

Industry	TECHNOLOGY
Bloomberg	TELX IN
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Recovery in Automotive gives positive hopes while postponed wage hike to pressurize margins

2QFY20 Result update

Result highlights

Revenue in line , PAT impacted by one off

- ❑ TATAELXSI reported mixed set of numbers in 2QFY20 result. Revenue came at Rs 386crore (in line with our estimates of Rs378crore), a growth of 6.7% mainly led by improvement in top client while Pat for the quarter stood at Rs 49.8crore (below estimates), a growth of 2.1%QoQ impacted by margin miss.
- ❑ PBT for the quarter was at Rs70.4 crore ,a muted growth of 0.3%QoQ. Margin declined 120bps to18.3% owing to onetime provision provided for retired benefit for ex MD (Rs21.60crore).Ex one off, margin was 23.9% which is within the guided range of 22% to 24%.
- ❑ Utilization for the quarter was 71% vs. 55% last quarter.
- ❑ IP revenue remained muted and contributed below 5%.However it helped the company to wins deals.
- ❑ Top client (JLR) revenue improved 4.1%QoQ during the quarter.

Growth Trajectory back with improvement in transportation industry

The company has seen tepid growth in last few quarters due to challenges in largest verticals .However 2QFY20 saw improvement in EPD business(largest business) with recovery in Transportation segment .Transportation during the quarter grew 9%QoQ mainly led by improvement in JLR account (largest account in Automotive segment) and some deal wins. Also diversification within this segment in adjacent verticals like aero, rail and off road vehicle has resulted in 4% growth coming from these segment .Other segment in EPD business like Broadcast and Media also saw steady growth of 4.3%QoQ While medical which posted a strong growth in 1QFY20, reported a blip in the quarter due to delays in paperwork completion of deal wins.

Industry trends still remained sluggish

Despite the strong growth came in 2QFY20 , the company is seeing trend of smaller deals picking up however large deals are taking 2 to 3quarters to close. Some deal which was expected to sign in 1QFY20 got pushed to 2QFY20 and further now to 3QFY20.Thus the management believe demand is there but still sees sluggish growth in large deal ramp ups in 3QFY20.

Double digit growth guidance for FY20 while margins to see wage hike in 3Q

The company expects to deliver double digit growth in FY20 as the deal pipeline remains healthy(earlier was 15% growth in beginning of the year) but still sees delay in large deal ramp ups .Margin will see furlough , wage hike impact in 3QFY20 However with revenue growth and cost optimization expects to aspire to achieve22% to 24% PBT margins.

View and Valuation

Tata Elxsi is an integrated design and engineering services company with Automotive, Broadcast & Communication being key verticals. However in last few quarters, the company saw tepid growth due to delay in project particularly in the JLR portfolio impacting its Automotive segment. Going forwards, we expect the revenue growth to improve in H2 mainly owing to stability in JLR account and robust growth coming in broadcast (~41% in EPD business)& medical segment(6.7% in EPD business).However as delay in decision making are still impacting large deal wins , thus we expect Automotive to grow however to get back to normal growth will require some more quarters .On margin front wage hike and furlough will impact the margin in near term. Post result we have reduced revenue and PAT estimates for FY20 by 1%/4% due to margin miss .Thus we largely maintain Neutral stance on the stock with target price of Rs 742 .

Key Risks to our rating and target

- ❑ Prolonged weakness in transportation verticals
- ❑ Slow down in order booking.

RATING	NEUTRAL
CMP	702
Price Target	742
Potential Upside	6%

Rating Change	↔
Estimate Change	↓
Target Change	↔

Stock Info

52wk Range H/L	1089/593
Mkt Capital (Rs Cr)	4372
Free float (%)	55%
Avg. Vol 1M (000)	86
No. of Shares (Crs)	6
Promoters Pledged (Crs)	0

Fig in Rs cr

FINANCIAL	FY19	FY20E	FY21E
Net Sales	1,597	1,605	1,855
EBITDA	415	335	420
EBIT	390	296	381
PAT	290	245	308
EPS (Rs)	47	39	49
EPS	21%	-15%	26%
ROE (%)	35	24	25
ROCE (%)	46	29	31
BV	151	177	214
P/B (X)	6	4	3
P/E (x)	21	18	14

