

IT Services

Tighter budgets and lower discretionary spend key dampeners

Summary

Weak macro, lower discretionary spend and tighter budget to impact revenues of IT companies in Q4FY24E and beyond. Longer tenured deal led by cost efficiency deals, delayed decision making, slower ramp up in deals and slower deal conversion are key commentary by IT companies. This commentary cast doubt of a significant recovery in H2FY25E and overall outlook for FY25E. The only near term trigger is generative AI. For Q4FY24E, in terms of large caps we expect dollar revenue growth in the range of -1.3% - +1.5% QoQ and cross currency tailwind of average 36 bps. Among mid-caps we expect -1.1 to +2% QoQ growth. In terms of margins, we expect it to improve across companies (except Zensar, LTIMindtree & HCL tech) due to absence of furloughs and higher utilization. We expect Coforge, Newgen & Birlasoft to report healthy numbers. Newgen & Sonata are our top picks.

Key Highlights

- **Revenue Outlook:** Despite lower base in Q3, Q4 is more or less is expected to be muted for tier 1. What needs to be watched out is deal trend, budget outlook, discretionary spend comments and FY25E outlook. Among mid-caps, we expect Birlasoft (1.7% QoQ growth), Coforge (2% QoQ) and Newgen (25% YoY growth) to lead the pack. **In terms of guidance we expect Infosys to guide in the range of 4%-5% YoY. We expect Wipro to guide -0.5 to -1% QoQ revenue guidance for Q1FY25E. We expect Cyient and Coforge to guide in the range of 10%-12%.**
- **Margins Outlook:** We expect TCS and Wipro margins to report 52 bps & 40 bps increase due to absence of furloughs & higher utilisation. We expect HCL tech to report 222 bps QoQ dip in margins due to dip in product revenues and wage hike. Among mid-caps we expect Birlasoft, Coforge & Newegen to report margin improvement of 33 bps QoQ, 161 bps QoQ and 81 bps YoY.

India IT Sector: Valuation and Rating

Companies	Rating	CMP (Rs)	TP (Rs)	Upside (%)	Mkt Cap (Rs bn)	P/E (x)	
						FY25E	FY26E
TCS	HOLD	3,882	4,000	3	14,051	27	24
Infosys	BUY	1,483	1,730	17	6,221	21	19
HCL Tech.	HOLD	1,528	1,470	(4)	4,146	24	21
Wipro	BUY	481	535	11	2,514	20	18
Tech Mah.	HOLD	1,236	1,345	9	1,207	21	17
LTIMindtree	SELL	4,900	5,660	16	1,451	27	22
Cyient Ltd	BUY	2,009	2,360	17	222	26	22
Zensar Tech.	HOLD	600	605	1	137	20	18
Birlasoft	HOLD	766	785	2	205	29	25
Newgen	BUY	789	1,042	32	110	34	26
Coforge	HOLD	5,566	6,130	10	344	29	24
Sonata Software	BUY	734	915	25	203	32	24

Source: IDBI Capital, Company

Devang Bhatt

Devang.bhatt@idbicapital.com
+91-22-2217 1846

Exhibit: Estimates

(Rs mn)

