

Market statistics

Current stock price (₹)	298
Shares O/S (cr.)	19.7
Mcap (₹ cr)	5,894
52W H/L (₹)	305/105
6m avg. volume	2,650,073
Bloomberg	KPIT.IN

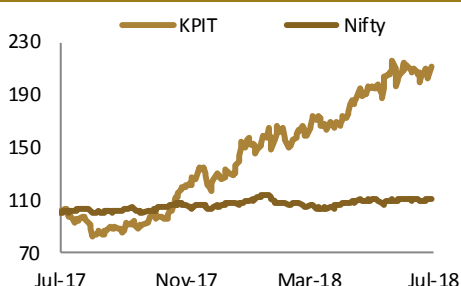
KPIT's 1QFY19 revenue increased 0.2% QoQ in US\$ terms at US\$150.5mn, slightly lower than our expectations. EBITDA margin (adjusted for legal costs) was at 13.2%, up 48bps QoQ. Recurring PAT was at ₹882mn. Amid robust revenue growth momentum, upcoming investments, KPIT maintained 8-10% cc revenue growth guidance for FY19. KPIT has announced a transaction with Birlasoft which will initially create one new combined entity, which will then segregate into two separate entities – Engineering services and IT Services. The current valuations capture a fairly robust recovery in margins for KPIT, continued strong growth in Engineering, and also revenue momentum in Birlasoft. We maintain our Hold rating on the stock, till further clarity on the demerger-merger process between KPIT and Birlasoft.

Shareholding pattern

Promoters	18.93
Domestic Institution	4.96
Foreign Institution	49.55
Non-institution	26.55
of which more than 1%	

Decent profitability performance: KPIT's 1QFY19 revenue increased 0.2% QoQ to US\$150.5mn. Operational EBITDA margin was at 13.2%, up 48bps QoQ. The quarter included expenses related to the demerger of the Engineering business and the merger with Birlasoft. Including these expenses, EBITDA margin was at 12.1%, up 75bp QoQ. In terms of geographies, US (2.8% QoQ) led growth. Europe (-3.4% QoQ) and ROW (-4.5% QoQ) remained soft during the quarter. Among SBU's, growth was led by Product Engineering Services (5.5% QoQ) and Digital transformation (2.1% QoQ). Products and SAP were subdued at -39.6% QoQ and -3.6% QoQ respectively. Amongst verticals, Automotive & Transportation and manufacturing grew on the back of strength seen in Engineering.

KPIT vs Nifty



Other Key details – 1) Top 20 constituted 52.5% of the total revenues and grew by 1.7%. Similarly, the 40 top accounts constituted 65.1% of the revenues and had a QoQ growth of 3.4%. 2) On the revenue front, 12% YoY growth in 1QFY19 implies some possibility of exceeding the guided range of 8-10%. 3) YoY revenue growth of 12% was backed by Product Engineering (+5.5% QoQ) and Digital transformation (+2.2% QoQ). Product remained inherently lumpy with revenue decline of 41% QoQ. 4) The IT services business remains sluggish with SAP declining by 3.5% QoQ.

Concall details. 1) Margins likely to be in the range of 11.5-12.5%: KPIT margins for the next quarter would be impacted by wage hike (220-240bps). However, growth and cost levers should help offset ~100bp of this impact. The remaining should be recouped through the course of 2H. 2) More constructive on IT Services: SAP business was impacted by yet another quarter; H1 to remain soft for SAP. However, IES' good run should continue, 3) Significant traction in Engineering: KPIT has shown growth in PES business and registered growth of 5.5% sequentially. 4) Positive on Europe and Americas: Although revenue from Europe declined sequentially by 3.4%, KPIT is bullish on deals coming from Germany. This quarter growth was led by the US.

Capital efficiency & valuations

Particulars	FY18	FY19E	FY20E
RoE (%)	15.2	17.1	16.5
EPS (₹)	12.6	16.2	18.4
CEPS (₹)	16.9	22.5	24.6
P/E (x)	17.2	17.7	15.6
P/BV (x)	2.4	2.7	2.4
EV/EBITDA (x)	10.2	9.8	8.1
Income growth (%)	10.3	14.3	8.7
EBITDA growth (%)	8.6	37.5	11.6
PAT growth (%)	17.8	33.1	9.9

Deal wins showing traction: Over recent quarters, KPIT won deals across Engineering, SAP, JDE, EPLM, and ES. There was an increased traction in the areas of AMS & IMS combined, around SAP, Oracle, BI and ES. These opportunities seen were across all geographies, including Europe and Asia. Their investments in SBU & IBU and focus on large deals will start showing results. KPIT's Strategic Client Engagement team is focusing on winning large annuity deals.

