



In partnership. With trust.

eClerx Services

Sector: Technology

4QFY16 Result Update

CMP: ₹ 1,414

Unsustainable margins, Outlook muted

Recommendation: Hold

Market statistics

Current stock price (₹)	1,414
Shares O/S (cr.)	4.1
Mcap (₹ cr)	5,752
52W H/L (₹)	1,640/1,052
6m avg. volume	34,596
Bloomberg	ECLX.IN

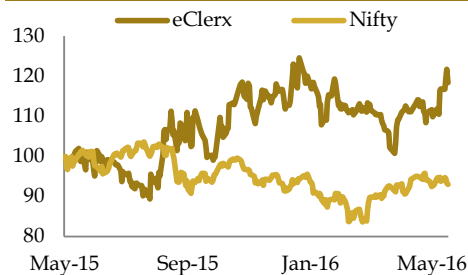
eClerx reported lower-than-expected revenue, but margin was higher. US\$ revenue was down 2% QoQ (down 2.5% in cc terms). Operating margin at 41% (up 480bps QoQ) on account of lower employee costs and partially helped by favourable currency movement. PAT stood at ₹1,083mn (vs an expected ₹894mn) helped by lower-than-expected tax expense. eClerx anticipates organic growth in FY17 to be soft as compared to FY16. We maintain our Hold recommendation on the stock since the robust performance is on the back of substantial growth contribution from short term projects and revenues are expected to be flattish over the next couple of quarters.

Shareholding pattern

Promoters	50.38
Domestic Institution	14.06
Foreign Institution	27.16
Non-institution	8.40
of which more than 1%	
Matthews India Fund	7.50
Fidelity Puritan Trust Fidelity Low Priced Stock Fund	4.41

Q4FY16 P&L break up - margin higher than expected. US\$ revenues was down 2% QoQ. Break up of EBIT margin YoY S&D expenses (-250bps), Employee cost (+310bps), Depreciation & Amortization (-130bps), G&A expenses (-130bps) Exchange movement (-310bps). Hence, increase of 500bps YoY in EBIT margin. Q4 EBIT margin stood at 33.2%. Profits at ₹1,083mn (up 21.9% QoQ) was higher-than-expectations (our expectation of ₹894mn). Top-10 clients increased 11.8% (organic) YoY in US\$ terms. The company reported strong beat at margin driven by substantial decline in employee costs (down 12.6% QoQ). Going forward, ECLX expects revenues to be flattish over the next couple of quarters. 4Q had provision write-backs in salaries and bonuses of offshore employees and sales team, in order to reflect weak revenue trajectory for the quarter. 1H17 is expected to be flattish in terms of QoQ revenue growth.

eClerx vs Nifty



Subdued outlook, organic growth in FY17 expected to be lower than FY16 levels. eClerx anticipates organic growth in FY17 to remain lower compared to FY16 levels. Management continues to expect a 'low to mid teens' revenue growth for FY17 indicating that growth from financial services clients continues to remain sluggish (though outlook has improved slightly) while continues to see better growth in the Sales and Marketing segment and the Cable/Media business. Emerging accounts organically on a YoY basis was tepid this quarter at 35.8% YoY (organic basis).

Margins to see near-term pressure. We see at least three longer term margin challenges for eClerx: (a) given eClerx works on short term and smaller projects, with dynamic client needs, the ability to use fixed price/transaction based/outcome based pricing is limited; (b) with relatively lower utilization in faster growing Capital markets and Cable business, there remains lower scope for utilization expansion (furthermore, fastest growing Cable business has below company average margin profile); and (c) need to shift from 100% offshore delivery to global delivery model.

