Thematic | June 2017
Sector: Technology

Staffing

Well placed!

Ashish Chopra (Ashish.Chopra@MotilalOswal.com); +91 22 3982 5424

Sagar Lele (Sagar.Lele@MotilalOswal.com); +91 22 3982 5585

Thematic | June 2017
Sector: Technology

Staffing

Well placed!

Ashish Chopra (Ashish.Chopra@MotilalOswal.com); +91 22 3982 5424
Sagar Lele (Sagar.Lele@MotilalOswal.com); +91 22 3982 5585

Thematic | June 2017
Sector: Technology

Staffing

Well placed!

Ashish Chopra (Ashish.Chopra@MotilalOswal.com); +91 22 3982 5424

Sagar Lele (Sagar.Lele@MotilalOswal.com); +91 22 3982 5585

Thematic | June 2017

Sector: Technology

Staffing

Well placed!

Ashish Chopra (Ashish.Chopra@MotilalOswal.com); +91 22 3982 5424

Sagar Lele (Sagar.Lele@MotilalOswal.com); +91 22 3982 5585

Contents

Staffing

Well placed!

Multiple opportunities ensure sustenance of superior growth

- **Over 2009-14, the staffing industry has grown at a CAGR of 20%. Estimates for the next five years maintain the high historical growth rate seen by the industry, which is possible with the confluence of favorable macroeconomic conditions and supportive policy changes.**
- **The factors that compound the growth story are [1] India's adoption of temporary staffing stands at a third of the global average and [2] Shift of the market to the organized segment post GST implementation and other upcoming labor reforms.**
- **The industry poses several other growth avenues, including forays into other businesses and HR services. This could lead to a sustained period of high growth. We expect revenue CAGR of 25%+ for both Quess Corp and TeamLease over FY17-20.**
- **The staffing industry requires minimal capital expenditure and sees disproportionate increase in profitability and return ratios on gaining scale. We expect TeamLease to be the key beneficiary of an improving Associate/Core Employee ratio because of its dominance in general staffing.**
- **For Quess, we see value emerging out of its aggressive inorganic foray that has opened multiple avenues of growth and profitability expansion. Its track record on integration of acquisitions has been impeccable since inception.**
- **Recent listings of Quess Corp and TeamLease provide little history to cement the sustenance of high valuations of 40x FY18E EPS and 30x FY19E EPS. However, globally, the performance of staffing companies has been highly correlated with economic activity and the industry has seen a PEG of 1 through cycles.**
- **Apart from growth, valuations would be driven by potential headroom, breadth of services, return ratios and cash generation. We initiate coverage on TeamLease with a Buy rating and target price of INR1,990 (22% upside), and on Quess Corp with a Buy rating and target price of INR990 (21% upside).**
- **We view these companies to be on a structural growth path, led by favorable macroeconomic factors, hence being less worried about high valuations. Our positive stance gets enforced to a larger extent, if we further extend our time horizon.**

Temporary staffing – an under-penetrated space

- The global workforce solutions ecosystem has staffing (70% of revenue) at its heart and supports business in multiple other ways including recruitment, payroll/compliance, contracting/consulting, talent acquisition technology, process outsourcing and other workforce solutions.
- Temporary staffing across the globe has gained prominence in the last few years, as companies seek flexibility and better cost management. This segment constitutes 2-4% of the total workforce for developed countries, and averages at 1.6% for the world. **However, it constitutes only 0.5% of the workforce in India.** A convergence to the global average itself can triple the industry.

Add to this, the move towards organized players

Though India has a total workforce of ~550m people, its organized workforce stands only at ~USD30m (~6% of total). Similar is the story for the staffing industry. Organized players have <30% market share in the Indian staffing industry. However, the industry is increasingly moving towards organized players, as they are able to provide services at greater speed, with transparency and full compliance.

GST – a key trigger…: Currently, there are around 10,000 unorganized players in India that provide staffing services. They had been charging clients on a per employee per month basis including service tax; however, they did not remit the tax to the government. On the other hand, the organized players charged service tax to clients and remitted the amount to the government. This resulted in a non-level playing field, benefitting the unorganized players to the tune of ~15%. GST implementation is likely to shift preferences of customers towards organized players, led by the mechanism of input credit.

…And so is 80JJAA: Section 80JJAA of the Income Tax Act allows for deduction of 30% of the additional employee expenses for a period of three years provided the payments are made by cheque, draft or electronic transfers (amongst multiple other conditions). Our analysis suggests, the provisions would boost earnings for staffing companies by 20-40%, providing for another trigger towards the movement to being organized.

Other services: Smaller in size, but a good profitability boost

- The employment and recruitment industry has diversified into various ancillary services over time. Though staffing is still the most important service provided and constitutes the largest share of revenue in the employment industry, it is closely followed by recruitment. Other services including payroll, education and training, recruitment process outsourcing, and HR consultancy amongst others are gaining in importance and growing much faster.
- In the listed Indian space, Quess and TeamLease have adopted different approaches towards expansion. While Quess has been expanding in several directions (facilities management, industrial asset management, security solutions, etc), TeamLease has been focused on staffing, and may acquire for scale in this business.
- While acquisitions aimed at diversification elevate the risk of integration and management of businesses that are different from core expertise, these businesses have exhibited higher growth than staffing, and higher profitability too. This is clearly reflected in the margin differential of 2pp between the two companies.

Valuations: Steep; but so is growth!

- Quess is currently trading at 44/30x FY18/19E earnings and TeamLease at 45/30x. While valuations seem expensive; growth and positioning have been favorable, and the industry conducive for sustenance of performance.
- The opportunity is large (and multi-directional) for both Quess and TeamLease; and is largely based on the themes of under-penetration and formalization, which makes us positive on both the companies despite perfectly contrasting strategies - expansive for Quess and focused for TeamLease.
- We value Quess using DCF to reach a price target of INR990, implying an upside of 21%. Over FY17-20, we expect 28% revenue CAGR, 37% EBITDA CAGR and 58% PAT CAGR.
- We value TeamLease using DCF to reach a price target of INR1,990, implying 22% upside. Over FY17-20, we expect 25% revenue CAGR, 35% EBITDA CAGR and 26% PAT CAGR.

Industry 101

The structure and dynamics

The workforce solutions ecosystem has its core in staffing (both temporary staffing and placements). But with that at the heart, the industry also supports businesses in several other ways:

- **Payroll/Compliance:** Managing a company's records and processes around salaries, wages, bonuses, taxes, and regulatory and compliance requirements.
- **Contracting/Consulting:** Supporting resource needs that are not employed full-time, or are utilized on an as-per-need basis.
- **Talent acquisition technology:** Providing and supporting solutions that are based on technology.
- **Process outsourcing:** Taking over of HR processes.
- **Other workforce solutions:** Training and development, HR consulting, recruitment support, etc.

The temporary or flexi staffing market has gained prominence in the last few years, with companies finding the need for organized staffing and workforce solutions. In temporary staffing, a staffing agency enters into a service level agreement with the client/user company and provides employees for a specific duration or a project and gets paid on a per employee per month basis (including margins).

The employees are deployed at the client's locations and work under the supervision of the client, whereas the staffing agency is responsible for paying salaries and other mandatory obligations like provident fund (PF), insurance, etc.

Diversification from staffing and recruitment

The employment and recruitment industry has diversified into various ancillary services over time. Though staffing work is still the most important service provided, and constitutes the largest share of revenue in the employment industry, it is closely followed by recruitment. Other services including payroll, outplacement, education and training, recruitment process outsourcing, outsourcing/contracting, and HR consultancy amongst others are gaining in importance and growing much faster.

Exhibit 1: Workforce solutions ecosystem

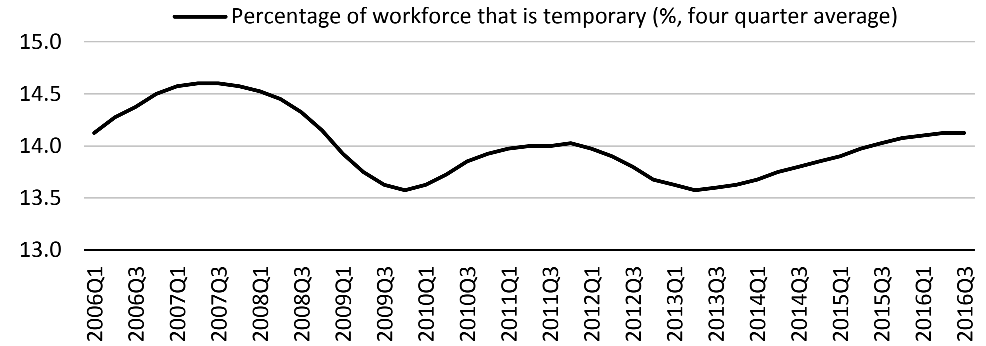
Source: World Employment Confederation

Sustenance of temporary employment

We looked at data in the European Union (EU) to get a sense on how the share between permanent and temporary staffing has moved over the years. Over the last decade, the proportion of workforce on temporary contracts has remained consistent in a tight range (13.5-14.6%), with mild cyclical movement within these bounds every four years. This includes temporary employment (10-12%) and staffing work (2-4%); the share of both these has remained steady through the last decade.

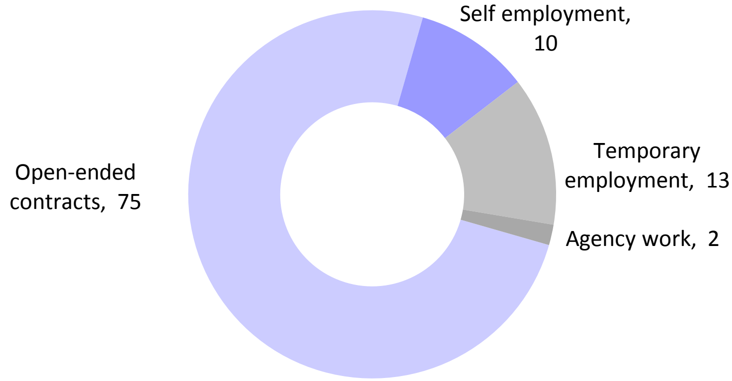
While companies and workers are demanding more flexibility, it hasn't been coming at the cost of permanent employment. However, it would suffice to say that a developed economy sees a stagnation of share with counteracting forces maintaining equilibrium over longer durations. The desire for and constant movement of employees from temporary to permanent recruitment on the one hand, and lack of permanent employment opportunities and demand from employers to maintain flexibility on the other, have resulted in the tight band in EU.

