# Sonata Software BUY

## Driving resilient growth with intelligent modernization


### Summary

**Sonata Software delivered a resilient Q3 FY26 performance despite headwinds from a few large clients. Revenue grew marginally QoQ, but profitability improved sharply, with EBITDA rising to ~19.5%, driven by higher utilization, offshore mix improvement, AI-led productivity, and cost optimization, even after absorbing wage hikes and higher cloud costs. The company's strategy as a modernization engineering firm powered by platforms and AI is gaining traction, with AI-led deals now contributing 14% of the order book and cloud/data forming ~50% of the pipeline. Large deal momentum remains strong, with two multi-year BFSI wins improving medium-term revenue visibility. BFSI and Healthcare continue to be core growth engines, while Retail and some TMT segments remain soft due to client-specific budget cuts. North America now contributes over 70% of revenue, reflecting deeper client penetration. Management expects near-term growth to remain muted for 1–2 quarters but is confident of returning to YoY growth as large deals ramp up. Overall, Sonata's improving margins, strong order book, AI differentiation, and disciplined execution support a stable medium-term outlook despite short-term revenue volatility. We upgrade our rating to BUY due to the recent stock price correction, valuing the stock at 17.8x FY27E EPS with a same target price of Rs 355.**


### Key Highlights and Investment Rationale

- **Near term challenges and growth story remains intact:** Near-term growth faces client-specific slowdowns, but large deal wins, AI adoption, and margin strength support a steady medium-term growth story.
- **Deal TCV & Margin outlook:** Strong large-deal TCV improves revenue visibility, while AI-led efficiency, offshore mix, and utilization gains support sustained high-teens to low-20s margins.

| TP | Rs355 |
|---|---|
| **CMP** | **Rs306** |
| Potential upside | 16% |
| Previous Rating | HOLD |

**Price Performance (%)**

| | -1m | -3m | -12m |
|---|---|---|---|
| Absolute | (15.5) | (16.9) | (37.5) |
| Rel to Sensex | (14.8) | (17.3) | (44.9) |

**V/s Consensus**

| EPS (Rs) | FY26E | FY27E |
|---|---|---|
| IDBI Capital | 16.7 | 19.9 |
| Consensus | 16.9 | 20.0 |
| *% difference* | *(1.1)* | *(0.3)* |

**Key Stock Data**

| | |
|---|---|
| Bloomberg/Reuters | SSOF IN / SOFT.BO |
| Sector | IT Services |
| Shares o/s (mn) | 280 |
| Market cap. (Rs mn) | 85,838 |
| 3-m daily avg Trd value(Rs mn) | 32.5 |
| 52-week high / low | Rs499 / 286 |
| Sensex / Nifty | 83,580 / 25,694 |

**Shareholding Pattern (%)**

| | |
|---|---|
| Promoters | 28.2 |
| FII | 8.8 |
| DII | 26.0 |
| Public | 37.0 |

**Financial snapshot** (Rs mn)

| Year | FY23 | FY24 | FY25 | FY26E | FY27E |
|---|---|---|---|---|---|
| Revenue | 74,491 | 86,131 | 1,01,703 | 1,06,312 | 1,16,360 |
| *Change (yoy, %)* | *34.1* | *15.6* | *18.1* | *4.5* | *9.5* |
| EBITDA | 6,041 | 7,274 | 7,027 | 7,058 | 8,087 |
| *Change (yoy, %)* | *30.3* | *20.4* | *(3.4)* | *0.4* | *14.6* |
| *EBITDA Margin(%)* | *8.1* | *8.4* | *6.9* | *6.6* | *7.0* |
| Adj.PAT | 4,519 | 4,831 | 4,377 | 4,694 | 5,594 |
| EPS (Rs) | 32.6 | 17.2 | 15.6 | 16.7 | 19.9 |
| *Change (yoy, %)* | *20.0* | *(47.1)* | *(9.4)* | *7.2* | *19.2* |
| PE(x) | 12.6 | 23.7 | 26.2 | 24.4 | 20.5 |
| Dividend Yield (%) | 3.9 | 1.9 | 2.0 | 2.0 | 2.0 |
| EV/EBITDA (x) | 8.7 | 15.2 | 16.0 | 15.1 | 12.6 |
| RoE (%) | 37.7 | 35.7 | 28.1 | 25.7 | 26.5 |
| RoCE (%) | 26.7 | 23.4 | 25.1 | 27.6 | 33.8 |

