Enriching India, one investor at a time

Volume No. I Issue No. 18

Hinduja Global Solutions Ltd.

May 20th, 2015

BSE Code: 532859 | NSE Code: HGS | Reuters Code: HGSL.NS | Bloomberg Code: HGSL:IN

Incorporated in 2000, as a part of the Hinduja Group, Hinduja Global Solutions Ltd. (HGS) is a leading Business Process Management (BPM) and IT solutions provider to Healthcare/Insurance, Financial Services, Telecommunications and Consumer Products sector. HGS is accredited as one of the foremost players in Contact Center Outsourcing space by the analyst and advisor community. By relating analytics and interaction transformation design to provide innovation and thought leadership, HGS upturns revenue, increases operating efficiency and aids to hold valued customers. Its expertise spans across the telecommunications and media, healthcare, insurance, banking, consumer electronics and technology, retail, consumer packaged goods industries, as well as the public sector. Its client base contains particularly the world's most recognized brands across North America, Europe, Asia and Africa.

Investment Rationale

Healthcare segment provides high revenue visibility: During Q3FY15, HGS' growth was largely driven by the expanding capabilities in its healthcare segment. Over the last few years, it has grown significantly and now contributes 33.8% to the top-line. It has emerged as a leader in providing end-to-end services to the healthcare industry for both payers and providers, including 5 of the top 10 healthcare payers and over 10 large hospital groups in the US. Moreover, its recent acquisition of Colibrium Inc will further aid in developing competences, hence providing HGS a market edge.

Client retention-a key growth driver: HGS attributes a large chunk of its revenue to the top 5 clients that the company handles. Moreover, it client tenures comprises of only ~6% of the clients with a relationship of less than 5 years. 94% of the total clients have been with the company for more than 5 years, hence testifying the high execution potential and the quality service of the company.

Debt levels to stabilise in the coming years: HGS has registered ~16% CAGR in the debt levels from FY13A leading to a debt of ~₹6,047.1 mn accounting for ~38% of the total shareholder's equity at the end of H1FY15 from ~35% in FY13A. This has created a need for the management to address the high debt problem in order to prevent a pile-up in case of future expansion plans. However, we believe that the debt will moderate given no capex plans of the company for the coming years along with the company's efforts to transmit cash from its overseas subsidiary to the domestic business, capturing benefit of the tax window.

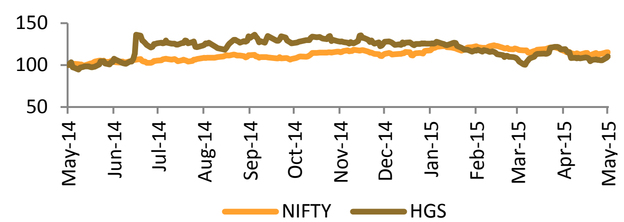
Market Data

Rating	**BUY**
CMP (₹)	555
Target (₹)	**689**
Potential Upside	~24%
Duration	Long Term
Face Value (₹)	10.0
52 week H/L (₹)	736.5/475.0
Adj. all time High (₹)	736.5
Decline from 52WH (%)	24.6
Rise from 52WL (%)	16.9
Beta	1.1
Mkt. Cap (₹bn)	114.4
Enterprise Value (₹bn)	115.3

Fiscal Year Ended

Y/E	FY14A	FY15E	FY16E	FY17E
Revenue (₹bn)	25.0	28.7	32.8	37.5
Net profit (₹bn)	1.6	1.6	2.0	2.3
EPS (₹)	12.4	12.2	14.8	16.8
P/E (x)	44.8	45.4	37.5	33.0
P/BV (x)	7.9	7.3	6.6	6.0
ROE (%)	11.7	10.0	11.6	12.0

One year Price Chart



Shareholding Pattern	Mar-15	Dec-14	Chg
Promoters	67.7	67.8	(0.1)
FII	12.0	12.0	0.0
DII	5.0	5.0	0.0
Others	15.3	15.2	0.1

Hinduja Global solutions Ltd. is a firm involved in the pure play BPO business catering to a wide range of industries spanning from telecom to healthcare.