Exhibit 2: Temporary staffing consistent over the last decade in the EU



Source: Eurostat LFS Data

Exhibit 3: Employment split in the EU



Source: Eurostat LFS Data, MOSL

Steady share of temporary staffing in the overall workforce

We looked at data in the European Union to get a sense on how the share between permanent and temporary staffing has moved over the years. Over the last decade, the proportion of workforce on temporary contracts has remained consistent in a tight range of 13.5% and 14.6%, with mild cyclical movement within these bounds every four years. This includes temporary employment (10-12%) and flexi-staffing work (2-4%); and the share of both of these has remained steady through the last decade.

Exhibit 4: Sustenance of the temporary staffing industry

Source: Eurostat LFS Data, MOSL

Why workers choose agencies?

The reasons why workers choose to work through an agency revolve around:

- Finding work, gaining experience, and the ease of getting a certain kind of job
- Using the opportunity as a stepping stone to permanent employment, rotating job roles before settling for one, and ability to choose role and working hours
- Fighting the inability of getting permanent employment
- Earning additional income

Why employers choose agencies?

The reasons why employers choose to work through an agency and hire temporary staff include:

- Ability to try and test the resource before hiring permanently
- Speed at which positions can get filled
- Flexibility achieved in changing workforce dynamics (size, skill set, costs, etc) as per need
- Managing costs and adjusting them to cycles in demand
- Staffing for time-limited projects
- Less administration compared to directly employing

How flexi-staffing employment model works

In the flexi-staffing employment model, the clients/companies notify staffing agencies like Quess, TeamLease, Manpower, Adecco, Randstad, etc regarding the requirement of employees on temporary basis. The staffing agencies identify the potential employees suiting the requirements of the companies using their own database, feet-on-ground employees, job portals, and so on.

The staffing agency that provides the best-fit employees in the shortest span of time is usually awarded the contract. The clients/companies enter into service level agreements with the staffing agency, detailing the amount to be paid per employee per month (which also includes the margins for staffing agency) for a specific duration or till the completion of the project, depending on the contractual terms.

These employees are on the payroll of the staffing agency and the staffing agency is the employer for all practical purposes. The employees are placed at the clients' locations and work under the supervision of client, while all the monetary benefits in terms of salary and other mandatory obligations including provident fund, insurance, medical coverage and so on are the responsibility of the staffing agency. The model involves a tri-party agreement, wherein the staffing agency plays an intermediary role between employees and the client organization.

The flexi-staffing market involves both professional and general staffing. In case of professional staffing, the potential employees need to have specific functional expertise and final selection is done by the client from the initial shortlist provided by the staffing agency. However, general staffing does not require any specific skillset; for example, delivery personnel in retail and logistics – the client can directly draw the resources from the pool provided by the staffing agency.

Key growth drivers

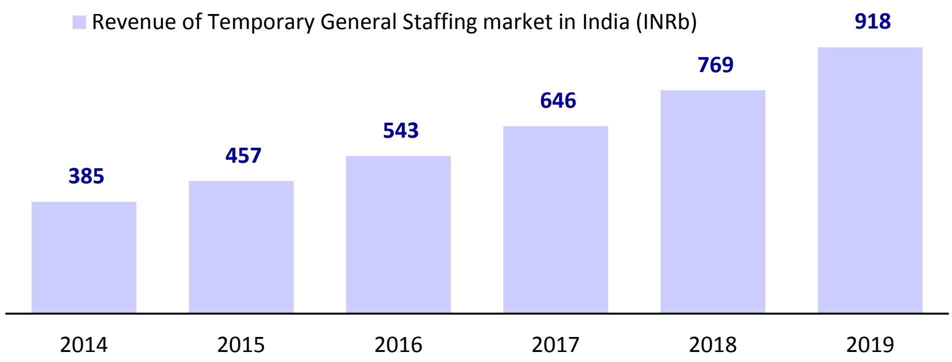
Three key drivers - under-penetration, employee productivity and the shift to organized

The temporary general staffing market in India had revenue of INR385b in 2014 and is expected to grow at a CAGR of 19% over 2014-19.

In India, there are 1.3m temporary workers presently in the organized sector and demand for temporary workers is estimated to swell to 9m in the next 10 years. Growth of the temporary staffing segment would be spurred by growth in the Retail, Telecom, BFSI, Healthcare and BPO industries.

Organizations and companies may not always have the resources or the ability to manage labor-related issues – both operational and compliance-specific – that might require liaising with local authorities. The need to have flexibility in hiring while managing operational and compliance issues is driving clients to increasingly adopt temporary staffing.

Exhibit 5: Expect 19% CAGR in the general staffing market over the next five years



Source: F&S Research

Flexi-staffing includes professional staffing, wherein the employees need to have functional expertise, and general staffing, where specific skillsets are not required.

The professional staffing industry is a third of the size of the general staffing industry, and is expected to grow slightly faster than general staffing at a CAGR of 22% over the next five years.

Key drivers of growth

The main drivers of the high-industry growth rate for India are:

[1] Under-penetration of temporary staffing in India
[2] Non-linearity provided by an increase in employee productivity
[3] Shift of market from unorganized to organized

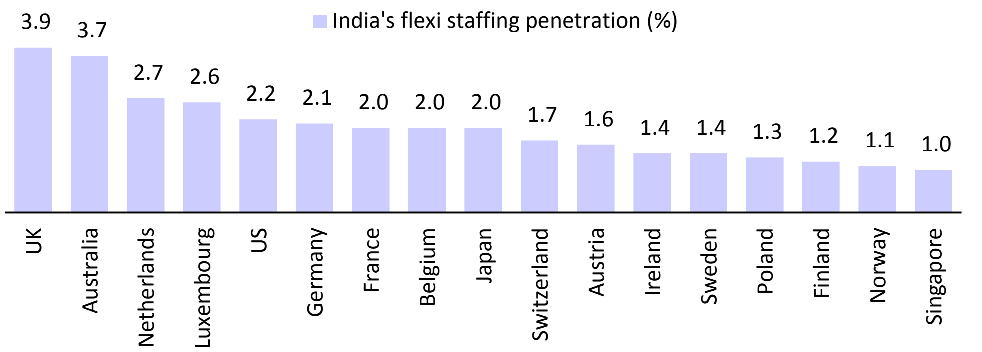
[1] India – an underpenetrated market

In the flexi-staffing employment model, clients/companies notify staffing agencies like Quess Corp, TeamLease, Manpower, Adecco and Randstad about the requirement of employees on temporary basis. The staffing agencies identify the potential employees suiting the requirements of the companies using their own database, feet-on-ground employees, job portals, and so on.

The flexi-staffing industry constitutes 0.5% of the total workforce in India, whereas the global average stands at 1.6%. Penetration is higher in developed countries – 2.2% in the US, 1.8% in the EU, and 2% in Japan.

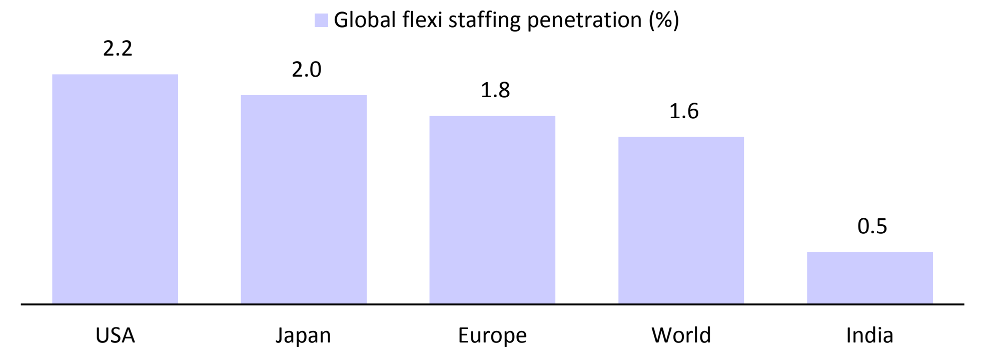
Convergence of the ratio in India with the global average would in itself double the opportunity for the Indian flexi-staffing industry.

Exhibit 6: India's flexi-staffing penetration stands at ~0.5%



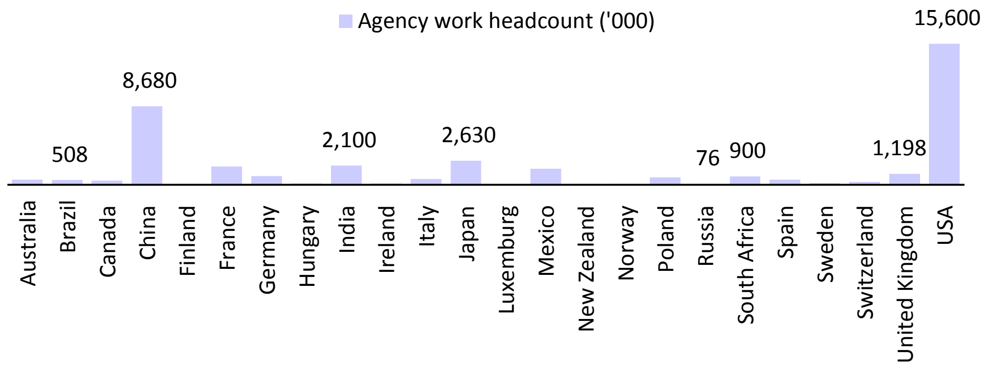
Source: CIETT Economic Report 2016

Exhibit 7: The average global flexi-staffing penetration stood at ~1.6%



Source: CIETT economic report 2016

Exhibit 8: India has only 2.1m associates in temporary staffing



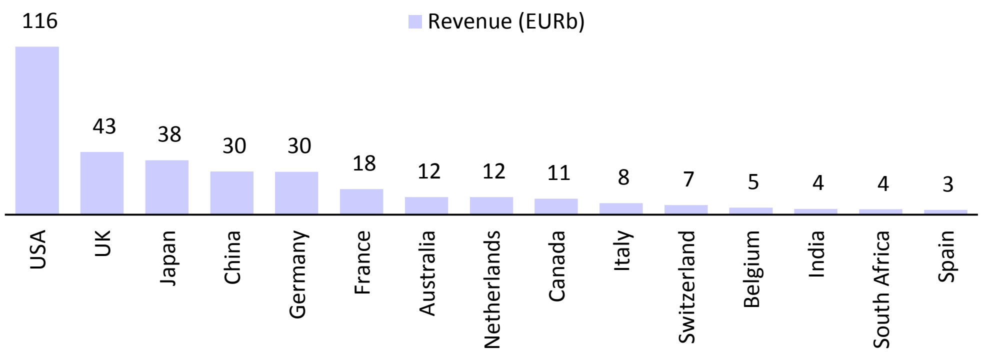
Source: WEC

[2] Non-linearity provided by increase in employee productivity

Growth of the staffing industry in terms of size/revenue will not be a simple linear function of the increase in staffing employees. It will also be a function of the increase in the average salary per person staffed.