*Source: Company, IDBI Capital Research*


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## Con-call Highlights:

- International Services revenue grew ~40 bps QoQ in constant currency, reflecting resilience despite headwinds from three large clients. YoY revenue growth remained modest, constrained primarily by ramp-downs in one large BFSI client, one large TMT client, and an unexpected ramp-down in a large retail client.
- Management emphasized that outside these three clients, the rest of the portfolio delivered healthy growth, highlighting underlying business strength.
- The domestic business showed strong momentum, with revenue growth of ~68% QoQ, driven by system integration deals, expanded Microsoft channel focus, and OEM-led partnerships.
- EBITDA margin improved sharply to ~19.5%, up from ~17.3% QoQ, marking a ~220 bps QoQ expansion.
- Margin expansion was driven by AI-led productivity improvements, higher utilization (90% vs 87.3% QoQ), offshore mix improvement (63% vs 57% QoQ), pyramid optimization, and delivery efficiencies. These positives were partially offset by higher cloud (CSP) and AI-related pass-through costs, especially in bundled cloud-services deals.
- Management reiterated confidence that Sonata is now structurally a high-teens to low-20s EBITDA margin company, with margins expected to remain broadly stable in the 18–21% range going forward.
- Normalized PAT grew ~6% QoQ and ~21% YoY, reflecting strong operational leverage.
- Reported PAT was impacted by a one-time labor code provision (~INR 28–31 crore), which management clarified as non-recurring.
- BFSI and Healthcare & Life Sciences remain Sonata’s strongest verticals, together contributing ~31% of total revenue, up sharply from ~13% three years ago.
- BFSI weakness in Q3 was entirely attributable to a single large client, with management confirming the impact is now fully absorbed, and growth expected from Q4 onward supported by two newly signed large BFSI deals.
- TMT showed mixed performance, with strong momentum in engineering and AI-led modernization work, partially offset by continued budget pressure in non-engineering programs at one large client.

- Retail & Manufacturing remains soft, with further near-term impact expected from a large retail client ramp-down, though management expects stabilization and gradual recovery from FY27.
- North America now contributes over 70% of total revenue, up from ~54% three years ago, reflecting deeper wallet share and large-deal success.
- Europe and other regions remain stable, with no major structural weakness highlighted.
- Management expects geographic mix to remain NA-led, with diversification supported by selective Europe and APAC wins.
- Sonata secured two large multi-year deals in Q3, both in BFSI, including one with a Fortune 500 fintech/payments company and another with a leading mortgage provider.
- Order book stood at USD ~97 mn, with a book-to-bill ratio of 1.18, indicating healthy deal momentum.
- AI-led deals contributed ~14% of total order bookings, up from ~10% in the previous quarter, reflecting accelerating AI adoption.
- The number of clients with USD 10 mn+ annual run-rate increased to eight, indicating stronger strategic account depth.
- Sonata is increasingly positioned as a modernization engineering and AI transformation partner, rather than a traditional IT services vendor.
- Clients value Sonata’s platform-led and AI-integrated delivery model, particularly for regulated, complex legacy environments in BFSI and healthcare.
- LTM attrition stood at ~11%, remaining stable and healthy.
- Total headcount increased to ~6,404, over 92% of employees and 80% of managers are AI-trained, reinforcing Sonata’s AI-first operating model.
- AI is now core to Sonata’s growth strategy, embedded across delivery, platforms, and internal operations, with production-grade AI agents deployed via its Agent Bridge platform.
- Management views AI as net-positive, enabling market-share gains, faster delivery, and margin expansion, despite clients demanding higher productivity.

