

Tata Elxsi

In-line Q3; building hope on Q4

In-line Q3; delayed ramp-ups to likely ensue in Q4

Tata Elxsi (TELX IN) posted an in-line Q3, with QoQ dollar growth at 2.8%, slightly ahead of consensus estimates by 0.7%. EBIT margin at 26.8% was a tad miss on streets expectations by 30bps and in line with ours. Growth was broad-based, except for Media & Communications, wherein spending was laggard, and thus the caution on demand. But this was offset by robust demand in Lifesciences (+3.9% QoQ CC). Transportation saw a steady performance of 1.9% QoQ CC growth. Softness in growth was due to delayed ramp-ups and Q3 weakness. But talent addition (+350 employees QoQ) in a weak Q3 is possibly a reflection of ramp-ups finally ensuing in Q4.

Design-led growth and AI-led capabilities prop deal momentum

Digital propelled the Industrial Design business that saw sharp 11.7% QoQ and 17.9% YoY CC growth. This also paves way for downstream value in Systems Integration business, reflecting in related 11.7% QoQ / 20% YoY CC growth. TELX is building capabilities in AI via new deals. It already has an AI component in its automation and ADAS offerings and adding gAI aids faster time to market. TELX bagged four key deals in Q3, one in design services, two in product engineering and one in Lifesciences, thus backing demand momentum.

Valuations: Maintain Accumulate; TP raised to INR 8,610

We favor TELX given: a) its digital design prowess, b) industry-leading operating margin (~30% EBITDA), c) marquee clientele (75% offshore mix) and d) strong return ratios (RoE/RoIC at 41%/93%). Orderbook continues to be robust in Transportation and Medical verticals. However, the soft outlook for Media and Telecom sector may continue to weigh on growth. We slightly raise FY25E/ 26E earnings by 0.6% / 1.7% respectively. We maintain Accumulate with raised TP of INR 8,610 (earlier INR 8,490, on 51x Dec-25E EPS of INR 168 (five-year average + 0.5std. deviation). In FY23-26E, expect USD revenue/EBIT CAGRs of ~16%/18%, implying an EPS CAGR of ~15%.

Rating: Accumulate

Target Price: INR 8,610

Upside: 5%

CMP: INR 8,196 (as on 23 January 2024)

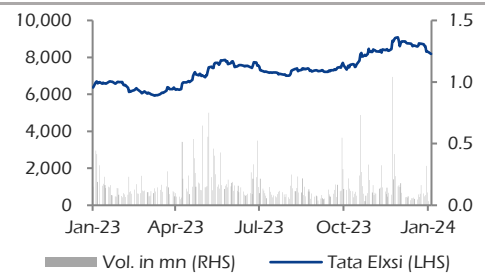
Key data*

Bloomberg/Reuters Code	TELX IN /TTEX.BO
Current/Dil. Shares O/S (mn)	62/62
Mkt Cap (INR bn/USD mn)	510/6,136
Daily Volume (3M NSE Avg)	145,155
Face Value (INR)	10

1 USD = INR 83.2

Note: *as on 23 January 2024; Source: Bloomberg

Price & Volume



Source: Bloomberg

Shareholding (%)	Q4FY23	Q1FY24	Q2FY24	Q3FY24
Promoter	43.9	43.9	43.9	43.9
Institutional Investors	17.4	18.3	18.6	20.7
Other Investors	4.5	4.5	4.4	4.2
General Public	34.2	33.3	33.1	31.1

Source: BSE

Price performance (%)	3M	6M	12M
Nifty	8.7	7.6	17.8
Tata Elxsi	11.7	12.1	23.1

Source: Bloomberg

(INR mn)	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ (%)
Revenue (USD mn)	109.9	99.4	10.6	106.9	2.8
Revenue (INR mn)	9,142	8,177	11.8	8,817	3.7
EBITDA	2,701	2,469	9.4	2,635	2.5
Depreciation	254	214	18.8	250	1.8
EBIT	2,447	2,254	8.5	2,385	2.6
Other income	349	191	82.5	311	12.2
PBT	2,741	2,401	14.2	2,639	3.9
Total tax	676	454	48.9	638	6.0
Adjusted PAT	2,064	1,947	6.0	2,000	3.2
Reported PAT	2,064	1,947	6.0	2,000	3.2
Reported EPS	33.1	31.3	6.0	32.1	3.2

