India

Neutral *(no change)*

IT Services

1QFY25 results preview

- Average US$ revenue growth for our coverage universe stabilizing at 4.4% yoy vs. 4.5% yoy in 4QFY24.
- We expect 16bp/-5bp qoq change in average EBIT margin for Tier-I/II companies.
- Our industry interactions suggest contracting activity mix is likely shifting to short cycle projects. This bodes well for 2QFY25F.

1QFY25 earnings preview

We expect Tier-I IT services companies to report an average 0.8% qoq constant currency (CC) revenue growth in 1QFY25F, as ramp-up of deals won earlier outweigh the quantum of discretionary project roll-offs. Reported growth in US$ terms could be lower as the US$ appreciated average 0.5% vs. the GBP () and 0.9% vs. the Euro (), respectively. Deal ramp-up and absence of one-offs could aid Infosys' revenue (up 2% qoq cc) while HCL Technologies' revenue could decline by 1.2% qoq in CC terms, largely due to seasonal pass-back of productivity benefits. The growth of Tata Consultancy Services or TCS could be 1% qoq while Wipro & Tech Mahindra's sequential growth could be muted. Tier-II companies' US$ revenue growth could be slightly higher at an average 0.9% qoq led by Persistent Systems (PSYS) while weak seasonality in the SWC business could impact L&T Technology Services (LTTS).

Contracting activity mix likely shifting to short-cycle projects

Our recent industry interactions suggest that talent shortage and restructuring-led layoffs are leading to a change in the speed of decision-making, with clients leaning on vendors for competencies. This is driving an uptick in short-cycle consulting-led projects, with near-term revenue kicker and at better gross margin. This, coupled with the continuing trend of declining quantum of discretionary project roll-offs, could aid an improvement in the yoy growth trajectory from 2QFY25F. Click 01 July, 2024 for our recent report.

Vertical commentary: E&U replacing financial services

Our discussions suggest that large/mega deals are being constructed especially in the energy & utilities (E&U) vertical while communication, healthcare, & insurance verticals are witnessing better traction, and manufacturing, automotive, consumer packaged goods (CPG), retail, travel & tourism verticals' growth could moderate. Within the financial services vertical, large/mega deal activity has moderated, but is partly compensated by multiple smaller deals while the regional banks' recovery continues.

Recovery in short-cycle projects may change the margin narrative

Slow revenue trajectory, transition cost of large deals, and investments in capabilities were key margin headwinds till date while growth leverage, employee pyramid and operational efficiency were the tailwinds. However, the return of short-cycle projects could alleviate margin headwinds going into 2QFY25F, to an extent, given the better deal structuring with milestone payments, vs. elongated outcome-based earlier, and moderating employee cost trajectory driven by lower attrition, replacement costs and wage inflation. Conversely, demand uptick could drive the attrition rate higher and weigh on the cost of delivery. As a reminder, Accenture witnessed a 200bp increase in quarterly voluntary annualized attrition over the past two quarters to 14%. As for 1QFY25F, wage hikes could impact the EBIT margin of TCS while it may impact others from 2QFY25F. Finally, we expect Tier-I/Tier-II companies' EBIT margin to increase/decrease by an average 16bp/-5bp qoq, respectively.

We remain selective and prefer restructuring stories

1QFY25F is unlikely to drive the upgrades but could limit the downgrades and potentially change the messaging, while the continuation of this trend in 2QFY25F could improve the visibility & drive FY25F upgrades. Although the recovery in discretionary projects, if any, is positive for Tier-I companies, given their favourable valuations, select Tier-II companies could benefit too.

