



Hexaware

Sector: Technology

1QCY16 Result Update

CMP: ₹227

Remaining of CY16 to be better, Rich valuations

Recommendation: Hold

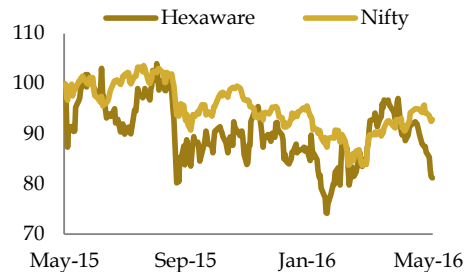
Market statistics

Current stock price (₹)	227
Shares O/S (cr.)	30.2
Mcap (₹ cr)	6,846
52W H/L (₹)	299/202
6m avg. volume	1,175,647
Bloomberg	HEXW.IN

Shareholding pattern

Promoters	71.26
Domestic Institution	13.12
Foreign Institution	5.03
Non-institution	10.59
of which more than 1%	
HDFC Trustee Co.Ltd-A/C HDFC	2.02
MICCAP	
T ROWE Price International	1.27
Discovery Fund	

Hexaware vs Nifty



Capital efficiency & valuations

Particulars	CY15	CY16E	CY17E
RoE (%)	30.3	28.5	31.2
EPS (₹)	13.7	13.9	16.1
CEPS (₹)	15.3	15.8	18.2
P/E (x)	17.9	16.3	14.1
P/BV (x)	5.2	4.5	4.3
EV/EBITDA (x)	12.2	11.0	9.4
Income growth (%)	21.0	7.1	11.7
EBITDA growth (%)	16.3	4.2	15.6
PAT growth (%)	26.5	1.9	16.3

Hexaware's quarterly result was lower-than-expectation both on the margin as well as revenue growth. The company's Q1CY16 revenue at US\$121.7mn, down 1.9% QoQ (decline of 1.8% in constant currency terms). Company won new business worth TCV of US\$36mn this quarter (US\$120mn in CY15). HEXW has invested in sales and marketing engine in CY15 to build base for future growth. We maintain our rating on the stock at Hold on account of rich valuations. HEXW's decision to develop core competence and differentiation in key areas - Capital Markets, Travel and Transportation, EAS and Testing - is the right approach for a relatively small player trying to develop a niche for itself.

Disappointing quarter. Q1CY16 revenues declined by 1.9% in cc terms and 1.8% QoQ in US\$ terms to US\$121.7mn. EBITDA margins for the quarter contracted by 54bps QoQ to 15.4% driven by weak revenue trajectory. Utilisation for the quarter stood at 69.6% (69.7% in 4QCY15). EPS for the quarter (excluding ESOPs) declined by 8.8% QoQ to Rs3.0. Foreign exchange gain stood at `44mn vs. `70mn in 4Q. Vertical splits: Banking and Financial Services was up 2.5% QoQ, while Travel & Transportation was down 9.3%, Healthcare & Insurance was down 1.1% and Manufacturing & Consumer was down 4.1% respectively.

Operating metrics - weakening. 1) Europe was down 10.4% QoQ. America was down 1.8%, while RoW increased 16% QoQ respectively. HEXW added 3 clients in 1QCY16 to take the list to 229. 2) Offshore: onsite mix of revenue share changed in favour of onsite by 80bps QoQ to 36.9:63.1. 3) Attrition (LTM) decreased 90 bps QoQ to 16% in Q1CY16. 4) HEXW employed 11,599 professionals (added 224 QoQ, 12 freshers), 5) Hexaware has forward contracts worth US\$147mn @ ₹70.68/US\$ and hedges worth €5mn @ ₹77.95/US\$, GBP4.2mn @ ₹106.69/US\$ maturing over next eight quarters. 6) DSO, billed and including unbilled accruals remained flat QoQ and increased by 6 at 49 and 78 respectively. 7) Hexaware lost 1 client QoQ from the US\$5-10mn. 8) HEXW has signed US\$36mn worth of TCV deals (YTD). 9) Services Lines Split: ADM was down 2.6%, Enterprise Solutions was down 5.9%, Testing was down 4%, IMS was down 1.7% while Business Intelligence and Analytics grew 6.3% QoQ.

