

Happiest Minds Technologies

Valuation can remain elevated

We met the management of Happiest Minds (HAPPSTMN) and believe that the company has growth catalysts despite services being more discretionary. The company is transitioning from an EduTech-heavy portfolio to a higher mix of BFSI and Healthcare (larger spending pool and pipeline)—recent acquisitions will accelerate growth prospects in the vertical with the up-sell opportunity. HAPPSTMN reiterated its long-term ambition to reach USD 1bn over the next eight years (23% CAGR including inorganic)—FY25E revenue growth outlook is 35 to 40% (including inorganic Pure Software & Aureus, implying organic at 10-15%). HAPPSTMN has recently changed its organisational structure and moved to an industry/vertical structure (*Happiest Minds - Organisational rejig for better growth*). We continue to believe that the current scale of the business, the distinction in quality and the disproportionate impact from potential recovery in discretionary services in the sector can keep valuation higher than peers for HAPPSTMN. We factor USD revenue growth at 34% and 26% for FY25E and FY26E respectively; factor EBITM at 16.1% and 17.8%, translating to an EPS CAGR of 27% over FY24-26E—maintain ADD with TP of INR 900, at 36x FY26E EPS.

GenAI growth driver: HAPPSTMN has set up GenAI business unit (GBS) as compared to peers that have predominantly set up a Center of Excellence (CoE) in GenAI. The GBS unit which currently includes 80 employees is expected to scale to 250 employees over the next year. Currently, the project size in GenAI is USD 150-250k and includes opportunities in contextual chatbots, learning simulators, sentiment analysis, and content generation. GenAI is also expanding the company's geography base in regions such as APAC.

EduTech may lag growth: HAPPSTMN's EduTech vertical contributes 22% to the revenue and includes a diverse set of clients largely in the US geography. HAPPSTMN is a strategic vendor for its large clients in the vertical. In the EduTech segment, competition is also from tier-1 IT peers. EduTech vertical is expected to grow below the company average over the medium term (likely 5-10% organic), which is also influenced by client concentration.

Scale up in Healthcare and India business: HAPPSTMN has scaled its healthcare vertical from 4-5% of revenue in FY22 to 16% of revenue or USD 30mn+ revenue rate and the company has invested in building capabilities in areas such as bioinformatics. This is likely to get to USD 50mn revenue run-rate business, following the consolidation of the Pure Software acquisition. The scale-up in the vertical was supported inorganically with the acquisition of SMI (USD 10mn revenue) and also improved the offshore delivery network of the company. HAPPSTMN has supported key projects such as the setup of a Security Operations Center (SOC) for India's leading telco. Several large Indian automotive OEMs and universities feature in the company's client roster.

Financial Summary

| YE March (INR bn) | FY21 | FY22 | FY23 | FY24 | FY25E | FY26E |
|-------------------|------|-------|-------|-------|-------|-------|
| Revenue (USD mn) | 104 | 147 | 178 | 196 | 263 | 331 |
| Net Sales | 7.73 | 10.94 | 14.29 | 16.25 | 21.95 | 28.09 |
| EBIT | 1.69 | 2.25 | 3.17 | 2.78 | 3.54 | 4.99 |
| APAT | 1.62 | 1.86 | 2.36 | 2.38 | 2.72 | 3.81 |
| Diluted EPS (INR) | 10.7 | 12.2 | 15.5 | 15.6 | 17.9 | 25.0 |
| P/E (x) | 82.9 | 72.5 | 57.1 | 56.6 | 49.4 | 35.3 |
| EV / EBITDA (x) | 68.3 | 50.5 | 36.9 | 37.4 | 28.8 | 21.1 |
| RoE (%) | 40.0 | 30.6 | 31.3 | 20.5 | 17.4 | 21.5 |

Source: Company, HSIE Research

ADD

| | |
|-------------------------|---------|
| CMP (as on 18 Jun 2024) | INR 884 |
| Target Price | INR 900 |
| NIFTY | 23,558 |

| KEY CHANGES | OLD | NEW |
|--------------|---------------|---------------|
| Rating | ADD | ADD |
| Price Target | INR 875 | INR 900 |
| EPS % | FY25E -1.7 | FY26E +2.9 |

