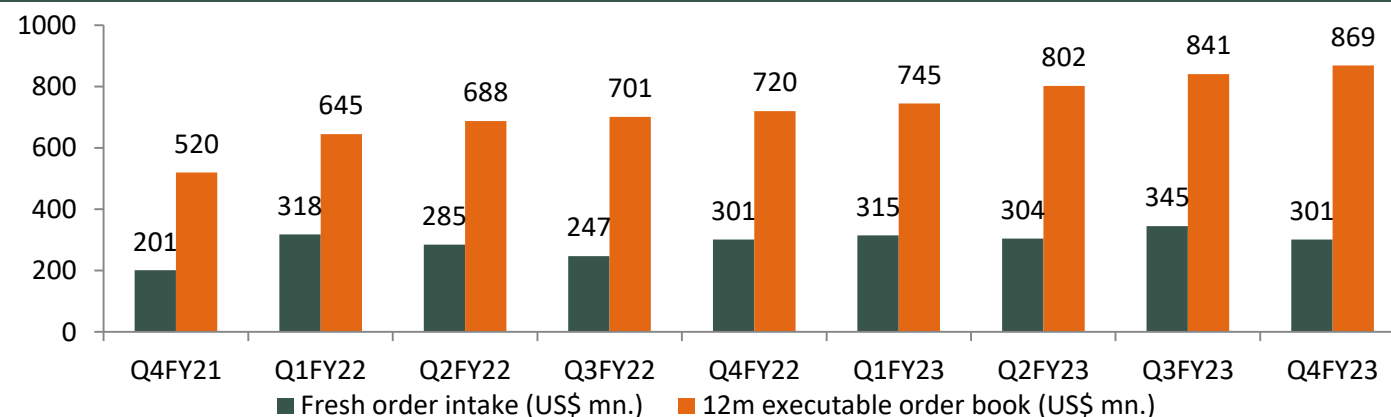


Source: Company; IDBI Capital Research

Exhibit 6: EBIT margin improved 93 bps QoQ



Source: Company; IDBI Capital Research

Exhibit 7: 12 month order book continued to be robust

Source: Company; IDBI Capital Research

Exhibit 8: Revenue growth across various segments (%)

	% of revenue (%)	YoY (%)
Total revenue		13.8%
by geography		
North America	48.3%	10.1%
Europe	39.6%	13.1%
RoW	12.1%	33.6%
by vertical		
BFS	31.0%	27.3%
Insurance	22.2%	-1.7%
Transportation	18.8%	6.4%
Others	28.0%	20.2%

