

20 February 2020

## Cyient Ltd.–BUY

**CMP** :Rs.442  
**Target Price** :Rs.552.0  
**Upside** : 24%+  
**Stop Loss** :Rs.396 (Closingbasis)

### Investment Thesis

Recently, the stock price of Cyient Ltd.(Cyient) corrected by ~34% from 52-week high of Rs.694.00 as the company reported lower-than-expected revenue growth in the recent quarters.

Cyient is one of the leading players in the IT enabled services, providing services to the Engineering Research and Development (ER&D) segment, which generates ~65% of revenue. Cyient has been instrumental in providing services to Aerospace and defence segment which has been reporting soft set of numbers since last 2 quarters due to client specific concerns. Both the verticals, Aerospace & defence and communication is expected to show growth powered by improvement in client spending, after sales services and 5G deployment. Transportation segment is also expected to improve in the coming quarters as new orders start coming in. Growth in ER&D spends across the globe and in key services like aerospace and defence, communication and healthcare to propel order intake and improve revenue of Cyient from FY21E onwards.

Cyient has set a long-term vision and aspires to be an IP solution provider by 2030. The company is planning to change IP solution/services ratio from the current 10:90 levels to 80:20 by the end of year 2030. Largely aligned to the S3 strategy, Cyient is aiming to enhance growth by bringing new domain expertise and strengthening the presence in emerging technology. The company has done two key acquisitions in 2018 namely B&F Design Inc and AnSem N.V. B&F Design Inc; is a Connecticut based tooling and precision engineering company that focuses on the aerospace and defence Industry. They expertise in design and manufacturing of engine assembly equipment repair and tooling and precision engineering where as AnSem N.V specializes in advance analog, radio frequency and mixed- signal integrated circuit design.

### Financials

- During the past 5 years, revenue of Cyient grew at a CAGR of 15.9% while PAT grew at a CAGR of 12.5% in the same period.

Consol. (Rs.Mn.)	FY17	FY18	FY19	FY20E	FY21E
Revenue	35,858	39,139	46,175	53,101	61,066
EBITDA	4,635	5,354	6,139	7,060	8,119
% growth	12.9	15.5	14.7	15.0	15.0
PAT	3,438	4,054	4,785	5,512	6,345
EPS (INR)	30.5	36.0	43.3	49.9	57.5
P/E (x)	15.1	12.8	10.6	9.2	8.0
RoE (%)	15.9%	17.0%	18.7%	19.6%	20.6%

- Cyient has reported 4.6% QoQ and 6.9% YoY de-growth in revenue to Rs.11,059mn led by delay in deals and demand in Aerospace vertical shifted towards MRO and new product development in Q3FY20.

### Stock Data

Market Cap (Rs. Mn)	51,386
Market Cap (\$ Mn)	721.7
Shares O/S (in Mn)	110.4
Avg. Volume (3 month)	1,70,000
52-Week Range (Rs.)	693.8/ 380.0

### Shareholding Pattern

Promoters	22.82%
FII's	44.31%
Institutions	20.93%
Others (incl. body corporate)	11.94%

Performance (%)	1M	6M	1Yr
Absolute	9.1%	-0.1%	-23.3%
BSE 500	1.4%	2.7%	7.9%

### Key Ratios

Div Yield	3.2%
TTM PE	10.8x
ROE	18.4%
TTM EPS (Rs.)	42.6/-

- Geography-wise APAC (17% of revenue of Cyient) grew 17.5% QoQ whereas EMEA (26% of topline) and America (58% of revenue) reported a de-growth of -8.4% QoQ and -9.7% QoQ respectively. Whereas, Services (90% of revenue) was largely flat during Q3FY20 with while DLM (10% of revenue) de-grew by -36% QoQ.
- EBITDA of Cyient declined by 5.1% QoQ and 12.6% YoY to Rs.1,522mn in Q3FY20 led by higher onsite deployment in aerospace vertical and investments in cost optimization initiatives. As a result, EBITDA margin also impacted by 7bps QoQ and 90bps YoY to 13.8% in Q3FY20.

## Key Business Highlights

- Cyient is IT engineering focused company engage in engineering, Manufacturing, data analytics and networks & operations. It derives 89% of its revenues from IT Engineering services and 11% from Design Led Manufacturing services.
- Cyient has over 15,000 employees across 21 global locations. Its global workforce span across three major regions: Asia Pacific (84%), North America (12%), and Europe, Middle East and Africa (4%).
- Cyient offered Geographic information, i.e. Mapping services which is largely design services and company has evolved from a pure engineering design firm to manufacturing and MRO (Maintenance, Repair and Overhaul) company.

