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FIRST LIGHT

23 October 2024

RESEARCH

SUPREME INDUSTRIES | TARGET: Rs 5,250 | +17% | BUY

Weak Q2; upgrade to BUY on reasonable valuations

KAJARIA CERAMICS | TARGET: Rs 1,450 | +13% | HOLD

Miss estimates on sharp margin contraction; maintain HOLD

PERSISTENT SYSTEMS | NOT RATED

Strong quarter both on revenue and margins

ZENSAR TECHNOLOGIES | NOT RATED

Unseasonal furloughs in TMT clients impacts revenue growth

SUMMARY

SUPREME INDUSTRIES

- Weak Q2 on destocking of pipe inventories in the channel in a falling resin price environment, and MTM inventory loss
- Guidance for volume revised down to 14-15% (vs 20%) and margin to 14.5-15.25% (vs 15.0-15.5%) for FY25 based on the weak Q2 result
- Upgrade to BUY from HOLD as valuation has now become reasonable on relative basis; cut TP by 3% to Rs 5,250

Click here **for the full report.**

KAJARIA CERAMICS

- Weak Q2 on sharp margin contraction due to high share of outsourced sales volume and high overhead costs of new commissioned units
- Guidance for volume growth revised down to 9-10% (vs 11-12%) and margin to 15% (vs 15-17%) for FY25 based on the weak Q2 result
- Maintain HOLD with unchanged TP of Rs 1,450 as the future earnings potential is well captured in the current valuation

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PERSISTENT SYSTEMS

- Met revenue estimate. But a beat on EBIT margin. Strong 1H and ACV should mean high teen revenue growth with flat EBIT margin vs FY24
- Reiterates US$2bn revenue/16.5%-17.5% EBIT margin by FY27. Believes platform-based approach and SGA leverage will drive margins.
- Likely to have among fastest earnings growth among >US$1bn revenue Indian IT services players. Will initiate coverage on company soon

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ZENSAR TECHNOLOGIES

- Weak QoQ growth due to client specific issues in TMT vertical whereas BFSI and HLS show good traction.
- Weaker Gross margin QoQ set off by lower SGA. Reiterates mid-teen EBITDA margin guidance.
- TCV clocked is the highest ever. And more of it is in the managed services type of work. Will be reinitiating coverage soon.

Click here **for the full report.**

BUY
TP: Rs 5,250 | ⮝ 17%

SUPREME INDUSTRIES | Building Materials | 22 October 2024

Weak Q2; upgrade to BUY on reasonable valuations

- **Weak Q2 on destocking of pipe inventories in the channel in a falling resin price environment, and MTM inventory loss**
- **Guidance for volume revised down to 14-15% (vs 20%) and margin to 14.5-15.25% (vs 15.0-15.5%) for FY25 based on the weak Q2 result**
- **Upgrade to BUY from HOLD as valuation has now become reasonable on relative basis; cut TP by 3% to Rs 5,250**

Utkarsh Nopany
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Weak Q2: SI missed our estimates (Revenue/EBITDA/APAT: -8%/-17%/-21%) driven by weak sales volume (+0.2% YoY vs +13.4% estimate) as well as lower EBITDA margin (-139bps YoY to 14.0% vs 15.5% estimate). Overall, SI's Revenue/EBITDA/APAT de-grew by 1.5%/10.4%/15.0% YoY in Q2FY25. However, SI EBITDA grew at a decent pace of 13% CAGR on a 5Y CAGR basis in Q2FY25.

Key highlights: Pipe volume was down 0.7% YoY (5Y CAGR: +8.6%) in Q2FY25 due to volatile resin prices, weak infra demand and extended monsoon. Pipe margin declined 142bps YoY/ 77bps QoQ to 14.9% in Q2FY25 due to (MTM) inventory loss and negative operating leverage. Non-pipe volume grew by 2.9% YoY (5Y CAGR: +6.9%) as increased packaging volume (+11.4%) more than offset the impact of weak sales volume of industrial (-2.0%) and consumer (-8.5%). However, non-pipe EBITDA margin contracted by 138bps YoY to 13.4% in Q2FY25.