Growth in industry = [(1 + Increase in temporary staffed employee base) * (1 + Growth in salary per employee staffed)] -1

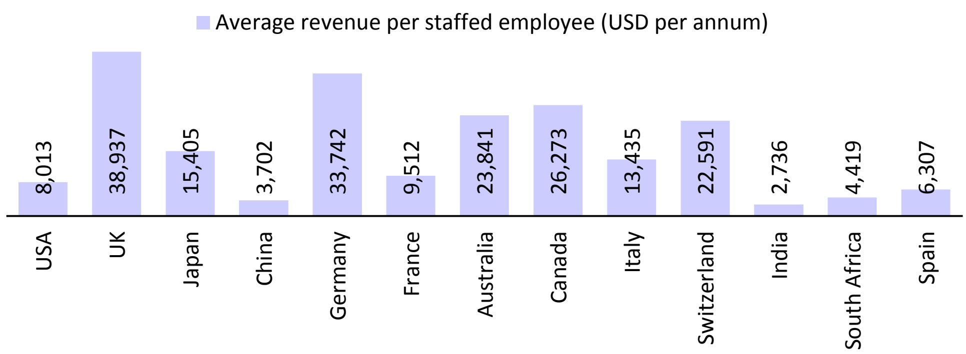
Exhibit 9: Top-15 countries ranked by temporary staffing revenue



Source: WEC

India has 2.1m agency workers and the industry derives revenue of INR400b from it. This translates to average revenue of INR358k per associate per annum (USD2,736 per associate per annum).

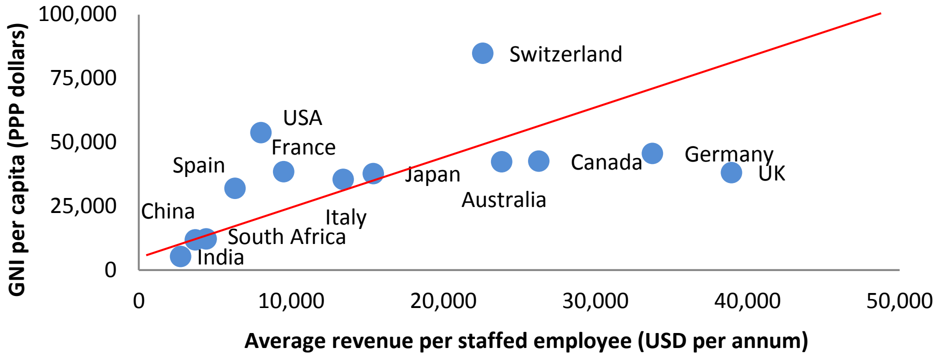
Exhibit 10: India lowest in terms of average revenue per temporary staffed employee



Source: MOSL, WEC

There is an obvious correlation between the average revenue per employee and GDP per capita of that country. As India moves higher along the red line in the exhibit below, its revenue per associate would also inch up, resulting in an increase in the size of the industry.

Exhibit 11: Industry size will also be a function of an increase in per capita GDP



Source: MOSL, WEC, World Bank

Effectively, one way to look at the industry would be to consider average wage inflation as the minimum growth that staffing companies will exhibit, assuming volumes are constant.

Going up the value chain would also result in higher productivity

The other vector that will also result in an increase in the average revenue per associate is the penetration of temporary staffing in higher-end jobs. A great opportunity for the Indian market is the professional IT staffing market.

Given India's IT employee population, and under-penetration of temporary staffing in this industry as well, there lies an opportunity for growth, especially given structural developments in the industry.

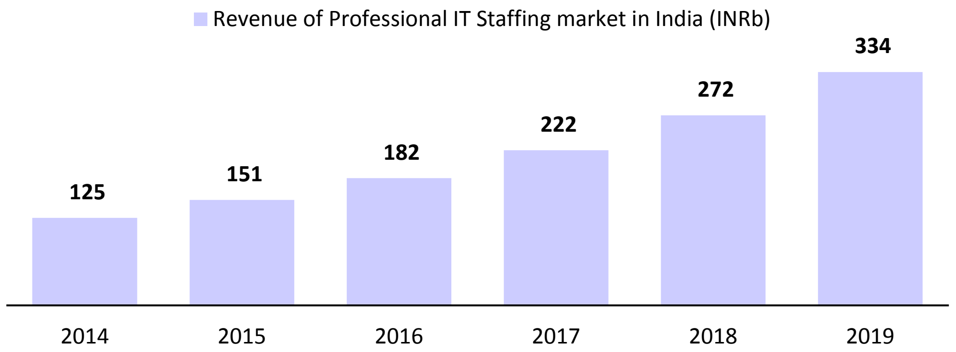
In professional IT staffing, staffing agencies provide employees possessing domain expertise and specific skillsets to customers on a temporary basis. This arrangement can either be for specific projects, or can be contracted for a stipulated duration.

The professional IT staffing market grew at a CAGR of 19% during 2009-14 to INR125b and is expected to grow at a CAGR of 22% during 2014-19.

Faster growth in the market in the future is likely to be driven by:

- **Technology service providers:** The current flexi-staff penetration in the Indian IT industry stands at 10% compared to ~20% in the developed nations. With increasing competition and margin pressures, IT companies are moving towards recruiting more temporary staff to optimize their bench and resource allocation.
- **Captives:** According to NASSCOM, India houses 300-380 captives, which contribute 10-12% of the IT services industry revenue and 10-15% of the total employee base. Growth in the activity of captives, and consequently, in their use of temporary staffing, would also result in an opportunity for staffing agencies.

Exhibit 12: 24% CAGR expected in the Professional IT staffing market

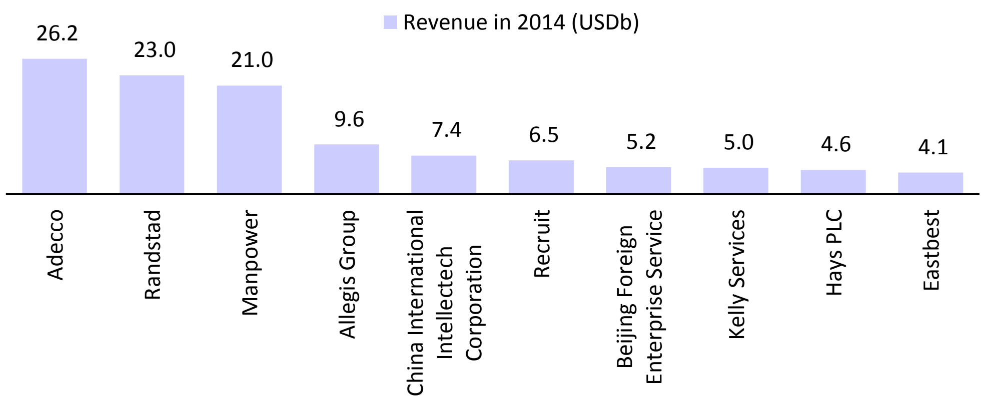


Source: F&S Research

[3] Shift of market from unorganized to organized

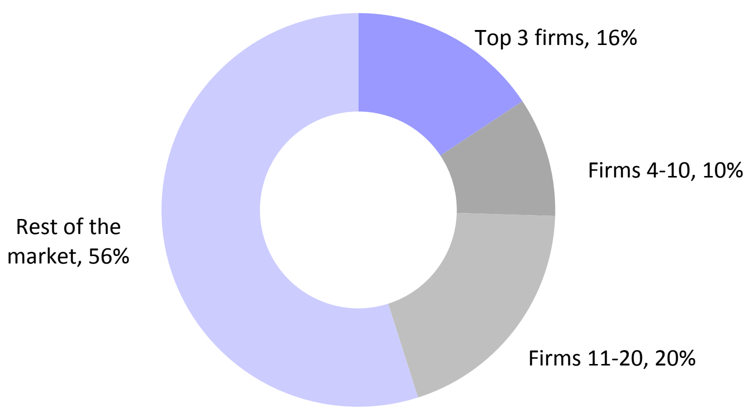
The impact of increasing industry size on leading vendors has been quite dramatic. The top-10 firms took up about 26% of the total temporary staffing market in 2015. Of the top-100 companies, 49 are headquartered in Europe, 36 are US-based, and the other 15 are from the rest of the world, according to Staffing Industry Analysts (SIA), a global advisor on staffing and workforce solutions.

Exhibit 13: Top-10 firms' sales revenue (USDb)



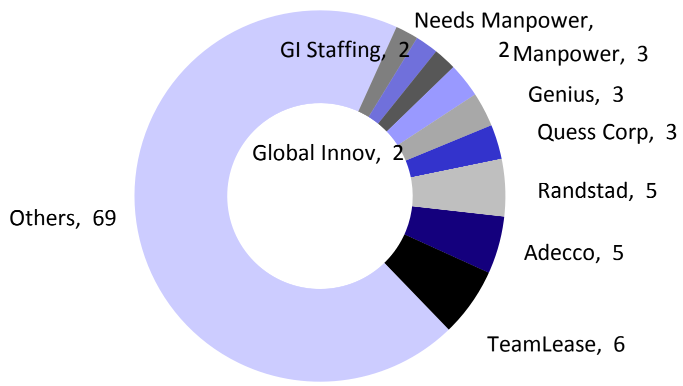
Source: MOSL, CIETT economic report 2016

Exhibit 14: Concentration in the global staffing market (% of revenue)



Source: CIETT economic report 2016

Exhibit 15: Indian market largely unorganized



Source: CRISIL Research

Unfair advantage for unorganized players

There are around 10,000 unorganized players in India that provide staffing services. In the service tax era, they charged clients on a per employee per month basis, including service tax. However, they did not remit the service tax to the government, whereas the organized players charged service tax to the clients and remitted the amount to the government. This created a non-level playing field, wherein unorganized players were better off than the organized players to the tune of the service tax amount, ~15%.

The client typically claims input tax credit from the government and the client is not bothered or affected by the payment or non-payment of service tax by the staffing agency (organized or unorganized player) to the government. Hence, the client is indifferent to whether the staffing agency is an organized or unorganized player and is bothered only to the extent of getting satisfactory services from these agencies.

GST to create level-playing field

In a post-GST scenario, the client will be able to take input tax credit from the government only if the staffing agency that services the client pays the service tax to the government. In this case, the client would be bothered and affected if the staffing agency does not remit the service tax to the government. So, the client would be forced to shift to an organized staffing agency that pays the service tax to the government.

