

SONATA SOFTWARE LTD.

CMP : ₹487.35 | **Target price: ₹735** | **HP* : Upto 3 years**

Our Vriddhi pick for the month of March 2021 is Sonata Software Limited (SSL), which is an information technology (IT) services & solutions company. It enables successful platform-based digital transformation initiatives for enterprises, to create businesses that are connected, open, intelligent, and scalable. It provides solutions for software, retail & distribution, and travel companies with integrated technological solutions like mobility, analytics, cloud & enterprise resource planning. In terms of the geographical mix in FY20, the company's 34 per cent of total consolidated revenue was from international IT services while the rest 66 per cent came from domestic products & services.

Platformation to be a key growth driver

Sonata has developed a proprietary model for the digital transformation of enterprises called Platformation. Through this Platformation, the company is looking to extend its services beyond just IT vendors to use platforms & IP as business transformation drivers and become a long-term partner. In FY20, it acquired Melbourne-based GAPbusters for USD 4.8 million, which has been amongst the pioneers in the customer experience (CX) domain. This acquisition is a reaffirmation of Sonata's Platformation-led approach to digital transformation, adding a major platform-led customer experience offering to current solutions. It also made a strategic investment by acquiring a 17 per cent stake in SemiCab Inc., Atlanta-based start-up that offers technology platforms to logistics providers. It will also invest USD 1.4 million for the stake along with an additional USD 3 lakh for SemiCab's services over the next one year. The deal is in line with Sonata's strategy to invest in companies that are digitally transforming their customers' businesses. Such strategic acquisitions and partnerships have led to improvement & consolidation in its position, leading to becoming the most preferable partners of choice for its customers. With this, the company will go for inorganic growth in the near term.

Microsoft Dynamics - another growth engine

Sonata Software has continued to strengthen its alliance with Microsoft and focussed on delivering high-quality services to its clients, which increased the stickiness of the business. Sonata is positioned as a major player in the IDC MarketScape for 'Microsoft Dynamics 365 implementation services for Asia/Pacific (excluding Japan)'. As per Microsoft, Sonata's platform, Rezopia is among the first 15 transactable applications in Azure Marketplace. Sonata has entered the Agri-commodity business with the acquisition of scalable data systems. Scalable Data Systems designs digital platforms that can scale up or down as business demands, powered by Microsoft Dynamics. The recovery in Microsoft services portfolio is expected from FY22, based on the strong pipeline. Microsoft Dynamics modernisation program is a multi-year opportunity, and the company is looking to invest in R&D and sales capabilities to fuel growth.

*HP : Holding Period

Company Details

Industry	IT - Software
Chairman	Pradip P Shah
Managing Director	P Srikar Reddy
Company Secretary	Mangal Kulkarni
ISIN Code	INE269A01021
Bloomberg Code	SSOF IN
BSE Code	532221

Key Market Ratio

Latest Date	10-Mar-21
Latest Price (Rs)	487.35
Previous Close (Rs)	488.05
1 Day Price Var %	-0.54
1 Year Price Var %	53.76
52 Week High (Rs)	528.1
52 Week Low (Rs)	148.1
Beta	0.64
Face Value (Rs)	1
Industry PE	27.53
TTM Period	202012
TTM EPS (Rs)	21.18
TTM CEPS(Rs)	24.93
Price/TTM CEPS(x)	19.17
TTM PE (x)	22.57
Price/BV(x)	5.85
EV/TTM EBIDTA(x)	12.4
EV/TTM Sales(x)	1.16
Dividend Yield%	4.24
MCap/TTM Sales(x)	1.23
Latest Book Value (Rs)	81.74
Market Cap (Rs in Crores)	5026
EV (Rs)	4715
Latest no. of shares Crores	11

Share Holding Pattern as on 202012

Promoter No of shares (Rs in Crores)	8-Mar-21
Promoter %	0.64
FII No of Shares (Rs in Crores)	1
FII %	27.53
Total No of Shares (Rs in Crores)	202012
Free Float %	21.18

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DSJ Pvt. Ltd. : Office no 211, Vascon Platinum Square, Next to Hyatt Regency, Vimanagar, Pune- 411014 | For Customer Service : 020-66663-802/803 OR service@dsj.in

Registered Office Address: 419-A, 4th Floor, Arun Chambers, Tardeo, Next to AC Market, Mumbai - 400034

CIN No. : CIN-U22120MH2003PTC139276 SEBI Research Analyst - INH000006396

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Deriving strength from international IT services

The company derives 34 per cent of its revenue from international IT services business. Of that, 54 per cent is derived from the US market and 30 per cent from the European market. During December 2020 quarter, the USA revenue grew by 7.1 per cent QoQ while Europe revenue grew by 4.9 per cent QoQ. In FY20, it had added 29 new logos across verticals, regions in the international services segment. The company's pipeline continues to be healthy and strong through multiple new digital wins from its existing and new customers. It has added 8 new customers in the international IT services segment during the latest December 2020 quarter.