Concall KTAs: The company revised down its consolidated/pipe volume growth guidance to +14-15% YoY (+20% earlier)/ +16-18% YoY (+25% earlier) for FY25 based on a weak H1FY25 performance. However, the company expects a good recovery in demand in H2FY25 due to stabilization of polymer prices. EBITDA margin guidance has also been lowered from the earlier 15.0-15.5% to 14.5-15.25% for FY25. The company expects its pipe segment margin to be 14-16% and packaging at 16-18% on a sustainable basis.

Upgrade to BUY, cut TP by 3% to Rs 5,250: We upgrade our rating to BUY from HOLD on strong business risk profile (EPS to grow at a healthy 20% CAGR over FY19-FY27E with an average ROIC profile of >40%) and valuation has now become reasonable in comparison to other leading building material companies. At CMP, the stock trades at 40.8x on 1Y forward P/E vs. 5Y average of 31.2x. We cut our TP to Rs 5,250 (Rs 5,400 earlier) due to the earnings downgrade (-4.7%/-1.8%/-1.8% for FY25E/FY26E/FY27E) based on a weak Q2FY25. Our target P/E remains unchanged at 45x on Sep'26 estimate (Jun'26 earlier).

Key changes

Target	Rating
▼	▲

Ticker/Price	SI IN/Rs 4,486
Market cap	US$ 6.8bn
Free float	51%
3M ADV	US$ 7.8mn
52wk high/low	Rs 6,460/Rs 3,601
Promoter/FPI/DII	49%/26%/11%

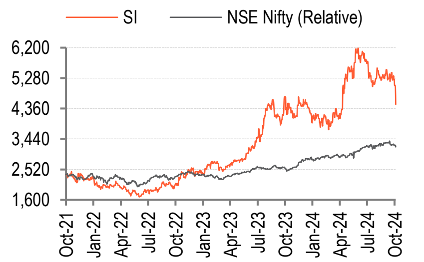
Source: NSE | Price as of 22 Oct 2024

Key financials

Y/E 31 Mar	FY24A	FY25E	FY26E
Total revenue (Rs mn)	101,343	115,667	137,249
EBITDA (Rs mn)	15,473	18,141	21,959
Adj. net profit (Rs mn)	10,697	12,521	15,012
Adj. EPS (Rs)	84.2	98.6	118.2
Consensus EPS (Rs)	84.2	101.9	121.1
Adj. ROAE (%)	22.5	22.7	23.3
Adj. P/E (x)	53.3	45.5	38.0
EV/EBITDA (x)	37.2	31.9	26.5
Adj. EPS growth (%)	23.6	17.0	19.9

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

RESULT REVIEW

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HOLD
TP: Rs 1,450 | ⮝ 13%

KAJARIA CERAMICS | Building Materials | 22 October 2024

Miss estimates on sharp margin contraction; maintain HOLD

- **Weak Q2 on sharp margin contraction due to high share of outsourced sales volume and high overhead costs of new commissioned units**
- **Guidance for volume growth revised down to 9-10% (vs 11-12%) and margin to 15% (vs 15-17%) for FY25 based on the weak Q2 result**
- **Maintain HOLD with unchanged TP of Rs 1,450 as the future earnings potential is well captured in the current valuation**

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Weak Q2: KJC's Q2FY25 result came below our expectation (Revenue: -2%; EBITDA: -13%; APAT: -23%) mainly due to the sharp contraction in EBITDA margin (-255bps YoY to 13.5% vs +15.1% estimate). Overall, KJC revenue grew by 5.1% YoY, but EBITDA/APAT de-grew by 11.6%/21.9% in Q2FY25. However, KJC EBITDA grew at a nominal pace of 8.6% on a 5Y CAGR basis in Q2FY25.

Key highlights: KJC gained market share as its tiles volume (+8.4% YoY) grew at a better pace than the industry (~2-3%) in Q2FY25. However, tile segment EBIT was down 9.7% YoY in Q2FY25 due to margin contraction (-207bps YoY to 12.0%) on account of higher outsourced sales volume mix and high overhead of the newly-acquired Keronite unit. Non-tile segment revenue de-grew by 1.1% YoY in Q2FY25 as weak plywood sales (-25.6%) more than offset the impact of increased sales of bathware (+5.7%)/adhesives (+39.4%). Non-tile segment reported EBIT loss of Rs 107mn in Q2FY25 (vs profit of Rs 7.3mn in Q2FY24) largely attributable to losses incurred in the recently commissioned sanitaryware unit in Morbi.

