Happiest Minds Technologies Ltd

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COMPANY PROFILE

Happiest Mind Technologies Ltd was incorporated in 2011 and promoted by Mr Ashok Soota. Prior to incorporating Happiest Mind Mr. Soota was Founding Chairman and Managing Director of Mindtree Ltd. Positioned as "Born Digital. Born Agile", the company's focus is on delivering a seamless digital experience to its customers.

The company has three business units – Digital Business Services (DBS), Product Engineering Services (PES) and Infrastructure Management & Security Services (IMSS). These are supported by three Centres of Excellence (COE) – Internet of Things (IoT), Analytics/Artificial Intelligence (AI) and Digital Process Automation (DPA).

97% of the company's revenues are classified as digital, compared to 35-50% for traditional Indian IT services. The company offers services such as Digital Infrastructure/Cloud, Saas, Security Solutions, Analytics/AI and IoT.

Since inception the company has focused on software product development, refined through repeat, multi year engagements with Independent Software Vendors (ISV) such as Microsoft, Amazon Web Services (AWS), Salesforce, Pimcore etc. This has enabled it to grow its business in multiple industries, including Edutech, HiTech, Industrial/Manufacturing, BFSI and Retail.

As of June 2020, the company had 148 active customers and 2,658 employees including 189 contract workers. The company's repeat business has steadily grown and contributed a significant portion to the total revenues over the years indicating a high degree of customer stickiness.

The company has delivered 90% and 88% of its projects during 1QFY21 and FY20 via agile delivery methodology. The company has successfully implemented business continuity plans during the COVID – 19 pandemic through its agility and resilience developed over the years.

OBJECTS OF THE ISSUE

- The company proposes to utilize Rs 101cr from the net proceeds towards meeting the working capital requirement.
- General corporate purposes

BRIEF FINANCIAL DETAILS

Particulars (Rs Cr)	FY18	FY19	FY20	1QFY21
Revenue	463	590	698	177
Total Expenditure	482	536	601	139
EBITDA	-19	55	97	38
EBITDA Margin	-4%	9%	14%	21%
Other Income	26	11	16	10
Finance Cost	10	16	8	2
Depreciation	21	25	20	5
PBT	-23	26	85	41
Impairment of Goodwill	-	13	11	-
Tax Expense	-1	-1	2	-9
PAT	-22	14	72	50
Adj. PAT	-22	27	83	50
EPS (Rs/Share)	-3.1	1.2	5.4	3.7
Adj EPS	-3.1	2.2	6.2	3.7
ROE %	-	-	27.1	-

Particulars	
Issue Size (Rs Cr)	698 – 702
Price Band	165 – 166
Issue Open Date	07 Sep 2020
Issue Closing	09 Sep 2020
Face Value (Rs)	2
Lot Size	90

Issue break-up	(%)
QIB	75
NIB	15
Retail	10

Shareholding Pattern (Pre Issue)	(%)
Promoters & Promoters Group	61.77
Others	38.23

Book Running Lead Managers

ICICI Securities, Nomura Financial

Issue Details

Fresh Issue of Equity shares aggregating upto Rs 110 Cr and Offer for sale of up to 35,663,585 Equity Shares.

Brief overview of the Tech industry

Global overview

According to Frost & Sullivan the global tech spending is estimated to register a CAGR of 6% during 2019-2025 reaching USD 6,080bn. The accelerated spending on emerging technologies and the increase in the technology product mix within organisations that have conventionally invested in non-IT solutions are key reasons for the projected market growth. Digitisation and connectivity has created opportunities for service providers to focus more on R&D and consequentially created a demand within the software space, which is expected to increase going forward. Globally legacy IT services is estimated to report CAGR of 2% compared to 20% for digital during 2018-2025.

The increasing utilisation of robotic process automation (RPA) in business process integration is expected to deliver a healthy growth of the segment that is projected to reach a market size of over USD 7bn by 2025, growing at a CAGR of 25% respectively.

According to Frost & Sullivan during 2019-2025, AI & machine learning, Blockchain, Cyber-security, Cloud computing & related services and IoT segment are expected to grow at compounded rate of 55%/80%/14%/21%/14%.

