

# Technology Sector Update

*Traditional sourcing to grow at 2% in CY18*

	CMP(₹)	3M ret.(%)	Yearly (%)
<b>Index Returns</b>			
Nifty	10,564	(3)	16
CNX IT	13,910	10	39
<b>Large-Caps</b>			
TCS	3,406	15	46
INFO	1,178	3	27
WPRO	298	(9)	19
HCLT	1,062	11	30
TECHM	701	27	67
<b>Mid-Caps</b>			
MTCL	980	40	122
MPHL	903	14	67
HEXW	436	24	111
ECLX	1,351	(12)	2
KPIT	243	24	91
NITEC	993	36	133
CYL	710	9	41
PSYS	734	(5)	29

ISG Outsourcing (TPI) came out with its findings on global outsourcing industry for Q1CY18. Commercial Combined Market ACV, up 11% YoY, surpasses US\$12bn for the first time ever. Traditional Sourcing declines moderately at 6% YoY, while As-a-Service increases 40%. Traditional Sourcing has its third straight quarter over US\$6bn but pulls back slightly YoY; As-a-Service ACV breaks through the US\$5bn level for the first time with stepped-up activity in the Public Cloud market segment. Deal values are expected to remain small with focus on security, Digital and Cloud. For 2018, on a global basis, ISG forecasts 20%+ growth in as-a-service sourcing, and 2% growth in traditional sourcing.

**Key highlights:** 1) Commercial Combined Market ACV, up 11% YoY, surpasses US\$12bn for the first time ever, 2) Traditional Sourcing declines moderately at 6% YoY, while As-a-Service increases 40% YoY, 3) Americas ACV up 32% YoY as both Traditional Sourcing and As-a-Service generates strong results; Traditional Sourcing sees strength in Applications and many BPO functional areas, 4) EMEA ACV down 20% YoY; Traditional Sourcing weighs down results with weakness in UK and DACH, 5) Asia Pacific ACV up 62% YoY versus a soft 1Q17; Traditional Sourcing up on strength in Applications and SE Asia and China activity; As-a-Service ACV breaks through US\$1bn for the first time.

**Trends across geographies:** **Global Contracting Trends** - Combined Market up 11% YoY, surpassing US\$12bn in ACV; Traditional Sourcing has its third straight quarter over US\$6bn but pulls back slightly YoY; As-a-Service ACV breaks through the US\$5bn level for the first time with stepped-up activity in the Public Cloud market segment. **Americas Contracting Trends** - Combined Market ACV up 32% YoY as the Americas registers strong results in both Traditional Sourcing and As-a-Service ACV; robust applications contracting and across the board in many BPO functional areas, while Public Cloud growth remains on a high trajectory. **Asia Pacific Contracting Trends** - Combined Market up 62% versus a soft 1Q17; As-a-Service ACV passes US\$1bn for the first time and now accounts for nearly 70% of market activity; Traditional Sourcing sees stepped-up activity in Applications contracting as well the China and Southeast Asia regions. **EMEA Contracting Trends** - Combined Market ACV in EMEA retracts 20% YoY as Traditional Sourcing sees its third straight weaker quarterly result on tepid activity in the UK and DACH; As-a-Service ACV remains on slow but steady journey upward but not enough to make up for slowing sourcing results.

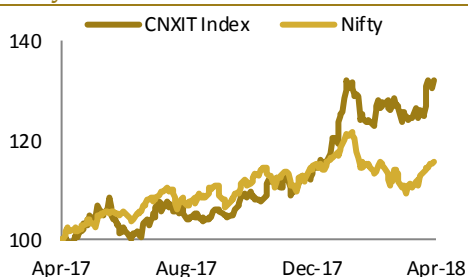
**Market Summary:** 1) Combined Commercial Market ACV continued to see double-digit YoY growth, surpassing US\$12bn for the first time ever, 2) Regional results were uneven as the Americas generated strong growth in both Traditional Sourcing and As-a-Service, while Asia Pacific generated very high growth but against a soft YoY compare, 3) EMEA saw its third straight weaker quarter in Traditional Sourcing, and even though As-a-Service activity continued to rise, it wasn't enough to offset the pullback in key markets like the UK and DACH.