Capital efficiency & valuations

Particulars	FY16	FY17E	FY18E
RoE (%)	40.3	29.9	29.0
EPS (₹)	89.1	85.9	96.3
CEPS (₹)	101.5	101.4	113.3
P/E (x)	14.6	16.5	14.7
P/BV (x)	4.9	4.6	3.9
EV/EBITDA (x)	9.2	9.9	8.5
Income growth (%)	39.5	2.6	13.0
EBITDA growth (%)	53.9	0.3	14.3
PAT growth (%)	57.7	(3.0)	12.8

Operating metrics. 1) Cash and cash equivalents of ₹5.45bn (translating to ₹134/share, 9.5% of Mcap in cash) as on Mar'16. 2) DSO increased by 2 QoQ to 73 days. 3) Hedge position of US\$124.7m. 4) Headcount increased by 272 QoQ to 8,862. 5) Client metrics continue to reflect the progression as no. of US\$1mn+ clients increased to 17 in Mar'16 quarter (up from 7 in Mar'15 quarter) 6) S&M went down this quarter to 12.5% of revenues vs 12.9% in Q3FY16 and 17.3% in Q4FY15. 7) ECLX's revenue declined 2.5% in cc terms. 8) FY17 margins are expected to be lower compared to FY16.

Valuation: eClerx's continues to struggle for growth in an overall improving demand environment for IT services. The Cable business has been leading the growth over the last couple of years (~50% CAGR). However, it has slowed down over the last couple of quarters given ongoing Cable industry consolidation uncertainty in the US. On the other hand, its Sales and Marketing Services (SMS) business (~40% of revenues) continues to struggle given growth stagnation in its top account. Although eClerx has taken initiatives to broad base its service offerings to the Capital market clients (outside the top 5 accounts), it seems to have achieved limited success. Retain Hold on eClerx given strong ROE's and superior cash generation.

ANALYST

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Exhibit 1: Quarterly details

₹ mn	4QFY15	3QFY16	4QFY16	QoQ (%)	YoY (%)	Comments
Revenues (In US\$m)	40.6	51.8	50.7	(2.0)	24.9	Revenue was down 2.5% in cc terms. Top 10 clients increased 11.8% QoQ (organic basis).
Revenues	2,513	3,443	3,432	(0.3)	36.6	
- Operating costs	1,784	2,197	2,025	(7.8)	13.5	
EBITDA	729	1,247	1,407	12.9	92.9	Break up of EBIT margin YoY: S&D expenses (-250bps), Employee cost (+310bps), Depreciation & Amortization (-130bps), G&A expenses (-130bps) Exchange movement (-310bps).
EBITDA margin (%)	29.0	36.2	41.0	480bps	1,198bps	
- Interest expense	-	0	0			
- Depreciation	146	139	138	(1.0)	(5.2)	Q4FY16 had a forex loss of ₹0.5mn vs a gain of ₹2.9mn in Q3FY16
+ Other income, net (incl forex)	97	41	90	117.5	(7.1)	
PBT	680	1,148	1,359	18.3	99.7	
- Taxes	149	262	276	5.5	85.2	Tax rate to be in the range of 23-24% in FY17
Effective tax rate (%)	21.9	22.8	20.3	(247)bps	(159)bps	
PAT	531	887	1,083	22.1	103.8	
Net margin (%)	21.1	25.7	31.6	580bps	1,041bps	
Reported profits	531	887	1,083	22.1	103.9	

Source: Company

Exhibit 2: Change in estimates

₹ mn	FY17E			FY18E		
	Old	New	%Chg	Old	New	%Chg
Revenue (US\$ mn)	224	207	(7.6)	253	234	(7.5)
Revenue	14,346	13,484	(6.0)	16,226	15,239	(6.1)
EBITDA margin (%)	34.8	36.2	135bps	35.1	36.6	145bps
EPS (₹)	85.7	85.9	0.2	96.0	96.3	0.3

Source: Trust Research

Quarterly details: Client metrics continue to reflect the progression as no of US\$ 1mn+ clients increased to 17 in Mar'16 quarter up from 7 in Mar'15 quarter)

