

IT Services

Sector Update

Hyperscalers are accelerating aggressively!

Quick Pointers:

- Hyperscalers (AWS, Azure & Google cloud) continue their strong growth momentum, 40% up YoY in 2QCY21 on a high base. (Exhibit 2)
- Deep cloud adoption is critical for achieving exceptional business performance as New technologies, enhanced connectivity and abundant computing power have converged in cloud systems to deliver new business growth and foster innovation.
- We believe stronger cloud adoption/cloud led transformation journey will help to sustain double digit revenue growth momentum in Indian IT Services even after post- Covid era.

Hyperscalers (AWS, Azure, GCS) revenue growth has further accelerated (37%/51%/54% YoY) in 2QCY21 on top of strong growth (29%/47%/43% YoY) in 2QCY20. In a hyper-connected world, cloud and AI can power scalable mass automation. By using enterprise applications on the cloud, business service providers can engage with their geographically dispersed customers in a cost-efficient yet personalized manner. Enterprise SaaS and domain-specific SaaS solutions are key to enterprise hybrid multi-cloud strategy. SaaS provides rich feature sets and faster time-to-market for standardized business processes, with low operational overhead and high reliability.

We believe that cloud led digital transformation opportunity will bring strong double digit growth for IT services in next 3-5 years given 1) public cloud adoption (currently low at 15-20%), expected to go up to 60-70% in next 3-4 years, 2) transformation of entire application landscape for large organizations to take another 3-5 years and 3) creation of innovative business models on top of cloud-based digital core, 4) opportunities arising from regulatory changes, data sovereignty (GDPR, CCPA etc.)- more focus on personalization, customization & decreased latency, 5) reverse migration (from public cloud to hybrid, private cloud).

Indian IT players have a strong collaboration with Hyperscalers & it provides a win-win situation for both as IT services providers help in improving utilization of Hyperscaler's cloud by accelerating client's transformation journey. Companies like TCS, INFY, HCLT, TECHM have developed strong organic cloud platforms & it is yielding outstanding results. Among tier-2 players, we would like to highlight MTCL, LTI, COFO are having strong collaborations across & are expanding aggressively in cloud opportunities.

- **Sustained strong growth for Hyperscalers:** Hyperscalers (AWS / Azure / GCS) continued their strong growth momentum in Q2CY21 at 37%/51%/54% YoY. Bookings also grew at strong rate of 25% for Microsoft led by core annuity sales and higher number of larger long term Azure contracts. AWS also saw increasing number of clients accelerating their journey to cloud with renewed long-term contracts.

August 17, 2021

Exhibit 1: PL Universe

Companies	Rating	CMP (Rs)	TP (Rs)
TCS	BUY	3,473	3,807
Infosys	BUY	1,704	1,847
Wipro	BUY	614	665
HCL Tech	BUY	1,124	1,239
Tech M	BUY	1,368	1,509
L&T Infotech	BUY	4,775	5,416
Mphasis	BUY	2,746	3,348
Mindtree	BUY	2,905	3,450
L&T Tech.	BUY	3,675	4,018
COFORGE	BUY	4,796	5,393
Persistent	BUY	3,114	3,603
Redington India	BUY	343	397
Cyient	BUY	969	1,088
Zensar	BUY	437	424
Sonata Software	BUY	845	927
Teamlease	BUY	4,127	4,716

Source: Company, PL

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The term “hyperscale” refers to scalable cloud computing systems in which a very large number of servers are networked together. The number of servers used at any one time can increase or decrease to respond to changing requirements. This means the network can efficiently handle both large and small volumes of data traffic.