Research Analyst

NIHARIKA OJHA

niharika@narnolia.com
+91-22-62701230

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2QFY20 Results

Mixed performance

Financials	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	YoY %	QoQ%	Fig in Rs cr		
								FY18	FY19	YoY %
Net Sales	403	407	405	362	386	-4.2%	6.7%	1386.26	1596.93	15.2%
Other Income	23	(3)	15	12	12	-46.8%	2.3%	43	43	0.5%
COGS	23	23	30	15	23	2.3%	51.3%	77	99	28.0%
Employee Exp	214	218	214	218	237	10.6%	9.0%	749	843	12.5%
Other Expenses	59	62	62	59	55	-6.4%	-6.3%	214	240	12.2%
EBITDA	107	103	98	70	70	-34.1%	0.7%	346	415	20.0%
Depreciation	6	6	7	10	11	80.3%	4.9%	25	25	-1.0%
EBIT	101	97	92	59	59	-41.0%	0.0%	321	390	21.6%
Interest	-	-	-	1	1		2.6%	-	-	
PBT	124	94	107	70	70	-43.2%	0.3%	364	433	19.1%
Tax	42	28	35	21	21	-50.6%	-3.6%	124	143	15.8%
PAT	82	66	71	49	50	-39.4%	2.1%	240	290	20.8%

Concall Highlights

- **Back to growth trajectory:** The company managed to improve growth in 2QFY20 from top customer which had impacted the growth in 1QFY20. The company grew 6.7% QoQ primarily volume growth with negligible forex gain. The company has almost makeup the growth as the gap between 2QFY19 and 2QFY20. Volume growth is 1%. Top customer remained constant in volume in 2QFY20.
- **IP revenue:** During the quarter IP revenue remained muted and contributed below 5%. However it helped the company to win deals.
- **Industry Trend:** the company is seeing trend of smaller deals picking up however large deals are taking 2 to 3 quarters to close. Thus the company has seemed some deal in 1QFY20 which got pushed to 2QFY20 and further now to 3QFY20.
- **Growth across regions and market verticals:**
 - **EPD:**
 - In EPD which is largest business for TATAELXSI grew ~5.3% QoQ. Within EPD, transportation grew 9% QoQ led by some good design wins. V2X is where the company is seeing work in autonomous car and expect to grow in coming years
 - Broadcast and Media posted a steady growth of 5% QoQ. The company has large customers in this segment (no 1, 2, 3 media operator are customers). As the operator are going through digital transformation, the company is seeing large opportunities and thus expects to continue to dominate this segment.
 - Medical posted a strong growth in 1QFY20 however reported a blip in the quarter due to delays in paperwork completion of deal wins. However, company sees enough traction in medical vertical and expects in next 3 years to contribute majorly like broadcast (~40% of revenue). 3QFY20 to see growth in medical business.
 - **Design business** which contributes 9.7% of revenue also grew 12.9% QoQ. Design has started to pay dividend for the company. Visualization space has won some significant long term deal on content development side. It is not from entertainment side but more for corporate development thus will bring steadiness and predictability in revenues. Also will bring margin improvement
 - **System integration business (SI)** also grew by 27% although from small base. The large part is reengineering for SI which is being able to focus on software, valued added services and experience centers. Though it has small base however the management expects to start to reengineer that business in stages.
 - **Geography wise,** US market grew 9% QoQ, India grew 18% QoQ and RoW grew about 15% owing to new customer addition and growth in existing accounts. Europe for the company has remained flat predominantly due to bit of forex losses in GBP and Euro. However in CC terms Europe grew 1% QoQ While US grew 7.5% QoQ.
 - **Diversification update:** Despite JLR remained muted for the company, transportation segment improved 9% QoQ due to diversification in other accounts. As announced earlier, the company posted growth in adjacent verticals like aero, rail and off road vehicle. Now 4% revenue growth in transportation came from these segments. Hopefully the company expects to continue to grow this segment.