Hinduja Global Solutions Ltd - a leading BPM and IT solutions provider

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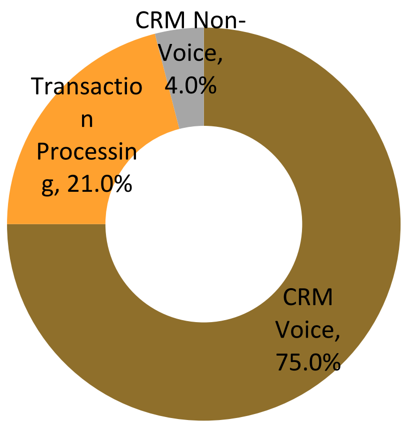
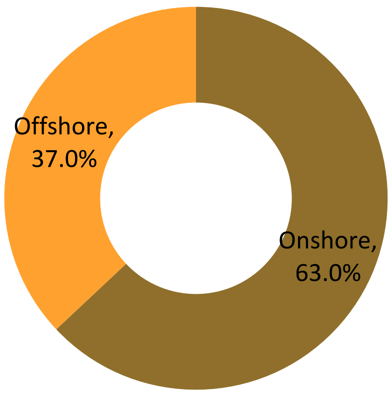
HGS operates on a global landscape with 28,000+ employees in 60 worldwide locations delivering localized solutions. HGS commands a worldwide footprint with 58 delivery centers spanning across Italy, India, Jamaica, Canada, France, the Netherlands, the Philippines, the United Kingdom, the United States of America Germany and Mauritius. Over the years, the company has adopted a proactive strategy of organic growth, and has acquired entities in the US, UK, Philippines, Canada and India.

Segmental revenue contribution across service



HGS's offering mix



Strong revenue growth bodes well for the company

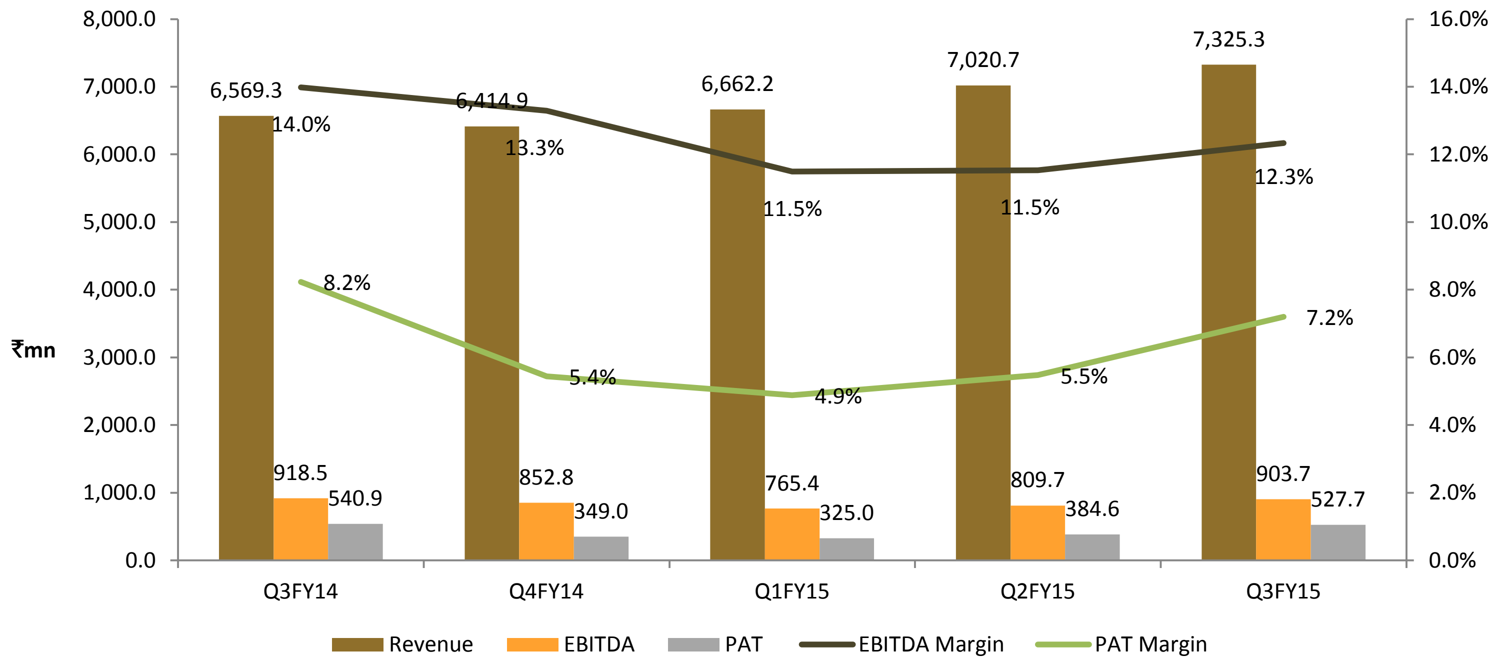
Revenue growth driven by healthcare segment: For the quarter ended December 2014, HGS' revenue grew 11.5% YoY and 4.3% QoQ to ₹7,325.9 mn. The growth was driven by increased contribution from the healthcare vertical. Revenue growth was broad-based across geographies with Philippines being the major contributor. The Philippines operations experienced client expansion. It received two new contracts from a fitness client and a durable medical equipment provider. The company's fifth facility at Alabang continued operating at optimum levels, whereas its sixth facility with a capacity of 420 FTEs started in March 2015, hence will aid to revenues in the upcoming quarters.