- While AI increases pricing pressure in some cases, Sonata is able to retain part of productivity gains, particularly where faster time-to-market is prioritized over cost savings.
- The IT services sector is seen as resilient but selective, with spending focused on modernization, AI, and regulated transformation rather than discretionary digital programs.
- Management expects near-term growth trajectory to remain similar over the next 1–2 quarters, as residual impact from large clients plays out.
- Return to YoY growth is expected by Q2FY27, as new large deals ramp up and client headwinds normalize.

**Exhibit 1: Financial snapshot** (Rs mn)

| Year-end: March | Q3FY26 | Q2FY26 | *QoQ (%)* | Q3FY25 | *YoY (%)* |
|---|---|---|---|---|---|
| **International Revenue (US$mn)** | **82** | **82** | ***0.4*** | **87** | ***(5.4)*** |
| **Revenues** | **30,806** | **21,193** | ***45.4*** | **28,428** | ***8.4*** |
| COGS | 27,718 | 18,010 | *53.9* | 24,366 | *13.8* |
| Gross profit | 3,088 | 3,183 | *(3.0)* | 4,062 | *(24.0)* |
| SG&A | 1,086 | 1,456 | *(25.4)* | 2,426 | *(55.2)* |
| **EBITDA** | **2,002** | **1,727** | ***15.9*** | **1,636** | ***22.4*** |
| Depreciation & amortization | 265 | 263 | *1.1* | 323 | *(17.8)* |
| EBIT | 1,737 | 1,464 | *18.6* | 1,313 | *32.3* |
| Other income | 114 | 314 | *(63.6)* | 215 | *(47.0)* |
| PBT | 1,408 | 1,636 | *(13.9)* | 1,368 | *2.9* |
| Tax | 364 | 434 | *(16.1)* | 318 | *14.5* |
| Minority interest | | | | | |
| Adjusted net profit | 1,356 | 1,202 | *12.9* | 1,050 | *29.2* |
| Extraordinary items | -313 | 0 | | 0 | |
| **Reported net profit** | **1,044** | **1,202** | ***(13.2)*** | **1050** | ***n.m*** |
| **Recurring EPS (Rs)** | **3.8** | **4.3** | ***(13.2)*** | **3.8** | ***n.m*** |

| **As % of net revenue** | | | | | |
|---|---|---|---|---|---|
| Gross profit | 10.0 | 15.0 | | 14.3 | |
| SG&A | 3.5 | 6.9 | | 8.5 | |
| EBITDA | 6.5 | 8.1 | | 5.8 | |
| EBIT | 5.6 | 6.9 | | 4.6 | |
| Reported net profit | 3.4 | 5.7 | | 3.7 | |
| Tax rate | 34.9 | 36.1 | | 30.3 | |

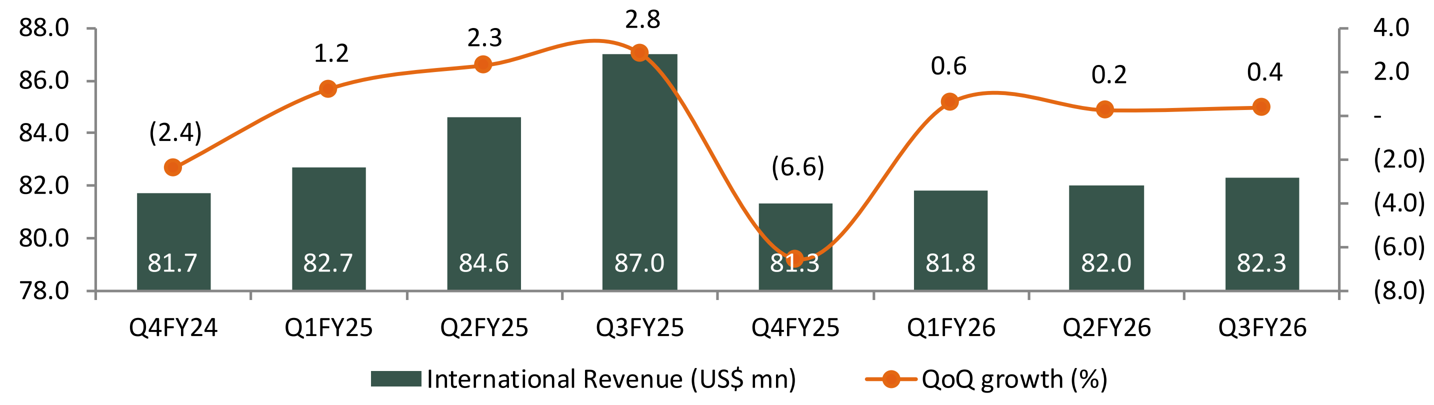
*Source: Company; IDBI Capital Research*