- **Margin performance:** PBT for The quarter is 17.4%. The decline in margins came due to onetime provision provided for retired benefit for ex MD (Rs21.60crore).Ex one off, margin was 23.1% which is within the guided range of 22% to 24%.Utilization for the quarter was 71% vs. 55% last quarter. Going forward, 3QFY20 will see wage hike as it was postponed from 2QFY20 and also adding new employees during H2.Thus company endeavor will be of 22% to 24% margin range.
- **Deal wins:**
 - Automotive :The company won couple of deals in Automotive segment in electric vehicle space with large Tier 1 supplier in Europe and other deal was won with a startup company .The company also won a large deal again with Tier 1 supplier in Europe On connected car space. The company believe that this deal have the potential to grow significantly over next couple of quarters.
 - Media and entertainment space: The company won a significant deal on OTT side .The investment in OTT space done by the company in past will leverage to wins for deals in this space.The company has good confidence of growth going forward.
 - However in 2QFY20, only 2% deal came from new while majorly came from existing customers but going forward, company expects it to increase.
 - H2 will see significant improvement in revenue as the couple of contract announcement will start to ramp up.
- **Outlook for FY20:**The company expects to deliver double digit growth in FY20 as the deal pipeline remains healthy(earlier was 15% growth in beginning of the year) but still sees delay in large deal ramp ups .Margin will see furlough , wage hike impact in 3QFY20 However with revenue growth and cost optimization will support the margins.

Revenue Mix

Growth across segments

Segments (crore)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	QoQ%	YOY%
Embedded Product Design	328.164	349.202	352.462	346.76783	318.305	335.275	5%	-4%
Industrial Design & Visualization	40.8772	41.8881	41.107	42.13067	33.27734	37.4243	12%	-11%
System Integration & Support	12.989	11.6803	13.431	16.204104	10.12789	13.1178	30%	12%

Revenue by industry

Recovery seen in transportation

Industry Vertical(crore)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	QoQ%	YOY%
Transportation	204	221	219	216	169	186	11%	-16%
Broadcast & Communications	139	142	148	146	149	158	6%	11%
Healthcare & Medical Devices	12	16	18	21	28	25	-10%	56%
Others	27	24	22	22	16	17	4%	-30%

Revenue by Geography

US posted moderate growth, Europe remained flat

Geography(crore)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	QoQ%	YOY%
Europe	179	176	183	169	154	154	0%	-13%
USA	111	126	127	124	124	135	9%	7%
India	41	43	47	62	41	48	18%	13%
Row	52	58	49	50	42	49	15%	-16%

Revenue by Customer Concentration

Growth improved across clients

CLIENT(%)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	QoQ%	YOY%
Top	98	93	90	86	60	63	4%	-33%
Top 5	166	166	168	166	141	148	5%	-11%
Top10	209	214	210	211	183	196	7%	-9%

Exhibit: Revenue trend

Recovery in automotive led to growth in overall revenue

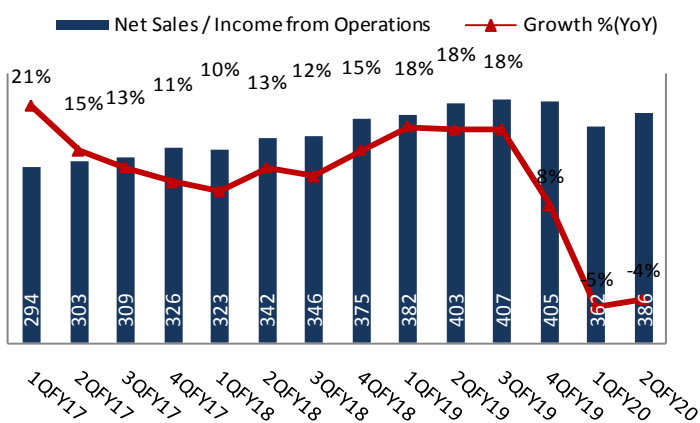


Exhibit: SDS Revenue trend

Strong growth from EPD and industrial design led the overall performance.

