

September 6th, 2014

BSE Code: 532129 NSE Code: HEXAWARE Reuters Code: HEXT.NS Bloomberg Code: HEXW:IN

Hexaware technologies Ltd (Hexaware), founded in 1990, is engaged in the business of information technology consulting, software development and business process outsourcing. While focusing on key domains like Banking & Financial Services, Travel & Transportation, Insurance & Healthcare and Manufacturing & Services, the company delivers business results and leverage technology solutions by specializing in Business Intelligence & Analytics, Enterprise Solutions, Quality Assurance and Testing Services, Remote Infrastructure Management Services and Business Process Services. Hexaware has a well-established global delivery model armed with proven proprietary tools and methodologies, skilled human capital and SEI CMMI-Level 5 certification. Internationally, the company has its footprints in American, European and Asia-Pacific markets.

Investor's Rationale

Revenue to grow at a CAGR of ~21.9% over CY12-CY15E – We expect Hexaware's revenue to grow by ~18% YoY in CY14E as well as in CY15E backed by healthy growth across its business verticals. PAT is likely to grow by 5.7% in CY14E and by 16.9% YoY in CY15E. EBITDA margin is expected to remain in the current range of ~20-21% as higher proportion of onsite revenue limits any improvement in the margins.

Sees potential in Banking & Financial services space – During Q2CY14, Hexaware posted healthy numbers, with a growth of 13.8% YoY in consolidated revenues at ₹2,109.7 mn. The growth in revenues was majorly contributed by its Banking & Financial Services (contributed ~34.6% to the total revenue) and Travel & Transportation (contributed ~19.2% of the total revenue) business verticals. The management sees great potential in the Banking & Financial services segment as foray into European market, healthy deal pipeline and promising customer base enhances the outlook of the given vertical, thereby strengthening the overall outlook for the company.

Healthy deal pipeline – The company has 2-3 large deals in the pipeline for which it is competing and is hopeful of sealing at least one in Q3CY14. Apart from this large deals, there are two deals which are in progress and two for which request for proposal have been made. With the sealing of these deals in hand, we expect the company's revenue to improve substantially in the coming quarters.

Revenue growth momentum expected to continue in Q3CY14 – We expect the company to sustain the growth momentum in Q3CY14 driven by healthy deal pipeline and addition in the client-base. Considerable investments have been made in marketing which will start showing results in Q3CY14. Therefore, the company is likely to post much improved results in the near-term.

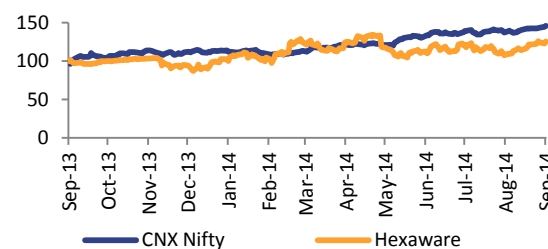
Market Data

Rating	BUY
CMP (₹)	170
Target (₹)	205
Potential Upside	~20.7%
Duration	Long Term
Face Value (₹)	2.0
52 week H/L (₹)	180/109.5
Adj. all time High (₹)	170
Decline from 52WH (%)	5.7
Rise from 52WL (%)	55.1
Beta	1.2
Mkt. Cap (₹bn)	51.1
Enterprise Value (₹bn)	48.1

Fiscal Year Ended

Y/E	CY12A	CY13A	CY14E	CY15E
Revenue (₹bn)	19.5	22.9	27.0	31.8
EBITDA (₹bn)	3.9	4.8	5.4	6.4
Net Profit (₹bn)	3.3	3.8	4.0	4.7
EPS (₹)	10.9	12.6	13.3	15.6
P/E (x)	15.6	13.5	12.8	10.9
P/BV (x)	4.2	4.3	4.2	4
EV/EBITDA (x)	12.5	10.0	9.0	7.6
ROCE (%)	32.3	38.4	42.2	46.3
ROE (%)	27.2	31.6	33.1	36.2

One year Price Chart



Shareholding Pattern

Shareholding Pattern	Jun'14	Mar'14	Diff.
Promoters	63.8	63.8	-
FII	15.7	16.1	(0.4)
DII	2.2	2.5	(0.3)
Others	18.3	17.6	0.7

Hexaware provides cutting edge solutions to small, large & fortune 500 companies across the globe while operating through five main verticals, namely, Banking & Financial Services, Travel & Transportation, Insurance & Healthcare and Emerging segments.