- **Cloud has become the foundation of digital transformation:** Cloud has become even more critical enabler as companies across verticals and geographies are undergoing rapid enterprise wide transformation. Benefits of cloud include scalability, resilience, quick deployment, low upfront capex etc. We believe that the digital transformation opportunity will last for next 3-5 years. Currently in the initial phase enterprises are building a cloud-based foundation that will serve as a resilient, secure and scalable digital core. In subsequent phases, native capabilities of these platforms will be utilized to create innovative new business models and differentiated customer experiences.
- **Surge in cloud adoption translating into strong growth for IT services:** IT services providers help in speeding up cloud transformation journey thereby improving the utilization of cloud capacity subscribed by clients thus translating bookings into revenues for Hyperscaler partners. For every dollar spent by a customer on hyperscaler, IT services provider revenue for cloud migration is between 0.2-0.3 cents. IT services companies aim to maximize their cloud wallet share to 1.5x-2x with broad-based cloud revenue multiplier strategy. This involves providing data modernization, application transformation, digital commerce, platforms etc. services.
- Most of the IT companies have developed a cloud transformation platform to help clients accelerate their client’s cloud journeys. Recently Wipro launched FullStride Cloud Services and committed to invest \$1 Bn over three years to strengthen their cloud capacity. Wipro also partnered with ‘du EITC UAE’ launched multi-cloud platform to deliver multi-cloud management and migration capabilities through this platform. TCS’s Cloud suite, HCL Cloud Smart, LTI’s Mosaic etc. are some other examples of cloud platforms.
- **Infy’s cloud platform “Cobalt”** acts as a force multiplier for cloud-powered enterprise transformation. Cobalt offers over 14,000 cloud assets and over 200 industry cloud solution blueprints. **Infosys ranks 3rd among top 10 hyperscaler cloud service providers’ rankings by HFS research.** Strong capabilities of Cobalt have helped them win the highly competitive mega deal from Daimler and Vanguard. 80% of new deals won by Infy has Cobalt as an important element.
- **Cloud has long runway for growth:** Public cloud adoption is still only 15-20% of total IT workload and can move to 60-70% in next 3-4 years. **As per Infosys survey, 41% (vs 17% in 2020) of companies will be shifting more than 60% of their workload to cloud by 2022.** Amazon’s new CEO says that cloud still accounts for less than 5% of global IT spending. Similarly, Microsoft CEO believes that technology spending which is at 5% of GDP currently will double in the next decade and the process itself has been accelerated.
- **Technology spends of banks continue to remain healthy:** Technology spends of CITI and BOA continued to grow at strong pace of 8.8%/14.5% YoY in 2QCY21. Tech spend of JPM declined by 3.9% YoY but its share of revenue continues to remain healthy at 8.2%. Banks continue to invest in technology to stay relevant for customer and reduce costs. Standard Chartered bank has adopted a multi cloud approach where in significant amount of the bank’s applications - including its core banking and trading systems, as well as virtual banking and banking-as-a- service - will be cloud based by 2025.

Exhibit 2: Sustained strong growth for Hyperscalars in 2QCY21 on top of strong growth in 2QCY20

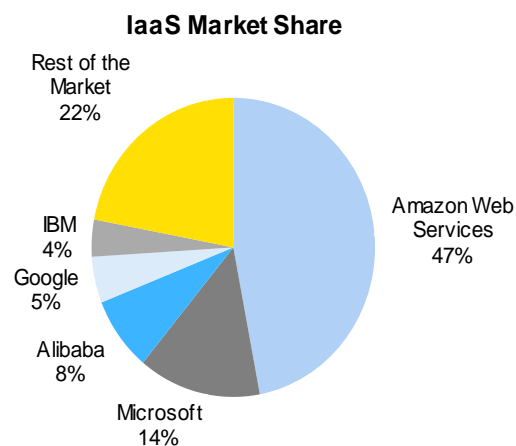
YoY Revenue growth	CY19	1QCY20	2QCY20	3QCY20	4QCY20	CY20	1QCY21	2QCY21
IaaS/ PaaS								
Amazon Web Services	36.5%	32.8%	29.0%	29.0%	28.0%	29.5%	32.1%	37.0%
Microsoft Azure	64.3%	59.0%	47.0%	48.0%	50.0%	51.0%	50.0%	51.0%
Google	59.5%	57.9%	43.2%	44.8%	46.5%	47.5%	45.7%	53.9%
Alibaba	63.7%	49.9%	54.1%	68.8%	50.0%	55.5%	48.3%	42.3%
IBM	13.0%	23.0%	30.0%	19.0%	10.0%	19.7%	21.0%	13.0%
Salesforce.com	46.9%	48.1%	47.8%	24.2%	26.3%	34.8%	18.4%	NA
SaaS								
Microsoft	28.2%	25.0%	19.0%	21.0%	21.0%	21.4%	22.0%	25.0%
Office 365 commercial	42.7%	47.0%	38.0%	38.0%	39.0%	40.4%	45.0%	49.0%
Dynamic 365	25.2%	21.0%	10.0%	16.0%	23.0%	17.6%	25.0%	46.0%
LinkedIn Commercial	3.0%	4.0%	2.0%	4.0%	2.0%	3.0%	4.0%	NA
Oracle	31.3%	23.1%	16.3%	15.3%	17.4%	17.9%	16.5%	21.8%
SAP	13.0%	23.0%	30.0%	19.0%	10.0%	19.7%	21.0%	13.0%
IBM	29.8%	25.8%	23.0%	21.3%	20.3%	22.4%	13.7%	NA
Workday	18.3%	19.3%	16.5%	16.4%	14.6%	16.6%	15.9%	NA
Salesforce.com	18.1%	18.0%	17.0%	17.0%	19.0%	17.8%	17.0%	20.0%
Red Hat	28.2%	25.0%	19.0%	21.0%	21.0%	21.4%	22.0%	25.0%