In summary, post the onset of GST, the unorganized players need to pay the tax to the government and this creates a level playing field between an organized player and an unorganized player. So, there will be a shift from the unorganized sector to the organized sector and the current organized players will be benefited with GST, as they can compete with the unorganized players on equal terms.

The business models of unorganized staffing companies might face disruption post GST implementation, as [1] they might have to compulsorily deposit service tax recovered from customers with the government on time, and [2] they will also have to regularly deposit statutory employee payments such as ESIC and EPF.

These changes may significantly narrow the pricing differential between unorganized and organized companies, thus benefiting the organized players.

Our analysis below indicates that unorganized staffing companies are able to price their staff 20-25% below organized companies, despite paying the same in-hand salaries to their staff, primarily due to non-payment of statutory levies such as EPF (12% of basic pay) and ESIC (6.5% of gross salary).

In a post GST scenario, if the unorganized players try to charge the same rates as earlier, they'll end up eroding their profitability by >30%. And if they start pricing themselves equivalent to the organized players, they will lose their low-price edge and will come on a level-playing field with the market.

This would result in a disproportionate gain for the organized players, as they would be preferred because of their size, compliance and agility.

Exhibit 16: Level playing field in the market after GST implementation

	Pre GST		Post GST	
	Organized	Unorganized	Case 1	Case 2
Revenue for staffing company	21,611	16,560	21,611	21,440
Salary (INR per person per month)	20,880	16,000	20,880	20,880
Basic pay	16,000	16,000	16,000	16,000
EPF	3,840	-	3,840	3,840
Employee contribution (12%)	1,920	-	1,920	1,920
Employer contribution (12%)	1,920	-	1,920	1,920
ESIC	1,040	-	1,040	1,040
Employee contribution (4.75%)	760	-	760	760
Employer contribution (1.75%)	280	-	280	280
Commission earned by staffing company (3.5%)	731	560	731	560
Financials of a staffing company (INRm)				
Amount charged by staffing company to customer (INR per person per month)	21,611	16,560	21,611	21,440
Number of people staffed (nos.)	100	100	100	100
Gross annual revenue of staffing firm	26	20	26	26
Staffing cost	25	19	25	25
Own employee cost	0.5	0.5	0.5	0.5
Own staff per 100 employees staffed	1.2	1.2	1.2	1.2
Own staff salary (INR per person per month)	31,320	31,320	31,320	31,320
Total employee cost	26	20	26	26
Profit margin (%)	1.6%	1.1%	1.6%	0.9%

Source: MOSL, Company

Additional thrust because of section 80JJAA

With effect from April 1, 2017, section 80JJAA of the Income Tax Act allows for a deduction in respect of employment of new employees to the extent of 30% of additional employee cost incurred in the previous year, for three consecutive assessment years. The conditions for this to applicable include but aren't limited to,

- There has to be an increase in the number of employees
- Payment to employees have to be made by an account payee cheque or account payee bank draft or by use of electronic clearing system through a bank account

An employee is deemed additional if he adds to the total employees count compared to the previous year, and is subject to,

- Compensation of less than INR25,000 per month
- Employment of a period of more than 240 days during the previous year
- Participation in the recognized provident fund

The compensation cap to the employee does not include

- Contribution by the employer to any pension fund or provident fund or any other fund for the benefit of the employee under any law
- Lump sum payments at the time of termination of service or superannuation or voluntary retirement, such as gratuity, severance pay, leave encashment, voluntary retrenchment benefits, commutation of pension and the like.

As per our analysis, this provision is likely to positively impact earnings for Quess to the tune of 12-27% and for TeamLease to the extent of 17-39%.

Exhibit 17: Assessment of the impact of 80JJAA on Earnings

	Year			
	-	1	2	3
Employees (no.) (growth of 20%)	100	120	144	173
Salary (INR) (growth of 5%)	10	11	11	12
Revenue (3.5% markup on salaries paid)	**1,035**	**1,304**	**1,643**	**2,070**
Employee expenses	1,000	1,260	1,588	2,000
Gross profit	**35**	**44**	**56**	**70**
Gross profit (%)	3.4%	3.4%	3.4%	3.4%
SGA (operating leverage assumed given growth)	21	25	30	36
EBITDA	**14**	**19**	**26**	**34**
EBITDA margin (%)	1.4%	1.5%	1.6%	1.7%
Other income	10	13	16	21
PBT	**25**	**32**	**42**	**55**
Tax (at 35%)	9	11	15	19
PAT	**16**	**21**	**27**	**36**
QUESS				
80JJAA benefit		2	6	10
Incremental employees		20	24	29
Eligible employees (assuming % of general staffing and attrition)		2	2	3
Expense associated with them		21	27	34
New PAT		23	33	45
PAT impact		12%	20%	27%
ETR		35.0%	35.0%	35.0%
ETR new		27.4%	21.8%	17.7%
TEAMLEASE				
80JJAA benefit		4	8	14
Incremental employees		20	24	29
Eligible employees (assuming % of general staffing and attrition)		3	4	4
Expense associated with them		31	39	49
New PAT		25	36	50
PAT impact		17%	30%	39%
ETR		35.0%	35.0%	35.0%
ETR new		23.9%	15.7%	9.8%

Source: MOSL

The thin profit margins of general staffing companies result in high double-digit benefits from the provisions of Section 80JJAA. This would encourage more firms to take advantage of this, resulting in higher velocity of shift from unorganized to organized. Moreover, the conditions laid out for the applicability of 80JJAA benefits would enforce companies to adhere to payment methods that are traceable and hence even curb avoidance of contribution towards EPF and ESIC.

Assessing possibilities (and their viability)

Addressable market has potential to grow 3x in five years, 6x in 10 years

In the earlier section, we divided growth drivers for the industry into three key areas:

- Volume growth led by increased penetration of the temporary staffing industry in India to the global average of 1.5% (from 0.5% currently)
- Increase in India's per capita GDP, resulting in higher realization per temporary employee
- Shift of the market away from the unorganized segment, which currently comprises ~70% of the total industry

A combination of these factors, we believe, can lead to 23% revenue CAGR for the organized staffing market over the next five years, and 16% for the five after that. This would lead to an expansion of the organized staffing market by 3x in five years and 6x in 10 years.

The Indian Staffing Federation predicts CAGR of 19% over 2019. But the additional top-up in our expectations is emerging from the shift from the unorganized to the organized segment, especially driven by the implementation of GST.

The first five years would see accelerated growth because of the small base. Growth in the five years from then would be driven by kick-starting of key triggers following GST implementation. We believe implementation of GST and benefits provided by Section 80JJAA of the Income Tax Act would be a necessary factor for the shift in the share of organized players from 30% currently to 40% in five years and 50% in 10.

Exhibit 18: Industry potential quantified

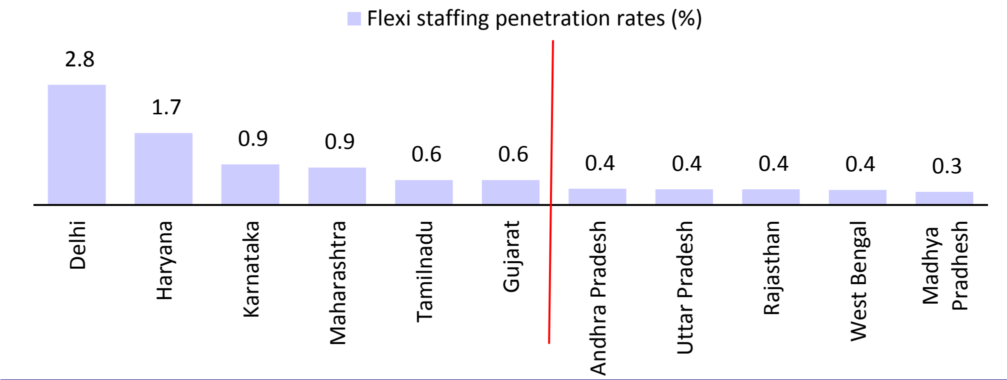
				CAGR	
	2015	**2020**	**2025**	**2015-20**	**2020-25**
A - Volume					
Population	1,311	1,389	1,474	1.2%	1.2%
Total workforce	524	556	590	1.2%	1.2%
% of population	*40.0%*	*40.0%*	*40.0%*		
Number of contract workers	2.6	4.2	5.9	9.7%	7.2%
% of total workforce	*0.5%*	*0.8%*	*1.0%*		
B - Value					
GDP (INR b)	105,227	147,586	188,361	7.0%	5.0%
GDP per capita (INR)	80,262	106,264	127,771	5.8%	3.8%
C - Industry size					
Number of contract workers (a)	2.6	4.2	5.9	9.7%	7.2%
Revenue per contract worker (INR) (b)	174,288	230,753	277,454	5.8%	3.8%
Revenue of staffing industry (INR b) (a*b)	457	961	1,636	16.0%	11.2%
D - Shift to organized					
Organized market (% of total)	30%	40%	50%		
Revenue of organized market (INRb)	**137**	**385**	**818**	**22.9%**	**16.3%**

Source: MOSL

Ample opportunities in India

In India, the penetration of flexi-staffing varies across states.

