

15 November 2024

India | Equity Research | Q2FY25 results review

## Happiest Minds Technologies

Technology

### Banking on acquisition synergies; tall ask to achieve growth guidance

Happiest Minds (HAPPSTMN) reported Q2FY25 revenue growth of 12.7/12.3% QoQ CC/USD. Organic revenue declined 3.4% QoQ USD (as per our estimates), implying growth challenges in organic portfolio. Management is witnessing positive changes in demand environment and expects strong Q4 led by cross-selling synergies from acquisitions, strong deal pipeline and ramp up of existing deals. However, ask rate of 5.2% CQGR in H2FY25 to achieve lower end of the guidance (30-35% YoY CC in FY25) seems a tall ask, given the seasonal headwinds in Q3. We model in 28% YoY CC (6.5% organic) growth in FY25E. Cut EPS by 22%/15%/13% for FY25/26/27E led by cut in revenue and margin estimates and higher interest costs on account of additional loans taken by the company in Q2. Retain **HOLD** with revised TP of INR 710 (average of P/E INR 620 and DCF of INR 800).

### Miss on revenue, muted organic revenue

HAPPSTMN reported revenue growth of 12.7/12.3% QoQ CC/USD, lower than our expectations of 16.1% QoQ CC. We estimate 2-month incremental impact of acquisitions (PureSoftware and Aureus) of USD 8.8 mn, implying decline in organic revenue growth of -3.4% QoQ USD. Revenue growth was led by PDES (15.3% QoQ USD) and GBS (18.6% QoQ USD). IMSS declined 1.5% QoQ USD. Management mentioned growth was led by stable demand environment and higher volumes.

### Tall ask to achieve lower end of revenue guidance

HAPPSTMN retained revenue guidance of 30-35% YoY CC for FY25. Ask rate of 5.2% CQGR in H2FY25 to achieve lower end of the guidance seems a tall ask given the seasonal headwinds in Q3. Management is witnessing positive changes in demand environment and expects a strong Q4. Demand in BFSI and manufacturing has improved. For H2FY25, the company is baking in – 1) couple of deal closures in Arttha banking platform and strong seasonality in Arttha in Q4, 2) cross-selling synergies from acquisitions, 3) ramp up in two USD5mn+ clients and 4) ramp up of Gen AI projects and large deals.

### Margin impacted by wage hikes and Gen AI investments

EBITDA margin (excluding other income) stood at 17.6%, down ~210bps QoQ due to 1) wage hike impact of 230bps QoQ, 2) INR 90mn investments in Gen AI with impact of 150bps QoQ and 3) investments in sales leadership.

### Financial Summary

Y/E March (INR mn)	FY24A	FY25E	FY26E	FY27E
Net Revenue	16,247	20,812	25,753	30,274
EBITDA	3,359	3,932	5,542	6,853
EBITDA Margin (%)	20.7	18.9	21.5	22.6
Net Profit	2,484	2,166	2,930	3,727
EPS (INR)	15.7	14.8	19.5	24.8
EPS % Chg YoY	(3.9)	(5.6)	31.4	27.2
P/E (x)	46.8	49.6	37.7	29.7
EV/EBITDA (x)	33.6	30.7	21.6	17.3
RoCE (%)	12.5	9.4	12.0	15.3
RoE (%)	21.4	14.1	17.8	20.7

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#### Market Data

Market Cap (INR)	112bn
Market Cap (USD)	1,326mn
Bloomberg Code	HAPPSTMN IN
Reuters Code	HAPP BO
52-week Range (INR)	961 /732
Free Float (%)	53.0
ADTV-3M (mn) (USD)	4.6

Price Performance (%)	3m	6m	12m
Absolute	(2.1)	(9.6)	(11.8)
Relative to Sensex	(0.2)	(15.8)	(31.3)

ESG Score	2023	2024	Change
ESG score	72.1	NA	NA
Environment	45.4	NA	NA
Social	77.8	NA	NA
Governance	81.2	NA	NA

Note - Score ranges from 0 - 100 with a higher number indicating a higher ESG score.

Source: SES ESG, I-sec research

Earnings Revisions (%)	FY25E	FY26E	FY27E
Revenue	(3.3)	(4.6)	(5.3)
EBIT	(16.5)	(15.2)	(12.7)
EPS	(22.1)	(15.5)	(13.2)

#### Previous Reports

14-08-2024: [Q1FY25 results review](#)

08-05-2024: [Q4FY24 results review](#)

### Margin outlook

The company maintained EBITDA (including other income) margin guidance of 20-22% for FY25. In Q3, there would be headwinds from seasonal furloughs, lower billing days, pay hike to senior employees and investments in Arttha banking platform. We assume margin at the lower end of the guidance band at ~20% for FY25 and expect it to improve in FY26 and FY27 as investments in sales leadership yield results and Gen AI BU scales up.

