

May 20, 2016

## Majesco Ltd (MAJLIM)

₹ 567

### Value discovered; focus shifts to earnings...

We attended Majesco's analyst day wherein it provided business, financial update and strategic direction as it enters the second year of its three year restructuring journey. The company has hired senior sales people in US (60), built a decent order book (\$158 million) and hopes to capitalise on the same. Execution miss led by a rise in SG&A spends remains a key risk to valuation as the discovery stage is behind us and sustainable earnings delivery is key to stock outperformance.

#### Booking supports 25%+ YoY revenue growth in FY17E...

Majesco ended FY16 with 12M order backlog of \$73.1 million while total bookings were \$158 million in FY16. Historically, next 12M revenue to 12M order backlog ratio was 2x. Assuming similar ratio implies FY17E revenue could range at ~\$145 million and translates to 28% growth YoY. We remain conservative and model ~19% YoY rupee revenue growth.

#### Rise in gross margins key to EBITDA margin expansion...

Majesco currently operates at 44.5% gross margin (GM) which is lower compared to Guidewire's 66% (FY15 ending July) led by variety of reasons including lower licence sales (8% in FY16 vs. 47% for Guidewire), higher professional services contribution (60% vs. 40%) that has lower margins (~35%) and lower GM's in ex-billing business. Though billing makes 60% gross, given product maturity and higher Go-lives (60), policy admin and claims margins could rise as Go-Lives improve. Finally, shift to annual licence sales vs. one-time earlier could aid gross margin improvement. Discussions suggest achieving 60% as the company average GM seems tricky but modest improvements could continue.

#### Rise in S&M costs may be key risk to EBITDA margins...

Majesco's FY18E goals include 1) revenues of \$220-225 million (vs. \$113.3 million in FY16), 2) GM of 49-50% (44.5%), 3) S&M expense as percentage of revenue (13-14% vs. 15.1%), 4) G&A (14-15% vs. 18.7%), 5) R&D (12% vs. 14.4%) and EBITDA of 12-14% vs. 0.5% in FY16. Discussions suggest 60 sales people hired in the US could help accelerate growth while 500-600 bps of margins tailwinds could accrue from SG&A rationalisation. Interestingly, Majesco was shy to confirm whether the current sales engine is good enough to achieve FY18E organic revenue goals. Given onsite sales staff is not inexpensive, rise in their number and costs subsequently, could pressure EBITDA margin expansion thesis.

#### Account mining could improve...

Majesco has 17 customers with direct written premium (DWP) in excess of >\$5 billion that increased from nine in FY14 (refer exhibit 1) while customers with \$1-5 billion DWP rose to 27 vs. 21 in FY14. Analysing similar data for Guidewire suggests that despite having modest 1.4x higher number of customers with DWP in excess of \$5 billion, revenue is higher by 3.4x. Further, revenue/customer is also substantially higher at \$1.8 million vs. \$690k for Majesco and suggests deeper engagements & high wallet share.

#### On firm footing post re-organisation but earnings delivery key...

Majesco's revenue could grow at 25% CAGR in FY15-18E led by deal wins while PAT could grow at 128% CAGR in FY16-18E with average 9.2% EBITDA margins. We value Majesco at ₹ 750, i.e. at 2.6 FY17E sales. The target multiple is at ~35% discount to global peer group average of 4x to account for modest growth/margin profile. Product companies are valued on P/S multiple given substantial R&D investments in formative years. Inability to deliver earning growth could jeopardise our thesis.

Rating matrix	
Rating	Buy
Target	₹ 750
Target Period	12-18 months
Potential Upside	32%

What's Changed?	
Target	Unchanged
EPS FY17E	Unchanged
EPS FY18E	Unchanged
Rating	Unchanged

Key Financials				
₹ crore	FY15	FY16E	FY17E	FY18E
Net Sales	493.6	690.0	820.0	973.0
EBITDA	2.0	6.0	50.0	120.0
EBITDA margin (%)	0.4	0.9	6.1	12.3
PAT	-18.8	5.0	21.0	60.0
EPS	-8.3	2.2	9.2	26.2