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Figure 1: 1QFY25 results preview commentary

Rsm	Jun-23	Mar-24	Jun-24	QoQ (%)	YoY (%)	Comments
Birlasoft						
Revenue (US$ m)	154	164	166	1.2	8.0	Ramp-up of FSI and healthcare deals could aid growth.
Revenue (Rs m)	12,628	13,625	13,833	1.5	9.5	Investments in domain capabilities could offset margin tailwinds from growth leverage.
EBIT (Rs m)	1,717	2,006	1,999	(0.3)	16.4	Sequential PAT could be impacted due to the absence of one-time insurance
EBIT margin(%)	13.6	14.7	14.5	-27 bp	85 bp	claim in 4QFY24.
Profit (Rs)	1,375	1,800	1,651	(8.3)	20.0	Key monitorable: New deal wins, traction in top-20 accounts, annuity mix and
EPS (Rs)	4.9	6.4	5.9	(8.3)	20.0	capital allocation.
Coforge						
Revenue (US$ m)	272	287	291	1.4	6.9	Moderation in discretionary spending to limit growth.
Revenue (Rs m)	22,210	23,585	24,243	2.8	9.2	
EBIT (Rs m)	2,559	3,405	3,261	(4.2)	27.4	Deferral of wage hikes and operational efficiency to help offset visa cost
EBIT margin(%)	11.5	14.4	13.5	-99 bp	193 bp	headwinds. A higher sequential tax rate could limit PAT growth.
Profit (Rs)	1,653	2,238	2,255	0.8	36.4	Key monitorable: Order intake and executable order book over the next 12 months
EPS (Rs)	26.5	35.9	36.2	0.8	36.4	and spending trend in FSI & travel verticals.
Cyient - DET business						
Revenue (US$ m)	177	179	175	(2.3)	(1.1)	Softness in aerospace, communication and sustainability portfolio to impact
Revenue (Rs m)	14,546	14,890	14,607	(1.9)	0.4	revenue.
EBIT (Rs m)	2,336	2,383	2,279	(4.4)	(2.5)	
EBIT margin(%)	16.1	16.0	15.6	-40 bp	-46 bp	Revenue weakness to weigh on margin and PAT.
Profit (Rs)	1,618	1,733	1,624	(6.3)	0.4	Key monitorable: Outlook on aerospace, transportation & communication verticals
EPS (Rs)	14.8	15.8	14.8	(6.3)	0.4	and DLM, margin levers and capital allocation.
HCL Technologies						
Revenue (US$ m)	3,200	3,430	3,387	(1.3)	5.8	Pass-back of annual productivity gains and offshoring of a large deal to impact
Revenue (Rs m)	2,62,960	2,84,990	2,82,485	(0.9)	7.4	revenue.
EBIT (Rs m)	44,600	50,180	48,870	(2.6)	9.6	Revenue weakness to weigh on margin.
EBIT margin(%)	17.0	17.6	17.3	-31 bp	34 bp	
Profit (Rs)	35,340	39,860	38,421	(3.6)	8.7	Key monitorable: FY25F guidance, outlook on IT services, ER&D & products
EPS (Rs)	13.0	14.7	14.2	(3.4)	8.9	business and capital allocation.
Infosys						
Revenue (US$ m)	4,617	4,564	4,649	1.9	0.7	Ramp-up of deals and absence of one-offs could aid revenue.
Revenue (Rs m)	3,79,330	3,79,230	3,87,759	2.2	2.2	Growth leverage, absence of one-off impact and operational efficiency are margin
EBIT (Rs m)	78,910	76,210	80,460	5.6	2.0	tailwinds partly offset by large deal transition costs.
EBIT margin(%)	20.8	20.1	20.8	65 bp	-5 bp	Absence of income-tax refunds and lower other income could impact sequential PAT.
Profit (Rs)	59,450	79,690	62,336	(21.8)	4.9	Key monitorable: FY25F guidance, outlook on ramp-up of large deals, vertical