**Exhibit 2: Large client metrics**

| Year-end: March | Q3FY24 | Q4FY24 | Q1FY25 | Q2FY25 | Q3FY25 | Q4FY25 | Q1FY26 | Q2FY26 | Q3FY26 |
|---|---|---|---|---|---|---|---|---|---|
| Top 10 | 56 | 52 | 50 | 63 | 66 | 61 | 56 | 53 | 55 |
| Top 20 | 69 | 61 | 60 | 77 | 78 | 73 | 73 | 70 | 71 |
| Top 10-20 | 13 | 9 | 10 | 14 | 12 | 12 | 17 | 17 | 16 |
| Non top 20 | 31 | 39 | 40 | 23 | 22 | 27 | 27 | 30 | 29 |

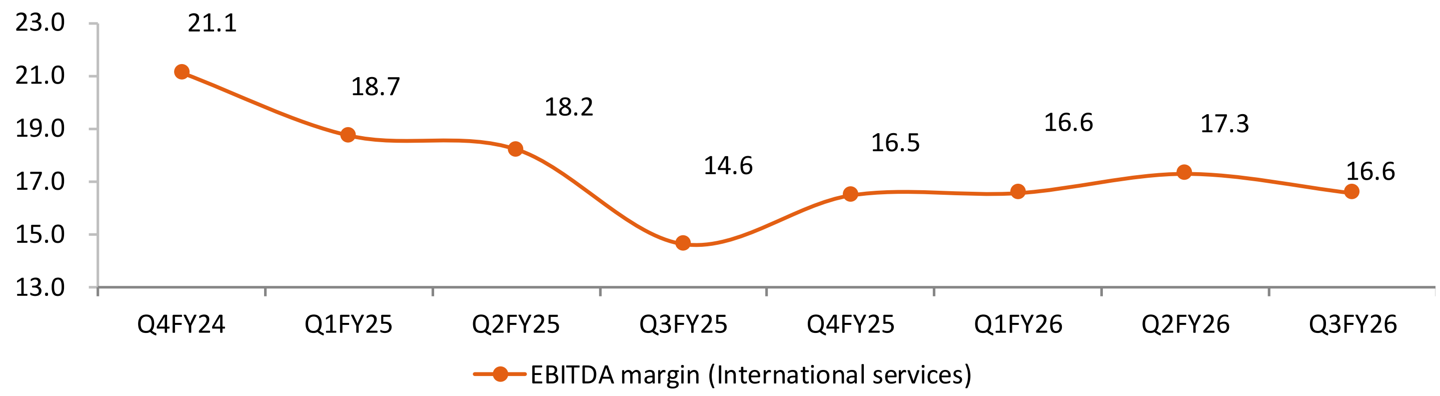
*Source: Company; IDBI Capital Research*