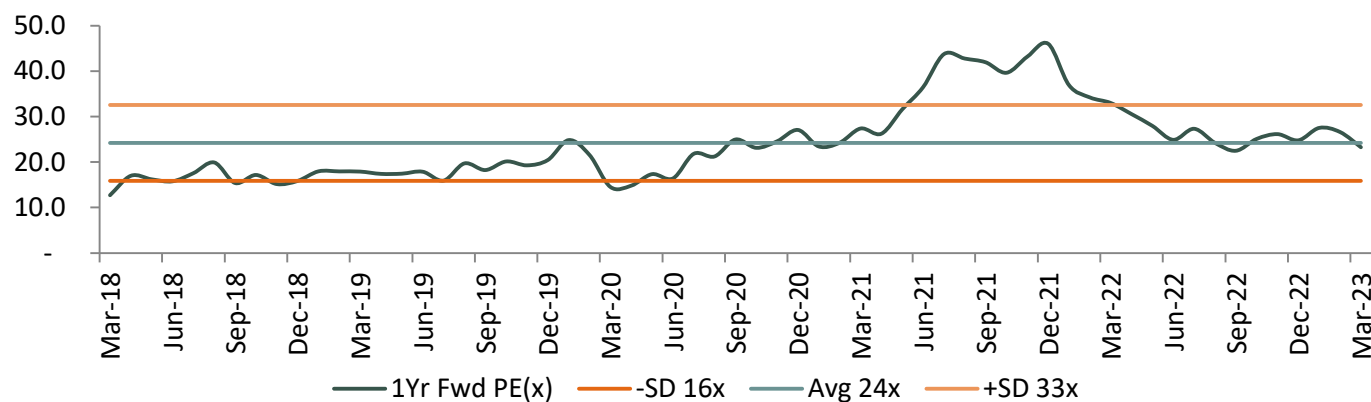
Source: Company; IDBI Capital Research

Exhibit 9: Geo wise Adj. EBITDA margin trend

Regions	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23
Americas	16%	16%	18%	20%	18%	16%	18%	15%	13%
Europe	22%	17%	21%	21%	23%	21%	21%	24%	19%
APAC	11%	10%	13%	10%	10%	9%	12%	16%	15%
India	-6%	-8%	-3%	-9%	-11%	-17%	-19%	-15%	5%

Source: Company; IDBI Capital Research

Exhibit 10: One-year forward PER trend



Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY20	FY21	FY22	FY23	FY24E	FY25E
Net sales	41,839	46,628	64,320	80,146	94,339	110,564
<i>Change (yoy, %)</i>	13.8	11	38	25	18	17
Operating expenses	(34,641)	(38,763)	(53,166)	(66,093)	(77,764)	(90,414)
EBITDA	7,198	7,865	11,154	14,053	16,576	20,150
<i>Change (yoy, %)</i>	11.6	9	42	26	18	22
<i>Margin (%)</i>	17.2	16.9	17.3	17.5	17.6	18.2
Depreciation	(1,730)	(1,836)	(2,272)	(2,585)	(2,915)	(3,204)
EBIT	5,468	6,029	8,882	11,468	13,660	16,947
Interest paid	-	-	-	-	-	-
Other income	558	113	(266)	(630)	(122)	(316)
Pre-tax profit	6,026	6,142	8,616	10,838	13,538	16,631
Tax	(1,278)	(1,302)	(1,468)	(2,061)	(2,897)	(3,559)
<i>Effective tax rate (%)</i>	21.2	21.2	17.0	19.0	21.4	21.4
Minority Interest	(236.0)	(104.0)	(530.0)	(513.0)	(735.1)	(915.0)
Net profit	4,441	4,556	6,618	9,590	10,045	12,157
Exceptional items	-	-	-	-	-	-
Adjusted net profit	4,583	4,916	6,618	6,938	9,766	12,157
<i>Change (yoy, %)</i>	10.6	7	35	5	41	24
EPS	73.7	79.1	106.5	111.7	157.2	195.7
DPS	31.0	23.6	50.7	64.2	75.5	93.9
<i>Dividend Payout (%)</i>	42	30	48	58	48	48

Balance Sheet							(Rs mn)
Year-end: March	FY20	FY21	FY22	FY23	FY24E	FY25E	
Shareholders' funds	23,965	24,661	27,331	30,825	35,903	42,225	
Share capital	625	606	609	611	611	611	
Reserves & surplus	23,340	24,055	26,722	30,214	35,292	41,614	
Total Debt	48	5	3,365	3,382	3,382	3,382	
Other liabilities	2,285	1,723	9,074	7,410	11,755	13,196	
Curr Liab & prov	8,477	8,895	15,585	17,903	21,073	24,698	
Current liabilities	8,148	8,750	12,156	17,725	16,107	18,804	
Provisions	329	225	316	360	463	543	
Total liabilities	10,433	10,473	21,230	25,135	27,862	31,999	
Total equity & liabilities	34,398	35,134	49,544	56,834	65,375	76,748	
Net fixed assets	10,796	10,208	20,835	23,165	22,136	21,144	
Investments	-	-	-	-	-	-	
Other non-curr assets	2,092	3,631	4,809	5,833	6,798	7,320	
Current assets	21,510	21,295	23,900	27,836	36,441	48,284	
Inventories	-	-	-	-	-	-	
Sundry Debtors	8,565	8,895	15,585	17,903	21,073	24,698	
Cash and Bank	9,171	8,246	4,535	5,787	9,823	17,088	
Loans and advances	-	-	-	-	-	-	
Total assets	34,398	35,134	49,544	56,834	65,375	76,748	