KEY STOCK DATA

| | |
|------------------------------|---------------|
| Bloomberg code | HAPPSTMN IN |
| No. of Shares (mn) | 152 |
| MCap (INR bn) / (\$ mn) | 137/1,614 |
| 6m avg traded value (INR mn) | 467 |
| 52 Week high / low | INR 1,023/738 |

STOCK PERFORMANCE (%)

| | 3M | 6M | 12M |
|--------------|------|--------|--------|
| Absolute (%) | 12.3 | (5.6) | (2.6) |
| Relative (%) | 5.9 | (13.7) | (24.6) |

SHAREHOLDING PATTERN (%)

| | Dec-23 | Mar-24 |
|-----------------|--------|--------|
| Promoters | 50.24 | 50.24 |
| FIs & Local MFs | 2.41 | 2.57 |
| FPIs | 5.05 | 4.69 |
| Public & Others | 42.30 | 42.50 |
| Pledged Shares | 3.60 | 3.60 |

Source : BSE

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Pure Software acquisition: The acquisition rationale is to build depth in industry verticals - BFSI and Healthcare, cross-sell opportunity into marquee logos (Prudential, S&P etc.), banking as a service platform (Arthta) and access nearshore delivery centers of Mexico.

Key highlights include: (1) Pure Software was acquired by the company for a purchase consideration of USD 94.5mn (including upfront USD 77mn and an earnout of USD 17mn in a year) at 2.2x revenue (including earn-out) and approx. 12x EBITDA. (2) Pure Software is a software product engineering and IT services company headquartered in Noida with global operations and 1,200 employees. (3) It operates in verticals of BFSI, Lifescience, and Healthcare with BFSI nearly 50% of its revenue. (4) The company has a partnership with Oracle in cloud services by providing SLA-based services and operations support (Identity Cloud Service, OCI Cloud Solutions, OCI Core Infrastructure). (5) The acquisition will add ~22% to Happiest Minds' revenue and can scale its BFSI revenue as well as its Healthcare revenue—currently, the BFSI revenue is at USD 21mn and Healthcare revenue is at USD 28mn, both of which will double with the acquisition. (6) PureSoftware's Board includes Anil Baid (Founder and Chief Strategy Officer) and Manish Sharma, CEO since 2016 (earlier VP, Business Head – ASEAN and China at HCL Tech).

Aureus acquisitions: The acquisition rationale is to scale Happiest Minds' BFSI revenue – currently, the Insurance segment is a small component of BFSI. Marquee client access to leading global reinsurers such as Swiss Re and Hannover Re with cross-sell opportunities in IMSS service-line and data & analytics seems to be the rationale.

Key highlights include: (1) Aureus Tech Systems LLC (Aureus) was acquired which is a US-based digital services company with Microsoft expertise largely operating in the Insurance vertical— HAPSTMN bought 100% in the company (all cash) for USD 8.5mn upfront and a deferred component (up to USD 8.5mn earnout over the next two years). (2) Aureus has 150 employees and revenue of USD 8.3mn (~4% of Happiest Minds revenue) with its revenue CAGR at 22% over CY21-23. (2) Its operating margins are ~20%, supported by 140 employees in its Hyderabad offshore office and ~10 onsite consultants. (3) Aureus' anchor customer is Swiss Re (>70% of Aureus' revenue). (4) Aureus is a Microsoft-certified Gold and co-sell partner and has supported Swiss Re's Corporate Solution business or its commercial insurance arm (CorSo). (5) Aureus has helped in transforming its CRM using Microsoft Azure, integration with Dynamics Marketing. (6) Swiss Re captive in India has 2,000 employees and was set up in 2001 with GBS presence in Hyderabad and Bangalore (*there are currently 120 job postings for India GBS of Swiss Re*). (7) Swiss Re has also undergone leadership change with CEO transition (group CEO Andreas Berger taking over in July 2024 and India CEO Amitabha Ray appointed in Apr 2024). (8) Key personnel in the company include Abhishek Pakhira—CEO and Debjit Kanjilal—MD (former Swiss Re SVP, Global IT).