As in FY13, revenue from America contributed ~66.4% to the total revenue, while Europe and Asia-Pacific contributed ~27.1% and ~6.5%, respectively.

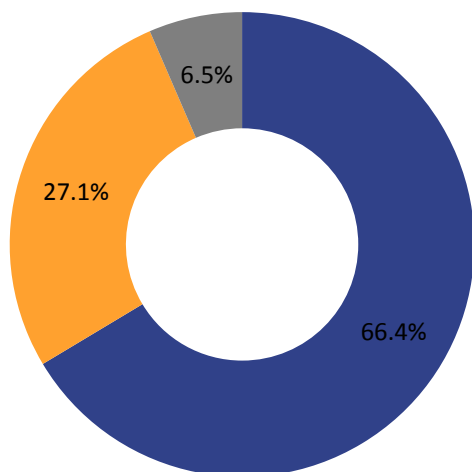
Hexaware Technologies Ltd - a leading global provider of IT, BPO and consulting services

Established in 1990, Hexaware Technologies Ltd (Hexaware) was incorporated as a public limited company under the name, Aptech Information Services Ltd. With a revenue of ₹22,853.5 mn (as on 31st December 2013), Hexaware is a global provider of information technology (IT), business process outsourcing (BPO) and consulting services. The company provides cutting edge solutions to small, large & fortune 500 companies across the globe while operating through five main verticals, namely, Banking & Financial Services, Travel & Transportation, Insurance & Healthcare and Emerging segments. Hexaware is very well focused on delivering business results and leveraging technology solutions by specializing in six service lines, namely, Application development & Maintenance (ADM), Business Intelligence & Analytics (BIA), Enterprise Solutions (ES), Quality Assurance and Testing Services (QATS), Remote Infrastructure Management Services (RIMS) and Business Process Management (BPM). The company has a well-established global delivery model armed with proven proprietary tools and methodologies, skilled human capital and SEI CMMI-Level 5 certification.

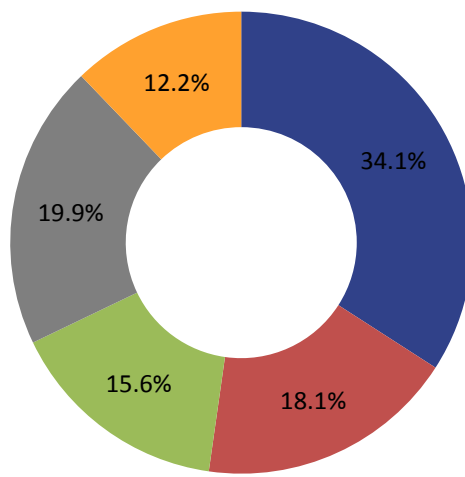
While maintaining six state-of-the-art development centers, four in Indian and one each in Germany and Mexico, Hexaware has expanded its footprints to North America, Europe and Asia Pacific. As in FY13, revenue from America contributed ~66.4% to the total revenue, while Europe and Asia-Pacific contributed ~27.1% and ~6.5%, respectively. During the year, the company added 48 new clients across all our key focus areas, taking the total client count by the end of 2013 to 233. On a quarterly basis, the company added 13 new clients in Q2CY13. With a significant addition in client base and expanded footprints in the overseas market, the company is well placed among its peers in the industry.

Revenue break-up as in CY13 (Consolidated)

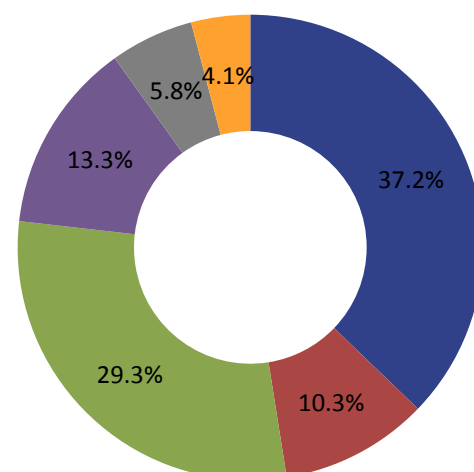
Geography split



Vertical split



Horizontal split



■ America ■ Europe ■ Asia-Pacific

■ Banking & Financial services
■ Travel & Transportation
■ Insurance & Healthcare
■ Manufacturing & services
■ Others

