

Estimate change	↔
TP change	↑
Rating change	↔

CMP: INR1,763 TP: INR1,980 (+12%) Buy

Stable performance; 2HFY24 requires more heavy lifting

Three engines firing | Connectivity still in pain

- Cyient (CYL) reported DET business revenue growth of 1.0% QoQ in CC terms in 2QFY24. The 2Q growth was led by the New Growth Areas and Sustainability verticals, which rose 4.9% and 2.7% QoQ in CC, respectively, followed by Transportation (+2.7% QoQ in CC). Growth was weak in Connectivity (-8.1% QoQ in CC). Normalized EBIT margin for the DET business came in at 16.5%, 30bp above our estimates, mainly led by the cost rationalization measures and efficiency gain in 2QFY24.
- Service order intake was modest at USD183.9m, -4.8% QoQ/+42.6% YoY in 2Q. However, the deal pipeline remained strong, with five large deals signed during the quarter. CYL has reiterated its confidence in delivering FY24 Service revenue growth of 15-20% YoY in CC and has maintained DET EBIT margin growth forecast at 150-250bp YoY.
- Overall, the management was quite optimistic about the continued growth momentum in Transportation verticals driven by healthy demand within the Commercial Aerospace. On the other hand, the MRO segment is gaining strength due to strong Air Traffic volume. Growth under Sustainability vertical should continue with strong demand within the ENU and Mining segments. Green energy and Hydrocarbon are gaining traction among large enterprises as they strive to become carbon neutral. However, CYL indicated continued softness in the Connectivity segment as telcos are reprioritizing investments on 5G. This segment is likely to remain weak until the telcos revisit their capex investment cycle. We expect the DET business to grow at the lower end of CYL's FY24 revenue growth guidance (our est. of 15.0% YoY in CC), resulting in a FY23-25 USD revenue CAGR of 14.8%.
- On EBIT margin, CYL's 2Q performance exceeded our estimates by 30bp QoQ despite the wage hikes. However, the remaining portion of the wage hike is expected to come through in 2H. Hence, we expect the company to deliver an FY24 EBIT margin of 16.2% (+250bp YoY). This should help DET report an FY23-25 INR PAT CAGR of 30%, which we view as attractive.
- On SOTP basis, we are valuing its stake in DLM at market valuation, applying a holding company discount of 25%. We value the DET business at 21x our FY25E EPS. **We broadly maintain our FY24/FY25 consol. PAT estimates. We maintain our BUY rating on the stock. Our SOTP-based TP of INR1,980 implies an upside of 12%.**

In-line DET (Service) revenue, beat on margins

- CYL's Service revenue rose 1.0% QoQ in CC to USD178.4m, marginally below our growth estimate of 1.1% QoQ.
- Sustainability, Transportation and New Growth Areas were up 4.9%, 2.7% and 5.7% QoQ in CC, respectively, while Connectivity was down 8.1% QoQ in CC.
- Service margin was at 16.5% (+50bp QoQ/+400bp YoY), above our estimate of 16.2%.

Bloomberg	CYL IN
Equity Shares (m)	113
M.Cap.(INRb)/(USDb)	195.3 / 2.3
52-Week Range (INR)	1945 / 724
1, 6, 12 Rel. Per (%)	8/54/122
12M Avg Val (INR M)	608

Financials & Valuations (INR b)

Y/E Mar	2023	2024E	2025E
Sales	60.2	72.7	84.2
EBIT Margin (%)	12.8	14.7	15.1
PAT	5.8	7.8	9.8
EPS (INR)	52.4	70.7	88.3
EPS Gr. (%)	9.6	35.1	24.8
BV/Sh. (INR)	314.6	340.5	375.8

Ratios

RoE (%)	17.5	21.6	24.7
RoCE (%)	14.7	17.3	18.6
Payout (%)	49.7	60.0	60.0

Valuations

P/E (x)	33.7	24.9	20.0
P/BV (x)	5.6	5.2	4.7
EV/EBITDA (x)	19.1	14.0	11.5
Div Yield (%)	1.5	2.4	3.0

Shareholding pattern (%)

As On	Sep-23	Jun-23	Sep-22
Promoter	23.2	23.4	23.4
DII	21.6	21.3	23.7
FII	36.6	37.5	33.6
Others	18.6	17.8	19.3

FII Includes depository receipts

- The order intake was moderate at USD183.9m (-4.8% QoQ). CYL won five large deals in the Service business with a total contract potential of USD51.4m in 2Q.
- Adjusted PAT stood at INR1,728m, up 1.5% QoQ.