Guidance downgrade: The company has lowered its tiles volume growth guidance to 9-10% (+11-12% earlier) and consolidated EBITDA margin guidance is expected to be around 15% (15-17% earlier) for FY25. The company aims to bring down the net working capital from 59 days in Mar'24 to 50 days by Mar'25. Tiles realisation is expected to remain stable over the next two quarters. The company plans to spend Rs 2.0bn in FY25 (H1FY25: Rs 1.35bn).

Maintain HOLD with unchanged TP of Rs 1,450: We maintain our HOLD rating on the stock as we believe strong earnings growth prospects (EPS to grow at 14% CAGR over FY24-FY27E) is quite well baked into the current valuations (the stock trades at 42.9x on 1Y forward P/E vs 5Y average of 41.7x). We have revised down our EPS estimates (-11.4%/-6.5%/-4.9% for FY25E/FY26E/FY27E) based on the weak Q2 result, but our TP remains at Rs 1,450 as we roll forward our valuation from Jun'26 to Sep'26. Our target P/E remains unchanged at 40x.

Key changes

Target	Rating
◀ ▶	◀ ▶

Ticker/Price	KJC IN/Rs 1,287
Market cap	US$ 2.4bn
Free float	53%
3M ADV	US$ 3.4mn
52wk high/low	Rs 1,579/Rs 1,110
Promoter/FPI/DII	47%/16%/28%

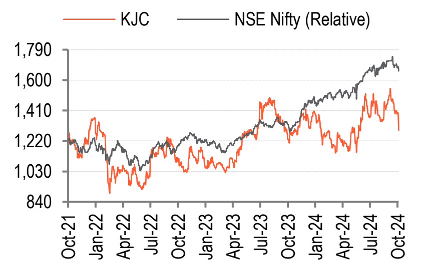
Source: NSE | Price as of 22 Oct 2024

Key financials

Y/E 31 Mar	FY24A	FY25E	FY26E
Total revenue (Rs mn)	45,784	49,853	57,649
EBITDA (Rs mn)	6,997	7,138	8,622
Adj. net profit (Rs mn)	4,221	4,133	5,233
Adj. EPS (Rs)	26.5	25.9	32.9
Consensus EPS (Rs)	26.5	30.5	37.5
Adj. ROAE (%)	16.6	14.8	17.3
Adj. P/E (x)	48.6	49.6	39.2
EV/EBITDA (x)	29.6	29.0	24.1
Adj. EPS growth (%)	20.0	(2.1)	26.6

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

NOT RATED

PERSISTENT SYSTEMS | IT Services | 22 October 2024

Strong quarter both on revenue and margins

- **Met revenue estimate. But a beat on EBIT margin. Strong 1H and ACV should mean high teen revenue growth with flat EBIT margin vs FY24**
- **Reiterates US$2bn revenue/16.5%-17.5% EBIT margin by FY27. Believes platform-based approach and SGA leverage will drive margins.**
- **Likely to have among fastest earnings growth among >US$1bn revenue Indian IT services players. Will initiate coverage on company soon**

Girish Pai
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Strong revenue growth in line but margin better: 5.1% CC QoQ growth was in line with our estimate of 5%. Growth was driven by Healthcare & Life Sciences and the BFSI verticals whereas the Hitech vertical was virtually flat. The EBIT margin was better than expected by 100bps QoQ at 14% (flat QoQ). But helped by continued large earn out reversals.

Margin Headwinds and tailwinds: Headwinds – wage hike (210bps), HR and other policy rationalization not being there (130), incremental ESOP impact (60), lower earn out reversal impact (60). A total of 460bps. Tailwinds – Utilization (120bps), lower subcon (70), lower resale of products (50), pricing and right shoring (130), currency (30) and no visa cost (60). Believes margins can move up higher in 2H. The earn-out reversals will be there in 2H too but will be largely accounted for in by FY25. The earn-out reversal helped 1QFY25 EBIT margin by 230bps.

Revenue growth delinked from industry: Persistent has delivered strong revenue growth (>5% CC QoQ) for the second consecutive quarter and has set itself apart from its peers, big and small. Its ability to pivot quickly to the requirements of the market is what it says has helped it grow much faster. This is visible in the TCV/ACV of the company.