Valuation and view: The merger that KPIT has announced with Birlasoft will initially create one new combined entity, which will then segregate into two separate entities – Engineering services and IT Services. Birlasoft will be nearly one-third of the combined entity, and hence visibility in that segment is key determinant of KPIT's value. However, that will remain elusive till the merger process completes. Current valuations capture a fairly robust recovery in margins for KPIT, continued strong growth in Engineering, and also revenue momentum in Birlasoft (~12-13% CAGR, mid-teens EBITDA margin), basis the numbers shared at the time of demerger announcement.

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Exhibit 1: Quarterly details

` mn	1QFY18	4QFY18	1QFY19	QoQ (%)	YoY (%)	Comments
Revenues (in US\$ mn)	134.4	150.2	150.5	0.2	12.0	12% YoY growth implies some possibility of exceeding the guided range of 8-10%.
Revenues	8,704	9,664	10,138	4.9	16.5	
- Operating costs	7,909	8,437	8,802	4.3	11.3	
EBITDA	795	1,227	1,336	8.9	68.1	
EBITDA margin (%)	9.1	12.7	13.2	48bps	405bps	KPIT has margin levers like people productivity, span of control and employee pyramid to gain expansion
- Interest expense	26	29	54	87.7	109.3	
- Depreciation	190	256	270	5.5	42.1	
+ Other income, net (incl forex)	121	191	162	(14.9)	34.4	
PBT	699	1,133	1,174	3.7	67.9	
- Taxes	170	165	241	45.5	41.8	Tax rate to be ~24-26%
Effective tax rate (%)	24.3	14.6	20.5	590bps	(378)bps	
PAT	530	967	934	(3.5)	76.2	
Net margin (%)	6.1	9.2	8.7	(50)bps	263bps	
Reported profits	555	760	774	1.9	39.6	

Source: Company

Exhibit 2: Geographical wise Performance

Geographical mix	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19
US	67.5	67.2	70.1	68.1	63.9	63.7	63.7	61.5	63.1
Europe	18.4	16.2	14.4	16.4	18.8	18.5	19.9	20.8	20.0
RoW	14.1	16.6	15.5	15.5	17.3	17.9	16.4	17.7	16.8
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company

LOB wise Performance: Among SBU's, growth was led by Product Engineering Services (5.5% QoQ) and Digital transformation (2.1% QoQ). Products and SAP were subdued at -39.6% QoQ and -3.6% QoQ respectively. Amongst verticals, Automotive & Transportation and manufacturing grew on the back of strength seen in Engineering.

Exhibit 3: Revenue spread by LOB

	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19
Integrated Enterprise Solutions	31.5	29.7	29.6	29.3	27.9	27.0	26.9	29.6	30.3
Product Engineering Services	33.7	33.3	31.8	33.5	35.2	37.7	39.0	36.3	38.2
Products & Platforms	2.2	4.5	3.9	3.7	5.5	4.2	3.8	5.4	3.3
SAP	24.0	22.8	23.4	23.2	21.6	20.5	20.0	18.4	17.7
Enterprise Solutions	8.6	9.7	11.4	10.2	9.8	10.6	10.3	10.3	10.5
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company, Trust Research



Human Resources: In Q1FY19, there was a net increase of 424 people. KPIT plans to add ~175-200 fresh graduates in 2Q/3Q/4QFY19.

Exhibit 4: Employee strength at KPIT

	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19
Development team - Onsite (avg)	1,651	1,634	1,664	1,664	1,692	1,751	1,762	1,764	1,856
Development team - Offshore (avg)	8,553	8,986	9,238	9,048	9,608	9,469	9,438	9,712	9,965
Onsite FTE	1,470	1,464	1,483	1,485	1,513	1,621	1,643	1,643	1,734
Offshore FTE	5,826	6,214	6,267	6,183	6,614	6,648	6,683	7,085	7,098
Development (at qtr end)	10,450	10,816	11,017	11,225	11,368	11,070	11,324	11,626	12,040
General (end of qtr)	604	608	616	629	635	630	636	645	651
Marketing (end of qtr)	234	242	248	256	258	246	251	256	260
Total (at qtr end)	11,288	11,666	11,881	12,110	12,261	11,946	12,211	12,527	12,951
Onsite utilization	89.0	89.6	89.2	89.3	89.4	92.6	93.3	93.1	93.4
Offshore utilisation	68.1	69.2	67.8	68.3	68.8	70.2	70.8	73.0	71.2