■ ADM ■ BIA ■ ES
■ QATS ■ RIMS ■ BPM

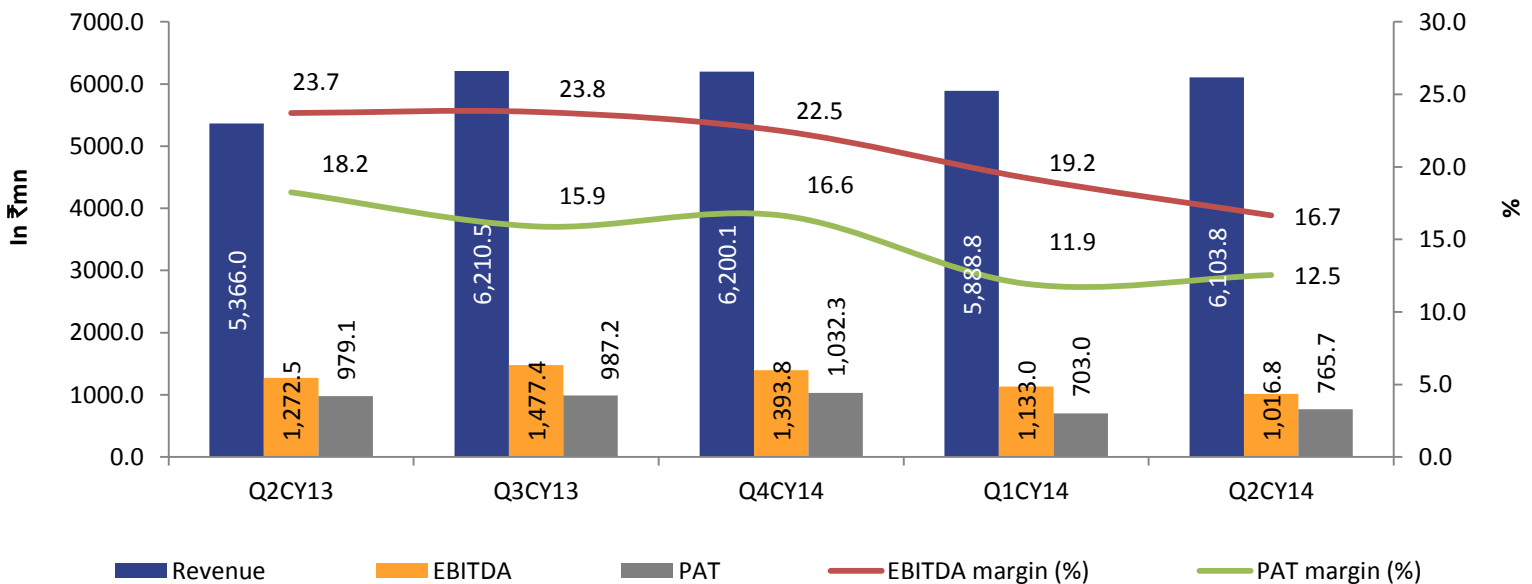
Upbeat revenue numbers in Q2CY14 while the margins disappointed; Outlook for Banking & Financial space remains positive

While the consolidated revenue grew by 13.8% YoY to ₹6,103.8 mn in Q2CY14, PAT declined by 21.8% YoY to ₹765.7 mn.

EBITDA fell by 20.1% YoY led by the H1B visa costs and selling/general & administrative (SGA) expenses.

Hexaware registered a healthy growth in its consolidated revenue by 13.8% YoY to ₹6,103.8 mn led by growth across Travel and Transportation (contributed ~19.2% to the total revenue in Q2CY14) and Banking & Financial Services business verticals (contributed ~34.6% to the total revenue in Q2CY14). Revenue from Travel and Transportation and Banking & Financial Services businesses grew by 6.5% and 6.3% YoY to ₹1,173.7 mn and ₹2,109.7 mn, respectively. However, EBITDA slipped sharply by 20.1% YoY to ₹1,016.8 mn on account of an increase in operating expenses by 24.3% YoY to ₹5,087.1 mn, resulting in a decline in EBITDA margin by 706bps YoY to 16.7% as against 23.7% in the corresponding period a year earlier. The decline was largely led by the H1B visa costs and selling/general & administrative (SGA) expenses which grew by nearly 42% in Q2CY14. The SGA has gone up primarily due to the recruitment cost of the advisory firm, reversal of certain provisions, including debtors and other provisions (one-time cost) and investments made in marketing. Net profit fell by 21.8% YoY to ₹765.7 mn due to a massive rise in interest cost by 67.2% YoY to ₹0.1 mn.