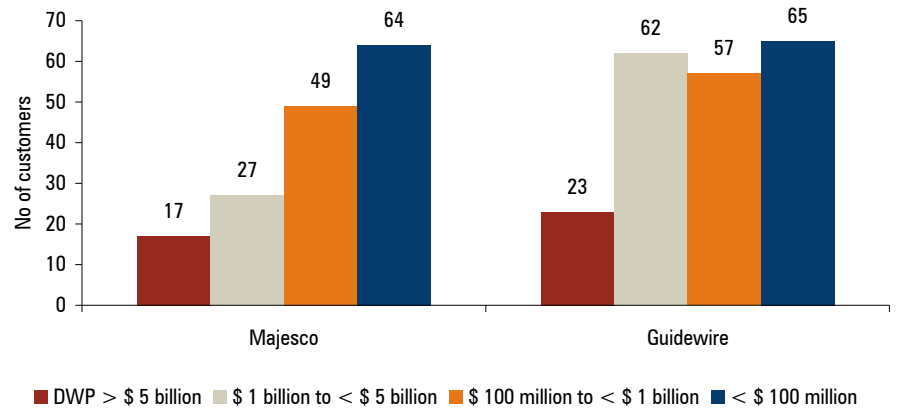
Valuation summary				
	FY15	FY16E	FY17E	FY18E
P/E	NM	NM	61.7	21.6
Target P/E	NM	340.1	81.7	28.6
EV / EBITDA	NM	204.2	24.5	10.2
P/BV	4.8	4.7	4.2	3.4
RoNW	NM	1.8	7.2	17.5
RoCE	NM	NM	6.4	19.8

Stock data	
Particular	Amount
Market Capitalization (₹ crore)	1295.9
Debt (₹ crore)	91.9
Cash and Cash Equivalent (₹ crore)	127.2
EV (₹ crore)	1260.6
52 Week High / Low (₹)	789 / 287
Equity Capital	275.9
Face Value	5.0

Price Performance				
	1M	3M	6M	12M
Sonata	(3.7)	(4.9)	(2.8)	0.8
Accelya Kale	21.1	18.9	20.9	14.5
MPS	6.2	7.6	-5.6	-19.8
Majesco	-5.0	6.0	44.1	NA

Research Analysts	
Abhishek Shindadkar	abhishek.shindadkar@icicisecurities.com
Tushar Wavhal	Tushar.wavhal@icicisecurities.com

**Exhibit 1: Client profile by Tier**



*For Guidewire Direct written premium (DWP) range is \$300 million to < \$1 billion, and < \$ 300 million. Source: Company, ICICIdirect.com Research*

## Financial summary

Profit and loss statement		₹ Crore			
(₹ crores)	FY15	FY16E	FY17E	FY18E	
Net Sales	493.6	690.0	820.0	973.0	
Growth (%)	NM	39.8	18.8	18.7	
Total Operating Expenditure	491.7	684.0	770.0	853.1	
EBITDA	2.0	6.0	50.0	120.0	
Growth (%)	NM	207.1	733.7	139.9	
Depreciation & Amortization	17.6	19.3	23.0	28.0	
Other Income incl interest income	6.4	11.0	13.0	14.0	
Interest costs	(1.4)	(3.0)	(4.0)	(4.0)	
PBT before Exceptional Items	(9.2)	(2.3)	40.0	106.0	
Growth (%)	NM	(74.8)	LP	165.0	
Tax	7.9	(14.6)	12.0	32.0	
PAT before Exceptional Items	(1.3)	(16.9)	52.0	138.0	
Exceptional items	(9.5)	(4.5)	-	-	
PAT before MI	(26.6)	7.7	28.0	74.0	
Minority Int & Pft. from associates	(7.8)	2.7	7.0	14.0	
PAT	(18.8)	5.0	21.0	60.0	
Growth (%)	NM	(126.8)	316.5	185.8	
EPS	(8.3)	2.2	9.2	26.2	
EPS (Growth %)	NM	LP	316.5	185.8	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
(₹ crores)	FY15	FY16E	FY17E	FY18E	
Net profit before Tax	2	(7)	40	106	
Depreciation & Amortization	18	19	23	28	
WC changes	5	(38)	(4)	(8)	
Other non cash adju.	(3)	(5)	(5)	(6)	
Income taxes paid	(6)	15	(12)	(32)	
CF from operations	16	(16)	42	88	
Capital expenditure	0	0	0	0	
Δ in investments	(69)	(17)	(18)	(20)	
Other investing cash flow	-	-	-	-	
CF from investing Activities	(69)	(17)	(18)	(20)	
Issue of equity	-	-	-	-	
Δ in debt funds	19	53	-	-	
Dividends paid	-	-	-	-	
Other financing cash flow	-	(3)	(4)	(4)	
CF from Financial Activities	27	47	(11)	(18)	
Δ in cash and cash bank balance	(35)	14	13	50	
Effect of exchange rate changes	(36)	14	13	50	
Opening cash	0	93	107	120	
Other cash adjustments	87	-	-	-	
Closing cash	93	107	120	170	