The growth in the top-line comes as the healthcare business and the Philippines expansion continues to yield higher sales.

Portfolio rationalisation costs hampered EBITDA: EBITDA for the quarter stood at ₹903.7 mn as against ₹918.5 mn declining by 1.6% YoY. EBITDA was squeezed by the ongoing ramp-up activities in Philippines and Canada. Cost related to the ongoing portfolio rationalization initiatives also had an adverse impact on the margin.

Higher depreciation and ramp-up costs affected the PAT adversely: PAT for Q3FY15 stood at ₹527.7 mn as against ₹540.9 mn in Q3FY15 reporting a decline of 2.4% YoY. Profitability was impacted by higher depreciation charge on account of implementation of the new Companies Act. The expansion in the Philippines coupled with the hostile movement of the Canadian dollar also had a negative impact on the bottom-line. However, the management is of the view that the profitability will improve on completion of ramp-ups in Philippines. Moreover, improvement in demand from telecom clients in Canada and steady performance of Europe and US operations strengthens confidence that the growth momentum will continue in the mid to long term.

Quarterly performance continue to gain traction

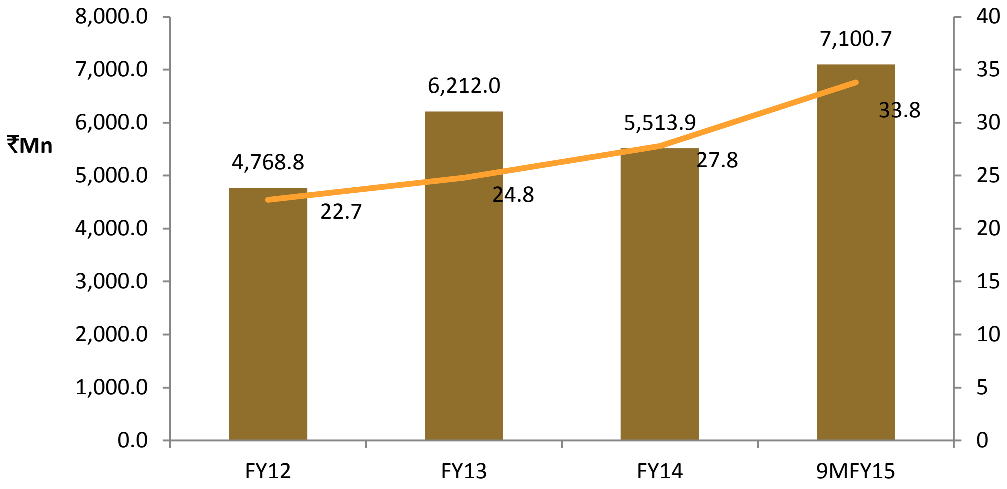


The takeover of the US healthcare major Colibrium will give the company access to cloud based software platform to provide automated healthcare services.

Acquisition of Colibrium to aid the healthcare segment

Over the past few years, HGS' healthcare segment has registered significant growth and has emerged as the largest contributor to the revenue, sharing a significant 33.8% of the pie. HGS's Extended Business Office Solutions Practice (HGS EBOS) supplements its clients' efforts in patient access, health information management and patient financial services by delivering solutions for financial clearance, medical coding and insurance claim resolution designed to improve net revenue, reduce bad debt and accelerate cash collections. Recently, the company acquired majority stakes of Colibrium Inc, a Healthcare Technology major in the US that devised a cloud based software platform that works closely by automating capabilities for Healthcare providers. ***The takeover is expected to offer an edge to Hinduja Global Solutions to upsurge the service competencies in trades and enrolment areas for the Americans as well Global health insurers.***

Strong traction from the healthcare business that contributes ~33.8% to the top-line

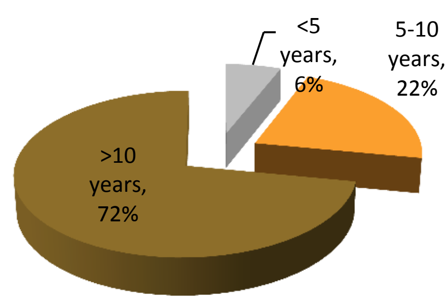


Client retention reflects quality service

HGS has a reputation of thriving on long standing clientele base, which drives a large chunk of its top-line. It draws ~50% of the revenue from its top 5 clients, ~66% from the top 10 clients and 79% from the top 20 clients.