## Valuation

- Dollar revenue growth of Cyient was pretty volatile from FY11 to FY16. Looking at the FY14 trend, that was the time when company did a rebranding exercise, Cyient took a comprehensive strategy development exercise with an objective to prepare ground for accelerated growth for upcoming years. Steps taken included, alignment of sales by geography and investment in sales and marketing that yielded higher sales in Dollar terms in FY15. Cyclical nature in the Design Led Manufacturing (DLM) business impacted growth in FY16. However, with current order intake stand at US\$274mn across segments, we expect the revenue growth trend from FY19 to continue further lead by growth in key verticals.
- Cyient has initiated a cost optimization program to achieve sustainable margins for the services business. The move is largely to curtail sales and administrative expenses and boost margins. We believe the cost optimization program to end in Q4FY21E, till the time improvement in margins due to a fall in sales expenses will be impacted by higher wage cost and one-time restructuring cost. Cyient also plans to continue to invest in projects which is expected to add to the revenue in the near term. Investment in new business accelerator program, which is an in-house investment vehicle created to provide end to end solution to clients is one among the major project of Cyient. In addition to that the acquisitions in the recent past like Ansem which is a 20% margin business is expected to aid EPS growth in the tune of 1.5%-3% by FY 21E.
- With one of the leading players in ER&D segment, aspires to be an IP solution provider, strong order intake gives revenue visibility and initiated a cost optimization program to achieve sustainable margins, we value Cyient at 9.6x FY21E EPS of Rs.57.50 to arrive at target price of Rs.552.00, an upside of ~20%.

## Risk & Concern

- Any client specific issues or cancelation of any client may lead to decline in revenue growth of Cyient.
- Global companies are setting up its captives in India for R&D engineering work, which may adversely impact growth of Cyient.
- Any inadequate hedging and risk arising owing to adverse currency fluctuations may impact margin of Cyient.

## Graphs & Charts

Figure 1: Net Sales Trend

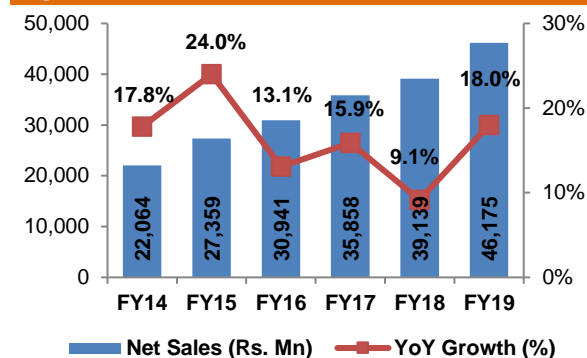


Figure 2: EBITDA & EBITDA Margin Trend

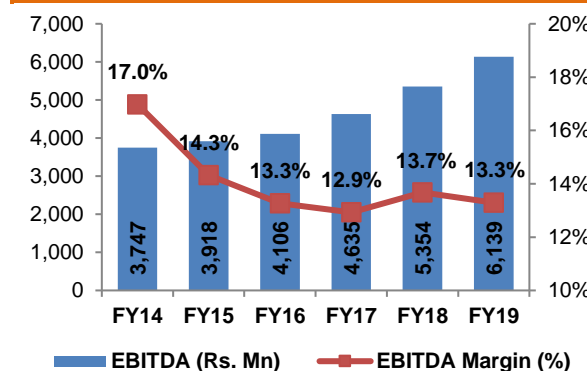


Figure 3: PAT Trend

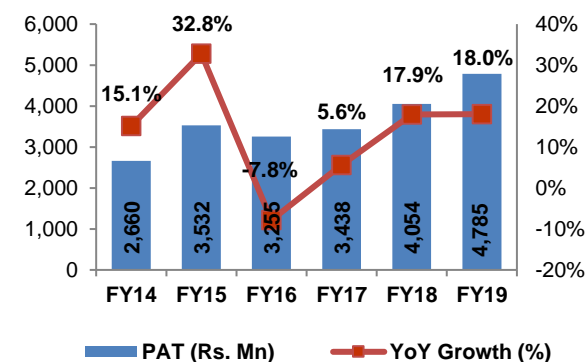
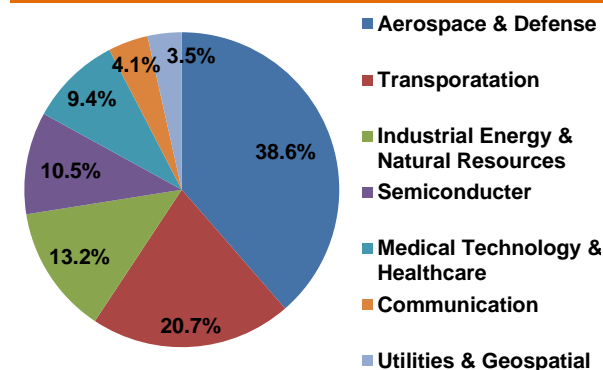


Figure 4: Vertical-wise Revenue (FY19)



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