Source: Company, PL

Exhibit 3: Global public cloud spending to sustain strong growth in CY21-22

(USD mn)	CY20	CY21	CY22
Cloud System Infrastructure Services (IaaS)	59,225	82,023	1,06,800
<i>Growth YoY %</i>		38%	30%
Cloud Application Infrastructure Services (PaaS)	46,335	59,451	71,525
<i>Growth YoY %</i>		28%	20%
Cloud Application Services (SaaS)	1,02,798	1,22,633	1,45,377
<i>Growth YoY %</i>		19%	19%
Cloud Management and Security Services	14,323	16,029	18,006
<i>Growth YoY %</i>		12%	12%

Source: Gartner, PL

Exhibit 4: IaaS Market share


Source: Company, PL

Exhibit 5: Infosys ranks 3rd among top 10 hyperscaler cloud service providers' rankings

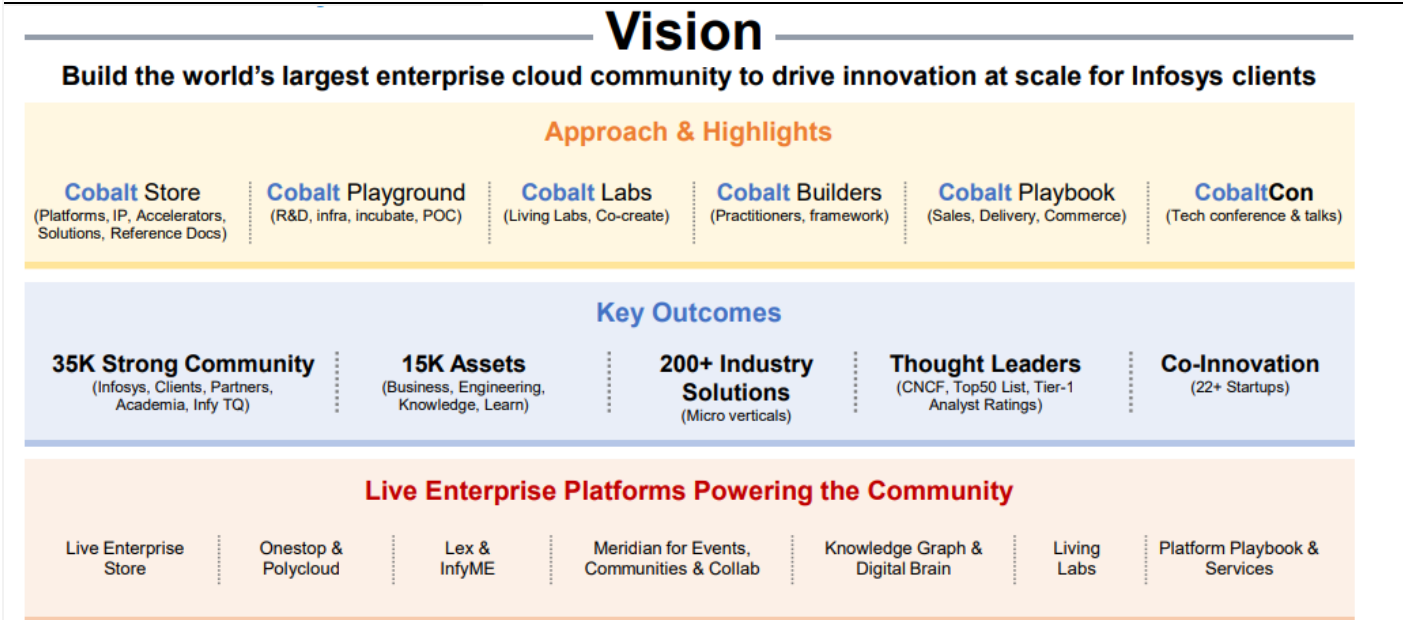
HFS Top 10 hyperscaler cloud service providers rankings