Says revenue/profit per capita should move up in the coming years: Believes its AI platform-based strategy of using SAASVA (which is technology related) and iAURA (for business) will lead to higher revenue/profit per employee which should drive lower employee intensity and higher margins.

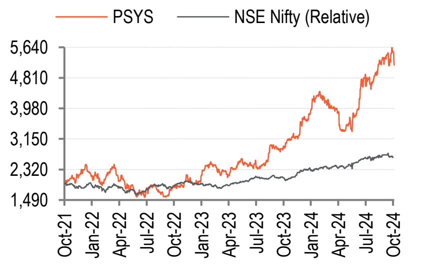
Headcount growth controlled: Persistent trimmed its employee base for the second consecutive quarter while taking up utilization to 84.8% (including trainees). Very likely it will start adding employees from here on as it is at the upper end of the utilization band it wants to operate in (83-85%).

Furloughs will be normal but 2H growth should be healthy: Does not see anything different this year. Strong TCV/ACV addition will drive growth.

Ticker/Price	PSYS IN/Rs 5,158
Market cap	US$ 9.4bn
Free float	68%
3M ADV	US$ 26.2mn
52wk high/low	Rs 5,690/Rs 2,840
Promoter/FPI/DII	31%/23%/27%

Source: NSE | Price as of 22 Oct 2024

Stock performance



Source: NSE

COMPANY UPDATE

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ZENSAR TECHNOLOGIES | IT Services | 23 October 2024

Unseasonal furloughs in TMT clients impacts revenue growth

- **Weak QoQ growth due to client specific issues in TMT vertical whereas BFSI and HLS show good traction.**
- **Weaker Gross margin QoQ set off by lower SGA. Reiterates mid-teen EBITDA margin guidance.**
- **TCV clocked is the highest ever. And more of it is in the managed services type of work. Will be reinitiating coverage soon.**

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Unseasonal furloughs impact revenue: The weak revenue growth of 0.3% in QoQ CC terms (against our estimate of 3% growth) was impacted by TMT vertical (~22% of revenue) declining by 8.8% due to unseasonal furloughs seen in 2-3 large clients. BFSI (~41%) grew by 3%, Manufacturing & consumer services (~26%) grew by 1.6% and healthcare & life sciences (~11%) grew by 8.6%. It was the seventh successive quarter of BFSI growth.

Margin walk: Lower SGA spending offset weaker than expected gross margin performance (Figure 1) Gross margin was down 230 bps QoQ, primarily due to 170bps from wage hikes, 110bps from lower utilization related to furloughs, and a 60bps from a prior R&D credit. This was partially offset by 70bps from currency and 40bps from operational efficiencies, including improved offshore mix. The gross margin drop was offset by SG&A reduction of 240bps QoQ, primarily due to provision for doubtful debts from a customer in the previous quarter which did not recur, reduced ESOP charges, and other savings.

Highest TCV clocked: US$201mn (up 3.6% YoY and 31% QoQ) was the stronger order inflow in its history

3Q should see weaker furlough impact compared to the past: While there are going to be more broad-based furloughs in 3Q, the impact is expected to be weaker due to the peculiar situation faced in 2Q by the company.

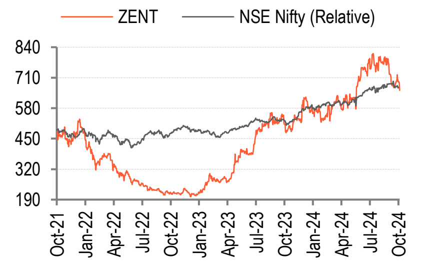
The strategy is to grow the non-TMT verticals: The TMT clients (legacy technology companies) are facing growth challenges, and the outlook remains uncertain, as clients themselves are unsure if they have reached the bottom of the current challenges. The strategy is to drive growth in other verticals and reduce exposure of TMT over the next 2-3 years.

Greater shift to offshore due to more managed services work being taken on: Offshore revenue has moved from 40% to 50% of total because of this.

Ticker/Price	ZENT IN/Rs 656
Market cap	US$ 1.8bn
Free float	50%
3M ADV	US$ 8.0mn
52wk high/low	Rs 840/Rs 456
Promoter/FPI/DII	49%/15%/19%

Source: NSE | Price as of 22 Oct 2024

Stock performance



Source: NSE

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