Source: Company, ICICIdirect.com Research

Balance sheet		₹ Crore			
(₹ crores)	FY15	FY16E	FY17E	FY18E	
Equity	11	11	11	11	
Reserves & Surplus	259	267	295	369	
Networth	270	278	306	380	
Minority Interest	35	32	25	11	
LT liabilities & provisions	51	104	104	104	
Source of funds	356	414	435	495	
Net fixed assets	229	235	239	241	
Deferred tax assets (net)	7	7	7	7	
Long term loans and advances	2	2	2	2	
Other non current assets	0	0	0	0	
Loans and advances	8	11	23	33	
Inventories	-	-	-	-	
Current Investments	-	-	-	-	
Debtors	51	90	98	107	
Cash & Cash equivalents	93	107	120	170	
Other current assets	43	45	53	63	
Current liabilities	74	72	93	111	
Provisions	6	14	16	19	
Net current assets	115	167	184	243	
Application of funds	356	414	435	495	

Source: Company, ICICIdirect.com Research

Key ratios		(Year-end March)			
	FY15	FY16E	FY17E	FY18E	
Per share data (₹)					
EPS-diluted	(8.3)	2.2	9.2	26.2	
Cash per share	40.7	46.8	52.5	74.4	
BV	118.2	121.6	133.8	166.2	
DPS	17.0	-	-	-	
Operating Ratios (%)					
EBITDA Margin	0.4	0.9	6.1	12.3	
Adjusted PBT Margin	(1.9)	(0.3)	4.9	10.9	
Adjusted PAT Margin	(0.3)	0.7	2.6	6.2	
Return Ratios (%)					
RoNW	NM	1.8	7.2	17.5	
RoCE	NM	NM	6.4	19.8	
RoIC	NM	NM	9.6	29.6	
Valuation Ratios (x)					
P/E	(68.1)	NM	61.7	21.6	
EV / EBITDA	627.1	204.2	24.5	10.2	
Price to Book Value	4.8	4.7	4.2	3.4	
EV/Total Revenues	2.5	1.8	1.5	1.3	
MCap/Total Revenues	2.6	1.9	1.6	1.3	
Turnover Ratios					
Debtor days	23	30	37	41	
Creditors days	13	7	1	1	
Solvency Ratios					
Total Debt / Equity	0.0	0.1	0.1	0.1	
Current Ratio	3.2	2.4	3.0	2.7	
Quick Ratio	3.2	2.4	3.0	2.7	
Debt / EBITDA	0.0	3.2	0.4	0.2	

Source: Company, ICICIdirect.com Research

## **RATING RATIONALE**

ICICIdirect.com endeavours to provide objective opinions and recommendations. ICICIdirect.com assigns ratings to its stocks according to their notional target price vs. current market price and then categorises them as Strong Buy, Buy, Hold and Sell. The performance horizon is two years unless specified and the notional target price is defined as the analysts' valuation for a stock.

Strong Buy: >15%/20% for large caps/midcaps, respectively, with high conviction;

Buy: >10%/15% for large caps/midcaps, respectively;

Hold: Up to +/-10%;

Sell: -10% or more;



**Pankaj Pandey**

**Head – Research**

**pankaj.pandey@icicisecurities.com**

**ICICIdirect.com Research Desk,  
ICICI Securities Limited,  
1st Floor, Akruiti Trade Centre,  
Road No 7, MIDC,  
Andheri (East)  
Mumbai – 400 093  
research@icicidirect.com**

## ANALYST CERTIFICATION

We /I, Abhishek Shindadkar, MBA, Tushar Wavhal, MBA, Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

### Terms & conditions and other disclosures:

ICICI Securities Limited is a Sebi registered Research Analyst having registration no. INH000000990. ICICI Securities Limited (ICICI Securities) is full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products. ICICI Securities is a wholly-owned subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on [www.icicibank.com](http://www.icicibank.com)

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities generally prohibits its analysts, persons reporting to analysts and their relatives from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts have any material conflict of interest at the time of publication of this report.

It is confirmed that Abhishek Shindadkar, MBA, Tushar Wavhal, MBA, Research Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities are engaged in various financial service businesses, they might have financial interests or beneficial ownership in various companies including the subject company/companies mentioned in this report.

It is confirmed that Abhishek Shindadkar, MBA, Tushar Wavhal, MBA Research Analysts do not serve as an officer, director or employee of the companies mentioned in the report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.