Exhibit 1: HAPSTMN's acquisition history

| Year | Acquisitions | Purchase consideration | Services |
|------|------------------------------------|------------------------------|--|
| 2024 | Aureus | USD 17mn (USD 8.5mn upfront) | Product engineering services - Azure (Insurance & Healthcare) – 150 employees |
| 2024 | Pure Software | USD 94mn (USD 77mn upfront) | Digital services (BFSI & Healthcare) – 1,200 employees |
| 2024 | Macmillan Learning India | INR 45mn | Software development services/ ODC takeover |
| 2023 | SMI (Sri Mookambika Infosolutions) | INR 1.10bn | Product engineering services - 400 employees, Offshore delivery - Madurai/Coimbatore |
| 2021 | PGS | USD 8.2mn | Pimcore implementation services |
| 2018 | OSS Cube | INR 0.21bn | Consulting & digital services |
| 2018 | Cupola Technology | INR 0.07bn | IoT solutions and services |

Source: Company, HSIE Research

Exhibit 2: Recent deal wins

| Vertical | Deals |
|------------|---|
| Healthcare | build an advanced AI Medical Preventive & Diagnostic solution for MindSculpt Analytics |
| Healthcare | strategic partnership in engineering and development for mission critical applications |
| Healthcare | build the asset management platform to provide actionable insights to the field service technicians for MedTech company |
| BFSI | GenAI solution for training employees on performance management & customer support |
| Retail | GenAI solution for local language and enterprise knowledge for SE Asia bottler |
| Hi-Tech | design and configure an end-to-end secure and scalable connected vehicle platform on cloud platform for professional services arm of global hyperscaler |
| Retail | revamp the User Experience of front facing applications of their Distributed Management Systems for global CPG company |
| TM&E | provide product engineering services for the Imagineering division of premier entertainment company |
| TM&E | providing digital transformation services leveraging the Pimcore Platform for global movie chain |
| Industrial | Strategic partnership to build platform to optimise wind energy generation for Enercon |
| EduTech | digital engineering services for technology platform |
| EduTech | build next generation solution for increased engagement and improved efficiency with students and universities |

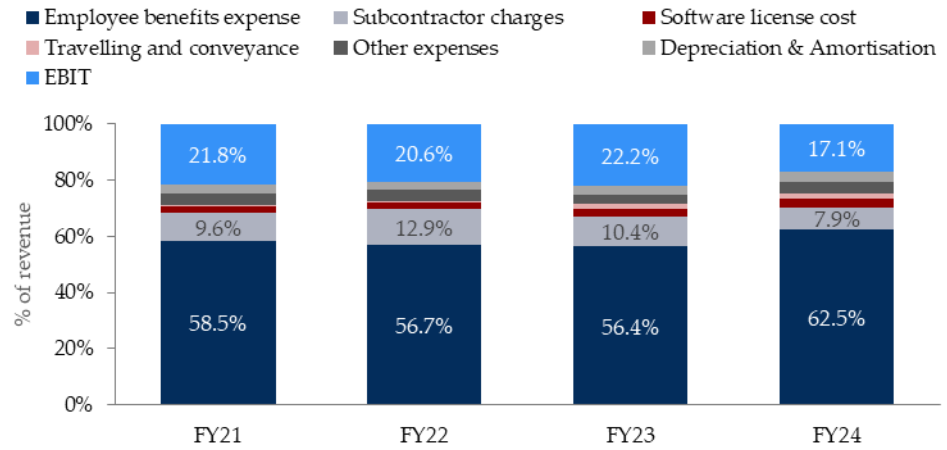
Source: Company, HSIE Research

Exhibit 3: Key Partnerships

| Partners | Partnership tiering |
|------------|--|
| AWS | Advanced Consulting Services Partner |
| Microsoft | Member of the Microsoft AI Cloud Partner Program |
| Pimcore | Strategic partnership |
| ServiceNow | Premier managed services partner |
| Outsystems | Strategic partnership |