### Progressive on Gen AI business unit

HAPPSTMN reported revenue of USD 1.01mn (1.6% of total revenue) in Q2. It won a large deal from European Health Research Institute to build its AI/ML platform. For a large beverage maker, HAPPSTMN is leveraging Microsoft Azure AI to implement a Gen AI solution to drive workforce efficiency and improve utilisation of customer-facing assets. It is working on 25 different Gen AI projects in areas of employee productivity, audio sentiment analytics, informational retrieval and classification, persona-based virtual engagements. It has 120 employees in Gen AI BU and 350+ in AI and Analytics CoE (Centre of Excellence). Utilisation in Gen AI BU is still low at 20-25% because projects are in POC stages. Projects involving adding Gen AI features to software products of clients are seeing better traction.

### Outlook on edutech (largest vertical)

Edutech vertical growth has been flattish over the last four quarters. In edutech vertical (~20% of revenue), HAPPSTMN serves three key segments -1) higher education, 2) K12 and 3) professional education. Higher education segment is impacted by structural challenges due to reduction in number of student enrolments and cost pressures faced by universities. Demand in K12 segment is cyclical. Professional education is growing well led by demand for up-skilling.

### Other highlights

- Company won multi-million dollar deal (largest ever) to provide cybersecurity services for one of the largest pharmaceutical contract manufacturers.
- Company appointed Maninder Singh, Chief Growth Officer, to focus on net new large deal wins. Before joining HAPPSTMN, Maninder was Business Segment Head and P&L owner for Retail and Consumer Goods vertical at Tech Mahindra. Before Tech Mahindra, Maninder has worked with Accenture, Genpact and HCL in various sales and leadership roles.
- Company has beefed up sales leadership for each industry vertical.
- 144 campus hires were onboarded in H1FY25.
- Company is increasing capacity across existing delivery centres of Bangalore, Pune and Noida, adding about 500 people in H1FY25. It is also expanding its capacity in Hyderabad by 150+ seats.
- Billion \$ clients increased to 82, +2 clients QoQ, +25 clients YoY.
- Average revenue per active customer at USD 842K improved 0.2% QoQ, 4.7% YoY.
- In contrast to IT services peers, LTM attrition increased 90bps QoQ to 14.4%.
- Interest costs increased to INR 255 mn (+47% QoQ, 141% YoY) due to debt raised for paying consideration for acquisitions. It borrowed USD 8mn for payment towards Auerus acquisition and borrowed 50% of up-front consideration of INR 6,350mn paid for PureSoftware acquisition.

**Key upside risks:** 1) Global macro concerns around high interest rates and inflation subsiding sooner than expected. 2) Stronger-than-expected demand.

**Key downside risks:** 1) Longer than expected current global macro down-cycle extending beyond CY24. 2) Inability to merge the acquired entities for synergy.

**Exhibit 1: Q2FY25 result review**

INR mn	Q2FY25	Q1FY25	QoQ	Q2FY24	YoY	Q2FY25E-ISEC	vs our estimates
Revenue QoQ CC	12.7%	11.4%		3.6%		16.1%	
Sales (USD mn)	62	56	12.4%	49	27.0%	64	-3.2%
Average (USD rate)	83.6	83.6	0.0%	82.8	1.0%	83.6	0.0%
<b>INR mn</b>							
Sales	5,216	4,638	12.5%	4,066	28.3%	5,386	-3.1%
EBIT	662	668	-0.9%	675	-1.9%	794	-16.7%
EBIT Margin	12.7%	14.4%	-171 bps	16.6%	-390 bps	14.7%	-206 bps
Reported PAT	495	510	-3.0%	585	-15.3%	644	-23.1%
EPS	3.3	3.4	-3.0%	3.9	-15.5%	4.3	-23.1%