Large accounts are critical for the stability of the business, especially in the case of mid-tier companies like Hexaware where they account for a large chunk of revenues. Predictability in top accounts gives the company better visibility of revenue growth and helps in planning its resource allocation. One of HEXW's Top 5 client underwent a re-structuring, which affected business (was known before the start of the quarter), while another Top-5 client too declined for HEXW (which was not anticipated). Both clients would see QoQ increase in business from 2Q. HEXW saw a permanent decline in one of its Testing related client, which again was not anticipated at the start of the quarter - all these added to a rough quarter.

Strong balance sheet, dividend payout remains strong. Hexaware has US\$46.5m in net cash (₹10.2/share). Hexaware declared a first interim dividend of ₹ 2.5/share. It had declared dividends of ₹ 8.65 and ₹ 9.45 in CY15 and CY14. The dividend declared in CY14/CY15 amounted to a dividend payout ratio of 102/74% respectively. We believe a dividend payout of ~75%+ over CY16/17E is sustainable, and we build dividend payouts of ~₹ 9.8/11.0 per share in CY16/17E. Even after paying out this dividend and meeting its capex requirements, the company will still have cash of more than ~15-20% of sales over this period.

Valuation: The company inked new customer deals of US\$36mn in 1QCY16 (US\$120mn TCV in CY15), which instills confidence in revenue growth going ahead. Our revenue forecast for HEXW for CY15-17 is 8.8% CAGR. Stock valuations, at 16.3x/14.1x CY16/CY17E EPS, are rich leaving limited upside from the current level.

ANALYST

Naushil Shah

+91-22 4224 5125

naushil.shah@trustgroup.co.in



Exhibit 1: Quarterly details

₹ mn	1QCY15	4QCY15	1QCY16	QoQ (%)	YoY (%)	Comments
Revenues (in US\$ mn)	114.9	124.1	121.7	(1.9)	5.9	Cc decline of 1.8%. Top 5 clients were down 0.3% QoQ, while #6-10 were down 2.7%.
Revenues	7,134	8,195	8,202	0.1	15.0	
- Operating costs	5,864	6,885	6,935	0.7	18.3	
EBITDA	1,270	1,310	1,267	(3.3)	(0.2)	
EBITDA margin (%)	17.8	16.0	15.4	(54)bps	(235)bps	EBITDA margins contracted on account of weak revenue trajectory
- Interest expense	0	0	0	NA	NA	
- Depreciation	115	131	138	5.3	20.0	
+ Other income, net (incl forex)	(96)	88	55	NA	NA	OI breakup: Forex gain of ₹44mn in Q1 vs. ₹70mn in the last quarter.
PBT	1,059	1,267	1,184	(6.6)	11.8	
- Taxes	225	265	269	1.5	19.6	
Effective tax rate (%)	21.2	20.9	22.7	180bps	147bps	Effective tax rate for CY16 to be between 23-24%
PAT	834	1,002	915	(8.7)	9.7	
Net margin (%)	11.7	12.2	11.2	(107)bps	(53)bps	
Reported profits	834	994	842	(15.3)	1.0	Hexaware took a hit of Rs73mn on account of a ESOP charge.

Source: Company

Exhibit 2: Change in estimates

₹ mn	CY16E			CY17E		
	Old	New	%Chg	Old	New	%Chg
Revenue (US\$ mn)	547	510	(6.8)	628	574	(8.6)
Revenue	35,024	33,450	(4.5)	40,190	37,355	(7.1)
EBITDA margin (%)	18.0	17.3	(65)bps	18.3	17.9	(35)bps
EPS (₹)	15.3	13.9	(9.2)	17.7	16.1	(8.9)

Source: Trust Research

Geography wise Revenues: Europe was down 10.4% QoQ. America was down 1.8%, while RoW increased 16% QoQ respectively.