**Market Outlook:** 1) Continue to forecast As-a-Service growth of 20%+ being led by growth in Public Cloud (30%+) and SaaS growth of 15%, 2) Traditional Sourcing growth forecast of 2% with uneven results across both the regions and industries.

**Hexaware, Polaris, Mindtree had deal signings across geographies among midcaps: Top-5 omnipresent:** Among the mid-caps in our coverage universe, Mindtree (Americas, EMEA), Hexaware (Americas, EMEA, APAC), Polaris (Americas, EMEA, APAC), KPIT (Americas) was mentioned in "The Breakthrough 15 Sourcing Standouts". L&T Infotech, which was present across Americas and EMEA in Q4CY17 was missing in 1QCY18.

	Rating	FDEPS (₹)	
		FY19E	FY20E
TCS	Hold	151.6	164.5
INFO	Buy	71.9	76.1
WPRO	Hold	20.6	22.4
HCLT	Buy	69.2	75.2
TECHM	Buy	40.1	43.2
MTCL	Buy	37.4	44.7
MPHL	Sell	45.8	50.8
HEXW	Hold	18.1	20.5
ECLX	Hold	72.4	83.1
KPIT	Hold	14.4	17.0
NITEC	Buy	52.9	60.3
CYL	Buy	41.9	46.9
PSYS	Hold	49.4	56.5

## Nifty vs CNX IT



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1) **Commercial Combined Market ACV, up 11% YoY, surpasses US\$12bn** for the first time ever, 2) **Traditional Sourcing declines moderately at 6% YoY, while As-a-Service increases 40% YoY**, 3) **Americas ACV up 32% YoY** as both Traditional Sourcing and As-a-Service generates strong results; Traditional Sourcing sees strength in Applications and many BPO functional areas, 4) **EMEA ACV down 20% YoY**; Traditional Sourcing weighs down results with weakness in UK and DACH, 5) **Asia Pacific ACV up 62% YoY** versus a soft 1Q17; Traditional Sourcing up on strength in Applications and SE Asia and China activity; As-a-Service ACV breaks through US\$1bn for the first time.

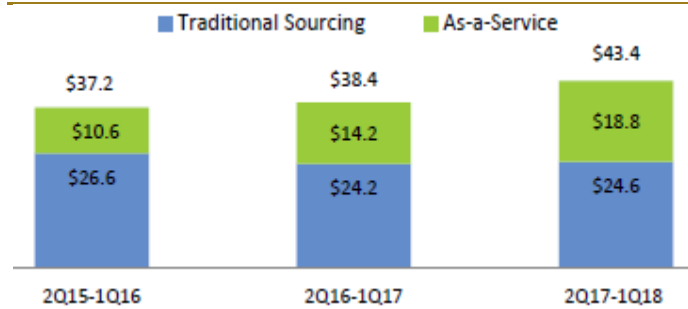
**Exhibit 1: Deal signings in Q1CY18 – At a glance**

Scorecard	1Q18 ACV (US\$ bn)*	1Q YoY Change (%)	TTM ACV (US\$ bn)	TTM Change (%)
<b>Global Commercial Combined Market</b>	<b>12.2</b>	<b>11</b>	<b>43.4</b>	<b>13</b>
By Type – Outsourcing	6.3	(6)	24.5	1
By Type – As-a-Service	5.9	40	18.8	32
By Region – Americas	6.9	32	23.3	24
By Region – EMEA	3.8	(20)	14.3	(9)
By Region – Asia Pacific	1.5	62	5.7	46

Source: 1Q18 – ISG – Outsourcing – Index, \*Contracts with ACV ≥ \$5M from the ISG Contracts Knowledgebase

