

IT Services

Remain selective due to macro challenges

Summary

Q4FY24 results were weak due to slowdown in discretionary spend, elongation of deal cycle and weak macro. Most of the companies are banking on growth in H2FY25E thereby pushing growth expectation to FY26E. Consequently we have cut our Revenue and EPS estimates by 4% & 3% for FY25E in large cap and by 3% & 7% for FY25E in midcaps. Challenges still persist in terms of slow decision making, focus on cost efficiency program and reprioritization of spends. This has led to cooling of stock prices. However, we still remain cautious in the IT sector. We prefer companies where there is valuation comfort and has healthy growth expectation. Hence we prefer Wipro & Infosys in large caps and Newgen, Sonata & Cyient in mid-caps. Key upside risk in the sector is earlier than expected FED interest rate cut which could boost client budgets (although seems difficult).

Key Highlights

- **Revenue outlook:** Infosys guided for 1-3% YoY growth in FY25E vs 1.9% growth FY24. Further, Coforge gave a broad guidance without hard numbers for FY25E, Cyient has tapered growth expectation of double digit growth to high single digit growth and despite HCL Tech's robust Q4 exit the company guided for 3-5% YoY growth in FY25E. This indicates macro challenges persist and the broad reason highlighted for tapered growth expectations are slowdown in discretionary spends, ramp downs and slower conversion. This has led us to build in 3% YoY & 9% YoY for large-caps and 10% YoY & 16% YoY for mid-caps in FY25E & FY26E.
- **Margin outlook:** Q4 witnessed rationalization of sub con cost and higher utilization due to subdued demand expectation. Going forward, we expect utilization, pyramid and lower discretionary expenses to drive IT companies margins. Hence, we expect margins to improve in the range of 37-673 bps over FY24-FY26E. Only aberrations are Zensar (-14 bps) and Sonata (- 14 bps).

India IT Sector: Valuation and Rating

Companies	Rating	CMP (Rs)	TP (Rs)	Upside (%)	Mkt Cap (Rs bn)	FY25E	FY26E	P/E (x)
TCS	HOLD	3,960	4,300	9%	14,328	27	24	
Infosys	BUY	1,440	1,635	14%	5,975	22	20	
HCL Tech.	HOLD	1,320	1,410	7%	3,582	21	19	
Wipro	BUY	456	521	14%	2,383	19	18	
Tech Mah.	HOLD	1,269	1,265	0%	1,240	23	18	
LTIMindtree	HOLD	4,658	5,000	7%	1,380	27	23	
Coforge	HOLD	4,302	5,495	28%	266	27	20	
Cyient	BUY	1,754	2,210	26%	195	23	20	
Birlasoft	BUY	604	780	29%	167	24	20	
Zensar Tech.	HOLD	581	615	6%	132	20	17	
Newgen	BUY	946	1,072	13%	133	40	30	
Sonata	BUY	519	770	48%	145	25	19	

Source: IDBI Capital, Company

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Exhibit 1: Q4FY24 performance of IT companies

Coverage Revenues	Q4FY24					
	US\$	QoQ (%)	YoY (%)	Deal wins	QoQ (%)	YoY (%)
TCS	7,363	1.1	2.3	13,200	63.0	32.0
Infosys	4,564	-2.1	0.2	4,500	38.8	114.3
Wipro	2,665	0.2	-6.1	3,600	-5.3	-12.2
HCL Tech	3,430	0.4	6.0	9,759	406.4	369.2
Tech Mahindra	1,548	-1.6	-7.2	500	31.2	-15.5
LTIM	1,069	-1.3	1.1	na	na	na
Coforge	287	1.7	8.5	774	118.6	157.1
Birlasoft	164	1.6	9.9	107	13.8	-6.1
Zensar	148	2.3	0.4	182	8.7	-6.8
Cyient	224	2.4	5.2	228	-23.3	7.2
Sonata	82	-2.4	24.2	na	na	na
Newgen (Inr mn.)	375	15.9	23.0	na	na	na

Non coverage	US\$	QoQ(%)	YoY(%)
Persistent	311	3.4	13.2
Mastek	94	-0.3	8.6
Happiest Minds	50	1.3	11.1
Mphasis	411	2.1	-0.3
Tata Elxsi (Rs. Mn)	9,059	-0.9	8.1
LTTS	305	5.2	19.6
KPIT	160	7.4	29.2