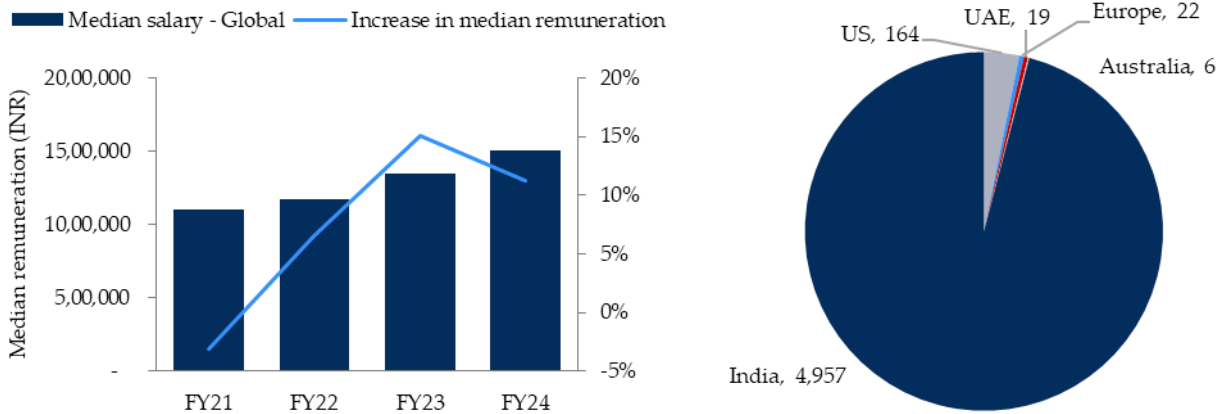
Source: FY24 Annual Report

Exhibit 4: Lower sub-contracting offset the impact of higher employee expense



Source: Company, HSIE Research

Exhibit 5: Increase in median remuneration and geo mix of employees



Source: Company, HSIE Research

Exhibit 6: Change in estimates

| YE Mar (INR bn) | FY25E Old | FY25E Revised | Change % | FY26E Old | FY26E Revised | Change % |
|------------------|-----------|---------------|----------|-----------|---------------|----------|
| Revenue (USD mn) | 262 | 263 | 0.4 | 330 | 331 | 0.3 |
| Revenue | 21.86 | 21.95 | 0.4 | 28.01 | 28.09 | 0.3 |
| EBIT | 3.60 | 3.54 | (1.8) | 4.86 | 4.99 | 2.7 |
| EBIT margin (%) | 16.5 | 16.1 | -36bps | 17.4 | 17.8 | 42bps |
| APAT | 2.77 | 2.72 | (1.7) | 3.70 | 3.81 | 2.9 |
| EPS (INR) | 18.2 | 17.9 | (1.7) | 24.3 | 25.0 | 2.9 |

