

Buy

Banking Solutions All-Rounder

OFSS' AR'22 talked about growing imperative of core modernization and improved offerings for customers. OFSS' offers a feature and functionality rich core-banking platform, offering smooth API integration, scalable digital banking solution which is used by 1400+ clients in over 160 markets. Management believes that the Customer centricity, led by hyper-personalization is pertinent for banks to stay competitive, while regulation compliance and risk management solutions remain firm agendas to ensure business continuity. OFSS introduced as well as built upon a no. of products in its repertoire, including embedded finance for transaction banking to advanced analytics to Financial crime mitigation and solutions for regulatory compliance. Signing 'largest ever SaaS based', multi-year deal for Tier-1 U.S bank stands out for FY22, reflecting acceptance in advanced and competitive markets like U.S, for SaaS related offerings.

Financial Performance satisfactory given discretionary nature

For FY22, Revenue rose by 3.7% YoY as license grew 36.6% at \$104.8mn on announced basis (17% on reported basis at \$91mn) and implementation revenue was up by 3.9% YoY. Strong growth in Licence signings suggest potential pick-up in growth in the implementation revenues in FY23. The remaining performance obligation is up 8.5% YoY (FY20 growth was 16.2% YoY). RPO just covers ~32% of the Revenue as it is largely limited to ongoing implementation and AMC contracts. The AMC Revenue growth was softer at 1.9% for FY22 (has very little churn).

During the year, revenues from Oracle Inc. channel has seen increased share by 300bps to 56%, maintaining its relatively faster traction within the overall sales, Revenues from Oracle Inc. channel has grown at 9% CAGR over last 5 years as compared to 4.5% growth on overall basis, resulting in its share increasing from 45% to 56%. OFSS saw marginal dip in profitability (46.1%, down 136bps YoY) but we expect gradual improvement in line with revenue growth.

Healthy pay-out to sustain (yields 6%+)

OFSS announced Rs190 per share as Dividend for FY22 (FY21: Rs. 200) The Dividend pay-out was 95% of its FCF (last 7 years average payout is 95%+ of FCF). The company still have cash and equivalent of about Rs51bn as of FY22 (up from Rs. 49bn in FY20) and continues to have very little investment needs towards Working Capital (no incremental investments over FY17-22) and Capex (Avg Rs445mn p.a.). Thus, continue to remain optimistic on sustained high payouts and that would add about 6%+ dividend yields to total shareholder returns.

Outlook

OFSS's performance in FY22 has been moderate, as in Q4 there was a large shift towards SaaS based offerings. However, this shift augurs well for OFSS as it is a win-win situation – recurring revenue for OFFSS, no large upfront investment for client. In near term, Q1FY23 will be key quarter to watch as it is the seasonally best quarter for OFSS in terms of new license wins and growth here would indicate for real momentum in the business.

The global leadership in underpenetrated CBS business, unmatched access, superior technology, integrated & reliable offering continue to comfort us that OFSS can emerge as most preferred vendor in the segment. Superior pricing and brand appeal would mean stronger profitability, improved cash generation and generous pay-outs (Dividend Yield 6%+). We continue to maintain OFSS as our preferred pick with Buy rating on the stock with DCF based TP of Rs. 5,000 (implies 17x on FY24E PER).

CMP	Rs 3,051
Target/Upside	Rs 5,000 / 64%
BSE Sensex	53,751
NSE Nifty	15,811

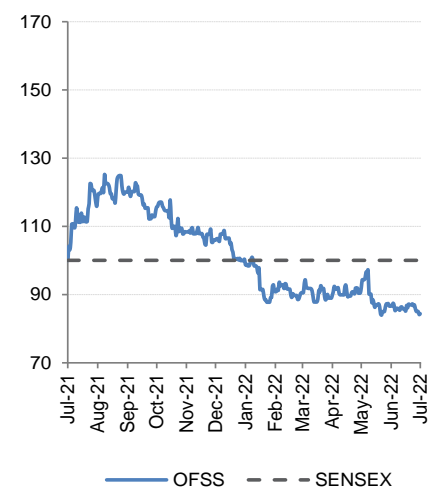
Scrip Details

Equity / FV	Rs 431mn / Rs 5
Market Cap	Rs 262bn
	US\$ 3bn
52-week High/Low	Rs 5,145/Rs 2,950
Avg. Volume (no)	75,280
NSE Symbol	OFSS
Bloomberg Code	OFSS IN