Source: IDBI Capital, Company

Exhibit 2: Q4FY24 Margin performance of IT companies

Companies	Gross Margin (%)	QoQ ch (bps)	YoY ch (bps)	EBIT Margin (%)	QoQ ch (bps)	YoY ch (bps)
TCS	40.6	29	98	25.9	250	145
Infosys	29.0	-100	-200	20.1	-41	-94
Wipro	29.2	-152	-62	16.0	130	21
HCL Tech	29.6	-161	-139	17.6	-213	-57
Tech Mahindra	23.4	287	-193	7.4	199	-380
LTIM	27.3	-42	-55	14.7	-66	-164
Coforge	34.1	173	2	14.4	66	-104
Birlasoft	43.6	272	311	14.7	34	282
Zensar	30.6	-46	-130	14.6	-7	298
Cyient	31.6	-21	-2,659	14.4	14	17
Sonata	17.0	125	158	5.0	-194	-189
Newgen	55.0	397	140	30.7	901	129

Source: IDBI Capital, company

Exhibit 3: Subcontracting rationalization helped margins in Q4FY24

Large Cap companies	Subcontracting cost (%)	QoQ ch (bps)	YoY ch (bps)
TCS	5	-157	-366
Infosys	13	-61	-141
Wipro	11	-64	-114
HCL Tech	13	-110	-140
Tech Mahindra	14	204	-55

Source: IDBI Capital, company

Exhibit 4: Utilisation and attrition trends

Companies	Utilization (%)	QoQ ch (bps)	YoY ch (bps)	Peak utilization (over 5 Yrs)	Attrition (%)	QoQ ch (bps)	YoY ch (bps)	Lowest attrition (over 5yrs)
TCS	83	0	0	83	13	-80	-760	7
Infosys	84	80	350	89	13	-30	-830	11
Wipro	87	290	520	87	14	0	-500	11
HCL Tech	-			-	12	-40	-710	10
Tech Mahindra	86	-200	0	88	10	0	-500	10
LTIM	87	-50	520	87	14	20	-580	14
Coforge	82	230	20	81	12	-60	-260	10
Birlasoft	86	-80	150	87	12	-20	-970	-
Zensar	84	300	230	84	11	-110	-890	12
Cyient	-			-	17	-100	-830	-
Sonata	87	160	100	91	-	-	-	-

Source: IDBI Capital, company

Exhibit 5: Vertical wise

Vertical wise (%) in term of CC	BFSI			Manufacturing			Retail			Communication			Healthcare & Life-science			Hi-tech			Others		
	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY
TCS	31	-0	-3	9	3	10	16	1	0	7	-0	-5	11	1	2	8	-1	-6	19	4	18
Infosys	26	-7	-8	15	-3	9	14	-4	-3	12	6	4	7	-6	2	9	11	9	16	-1	3
Wipro	34	3	-8	7	-1	-11	19	-0	-7	4	-5	-21	14	2	9	11	-6	-3	12	1	-9
HCL Tech	22	-0	8	20	2	13	9	-5	7	12	19	39	16	-0	-1	12	-3	-9	9	-9	-9
Tech Mahindra	16	4	-5	18	-1	6	8	-10	-4	36	-3	-16	-	-	-	11	0	-4	11	-2	-2
Average	-0	-3		-0	5		-4	-1		3	0		-1	2		0	-2		-1	0	

Source: IDBI Capital, company

Exhibit 6: Geowise

Geo wise (%) in term of CC	USA			Europe			Asia			ROW		
	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY	Q4FY24	QoQ	YoY
TCS	52	-0	-2	31	1	4	15	5	14	2	6	7
Infosys	60	-1	-2	29	-1	6	2	-10	-15	10	-10	2
Wipro	61	0	-4	28	1	-11	-	-	-	11	-2	-7
HCL Tech	65	2	8	29	0	6	-	-	-	6	-7	-14
Tech Mahindra	51	-4	-5	24	0	-11	-	-	-	25	1	-8
Average	-1	-1		0	-1		-1	-0		-2	-2	-4