Key Financials

YE	Revenue (INR bn)	YoY (%)	EBITDA (INR bn)	EBITDA Margin (%)	Adj PAT (INR bn)	YoY (%)	Fully DEPS (INR)	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)
March											
FY23	31.4	15.6	9.61	17.5	7.6	1.3	114	22.5	39.4	72.1	52.3
FY24E	36.0	12.6	10.75	17.1	8.2	32.5	151	25.9	38.2	54.5	46.1
FY25E	42.9	15.1	13.25	18.6	9.7	41.9	214	30.8	43.1	38.4	37.0
FY26E	50.5	16.1	15.54	18.6	11.5	20.3	257	31.1	42.5	31.9	31.2

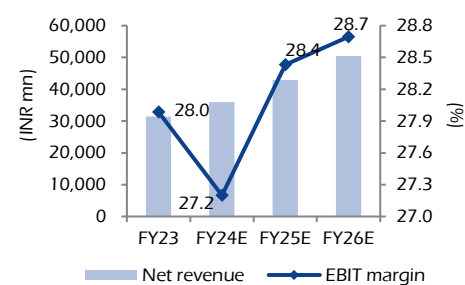
Note: Pricing as on 23 January 2024; Source: Company, Elara Securities Estimate

Financials (YE March)

Income Statement (INR mn)	FY23	FY24E	FY25E	FY26E
Net Revenues	31,447	35,956	42,935	50,471
EBITDA	9,615	10,751	13,253	15,540
Less :- Depreciation & Amortization	814	971	1,045	1,057
EBIT	8,801	9,780	12,207	14,483
Add:- Non operating Income	738	1,218	846	999
PBT	9,377	10,789	12,832	15,260
Less :- Taxes	1,823	2,631	3,167	3,766
Adjusted PAT	7,554	8,158	9,665	11,494
Reported PAT	7,554	8,158	9,665	11,494
Balance Sheet (INR mn)	FY23	FY24E	FY25E	FY26E
Share Capital	623	623	623	623
Reserves	20,235	25,130	30,929	37,825
Other Liabilities	4,263	4,470	4,627	4,639
Total Liabilities	25,120	30,222	36,178	43,087
Gross Block	3,794	4,094	4,394	4,694
Less:- Accumulated Depreciation	1,965	3,858	5,895	7,956
Net Block	1,829	1,315	677	(118)
Investments	685	0	0	0
Cash & cash equivalents	11,916	19,918	24,986	31,058
Net Working Capital	8,705	7,003	8,529	10,161
Other Assets	1,986	1,986	1,986	1,986
Total Assets	25,120	30,222	36,179	43,087
Cash Flow Statement (INR mn)	FY23	FY24E	FY25E	FY26E
Cash profit adjusted for non-cash items	9,297	13,334	16,301	18,821
Add/Less : Working Capital Changes	(1,159)	(3,311)	(3,453)	(4,171)
Operating Cash Flow	9,505	10,022	12,848	14,650
Less:- Capex	(1,537)	(1,500)	(1,600)	(1,600)
Free Cash Flow	7,968	8,522	11,248	13,050
Financing Cash Flow	(5,232)	(4,431)	(6,287)	(7,562)
Investing Cash Flow	(2,716)	(2,153)	(1,113)	(678)
Net change in Cash	1,557	3,438	5,448	6,411
Ratio Analysis	FY23	FY24E	FY25E	FY26E
Income Statement Ratios (%)				
Revenue Growth	15.6	12.6	15.1	16.1
EBITDA Growth	23.4	12.4	26.1	16.2
PAT Growth	1.3	32.5	41.9	20.3
EBITDA Margin	17.5	17.1	18.6	18.6
Net Margin	24.0	22.7	22.5	22.8
Return & Liquidity Ratios				
Net Debt/Equity (x)	(0.6)	(0.8)	(0.8)	(0.8)
ROE (%)	22.5	25.9	30.8	31.1
ROCE (%)	39.4	38.2	43.1	42.5
Per Share data & Valuation Ratios				
Diluted EPS (INR)	113.7	150.5	213.6	256.9
EPS Growth (%)	1.0	32.4	41.9	20.3
Book Value	113.7	150.5	213.6	256.9
DPS (INR)	45.5	60.2	85.4	102.7
P/E Ratio (x)	72.1	54.5	38.4	31.9
EV/EBITDA (x)	52.3	46.1	37.0	31.2
Price/Book (x)	72.1	54.5	38.4	31.9
Dividend Yield (%)	0.6	0.7	1.0	1.3