Shareholding Pattern Mar'22(%)

Promoters	73.2
MF/Banks/FIs	8.9
FIIIs	8.5
Public / Others	9.4

OFSS Relative to Sensex



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Chairman's Address - S Venkatachalam

- **Chairman Mr. S Venkatchalam** emphasized OFSS' wide-ranging, multi-geographic solutions (Grown from 141 in FY13 to 160 countries in FY22), widely applicable and relevant across banks/financial institutions of varying sizes (\$50mn - \$10bn size), from small/regional to global MNCs as well as maturity stages, including specialized banks. (Total Clients: FY22 – 1,484, FY21 – 1,432, FY20 – 1,401, FY19 – 1,362)
- Qualitatively, FY22 growth comprised of a.) New customer acquisition, witnessed across domains, viz. Corporate & Retail Banking, Modern Risk & Finance, etc, and b.) Existing clients, for which cross-selling and upselling opportunities saw improved traction.
- For its (organically developed) SaaS solution, **OFSS signed its largest ever, multi-year SaaS deal with a tier-1 U.S Bank**, while also providing Cloud or On-Prem deployment based on customers' preferences.
- New Product/ Enhanced Offerings include:
 - a.) **Embedded Finance for Transaction Banking solution** (personalized digital banking) to enable banks provide a personalized digital banking experience, with seamless payments, collections, holistic working-capital management recommendations, and virtual account management— built on a modern, data-rich cloud foundation that is integrated seamlessly with the clients' ERP systems.
 - b.) **Advanced Analytics** with Artificial Intelligence (AI) and Machine Learning (ML), to track financial crime and comply with evolving regulations.
- **Industry Recognition:** Retained leadership position in Gartner - Global Retail Core Banking Annual Survey (Feb 2022). Recognized as leader in world-wide end-to-end corporate banking by IDC MarketScape. Gartner recognized OFSS' shift to banking based on microservices and quality amongst highest in domain. OFSS' ALM solution was recognized by Asia Risk Awards and Risk Data Repository, while Regulation Asia awarded Oracle's anti-financial crime solutions high distinction for KYC) Onboarding, PEPs, and Sanctions Screening capabilities.

MD&A Takeaways

- Commenting on trends, OFSS' shared that technology interventions such as **hyper-personalization, real-time insights and data analytics driven learning systems, have helped to better identify customer needs** and provide better experiences.
- Financial services with **traditional business models face risk of losing out business unless they adopt new-age tools such as unified data modelling, integration of processes, etc., which can convert data into insight** for better growth and customer experience.
- Higher digitization has also led to **increased instances of financial crime, which needs to be countered with modern solutions such as advanced analytics with AI / ML**.
- **Newer Growth Avenues:** Digitization of trade and supply chain finance have also emerged as key priority areas since existing monolithic systems are unable to cater to expanded demands when economies are recovering from the effects of pandemic.
- Cloud / Software-as-a-Service (SaaS) based solutions offer flexibility, faster go-to-market and avoid large up-front investments.

New Offerings/Extensions for FY22:

- **For Banking Biz:** a.) Flexcube for Islamic banking, b.) Oracle Cash Management, c.) Oracle Treasury Management.
- **For Risk & Finance management:** a.) Oracle Financial Services Financial Crime and Compliance Studio product, b.) OFSS Accounting Foundation Cloud Service, c.) OFSS Treasury Risk Management products, d.) OFSS Applications for Regulatory Compliance, e.) OFSS Application for Financial Accounting Standards, f.) OFSS Finance and Risk Applications for Insurance.

Opportunities & Threats

- **Irreversible Digital Trend:** Increased digital investments in retail and corporate financial services. Create embedded financial services for customers (Machine learning, AI, hyperdata).
- **Regulatory Tailwind:** Tech spends needed to manage risks, develop insights and resilience.
- **Agile Framework:** Shifting to nimble point solutions with rapid deployment capability and SaaS / Cloud based deployments
- **Threats - Competitive Pressure:** Higher demand digital products/services led to no. of new players/challengers with niche solutions.

Other Key Takeaways

- Employee Base de-grew by 1.2% on YoY basis at 7,884 employees as against 7,977 in FY21. The median increase in remuneration in FY22 was 22%.
- **Customer Concentration:** While Top-client (Oracle INC. – parent entity) concentration rose by 300bps for FY22, Revenue from top-client has also seen a rise of 80bps YoY.
- **Oracle Inc. channel growing at 2x:** Revenues from Oracle Inc. channel has grown at 9% CAGR over last 5 years as compared to 4.5% growth on overall basis, resulting in its share increasing from 45% to 56%.