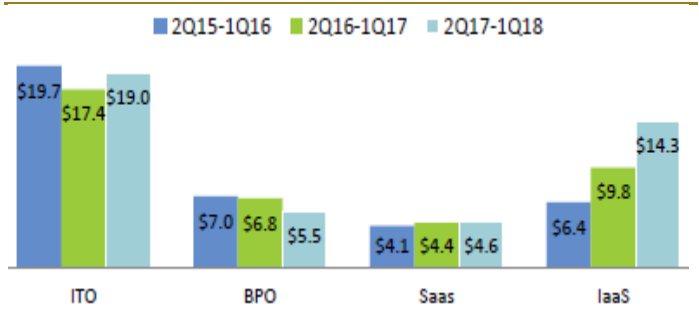
**Global Commercial Sector Contracting Trends** - Combined Market up 11% YoY, surpassing US\$12bn in ACV; Traditional Sourcing has its third straight quarter over US\$6bn but pulls back slightly YoY; As-a-Service ACV breaks through the US\$5bn level for the first time with stepped-up activity in the Public Cloud market segment.

**Exhibit 2: Global Commercial Sector TTM ACV (\$B)\***



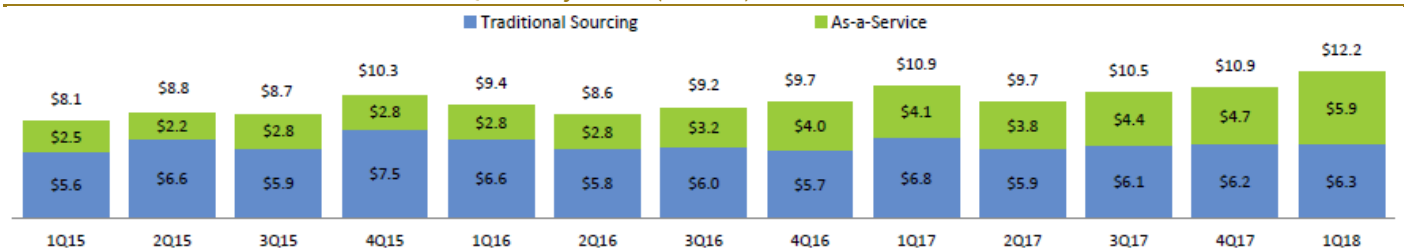
Source: 1Q18 – ISG – Outsourcing – Index

**Exhibit 3: Global Commercial Sector TTM ACV by type**



Source: 1Q18 – ISG – Outsourcing – Index

**Exhibit 4: Global Commercial Sector Quarterly ACV (US\$bn)\***

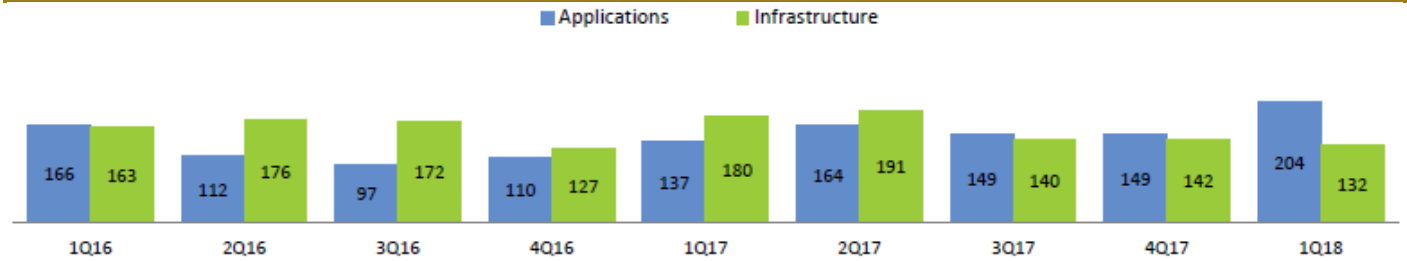


Source: 1Q18 – ISG – Outsourcing – Index, \*Contracts with ACV ≥ \$5M from the ISG Contracts Knowledgebase