Cash Flow Statement

(Rs mn)

Year-end: March	FY20	FY21	FY22	FY23	FY24E	FY25E
Pre-tax profit	6,026	6,142	8,616	10,838	13,538	16,631
Depreciation	1,766	138	724	2,585	2,915	3,204
Tax paid	(1,548)	(1,548)	(2,656)	(3,082)	(2,897)	(3,559)
Chg in working capital	(661)	272	(3,284)	3,251	(4,789)	(927)
Other operating activities	(2,614)	2,619	4,256	(2,833)	1,757	(302)
Cash flow from operations (a)	2,969	7,623	7,656	10,759	10,524	15,046
Capital expenditure	(4,361)	450	(11,351)	(4,915)	(1,887)	(2,211)
Chg in investments	-	-	-	-	-	-
Other investing activities	1,970	(2,817)	1,663	-	(242)	(185)
Cash flow from investing (b)	1,123	(2,354)	(9,564)	(4,915)	(2,129)	(2,396)
Equity raised/(repaid)	7	(19)	3	2	-	-
Debt raised/(repaid)	(52)	(43)	3,360	17	-	-
Dividend (incl. tax)	(1,927)	(1,467)	(3,150)	(3,989)	(4,688)	(5,835)
Chg in minorities	(311)	(104)	453	(622)	-	-
Other financing activities	1,194	(3,898)	(2,224)	-	328	451
Cash flow from financing (c)	(1,089)	(5,531)	(1,558)	(4,592)	(4,360)	(5,384)
Net chg in cash (a+b+c)	3,003	(262)	(3,466)	1,252	4,036	7,266

Financial Ratios

Year-end: March	FY20	FY21	FY22	FY23	FY24E	FY25E
Book Value (Rs)	385.3	397	440	496	578	680
Adj EPS (Rs)	73.7	79.1	106.5	111.7	157.2	195.7
Adj EPS growth (%)	9.1	7	35	5	41	24
EBITDA margin (%)	17.2	16.9	17.3	17.5	17.6	18.2
Pre-tax margin (%)	14.4	13.2	13.4	13.5	14.4	15.0
Net Debt/Equity (x)	-0.4	-0.3	0.0	-0.1	-0.2	-0.3
ROCE (%)	22.4	23	28	30	31	32
ROE (%)	20.5	20	25	24	29	31

DuPont Analysis

Asset turnover (x)	1.3	1.3	1.5	1.5	1.5	1.6
Leverage factor (x)	1.4	1.4	1.6	1.8	1.8	1.8
Net margin (%)	11.0	10.5	10.3	8.7	10.4	11.0

Working Capital & Liquidity ratio

Inventory days	0	0	0	0	0	0
Receivable days	75	70	88	82	82	82
Payable days	30	35	45	38	37	37

Valuations

Year-end: March	FY20	FY21	FY22	FY23	FY24E	FY25E
PER (x)	53.6	49.9	37.1	35.3	25.1	20.2
Price/Book value (x)	10.2	10.0	9.0	8.0	6.8	5.8
EV/Net sales (x)	5.7	5.1	3.8	3.0	2.5	2.1
EV/EBITDA (x)	32.8	30.2	21.9	17.3	14.4	11.5
Dividend Yield (%)	0.8	0.6	1.3	1.6	1.9	2.4

Source: Company; IDBI Capital Research



Notes

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Key to Ratings Stocks:

BUY: 15%+; **HOLD:** -5% to 15%; **SELL:** -5% and below.

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