Source: Company data, I-Sec research

**Exhibit 2: HAPPSTMN – change in estimates**

	Revised			Old			Change (%)		
	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E	FY25E	FY26E	FY27E
Revenues (USD mn)	249	307	360	257	321	380	-3.3%	-4.6%	-5.3%
Revenue YoY CC	28.1%	23.2%	17.6%	32.2%	24.8%	18.4%	-410bps	-160bps	-80bps
Revenue growth (USD, %)	26.9%	23.1%	17.6%	31.2%	24.8%	18.4%	-430bps	-170bps	-80bps
USD/INR	83.6	84.0	84.0	83.6	84.0	84.0	0.0%	0.0%	0.0%
<b>INR mn</b>									
Revenues	20,812	25,753	30,274	21,517	26,993	31,952	-3.3%	-4.6%	-5.3%
EBIT	2,893	4,278	5,367	3,463	5,048	6,150	-16.5%	-15.2%	-12.7%
EBIT margin	13.9%	16.6%	17.7%	16.1%	18.7%	19.2%	-220bps	-210bps	-150bps
EPS (INR/share)	14.4	19.5	24.8	18.5	23.1	28.6	-22.1%	-15.5%	-13.2%

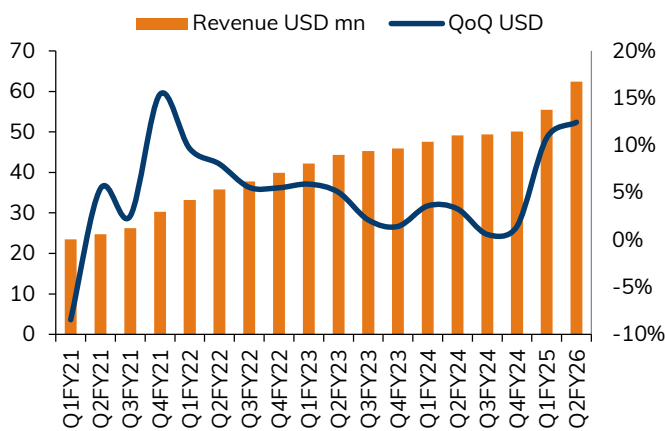
Source: Company data, I-Sec research

**Exhibit 3: Valuation methodology**

Valuation	Average of DCF, P/E
Weightage to DCF-based valuation	50%
P/E valuation-based Target Price arrived at by valuing at 30x Q2FY26 to Q1FY27 EPS of INR 21	INR 620
DCF valuation-based Target Price	INR 800
<b>Target Price</b>	<b>INR 710</b>