Exhibit 1: Customer Concentration Trend

Particulars (Rs.mn)	FY2017	FY2018	FY2019	FY2020	FY2021	FY2022
Product Revenue	37,614	39,379	43,527	43,146	44,252	46,917
Top Client	16,926	18,114	20,458	20,710	23,453	26,273
Top 5 Clients	21,064	22,052	24,811	26,319	28,321	31,434
Top 10 client	22,944	24,415	26,987	28,908	30,976	33,780

% YoY	FY2017	FY2018	FY2019	FY2020	FY2021	FY2022
Product Revenue		4.7%	10.5%	-0.9%	2.6%	6.0%
Top Client		7.0%	12.9%	1.2%	13.2%	12.0%
Top 5 Clients		4.7%	12.5%	6.1%	7.6%	11.0%
Top 10 client		6.4%	10.5%	7.1%	7.2%	9.1%

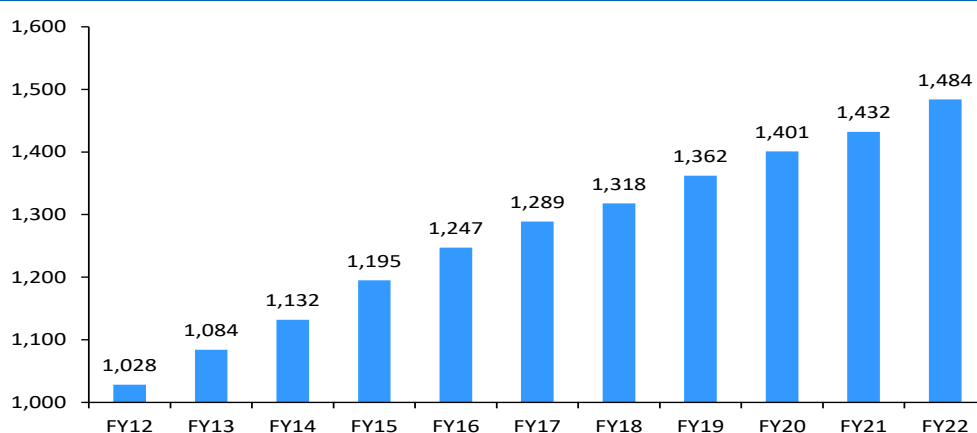
% Product Biz. Mix	FY2017	FY2018	FY2019	FY2020	FY2021	FY2022
Top Client	45%	46%	47%	48%	53%	56%
Top 5 Clients	56%	56%	57%	61%	64%	67%
Top 10 client	61%	62%	62%	67%	70%	72%
Total	100%	100%	100%	100%	100%	100%

Source: DART, Company

Deal highlights for the year

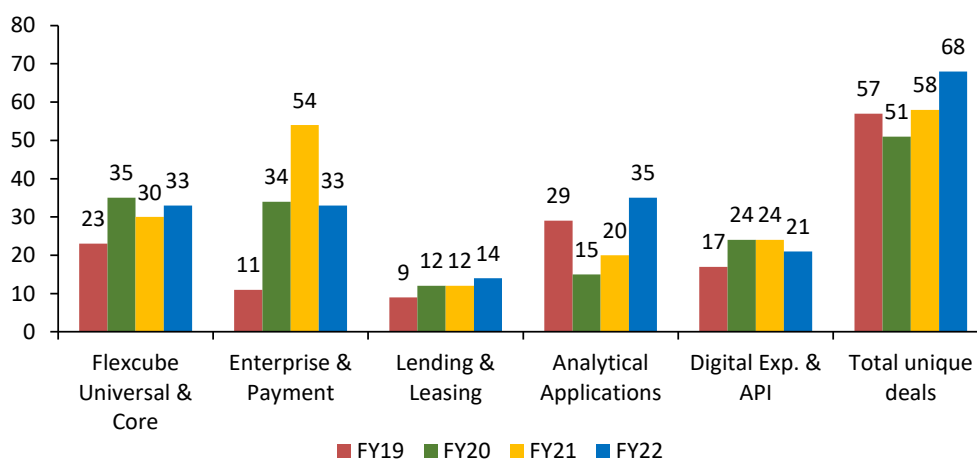
Deal wins in FY22: OFSS announced about 68 new unique deals in FY22 (21 of them in Q4) as against 58 deals in FY21. The deals wins were across its product offerings but bulk of them were in Corporate banking solutions. Analytics and Digital Experience continued to remain in traction as OFSS added about 21 deals featuring these products, respectively. The average deal size is ideally lower for these products however it helps both in terms of opening new logos that facilitate client mining opportunity and also help it garner good mind/wallet share as clients continues its preference for investing in these products compared for core modernization.