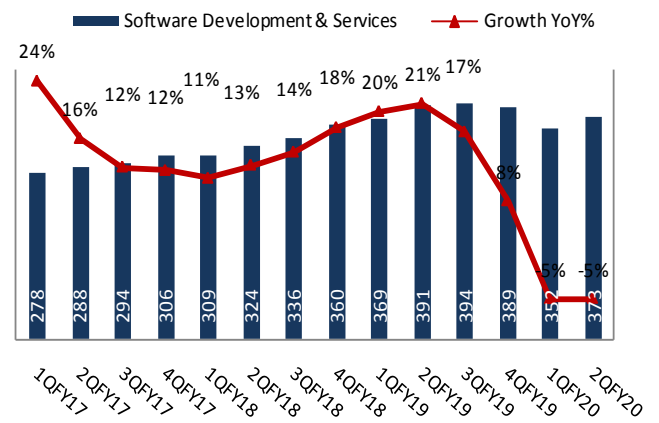


Exhibit: Margin Trend

One off impacted the margins

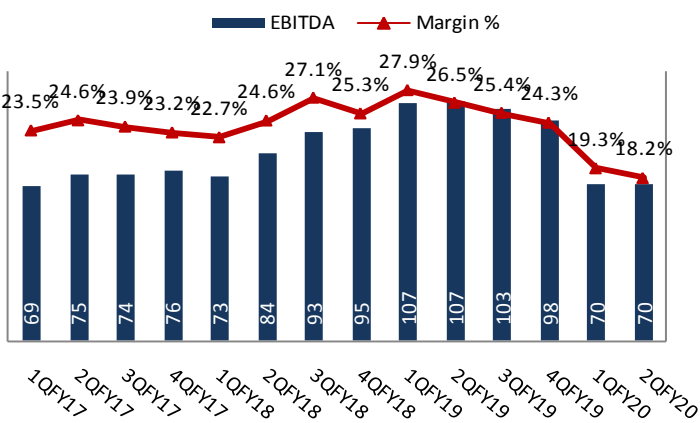


Exhibit: Attrition trend

Attrition still remain under control.

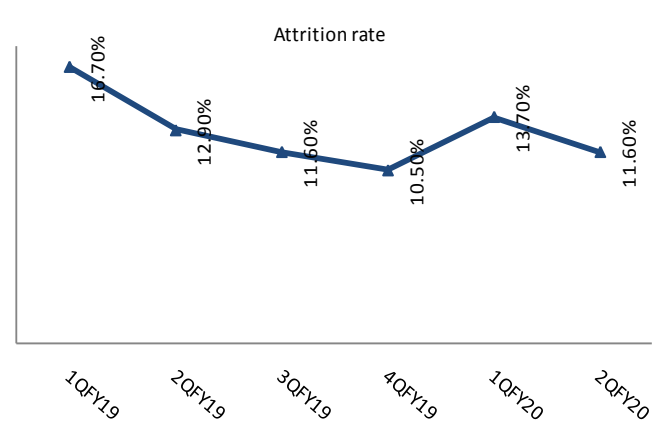
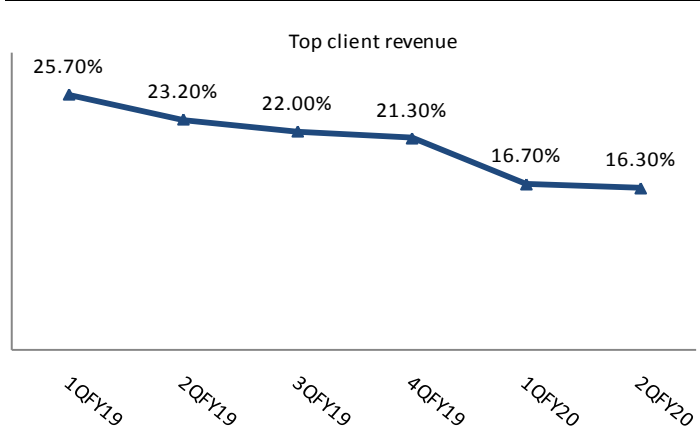


Exhibit: Top client revenue

Top client revenue recovered.



Financial Details

Balance Sheet

Fig in Rs cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	31	31	31	31	62	62	62	62
Reserves	204	252	355	528	676	880	1,043	1,268
Networth	235	283	386	559	738	943	1,105	1,330
Debt	-	-	-	-	-	-	-	-
Other Non Current Liab	12	11	18	19	19	14	14	14
Total Capital Employed	235	283	386	559	738	943	1,105	1,330
Net Fixed Assets (incl CWIP)	109	101	109	109	96	102	95	86
Non Current Investments	-	0	-	-	-	2	-	-
Other Non Cur Asst	-	-	-	-	2	3	3	3
Non Current Assets	150	138	146	149	140	135	128	120
Inventory	-	0	-	-	-	2	-	-
Debtors	156	154	215	245	307	357	358	414
Cash & Bank	50	133	182	252	394	516	674	872
Short-term loans and advances	12	15	23	20	1	1	1	1
Other Curr Assets	19	26	33	50	32	69	70	80
Curr Assets	237	328	454	566	809	1,008	1,178	1,431
Creditors	65	66	77	75	49	55	56	64
Provisions	46	68	89	35	17	10	10	11
Other Curr Liab	34	48	49	45	58	61	62	71
Curr Liabilities	140	171	196	137	191	187	187	207
Net Curr Assets	96	157	258	429	617	821	991	1,224
Total Assets	387	465	600	715	949	1,143	1,306	1,551