Quarterly performance trend



Healthy order pipeline and promising customer base enhance the outlook of Banking & Financial services vertical, thereby strengthening the overall outlook for the company.

ADM, the major contributor to the total revenue (~36.9%), registered a growth of 7.3% QoQ.

Going forward, Hexaware believes that the Banking & Financial services vertical, the major contributor to the total revenue in Q2CY14, will continue to be the strongest and fastest growing vertical as the company plans to foray into this segment in Europe. European business contributed ~ 27.4% to the company's total revenue in Q2CY14. Foray in Banking & Financial services vertical will further strengthen its position in that market, thereby strengthening the overall outlook for the company

Growth remained broad-based across services - From a service line perspective, Application Development & Maintenance (ADM), which contributed ~36.9% to the total revenue base in Q2CY14, registered a growth of 7.3% QoQ in revenues in Q2CY14. Revenue from Remote Infrastructure Management Services (RIMS) and Business Process Management (BPM) grew the most, up by 29.4% and 14.9% QoQ, while contributing ~7.9% and ~4.1% to the total revenue in Q1CY14, respectively. The company's management is particularly enthused about

Revenue from RIMS and BPM grew by 29.4% and 14.9% QoQ, respectively.

BPO and RIMS, though they are relatively smaller in size. Besides, Enterprise Solutions (ES) and Business Intelligence & Analytics (BIA) posted a growth of 1.8% and 7.5% in revenue, respectively. Quality Assurance and Testing Services (QATS) / Testing was the only service line which saw a decline in revenue by 0.3% QoQ.

RIMS and BPO service-lines grew the most in Q2CY14

Services	Contribution to total revenue (%)	Growth QoQ (%)	4 quarter CAGR (%)
ADM	36.9	7.3	1.0
ES	28.4	1.8	1.3
QATS	11.8	(0.3)	(0.6)
BIA	10.9	7.5	3.6
BPM	4.1	14.9	0.6
RIMS	7.9	29.4	12.0

Revenue from America, Europe and Asia-Pacific grew by 7.1%, 3.8% and 10.8% QoQ, during Q2CY14.

Performance across geographies remained healthy - In terms of geographies, revenue growth was broad-based with all the three geographies registering an impressive growth: revenue from America grew by 7.1% QoQ, Asia-Pacific also continued to be strong registering a growth of 10.8% QoQ followed by a 3.8% rise in revenue from Europe. America, Asia-Pacific and Europe contributed ~64.9%, ~7.7% and ~27.4% to the total revenue in Q2CY14, respectively.

America remain the major contributor to total revenue among the geographies in Q2CY14

Geographies	Contribution to total revenue (%)	Growth QoQ (%)	4 quarter CAGR (%)
Americas	64.9	7.1	1.0
Europe	27.4	3.8	2.9
Asia-Pacific	7.7	10.8	5.8

Going ahead, the company's management remains optimistic for strong revenue traction in H2CY14 aided both by visibility of business within top clients as well as steps taken/investments made to stimulate growth.

During Q2CY14, revenue from the top 2-5 clients grew by 6.0% QoQ, while growing by 15.0% QoQ for top 6-10 clients.

The company's management remains optimistic for strong revenue traction in H2CY14 aided both by visibility of business within top clients as well as steps taken/investments made to stimulate growth.

Significant growth in income from top clients strengthens Hexaware's prospects

During Q2CY14, revenue from the top client grew by 1.2% QoQ following two consecutive quarters of decline. There was a healthy growth in income from the rest of the top clients with top 2-5 clients registering a growth of 6% QoQ in revenue, while top 6-10 clients posted a growth of 15% QoQ in revenue, during the quarter. It was quite encouraging that the growth outside the top clients was healthy as it indicated that the revenue growth will remain diversified, thereby making the company less prone to the challenges faced by the multiple clients in the top 5 or top 10. During the quarter, the company added 1 more client to its

client-base generating revenue over USD 20 mn while adding 3 clients each to the base generating revenue between USD 1 to 5 mn and over USD 1 mn.