Source: Company, Trust Research

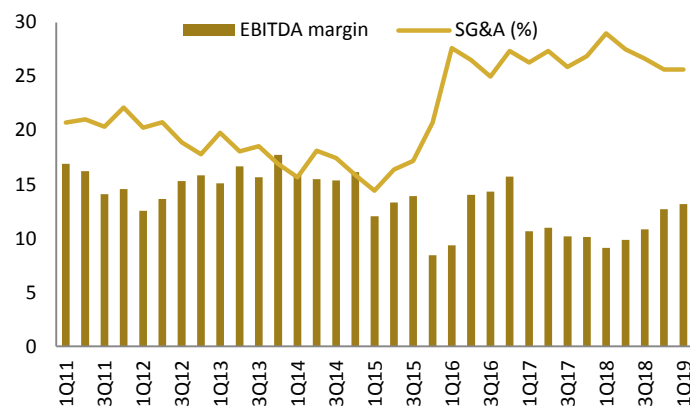
Details: In terms of geographies, US (2.8% QoQ) led growth. Europe (-3.4% QoQ) and ROW (-4.5% QoQ) remained soft during the quarter.

Exhibit 5: Client details

	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19
Clients Added	2	3	2	3	2	4	3	4	3
Total active clients	220	223	225	228	230	234	237	241	244
Customers with a run rate of \$1mn+	88	90	89	90	90	93	92	94	93
Top customer - Cummins (%)	12.8	13.1	12.6	12.7	12.5	12.0	12.2	12.1	NA
Top 20 Clients (%)	NA	NA	44.2	47.7	51.6	49.6	50.7	51.8	52.5
Top 40 Clients (%)	NA	NA	55.9	59.0	60.6	59.8	61.3	63.1	65.1

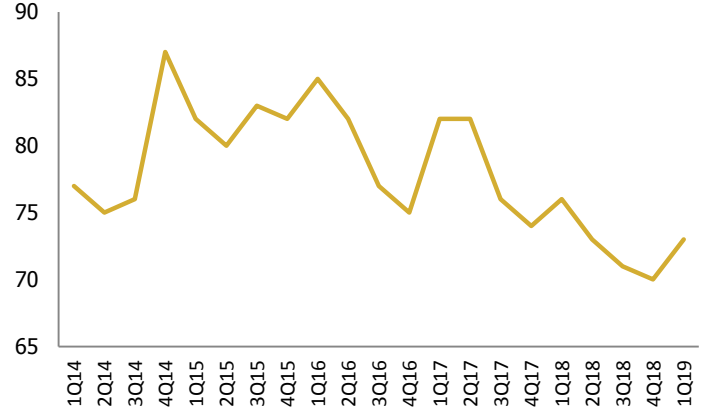
Source: Company

Exhibit 6: OPM was up 48bps QoQ operationally



Source: Company, Trust

Exhibit 7: DSO days were up 3 days QoQ to 73



Source: Company, Trust



Financials

Income Statement (` mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E
Revenues	32,264	33,234	36,656	41,906	45,541
Op. Expenses	27,922	29,747	32,871	36,702	39,734
EBITDA	4,342	3,487	3,785	5,204	5,808
Other Income	282	207	450	462	455
Depreciation	691	827	843	1,144	1,232
EBIT	3,933	2,867	3,392	4,522	5,031
Interest	165	136	104	158	150
PBT	3,767	2,731	3,288	4,364	4,881
Tax	845	606	698	1,032	1,220
PAT	2,922	2,125	2,591	3,332	3,661
Minority	-	-	(88)	-	-
Ex. ordinary	(113)	261	(103)	(108)	0
Adj Pat	2,809	2,386	2,400	3,224	3,661