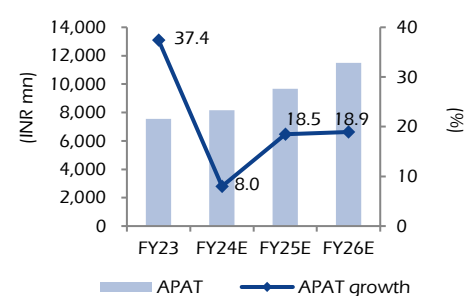
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Revenue & margin trend



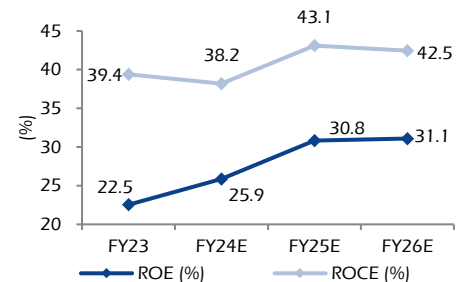
Source: Company, Elara Securities Estimate

Adjusted profit growth trend



Source: Company, Elara Securities Estimate

Return ratios



Source: Company, Elara Securities Estimate

Conference Call – Highlights

Vertical- and geography-wise commentary

- EPD, TELX's largest segment, was up 1.5% QoQ / 8% YoY in CC.
- Healthcare rebounded with 3.9% QoQ / 11.2% YoY CC growth, led by initiatives in new product engineering and regulatory services.
- Geography-wise, Europe and India continue to lead growth, up 4% and 9% QoQ. The US declined 2.9% QoQ, in-line with other industry players' results. Japan and APAC saw good growth.

Transportation vertical

- Transportation was steady 1.9% QoQ / 12.9% YoY in CC despite facing delays in planned ramp-ups and deal closures due to short quarter and holidays.
- SDV space, within transportation, is continuing to see good demand. There is a shift from supplier-led business to OEM-led business. Q4 may see acceleration in vertical demand.
- TELX is seeing pricing pressure in deals with North American tier-I OEMs. APAC region is doing well on the automotive side.

Media and Communications

- Media and Communications remained muted with -0.1% QoQ / +1.3% YoY CC growth. This was on account of weakness in some key US customers.
- Impact was seen from lower working days owing to shorter quarter and furloughs.
- Consolidation and M&A in the media & telco industry led to restricted spending.
- Demand continued to remain tepid with no green shoots yet. Most deals in the vertical were from cost takeout, consolidation and consulting space.
- TELX expects the overhang to remain for the vertical in the next few quarters.