Company		Mar-24	Dec-23	Mar-23	QoQ (%)	YoY (%)	Comments
TCS	Revenue (US\$ mn)	7,383	7,281	7,195	1.4	2.6	<ul style="list-style-type: none"> ■ We expect QoQ revenue to be up 1% in CC and positive impact of cross currency to the tune of 40 bps. Weak quarter, furloughs, lower discretionary spend and delay in deal ramp up is expected to impact revenues ■ We expect EBIT margin to increase by 52 bps QoQ on account of absence of furloughs and higher utilization ■ Would watch for: 1) Strategy of CEO to drive growth; 2) TCV of deal wins; 3) Deal pipeline conversion trend; 4) hiring & offshoring, 5) outlook on EBIT margin and its sustainability; 6) commentary on long term digital trends; 7) trends in Generative AI; 8) Banking, US & Europe outlook 9) trend in cost take out deals and 10) ACV trend indication 11) Outlook on budget, macro & FY25E
	Revenue (Rs mn)	6,12,784	6,05,830	5,91,620	1.1	3.6	
	EBIT (Rs mn)	1,46,812	1,41,970	1,44,880	3.4	1.3	
	EBIT margin (%)	24%	23%	25%	52 bps	(53 bps)	
	Net profit (Rs mn)	1,15,304	1,10,580	1,13,920	4.3	1.2	
	EPS (Rs)	31.5	30.2	31.1	4.3	1.2	
Infosys	Revenue (US\$ mn)	4,700	4,663	4,554	0.8	3.2	<ul style="list-style-type: none"> ■ We forecast revenue growth to grow by 0.5% CC terms and cross currency tailwind of 27 bps. The increase is mainly led by absence of furloughs, higher working days and higher utilization ■ We expect EBIT margin to increase by 16 bps to 20.7% ■ Would watch for: 1) Ramp up of large deals; 2) Trend in discretionary spends; 3) trends in Generative AI; 4) margin outlook; and 5) outlook on telecom, retail, BFSI & Hi tech verticals 6) Impact on revenues due to leadership changes 7) Outlook on conversion of pipeline and project run offs 8) hiring& utilization outlook 9) Budget trends 10) FY25E guidance
	Revenue (Rs mn)	3,90,077	3,88,210	3,74,410	0.5	4.2	
	EBIT (Rs mn)	80,606	79,610	78,770	1.3	2.3	
	EBIT margin (%)	21%	21%	21%	16 bps	(37 bps)	
	Net profit (Rs mn)	64,520	61,060	61,280	5.7	5.3	
	EPS (Rs)	15.6	14.7	14.77	5.7	5.5	
Wipro	Revenue (US\$ mn)	2,647	2,660	2,823	-0.5	-6.2	<ul style="list-style-type: none"> ■ We expect IT services revenue to contract by 0.9% in CC terms offset by cross currency tailwind of 33 bps. Softness in consulting business, extended furloughs in BFSI & Tech and client specific challenges across geos to impact revenue growth ■ We forecast EBIT margin to improve by 40 bps QoQ due to lower base in last quarter ■ Would watch for: 1) Outlook for Q1FY25E; 2) Outlook for consulting business; 3) Commentary on the large deal wins and its connect with revenue growth; 4) Leadership changes & impact; 5) Commentary on new strategy to turnaround; 6) Commentary across verticals - especially BFSI, Consumer, Hi Tech and Manufacturing business unit 7) Attrition trends 8) M&A and capital allocation 9) Outlook on any other macro challenges.
	Revenue (Rs mn)	2,19,732	2,22,051	2,31,903	-1.0	-5.2	
	EBIT (Rs mn)	33,147	32,603	36,587	1.7	-9.4	
	EBIT margin (%)	15%	15%	16%	40 bps	(69 bps)	
	Net profit (Rs mn)	27,055	26,942	30,745	0.4	-12.0	
	EPS (Rs)	5.2	5.2	5.6	0.4	-7.6	