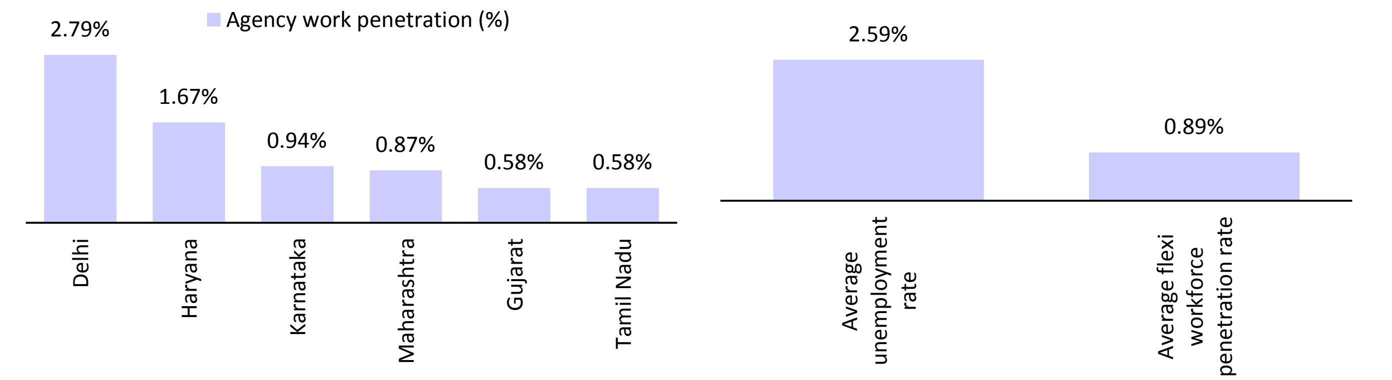
Exhibit 19: State-wise staffing penetration rates



Source: Indian Staffing Federation

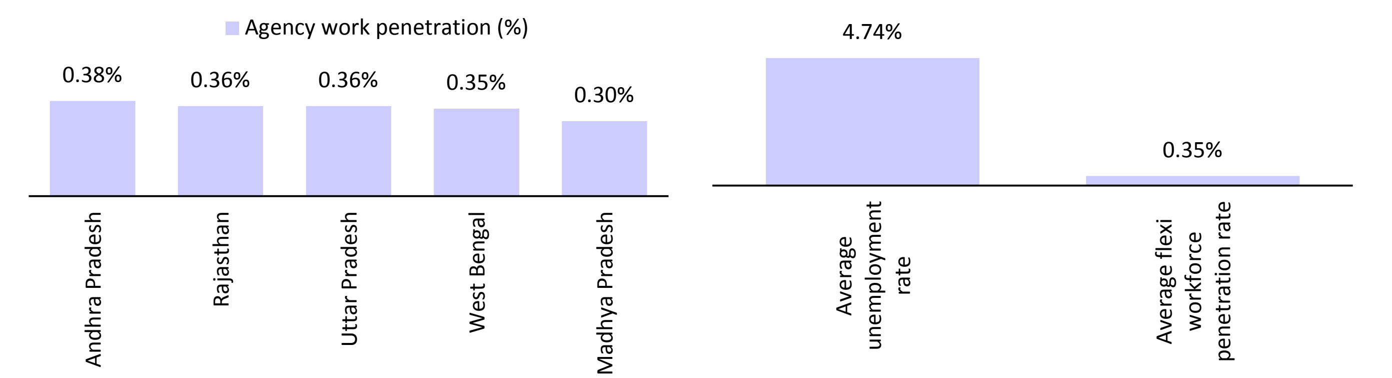
It has been noted that states with a higher penetration of agency work have seen lower unemployment. This might be because of the flexibility that this model provides businesses and employees.

Exhibit 20: States with higher agency work penetration than national average of 0.5%



Source: WEC

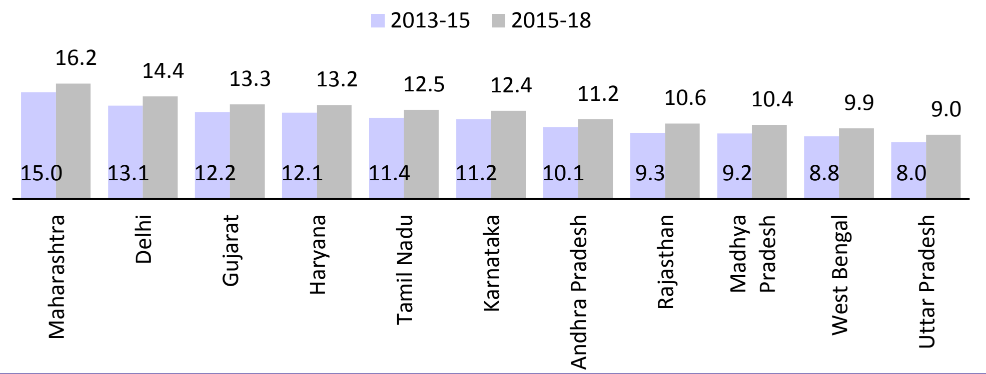
Exhibit 21: States with lower agency work penetration than national average of 0.5%



Source: WEC

Estimates for state-wise growth in temporary staffing made by the Indian Staffing Federation factor an acceleration in most states over 2015-18, compared to 2013-15. It is worth noting that this acceleration is observed irrespective of where the current penetration stands. Even for Delhi, where agency work penetration stands at 2.8%, above the country average of 0.5%, the market is expected to see a 14% CAGR over 2015-18. This, however, might also be a function of the growing working population of regions like Delhi.

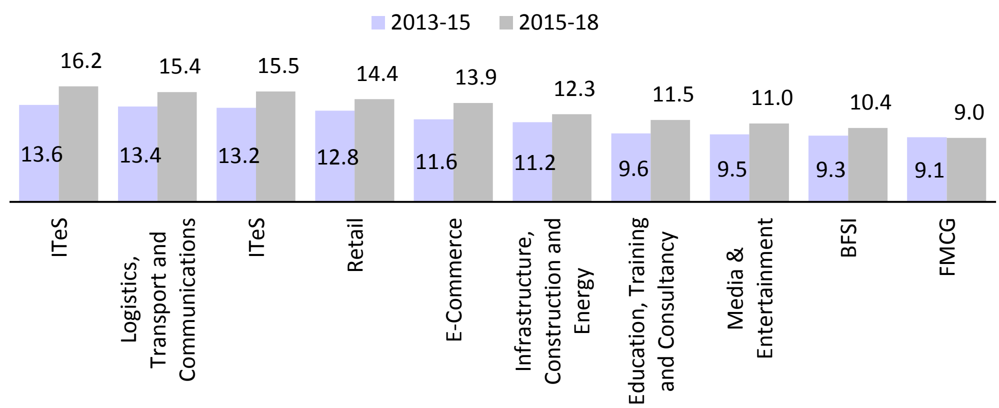
Exhibit 22: High growth even for states that have well-penetrated staffing markets



Source: Indian Staffing Federation

Similarly, an acceleration in growth rates is seen for the ITeS market, which already has a penetration of 84% in terms of formal workforce, and 10% in terms of flexi-staffing. Intuitively, this sector would appear to be slowing down in terms of growth of the temporary staffing market. However, there are ample factors that ensure continuing momentum.

Exhibit 23: High growth even for sectors that are well-penetrated in terms of staffing



Source: Indian Staffing Federation

This goes in tune with the fact that the market overall offers scope for growth from multiple dimensions, thus not just under-penetration.

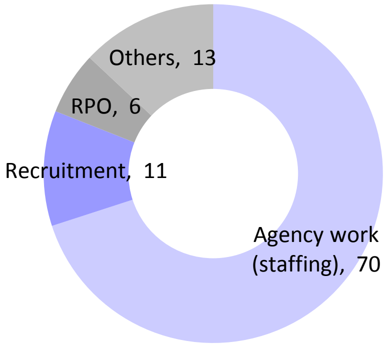
The current flexi-staff penetration in the Indian IT industry stands at 10% compared to ~20% in the developed nations. With increasing competition and margin pressures, IT companies are moving towards recruiting more temporary staff to optimize their bench and resource allocation.

More than just flexi-staffing

Other opportunities offer growth and higher profitability

Apart from providing staffing, some of the staffing agencies also get involved in service contracts with companies to provide facilities management services, which also entail providing consumables, in addition to employees.

Exhibit 24: Staffing constitutes to most of the human resource market



Source: CIETT economic report 2016

The scope of services delivered ranges across a wide array and can be broadly classified as follows:

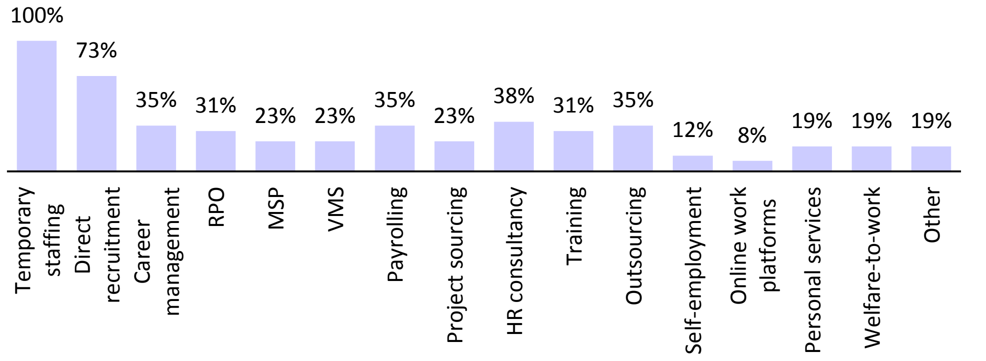
Exhibit 25: Ample potential for expansion within the human resource market

Labor market intelligence	Talent acquisition	Placement	Advisory services	Managed services	Career management
Supply & demand of work	Sourcing candidates	Agency Work	HR Consulting	RPO	Training
Regulatory environment	Employee referrals	Direct (perm & temporary)	Workforce Analytics	MSP	Outplacement
Labour market surveys	Testing	Contract for servicing	Job Search counseling	Human Cloud	Welfare-to-Work
Skills mapping	Skills assessment	Self-employed	Strategic Workshop Planning	BPO	Career Transitions
Thought leadership	On boarding	Apprenticeship	Capacity building	Payrolling	Coaching
	Off boarding	Process excellence	Leadership Development		
					Compensation & Benefits Performance Assessment

Source: WEC

The diversification is evident from the range of services offered by the members of the World Employment Confederation. Agencies have spread their wings across multiple service lines, given their association with staffing, and the fact that customers would be likely to opt for these ancillary services from a third-party.

Exhibit 26: Services provided by the members of the World Employment Confederation



Source: WEC

Indian companies like Quess Corp, however, have gone beyond these services into areas like facilities management and industrial asset management.

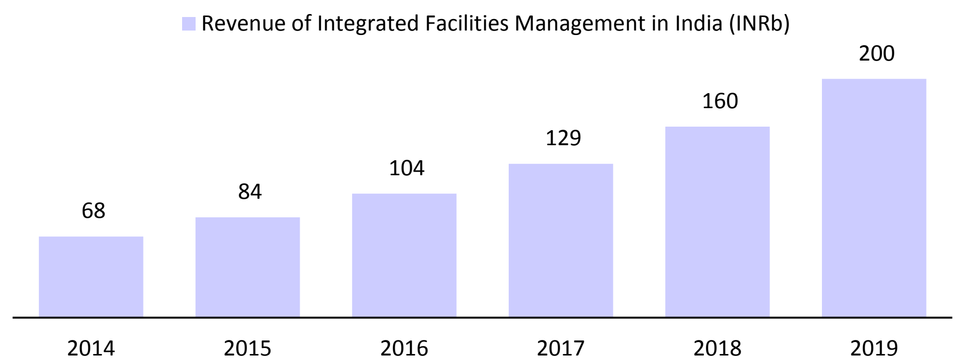
Facilities Management

Facilities management services include providing end-to-end services for maintaining buildings and properties for residential, commercial and industrial use. The services include HVAC maintenance, fire safety systems, plumbing, cleaning, housekeeping, catering, landscaping, pest control, and other services like security services, guest house management, etc.