Rank	Overall HFS Top 10 position	Execution					Innovation					Voice of the customer
		Partnerships	Talent and development	Breadth, scale, and reach	Pricing and commercial models	Overall execution	Marketing and thought leadership	IP and accelerators	Investment roadmap	Consulting and professional services	Overall innovation	
#1	accenture	accenture	accenture	IBM	HCL	IBM	accenture	IBM	accenture	accenture	accenture	IBM
#2	IBM	wipro	Infosys	accenture	Cognizant	accenture	IBM	accenture	IBM	IBM	IBM	accenture
#3	Infosys	Infosys	IBM	HCL	wipro	Infosys	Cognizant	Infosys	Infosys	EY	Infosys	Cognizant
#4	Cognizant	IBM	tcs TATA CONSULTANCY SERVICES	Infosys	tcs TATA CONSULTANCY SERVICES	HCL	Infosys	tcs TATA CONSULTANCY SERVICES	wipro	Capgemini	Cognizant	Infosys
#5	HCL	Cognizant	HCL	tcs TATA CONSULTANCY SERVICES	Infosys	tcs TATA CONSULTANCY SERVICES	tcs TATA CONSULTANCY SERVICES	Cognizant	Cognizant	tcs TATA CONSULTANCY SERVICES	tcs TATA CONSULTANCY SERVICES	HCL
#6	wipro	tcs TATA CONSULTANCY SERVICES	Cognizant	DXC technology	Capgemini	wipro	KPMG	wipro	Capgemini	Infosys	Capgemini	KPMG
#7	tcs TATA CONSULTANCY SERVICES	HCL	wipro	wipro	IBM	Cognizant	EY	HCL	HCL	KPMG	wipro	EY
#8	Capgemini	Capgemini	Capgemini	Cognizant	DXC technology	DXC technology	Capgemini	Capgemini	tcs TATA CONSULTANCY SERVICES	wipro	EY	Capgemini
#9	KPMG	DXC technology	EY	Atos	Atos	Capgemini	wipro	DXC technology	KPMG	Cognizant	KPMG	Atos
#10	EY	Atos	Atos	Capgemini	EY	Atos	HCL	KPMG	EY	Atos	HCL	wipro

HFS Research © HFS Research 2021 TOP 10

Source: Company, PL

Exhibit 6: Infosys' Cobalt platform – force multiplier for cloud powered enterprise journeys



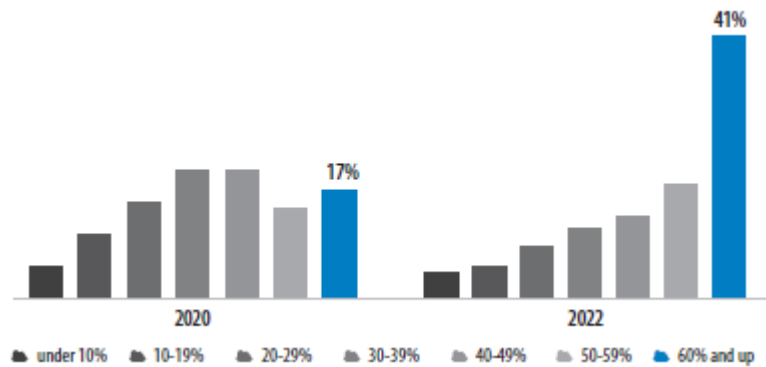
Source: Infosys, PL

Exhibit 7: Cloud capabilities of Tier 1 IT players

Company	Cloud Platform	Details
TCS	TCS Enterprise Cloud	TCS Enterprise Cloud is a scalable and secure cloud platform that provides a broad range of flexible cloud infrastructure options to support dynamic cloud services. It offers data services built on a proven open source stack - supporting big data, analytics, IOT, and streaming data workload requirements for global digital enterprises, while optimizing TCO.
Infosys	Infosys Cobalt	Infosys Cobalt is a set of services, solutions and platforms for enterprises to accelerate their cloud journey. It offers 14,000 cloud assets and over 200 industry cloud solution blueprints.
Wipro	Wipro FullStride Cloud Services	Wipro launched FullStride Cloud Services and announced its commitment to invest \$1 billion in cloud technologies, capabilities, acquisitions and partnerships over the next three years.
HCLT	HCL Cloud Smart	Cloud Smart by HCL Technologies reimagines the cloud to provide an adaptive portfolio of innovative cloud services driven by high-tech automation and a robust partner ecosystem.
TechM	iCOPS platform for Cloud.NxT	TechM launched intelligent cloud operations and subscription management platform, iCOPS, for global enterprises. The platform simplifies and streamlines cloud operations to improve efficiency by leveraging AIOps and analytics with data security and cost optimization.