Company		Mar-24	Dec-23	Mar-23	QoQ (%)	YoY (%)	Comments
HCLT	Revenue (US\$ mn)	3,384	3,415	3,235	-0.9	4.6	<ul style="list-style-type: none"> ■ We expect sequential revenue de-growth of 1.3% in CC terms offset by cross currency tailwind of 43 bps. The dip in revenue is mainly due to 18.5% QoQ decline in product revenues offset by 1% QoQ increase in IT services (mainly led by 1 month of Verizon deal and ramp up of deals won) ■ We expect EBIT margin to decline by 222 bps mainly due to impact of wage hikes and decline in product revenues ■ Would watch for: 1) Outlook on product business 2) Commentary on deal pipeline, especially large deals, pricing 3) hiring trend 4) Margin outlook; 5) M&A plans; 6) tech spends by clients 7) ER&D outlook and its drivers 8) Trend in discretionary spend in ER&D 9) Budget 10) FY25E guidance
	Revenue (Rs mn)	2,80,839	2,84,460	2,66,060	-1.3	5.6	
	EBIT (Rs mn)	49,177	56,150	48,360	-12.4	1.7	
	EBIT margin (%)	18%	20%	18%	(222 bps)	(67 bps)	
	Net profit (Rs mn)	38,107	43,500	39,830	-12.4	-4.3	
	EPS (Rs)	14.1	16.1	14.7	-12.4	-4.3	
TechM	Revenue (US\$ mn)	1,561	1,573	1,668	-0.7	-6.4	<ul style="list-style-type: none"> ■ We expect QoQ revenue to de grow by 1.0% in CC terms offset by positive cross currency of 32 bps. Extended furloughs and broad based weakness across verticals are key drag for revenues ■ We expect EBIT margin to increase by 167 bps QoQ on account of low base. Adjusting for normalized margins, we expect flat margins on QoQ basis ■ Would watch for: 1) Large deal wins; 2) CEO strategy & ways to improve growth 3) Commentary on revival in comms business & growth in enterprise business, 4) 5G trends 5) Restructuring of margin; 6) Outlook on geography 7) M&A and capital allocation 8) trend reversal in margins 9) FY25E outlook
	Revenue (Rs mn)	1,29,600	1,31,013	1,37,182	-1.1	-5.5	
	EBIT (Rs mn)	9,122	7,030	15,303	29.8	-40.4	
	EBIT margin (%)	7%	5%	11%	167 bps	(412 bps)	
	Net profit (Rs mn)	7,590	5,104	11,176	48.7	-32.1	
	EPS (Rs)	8.6	5.8	12.6	48.7	-32.1	
LTIMindtree	Revenue (US\$ mn)	1073	1084	1058	-1.0	1.5	<ul style="list-style-type: none"> ■ We forecast 1.1% QoQ de-growth in CC terms offset by 13 bps cross currency tailwind. Absence of pass through and extended furloughs to impact revenues ■ We expect EBIT margins to decline by 120 bps QoQ on account of revenue decline ■ Would watch for: 1) Order book & large deal trend; 2) Commentary on deal pipeline & its conversion, new logo addition, pricing; 3) Outlook on BFS & discretionary spend revival 5) Outlook for the margins; and 6) Trend in top clients and 7) Outlook on ability to achieve 17-18% margins in near term and long term margin trajectory 8) Commentary on budget 9) trend in discretionary spend
	Revenue (Rs mn)	89,048	90,166	86,910	-1.2	2.5	
	EBIT (Rs mn)	12,614	13,859	14,214	-9.0	-11.3	
	EBIT margin (%)	14%	15%	16%	(120 bps)	(219 bps)	
	Net profit (Rs mn)	10,524	11,689	11,137	-10	-5.5	
	EPS (Rs)	35.6	39.5	37.6	-9.9	-5.5	