**Exhibit 3: Q3FY26 International revenue stayed flat at +0.4% QoQ to USD 82.3mn**



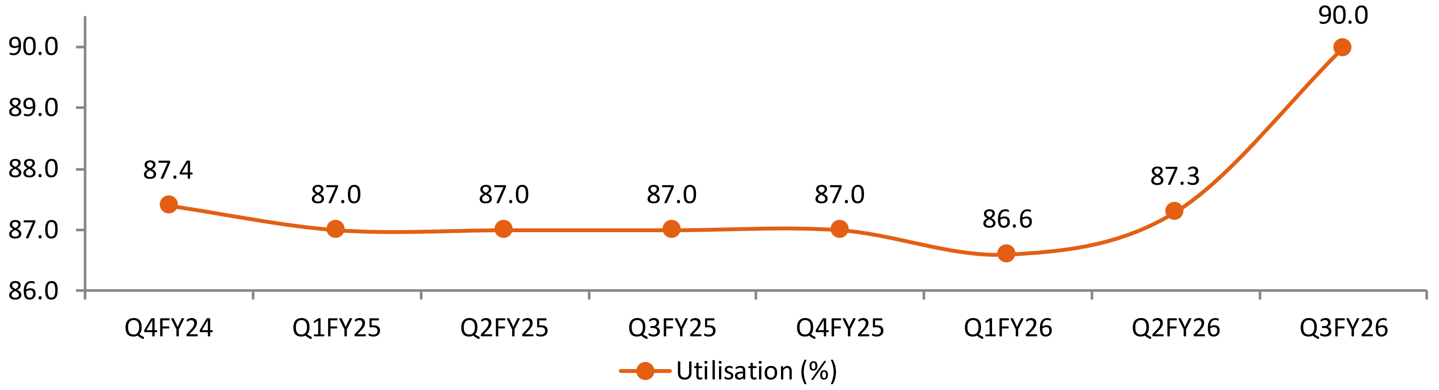

*Source: Company; IDBI Capital Research*

**Exhibit 4: Q3Y26 International services EBITDA margin contracted by ~70 bps to 16.6%**



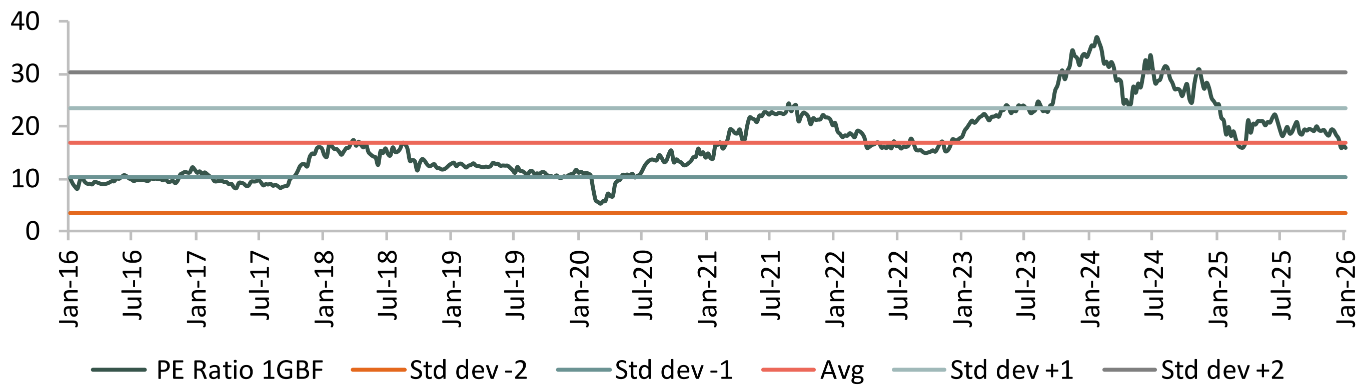

*Source: Company; IDBI Capital Research*

**Exhibit 5: Utilization (*International Services)* increased to 90%**




*Source: Company; IDBI Capital Research*

**Exhibit 6: One-year forward PER trend**




*Source: Company; IDBI Capital Research*

## Financial Summary

**Profit & Loss Account** (Rs mn)

| Year-end: March | FY22 | FY23 | FY24 | FY25 | FY26E | FY27E |
|---|---|---|---|---|---|---|
| **Net sales** | **55,534** | **74,491** | **86,131** | **1,01,703** | **1,06,312** | **1,16,360** |
| *Change (yoy, %)* | *31.3* | *34.1* | *15.6* | *18.1* | *4.5* | *9.5* |
| Operating expenses | (50,896) | (68,450) | (78,856) | (94,676) | (99,255) | (1,08,273) |
| **EBITDA** | **4,638** | **6,041** | **7,274** | **7,027** | **7,058** | **8,087** |
| *Change (yoy, %)* | *22.3* | *30.3* | *20.4* | *(3.4)* | *0.4* | *14.6* |
| *Margin (%)* | *8.4* | *8.1* | *8.4* | *6.9* | *6.6* | *7.0* |
| Depreciation | (473) | (591) | (1,319) | (1,215) | (1,156) | (1,277) |
| **EBIT** | **4,165** | **5,450** | **5,955** | **5,812** | **5,901** | **6,810** |
| Interest paid | (180) | (185) | (850) | (653) | (426) | 277 |
| Other income | 1,020 | 708 | 1,255 | 708 | 745 | 285 |
| **Pre-tax profit** | **5,004** | **5,973** | **4,614** | **5,867** | **6,220** | **7,372** |
| Tax | (1,239) | (1,454) | (1,529) | (1,490) | (1,526) | (1,779) |
| *Effective tax rate (%)* | *25* | *24* | *33* | *25* | *25* | *24* |
| Minority Interest | - | - | - | - | - | - |
| **Net profit** | **3,765** | **4,519** | **3,085** | **4,377** | **4,694** | **5,594** |
| Exceptional items | - | - | (1,747) | - | - | - |