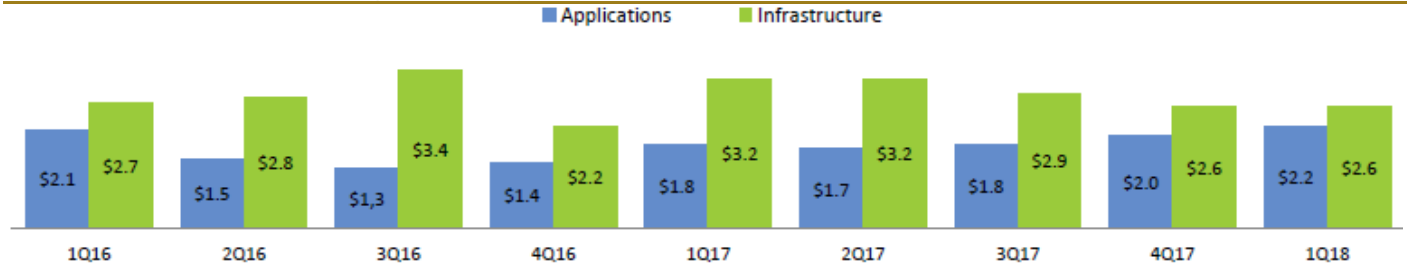
**ITO Award Trends -ADM/Infrastructure** - ADM shows strength across all three regions as ACV and number of awards are up 22% and 49% YoY, respectively; at the same time, Infrastructure Outsourcing ACV and number of awards fall 17% and 27% YoY, respectively, with weakness in EMEA and Asia/Pacific.

**Exhibit 5: Traditional Sourcing - Quarterly ADM/ Infrastructure (Number of Awards)**



Source: 1Q18 - ISG - Outsourcing - Index, \*Contracts with ACV ≥ \$5M from the ISG Contracts Knowledgebase

**Exhibit 6: Traditional Sourcing - Quarterly ADM/Infrastructure ACV (\$bn)\***



Source: 1Q18 - ISG - Outsourcing - Index, \*Contracts with ACV ≥ \$5M from the ISG Contracts Knowledgebase

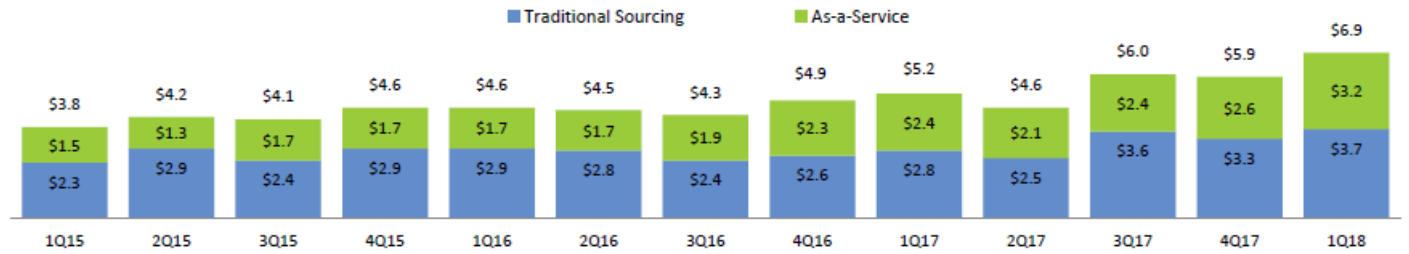
**Our view:** ISG commentary is in sync with the financial performance of Indian IT companies - with companies pointing out to revenue visibility being better than CY17, since Indian IT companies are still dependent on traditional outsourcing as their main business. We continue to prefer companies with stronger revenue momentum and margin of safety in valuations - HCLT and Tech Mahindra in large-caps.