Income Statement

Fig in Rs cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	772	849	1075	1233	1386	1597	1605	1855
Change (%)	28%	10%	27%	15%	12%	15%	0%	16%
EBITDA	136	177	247	293	346	415	335	420
Change (%)	97%	30%	40%	19%	18%	20%	-19%	25%
Margin (%)	18%	21%	23%	24%	25%	26%	21%	23%
Depr & Amor.	35	25	23	27	25	25	39	38
EBIT	101	152	224	266	321	390	296	381
Int. & other fin. Cost	2	0	-	-	-	-	5	5
Other Income	16	4	12	(5)	43	43	54	46
EBT	101	152	224	266	321	390	296	381
Exp Item	-	-	-	-	-	-	-	-
Tax	40	53	82	88	124	143	99	114
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	75	103	155	173	240	290	245	308
Adjusted PAT	75	103	155	173	240	290	245	308
Change (%)	258%	37%	50%	12%	39%	21%	-15%	26%
Margin(%)	10%	12%	14%	14%	17%	18%	15%	17%

Financial Details

Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	35	40	46	37	37	35	24	25
ROCE	40	56	64	54	48	46	29	31
Asset Turnover	7	8	10	11	14	16	17	21
Current Ratio	2	2	2.3	4.1	4.2	5.4	6.3	6.9
Debtor Days	74	66	73	72	81	81	81	81
Book Value Per Share	38	45	62	90	119	151	177	214
Payable Days	31	28	26	22	13	13	13	13
Earnings Per Share	12	17	25	28	39	47	39	49
P/E	23	35	38	26	26	21	18	14
Price / Book Value	7	13	15	8	8	6	4	3
EV/EBITDA	12	20	23	15	17	14	13	10
EV/Sales	2	4	5	4	4	4	3	2

Cash Flow Statement

Fig in Rs cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	115	156	236	261	364	290	344	422
(inc)/Dec in Working Capital			23	27	25	25	39	38
Non Cash Op Exp	41	18	0	0	0	0	0	0
Int Paid (+)			-5	-1	-21	-24	0	0
Tax Paid	-17	-39	-76	-96	-114	-143	-99	-114
(inc)/Dec in Working Capital	-12	9	-57	-46	-32	-97	-11	-36
CF from Op. Activities	126	143	121	144	197	215	160	183
(inc)/Dec in FA & CWIP	0	0	-38	-26	-12	-32	-32	-30
Free Cashflow			83	118	185	183	128	153
(Pur)/Sale of Inv	0	0	0	0	-250	-150	0	0
others	-20	-27	-29	-13	-247	-159	-32	-30
CF from Inv. Activities	-20	-27	-29	-13	-247	-159	-32	-30
inc/(dec) in NW			0	0	0	0	0	0
inc/(dec) in Debt			0	0	0	0	0	0
Int. Paid	-2	0	0	0	0	0	0	0
Div Paid (inc tax)	-18	-32	-41	-52	-60	-83	-83	-83
others	-59	0	0	0	0	0	0	0
CF from Fin. Activities	-79	-32	-41	-52	-60	-83	-83	-83
Inc(Dec) in Cash	28	85	51	78	-110	-26	45	70
Add: Opening Balance	20	45	128	169	193	83	54	98
Closing Balance	47	130	179	248	83	54	98	169

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Correspondence Office Address: Arch Waterfront, 5th Floor, Block GP, Saltlake, Sector 5, Kolkata 700 091; Tel No.: 033-40541700; www.narnolia.com.

Registered Office Address: Marble Arch, Office 201, 2nd Floor, 236B, AIC Bose Road, Kolkata 700 020; Tel No.: 033-4050 1500; www.narnolia.com

Compliance Officer: Manish Kr Agarwal, Email Id: mkagarwal@narnolia.com, Contact No.:033-40541700.

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