Key Parameters

Year End-March	FY16	FY17	FY18	FY19E	FY20E
Per share (`)					
EPS	15.0	10.8	12.6	16.2	18.4
CEPS	18.6	14.9	16.9	22.5	24.6
BVPS	71.0	80.2	91.9	106.1	120.3
DPS	2.2	2.2	2.4	3.0	3.5
Payout (%)	17.4	23.9	22.2	21.0	22.3
Valuation (x)					
P/E	9.6	12.0	17.2	17.7	15.6
P/BV	2.0	1.6	2.4	2.7	2.4
EV/EBITDA	5.6	6.5	10.2	9.8	8.1
Dividend Yield (%)	1.5	1.7	1.1	1.0	1.2
Return ratio (%)					
EBITDA Margin	13.5	10.5	10.3	12.4	12.8
PAT Margin	9.1	6.4	7.1	8.0	8.0
ROAE	21.8	14.3	15.2	17.1	16.5
ROACE	24.5	14.9	16.1	19.3	19.5
Leverage Ratios (x)					
Long Term D/E	0.1	0.1	0.0	0.0	0.0
Net Debt/Equity	(0.2)	(0.2)	(0.2)	(0.3)	(0.3)
Debt/EBITDA	0.4	0.3	0.2	0.1	0.1
Interest Coverage	24.1	19.6	28.2	25.7	30.4
Current ratio	2.1	1.9	2.2	2.3	2.5
Growth Ratios (%)					
Income growth	7.8	3.0	10.3	14.3	8.7
EBITDA growth	21.9	(19.7)	8.6	37.5	11.6
PAT growth	9.6	(27.3)	17.8	33.1	9.9
Turnover Ratios					
F.A Turnover x	11	8	8	9	10
Debtors Days	78	81	79	78	77
Payable days	17	17	17	17	16

Balance Sheet (` mn)

Year End-March	FY16	FY17	FY18	FY19E	FY19E
Equity Share Capital	376	376	379	379	379
Reserves & Surplus	13,432	15,465	17,826	20,351	23,197
Total Shareholders Fund	13,808	15,841	18,205	20,730	23,576
Minority Interest	-	-	-	-	-
Non- current liabilities	1,569	1,696	1,506	1,322	1,180
Long term Borrowings	1,673	1,117	818	618	418
Deferred tax liabilities	(620)	-	-	-	-
Other LT liabilities & prov	516	579	687	704	762
Current Liabilities	5,956	7,676	7,618	8,696	9,194
Short-term borrowings	498	2,217	2,109	2,059	2,009
Trade payables	1,233	1,311	1,587	1,609	1,742
Other cur liabilities & Prov	4,225	4,148	3,922	5,028	5,443
Total Liabilities	21,333	25,214	27,329	30,748	33,950
Assets					
Non- current Assets	4,531	6,465	6,482	6,889	6,933
Fixed assets	2,850	3,968	4,335	4,739	4,607
Goodwill	4,025	4,117	4,275	4,275	4,275
Non-current investments	118	118	118	118	118
Long-term loans & adv	1,510	1,548	1,707	1,952	2,121
Other non-current assets	53	832	322	80	87
Current assets	12,777	14,631	16,573	19,585	22,742
Current investments	0	0	0	0	0
Inventories	380	433	239	574	624
Trade receivables	6,861	7,843	8,057	9,874	10,730
Cash & bank balances	3,953	3,902	5,050	5,922	7,894
Short-term loans & adv	677	728	904	1,033	1,123
Other current assets	907	1,724	2,323	2,181	2,371
Total Assets	21,333	25,214	27,329	30,748	33,950

Cash flow Statement

Year End-March	FY16	FY17	FY18	FY19E	FY19E
PBT	3,767	2,731	3,288	4,364	4,881
Depreciation	592	1,446	843	1,144	1,232
Interest Exp	165	136	104	158	150
Others	(113)	261	(191)	(108)	-
CF before W.cap	4,412	4,574	4,044	5,558	6,263
Inc/dec in W.cap	(617)	2,659	284	999	755
Op CF after W.cap	5,029	1,915	3,760	4,560	5,508
Less Taxes	845	606	698	1,032	1,220
Net CF From Operations	4,183	1,309	3,063	3,527	4,287
Inc/(dec) in F.A + CWIP	1,822	1,944	1,210	1,548	1,100
(Pur)/sale of Investments	(2,369)	92	158	-	-
Others	(165)	(136)	(104)	(158)	(150)
CF from Invst Activities	382	(2,172)	(1,472)	(1,706)	(1,250)
Loan Raised	(2,286)	1,163	(406)	(250)	(250)
Equity Raised	(1,455)	157	520	-	-
Dividend	508	508	557	699	815
CF from Fin Activities	(4,249)	811	(443)	(949)	(1,065)
Net inc /(dec) in cash	316	(51)	1,147	872	1,972
Op. bal of cash	3,638	3,953	3,902	5,050	5,922
Cl. balance of cash	3,953	3,902	5,050	5,922	7,894



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