Source: HSIE Research

Financials

Income Statement

| Year ending March (INR bn) | FY21 | FY22 | FY23 | FY24 | FY25E | FY26E |
|-----------------------------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Net Sales (USD mn) | 104 | 147 | 178 | 196 | 263 | 331 |
| <i>Growth (%)</i> | 12.2 | 41.0 | 21.3 | 10.3 | 34.0 | 25.8 |
| Net Sales | 7.73 | 10.94 | 14.29 | 16.25 | 21.95 | 28.09 |
| <i>Growth (%)</i> | 10.8 | 41.4 | 30.7 | 13.7 | 35.1 | 28.0 |
| Employee Expenses | 4.52 | 6.20 | 8.07 | 10.15 | 13.41 | 17.03 |
| SG&A and Other Operating Expenses | 1.30 | 2.16 | 2.64 | 2.74 | 3.93 | 4.81 |
| EBIDTA | 1.91 | 2.58 | 3.59 | 3.36 | 4.62 | 6.25 |
| Depreciation | 0.23 | 0.33 | 0.42 | 0.58 | 1.08 | 1.26 |
| EBIT | 1.69 | 2.25 | 3.17 | 2.78 | 3.54 | 4.99 |
| <i>EBIT (%)</i> | 21.8 | 20.6 | 22.2 | 17.1 | 16.1 | 17.8 |
| <i>EBIT Growth (%)</i> | 119.5 | 33.2 | 41.0 | (12.4) | 27.5 | 41.1 |
| Other Income | 0.24 | 0.31 | 0.15 | 0.99 | 0.55 | 0.57 |
| Interest | 0.07 | 0.10 | 0.22 | 0.42 | 0.41 | 0.41 |
| PBT | 1.86 | 2.46 | 3.10 | 3.35 | 3.68 | 5.15 |
| Tax (incl deferred) | 0.24 | 0.65 | 0.79 | 0.86 | 0.96 | 1.34 |
| RPAT | 1.62 | 1.81 | 2.31 | 2.48 | 2.72 | 3.81 |
| APAT | 1.62 | 1.86 | 2.36 | 2.38 | 2.72 | 3.81 |
| <i>APAT Growth (%)</i> | 96.5 | 14.3 | 26.9 | 1.0 | 14.4 | 39.9 |
| EPS (INR) | 10.7 | 12.2 | 15.5 | 15.6 | 17.9 | 25.0 |
| <i>EPS Growth (%)</i> | 96.5 | 14.3 | 26.9 | 1.0 | 14.4 | 39.9 |

Source: Company, HSIE Research

Balance Sheet

| Year ending March (INR bn) | FY21 | FY22 | FY23 | FY24 | FY25E | FY26E |
|------------------------------------|-------------|-------------|--------------|--------------|--------------|--------------|
| SOURCES OF FUNDS | | | | | | |
| Share Capital - Equity | 0.28 | 0.29 | 0.29 | 0.30 | 0.30 | 0.30 |
| Reserves | 5.18 | 6.37 | 8.10 | 14.50 | 16.20 | 18.64 |
| Total Shareholders' Funds | 5.46 | 6.66 | 8.39 | 14.80 | 16.50 | 18.94 |
| Total Debt | 1.46 | 1.91 | 4.68 | 4.42 | 4.42 | 4.42 |
| Net Deferred Taxes | (0.03) | (0.02) | 0.08 | (0.03) | (0.03) | (0.03) |
| Long Term Provisions & Others | 0.53 | 0.70 | 0.92 | 0.83 | 0.83 | 0.83 |
| TOTAL SOURCES OF FUNDS | 7.43 | 9.24 | 14.07 | 20.02 | 21.72 | 24.16 |
| APPLICATION OF FUNDS | | | | | | |
| Net Block | 0.52 | 0.79 | 2.93 | 2.73 | 5.40 | 5.92 |
| CWIP | 0.00 | 0.00 | 0.02 | 0.00 | 0.00 | 0.00 |
| Goodwill | 0.76 | 0.79 | 1.39 | 1.40 | 6.92 | 6.92 |
| Other non-current assets | 0.39 | 0.33 | 1.21 | 0.40 | 0.40 | 0.40 |
| Total Non-Current Assets | 1.67 | 1.91 | 5.55 | 4.54 | 12.73 | 13.25 |
| Cash & Equivalent | 5.37 | 6.32 | 6.92 | 13.37 | 5.92 | 6.83 |
| Debtors | 1.22 | 1.67 | 2.13 | 2.54 | 3.44 | 4.40 |
| Other Current Assets | 0.86 | 1.28 | 1.68 | 1.87 | 2.42 | 3.01 |
| Total Current Assets | 2.08 | 2.95 | 3.81 | 4.41 | 5.86 | 7.41 |
| Creditors | 0.41 | 0.61 | 0.71 | 0.79 | 1.06 | 1.36 |
| Other Current Liabilities & Provns | 1.28 | 1.33 | 1.51 | 1.50 | 1.72 | 1.97 |
| Total Current Liabilities | 1.69 | 1.94 | 2.22 | 2.29 | 2.79 | 3.33 |
| Net Current Assets | 0.39 | 1.02 | 1.60 | 2.12 | 3.07 | 4.09 |
| TOTAL APPLICATION OF FUNDS | 7.43 | 9.24 | 14.07 | 20.02 | 21.72 | 24.16 |