Key highlights from the management commentary

- Connectivity was weak as the communication vertical was struggling, and the enterprises have been revisiting their budgets for 5G investments. The management is quite optimistic and expects a recovery in a couple of quarters, aided by a healthy deal pipeline and strong demand from government projects in the wireline business.
- The telecom infrastructure spending is facing headwinds in the near term due to consecutive rate hikes and elevated inflation. Hence, spending on communication is anticipated to be somewhat volatile in the near term.
- The management mentioned that it is witnessing some delays in decision-making and projects approvals. However, once a contract gets signed, it gets executed faster without any pause from the client.
- Management was confident of achieving the DET margin guidance (+150bp to +250bp), as the 2Q run-rate already exceeded the upper end of the guidance.

Valuation and Outlook

- CYL's service segment is shaping up quite well, with positive momentum in most of its growth engines. Conversely, other segments are on the verge of recovery and should incrementally contribute to its overall growth in FY24E.
- On SOTP basis, we are valuing its stake in DLM at market valuation with a holding company discount of 25%. We value the DET business at 21x our FY25E EPS.
- **We broadly retain our FY24/FY25 consol. PAT estimates. We maintain our BUY rating on the stock. Our SOTP-based TP of INR1,980 implies an upside of 12%.**

Quarterly performance (Consol)

Y/E March	FY23				FY24				FY23	FY24E	FY24E	(INR m)
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE			2QE	Var. (%/bp)
Revenue (USD m)	162	175	197	213	205	214	222	237	746	879	208	2.9
QoQ (%)	3.1	8.2	12.7	8.1	-3.6	4.4	3.7	6.5	22.7	17.7	1.4	293bp
Revenue (INR m)	12,501	13,962	16,182	17,514	16,865	17,785	18,450	19,644	60,159	72,745	17,214	3.3
YoY (%)	18.1	25.6	36.7	48.3	34.9	27.4	14.0	12.2	32.7	20.9	23.3	409bp
GPM (%)	36.8	38.4	37.8	38.0	36.6	35.7	36.8	37.3	37.8	36.6	36.2	-49bp
SGA (%)	21.2	22.0	20.6	19.6	17.9	17.4	18.2	18.4	20.8	18.0	18.1	-71bp
EBITDA	1,946	2,290	2,785	3,222	3,156	3,258	3,432	3,713	10,243	13,559	3,116	4.6
EBITDA margin (%)	15.6	16.4	17.2	18.4	18.7	18.3	18.6	18.9	17.0	18.6	18.1	22bp
EBIT	1,435	1,660	2,086	2,496	2,480	2,600	2,694	2,927	7,677	10,701	2,427	7.1
EBIT margin (%)	11.5	11.9	12.9	14.3	14.7	14.6	14.6	14.9	12.8	14.7	14.1	52bp
Other income	160	-148	60	-257	-176	-134	37	39	-185	-234	34	-489.2
ETR (%)	27.2	19.4	24.1	21.3	22.9	23.6	24.0	24.0	23.0	23.7	24.0	
Adj. PAT	1,161	1,218	1,628	1,762	1,767	1,831	2,022	2,201	5,769	7,820	1,861	-1.6
QoQ (%)	-24.7	4.9	33.7	8.2	0.3	3.6	10.4	8.9			5.3	-168bp
YoY (%)	0.9	0.5	23.7	14.3	52.2	50.3	24.2	24.9	10.5	35.6	52.8	-244bp
EPS (INR)	10.6	11.1	14.8	16.0	16.0	16.6	18.3	19.9	52.4	70.7	16.8	-1.6

Key performance indicators (Consol)