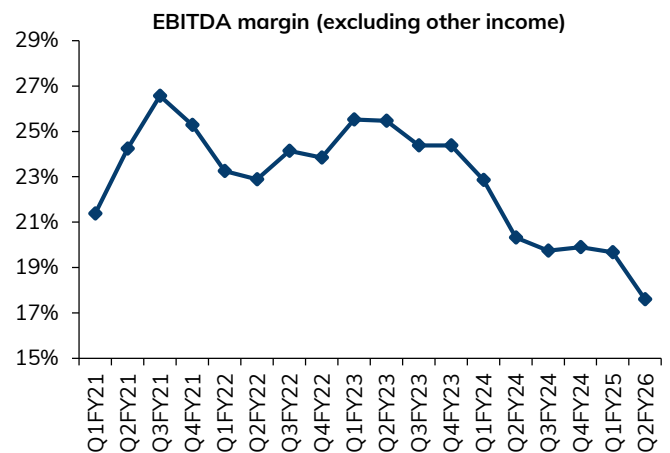
Source: I-Sec research, Company data

**Exhibit 4: Q2FY25 revenue growth boosted by acquisitions**



Source: I-Sec research, Company data

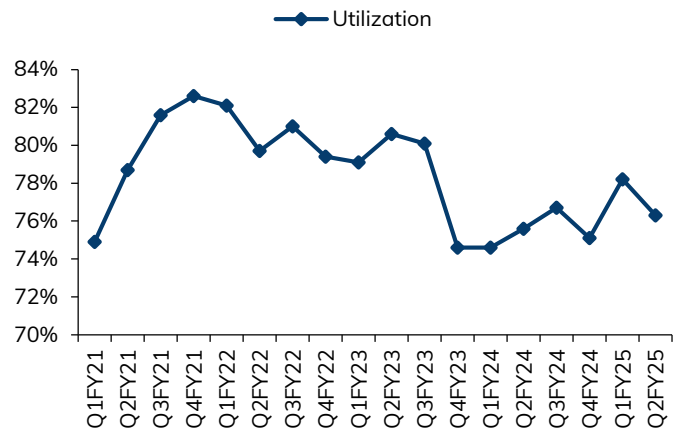
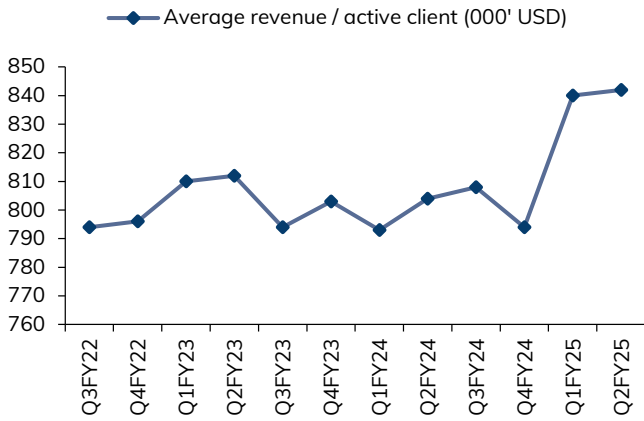
**Exhibit 5: EBITDA margin impacted wage hike and investments in Gen AI and sales**



Source: I-Sec research, Company data

**Exhibit 6: Average revenue per active client up ~5% YoY**

**Exhibit 7: Utilisation dipped QoQ due to fresher addition**



Source: I-Sec research, Company data

Source: I-Sec research, Company data

**Exhibit 8: Shareholding pattern**

%	Mar'24	Jun'24	Sep'24
Promoters	50.2	44.2	44.2
Institutional investors	7.3	7.3	9.5
MFs and others	1.3	1.5	2.7
FIs/Banks	0.0	0.0	0.0
Insurance	1.3	1.3	1.5
FIIIs	4.7	5.4	5.3
Others	42.5	47.6	46.3

Source: Bloomberg

**Exhibit 9: Price chart**



Source: Bloomberg

## Financial Summary

### Exhibit 10: Profit & Loss

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
<b>Net Sales (USD mn)</b>	<b>196</b>	<b>249</b>	<b>307</b>	<b>360</b>
<b>Net Sales (INR. mn)</b>	<b>16,247</b>	<b>20,812</b>	<b>25,753</b>	<b>30,274</b>
Operating Expense	12,888	16,881	20,211	23,421
<b>EBITDA</b>	<b>3,359</b>	<b>3,932</b>	<b>5,542</b>	<b>6,853</b>
EBITDA Margin (%)	20.7	18.9	21.5	22.6
Depreciation & Amortization	603	1,038	1,264	1,486
EBIT	2,755	2,893	4,278	5,367
Interest expenditure	402	939	1,020	1,020
Other Non-operating Income	854	1,059	750	750
<b>Recurring PBT</b>	<b>3,207</b>	<b>3,013</b>	<b>4,007</b>	<b>5,097</b>
<b>Profit / (Loss) from Associates</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Less: Taxes	863	783	1,077	1,370
PAT	2,344	2,231	2,930	3,727
Less: Minority Interest	-	-	-	-
<b>Net Income (Reported)</b>	<b>2,484</b>	<b>2,166</b>	<b>2,930</b>	<b>3,727</b>
Extraordinaries (Net)	-	-	-	-
<b>Recurring Net Income</b>	<b>2,484</b>	<b>2,166</b>	<b>2,930</b>	<b>3,727</b>

Source Company data, I-Sec research

### Exhibit 11: Balance sheet

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
<b>Total Current Assets</b>	<b>17,778</b>	<b>19,551</b>	<b>19,001</b>	<b>18,903</b>
of which cash & cash eqv.	1,147	631	(565)	(1,328)
<b>Total Current Liabilities &amp; Provisions</b>	<b>2,049</b>	<b>3,746</b>	<b>4,021</b>	<b>4,250</b>
<b>Net Current Assets</b>	<b>15,728</b>	<b>15,804</b>	<b>14,980</b>	<b>14,653</b>
Investments	-	-	-	-
<b>Net Fixed Assets</b>	<b>1,379</b>	<b>1,408</b>	<b>1,409</b>	<b>1,410</b>
ROU Assets	570	692	692	692
Capital Work-in-Progress	-	-	-	-
Goodwill	1,403	7,533	7,533	7,533
Other assets	568	707	707	707
Deferred Tax Assets	-	-	-	-
<b>Total Assets</b>	<b>20,429</b>	<b>28,712</b>	<b>27,890</b>	<b>27,563</b>
<b>Liabilities</b>				
<b>Borrowings</b>	<b>4,424</b>	<b>10,733</b>	<b>8,633</b>	<b>6,533</b>
<b>Deferred Tax Liability</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
provisions	334	499	499	499
other Liabilities	170	807	807	807
Minority Interest	-	-	-	-
Equity Share Capital	299	300	300	300
Reserves & Surplus*	14,504	15,543	16,820	18,593
<b>Total Net Worth</b>	<b>14,802</b>	<b>15,842</b>	<b>17,120</b>	<b>18,893</b>
<b>Total Liabilities</b>	<b>20,429</b>	<b>28,712</b>	<b>27,890</b>	<b>27,563</b>