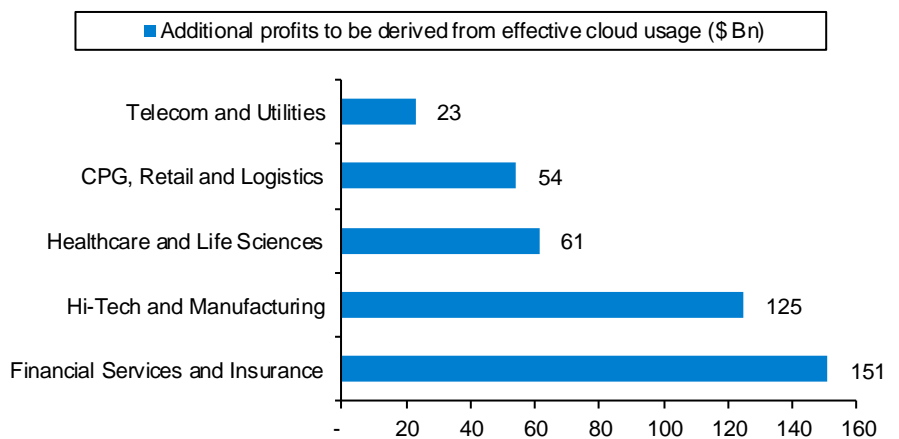
Source: Company, PL

Exhibit 8: 41% companies will have more than 60% tech on cloud by 2022



Source: Infosys, PL

Exhibit 9: Cloud can empower new profit growth of up to \$414 Bn



Source: Infosys, PL

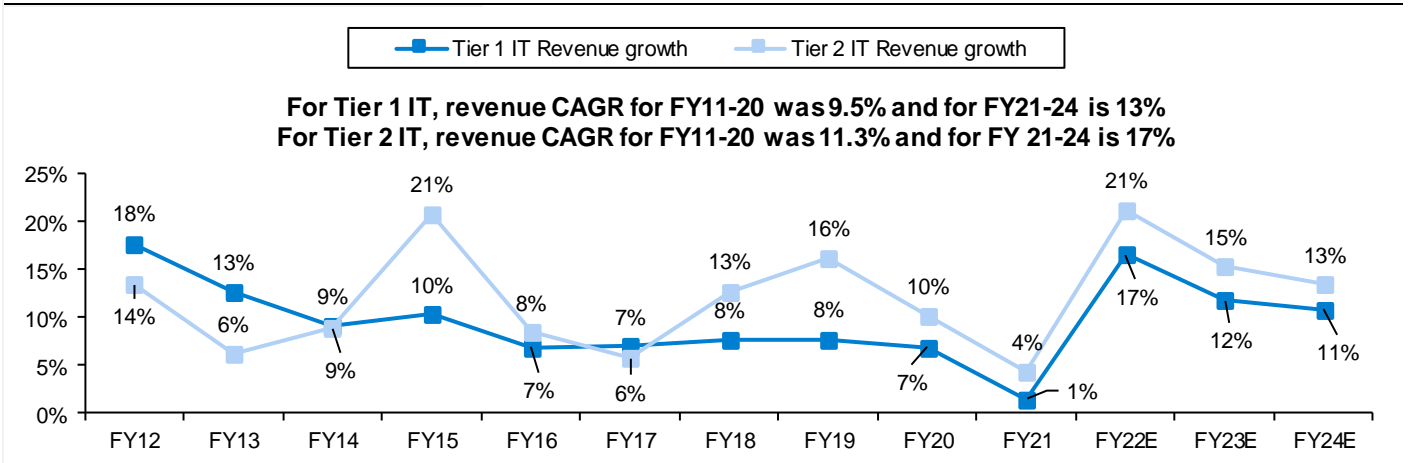
Exhibit 10: Tech spends of US Banks continue to remain healthy