Exhibit 3: Geographical wise Performance

Geographical mix	Q1CY14	Q2CY14	Q3CY14	Q4CY14	Q1CY15	Q2CY15	Q3CY15	Q4CY15	Q1CY16
US	78.1	78.7	78.8	78.8	80.8	81.0	80.8	81.3	81.4
Europe	14.3	14.2	14.3	15.1	13.1	13.4	13.8	13.1	12.0
RoW	7.6	7.1	6.9	6.1	6.1	5.6	5.4	5.6	6.6
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company

Services' wise Performance: ADM was down 2.6%, Enterprise Solutions was down 5.9%, Testing was down 4%, IMS was down 1.7% while Business Intelligence and Analytics grew 6.3% QoQ.

**Exhibit 4: Service offering segmentation**

Details	Q1CY14	Q2CY14	Q3CY14	Q4CY14	Q1CY15	Q2CY15	Q3CY15	Q4CY15	Q1CY16
Application dev & maintenance (ADM)	37.5	36.3	36.8	36.4	37.6	37.8	37.3	38.1	37.8
Enterprise application services (EAS)	18.1	18.6	17.1	16.6	15.5	14.3	14.6	14.3	13.7
Testing / QATS	21.1	19.9	20.2	20.9	20.7	20.9	20.8	20.6	20.2
Business intelligence & Analytics	13.4	14.3	15.2	15.4	15.4	15.1	14.7	14.0	15.2
BPO	3.7	4.0	4.2	4.3	4.8	5.2	5.7	5.7	5.8
Others	6.2	6.9	6.5	6.4	6.0	6.7	6.9	7.3	7.3
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company

Human Resources: Attrition (LTM) decreased 90 bps QoQ to 16% in Q1CY16. Global headcount increased 224 QoQ to 11,599. Hexaware added 12 fresh graduate engineers in 1Q.

Exhibit 5: Employee strength at HEXW

Details	Q1CY14	Q2CY14	Q3CY14	Q4CY14	Q1CY15	Q2CY15	Q3CY15	Q4CY15	Q1CY16
Onsite (%)	18.6	19.7	20.4	21.1	22.1	20.8	20.6	20.5	21.8
Offshore (%)	73.1	72.0	71.7	71.1	69.3	70.0	69.7	69.2	69.2
Total billable (%)	91.7	91.7	92.1	92.2	91.4	90.8	90.3	89.7	91.0
Marketing (Incl. sales support, %)	2.3	2.3	2.1	2.1	3.1	3.4	3.7	3.9	4.2
Others (Incl. sales support, %)	6.0	6.0	5.8	5.7	5.5	5.8	6.0	6.4	4.8
Total (%)	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Headcount (Nos.)	8,952	9,287	9,697	10,016	10,100	11,009	11,341	11,341	11,599
Utilisation	72.9	70.8	70.3	73.0	73.6	72.1	70.4	69.7	69.6
Attrition	12.8	12.7	13.0	14.1	16.6	17.1	17.4	16.9	16.0

Source: Company, Trust Research

Client Concentration: HEXW added 3 new clients on a net basis to take the list to 229. Top 5 clients were down 0.3% QoQ while Client #6-10 were down 2.7%.