Exhibit 2: Total Client Data serviced by OFSS (historical trend)



Source: DART, Company

Exhibit 3: Total Deal Wins (Product Wise)



Source: DART, Company

Annual Report Marco View

Particulars	Details		
Key Management	Anand Ramachandran has been elevated internally to Group VP, Global Banking Solutions. Chad Menke, elevated to role as VP of OFSAA – Europe & Americas. Sanjib Chakraborty promoted to group VP, Oracle Health Insurance consulting, and Unmesh Pai promoted to VP Software Development - Financial Service Global Business Unit.		
Board of Directors	No change in Board of Directors		
Auditors	No Change in Auditors. (Mukund M. Chitale & Co)		
Credit Ratings	No Change in Credit Rating.		
Pledged Shares	OFSS has no credit rating.		
Macro-economic factors	Uncertainties caused by COVID-19 pandemic, geo-political situations continue to play in the background and could impact the scale and speed of transformation by the customers		
Key Holders	Particulars (%)	FY21	FY22
	Promoters		
	i) Promoter Shareholding	73.3	73.1
	Bank, FIs, Insurance Companies & Mutual Funds		
	i) Mutual Funds	4.2	5.0
	ii) FIs & Banks	3.3	3.3
	iii) Insurance Companies	3.7	4.0
	iv) FIIs	10.6	8.0
	Non-Institutions	8.1	9.6

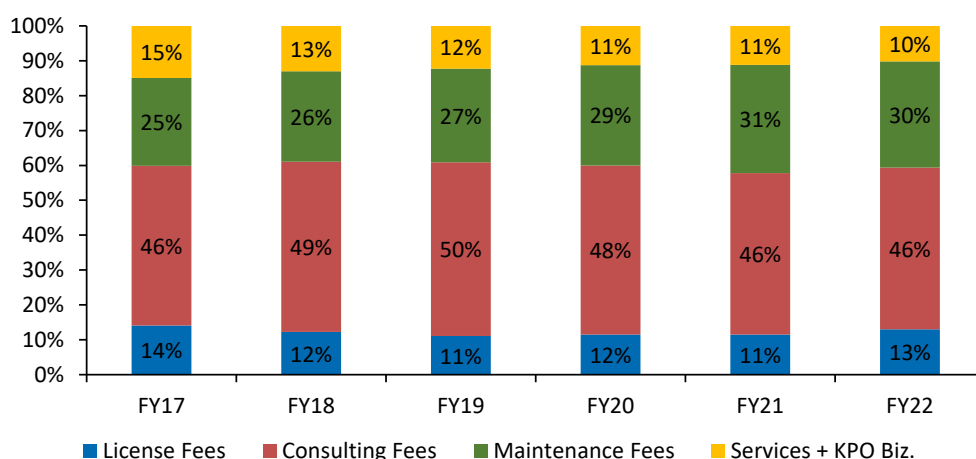
Source: DART, Company

Financial Performance – FY22

Profit & Loss Analysis

- OFSS reported USD revenue growth of 3.7% YoY in FY22 (after de-growth in FY21 of 1.3%). The growth was due to 5% YoY increase in Product Revenue (90% of Revenues), while Services Revenue (8.8% of Revenue), declined by -6.1%.
- Within the product business, Implementation Revenue (52% of Product Revenue) was up by 3.9% YoY and License revenues (~14.4% of rev) reported a double-digit growth of 17.3% on YoY basis. AMC Revenue (33.9% of Revenues) reported growth of 1.9% on YoY basis. The AMC Revenue saw marginal dip, contributing 33.9% in FY22 v/s 34.9% in FY21, License Revenue contributes 14.4% in FY22 from 12.9% in FY21 and Implementation revenue contribution was broadly the same at ~52%.
- The potential reason for strong performance in License revenue could be attributed to 17% growth in New License Fees signed. License to implementation revenue multiplier average for FY22 was 3.7x down from FY21 average of 4.2x, FY20 - 4.5x), suggesting increased SI based implementation.