Globally the spending on the system integration segment is expected to witness relatively higher growth as compared to the other segments of IT services owing to the need for bundled offerings, security concerns and advanced solutions that has led to a higher bargaining power of the system integrators. This segment is expected to grow at a CAGR of 12% from 2019 to 2025. Custom application development is also expected to see a healthy CAGR of 9% due to the increasing demand within the enterprise application development sector as well as from the mobile application development. Infrastructure services is expected to witness a drop in the overall spend owing to the projected investments in cloud services.

According to Frost & Sullivan during 2019-2025, tech spending by Global Edutech, BFSI, Manufacturing and Retail sector is expected to witness a CAGR of 5%/5%/3.5%/3.5% respectively.

Software and Engineering Research & Design (ER&D) services are expected to compound at 8% rate during 2019-2025.

The Global PES market is expected to witness a CAGR of 11% during 2019-2025

In 2019, the global enterprise digital spend stood at USD 691bn and represented about 16% of the total technology spend within the IT sector. By 2025, the enterprise digital spend is projected to be around 34% of the total technology spend.

Domestic overview

According to Frost & Sullivan during 2019-2025, Indian Digital services are expected to register a CAGR of 12% while legacy IT services is expected to report a CAGR of 3%. Spending on servers and storage is expected to decline. The cloud and SaaS market witnessed a CAGR of 12% from 2018 to 2020.

ER&D spend is core to a company and is part of its long-term strategy. It is anticipated that organisations will continue looking to invest in technology to make sure that they remain relevant in the long-term. Industry leaders believe that this is a critical time to focus on core-business and rethink strategic R&D investments to ensure organisations are better prepared to handle the post-COVID environment.

Customers may initiate plans to invest heavily on automating their back office and IT operations to reduce dependency on manual interventions. This may have some negative impact on commodity business for Indian IT companies. However, a focus on new automation projects may help to offset this impact.

India, being a traditionally recognised leader in the offshore outsourcing segment, is expected to benefit largely from opportunities that can stem from the outsourcing market owing to the COVID-19 crisis.

According to Frost & Sullivan during 2019-2025, Enterprise digital spend, PES and IMSS market is expected to register a CAGR of 20%/8%/10% respectively.

Domestic IT services is expected to have a growth rate of 6.3% with application development and system integration as major contributors to the growth of the segment.

Brief overview on Business Units (BU)

- Digital Business (DBS) Offerings are aimed at driving digital modernisation and transformation for to improve customer experience, enhanced productivity and better business outcomes. Implementation of solutions, capabilities for improving data quality of the customer's platform, assistance in designing and testing of operations and management of platform and modernisation of digital practices. The company also provides consulting and domain led offerings such as digital roadmap, mindful design thinking, and migration of on-premise applications to cloud under DBS.

The company has also created offerings in emerging technologies such as Blockchain, Drones & Robotics and Automation solutions.

- Product Engineering (PES) aims to help the customers capitalise on the transformative potential of 'digital' by building products and platforms that are smart, secure and connected. The company offers a blend of hardware and embedded software knowledge which combines with the software platform engineering skills provided by Happiest Minds to help create high quality, scalable and secure solutions. The offerings extend across the development lifecycle from strategy to final roll out while ensuring quality. The company embraces a cloud and a mobile friendly approach along with an agile model that is supported by test automation to help clients accelerate their time to market and build a competitive advantage.

The company also has engineered solutions that can be used as is by its customers as a part of their digital transformation such as Ellipse (AI enabled platform), Digital Content Monetisation (AI powered Engine), UniVu (Big Data based university analytics solution) and Pro-Rite (Test Automation framework)

- Infrastructure Management & Security Services (IMSS) offerings provide an end to end monitoring and management capability with secure ring fencing of customers' applications and infrastructure. The company provides continuous support and managed security services for mid-sized enterprises and technology companies. It strives to ensure that the data centre, cloud infrastructure and applications are safe, secure, efficient and productive. Its security offerings include cyber and infrastructure security, governance, risk & compliance, data privacy and security, identity and access management and threat and vulnerability management. The infrastructure offerings include DC and hybrid cloud services, workspace services, service automation (RPA, ITSM & ITOM), database and middleware services and software defined infrastructure services.