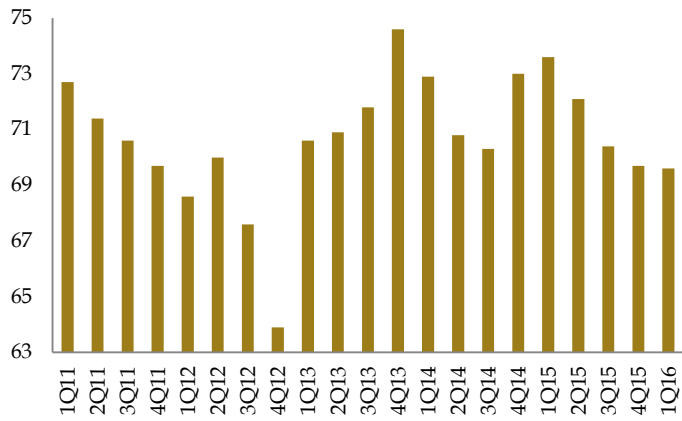
Exhibit 6: Client details

Details	Q1CY14	Q2CY14	Q3CY14	Q4CY14	Q1CY15	Q2CY15	Q3CY15	Q4CY15	Q1CY16
Top client (%)	14.1	13.4	14.4	14.9	14.9	15.0	13.6	NA	NA
Top 5 clients (%)	38.2	37.4	38.2	40.0	42.8	44.4	42.7	42.2	42.9
Top 10 clients (%)	50.7	50.9	51.4	53.1	55.5	56.1	54.4	54.7	55.3
> US\$1m+	56	56	61	61	62	62	65	69	73
Between US\$1-5m	41	40	42	40	42	43	48	53	58
Between US\$5-10m	6	8	11	13	11	10	8	7	6
Between US\$10m-20m	5	4	4	3	4	5	8	5	5
Over US\$20m+	4	4	4	5	5	4	5	4	4
Clients added	11	13	10	10	10	9	9	9	10
Clients billed	235	238	233	236	227	225	223	226	229

Source: Company

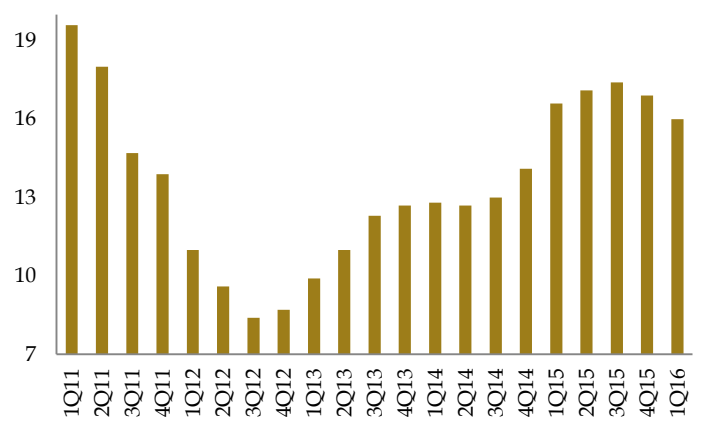


Exhibit 7: Utilisation to be used as margin lever



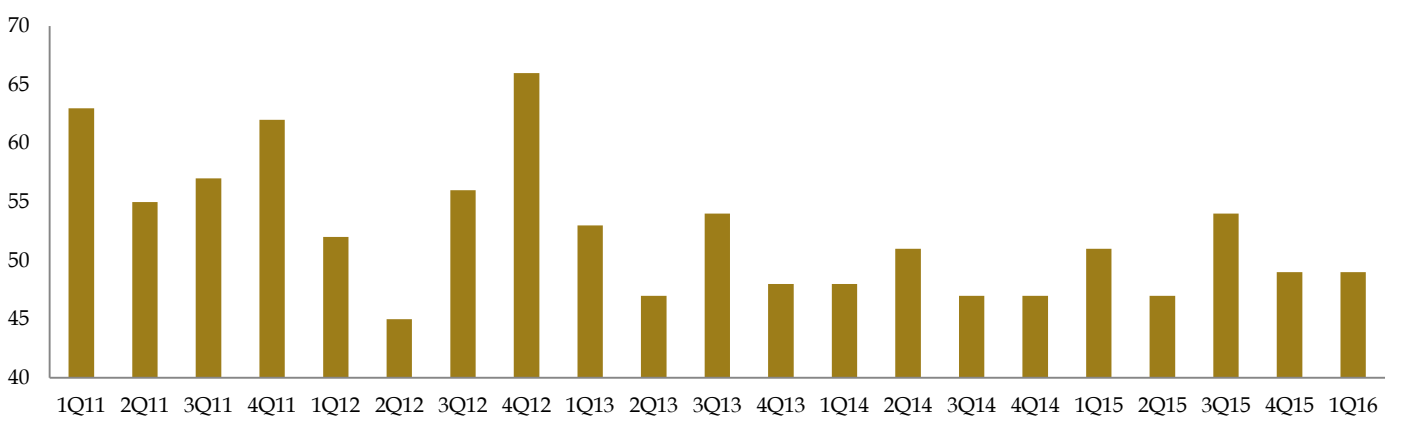
Source: Company, Trust

Exhibit 8: Attrition slowly declining over last 3 quarters



Source: Company, Trust

Exhibit 9: Billed DSO were flat QoQ at 49 days; unbilled DSO's were up 6 days QoQ to 78