Exhibit 4: Business Mix overall (Product + Services)



Source: DART, Company

- EBIT Margin for OFSS de-grew by 136bps YoY to 46.1% in FY22. This de-growth was led due to breakdown in Product margins. The Product business margins declined to 52.3% from 53.8%. The Services business margins improved to 21.6% from 20.8%.
- The decline was led by higher employee cost that led to impact of 190bps during FY22. Part of this decline was mitigated by savings in Travel Expenses which declined by 45% YoY to Rs. 350mn. It is now only 0.7% of Revenue v/s 1.3% of Revenue in FY21 (61bps change).
- The PAT grew by 7.2% YoY to Rs. 18.9Bn. The PAT Margin stood at 36.2% v/s 35.4% in FY21. The increase in PAT Margin was due to lower tax rate of 25.3% (FY21: 28.9%) and decrease in finance cost – largely rental led (Rs. 75mn from Rs. 191mn in FY21 driven by decrease in interest on income tax).

Balance Sheet Analysis

- Cash + Investments stood at Rs. 51.2bn from Rs. 49.1bn. Cash+ Balance per share stood at Rs.596 per share in FY22 vs. Rs.569 per share. Company announced dividend of Rs.190 per share compared to Rs. 200 per share in FY21.
- The Gross PPE Capex stood at Rs. 346.4mn v/s Rs. 197.6mn in FY21. The Gross Capex of Rs. 346.4mn was divided amongst Products Biz: Rs. 280mn, Services Biz: Rs. 42.1mn, and remaining was unallocated. The Right of Use Assets grew from Rs. 736mn to Rs. 812mn.
- The Billed DSO improved to 65 days for FY22 compared to 59 days from last year.

Cash Flow Analysis

- Net Cash Flow from Operating Activities de-grew by 5.8% to Rs. 18bn in FY22. Operating cash flows de-growth was led by 1) Unfavorable WC changes that burnt cash of about Rs. 515mn as against a positive WC of about Rs. 951mn, 2) Lower non-cash charges added back (Rs 928mn in FY22 vs. Rs.1,041mn in FY21).
- The FCF stood at Rs. 17,242mn (v/s Rs. 19,090mn).
- OFSS announced Rs190 per share as Dividend for FY22 (FY21: Rs. 200) The Dividend pay-out was 95% of its FCF (last 7 years average payout is 95%+ of FCF). Thus, continue to remain optimistic on sustained high payouts and that would add about 6%+ dividend yields to total shareholder returns.

Profit and Loss Account

(Rs Mn)	FY21A	FY22A	FY23E	FY24E
Revenue	49,840	52,215	60,257	68,572
Total Expense	25,153	27,225	31,441	35,658
COGS	22,018	24,059	26,768	28,826
Employees Cost	0	0	0	0
Other expenses	3,136	3,167	4,674	6,832
EBIDTA	24,686	24,990	28,815	32,914
Depreciation	1,041	928	857	880
EBIT	23,645	24,062	27,958	32,034
Interest	0	0	0	0
Other Income	1,128	1,221	1,328	1,847
Exc. / E.O. items	0	0	0	0
EBT	24,774	25,283	29,286	33,881
Tax	7,155	6,395	7,907	8,979
RPAT	17,619	18,889	21,379	24,903
Minority Interest	0	0	0	0
Profit/Loss share of associates	0	0	0	0
APAT	17,619	18,889	21,379	24,903

Balance Sheet

(Rs Mn)	FY21A	FY22A	FY23E	FY24E
Sources of Funds				
Equity Capital	430	431	431	431
Minority Interest	0	0	0	0
Reserves & Surplus	68,057	70,566	73,833	78,900
Net Worth	68,488	70,997	74,263	79,329
Total Debt	0	0	0	0
Net Deferred Tax Liability	1,023	357	422	537
Total Capital Employed	69,510	71,354	74,684	79,866

Applications of Funds

Net Block	8,739	8,612	8,315	8,080
CWIP	1	38	38	38
Investments	32,295	34,527	34,527	34,527
Current Assets, Loans & Advances	40,491	42,747	48,149	55,735
Inventories	0	0	0	0
Receivables	8,028	9,263	10,566	11,836
Cash and Bank Balances	16,948	16,799	20,338	25,962
Loans and Advances	0	0	0	0
Other Current Assets	15,515	16,684	17,246	17,937
Less: Current Liabilities & Provisions	12,015	14,571	16,346	18,515
Payables	458	397	517	586
Other Current Liabilities	11,557	14,174	15,829	17,929
<i>sub total</i>				
Net Current Assets	28,475	28,176	31,804	37,220
Total Assets	69,510	71,353	74,684	79,865