EPS (Rs)	14.4	19.2	15.0	(21.8)	4.8	commentary, and outlook on client budgets.
LTIMindtree						
Revenue (US$ m)	1,059	1,069	1,095	2.4	3.4	CC revenue could increase 2.5% qoq.
Revenue (Rs m)	87,021	88,929	91,306	2.7	4.9	Recovery in the FSI vertical, top customers and ramp-up of large deals to aid revenue growth.
EBIT (Rs m)	14,508	13,087	13,468	2.9	(7.2)	Margin tailwinds from the absence of project cancellations and growth leverage
EBIT margin(%)	16.7	14.7	14.8	3 bp	-192 bp	could be offset by visa and large deal transition costs.
Profit (Rs)	11,515	10,999	11,232	2.1	(2.5)	Key monitorable: Outlook on FSI, hi-tech and manufacturing verticals, merger
EPS (Rs)	38.9	37.1	37.8	2.1	(2.6)	synergies and capital allocation
L&T Technology Services						
Revenue (US$ m)	280	305	300	(1.8)	7.0	Modest growth in organic revenue could be offset by weak seasonality in SWC.
Revenue (Rs m)	23,014	25,375	24,980	(1.6)	8.5	
EBIT (Rs m)	3,954	4,282	4,119	(3.8)	4.2	Large deal transition costs to offset tailwinds from lower contribution of inferior
EBIT margin(%)	17.2	16.9	16.5	-38 bp	-69 bp	margin SWC business.
Profit (Rs)	3,111	3,408	3,295	(3.3)	5.9	Key monitorable: FY25F guidance, outlook on transportation, industrial & plant
EPS (Rs)	29.4	32.2	31.1	(3.3)	5.8	engineering verticals, deal wins, and DSO trajectory.
Mphasis						
Revenue (US$ m)	398	411	414	0.9	4.1	Bottoming out of portfolio challenges and TMT vertical could aid growth. BFS
Revenue (Rs m)	32,520	34,121	34,568	1.3	6.3	commentary critical.
EBIT (Rs m)	4,996	5,081	5,185	2.0	3.8	Margin to remain range bound, given revenue softness and capability
EBIT margin(%)	15.4	14.9	15.0	11 bp	-36 bp	investments.
Profit (Rs)	3,961	3,933	4,074	3.6	2.9	Key monitorable: Deal wins in direct channel, FSI vertical outlook and synergy
EPS (Rs)	20.9	20.7	21.4	3.6	2.2	from Silverline acquisition.
Persistent Systems						
Revenue (US$ m)	283	311	327	5.1	15.5	Traction in healthcare and FSI and recovery in technology vertical could aid
Revenue (Rs m)	23,212	25,905	27,241	5.2	17.4	growth.
EBIT (Rs m)	3,466	3,744	3,800	1.5	9.6	Large deal transition costs, S&M and GenAI investments could impact margins.
EBIT margin(%)	14.9	14.5	14.0	-50 bp	-98 bp	
Profit (Rs)	2,288	3,153	3,006	(4.7)	31.4	Key monitorable: Outlook on services BU, TCV and ACV deal wins, outlook on
EPS (Rs)	14.9	20.5	19.5	(4.7)	31.2	margin and capital allocation.
Sonata Software						
Revenue - IT services (US$ m)	77.3	81.7	83.2	1.9	7.7	Momentum in the technology vertical and stability in Quant Systems to aid growth.
Revenue (Rs m)	20,155	21,916	23,913	9.1	18.6	Domestic business gross contribution to remain steady.
EBIT (Rs m)	1,470.6	1,110.0	1,573.9	41.8	7.0	Growth leverage to aid services margin partly offset by large-deal transition costs.
EBIT margin(%)	7.3	5.1	6.6	152 bp	-71 bp	Moderation in other income and a higher sequential tax rate could limit qoq PAT.
Profit (Rs)	1,201.1	1,109.1	1,245.8	12.3	3.7	