**Top-5 omnipresent:** Among the mid-caps in our coverage universe, Mindtree (Americas, EMEA), Hexaware (Americas, EMEA, APAC), Polaris (Americas, EMEA, APAC), KPIT (Americas) was mentioned in "The Breakthrough 15 Sourcing Standouts". L&T Infotech, which was present across Americas and EMEA in Q4CY17 was missing in 1QCY18.



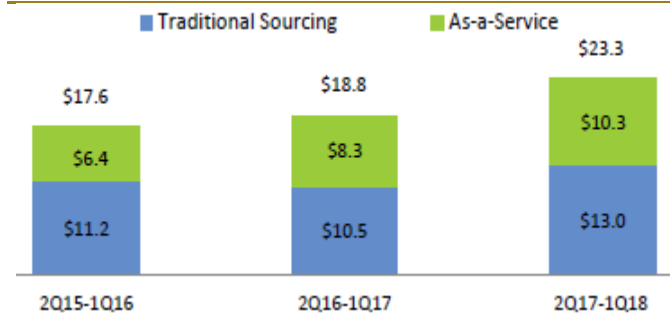
**Americas Commercial Sector Contracting Trends** - Combined Market ACV up 32% YoY as the Americas registers strong results in both Traditional Sourcing and As-a-Service ACV; robust applications contracting and across the board in many BPO functional areas, while Public Cloud growth remains on a high trajectory.

**Exhibit 7: Americas Commercial Sector Quarterly ACV (US\$bn)\***



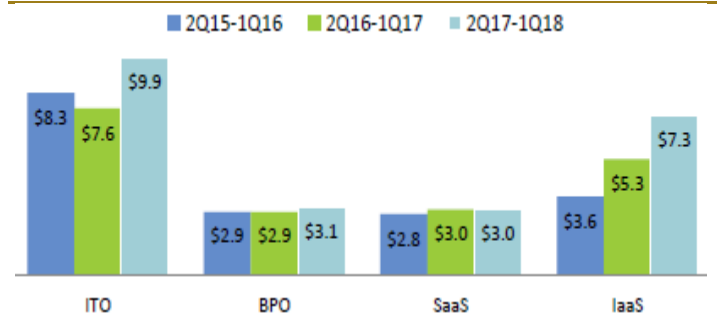
Source: 1Q18 - ISG - Outsourcing - Index, \*Contracts with ACV ≥ \$5M from the ISG Contracts Knowledgebase