Y/E March	FY23				FY24				FY23	FY24
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Margins (%)										
Gross Margin	36.8	38.4	37.8	38.0	36.6	35.7	36.8	37.3	37.8	36.6
EBIT Margin	11.5	11.9	12.9	14.3	14.7	11.9	12.9	14.3	12.8	14.7
Net Margin	9.3	8.7	10.1	10.1	10.5	8.7	10.1	10.1	9.6	10.8
Operating metrics										
Headcount	13,581	15,004	14,693	15,172	15,306	15,441			15,172	
Attrition (%)	27.9	28.4	26.5	25.0	23.0	20.4			25.0	
Key geographies (YoY %)										
North America	17%	16%	15%	12%	5%	0.1%			15%	
Europe	-9%	23%	52%	79%	104%	41%			37%	



Key highlights from the management commentary

Commentary on verticals

- **Connectivity:** The telecom infrastructure spending is facing headwinds in the near term due to consecutive rate hikes and elevated inflation. Otherwise, the functional areas of the Telecom Asset and Network Design are ramping up quite well. Both Europe and the US are generating equal opportunities for network fiberization and throughput on the 5G rollout.
- **Aerospace:** The Aerospace demand of the MRO and engineering services is relatively strong, while the design engineering service is volatile. The design service is expected to gain pace once the development cycle with a new platform gets initiated, although the timeline is uncertain.
- **Sustainability:** It has a larger scope on the regulatory and compliance fronts. The ancillary services on mining activities using IoT, AI, and sensors are gaining traction among its clients. With the acquisition of Citec, the company now has a significant presence in the Energy, Oil & Gas, and Electrofuel capabilities.
- **New Growth Area: (1)** The automotive segment is gaining traction on the autonomous and connectivity solutions. The overall demand trend for the segment remained strong, which is equally contributing to its service offerings on the embedded and software development horizontals. **(2)** The semicon segment remains in pain due to the inherent weakness led by chip shortage; however, it is expected to recover on the back of an increase in demand for AI and Auto segments.
- The management mentioned that it is witnessing some delays in decision-making and projects approvals. However, once a contract gets signed, it gets executed faster without any pause from the client.
- The Aerospace vertical is quite immune to 3Q seasonality and furloughs. However, connectivity is likely to see some impact from furloughs in 3QFY24.

Commentary on Margin

- The company has witnessed an improvement in operating margin despite the wage hike impact this quarter. The management indicated that the earlier investment in driving efficiency is benefiting the overall cost optimization efforts over the last couple of quarters. Additionally, the pricing benefits in a couple of segments have supported margins.
- The wage hike impact is expected to flow through 3Q and 4Q as well; however, management remained confident enough to absorb the impact through multiple margin levers.
- Management was confident of achieving the DET margin guidance (+150bp to +250bp), as the 2Q run-rate already exceeded the upper end of the guidance.

Exhibit 1: Growth from key geographies was weak in 2QFY24 (DET)

Geographies	Contribution to revenue (%)	QoQ growth (%)	YoY growth (%)
Americas	43.0	0.3	0.1
Europe	33.4	(2.2)	40.8
Asia Pacific	23.6	6.1	30.8

Source: Company, MOFSL

Valuation and view

- CYL's service segment is shaping up quite well, with positive momentum in most of its growth engines. Conversely, other segments are on the verge of recovery and should incrementally contribute to its overall growth in FY24E.
- On SOTP basis, we are valuing its stake in DLM at market valuation with a holding company discount of 25%. We value the DET business at 21x our FY25E EPS.
- **We broadly retain our FY24/FY25 consol. PAT estimates. We maintain our BUY rating on the stock. Our SOTP-based TP of INR1,980 implies an upside of 12%.**

Exhibit 2: Our SOTP valuation

	Valuation Metric	Tgt Multiple	Value (FY25E)
Cyient Service (INR m)	P/E	21	1,91,151
DLM (INR m)	Market Cap (25% holdco discount)		27,843
Total Market Cap (INR m)			2,18,994
O/S			110.6
Target Price (INR)			1,980.0
CMP (INR)			1,763.0
Upside %			12%