Source: Company, Trust



Financials

Income Statement (₹ mn)

Year End-Dec	CY13	CY14	CY15	CY16E	CY17E
Revenues	22,854	25,817	31,235	33,450	37,355
Op. Expenses	17,730	21,041	25,680	27,660	30,660
EBITDA	5,124	4,776	5,555	5,790	6,695
Other Income	58	(90)	173	286	345
Depreciation	386	440	482	582	636
EBIT	4,795	4,246	5,246	5,494	6,404
Interest	-	-	-	-	-
PBT	4,795	4,246	5,246	5,494	6,404
Tax	1,004	980	1,114	1,282	1,505
PAT	3,791	3,266	4,132	4,212	4,899
Extra-ordinary items	-	66	200	73	-
Adj Pat	3,791	3,200	3,932	4,139	4,899

Valuations Summary

Year End-Dec	CY13	CY14	CY15P	CY16E	CY17E
Per share (₹)					
EPS	12.7	10.9	13.7	13.9	16.1
CEPS	14.0	12.4	15.3	15.8	18.2
BVPS	40.2	43.1	47.5	50.1	53.3
DPS	11.1	9.5	8.7	9.8	11.0
Payout (%)	102.0	101.8	73.9	82.4	79.8
Valuation (x)					
P/E	10.9	22.3	17.9	16.3	14.1
P/BV	3.4	5.6	5.2	4.5	4.3
EV/EBITDA	6.7	13.9	12.2	11.0	9.4
Dividend Yield (%)	8.0	3.9	3.5	4.3	4.8
Return ratio (%)					
EBITDA Margin	22.4	18.5	17.8	17.3	17.9
PAT Margin	16.6	12.7	13.2	12.6	13.1
ROAE	31.6	26.2	30.3	28.5	31.2
ROACE	39.4	34.8	38.5	37.2	40.8
Leverage Ratios (x)					
Net Debt/Equity	(0.5)	(0.4)	(0.4)	(0.4)	(0.4)
Current ratio	1.9	2.4	2.2	2.3	2.2
Growth Ratios (%)					
Income growth	17.3	13.0	21.0	7.1	11.7
EBITDA growth	25.8	(6.8)	16.3	4.2	15.6
PAT growth	15.7	(13.9)	26.5	1.9	16.3
Turnover Ratios					
F.A. Turnover	6.2	6.9	8.0	8.3	8.9
Debtors Days	56	55	55	53	53
Payable days	11	11	12	11	12

Balance Sheet (₹ mn)

Year End-Dec	CY13	CY14	CY15P	CY16E	CY16E
Liabilities					
Equity Share Capital	600	602	603	603	603
Reserves & Surplus	11,393	12,304	13,729	14,582	15,600
Total Shareholders Fund	11,992	12,906	14,332	15,185	16,203
Non-current liabilities	262	144	82	109	150
Deferred tax liabilities	48	(175)	(270)	(270)	(270)
Other LT liabilities & prov	214	319	352	379	420
Current Liabilities	5,830	4,311	5,347	5,759	6,384
Trade payables	494	680	774	834	924
Other cur liabilities & Prov	5,336	3,631	4,573	4,926	5,460
Total Liabilities	18,084	17,361	19,761	21,053	22,737
Assets					
Non-current Assets					
Fixed assets	3,677	3,730	3,880	4,030	4,180
Non-current investments	1,698	1,763	1,763	1,763	1,763
Long-term loans & adv	1,291	1,399	1,712	1,833	2,047
Other non-current assets	177	328	385	412	461
Current assets	11,242	10,140	12,021	13,014	14,286
Current investments	3,378	1,851	1,851	1,851	1,851
Trade receivables	3,236	3,656	4,279	4,582	5,117
Cash & bank balances	3,011	2,865	3,709	4,244	4,708
Short-term loans & adv	483	538	642	687	768
Other current assets	1,134	1,230	1,540	1,650	1,842
Total Assets	18,084	17,361	19,761	21,053	22,737