**Exhibit 8: Americas Commercial Sector TTM ACV**



Source: 1Q18 - ISG - Outsourcing - Index

**Exhibit 9: America Comm. Sector TTM ACV**



Source: 1Q18 - ISG - Outsourcing - Index

**Exhibit 10: Americas Top 15s - Sourcing standouts grouped by company size**

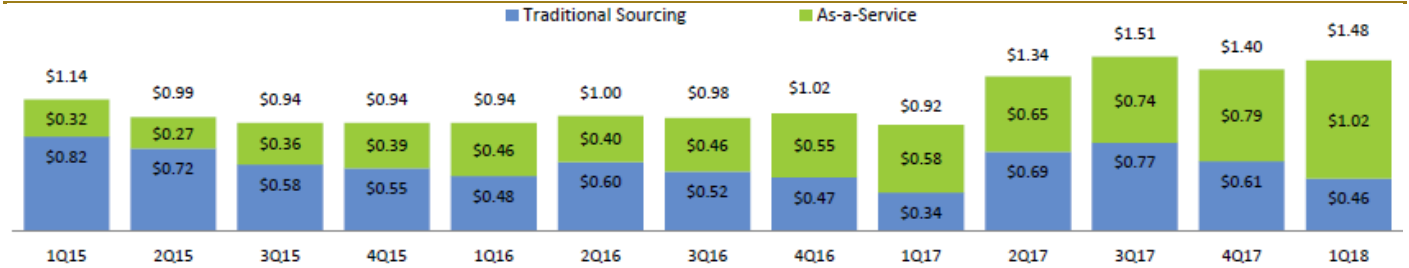
The Big 15 Co. Revenues > \$10 B	The Building 15 Co. Revenues \$1 -10 B	The Breakthrough 15 Co. Revenues < \$1 B
<p><b>Traditional Sourcing Market</b></p> <ul style="list-style-type: none"> <li>Accenture *</li> <li>AT&amp;T *</li> <li>Atos</li> <li>Capgemini</li> <li>Cognizant</li> <li>DXC Technology</li> <li>IBM</li> <li>Infosys</li> <li>NTT DATA</li> <li>TCS</li> </ul> <p><b>As-a-Service Market</b></p> <ul style="list-style-type: none"> <li>Amazon Web Services</li> <li>Google</li> <li>Microsoft</li> <li>Oracle</li> <li>Salesforce</li> </ul>	<p><b>Traditional Sourcing Market</b></p> <ul style="list-style-type: none"> <li>Alliance Data Systems *</li> <li>Black Knight Inc.</li> <li>Cerner *</li> <li>Global Payments *</li> <li>HCL</li> <li>OptumInsight *</li> <li>Tech Mahindra *</li> <li>Total System Services</li> <li>Unisys</li> <li>Vantiv *</li> <li>Wipro</li> </ul> <p><b>As-a-Service Market</b></p> <ul style="list-style-type: none"> <li>Adobe Systems</li> <li>Digital Realty</li> <li>Equinix</li> <li>Iron Mountain</li> </ul>	<p><b>Traditional Sourcing Market</b></p> <p>C3/CustomerContactChannels</p> <ul style="list-style-type: none"> <li>CSG Systems</li> <li>Ensono</li> <li>EXL *</li> <li>Hexaware</li> <li>HGS *</li> <li>KPIT Technologies *</li> <li>Mindtree</li> <li>StarTek *</li> <li>Syntel</li> <li>Virtusa</li> </ul> <p><b>As-a-Service Market</b></p> <ul style="list-style-type: none"> <li>Coresite</li> <li>CyrusOne</li> <li>IPSoft *</li> <li>LogMeIn</li> </ul>

Source: 1Q18 - ISG - Outsourcing - Index, Placements based on the annual value of commercial contract awards in the past 12 months sourced from ISG Contracts Knowledgebase



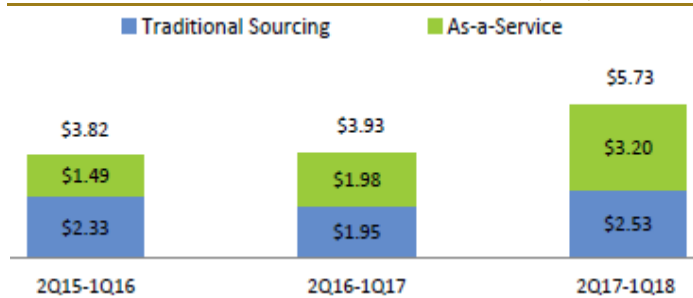
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**Exhibit 11: Asia Pacific Commercial Sector Quarterly ACV (\$B) \***



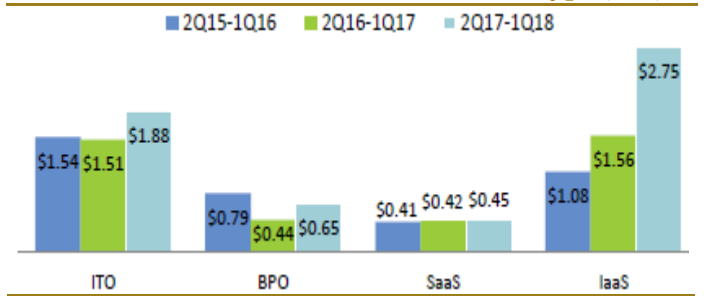
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**Exhibit 12: APAC Comm. Sector TTM ACV (\$bn)\***