Client data

Healthy growth across Top 2-10 clients

	Contribution to total revenue (%)	Growth QoQ (%)	4 quarter CAGR (%)
Top client	13.4	1.2	1.1
Top 2-5 clients (%)	24.0	6.0	1.7
Top 6-10 (%)	13.5	15.0	(1.1)

Client Size

Nos.	Q2CY13	Q3CY13	Q4CY13	Q1CY14	Q2CY14
More than USD 1 mn +	53	53	55	56	56
Between USD 1 to 5 mn	37	37	39	41	40
Between USD 5 to 10 mn	8	8	7	6	8
Between USD 10 to 20 mn	5	5	5	5	4
Over USD 20 mn	3	3	4	4	4

Hexaware added 13 new clients to its portfolio in Q2CY14: 8 from America, 3 from Europe and 2 from the APAC region.

Going ahead, we believe that the company will get a boost in its revenue-base following the addition of a number of clients which would translate into a strong revenue performance in H2CY14 and CY14 as a whole.

The company has two-three large deals in the pipeline and is expecting to close at least 1 in Q3CY14.

Client addition rate remains vibrant - Hexaware has always been consistent in adding new clients to its portfolio. The company added 13 new clients in Q2CY14; 8 from America, 3 from Europe and 2 from the APAC region. The company believes that out of these 13 clients there would be 3 to 4 customers which would be multi-million dollar account in the year ahead. From vertical perspective, of these 13, one client was added in the Healthcare & Insurance (H&I) Domain and 2 clients each were added in the Banking & Financial Services space and in the Travel and Transportation Vertical and 4 clients in the Manufacturing & Retail Vertical. From a horizontal service line perspective, 5 clients were added in Human Capital Space (Enterprise Solutions), 2 clients each in Business Intelligence and Business Analytics (BI/ BA) Horizontal and Business Process Services (BPS) and 1 client each in Quality Assurance and Testing Services (QATS) and Remote Infrastructure Management Services (Remote IMS) service line.

Going forward, we believe that the company will witness a boost in its revenue-base following the addition of a number of clients, which would translate into a strong revenue performance in H2CY14 and CY14 as a whole.

Strong deal pipeline to augment revenue growth going forward

Hexaware is likely to witness quite strong performance in Q3CY14 on the back of strong deal pipeline. The company has three large deals in the pipeline and is expecting to close at least one in Q3CY14. Along with this, Hexaware currently has two deals which are in process and there are other two, for which request for proposal have been made. Moreover, the company has made an investment of ₹200 mn in H1CY14 for building new facilities and has guided for a capex of ₹600 mn in H2CY14. **With strong pipeline and heavy spending on building capacities, we expect the company to earn higher returns, going forward.**

Eyes opportunities in the European market

Hexaware's European business which contributed ~27.4% to the total revenue in Q2CY14, showcased a growth of 3.8% QoQ in revenues. The company has a very good presence in the

As per our expectations, the company's investments and faith in European market may bring fruitful results as the company has already added 3 new clients to its account, thereby strengthening its client base in the region.

With new partnerships made in CY13, Hexaware is well placed to tap these opportunities in CY14 and in the years ahead.

Slowdown in any key account and failure to continue winning large deals are the key risks that could be faced by the company.

European market which it had strengthened over the years in the Benelux market. The Benelux market represents a union of states comprising three neighboring countries in midwestern Europe, namely, Belgium, the Netherlands and Luxembourg. Hexaware has decided to make more investments and focus on this particular region as its already strong presence and understanding of the nuances of working in that market will benefit the company to unleash new opportunities. Furthermore, Hexaware has forayed into Nordics in CY14 as the company believes that this market has a lot of opportunities that can be a source of good growth for the company. The Nordic countries consist of five countries, namely, Denmark, Finland, Iceland, Norway and Sweden.

We expect Hexaware's faith in European market may bring fruitful results as the company has already added 3 new clients to its account, thereby strengthening its client base in the region. Also, Hexaware has added sales people to increase its field presence in Europe and based on the pipeline it has, we believe, the European market will see a gradual but steady increase in revenues in the near-term.

New partnerships to sustain growth

During the year, the company has partnered with the US-based multinational computer technology corporation, Oracle to launch Oracle's PeopleSoft Test Framework (PTF) services, which allow customers to execute more tests with greater accuracy in a shorter time frame, and enable significantly reduced operational costs. With this offering, Hexaware will not only save money for its clients by helping to eliminate unnecessary and redundant processes, but will also enable an enhanced time-to-market solution with Return on Investment (ROI) within just two test cycles. Also, the company has partnered with the leading provider of tools for mobile test automation, manual testing and monitoring, Experitest. Experitest will help Hexaware to enhance its mobile automation delivery capabilities to meet the client's needs. With this partnership, Hexaware is now well equipped to keep up with the dynamics of technology in mobile test automation, and extend its model to include additional mobility test imperatives like device-level performance testing as a by-product of test automation. ***With new partnerships made in CY13, Hexaware is well placed to tap these opportunities in CY14 and in the years ahead.***