| **Adjusted net profit** | **3,765** | **4,519** | **4,831** | **4,377** | **4,694** | **5,594** |
| *Change (yoy, %)* | *54.3* | *20.0* | *6.9* | *(9.4)* | *7.2* | *19.2* |
| EPS | 27.2 | 32.6 | 17.2 | 15.6 | 16.7 | 19.9 |
| Dividend per sh | 21.0 | 15.8 | 7.9 | 8.0 | 8.2 | 8.2 |
| *Dividend Payout %* | *77* | *48* | *46* | *51* | *49* | *41* |

**Balance Sheet** (Rs mn)

| Year-end: March | FY22 | FY23 | FY24 | FY25 | FY26E | FY27E |
|---|---|---|---|---|---|---|
| **Shareholders' funds** | **10,992** | **13,007** | **14,063** | **17,059** | **19,454** | **22,749** |
| Share capital | 104 | 139 | 278 | 278 | 278 | 278 |
| Reserves & surplus | 10,888 | 12,868 | 13,785 | 16,782 | 19,177 | 22,471 |
| **Total Debt** | **380** | **4,936** | **6,743** | **4,416** | **1,856** | **-** |
| Other liabilities | 1,660 | 9,876 | 2,185 | 1,868 | (1,867) | (1,867) |
| **Curr Liab & prov** | **12,560** | **15,750** | **28,500** | **24,209** | **35,178** | **38,503** |
| Current liabilities | 12,275 | 15,440 | 28,130 | 23,781 | 34,721 | 38,003 |
| Provisions | 285 | 311 | 370 | 428 | 456 | 500 |
| **Total liabilities** | **14,600** | **30,562** | **37,428** | **30,492** | **35,166** | **36,636** |
| **Total equity & liabilities** | **25,592** | **43,569** | **51,491** | **47,552** | **54,621** | **59,384** |
| | | | | | | |
| Net fixed assets | 4,269 | 17,331 | 16,710 | 16,295 | 15,697 | 15,008 |
| Investments | 139 | 140 | 130 | 35 | 35 | 35 |
| Other non-curr assets | 1,741 | 1,948 | 3,896 | 3,905 | 4,572 | 4,923 |
| **Current assets** | **19,443** | **24,151** | **30,756** | **27,317** | **34,317** | **39,418** |
| Inventories | 29 | | 980 | 472 | 1,210 | 1,324 |
| Sundry Debtors | 9,220 | 12,362 | 16,051 | 17,409 | 19,812 | 21,684 |
| Cash and Bank | 9,144 | 9,361 | 10,971 | 6,945 | 9,896 | 12,689 |
| Other current assets | 1,051 | 2,140 | 2,754 | 2,490 | 3,400 | 3,721 |
| **Total assets** | **25,593** | **43,569** | **51,491** | **47,552** | **54,621** | **59,384** |