Source: 1Q18 - ISG - Outsourcing - Index

**Exhibit 13: APAC Comm. Sector TTM ACV Type (\$bn)**



Source: 1Q18 - ISG - Outsourcing - Index

**Exhibit 14: Asia Pacific Top 15s - Sourcing standouts grouped by company size**

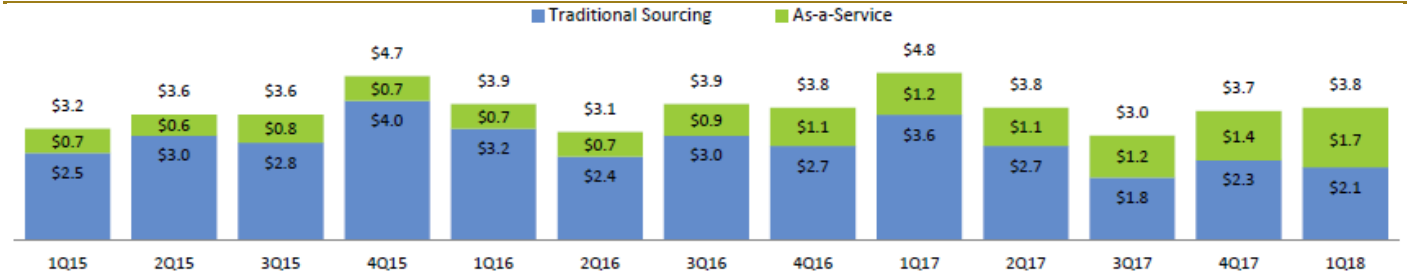
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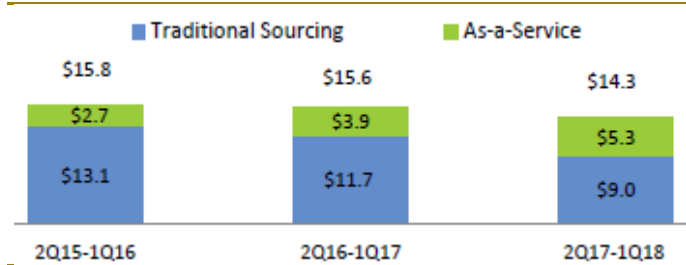
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**Exhibit 15: EMEA Commercial Sector Quarterly ACV (US\$ bn)\***



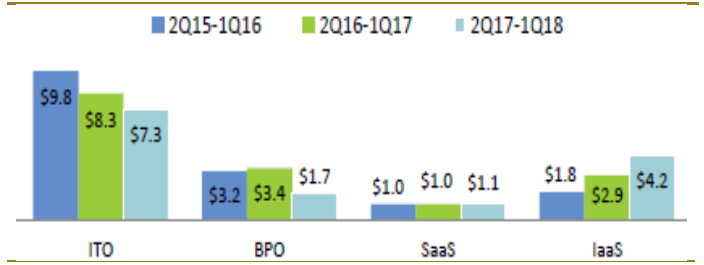
Source: 1Q18 - ISG - Outsourcing - Index, \*Contracts with ACV ≥ \$5M from the ISG Contracts Knowledgebase

**Exhibit 16: EMEA Comm. Sector TTM ACV (\$B)\***



Source: 1Q18 - ISG - Outsourcing - Index

**Exhibit 17: EMEA Comm. Sector TTM ACV by Type**



Source: 1Q18 - ISG - Outsourcing - Index

**Exhibit 18: EMEA Top 15s - Sourcing standouts grouped by company size**

The Big 15 Co. Revenues > \$10 B	The Building 15 Co. Revenues \$1 -10 B	The Breakthrough 15 Co. Revenues < \$1 B
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Source: 1Q18 - ISG - Outsourcing - Index, Placements based on the annual value of commercial contract awards in the past 12 months sourced from ISG Contracts Knowledgebase

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Disclosure of Interest Statement	Name of Company
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Served as Director or Employee	No

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Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	15% to -15%
Sell	Less than -15%

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