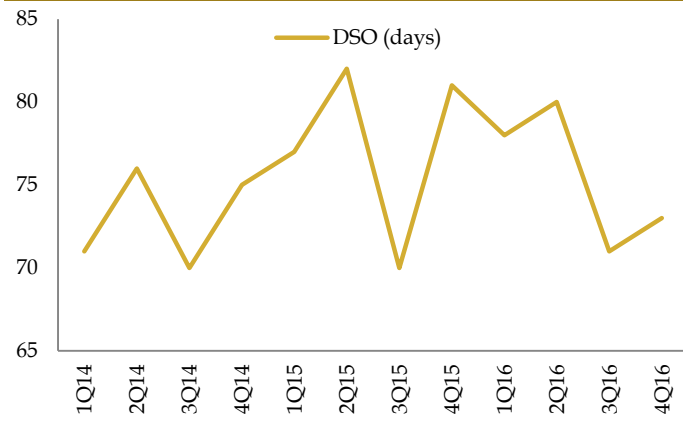
Exhibit 3: Operating metrics

Details	Q4FY14	Q1FY15	Q2FY15	Q3FY15	Q4FY15	Q1FY16	Q2FY16	Q3FY16	Q4FY16
US	74.0	73.0	74.0	78.0	78.0	72.0	67.0	67.0	66.0
Europe	22.0	22.0	23.0	18.0	18.0	25.0	29.0	29.0	30.0
RoW	4.0	5.0	3.0	4.0	4.0	3.0	4.0	4.0	4.0
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
FTE (%)	94.0	94.0	94.0	95.0	95.0	85.0	81.0	82.0	80.0
SEZ Revenue (%)	60.0	61.0	68.0	72.0	73.0	69.0	67.0	69.0	66.0
India Staff count (Nos.)	6,836	7,549	7,469	7,751	8,100	8,747	8,743	8,590	8,862
Revenue (US\$m)	35.5	36.2	38.0	38.8	40.6	46.4	50.2	51.8	50.7
Top 5 clients (%)	73.0	71.0	68.0	66.0	64.0	57.0	56.0	58.0	58.0
DSO (Days)	75.0	77.0	82.0	70.0	81.0	78.0	80.0	71.0	73.0
Cash/share (₹)	117.5	125.3	99.1	137.1	145.2	118.0	97.2	104.7	133.6

Source: Company

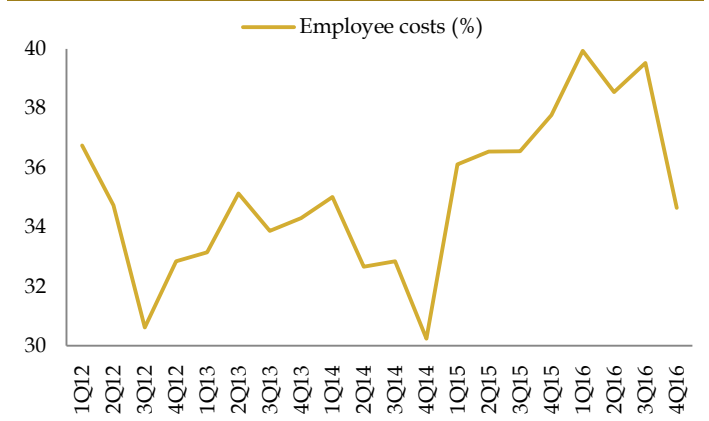


Exhibit 4: DSO days were up by 2 QoQ to 73



Source: Company, Trust

Exhibit 5: Margins were up due to lower employee cost



Source: Company, Trust



Financials

Income Statement (₹ mn)

Year End-March	FY14	FY15	FY16	FY17E	FY18E
Revenues	8,410	9,421	13,143	13,484	15,239
Op. Expenses	4,875	6,258	8,274	8,601	9,655
EBITDA	3,535	3,163	4,869	4,883	5,583
Other Income	110	324	404	392	425
Depreciation	330	500	507	636	704
EBIT	3,315	2,987	4,766	4,638	5,304
Interest	-	-	-	-	-
PBT	3,315	2,987	4,766	4,638	5,304
Tax	759	683	1,132	1,112	1,326
PAT	2,556	2,304	3,634	3,526	3,978
Ex. ordinary	-	-	-	-	-
Adj Pat	2,556	2,304	3,634	3,526	3,978