EPS (Rs)	4.3	4.0	4.5	12.3	3.4	Key monitorable: Outlook on the technology and FSI verticals, IT services margin trajectory and gross profit trend in the domestic business.
Tata Consultancy Services						
Revenue (US$ m)	7,226	7,363	7,457	1.3	3.2	Ramp-up of deals won earlier, recovery in the FSI and retail verticals, and momentum from the BSNL deal could aid growth.
Revenue (Rs m)	5,93,810	6,12,370	6,21,879	1.6	4.7	
EBIT (Rs m)	1,37,550	1,59,180	1,57,211	(1.2)	14.3	Operational efficiency and sequential moderation in third party & travel expenses could help partly offset the headwinds from wage hikes.
EBIT margin(%)	23.2	26.0	25.3	-71 bp	212 bp	
Profit (Rs)	1,10,740	1,24,340	1,23,098	(1.0)	11.2	Key monitorable: Conversion from deal pipeline, outlook on the FSI, retail & manufacturing verticals and ramp-up of large deals
EPS (Rs)	30.3	34.4	34.4	0.1	13.7	
Tata Elxsi						
Revenue (US$ m)	103.4	109.1	111.3	2.1	7.6	Deal ramp-up in the transportation vertical could aid overall growth partly offset by softness in the media and healthcare verticals.
Revenue (Rs m)	8,503	9,059	9,353	3.2	10.0	
EBIT (Rs m)	2,301	2,337	2,432	4.1	5.7	Operating efficiency to aid margins offset by continued investments.
EBIT margin(%)	27.1	25.8	26.0	20 bp	-106 bp	Sequential PAT could be impacted from lower other income and a higher tax rate.
Profit (Rs)	1,889	1,969	1,984	0.7	5.0	Key monitorable: Demand trend across segments, build-up of adjacencies in focus verticals.
EPS (Rs)	30.3	31.6	31.8	0.7	5.0	
Tata Technologies						
Services revenue (US$ m)	118.8	120.2	124.3	3.4	4.7	Deal ramp-up led by anchor clients and the aerospace vertical could aid growth.
Revenue (Rs m)	12,575	13,011	13,686	5.2	8.8	
EBIT (Rs m)	2,269	2,110	2,258	7.0	(0.5)	Growth leverage and operational efficiency could aid margins offset by growth in the low-margin technology business.
EBIT margin(%)	18.0	16.2	16.5	28 bp	-154 bp	
Profit (Rs)	1,915	1,572	1,813	15.3	(5.3)	Sequential moderation in the tax rate (31.9% in 4QFY24) could aid PAT.
EPS (Rs)	4.7	3.9	4.5	15.3	(5.1)	
Tech Mahindra						
Revenue (US$ m)	1,601	1,548	1,550	0.1	(3.2)	Growth in the enterprise portfolio partly offset by weak Comviva seasonality.
Revenue (Rs m)	1,31,590	1,28,713	1,29,252	0.4	(1.8)	
EBIT (Rs m)	8,914	9,464	10,534	11.3	18.2	Receding impact of low-margin business to aid margins.
EBIT margin(%)	6.8	7.4	8.2	80 bp	138 bp	Absence of goodwill impairment charge could aid sequential PAT growth.
Profit (Rs)	6,925	6,610	9,165	38.7	32.3	Key monitorable: Organization restructuring update, outlook on communication & enterprise business, DSO trend & capital allocation.
EPS (Rs)	7.8	7.5	10.3	38.7	32.1	
Wipro						
IT Services revenue (US$ m)	2,779	2,657	2,658	0.0	(4.3)	Expect IT services CC revenue to be flat qoq vs. -1.5% to 0.5% guided range.
Revenue (Rs m)	2,28,310	2,22,083	2,22,325	0.1	(2.6)	
EBIT (Rs m)	34,578	35,501	36,684	3.3	6.1	Operational efficiency could help offset the increase in SG&A expenses (post sharp reduction in 4QFY24).
EBIT margin(%)	15.1	16.0	16.5	51 bp	135 bp	
Profit (Rs)	28,701	28,346	29,922	5.6	4.3	Key monitorable: 2QFY25F revenue growth guidance, large deal win trajectory and ramp-up.
EPS (Rs)	5.1	5.4	5.7	5.6	11.5	

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