**Cash Flow Statement** (Rs mn)

| Year-end: March | FY22 | FY23 | FY24 | FY25 | FY26E | FY27E |
|---|---|---|---|---|---|---|
| Pre-tax profit | 5,004 | 5,973 | 4,614 | 5,867 | 6,220 | 7,372 |
| Depreciation | (473) | (591) | (1,319) | (1,215) | (1,156) | (1,277) |
| Tax paid | (1,311) | (1,193) | (2,413) | (1,461) | (1,526) | (1,779) |
| Chg in working capital | 973 | (212) | 8,369 | (5,142) | 7,830 | 1,338 |
| Other operating activities | 1,788 | 6,772 | (9,321) | (5,459) | (4,853) | (1,296) |
| **Cash flow from operations (a)** | **6,927** | **11,932** | **2,568** | **(4,980)** | **8,827** | **6,913** |
| | | | | | | |
| Capital expenditure | (1,505) | (13,653) | (698) | (800) | (558) | (588) |
| Chg in investments | (33) | (1) | 10 | 95 | - | - |
| Other investing activities | - | - | - | - | - | - |
| **Cash flow from investing (b)** | **(2,332)** | **(14,264)** | **(952)** | **(835)** | **(558)** | **(588)** |
| | | | | | | |
| Equity raised/(repaid) | - | 35 | 139 | 0 | - | - |
| Debt raised/(repaid) | (517) | 4,556 | 1,807 | (2,327) | (2,560) | (1,856) |
| Dividend (incl. tax) | (2,917) | (2,185) | (2,215) | (2,243) | (2,299) | (2,299) |
| Chg in monorities | - | - | - | - | - | - |
| Other financing activities | - | - | - | - | - | - |
| **Cash flow from financing (c)** | **(3,435)** | **2,406** | **(269)** | **(4,571)** | **(4,859)** | **(4,155)** |
| | | | | | | |
| **Net chg in cash (a+b+c)** | **1,161** | **73** | **1,347** | **(10,386)** | **3,410** | **2,170** |

### Financial Ratios

| Year-end: March | FY22 | FY23 | FY24 | FY25 | FY26E | FY27E |
|---|---|---|---|---|---|---|
| Book Value (Rs) | 79.3 | 93.8 | 50.2 | 60.8 | 69.4 | 81.1 |
| *Adj EPS (Rs)* | *27.2* | *32.6* | *17.2* | *15.6* | *16.7* | *19.9* |
| *Adj EPS growth (%)* | *15.6* | *20.0* | *(47.1)* | *(9.4)* | *7.2* | *19.2* |
| *EBITDA margin (%)* | *8.4* | *8.1* | *8.4* | *6.9* | *6.6* | *7.0* |
| *Pre-tax margin (%)* | *9.0* | *8.0* | *5.4* | *5.8* | *5.9* | *6.3* |
| *Net Debt/Equity (x)* | *(0.8)* | *(0.3)* | *(0.3)* | *(0.1)* | *(0.4)* | *(0.6)* |
| *ROCE (%)* | *34.7* | *26.7* | *23.4* | *25.1* | *27.6* | *33.8* |
| *ROE (%)* | *37.6* | *37.7* | *35.7* | *28.1* | *25.7* | *26.5* |
| **DuPont Analysis** | | | | | | |
| Asset turnover (x) | 2.5 | 2.2 | 1.8 | 2.1 | 2.1 | 2.0 |
| Leverage factor (x) | 2.2 | 2.9 | 3.5 | 3.2 | 2.8 | 2.7 |
| *Net margin (%)* | *6.8* | *6.1* | *5.6* | *4.3* | *4.4* | *4.8* |
| **Working Capital & Liquidity ratio** | | | | | | |
| Inventory days | 0 | 1 | 4 | 2 | 4 | 4 |
| Receivable days | 61 | 61 | 68 | 62 | 68 | 68 |
| Payable days | 76 | 69 | 66 | 60 | 64 | 64 |