Source Company data, I-Sec research

### Exhibit 12: Quarterly trend

(INR mn, year ending March)

	Dec-23	Mar-24	Jun-24	Sep-24
Net Sales	4,099	4,173	4,638	5,216
% growth (YOY)	0.8	1.8	11.2	12.5
EBITDA	809	830	913	918
Margin %	19.7	19.9	19.7	17.6
Other Income	142	151	80	15
Adjusted Net Profit	596	720	510	495

Source Company data, I-Sec research

### Exhibit 13: Cashflow statement

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
CFO before WC changes	3,347	2,949	4,007	5,097
<b>CFO after WC changes</b>	<b>3,150</b>	<b>2,029</b>	<b>4,149</b>	<b>5,397</b>
Capital Commitments	(103)	(9,107)	(1,265)	(1,487)
<b>Free Cashflow</b>	<b>2,229</b>	<b>10,354</b>	<b>4,337</b>	<b>5,514</b>
Other investing cashflow	(4,561)	1,271	750	750
<b>Cashflow from Investing Activities</b>	<b>(4,664)</b>	<b>(7,836)</b>	<b>(515)</b>	<b>(737)</b>
Issue of Share Capital	-	1	0	-
Interest Cost	(331)	-	-	-
Inc (Dec) in Borrowings	118	6,309	(2,100)	(2,100)
<b>Cash flow from Financing Activities</b>	<b>3,635</b>	<b>6,073</b>	<b>(3,753)</b>	<b>(4,054)</b>
Dividend paid	(860)	(1,127)	(1,653)	(1,954)
Others	4,708	890	-	-
<b>Chg. in Cash &amp; Bank balance</b>	<b>1,096</b>	<b>(516)</b>	<b>(1,196)</b>	<b>(763)</b>
Closing cash & balance	1,089	631	(565)	(1,328)

Source Company data, I-Sec research

### Exhibit 14: Key ratios

(Year ending March)

	FY24A	FY25E	FY26E	FY27E
<b>Per Share Data (INR)</b>				
Reported EPS	15.7	14.8	19.5	24.8
Diluted EPS	15.7	14.8	19.5	24.8
Cash EPS	20.7	21.3	27.9	34.7
Dividend per share (DPS)	5.8	7.5	11.0	13.0
Book Value per share (BV)	99.3	105.4	113.9	125.7
Dividend Payout (%)	36.7	50.5	56.4	52.4
<b>Growth (%)</b>				
Net Sales	13.7	28.1	23.7	17.6
EBITDA	(5.7)	17.1	40.9	23.7
EPS	(3.9)	(5.6)	31.4	27.2
<b>Valuation Ratios (x)</b>				
P/E	46.8	49.6	37.7	29.7
P/CEPS	35.5	34.5	26.4	21.2
P/BV	7.4	7.0	6.5	5.9
EV / EBITDA	33.6	30.7	21.6	17.3
P/S	6.7	5.3	4.3	3.7
Dividend Yield (%)	78.6	101.9	149.5	176.7
<b>Operating Ratios</b>				
EBITDA Margins (%)	20.7	18.9	21.5	22.6
EBIT Margins (%)	17.0	13.9	16.6	17.7
Effective Tax Rate (%)	26.9	26.0	26.9	26.9
Net Profit Margins (%)	14.4	10.7	11.4	12.3
Inventory Turnover Days	-	-	-	-
Fixed Asset Turnover (x)	11.9	14.9	18.3	21.5
Receivables Days	53	49	47	48
Payables Days	17	18	19	19
Working Capital Days	254	261	218	190
Net Debt / EBITDA (x)	5.4	9.7	7.3	5.3
<b>Profitability Ratios</b>				
RoCE (%)	12.5	9.4	12.0	15.3
RoC (%)	11.3	8.0	11.6	14.3
RoNW (%)	21.4	14.1	17.8	20.7

Source Company data, I-Sec research

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