Source: Company, HSIE Research

Cash Flow

| Year ending March (INR bn) | FY21 | FY22 | FY23 | FY24 | FY25E | FY26E |
|---------------------------------------|---------------|---------------|---------------|---------------|---------------|---------------|
| Reported PBT | 1.86 | 2.46 | 3.10 | 3.35 | 3.68 | 5.15 |
| Non-operating & EO items | (0.07) | (0.12) | (0.15) | (0.90) | (0.41) | (0.42) |
| Interest expenses | 0.07 | 0.10 | 0.22 | 0.42 | 0.41 | 0.41 |
| Depreciation | 0.23 | 0.33 | 0.42 | 0.58 | 1.08 | 1.26 |
| Working Capital Change | (0.29) | (0.55) | (0.63) | (0.31) | (0.95) | (1.02) |
| Tax paid | (0.36) | (0.53) | (0.89) | (1.02) | (0.96) | (1.34) |
| OPERATING CASH FLOW (a) | 1.44 | 1.68 | 2.07 | 2.13 | 2.86 | 4.05 |
| Capex | (0.01) | (0.04) | (1.39) | (0.10) | (9.28) | (1.78) |
| Free cash flow (FCF) | 1.43 | 1.64 | 0.68 | 2.02 | (6.42) | 2.27 |
| Investments | (2.83) | (0.84) | (2.03) | (4.56) | - | - |
| Non-operating income | - | - | - | - | 0.41 | 0.42 |
| INVESTING CASH FLOW (b) | (2.84) | (0.88) | (3.43) | (4.66) | (8.87) | (1.36) |
| Debt Issuance | 0.67 | (0.21) | (0.26) | (0.85) | - | - |
| Interest expenses | (0.04) | (0.03) | (0.15) | (0.33) | (0.41) | (0.41) |
| FCFE | 2.06 | 1.40 | 0.27 | 0.84 | (6.83) | 1.86 |
| Share capital Issuance | 1.06 | 0.02 | 0.01 | 0.02 | 0.01 | - |
| Dividend/buyback | - | (0.68) | (0.57) | (0.86) | (1.03) | (1.37) |
| FINANCING CASH FLOW (c) | 1.69 | (0.91) | (0.97) | (2.02) | (1.44) | (1.78) |
| NET CASH FLOW (a+b+c) | 0.29 | (0.11) | (2.32) | (4.56) | (7.44) | 0.91 |
| Non-operating and EO items | 3.80 | 1.06 | 2.92 | 11.01 | - | - |
| Closing Cash & Equivalents | 5.37 | 6.32 | 6.92 | 13.37 | 5.92 | 6.83 |