In 2017, Happiest Minds acquired OSSCube LLC and Cupola Technology Pvt. Ltd. to expand its DBS BU and IoT COE, respectively.

The company's core competency is full lifecycle software development services from roadmap to deployment and maintenance. It has developed experience in each of these areas by working collaboratively with partner ISVs and tech companies, creating a foundation for the evolution of its other offerings.

Multiple Business Units also help the company to cross-sell its solutions and services to existing customers. The company also helps its customers to prepare a digital roadmap for the transformation or upgrading their existing IT systems and implementing SaaS platforms. PES unit helps in building digital platforms. While IMSS offering covers various aspects of cloud lifecycle services catering to different infrastructure and security needs.

Brief overview on Centres of Excellence

- Internet of Thing (IoT) offerings includes consulting led digital strategy creation, device/edge/platform engineering, end-to-end system integration on industry standard IoT platforms, IoT security, and IoT enabled managed services, implementing IoT roadmap, deriving insights from connecting assets, connecting manufacturing, supply chain, products and services to deliver IoT led business transformation and new business models aimed at enhancing the customers' operations and customer experience.

In FY19 and FY20, revenues from IoT contributed 8% and 10%

- Analytics/AI offering includes implementation of advanced analytics using artificial intelligence, machine learning and statistical models, engineering big data platforms to deal with large volume of data, creating actionable insights with data warehousing, modernization of data infrastructure and process automation through AI.

In FY19 and FY20, revenues from Analytics/AI contributed 9.1% and 12%

- Digital Process Automation (DPA) offering includes consulting led digital transformation through process automation of core business applications, products and infrastructure landscape of the customers, leveraging various intelligent process automation tools and technologies including Robotic Process Automation (RPA), intelligent business process management (iBPMS) and cognitive automation using AI & machine learning based models.

In FY20, revenues from DPA contributed 21%

Financial Overview

During FY18-20, the Revenues for the company has registered a CAGR of 23%, while its EBIT margin improved from -9% to 11% and adjusted for impairment of goodwill net loss of Rs 23cr has grown to net profit of Rs 83cr in the same period. Free cash flows (FCFF) during FY18/FY19/FY20 stood at Rs 102cr/57cr/112cr. In FY20 FCFF stood at 136% of adj PAT. The company's cash balance (cash, liquid investments, fixed deposit and margin money) were Rs 328cr as of June 2020 and debt was Rs 76cr as of July 2020. For FY21 management will try to improve the EBITDA margin to 21-22% and EBIT margin to 18-19%. The carried forward tax loss will get exhausted in FY21 and management has guided for a Tax rate of 25% in FY22.

The workforce utilisation rate increased from 68% in FY18 to 77% in FY20

Business Highlight

Business Segment wise revenue

Revenue (Rs Cr)	FY18	FY19	FY20	CAGR FY18-20
Infrastructure Management & Security Services (IMSS)	99	129	154	25%
Digital Business Solutions (DBS)	154	181	192	12%
Product Engineering Services (PES)	210	280	353	30%
Total	**463**	**590**	**698**	**23%**

Source RHP

Segment wise contribution for PES, DBS, IMSS in FY20 was 22%/27%/51%

Digital Services wise revenue

				Contribution to total Rev	
Revenue (Rs Cr)	**FY19**	**FY20**	**Y-Y**	**FY19**	**FY20**
Digital infrastructure/Cloud	241	218	**-10%**	41%	31%
SaaS	169	205	**22%**	29%	29%
Security	60	104	**73%**	10%	15%
Analytics/	54	81	**51%**	9%	12%
IoT	50	68	**38%**	8%	10%
Total	**574**	**677**	**18%**	**97%**	**97%**

Source RHP

Digital revenues form 97% of total revenues, one of the highest in India.