Key Parameters

Year End-March	FY14	FY15	FY16	FY17E	FY18E
Per share (₹)					
EPS	63.5	56.9	89.1	85.9	96.3
CEPS	71.7	69.3	101.5	101.4	113.3
BVPS	146.4	176.7	266.3	309.7	358.9
DPS	26.3	26.3	1.0	35.0	40.0
Payout (%)	48.3	53.9	1.3	47.7	48.6
Valuation (x)					
P/E	13.0	21.1	14.6	16.5	14.7
P/BV	5.6	6.8	4.9	4.6	3.9
EV/EBITDA	8.1	13.7	9.2	9.9	8.5
Dividend Yield (%)	3.2	2.2	0.1	2.5	2.8
Return ratio (%)					
EBITDA Margin	42.0	33.6	37.0	36.2	36.6
PAT Margin	30.4	24.5	27.6	26.2	26.1
ROAE	43.4	32.2	40.3	29.9	29.0
ROACE	56.3	41.8	52.9	39.4	38.6
Leverage Ratios (x)					
Long Term D/E	-	-	-	-	-
Net Debt/Equity	(0.6)	(0.6)	(0.5)	(0.6)	(0.6)
Debt/EBITDA	-	-	-	-	-
Interest Coverage	-	-	-	-	-
Current ratio	3.1	3.3	5.8	6.7	7.0
Growth Ratios (%)					
Income growth	27.3	12.0	39.5	2.6	13.0
EBITDA growth	37.8	(10.5)	53.9	0.3	14.3
PAT growth	47.3	(9.9)	57.7	(3.0)	12.8
Turnover Ratios					
F.A Turnover x	14.8	13.3	15.1	13.9	13.7
Debtors Days	36	44	43	51	48
Payable days	1	1	7	6	6

Balance Sheet (₹ mn)

Year End-March	FY14	FY15	FY16	FY17E	FY18E
Equity Share Capital	302	304	408	411	413
Reserves & Surplus	5,588	6,847	10,455	12,300	14,345
Total Shareholders Fund	5,890	7,150	10,863	12,711	14,758
Minority Interest	-	-	6	6	6
Non- current liabilities	148	163	277	290	324
Deferred tax liabilities	(18)	(52)	7	7	7
Other LT liabilities & prov	166	215	270	283	317
Current Liabilities	1,839	2,209	1,492	1,567	1,781
Short term Liabilities	-	-	35	35	35
Trade payables	11	17	138	141	159
Other cur liabilities & Prov	1,829	2,192	1,318	1,390	1,587
Total Liabilities	7,877	9,522	12,638	14,573	16,869
Assets					
Non- current Assets	2,196	2,332	3,960	4,091	4,314
Fixed assets	569	707	869	969	1,115
Non-current investments	990	975	2,531	2,531	2,531
Long-term loans & adv	637	650	560	591	668
Current assets	5,681	7,190	8,677	10,482	12,555
Current investments	1,155	1,553	2,191	2,191	2,191
Trade receivables	987	1,261	1,861	1,884	2,129
Inventories	-	-	5	6	7
Cash & bank balances	2,406	2,866	3,268	4,997	6,642
Short-term loans & adv	81	151	236	222	250
Other current assets	1,053	1,359	1,116	1,182	1,336
Total Assets	7,877	9,522	12,638	14,573	16,869

Cash flow Statement

Year End-March	FY14	FY15	FY16	FY17E	FY18E
PBT	3,315	2,987	4,766	4,638	5,304
Depreciation	325	467	566	636	704
Others	-	-	6	-	-
CF before W.cap	3,640	3,454	5,337	5,275	6,008
Inc/dec in W.cap	438	246	1,053	19	257
Op CF after W.cap	3,202	3,208	4,284	5,256	5,751
Less Taxes	759	683	1,132	1,112	1,326
Net CF From Operations	2,443	2,525	3,152	4,144	4,425
Inc/(dec) in F.A + CWIP	339	638	670	736	850
(Pur)/sale of Investments	998	384	2,194	-	-
CF from Invst Activities	(1,336)	(1,022)	(2,863)	(736)	(850)
Loans raised/(repaid)	-	-	35	-	-
Equity Raised	186	199	127	3	3
Dividend	1,236	1,243	48	1,681	1,934
CF from Fin Activities	(1,050)	(1,044)	114	(1,678)	(1,931)
Net inc / (dec) in cash	57	460	403	1,729	1,644
Op. bal of cash	2,349	2,406	2,866	3,268	4,997
Cl. balance of cash	2,406	2,866	3,268	4,997	6,642



Institutional Equity Team

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