Tech Spends (YoY Growth)	1QCY20	2QCY20	3QCY20	4QCY20	1QCY21	1QCY22
CITI	0.2%	1.0%	6.1%	9.6%	7.5%	8.8%
J.P. Morgan Chase & Co.	9.1%	8.9%	2.8%	0.8%	-2.3%	-3.9%
Goldman Sachs	12.2%	19.0%	20.1%	10.7%	16.8%	7.5%
Bank of America	3.9%	9.3%	14.6%	21.8%	17.9%	14.5%
Wells Fargo					6%	21%

Tech spends as % of revenue	1QCY20	2QCY20	3QCY20	4QCY20	1QCY21	1QCY22
CITI	8.3%	8.8%	10.9%	12.3%	9.6%	10.8%
J.P. Morgan Chase & Co.	8.9%	7.7%	8.8%	8.9%	7.8%	8.2%
Goldman Sachs	3.7%	2.6%	3.2%	2.9%	2.1%	2.4%
Bank of America	5.3%	5.7%	6.6%	7.0%	6.2%	6.7%
Wells Fargo	4.5%	3.8%	4.2%	4.7%	4.7%	4.0%

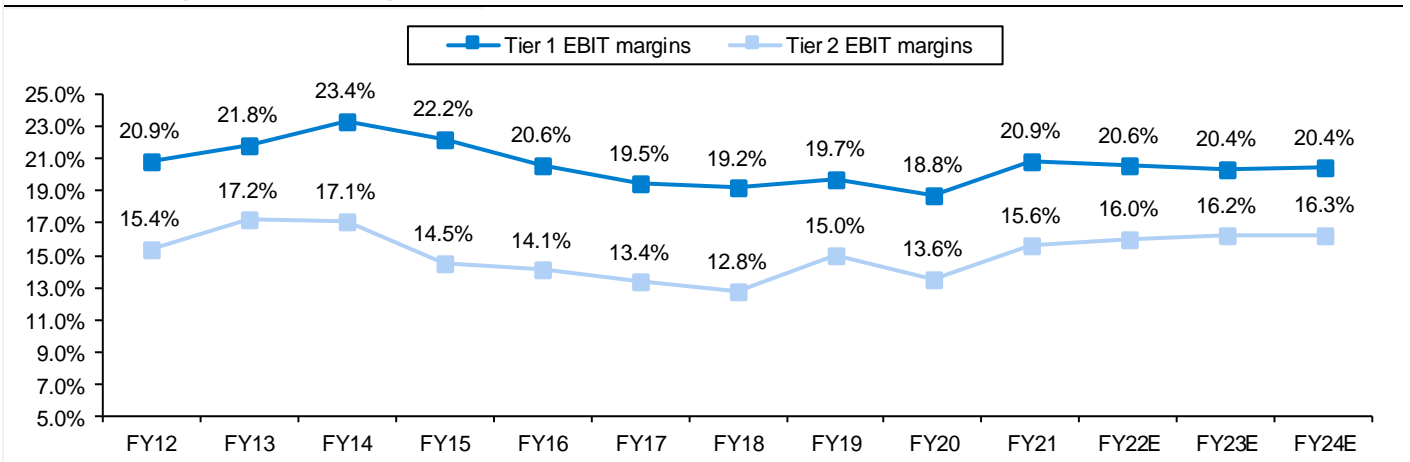
Source: Company, PL

Exhibit 11: Revenue CAGR FY21-24 higher than pre-covid level CAGR by 2-3% for Tier 1 and 4-5% for Tier 2