Exhibit 2: Change in estimates

(INR mn)	Old			New			% Change		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY25E
Revenue (USD mn)	434	513	599	434	516	607	0.1	0.6	1.2
YoY growth (%)	1,141.0	1,824.9	1,678.6	11.5	18.8	17.5			
Revenue	35,928	42,695	49,862	35,956	42,935	50,471	0.1	0.6	1.2
EBITDA	10,705	12,809	14,959	10,747	13,253	15,540	0.4	3.5	3.9
EBITDA margin (%)	29.8	30.0	30.0	29.9	30.9	30.8			
Net profit	8,170	9,604	11,302	8,154	9,665	11,494	(0.2)	0.6	1.7
EPS	131.2	154.2	181.5	131	155	185	(0.2)	0.6	1.7
TP (INR)			8,490			8,610			1.4

Source: Elara Securities Estimate

Margin uptick

- EBITDA margin at 29.5% was down 30bps QoQ. This was a result of headwinds from: 1) increased travel, visa and campus training costs (70-75bps), 2) AI investments (40bps), and 3) growth in people cost (10bps) though offset by tailwinds of :1) declining cost of sales (55bps) and 2) benefit from exchange rate (50bps).
- Employee addition was at 350 QoQ, taking the base to 13,221. And attrition rate was at 12.9% (versus 13.7% in Q2), in-line with the industry.
- TELX enjoys a good bench and is one of the few companies with net QoQ headcount addition. It continues to build strong talent pipeline and is augmenting its sales workforce.
- Offshore business grew 50bps sequentially at 74.7%. This reflects the solid execution of TELX.

Client and large deal commentary

- Top-5/10 clients posted steady performance in a weak quarter, up 1.2%/1.5% QoQ.
- Large deals were in the regulatory domain and new product business, with most being long term in nature.
- Ramp-up of deals won in Q2 is taking time due to union problems. Some ramp-up was visible in Q3, while remaining may come through in Q4.

Exhibit 1: Valuations

(INR)	
Current trailing twelve months (TTM) EPS	128
Current market price (CMP)	8610
Target EPS	168
Target EPS period	Dec '24E-Sep '25E
Target multiple (x)	51
Target price (per share)	8,610
Upside (%)	5%

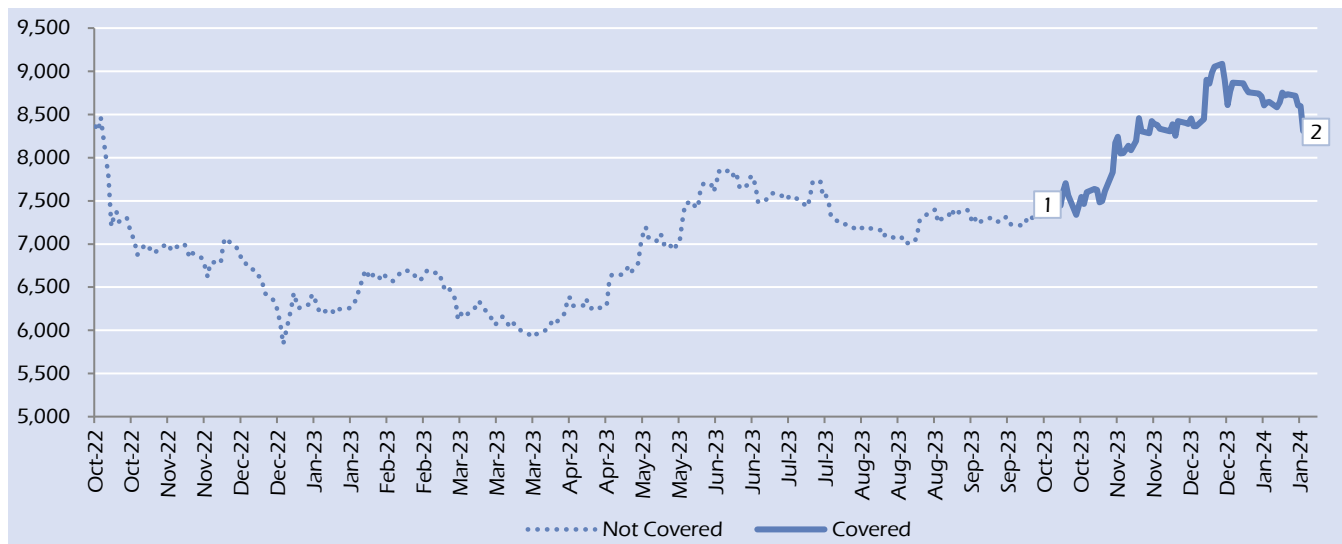
Note: Pricing as on 23 January 2024; Source: Elara Securities Estimate