Key Risks

- ✓ ***Slowdown in revenue from any of its top client accounts could impact the revenue growth*** - The company's top customers, which represent a good chunk of its overall revenue, are responsible for both the good times as well as the bad ones. Any decline in revenue income from these accounts can limit the profitability to a greater extent.
- ✓ ***Failure to continue winning large deals could hurt growth*** - Any failure in winning new contracts can have a significant impact on the company's profitability. However, Hexaware is making continuous efforts to win more deals. Currently, the company has three large deals that are active; there are a couple of more which are at early stages of development.
- ✓ Volatility in Exchange rates can have adverse impact on profitability as the company operates across various countries like America, Europe and Asia-Pacific.

Balance Sheet (Consolidated)

Y/E (₹mn)	CY12A	CY13A	CY14E	CY15E
Share Capital	593.1	599.8	599.8	599.8
Share Capital money pending allotment	0.4	0.9	0.9	0.9
Reserves & Surplus	11,445.1	11,391.9	11,522.5	12,331.3
Deferred tax liability (net)	130.5	275.5	275.5	275.5
Provisions	1,250.2	3,780.3	4,460.7	5,263.6
Other long term liabilities	77.6	9.2	11.0	13.0
Current liabilities	2,287.8	2,254.1	2,660.0	3,138.9
Total equity & liability	15,784.7	18,311.7	19,530.4	21,623.0
Fixed assets	5,199.4	5,370.8	5,821.4	6,234.1
Investments	2,354.4	3,382.6	3,990.7	4,708.2
Deferred tax assets (net)	203.6	227.3	227.3	227.3
Loans & adv.	1,597.5	1,774.1	2,067.7	2,421.3
Cash & Cash equivalents	1,969.0	3,010.5	2,072.8	1,734.1
Other non-current assets	170.0	176.7	194.4	213.8
Other current assets	4,290.8	4,369.6	5,156.1	6,084.2
Total assets	15,784.7	18,311.7	19,530.4	21,622.9

Key Ratios (Consolidated)

Y/E	CY12A	CY13A	CY14E	CY15E
EBITDA Margin (%)	20.2	21.0	20.0	20.0
EBIT Margin (%)	20.7	21.0	19.8	19.6
NPM (%)	16.8	16.6	14.9	14.7
ROCE (%)	32.3	38.4	42.2	46.3
ROE (%)	27.2	31.6	33.1	36.2
EPS (₹)	10.9	12.6	13.3	15.6
P/E (x)	15.6	13.5	12.8	10.9
BVPS(₹)	40.0	39.8	40.3	42.9
P/BVPS (x)	4.2	4.3	4.2	4.0
EV/Operating Income (x)	2.5	2.1	1.8	1.5
EV/EBITDA (x)	12.5	10.0	9.0	7.6

Profit & Loss Account (Consolidated)

Y/E (₹mn)	CY12A	CY13A	CY14E	CY15E
Revenue	19,481.8	22,853.5	26,967.1	31,821.2
Operating Expenses	15,554.7	18,043.2	21,570.9	25,456.9
EBITDA	3,927.0	4,810.3	5,396.3	6,364.2
Other Income	438.3	372.7	372.7	372.7
Depreciation	324.1	386.0	424.6	488.3
EBIT	4,041.2	4,797.0	5,344.3	6,248.6
Interest	1.6	2.0	-	-
PBT	4,039.6	4,795.0	5,342.3	6,246.6
Tax	763.1	1,003.6	1,333.6	1,559.6
PAT	3,276.5	3,791.4	4,008.3	4,686.5

Valuation and view

Hexaware Technologies is expected to grow at a CAGR of ~21.9% over CY12-CY15E on the back of strong growth across its different business verticals. The company has a healthy deal pipeline, which will improve its revenue-base in CY14 and in the years ahead. With the addition of 13 new clients to its client-base, Hexaware is now expected to post another good quarter in the coming time soon.

At a current market price (CMP) of ₹169.8, the stock trades at a P/E of 12.8x CY14E and 10.9x CY15E. We recommend 'BUY' with a target price of ₹205, which implies potential upside of ~20.7% to the CMP from long term perspective.



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