Vertical wise revenues

Industry wise Revenues	FY18	FY19	FY20	CAGR FY18-20
Edutech	18%	21%	21%	34%
Hitech	25%	21%	21%	13%
BFSI	18%	18%	18%	22%
Travel, Media and Entertainment (TME)	11%	14%	17%	53%
Retail	7%	7%	8%	27%
Industrial	6%	8%	7%	31%
Manufacturing	3%	4%	4%	33%
Others	12%	7%	5%	-22%
Total	**100%**	**100%**	**100%**	**23%**

Source RHP

The 23% CAGR in revenues during FY18-20 has been led by TME

Experience with renowned ISVs and emerging innovative tech companies enabled to develop vertical specific domain knowledge.

Geography wise revenue contribution

Geography wise Revenue	FY18	FY19	FY20
USA	74%	76%	78%
India	12%	12%	12%
UK	11%	10%	7%
Others	3%	3%	3%

Source RHP

United States which has the majority market share of global technology spend is the largest contributor to topline

Number of customers based on quarter revenues on an annualized basis

No of Customers	FY18	FY19	FY20
USD 1 – 5 million	14	18	24
USD 5 – 10 million	2	2	-
More than USD 10 million	-	1	1
Total	**16**	**21**	**25**

Source RHP

Average revenue per customer reported CAGR of 14% during FY18-20 to USD 614,675 led by up-sell and cross-sell aided by the company's broad range of offerings

Revenue Mix

Revenue Mix	FY18	FY19	FY20
Onsite	21%	22%	23%
Offshore	79%	78%	78%

Source RHP

Offshore business is generally at a higher margin and scalable due to low personnel cost in India

Contract Structure

Contract Structure	FY18	FY19	FY20
Fixed Price	18%	17%	19%
Time and Material	82%	83%	81%

Source RHP

For digital projects, the share of time and material contracts tends to be greater as these projects are iterative in nature. Fixed cost contracts involve more financial risk comparatively

Impact of COVID – 19

The company already had an existing work-from-home (WFH) policy, information security policy as well as remote working tools (including MS Teams and Webex) and laptops available to most of our workforce. It also had business continuity plans and security systems in place as part of its normal operational readiness. As a result of which entire team was able to work from home from shortly after the onset of the pandemic in India.

According to the company, agile response and proactive steps taken have mitigated the impact of the Novel Coronavirus pandemic on the business and personnel thus far. A large part of the business comes from clients in sector that have not been immediately affected including Edutech, HiTech, retail, BFSI and manufacturing/industrials and the company has limited exposure in affected sector such as travel and tourism.

A substantial majority of the contracts are time and material based rather than fixed price which helps mitigate cost and completion risks. To manage costs the company has placed discretionary spends on hold, have reduced travel costs (including for visas) and utility costs. It has also renegotiated terms with its lenders. The company is negotiating some rate reductions with clients and also monitoring USD exchange rates, where INR depreciation has been favorable to thus far.

Risks

The company derives 48% of its revenues from its Top – 10 clients, while its top client contributes 12% of its revenues. The company is expanding its offerings and increasing its reach to mitigate this risk.

The volatility in currency might impact earnings. Company hedges part of its currency risk.

There is a shortage of employees skilled in emerging technologies. The company is providing an enabling environment to up-skill its existing employees and attract new talent.

There is a high competition in the sector with presence of established incumbents. However, the company is creating niche for itself by focussing on emerging technologies.

Political uncertainty regarding immigration laws in the US as the country contributed 78% of revenues as well as Global economic contraction could impact earnings and valuation of the entire sector going forward.

CONCLUSION

The company has registered good performance during FY18-20 with revenues witnessing CAGR of 23%, margin expansion and improvement in profitability. Considering free cash flow generating business with limited capital requirement and opportunities available in digital technologies space long term investors can consider subscribing to the issue.

Happiest Minds Technologies Ltd has priced its issue at Rs 165 - Rs 166 per share which is 26.8 times (at the upper price band) of its adjusted FY20 EPS of Rs 6.2 per share which is comparable to its larger midcap peers such as LTI, Mindtree and Coforge (NIIT Tech).

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