Company		Mar-24	Dec-23	Mar-23	QoQ (%)	YoY (%)	Comments
CYIENT	Revenue (US\$ mn)	225	219	213	3.0	5.8	<ul style="list-style-type: none"> ■ We expect revenue to grow by 3.0% QoQ mainly led by 10% QoQ growth in DLM. Growth of services revenue is expected to be up 1.5% QoQ. In terms of verticals, transportation, automotive and sustainability to drive growth. We expect Services revenue for full year to be at lower end of guided range ■ We forecast EBIT margin to decline marginally on QoQ basis led by wage hike and de-growth in consulting revenues ■ Would watch for: 1) Outlook on verticals like Aerospace and Communications, Transportation and ENU; 2) FY25E guidance; 3) Outlook on EBIT margin; 4) Outlook on attrition; 5) M&A6) New growth verticals outlook 7) Order book trend
	Revenue (Rs mn)	18,744	18,215	17,514	2.9	7.0	
	EBIT (Rs mn)	2,626	2,600	2,494	1.0	5.3	
	EBIT margin (%)	14%	14%	14%	(26 bps)	(23 bps)	
	Net profit (Rs mn)	1,909	1857	1,760	2.8	8.4	
	EPS (Rs)	17.4	16.9	16.0	2.8	8.4	
Zensar	Revenue (US\$ mn)	147	145	148	1.7	-0.2	<ul style="list-style-type: none"> ■ We forecast revenue to increase by 1.5% QoQ in CC terms further pushed by 18 bps increase in cross currency tailwind. We expect revenue growth to be driven by BFSI and Consumer offset by Hi Tech ■ We forecast EBIT margin to decline by 82 bps QoQ to 13.8% ■ Would watch for: 1) Comments on expected turnaround in the company; 2) Outlook on the BFSI, manufacturing, Hi tech & retail given the global challenges; 3) Deal pipeline 4) Large deal wins 5) New logo addition and client mining trend 6) attrition trends 7) Order book trend 8) Outlook on EBIT margin 9) Deal decision making, pipeline conversion and outlook on budget
	Revenue (Rs mn)	12,214	12,041	12,127	1.4	0.7	
	EBIT (Rs mn)	1689	1764	1407	-4.3	20.0	
	EBIT margin (%)	14%	15%	12%	(82 bps)	223 bps	
	Net profit (Rs mn)	1,514	1,617	1,192	-6.4	27.0	
	EPS (Rs)	6.7	7.1	5.3	-6.4	26.8	
Birlasoft	Revenue (US\$ mn)	164	161	149	1.8	10.1	<ul style="list-style-type: none"> ■ Revenue is expected to record growth of 1.7% QoQ in CC terms due to tailwinds in manufacturing and insurance. ■ EBIT margins are expected to be up 33 bps QoQ mainly led by absence of furloughs ■ Would watch for: 1) Outlook on top clients; 2) Deal pipeline 3) Large deal wins 4) new logo addition and client mining trend 5) Outlook on EBIT margin; 6) outlook on BFSI, manufacturing & hitech; 7) commentary on client related issues; 8) outlook on Europe and 9) Order book trend 10) trend in ERP
	Revenue (Rs mn)	13,629	13,430	12,264	1.5	11.1	
	EBIT (Rs mn)	2,007	1,932	1,460	3.8	37.4	
	EBIT margin (%)	15%	14%	12%	33 bps	282 bps	
	Net profit (Rs mn)	1,612	1,611	1,122	0.1	43.7	
	EPS (Rs)	5.75	5.73	4.02	0.4	43.1	

Company		Mar-24	Dec-23	Mar-23	QoQ (%)	YoY (%)	Comments
Newgen	Revenue (Rs mn)	3,802	3,237	3,051	17.5	24.6	<ul style="list-style-type: none"> ■ We forecast revenue to grow by 25% YoY & 17% QoQ mainly led by higher license sale and implementation revenues ■ We forecast EBIT margin to expand by 81 bps YoY to 30% mainly led by healthy revenue growth ■ Would watch for: 1) New logo additions; 2) Outlook on SaaS revenue growth; 3) Commentary on GSI deals 4) Outlook on EBIT margin; 5) outlook on the mature market penetration 6) Annuity trends 7) SAAS trends 8) Geo wise growth trends 9) FY25E outlook & deal wins trajectory
	EBIT (Rs mn)	1,149	701	897	63.8	28.1	
	EBIT margin (%)	30%	22%	29%	853 bps	81 bps	
	Net profit (Rs mn)	951	683	786	39.1	20.9	
	EPS (Rs)	6.81	4.90	5.65	39.1	20.6	
Coforge	Revenue (US\$ mn)	288.5	282	264	2.3	9.1	<ul style="list-style-type: none"> ■ We forecast revenue to grow by 2.0% QoQ in CC terms and 30 bps of cross currency tailwind. We expect the company to be at the lower end of the guidance for FY24E. ■ We forecast EBIT margin to improve by 161 bps mainly led by operating efficiency ■ Would watch for: 1) Trend in discretionary spend 2) New logo addition and client mining trend 3) Outlook on growth & EBIT margin; 4) outlook on BFS vertical due to macro challenges; 5) Outlook on top clients ; 6) Deal pipeline conversion; 7) outlook on TTH and 8) Large deal wins 9) Outlook on order book 10) Budget trend and FY25E guidance
	Revenue (Rs mn)	23,942	23,233	21,700	3.1	10.3	
	EBIT (Rs mn)	3,686	3,201	3,359	15.2	9.7	
	EBIT margin (%)	15%	14%	16%	161 bps	(08 bps)	
	Net profit (Rs mn)	2,600	2,380	2,474	9.3	5.1	
	EPS (Rs)	41.7	38.1	39.8	9.3	4.8	
Sonata Software	Revenue (US\$ mn)	84.5	83.7	65.8	1.0	28.5	<ul style="list-style-type: none"> ■ We forecast Services revenue to grow by 1.0% QoQ. A subdued quarter compared to previous growth due to seasonality in Quant and decline in base business ■ We forecast EBIT margin to be flat QoQ ■ Would watch for: 1) Large deal wins; 2) CEO strategy & ways to improve growth 3) Outlook on services margins 4) Deal pipeline 5) new logo addition and client mining trend 6) BFSi and Healthcare trend 7) outlook on TTH 8) deal pipeline delay 9) FY25E outlook and budget trend
	Revenue (Rs mn)	22,234	24,934	19,135	-10.8	16.2	
	EBIT (Rs mn)	1,612	1,740	1,327	-7.4	21.5	
	EBIT margin (%)	7%	7%	7%	27 bps	32 bps	
	Net profit (Rs mn)	1,192	1,285	1,138	-7.3	4.8	
	EPS (Rs)	4.3	4.6	4.1	-7.2	4.8	