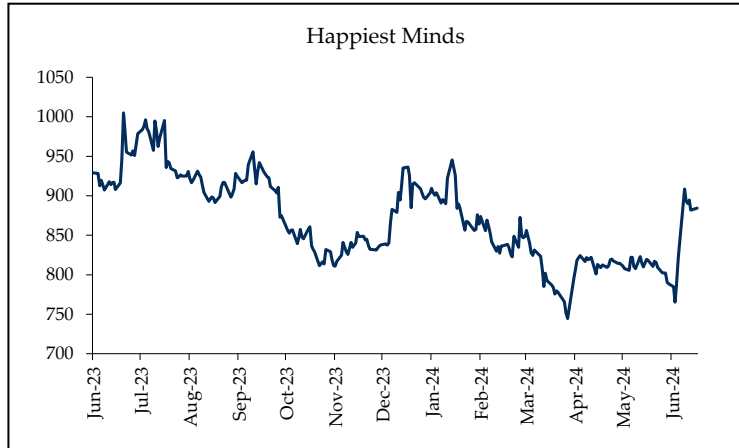
Source: Company, HSIE Research

Key Ratios

| | FY21 | FY22 | FY23 | FY24 | FY25E | FY26E |
|------------------------------------|-------|-------|-------|-------|-------|-------|
| PROFITABILITY (%) | | | | | | |
| GPM | 41.5 | 43.3 | 43.6 | 37.5 | 38.9 | 39.4 |
| EBITDA Margin | 24.8 | 23.6 | 25.1 | 20.7 | 21.0 | 22.3 |
| APAT Margin | 21.0 | 17.0 | 16.5 | 14.6 | 12.4 | 13.6 |
| RoE | 40.0 | 30.6 | 31.3 | 20.5 | 17.4 | 21.5 |
| RoIC (or Core RoCE) | 66.3 | 66.5 | 46.9 | 29.8 | 23.3 | 22.3 |
| RoCE | 30.4 | 23.2 | 21.6 | 15.8 | 14.5 | 17.9 |
| EFFICIENCY | | | | | | |
| Tax Rate (%) | 12.7 | 26.3 | 25.5 | 25.8 | 26.0 | 26.0 |
| Fixed Asset Turnover (x) | NA | NA | 7.4 | 7.9 | 9.0 | 9.7 |
| Debtors (days) | 58 | 56 | 54 | 57 | 57 | 57 |
| Other Current Assets (days) | 41 | 43 | 43 | 42 | 40 | 39 |
| Payables (days) | 19 | 20 | 18 | 18 | 18 | 18 |
| Other Current Liab & Provns (days) | 60 | 44 | 39 | 34 | 29 | 26 |
| Cash Conversion Cycle (days) | 18 | 34 | 41 | 48 | 51 | 53 |
| Debt/EBITDA (x) | 0.8 | 0.7 | 1.3 | 1.3 | 1.0 | 0.7 |
| Net D/E (x) | (0.7) | (0.7) | (0.3) | (0.6) | (0.1) | (0.1) |
| Interest Coverage (x) | 24 | 23 | 14 | 7 | 9 | 12 |
| PER SHARE DATA (INR) | | | | | | |
| EPS | 10.7 | 12.2 | 15.5 | 15.6 | 17.9 | 25.0 |
| CEPS | 12.2 | 15.0 | 19.1 | 19.5 | 25.0 | 33.3 |
| Dividend | 3.0 | 3.8 | 5.4 | 5.8 | 6.8 | 9.0 |
| Book Value | 36 | 46 | 58 | 97 | 108 | 124 |
| VALUATION | | | | | | |
| P/E (x) | 82.9 | 72.5 | 57.1 | 56.6 | 49.4 | 35.3 |
| P/BV (x) | 24.7 | 19.3 | 15.3 | 9.1 | 8.2 | 7.1 |
| EV/EBITDA (x) | 68.3 | 50.5 | 36.9 | 37.4 | 28.8 | 21.1 |
| EV/Revenues (x) | 16.9 | 11.9 | 9.3 | 7.7 | 6.1 | 4.7 |
| OCF/EV (%) | 1.1 | 1.3 | 1.6 | 1.7 | 2.1 | 3.1 |
| FCF/EV (%) | 1.1 | 1.3 | 0.5 | 1.6 | (4.8) | 1.7 |
| FCFE/Mkt Cap (%) | 1.5 | 1.1 | 0.2 | 0.6 | (5.1) | 1.4 |
| Dividend Yield (%) | 0.3 | 0.4 | 0.6 | 0.7 | 0.8 | 1.0 |

Source: Company, HSIE Research

1 Yr Price Movement



Rating Criteria

BUY: $>+15\%$ return potential

ADD: $+5\%$ to $+15\%$ return potential

REDUCE: -10% to $+5\%$ return potential

SELL: $> 10\%$ Downside return potential

Disclosure:

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