Source: MOFSL

Exhibit 3: Revisions to our estimates

	Revised estimates		Earlier estimates		Change in estimates	
	FY24E	FY25E	FY24E	FY25E	FY24E	FY25E
USD:INR	82.7	83.0	82.7	83.0	0.0%	0.0%
Revenue (USD m)	728	834	728	833	0.0%	0.1%
Growth (%)	15.1	14.6	15.1	14.5	0bps	10bps
EBIT margin (%)	16.2	16.7	16.3	16.7	0bps	0bps
PAT (INR m)	7,310	8,932	7,487	8,916	-2.4%	0.2%
EPS	66.1	80.8	67.7	80.6	-2.4%	0.2%

Source: MOFSL

Exhibit 4: DET P&L Statement (INR m)

Y/E March	FY21	FY22	FY23	FY24E	FY25E
Sales	34,242	37,544	50,936	60,192	69,228
Cost of Services	21,071	21,808	29,535	35,928	40,740
Gross Profit	13,170	15,736	21,401	24,264	28,487
EBITDA	5,514	7,470	9,309	12,324	14,503
% of Net Sales	16.1%	19.9%	18.3%	20.5%	21.0%
EBIT	3,754	5,740	6,970	9,779	11,526
% of Net Sales	11.0%	15.3%	13.7%	16.2%	16.7%
Net Income	3,254	4,696	5,243	7,310	8,932
Change (%)		44.3%	11.7%	39.4%	22.2%

* FY23 and Previous year data are on a Pro Forma basis

Financials and valuations

Income Statement							(INR m)	
Y/E March	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Sales	39,176	46,175	44,275	41,325	45,344	60,159	72,745	84,207
Change (%)	8.6	17.9	(4.1)	(6.7)	9.7	32.7	20.9	15.8
Cost of Services	25,387	30,125	28,964	27,162	28,453	37,415	46,107	52,664
SG&A Expenses	8,296	9,606	9,352	8,056	8,675	12,501	13,080	15,494
EBITDA	5,493	6,444	5,959	6,107	8,216	10,243	13,559	16,049
As a percentage of Net Sales	14.0	14.0	13.5	14.8	18.1	17.0	18.6	19.1
Depreciation	1,051	1,692	1,878	1,944	1,923	2,566	2,858	3,368
Other Income	1,207	864	734	684	687	-185	-234	168
PBT	5,649	5,616	4,815	4,847	6,980	7,492	10,467	12,849
Tax	1,381	2,327	1,076	1,133	1,761	1,723	2,477	3,086
Rate (%)	24.4	41.4	22.3	23.4	25.2	23.0	23.7	24.0
Net Income	4,268	3,307	3,726	3,714	5,219	5,769	7,820	9,762
Change (%)	20.8	-22.5	12.7	-0.3	40.5	10.5	35.6	24.8

Balance Sheet							(INR m)	
Y/E March	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Share Capital	563	552	550	550	552	553	553	553
Reserves	22,876	25,089	25,059	29,023	30,614	34,114	37,109	41,014
Net Worth	23,439	25,641	25,609	29,573	31,166	34,667	37,662	41,567
Other liabilities	1,636	2,240	4,194	3,812	4,061	5,644	6,831	7,913
Loan	2,410	3,253	3,738	2,755	3,264	9,336	9,336	9,336
Capital Employed	27,485	31,134	33,541	36,140	38,491	49,647	53,830	58,816
Applications								
Gross Block	12,217	13,289	17,388	18,558	19,223	21,776	22,776	23,776
Less: Depreciation	7,791	8,766	9,712	10,779	11,959	14,525	17,383	20,751
Net Block	3,220	3,530	6,909	7,181	6,787	7,251	5,393	3,025
CWIP	213	300	800	113	134	27	27	27
Intangibles	5,057	6,990	6,800	7,191	6,662	21,413	21,413	21,413
Other assets	2,380	2,219	2,638	1,925	5,318	4,877	5,106	5,314
Curr. Assets	23,456	25,853	24,650	28,518	28,972	31,913	41,902	51,100
Debtors	6,913	8,137	7,262	8,026	7,333	11,271	12,357	14,304
Cash and Bank Balance	9,604	9,073	8,995	14,408	12,157	6,215	10,959	14,290
Other Current Assets	5,809	8,365	8,393	6,084	8,616	12,709	15,368	17,789
Current Liab. and Prov.	6,841	7,758	8,256	8,788	9,382	15,834	20,011	22,063
Trade payables	3,813	3,712	3,729	4,532	5,259	7,142	10,962	12,689
Other liabilities	2,799	3,757	4,150	3,872	3,709	7,555	7,674	7,783
Provisions	229	289	377	384	414	1,137	1,375	1,591
Net Current Assets	16,615	18,095	16,394	19,730	19,590	16,079	21,891	29,037
Application of Funds	27,485	31,134	33,541	36,140	38,491	49,647	53,830	58,816