The commercial sector has been the key contributor to the market, with growth in IT/ITeS, banking and finance sectors. Lately, the residential sector has also been showing traction, with the incidence of high-rise buildings necessitating comprehensive solutions for maintenance.

The Facilities management services market is expected to grow from INR68.2b in 2014 to INR199.6b in 2019 at a CAGR of 24%.

Exhibit 27: 24% CAGR expected in the Facilities Management industry



Source: F&S Research

Industrial Asset Management

Industrial asset management services include plant services like performance testing, pre-commissioning activities, testing, etc, and O&M services including repair & overhaul, renovation & modernization, quality audits, etc.

The growth of industrial asset management services is directly linked to the growth in the industrial sector, with greater focus on improving productivity and outsourcing non-core activities.

Asset management services revenues grew at a CAGR of 8.2% during 2009-14 and are expected to grow at a CAGR of 10.8% during 2014-19 to INR67b.

Advantages of broadening into multiple service lines

Agencies have spread their wings across multiple service lines, given their association with staffing, and the fact that customers would be likely to opt for these ancillary services from a third party.

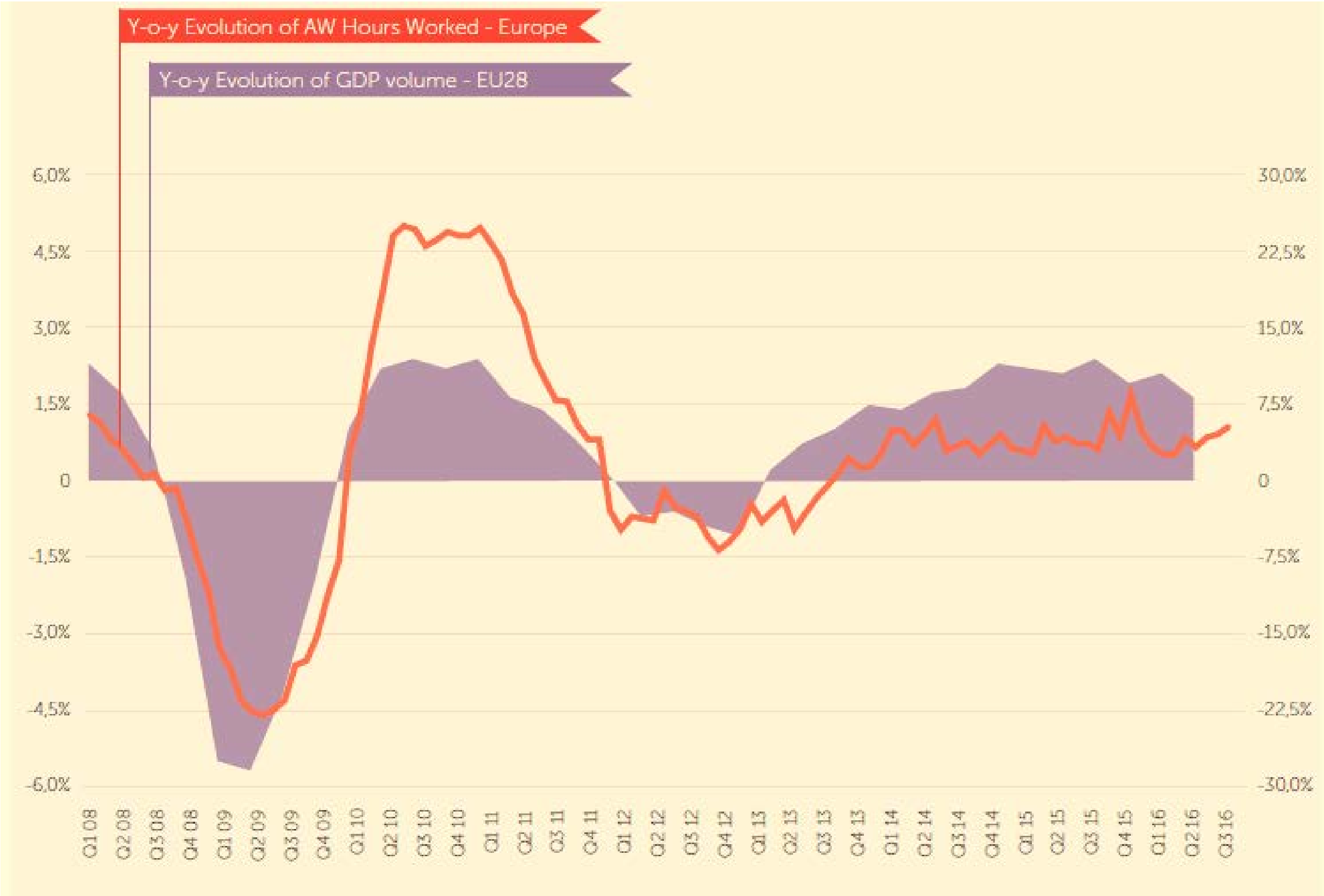
1. **Avoid cyclicality / Diversify**

The staffing business, because of its direct linkage to employment, is highly correlated with economic activity. This causes the industry to move in a direction (and quantum) similar to that of overall macroeconomic factors. The perils of this were witnessed in the period 2008-10, when TeamLease had more than 50% of its revenue coming from the verticals of BFSI and Telecom. This resulted in its associate count (and consequently revenue) reducing to half. Because of the wafer-thin operating margins in the business, profitability took a further hit.

TeamLease has now managed to create a buffer by diversifying. Now, no vertical contributes more than 20% of its overall revenue. The benefit of this was evident from the fact that TeamLease saw higher growth post demonetization. The demand for temporary staffing to meet the surge in footfalls in banks was enough to more than offset the decline in hiring demand seen in other verticals.

Quess would also now be relatively insulted from these movements because of its presence in relatively stable businesses like facilities management and asset management. These activities, because they are not core to the business owner, tend to remain outsourced / managed by third-party providers even during downturns.

Exhibit 28: Staffing highly dependent on economic cycles (EU in the chart)



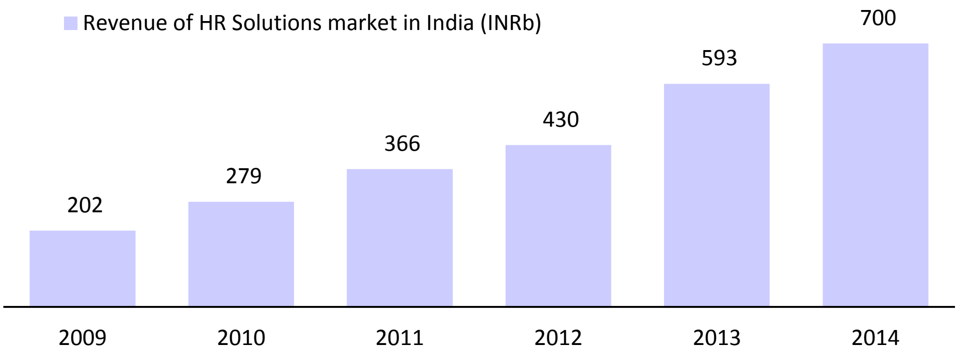
Source: CIETT Economic Report 2016

2. **Grab high-growth opportunity areas**

The HR solutions market in India has been growing at a CAGR of 28% for the last five years. As the share of organized employment increases, so will the velocity of growth in HR solutions.

Similarly, high growth is expected in the areas of facilities management and industrial asset management, as the propensity to outsource these areas to third parties increases.

Exhibit 29: 28% CAGR in HR solutions over the last five years



Source: F&S Research

3. **Improve overall profitability**

Profitability in the general staffing business in India has been in the range of 2-4%, making companies operate at thin margins with little safety when downturns are witnessed. In other ancillary businesses, despite the smaller scale, profitability is better. Professional staffing, recruitment, HR solutions, facilities management, industrial asset management, and other services usually command double-digit margins, thereby improving profitability at the overall company level.

Financial performance and valuations

A peek into well-established global peers

Limited history; hence, look at global peers

Both Quess Corp and TeamLease got listed in 2016, and were the first in their space to get listed on the markets in India. This limits the history we can evaluate and cement our understanding on.

Hence, we look at global peers, which have been well-established companies, with operations across a range of geographies. We assess these companies' valuations on three parameters that we find relevant to look at from an Indian perspective.

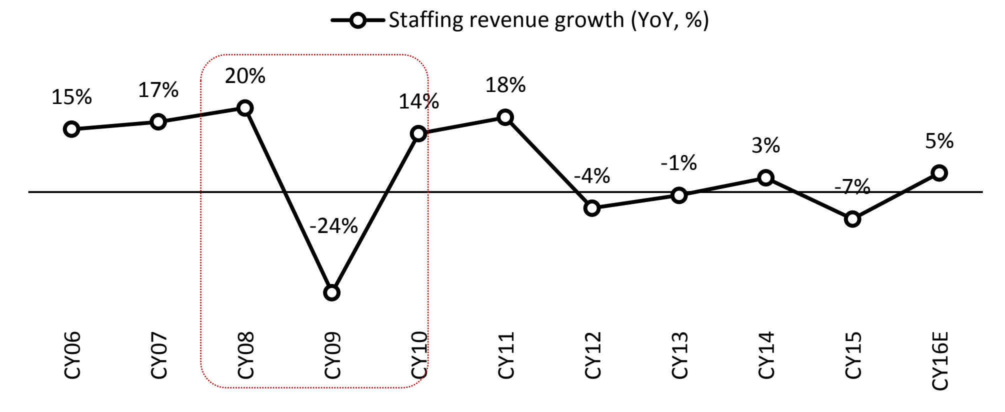
- Correlation of performance with economic cycles, and consequent impact on valuations
- Differences in how the market values general staffing companies and professional staffers
- Inorganic activity amongst global peers, success rates, and their impact on valuations

Correlation of performance to economic cycles

The staffing industry has shown a high correlation with economic cycles. In 2008-09, all staffing companies witnessed a decline in revenue, and a subsequent bounce-back. Peak-to-trough revenue decline for Adecco and Randstad were to the extent of 30% during this period; highlighting the elevated movement during sharp swings in the underlying economy. Similar was the case of professional staffing companies.

To get a sense on the deviation these companies have seen in performance, in CY08, staffing companies saw growth of 20%. However, in CY09, revenue declined 24%. And once the shock was largely behind, CY10 again saw a rebound to 14% growth.