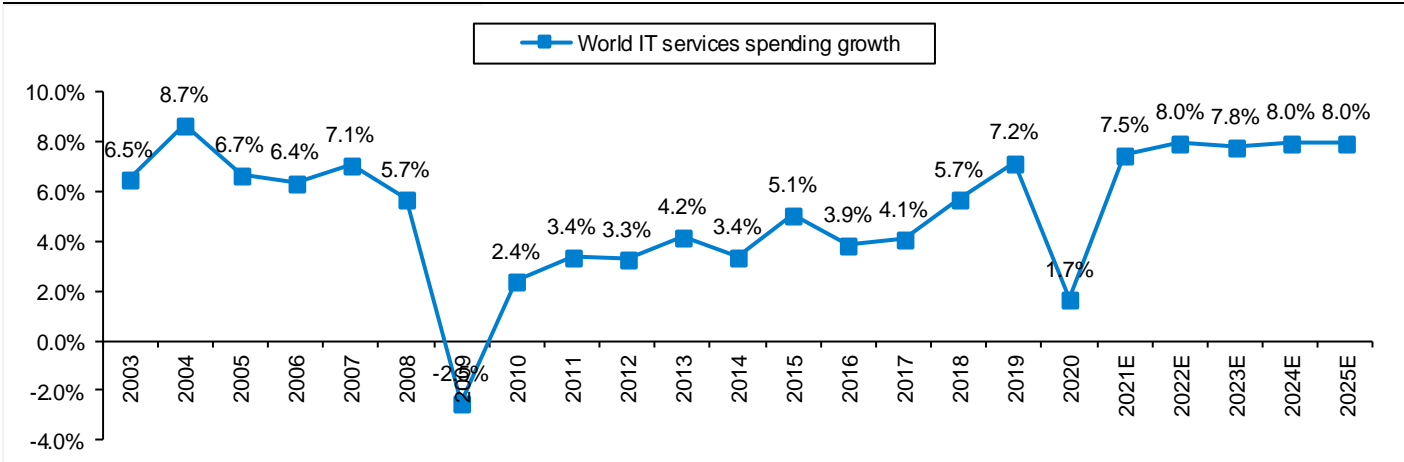


Source: Company, PL, Note: Tier 1 IT consists of TCS, INFY, WIPRO, HCLT, TECHM and Tier 2 IT consists of LTI, MTCL, MPHL, COFORGE, PSYS & LTTS

Exhibit 12: Margins in FY21-24 higher than pre-covid (FY17-20) levels



Source: Company, PL, Note: Tier 1 IT consists of TCS, INFY, WIPRO, HCLT, TECHM and Tier 2 IT consists of LTI, MTCL, MPHL, COFORGE, PSYS & LTTS

Exhibit 13: Indian IT services expected to grow higher by ~4-5% vs worldwide IT services spending


Source: Gartner, PL

Exhibit 14: DFC Valuation & Assumptions

	Risk Free Rate	Equity Risk Premium	Beta	WACC	Terminal Growth rate	TP	CMP	FY21-24 Revenue CAGR	FY24-30 Revenue CAGR	Long term EBIT margin
TCS	6.2%	5.8%	0.737	10.5%	5.5%	3807	3,473	12.6%	9.7%	25.5%
INFY	6.2%	5.8%	0.750	10.6%	5.5%	1847	1,704	13.4%	9.5%	23.0%
WIPRO	6.2%	5.8%	0.814	10.9%	5.5%	665	614	15.6%	9.8%	17.5%
HCLT	6.2%	5.8%	0.861	11.2%	5.5%	1239	1,124	8.3%	7.5%	19.5%
TECHM	6.2%	5.8%	0.769	10.7%	5.5%	1509	1,368	12.9%	8.5%	14.5%
LTI	6.2%	5.8%	0.755	10.6%	6.5%	5416	4,775	15.8%	11.3%	18.0%
LTTS	6.2%	5.7%	0.876	11.2%	7.5%	4018	3,675	16.5%	11.6%	16.5%
MTCL	6.2%	5.8%	0.784	10.7%	6.0%	3450	2,905	16.9%	10.6%	17.5%
MPHL	6.2%	5.8%	0.650	10.0%	6.0%	3348	2,746	15.1%	11.3%	15.5%
Coforge	6.2%	5.8%	0.858	11.2%	6.5%	5393	4,796	22.2%	11.2%	15.0%
Persistent	6.2%	5.8%	0.733	10.5%	6.5%	3603	3,114	18.1%	11.6%	13.5%