HGS' long standing client tenures is a testimony for service quality and execution capabilities.

HGS' client tenures



Albeit this poses a concentration risk for the company, but HGS has had a majority of them since more than a decade owing to its high-quality service delivery. It also recently completed 40 years of service with its top client in the consumer durables sector. The contribution from the top 5 clients increased from 17% in Q3FY12 to 50% in Q3FY15. In addition to this, the company has been able to grow its client base as banking upon expansion in existing capacities, healthy client retention records and entering new geographies.

The number of clients (direct and payroll processing clients) have grown at a CAGR of 11.4% over last four years from 482 clients in Q3FY12 to 667 in Q3FY15. These factors give us confidence on the execution capabilities of the company and its service quality, thus making us optimistic about its growth.

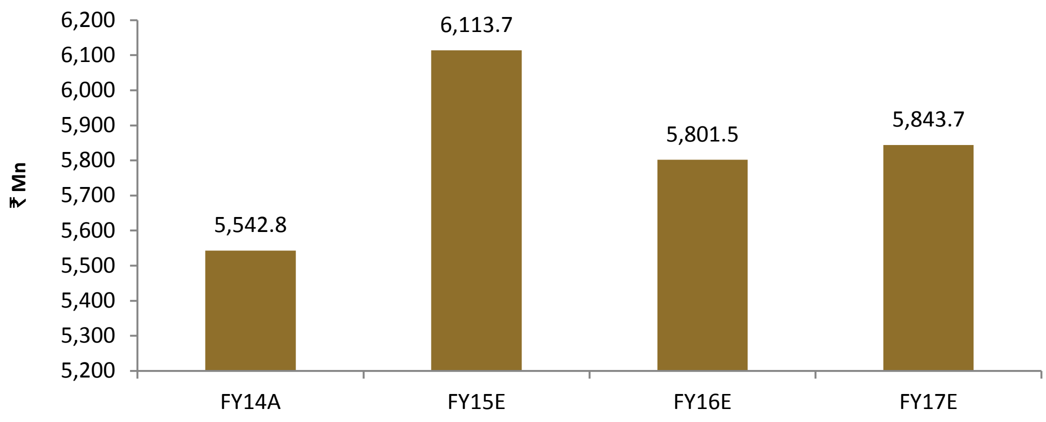
With no major capex in sight, debt levels are likely to come down

HGS has aggressively relied on mergers and acquisitions (M&A) to achieve economies of scale, hurting its balance sheet with debt. The company had a debt of ₹5,542.8 mn in FY14 and ₹6,047.1 mn in H1FY15 growing at an average of ~23.2% and 34.4% respectively from FY13. A majority of this is due to Online Support acquisition in FY12, which helped the company gain entry into the Canadian market and the on-going ramp-ups in Philippines. However, we believe that the debt levels will likely retreat going forward. With no large capex or M&A planned, company's requirements for capital will go down generating higher free cash flows and healthy returns. Additionally, the company is progressively transmitting cash from its overseas subsidiary to the domestic business, capturing benefit of the tax window available to it.

All these factors direct to a healthier balance sheet moving forward. All put together, the management expects to moderate debt considerably by Sep'18.

HGS has no major capex planned for FY16 and FY17; hence we believe that the company's borrowings are likely to go down.

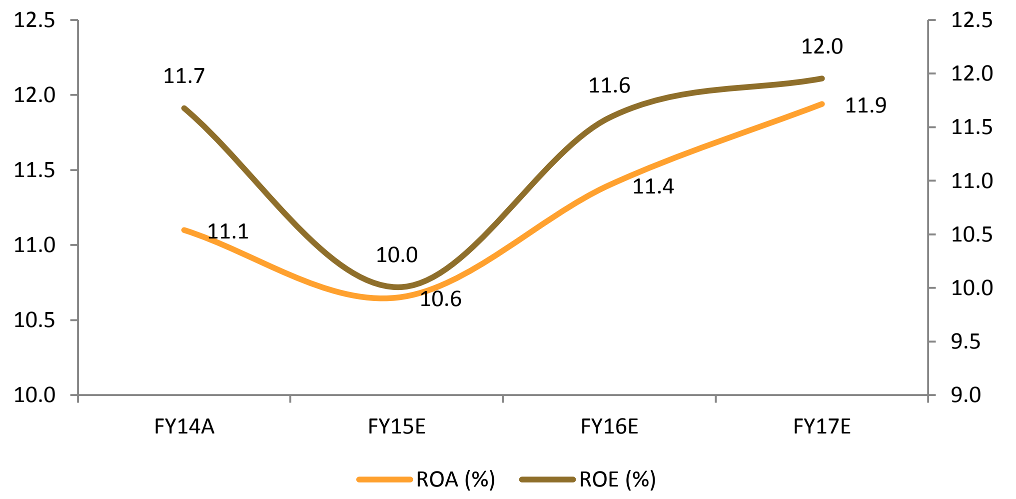
Debt likely to stabilise in the coming years