Exhibit 2: Valuation summary

	Ticker	Currency	Mcap	Rating	Price	TP	Upside	Turnover ^{'23}	FY23-26E		EV/sales		P/E		Div. yield (%)		ROE (%)	
									Sales CAGR %	EPS CAGR %	FY24E (x)	FY25E (x)	FY24E (x)	FY25E (x)	FY24E	FY25E	FY24E	FY25E
			USD bn		INR	INR	(%)	USD mn										
Large Indian IT services cos.																		
TCS	TCS IN	INR	169.8	Buy	3,858	4,430	15	27,927	5.8	9.4	5.7	5.3	30.5	28.1	1.3	1.4	47.9	42.9
Infosys	INFO IN	INR	82.0	Sell	1,642	1,260	(23)	18,212	4.7	6.3	4.2	4.0	27.7	26.4	1.8	1.9	29.4	29.1
Wipro	WPRO IN	INR	29.5	Reduce	470	450	(4)	11,232	1.9	6.8	2.4	2.2	21.9	20.2	0.5	0.5	12.7	12.3
HCL Technologies	HCLT IN	INR	49.7	Sell	1,524	1,430	(6)	12,586	8.1	9.2	3.6	3.2	26.2	23.2	2.9	3.2	23.6	25.9
Tech Mahindra	TECHM IN	INR	16.0	Buy	1,367	1,360	(0)	6,607	2.8	11.4	2.4	2.3	43.6	21.5	0.8	1.7	9.4	17.3
Tier-1 IT AVG								15,313	4.6	8.6	3.7	3.4	30.0	23.9	1.5	1.8	24.6	25.5
Tier-1 IT Median								12,586	4.7	9.2	3.6	3.2	27.7	23.2	1.3	1.7	23.6	25.9
Mid-sized Indian IT services cos.																		
LTIMindtree	LTIM IN	INR	20.1	Buy	5,639	6,570	17	4,106	10.4	16.8	4.4	4.0	33.9	25.9	1.2	1.5	27.6	31.0
Mphasis	MPHL IN	INR	5.8	Accumulate	2,533	2,380	(6)	1,712	4.6	6.3	3.3	3.0	29.2	27.0	1.9	2.0	19.5	19.4
Persistent	PSYS IN	INR	7.6	Accumulate	8,254	8,300	1	1,036	14.4	23.2	6.2	5.4	55.6	43.7	0.7	0.8	23.4	24.2
Coforge	COFORGE IN	INR	4.6	Buy	6,202	8,100	30	1,002	14.6	31.2	4.0	3.4	41.2	29.0	2.4	3.4	25.9	30.8
eclerx	ECLX IN	INR	1.5	Accumulate	2,614	2,500	(4)	333	11.3	18.9	4.1	3.5	23.7	18.2	0.7	0.9	28.3	32.1
Sonata Software	SSOF IN	INR	2.5	NR	740	NA	-	897	9.2	20.3	2.8	2.3	39.1	31.3	1.3	1.6	36.7	38.4
Happiest Minds	HAPPSTMN IN	INR	1.6	NR	856	NA	-	172	16.6	11.2	7.5	6.4	53.9	43.0	0.0	0.0	23.3	23.3
Firstsource solutions	FSOL IN	INR	1.6	NR	191	NA	-	721	8.0	10.6	2.3	2.1	25.1	20.5	2.2	2.5	15.7	17.9
Birlasoft	BSOFT IN	INR	2.7	NR	801	NA	-	578	11.4	44.6	3.9	3.5	38.3	31.9	0.8	0.9	21.8	22.4
Zensar Tech	ZENT IN	INR	1.5	NR	544	NA	-	584	5.0	38.7	2.3	2.1	19.6	19.5	1.4	1.4	19.5	16.9
Intellect design arena	INDA IN	INR	1.5	NR	893	NA	-	269	14.3	27.8	4.7	4.1	35.4	27.5	0.3	0.4	16.1	17.9
Mastek	MAST IN	INR	1.0	NR	2,682	NA	-	309	17.7	14.9	2.8	2.4	28.1	20.9	1.1	1.0	16.5	19.4