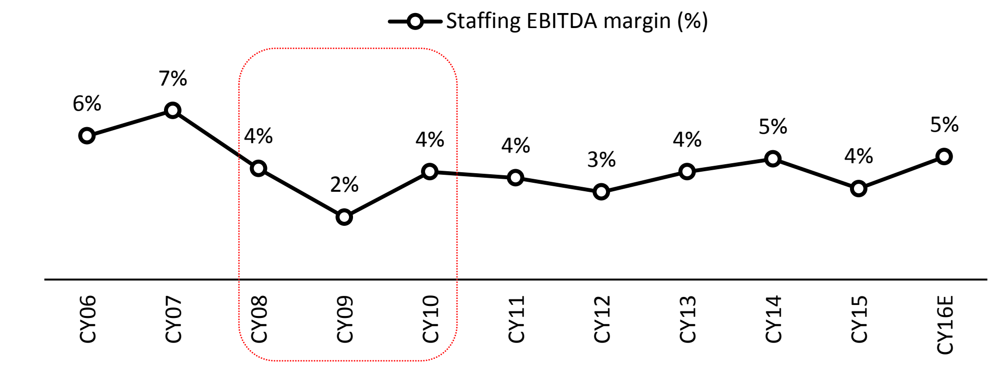
Exhibit 30: Sharp economy-related deviations in performance



Source: Bloomberg, MOSL

With wafer-thin margins, one would imagine operational losses on heavy volatility in revenue performance. However, the margin decline seems limited. Margins during the downturn did take a hit and declined 200bp when revenue declined, indicating a greater impact on profitability relative to revenue growth. However, the quantum of decline given the relatively low cushion available in low-single-digit margins has been small.

Exhibit 31: Margins positive even in downturns



Source: Bloomberg, MOSL

The cushioning can be explained by the business model. A majority of the cost is the salary paid to staffed employees. Note: the structure of operations is such that any reduction in the staffed employee base would result in a direct and proportional reduction in the cost associated with them.

What doesn't reduce is the employee cost of the staffing agency and its SG&A expense. SGA has the potential to reduce; however, 80% of SG&A is personnel and premises cost, which cannot be adjusted in tandem with the decline, and immediately.

Exhibit 32: Margins resilient because of business model

	Steady state	Downturn	Change (%)
Revenue (salary paid + commission)	105.0	73.5	-30%
Salary paid to staffed employees	100.0	70.0	-30%
Own employee costs	1.5	1.5	0%
Gross profit	3.5	2.0	-43%
Gross profit margin (%)	3.3%	2.7%	(61)
SGA	1.5	1.2	-20%
EBITDA	2.0	0.8	-60%
EBITDA margin (%)	1.9%	1.1%	(82)

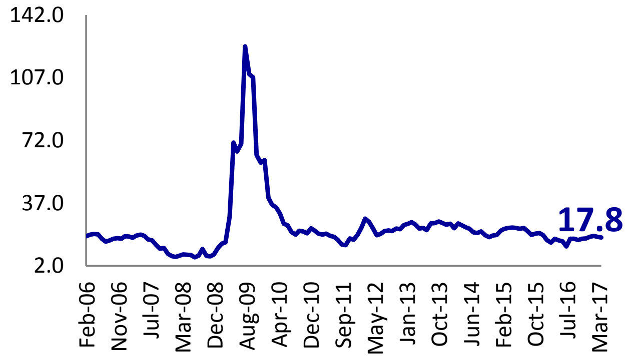
Source: Bloomberg, MOSL

Valuations during this period plunged, and subsequently bounced back.

Exhibit 33: One-year forward P/E for general staffing companies (Adecco and Randstad, respectively)

Source: Bloomberg

Exhibit 34: One-year forward P/E for professional staffing companies (Hays and Page, respectively)



Source: Bloomberg

General versus professional staffing

We can broadly divide the staffing market into two key areas: General and Professional. While growth rates have been similar for both these categories, we see a difference in their margins and return ratios. Specialist staffing companies have been historically enjoying higher profitability compared to general staffing companies. This is reflected in their significantly superior RoEs, and has also resulted in superior valuations for specialist staffing companies. **On average, specialists have traded at a 25-30% premium to general staffing companies.**

Exhibit 35: Professional staffing companies have superior financials

	CY06	CY07	CY08	CY09	CY10	CY11	CY12	CY13	CY14	CY15	CY16E
Revenue growth (YoY, %)											
General	16%	16%	20%	-24%	15%	18%	-6%	-1%	3%	-8%	5%
Professional	11%	29%	20%	-26%	9%	23%	8%	0%	5%	0%	3%
EBITDA margin (%)											
General	5%	6%	3%	2%	4%	4%	3%	4%	5%	3%	5%
Professional	12%	13%	12%	6%	4%	6%	5%	5%	6%	6%	5%
ROE											
General	40	35	9	1	12	10	6	12	14	8	19
Professional	168	161	111	41	21	40	32	29	34	36	34

Source: Bloomberg

Acquisitions have been the method for global peers

Staffing firms globally have been undertaking large M&A for more than half a century now. Their primary motivations for inorganic growth have been gaining scale, presence in ancillary services, and geographical expansion.

We see aggressive M&A in a human capital intensive industry as risky, with a likelihood of value destruction that cannot be ignored. Globally, companies like Adecco and Randstad have been disciplined in capital allocation. They have been heavy on inorganic growth, too. However, they have laid out principles for acquisitions.

Adecco's approach has been to diversify by adding capabilities in professional staffing and other HR solutions. However, it has ensured that there are revenue/cost synergies in the acquisitions, and that the acquisitions are EVA positive within a period of three years.

Exhibit 36: Adecco's acquisitions have helped expand geographical reach

Announce Date	Target Name	Function	Geography	Announced Total Value (mil.)
22-Mar-01	Olsten Personal Norden AS	Staffing	US	-
21-May-01	Management Recruiters	Recruitment	Australia	-
21-May-01	Temps & Co	Staffing	Australia	-
6-Feb-02	Jobpilot GmbH	Online recruitment company	Europe	29
8-May-02	WorkCard Co Inc	Web-based vendor management software		-
6-Sep-02	Resume.com Solutions Inc	Job counselling	US	-
22-Sep-04	Peopleone Consulting India Pvt Ltd	Temporary staffing	India	-
25-Jan-05	Altedia SA	HR consulting	Europe	68
29-Apr-05	Humangroup	HR services	Spain	85
17-Oct-05	StaffWise Legal	Staffing for the legal profession		-
21-Dec-05	3W Direct Management Solutions	Management experts and consultants	Benelux	-
9-Jan-06	DIS AG	Managed professional staffing	Germany	440
18-Jun-07	TUJA Zeitarbeit GmbH	Temporary staffing	Germany	1,073
13-Aug-07	TalentTrack LLC	Recruitment and HR		-
1-Sep-08	DNC de Nederlanden Co NV	Staffing	Netherlands	81
11-Aug-09	Spring Group Ltd	HR consulting and telecommunication services	UK	102
20-Sep-09	Groupe Datavance SAS	HR services and staffing	France	-
24-Sep-09	XPE Group	Project staffing and permanent placement	Belgium	-
20-Oct-09	MPS Group Inc	Professional staffing in the US		1,186
26-Jul-11	Drake Beam Morin Inc	Career transition and talent development	US	216
3-Jan-12	VSN Inc	Professional staffing	Japan	117
12-Jun-14	Shenzhen Fangsheng Human Resources Service Co Ltd	HR services	China	-
11-Aug-14	OnForce Inc	Vendor management software, freelancer management system	US	-
11-Mar-15	Knightsbridge Human Capital Management Inc	Career transition, leadership development and recruitment services	Canada	63
9-Mar-16	Penna Consulting PLC	Career and talent solutions	UK	129
4-Oct-16	D4 LLC	Legal staffing	US	-
7-Dec-16	Talentoday Inc	Talent assessment and people analytics		3

Source: Bloomberg, MOSL

Randstad's approach has been towards gaining leadership in the segments it operates in. It has been more focused on scale, which would add to risk factor, especially in terms of integration. It has been active in acquiring capabilities in online marketplaces and HR solutions and software, giving it quick capabilities in digital services.

Exhibit 37: Randstad's acquisition rationale has been focused on gaining leadership

Announce Date	Target Name	Function	Geography	Announced Total Value (mil.)
3-Jul-00	Temps & Co	Staffing in administrative, accounting and legal	US	15
7-Jun-02	JMW Horeca Uitzendbureau BV	Jobs in hotels, restaurants, catering and event business	Netherlands	-
21-Oct-03	Thuiszorg Perfect BV	Homecare	Netherlands	-
9-Jan-04	Take Air	Airport-related staffing	France	-
30-Sep-04	Arvako Sverige AB	Staffing	Sweden	-
7-Dec-04	Assist Interim	Paramedical personnel	Belgium	-
22-Nov-05	Gamma Dienstverlening	Payroll processing	Netherlands	-
29-Nov-05	EmmayHR	Permanent recruitment in banking, BPO, travel and leisure	India	-
13-Dec-05	Galilei	Outplacement, transition, assessment and coaching	Europe	-
21-Dec-05	Martin Ward Anderson Ltd	Financial recruitment	UK	-
10-Jan-06	Bindan GmbH		Germany	-
10-Jan-06	Teccon GmbH		Germany	-
13-Apr-06	Team HR Services Pvt Ltd	Staffing	India	-
10-May-06	Talent Shanghai Co Ltd	Staffing	China	-
29-Mar-07	Thremen BV	Administrative processes in public and financial sector	Netherlands	-
14-Sep-07	Team BS GmbH	Staffing in pharmaceutical, chemical, consumer goods and automotive	Germany	98
3-Dec-07	Vedior NV	Professional staffing	Netherlands	5,908
30-Sep-10	ProfiPower	Permanent and temporary recruitment services	Hungary	-
13-Oct-10	Ma Foi Management Consultants Ltd	Managed payroll services and social benefits administration	India	-
20-Jul-11	SFN Group Inc	Workforce solutions	US	716
4-Apr-13	USG People	General staffing	Europe	26
20-Mar-14	Gigwalk Inc	Workforce management software	Japan	10
4-Nov-14	VONQ UK Ltd	Online recruitment marketing services	UK	-
25-Jun-15	Brazen Software Inc	Real-time messaging and collaboration	US	5
25-Sep-15	RiseSmart Inc	Outplacement career transition services	US	100
30-Nov-15	Proffice AB	Staffing, recruitment and outplacement	Nordics	203
15-Jan-16	Focus Orange Technology BV	SaaS based HR analytics solution	Netherlands	-
9-Feb-16	Pymetrics Inc	Big data, neuroscience and gamification in career management		6
20-May-16	Obiettivo Lavoro - Agenzia per il Lavoro SpA	Staffing	Italy	71
10-Jun-16	Careo Co Ltd	Temporary staffing of engineers, clerical workers and telemarketers	Japan	-
14-Jun-16	Team2Venture GmbH	Freelance marketplace	Europe	-
20-Jun-16	Ausy	Consulting and engineering firm in advanced technologies	France	433
9-Aug-16	Monster Worldwide Inc	Job seeking, recruitment and talent management		355
16-Dec-16	BMC Group BV	Secondment and organizational consultancy for the public sector	Netherlands	68

Extending the analysis for India

Ample opportunities to sustain growth at current levels

PAT in the staffing business can be expected to grow at a CAGR of 20%+ over the next 5-10 years. We see this growth being supported by:

- Under-penetration of the Indian market in terms of staffing,
- Increasing per capita incomes, naturally supporting growth for staffing companies,
- Higher revenue per staffed employee, as the share of specialist staffing increases, and
- Foray into newer and emerging areas that have higher growth rates (and profitability) compared to staffing.