E – Estimates

Important Ratios

Particulars	FY21A	FY22A	FY23E	FY24E
(A) Margins (%)				
EBIDTA Margin	49.5	47.9	47.8	48.0
EBIT Margin	47.4	46.1	46.4	46.7
Tax rate	28.9	25.3	27.0	26.5
Net Profit Margin	35.4	36.2	35.5	36.3
(B) As Percentage of Net Sales (%)				
COGS	44.2	46.1	44.4	42.0
Employee	0.0	0.0	0.0	0.0
Other	6.3	6.1	7.8	10.0
(C) Measure of Financial Status				
Gross Debt / Equity	0.0	0.0	0.0	0.0
Interest Coverage				
Inventory days	0	0	0	0
Debtors days	59	65	64	63
Average Cost of Debt				
Payable days	3	3	3	3
Working Capital days	209	197	193	198
FA T/O	5.7	6.1	7.2	8.5
(D) Measures of Investment				
AEPS (Rs)	204.7	219.0	247.9	288.7
CEPS (Rs)	216.8	229.8	257.8	298.9
DPS (Rs)	200.0	190.0	210.0	230.0
Dividend Payout (%)	97.7	86.8	84.7	79.7
BVPS (Rs)	795.9	823.2	861.1	919.8
RoANW (%)	26.3	27.1	29.4	32.4
RoACE (%)	25.9	26.8	29.3	32.2
RoAIC (%)	44.7	44.9	51.3	59.2
(E) Valuation Ratios				
CMP (Rs)	3051	3051	3051	3051
P/E	14.9	13.9	12.3	10.6
Mcap (Rs Mn)	2,62,341	2,62,341	2,62,341	2,62,341
MCap/ Sales	5.3	5.0	4.4	3.8
EV	2,45,393	2,45,542	2,42,003	2,36,379
EV/Sales	4.9	4.7	4.0	3.4
EV/EBITDA	9.9	9.8	8.4	7.2
P/BV	3.8	3.7	3.5	3.3
Dividend Yield (%)	6.6	6.2	6.9	7.5
(F) Growth Rate (%)				
Revenue	2.5	4.8	15.4	13.8
EBITDA	10.8	1.2	15.3	14.2
EBIT	11.4	1.8	16.2	14.6
PBT	10.0	2.1	15.8	15.7
APAT	20.5	7.2	13.2	16.5
EPS	20.2	7.0	13.2	16.5

Cash Flow

(Rs Mn)	FY21A	FY22A	FY23E	FY24E
CFO	19,195	18,080	20,884	24,259
CFI	458	(1,849)	768	1,202
CFF	(15,898)	(16,386)	(18,113)	(19,836)
FCFF	19,090	17,242	20,324	23,614
Opening Cash	13,316	16,948	16,793	20,332
Closing Cash	16,948	16,793	20,332	25,956

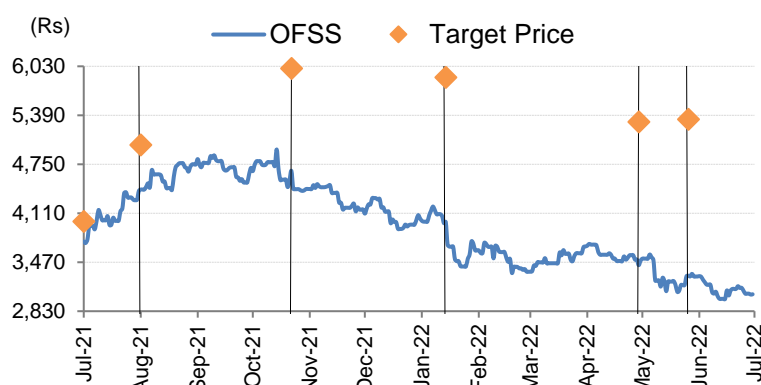
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Jul-21	Buy	4,000	3,741
Aug-21	Buy	5,000	4,420
Oct-21	Buy	6,000	4,664
Jan-22	Buy	5,885	3,996
May-22	Buy	5,300	3,431
May-22	BUY	5,334	3,294

*Price as on recommendation date

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