Mid-size IT AVG								977	11.5	22.0	4.0	3.5	35.3	28.2	1.1	1.4	22.9	24.5
Mid-size IT Median								653	11.3	19.6	4.0	3.5	34.7	27.2	1.1	1.2	22.6	22.9
Indian IT ER&D cos.																		
L&T Tech	LTTS IN	INR	6.8	Sell	5,361	4,240	(21)	990	14.3	11.9	5.5	5.0	43.5	38.6	0.8	0.9	25.5	24.8
Cyient	CYL IN	INR	2.8	Buy	2,120	2,500	18	746	14.1	27.0	3.2	2.8	26.2	22.6	1.9	2.2	24.1	24.7
Tata Elxsi	TELX IN	INR	6.1	Accumulate	8,196	8,610	5	390	15.9	15.0	13.6	11.3	62.6	52.8	0.6	0.8	40.2	32.2
KPIT Tech	KPIT IN	INR	5.0	Buy	1,502	1,480	(1)	418	24.6	37.1	8.4	7.0	70.9	55.7	0.5	0.6	31.4	32.5
Tata technologies	NA	INR	5.6	NR	1,142	NA	-	532	10.7	13.7	11.0	9.8	83.2	72.6	1.0	1.1	21.0	23.0
Mid-tier IT AVG								615.1	15.9	20.9	8.4	7.2	57.3	48.4	1.0	1.1	28.4	27.4
Mid-tier IT Median								532	14.3	15.0	8.4	7.0	62.6	52.8	0.8	0.9	25.5	24.8
Global peers																		
IBM	IBM US	USD	158.3	NA	173	NA		60,530	2.5	122.5	3.3	3.2	18.2	17.5	3.8	3.9	36.2	32.3
Accenture	ACN US	USD	245.8	NA	368	NA		61,594	7.3	10.4	3.7	3.4	30.2	27.5	1.4	1.5	28.2	28.2
Cognizant	CTSH US	USD	38.8	NA	77	NA		19,428	0.8	7.2	2.0	1.9	17.6	16.8	1.5	1.6	17.3	16.6
Capgemini	CAP FP	EUR	37.6	NA	201	NA		23,167	4.6	14.9	1.7	1.7	15.8	15.2	1.8	2.0	18.5	18.0
Endava	DAVA US	USD	4.6	NA	80	NA		871	16.3	20.4	4.5	3.8	38.1	27.6	-	-	14.5	18.3
EPAM	EPAM US	USD	17.3	NA	300	NA		4,825	0.6	23.1	3.3	3.2	29.1	28.3	-	-	19.0	16.4
Globant	GLOB US	USD	10.1	NA	237	NA		1,780	17.7	28.5	4.8	4.1	41.6	35.9	-	-	14.1	14.7
NAGARRO SE	NA9 GY	USD	1.4	NA	91	NA		902	10.4	-5.1	1.6	1.5	20.7	16.9	-	-	32.0	30.5
Global IT AVG								24,599	7.1	32.4	3.3	3.0	27.2	24.1	2.1	2.2	21.1	20.6
Global IT Median								19,428	4.6	20.4	3.3	3.2	29.1	27.5	1.7	1.8	18.5	18.0

Note: Pricing as on 23 January 2024; Bloomberg Consensus for Not Rated companies; Source: Elara Securities Estimate

Coverage History



	Date	Rating	Target Price	Closing Price
1	12-Oct-2023	Accumulate	INR 8,490	INR 7,355
2	23-Jan-2024	Accumulate	INR 8,610	INR 8,196

Guide to Research Rating

BUY	Absolute Return >+20%
ACCUMULATE	Absolute Return +5% to +20%
REDUCE	Absolute Return -5% to +5%
SELL	Absolute Return < -5%

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