Source: IDBI Capital, company

Exhibit 7: Concall highlights

Large caps	Region	Vertical	Growth drivers
TCS		Good demand in BFSI within that insurance is doing well, green shoots is seen in consumer business, transportation is growing well,	Growth drivers of transformation deals are digital transformation, cloud migration, sustainability and integration of Gen AI and hyper personalization.
Infosys		BFSI growth in FY25E is expected to be better than FY24. cautiously optimistic outlook in E&U mainly due to cost optimization deals, Manufacturing would see slower growth and could improve with traction in areas like IoT, supply chain, manc manufacturing and Retail is seeing improvement led by cost take out deals and Generative AI.	Strong traction in Generative AI across verticals.
Wipro		Green shoots in BFSI sector and healthcare, E&U & manufacturing is expected to be soft in near term	
HCL Tech			Engineering & Research development spending and outsourcing will continue to grow globally.
Tech M		BFSI practice with strengths in quite a few areas such as core banking, customer experience and insurance platforms, aided by acquisitions	Key markets and service lines to create a sustainable growth engine.
Mid caps			
LTIM		BFSI could see recovery in Q1FY25E on the back of strong deal pipeline, Manufacturing would continue to show the seasonality impact	
Coforge		Growth drivers would be three new verticals: Retail, Hi-tech & Healthcare, recovery in travel could be seen	
Birlasoft		BFSI is doing good; Life-science would still show softness for two more quarters, however expects rebound post the softness	Traction in ERP, infra services and AI/ gen AI
Zensar	BFSI is growing good in US region than UK & South Africa	Hi-tech furloughs have continued and overall it would be under pressure. BFSI is growing good in US region than UK & South Africa and growth is expected in the sector.	
Cyient		Near term challenges in aerospace & communication, new growth verticals to improve growth in FY25E.	Aerospace, sustainability and communication to drive growth.
Sonata		Demand in healthcare & hi-tech to be in good momentum; BFSI and Hi-tech to show flattish to slight growth in near term and emerging to be continue in pressure.	Strong growth from digital based competencies like Managed cloud services and Digital Platformation Services (Microsoft & Open source) and focused verticals like TMT, Healthcare & Life Sciences, Manufacturing, Retail / CPG/ TTH and BFSI.
Newgen	Recovery in APAC region from next year onwards	Trade finance, digital engineering, supply chain solutions have good traction.	Insurance vertical to drive growth and expects major revenue share in next 2 years.

Source: IDBI Capital, company

Exhibit 8: Estimates for IT companies

Coverage	Revenues (US\$)	Growth YoY %					
		FY23	FY24	FY25E	FY26E	FY24	FY25E
TCS	27,927	29,080	31,226	34,568	4.1	7.4	10.7
Infosys	18,212	18,562	19,253	20,983	1.9	3.7	9.0
Wipro	11,160	10,831	10,777	11,495	-2.9	-0.5	6.7
HCL Tech	12,586	13,270	13,820	15,040	5.4	4.1	8.8
Tech Mahindra	6,607	6,277	6,362	6,869	-5.0	1.3	8.0
LTIM	4,106	4,287	4,550	5,105	4.4	6.1	12.2
Coforge	1,002	1,119	1,334	1,664	11.7	19.2	24.8
Birlasoft	595	637	701	813	7.1	10.0	16.0
Zensar	604	592	625	706	-2.0	5.5	13.0
Cyient	746	863	962	1,070	15.6	11.4	11.2
Sonata	241	324	356	429	34.3	10.1	20.4
Newgen (Inr mn.)	974	1,244	1,579	2,017	27.7	26.9	27.7

Source: IDBI Capital, company

Exhibit 9: EBIT margin estimates

Companies	FY23	FY24	FY25E	FY26E	Change (bps) FY24-26
TCS	24.1	24.2	25.8	26.7	251
Infosys	21.1	20.7	22.0	22.0	134
Wipro	14.9	15.1	16.5	16.7	162
HCL Tech	18.2	18.2	19.0	19.4	116
Tech Mahindra	11.4	5.8	10.1	12.5	673
LTIM	16.2	15.7	16.7	17.6	194
Coforge	14.3	12.9	13.4	14.4	145
Birlasoft	12.3	14.2	15.1	15.4	116
Zensar	7.6	15.1	14.8	14.9	-14
Cyient	12.4	14.4	14.6	14.8	37
Sonata	25.1	23.4	22.6	23.3	-14
Newgen	19.3	20.9	21.4	22.4	149

Source: IDBI Capital, company

Exhibit 10: Stock price performance

Change (%)	1-mnth	3-mnth	6-mnth	1-yr
SENSEX	-3.1%	1.4%	11.6%	16.9%
BSEIT	-5.3%	-12.1%	8.8%	21.6%
TCS	0.3%	-4.2%	18.8%	20.5%
INFOSYS	-3.7%	-14.9%	5.2%	14.0%
WIPRO	-4.2%	-6.7%	20.2%	18.8%
HCL TECH	-14.3%	-19.2%	5.1%	22.4%
TECH MAHINDRA	1.4%	-3.1%	11.5%	21.3%
LTIM	-4.8%	-14.1%	-11.5%	1.4%
COFORGE	-24.7%	-34.9%	-16.3%	4.3%
BIRLASOFT	-17.1%	-27.9%	3.6%	96.8%
ZENSAR	-4.3%	-0.3%	20.7%	90.8%
CYIENT	-15.7%	-20.0%	5.6%	39.5%
SONATA	-31.6%	-35.0%	-21.3%	21.8%
NEWGEN	13.8%	17.3%	57.0%	236.9%

Source: Bloomberg



Notes

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