Source: IDBI Capital Research; Note: data for EBIT Margin YOY and QOQ is in bps.

Exhibit: Stock price performance

Change (%)	1-mnth	3-mnth	6-mnth	1-yr
SENSEX	0.0%	2.7%	12.5%	24.9%
BSE IT	-6.8%	-0.3%	10.1%	25.7%
TCS	-5.4%	2.7%	8.3%	21.5%
INFO	-10.4%	-3.2%	1.5%	5.2%
WPRO	-7.9%	2.6%	18.3%	30.8%
HCLT	-6.3%	4.9%	24.8%	40.4%
TECHM	-2.4%	-2.8%	3.1%	12.6%
LTIM	-7.5%	-20.3%	-6.3%	3.4%
CYL	-1.2%	-13.0%	19.6%	101.9%
ZENT	10.0%	2.3%	12.8%	118.7%
BSOFT	-2.5%	11.7%	49.5%	187.8%
NEWGEN	-5.8%	1.0%	79.4%	259.3%
COFORGE	-14.8%	-8.2%	6.5%	44.0%
SONATA SOFTWARE	-12.1%	1.8%	39.5%	68.2%

Source: Bloomberg

Exhibit: Cross-currency movement trend

Currency	Details	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24
USD/INR	Average	77.2	79.8	82.2	82.3	82.2	82.7	83.3	83.0
	QoQ	2.7	3	3	0	(0)	1	1	(0)
	Closing	79.0	81.9	82.9	82.2	82.0	83.0	83.2	83.4
	QoQ	3.9	4	1	(1)	(0)	1	0	0
GBP/USD	Average	1.3	1.2	1.2	1.2	1.3	1.3	1.2	1.3
	QoQ	(6.1)	(6)	(0)	3	3	1	(2)	2
	Closing	1.2	1.1	1.2	1.2	1.3	1.2	1.3	1.3
	QoQ	(7.0)	(11)	10	2	3	(4)	4	(1)
EUR/USD	Average	1.1	1.0	1.0	1.1	1.1	1.1	1.1	1.1
	QoQ	(5.5)	(5)	1	5	2	(0)	(1)	1
	Closing	1.1	1.0	1.1	1.1	1.1	1.1	1.1	1.1
	QoQ	(5.4)	(7)	9	2	1	(3)	5	(3)
AUD/USD	Average	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.7
	QoQ	(0.6)	(5)	(4)	4	(2)	(2)	(1)	1
	Closing	0.7	0.7	0.7	0.7	0.7	0.6	0.7	0.7
	QoQ	(11.1)	(2)	3	(1)	(1)	(3)	6	(5)

Source: Bloomberg



Notes

Dealing	(91-22) 6836 1111	dealing@idbicapital.com
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IDBI Capital Markets & Securities Ltd.**Equity Research Desk**

6th Floor, IDBI Tower, WTC Complex, Cuffe Parade, Colaba, Mumbai – 400 005. Phones: (91-22) 4069 1700; Fax: (91-22) 2215 1787; Email: info@idbicapital.com

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Compliance Officer: Mr. Pushkar Vartak;; Email: compliance@idbicapital.com; Telephone: (91-22) 4069 1907

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