Source: Company, PL

Exhibit 15: Valuation Metrics

Companies	USD Revenue Growth				EBIT Margin				EPS				P/E				EV/Sales			
	'21	'22E	'23E	'24E	'21	'22E	'23E	'24E	'21	'22E	'23E	'24E	'21	'22E	'23E	'24E	'21	'22E	'23E	'24E
TCS	0.6%	16.3%	11.7%	10.6%	25.9%	26.1%	25.7%	25.7%	88.1	103.4	118.8	132.9	39.4	33.6	29.2	26.1	7.5	6.3	5.4	4.7
Infosys	6.1%	17.7%	12.0%	10.6%	24.5%	23.7%	23.2%	23.4%	45.9	52.7	61.2	69.9	37.2	32.3	27.8	24.4	6.8	5.7	5.0	4.2
Wipro	-2.4%	24.8%	11.9%	10.5%	19.4%	17.4%	17.7%	18.0%	19.1	21.9	25.2	29.0	32.1	28.0	24.4	21.2	5.0	4.1	3.4	2.9
HCL Tech	2.4%	11.5%	11.8%	10.3%	20.4%	19.6%	19.8%	19.8%	45.8	49.3	57.5	64.1	24.5	22.8	19.5	17.5	3.6	3.2	2.7	2.3
Tech M	-1.6%	13.8%	13.1%	11.8%	14.2%	15.3%	15.0%	15.0%	50.7	63.5	70.9	79.5	27.0	21.5	19.3	17.2	2.8	2.4	2.0	1.7
L&T Infotech	9.5%	18.7%	15.0%	13.6%	19.6%	17.6%	18.5%	18.1%	112.4	120.8	144.9	163.3	42.5	39.5	33.0	29.2	6.4	5.4	4.5	1.8
Mphasis	5.6%	17.6%	14.3%	13.5%	16.1%	16.4%	16.0%	16.1%	65.3	78.6	89.8	104.1	42.1	35.0	30.6	26.4	5.0	4.2	3.6	3.0
Mindtree	-1.1%	22.6%	15.3%	13.0%	17.4%	17.8%	18.0%	18.6%	67.3	86.2	105.7	124.4	43.2	33.7	27.5	23.3	5.7	4.6	3.8	3.2
L&T Tech.	-6.4%	17.2%	16.7%	15.5%	14.5%	17.4%	16.4%	16.0%	63.8	84.1	100.5	109.5	57.6	43.7	36.6	33.6	6.7	5.7	4.7	2.6
COFORGE	5.9%	37.7%	15.7%	14.4%	14.1%	14.2%	15.0%	15.0%	86.8	117.8	148.9	172.7	55.2	40.7	32.2	27.8	5.9	4.3	3.6	3.1
Persistent	12.8%	26.2%	15.2%	13.4%	12.1%	13.1%	13.7%	14.0%	56.4	81.6	98.7	105.0	55.3	38.2	31.6	29.7	5.3	4.2	3.5	2.7
Redington India	6.1%	16.9%	12.5%	9.8%	2.1%	2.2%	2.1%	2.1%	21.2	28.4	31.6	34.6	16.1	12.1	10.8	9.9	0.2	0.1	0.1	0.0
Cyient	-10.9%	13.5%	13.6%	10.4%	10.0%	12.6%	12.8%	12.2%	33.4	45.0	53.1	56.0	29.0	21.5	18.3	17.3	2.2	1.9	1.7	1.3
Zensar	-16.2%	8.9%	17.3%	15.3%	13.9%	13.3%	14.1%	14.5%	17.8	17.4	21.6	25.5	24.6	25.2	20.2	17.1	2.2	2.3	2.0	1.1
Sonata Software	7.7%	31.8%	14.9%	12.8%	8.0%	8.0%	8.8%	8.8%	23.5	34.8	43.2	49.5	36.0	24.3	19.6	17.1	1.9	1.4	1.2	1.0
Teamlease	-10.2%	24.6%	24.2%	18.1%	1.3%	1.8%	2.1%	2.0%	45.5	73.2	106.9	117.7	90.6	56.4	38.6	35.1	1.2	1.0	0.8	0.6

Source: Company, PL

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Coforge	BUY	5,393	4,790
2	Cyient	BUY	1,088	967
3	HCL Technologies	BUY	1,239	1,050
4	Infosys	BUY	1,847	1,650
5	L&T Technology Services	BUY	4,018	3,697
6	Larsen & Toubro Infotech	BUY	5,416	4,763
7	Mindtree	BUY	3,450	2,842
8	Mphasis	BUY	3,348	2,695
9	Persistent Systems	BUY	3,603	3,118
10	Redington (India)	BUY	397	330
11	Sonata Software	BUY	927	842
12	Tata Consultancy Services	BUY	3,807	3,310
13	TeamLease Services	BUY	4,716	3,954
14	Tech Mahindra	BUY	1,509	1,265
15	Wipro	BUY	665	598
16	Zensar Technologies	BUY	424	429

PL's Recommendation Nomenclature

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

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