Financials and valuations

Ratios

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Basic (INR)								
EPS	38.0	30.0	33.8	33.8	47.8	52.4	70.7	88.3
Cash EPS	47.4	45.3	50.8	51.5	65.3	75.6	96.5	118.7
Book Value	209.8	232.3	232.0	269.1	285.1	314.6	340.5	375.8
DPS	13.0	13.0	27.0	24.5	24.0	26.0	42.4	53.0
Payout (%)	34.2	43.4	80.0	72.5	50.3	49.7	60.0	60.0
Valuation (x)								
P/E ratio	46.4	58.9	52.2	52.2	36.9	33.7	24.9	20.0
Cash P/E ratio	37.2	38.9	34.7	34.2	27.0	23.3	18.3	14.8
EV/EBITDA ratio	34.3	29.3	31.8	29.8	22.3	19.1	14.0	11.5
EV/Sales ratio	4.8	4.1	4.3	4.4	4.0	3.3	2.6	2.2
Price/Book Value ratio	8.4	7.6	7.6	6.6	6.2	5.6	5.2	4.7
Dividend Yield (%)	0.7	0.7	1.5	1.4	1.4	1.5	2.4	3.0
Profitability Ratios (%)								
RoE	19.1	13.5	14.6	13.5	17.2	17.5	21.6	24.7
RoCE	13.8	10.2	10.6	9.9	13.6	14.7	17.3	18.6
Turnover Ratios								
Debtors (Days)	62	59	63	68	62	68	62	62

Cash Flow Statement

(INR m)

Y/E March	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
CF from Operations	4,622	5,411	5,496	5,872	7,318	9,024	10,847	13,131
Cash for Working Capital	-1,659	-1,710	328	2,686	-973	-3,485	1,391	-1,443
Net Operating CF	2,963	3,701	5,824	8,558	6,345	5,539	12,238	11,688
Net Purchase of FA	-1,469	-1,440	-2,138	-949	-626	-625	-1,000	-1,000
Free Cash Flow	1,494	2,261	3,686	7,609	5,719	4,914	11,238	10,688
Net Purchase of Invest.	600	-767	568	-58	-3,197	-9,675	-1,500	-1,500
Net Cash from Invest.	-869	-2,207	-1,570	-1,007	-3,823	-10,300	-2,500	-2,500
Proc. from equity issues	9	22	17	37	121	79	0	0
Proceeds from LTB/STB	526	549	-916	-2,134	-1,994	1,458	0	0
Dividend Payments	-1,894	-2,892	-3,564	-10	-2,952	-2,630	-4,692	-5,857
Cash Flow from Fin.	-1,359	-2,321	-4,463	-2,107	-4,825	-1,093	-4,692	-5,857
Exchange difference	298	296	131	-31	52	-88	-302	0
Net Cash Flow	1,033	-531	-78	5,413	-2,251	-5,942	4,744	3,330
Opening Cash Bal.	8,571	9,604	9,073	8,995	14,408	12,157	6,215	10,959
Add: Net Cash	1,033	-531	-78	5,413	-2,251	-5,942	4,744	3,330
Closing Cash Bal.	9,604	9,073	8,995	14,408	12,157	6,215	10,959	14,290

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NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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