Key risks

- Given a vast global presence, the company is exposed to currency risk.
- Being a pure play BPO service provider, HGS stands to lose if integrated IT-BPM players expand. HGS faces tough competition from MNCs and Indian BPM-IT vendors.
- HGS relies heavily on its top clients and draws a major share of its revenue from them which expose it to concentration risk.

Healthy returns going ahead



Balance Sheet (Consolidated)

Y/E (₹mn)	FY14A	FY15E	FY16E	FY17E
Share Capital	206.2	206.2	206.2	206.2
Reserve and surplus	14,314.5	15,457.5	17,030.4	19,004.6
Net Worth	**14,520.6**	**15,663.7**	**17,236.6**	**19,210.7**
Minority Interest	0.1	0.0	0.0	0.0
Loans	5,542.9	6,113.7	5,801.5	5,843.7
Deferred tax liability	297.3	217.0	217.0	217.0
Long term Provisions	64.0	70.2	77.3	77.3
Current Liabilities	3,872.4	3,118.3	3,239.1	3,300.4
Capital Employed	**24,297.3**	**25,182.9**	**26,571.5**	**28,649.1**
Fixed Assets	10,902.9	12,089.2	13,404.5	14,863.0
Long term loans and advances	1,364.6	1,530.8	1,717.3	1,926.5
Non- Current Investments	68.5	79.2	79.2	79.2
Other non-current assets	77.7	69.5	69.5	69.5
Current Assets	11,883.7	11,414.2	11,301.0	11,710.9
Capital Deployed	**24,297.3**	**25,182.9**	**26,571.5**	**28,649.1**

Profit & Loss Account (Consolidated)

Y/E (₹mn)	FY14A	FY15E	FY16E	FY17E
Net Sales	25,048.5	28,664.9	32,792.6	37,514.7
Expenses	21,829.6	25,270.6	28,964.2	33,197.8
EBITDA	**3,219.0**	**3,394.3**	**3,828.4**	**4,316.9**
Other Income	340.0	242.7	259.7	277.8
Depreciation	862.0	955.0	1,059.0	1,174.2
EBIT	2,697.0	2,681.9	3,029.1	3,420.6
Net Interest cost	387.5	458.5	435.1	438.3
Profit Before Tax	2,309.5	2,223.4	2,594.0	2,982.3
Tax	681.7	655.9	596.6	685.9
Net Profit	**1,627.8**	**1,567.5**	**1,997.4**	**2,296.4**

Key Ratios (Consolidated)

Y/E	FY14A	FY15E	FY16E	FY17E
EBITDA Margin (%)	12.9	11.8	11.7	11.5
EBIT Margin (%)	10.8	9.4	9.2	9.1
NPM (%)	6.5	5.5	6.1	6.1
ROCE (%)	13.9	12.8	13.5	14.0
ROE (%)	11.7	10.0	11.6	12.0
EPS (₹)	12.4	12.2	14.8	16.8
P/E (x)	44.8	45.4	37.5	33.0
BVPS(₹)	70.4	76.0	83.6	93.2
P/BVPS (x)	7.9	7.3	6.6	6.0
EV/Operating Income (x)	32.4	32.4	28.9	25.7
EV/EBITDA (x)	35.8	34.7	30.8	27.3

Valuation and view

Over the years, HGS has been capitalising on its strong clientele base, technical expertise and successful acquisitions in order to strengthen its balance sheet and increase its revenues. Given its pure play BPO services and its market standing, we believe that the company is in a favourable position to further leverage on its expanding capacities in the Healthcare and the telecom segments. We expect HGS' net profit to grow at a CAGR of ~11% during FY14-FY16E and believe that it will continue to deliver strong return ratios as well.

At the current market price (CMP) of ₹555.5, the stock trades at a P/E of 37.5x FY16E and 33x FY17E. We recommend 'BUY' with a target price of ₹689.0, which implies a potential upside of ~24% to the CMP from a long term perspective.

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