Growing domestic industry

In today's world, organisations have increased their focus on providing a better customer experience, which has resulted in higher spending on enterprise application software. India continues to be a preferred destination for IT services, owing to strong digital execution capabilities, cost advantages, favourable talent landscape, and increased government focus on IT infrastructure. India's IT spending is estimated to be a total of USD 94.3 billion in 2020, with a growth of 6.6 per cent over 2019, primarily driven by spending on software. This IT spending continues to be driven by digital business transformation initiatives from both private and public organisations. Such increased focus and adoption-changing business models would pave a path of growth for companies involved in digital space like Sonata Software.

Financial performance

The company has clocked a CAGR of 17 per cent in revenue over the last 5 years. Also, PAT has replicated the revenue growth and recorded a 16 per cent CAGR over the same period.

On the revenue front, the company witnessed a growth of 12.88 per cent YoY and 73.7 per cent QoQ to Rs 1,396.16 crore in Q3FY21. In the international IT services segment, revenue in USD was 41 million, with QoQ revenue growth of 5 per cent in USD terms and constant currency growth of 4.5 per cent. In terms of revenue contribution in Indian rupees, international IT services contributed Rs 300.9 crore while domestic products & services contributed Rs 1,099.4 crore. PBIDT (excluding OI) came in at Rs 110.92 crore, higher by 1.14 per cent YoY and 27.09 per cent QoQ. The corresponding margin contracted to 7.94 per cent from 8.87 per cent in the year-ago period. PAT was reported at Rs 53.79 crore, down by 29.09 per cent YoY, led by a 62 per cent decline in other income. PAT margin was reported at 7.12 per cent, expanding by 99 bps during the quarter.

The company has a strong balance sheet and it has been paying a continuous dividend to its shareholders over the last few years and has maintained a dividend payout ratio of around 62 per cent. The company also has strong cash and bank balance of around Rs 642 crore.

Inc/Exp Statement (Consolidated)

Description	202003	201903	201803	201703	201603
Net Sales	3743.26	2960.90	2453.94	2370.78	1940.50
Total Income	3801.66	2988.15	2499.39	2417.89	1984.28
Total Expenditure	3370.45	2625.29	2222.95	2179.23	1748.61
PBIDT	431.21	362.86	276.44	238.66	235.68
PAT	276.93	248.88	192.13	156.92	158.59
Dividend %	2025.00	1275.00	1050.00	900.00	900.00
Adj. EPS(Rs)	26.65	23.99	18.55	15.07	15.08



Strategic acquisitions and partnerships have led to improvement & consolidation in its position



Microsoft Dynamics modernisation program is a multi-year opportunity

Quarter On Quarter (Consolidated)

Particulars	202012	202009	Q on Q Var %	201912	Y on Y Var %
Net Sales	1396.16	803.77	73.7	1236.88	12.88
Total Expenditure	1285.24	716.49	79.38	1127.21	14.02
PBIDT (Excl OI)	110.92	87.28	27.09	109.67	1.14
PAT	53.79	57.2	-5.96	75.86	-29.09
PBIDTM% (Excl OI)	7.94	10.86	-26.89	8.87	-10.48
PBIDTM%	8.18	11.16	-26.7	9.56	-14.44
PATM%	3.85	7.12	-45.93	6.13	-37.19
Adj. EPS(Rs)	5.18	5.51	-5.99	7.3	-29.04

Valuation

The company is trading at TTM P/E of 22.5x with TTM EPS of Rs 21.18. In terms of return ratios, the company enjoyed strong RoE and RoCE of 46.8 per cent and 61.7 per cent, respectively in FY20. Stability in the top client, upgrades in Microsoft Dynamics & improved traction in the cloud, expansion in new verticals like an agricultural commodity business, and traction in ISV vertical & retail, are expected to drive revenues. The company believes that there is a huge opportunity for upgrades and has numerous clients in the medium to the large category to tap, which can boost long-term revenue growth. Considering all these factors, we see a potential upside of 51 per cent with a target price of Rs 735 for a period of three years.

About the company

Sonata Software Ltd (SSL) provides IT consulting, product engineering services, application development, application management, managed testing, business intelligence, infrastructure management, packaged applications, and travel solutions. It also includes the manufacturing, retail, and consumer packaged goods verticals, and offers outsourced research & development services to independent software vendors. It operates a software distribution business for companies such as Microsoft, Oracle, and IBM. The company's business has two broad lines as products & services. Under products, it focusses on multi-cloud, SI business and security business.



Its international pipeline continues to be healthy and strong through multiple new digital wins



India's IT spending is estimated to be a total of USD 94.3 billion in 2020, with a growth of 6.6 per cent over 2019



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