Cash flow Statement

Year End-Dec	CY13	CY14	CY15P	CY16E	CY17E
PBT	4,795	4,246	5,246	5,494	6,404
Depreciation	508	217	387	582	636
Others	-	(66)	(200)	(73)	-
CF before W.cap	5,303	4,397	5,433	6,003	7,040
Inc/dec in W.cap	(2,166)	2,245	337	167	404
Op CF after W.cap	7,469	2,152	5,096	5,836	6,636
Less Taxes	1,004	980	1,114	1,282	1,505
Net CF From Operations	6,465	1,172	3,982	4,554	5,131
Inc/(dec) in F.A + CWIP	370	493	632	732	786
(Pur)/sale of Investments	1,216	(1,462)	-	-	-
CF from Invst Activities	(1,586)	969	(632)	(732)	(786)
Equity Raised	53	1,037	547	183	30
Dividend	3,890	3,323	3,053	3,469	3,911
CF from Fin Activities	(3,837)	(2,286)	(2,506)	(3,286)	(3,881)
Net inc/(dec) in cash	1,042	(146)	844	535	464
Op. bal of cash	1,969	3,011	2,865	3,709	4,244
Cl. balance of cash	3,011	2,865	3,709	4,244	4,708



Institutional Equity Team

Names	Designation	Sectors	Email ID's	Desk-Number
Naren Shah	Head Of Equity		naren.shah@trustgroup.co.in	+91-22-4084-5074
Institutional Sales				
Sriram Rangarajan	Sales		sriram.rangarajan@trustgroup.co.in	+91-22-4224-5216
Vivek Kumar	Sales		vivek.kumar@trustgroup.co.in	+91-22-4224-5197
Sales Trading & Dealing				
Rajesh Ashar	Sales Trader		rajesh.ashar@trustgroup.co.in	+91-22-4224-5123
Nitin Dalvi	Dealer		nitin.dalvi@trustgroup.co.in	+91-22-4084-5089
Dealing Desk			trustfin@bloomberg.net	+91-22-4084-5089
Research Team				
Binyam Taddese	Analyst	Rates & Credit Research	binyam.taddese@trustgroup.co.in	+91-22-4224-5037
Naushil Shah	Analyst	Technology, Media & Telecom	naushil.shah@trustgroup.co.in	+91-22-4224-5125
Naveen Trivedi	Analyst	Consumer Staple & Durable	naveen.trivedi@trustgroup.co.in	+91-22-4224-5181
Shashwat Nanda	Analyst	Rates & Credit Research	shashwat.nanda@trustgroup.co.in	+91-22-4224-5038
Tejas Sarvaiya	Analyst	Seeds, Exchanges & MidCap	tejas.sarvaiya@trustgroup.co.in	+91-22-4084-5064
Ritu Chaudhary	Associate	Consumer Durable	ritu.chaudhary@trustgroup.co.in	+91-22-4224-5183

DISCLAIMER

We are committed to providing completely independent and transparent recommendations to help our clients reach a better decision. This document is provided for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Nothing in this document should be construed as investment or financial advice, and nothing in this document should be construed as an advice to buy or sell or solicitation to buy or sell the securities of companies referred to in this document. The intent of this document is not in recommendatory nature. The recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. Trust Financial Consultancy Services Pvt. Ltd. has not independently verified all the information given in this document. Accordingly, no representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the information and opinions contained in this document. The Company reserves the right to make modifications and alternations to this statement as may be required from time to time without any prior approval. Trust Financial Consultancy Services Pvt. Ltd., its affiliates, their directors and the employees may from time to time, effect or have effected an own account transaction in, or deal as principal or



agent in or for the securities mentioned in this document. They may perform or seek to perform investment banking or other services for, or solicit investment banking or other business from, any company referred to in this report. Each of these entities functions as a separate, distinct and independent of each other. The recipient should take this into account before interpreting the document. This report has been prepared on the basis of information, which is already available in publicly accessible media or developed through analysis of Trust Financial Consultancy Services Pvt. Ltd. The views expressed are those of analyst and the Company may or may not subscribe to all the views expressed therein. Neither the Firm, not its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information. This document is being supplied to you solely for your information and may not be reproduced, redistributed or passed on, directly or indirectly, to any other person or published, copied, in whole or in part, for any purpose. Copyright in this document vests exclusively with Trust Financial Consultancy Services Pvt. Ltd.