### Valuations

| Year-end: March | FY22 | FY23 | FY24 | FY25 | FY26E | FY27E |
|---|---|---|---|---|---|---|
| PER (x) | 15.1 | 12.6 | 23.7 | 26.2 | 24.4 | 20.5 |
| Price/Book value (x) | 5.2 | 4.4 | 8.2 | 6.7 | 5.9 | 5.0 |
| EV/Net sales (x) | 0.9 | 0.7 | 1.3 | 1.1 | 1.0 | 0.9 |
| EV/EBITDA (x) | 10.3 | 8.7 | 15.2 | 16.0 | 15.1 | 12.6 |
| *Dividend Yield (%)* | *5.1* | *3.9* | *1.9* | *2.0* | *2.0* | *2.0* |

*Source: Company; IDBI Capital Research*

SAPTARSHI MUKHERJEE

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**Key to Ratings Stocks:**

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

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## Analyst Disclosures

We, Saptarshi Mukherjee, and Shubham Satavase, hereby certify that the views expressed in this report accurately reflect our personal views about the subject companies and / or securities. We also certify that no part of our compensation were, was or would be directly or indirectly related to the specific recommendations or views expressed in this report. Principally, We will be responsible for the preparation of this research report and have taken reasonable care to achieve and maintain independence and objectivity in making any recommendations herein.

## Other Disclosure

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## Most Important Terms and Conditions

1. These terms and conditions, and consent thereon are for the research services provided by the Research Analyst (RA) and RA cannot execute/carry out any trade (purchase/sell transaction) on behalf of, the client. Thus, the clients are advised not to permit RA to execute any trade on their behalf.
2. The fee charged by RA to the client will be subject to the maximum of amount prescribed by SEBI/ Research Analyst Administration and Supervisory Body (RAASB) from time to time (applicable only for Individual and HUF Clients).

   Note:

   2.1. The current fee limit is Rs 1,51,000/- per annum per family of client for all research services of the RA.

   2.2. The fee limit does not include statutory charges.

   2.3. The fee limits do not apply to a non-individual client / accredited investor.
3. RA may charge fees in advance if agreed by the client. Such advance shall not exceed the period stipulated by SEBI; presently it is one quarter. In case of pre-mature termination of the RA services by either the client or the RA, the client shall be entitled to seek refund of proportionate fees only for unexpired period.
4. Fees to RA may be paid by the client through any of the specified modes like cheque, online bank transfer, UPI, etc. Cash payment is not allowed. Optionally the client can make payments through Centralized Fee Collection Mechanism (CeFCoM) managed by BSE Limited (i.e. currently recognized RAASB).
5. The RA is required to abide by the applicable regulations/ circulars/ directions specified by SEBI and RAASB from time to time in relation to disclosure and mitigation of any actual or potential conflict of interest. The RA will endeavor to promptly inform the client of any conflict of interest that may affect the services being rendered to the client.
6. Any assured/guaranteed/fixed returns schemes or any other schemes of similar nature are prohibited by law. No scheme of this nature shall be offered to the client by the RA.
7. The RA cannot guarantee returns, profits, accuracy, or risk-free investments from the use of the RA's research services. All opinions, projections, estimates of the RA are based on the analysis of available data under certain assumptions as of the date of preparation/publication of research report.
8. Any investment made based on recommendations in research reports are subject to market risks, and recommendations do not provide any assurance of returns. There is no recourse to claim any losses incurred on the investments made based on the recommendations in the research report. Any reliance placed on the research report provided by the RA shall be as per the client's own judgement and assessment of the conclusions contained in the research report.
9. The SEBI registration, Enlistment with RAASB, and NISM certification do not guarantee the performance of the RA or assure any returns to the client.
10. For any grievances,

    Step 1: the client should first contact the RA using the details on its website or following contact details:

    (RA to provide details as per 'Grievance Redressal / Escalation Matrix')

    Step 2: If the resolution is unsatisfactory, the client can also lodge grievances through SEBI's SCORES platform at www.scores.sebi.gov.in

    Step 3: The client may also consider the Online Dispute Resolution (ODR) through the Smart ODR portal at https://smartodr.in
11. Clients are required to keep contact details, including email id and mobile number/s updated with the RA at all times.
12. The RA shall never ask for the client's login credentials and OTPs for the client's Trading Account Demat Account and Bank Account. Never share such information with anyone including RA.