Valuations are currently rich for Indian staffing companies, with Quess Corp trading at 44x FY18E and 30x FY19E earnings, and TeamLease at 45x FY18E and 29x FY19E earnings. But while valuations are at a premium compared to global peers, so is the potential of organic growth in the staffing business. Global peers, because of their decades-old existence, have seen saturation in developed markets, and have hence actively moved into other geographies in Europe and in APAC.

The portfolio skew towards developed markets has led to a dependency of performance on economic cycles rather than on growth opportunities. The valuation premium attached to growth characteristics would be justified for Indian players.

We see a case for Indian players to continue trading at rich valuations till growth opportunities are even partly exhausted. Correlation to economic cycles cannot be ignored for India, given the nature of the business. However, India is at a stage where uncertainty around economic growth is lower, and confidence around acceleration has only been increasing. This places India at the beginning of a growth cycle, which is likely to be mirrored in the growth of the staffing industry, as well.

PEG of 1 observed

We take two examples: [1] multiples at which the technology services industry used to trade over FY03-08, and [2] multiples that global companies like Addecco and Randstad got at the peak of their growth period.

In the case of the Indian technology services companies, during their peak growth period, they traded at very close to their earnings growth, that is, PEG of 0.9-1.

In the case of global staffing companies, a PEG of greater than 1 has been observed in times of peak growth cycles and times of recovery post-depression in the market.

Given the visibility of revenue and earnings growth for Quess Corp and TeamLease, PEG ratio of 1 should sustain, provided the economic cycle is stable.

Offerings and risks may lead to relative premium/discount

Amongst companies, valuations are likely to differ based on the [1] superiority of offerings, and [2] risks associated with growth.

While we reckon Quess has been at the forefront of expanding service lines, and consequently achieving diversification, higher growth and better profitability; this comes with its perils of heightened risks associated with inorganic expansion.

The premium that Quess Corp can command because of its superior margins and diversification benefits seems to be getting offset by the negative cash flows and the risk the company has been taking on, despite the prudency shown in making decisions around acquisitions.

Companies

Quess

TeamLease™

Quess Corp

BSE SENSEX	S&P CNX
31,103	9,607

CMP: INR830 TP: INR990 (19%) Buy

Blitz-scaling!

Aggressive inorganic foray opening new avenues for growth

Stock Info

~~Bloomberg~~	~~TCOM IN~~
~~Equity Shares (m)~~	~~285.0~~
~~52-Week Range (INR)~~	~~784 /427~~
~~1, 6, 12 Rel. Per (%)~~	~~-9/-6/32~~
~~M.Cap. (INR b)~~	~~192.6~~
~~M.Cap. (USD b)~~	~~2.9~~
~~Avg Val, INRm~~	~~530~~
~~Free float (%)~~	~~25.0~~

Financials Snapshot (INR b)

Y/E MARCH	FY17	FY18E	FY19E
Sales	41.6	61.7	76.2
EBITDA	2.2	3.6	4.6
NP	1.1	2.5	3.4
EPS (Rs)	10.0	22.1	30.2
EPS Gr. (%)	395.5	68.6	183.4
BV/Sh. (INR)	73.8	95.9	126.1
P/E (x)	72.1	32.6	23.9
P/BV (x)	9.8	7.5	5.7
EV/EBITDA (x)	37.9	23.5	18.0
EV/Sales (x)	2.0	1.4	1.1
RoE (%)	19.2	26.1	27.2
RoCE (%)	12.7	17.3	19.6

~~Shareholding pattern (%)~~

~~As On~~	~~Mar-17~~	~~Dec-16~~	~~Mar-16~~
~~Promoter~~	~~75.0~~	~~75.0~~	~~75.0~~
~~DII~~	~~8.0~~	~~9.1~~	~~14.7~~
~~FII~~	~~11.4~~	~~11.1~~	~~3.3~~
~~Others~~	~~5.6~~	~~4.9~~	~~7.0~~

~~FII Includes depository receipts~~

Stock Performance (1-year)

- **Quess Corp is a leading integrated business services provider established in 2007. It has a pan-India presence, with 65 offices across 34 cities. It also has operations in nine countries across North America, the Middle East and South East Asia.**
- **It is a step down subsidiary of Fairfax Financial Holdings Group (FFH CN), held through its Indian listed subsidiary, Thomas Cook India Limited (TC IN). In FY17, it reported revenue of INR41.57b.**
- **Driven by continued organic momentum, and the addition of recently acquired companies, we expect 28% revenue CAGR, 37% EBITDA CAGR and 58% PAT CAGR over FY17-20.**
- **Quess has grown at a CAGR of 46% over the last five years. PAT has grown at a CAGR of 79% on account of its entry into higher-value-add businesses.**
- **It has been actively acquiring businesses over the last eight years, and has a successful track record of integrating and running them. It has spent more than INR5b on acquisitions from FY12-17. Over this period, it has generated a cumulative OCF of only INR309m (5% of EBITDA). Although cash flow generation improved in FY17, we are yet to see sustained delivery on this aspect. A failure to generate cash consistently, in our view poses a risk on the sustenance of current valuations.**
- **Given the multi-dimensional opportunity and its execution prowess, we initiate coverage on Quess with a Buy rating, valuing it on a DCF basis at INR990 per share.**

A leading integrated business services provider

- Quess operates through four key business segments: [1] Global Technology Solutions (GTS), [2] People & Services (P&S), [3] Integrated Facility Management (IFM) and [4] Industrials. All of these areas have been witnessing high growth, which is expected to continue going forward as well.
- In terms of penetration, it has barely scratched the surface in its core staffing business as well as other areas. In general staffing, India's low penetration of 0.5% of working population (versus global average of 1.6%) itself should drive high velocity growth.
- In business services, Quess intends to be part of anything that is non-core to a business and that can be outsourced to a third party. While it has touched upon the areas of facilities management, catering, security and industrial asset management, the directions for further growth are ample.

Good track record on acquisitions so far

- Inorganic growth has been a key component for Quess' growth, improvement in profitability and diversification. It has demonstrated successful integration with margin accretion and retention of management personnel.
- The diversification it has achieved over the years makes it a well-spread and stable bet in case of volatility in the economic cycle. Staffing companies across the globe witnessed a 40% gap between the peak and trough during the CY08-09 global financial meltdown.

- Validation also comes from the following examples;

[1] Over the last eight years, revenue at Avon (a facilities management acquisition) has grown at a CAGR of 52% and EBITDA margin has expanded to 5.1% from 1.7% at the time of acquisition.

[2] Magna (an acquired IT staffing company) has grown at 15% CAGR since acquisition and its margins have improved to 13% from 5.5% at the time of acquisition.

Strong growth expectations, going ahead…

- With the strategy in place, and execution being impeccable, we expect 28% revenue CAGR over FY17-20. This would be fueled by the current portfolio and any inorganic activity would only add to these expectations.
- Over the same period, we also expect cumulative EBITDA margin expansion of 120bp to 6.6%. The visibility for this comes from [1] continued improvement in profitability in Brainhunter and MFX, which were loss-making entities, [2] addition of Manipal Integrated Services, Terrier Security and Comtel Solutions, all of which have better margins than company average, and [3] margin expansion in the People & Services business, led by operational leverage and continued growth in Training & Development.

…but cash flow improvement necessary too

- Cumulative OCF/FCF for Quess over the last five years has been +INR258/-4,382m. Debtor days are worse for Quess (45 v/s 20 for TeamLease) because of its presence in businesses other than Staffing (60-65 days). Moreover, in the P&S business, it extends funding for 40% of its revenue, compared to 20% for TeamLease, thereby increasing working capital requirements.
- High growth at the cost of cash generation would be value-dilutive. We view this as a risk factor, given that Quess hasn't been able to show any improvement in cash generation (even at the operating level) despite spending to beef up offerings and revenue; except in FY17, where it exhibited improvement on this front.

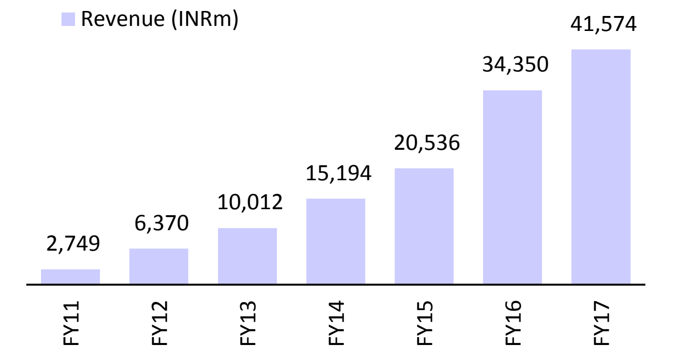
Valuation and view: Promising, but keep an eye on risks

- We value Quess using a DCF to reach a price target of INR990, implying 19% upside.
- Valuations are rich given its strong growth history, and continued aggressive thrust on acquisitions. A value of INR990 implies required organic revenue CAGR of 20% and required organic NOPAT CAGR of 26% for the next ten years.
- Over FY17/20E, we expect revenue/EBITDA/PAT CAGR of 28/37/58%, led by our assumption of 20% growth in the organic business and incremental contribution by recent acquisitions.
- At current valuations, there seems to be little room for error on execution – both on organic growth and on the integration of acquisitions. One thus has to take into consideration these risks given steep valuations. **The long-term prospects of the company stand bright given the high-growth opportunities, aggression shown on expansion and flawless execution.**

Key risks: [1] Integration of current/future acquisitions going wrong, [2] inability to manage diverse portfolio of businesses, leading to inferior growth, [3] economic downturn, leading to a proportional and direct impact on business.

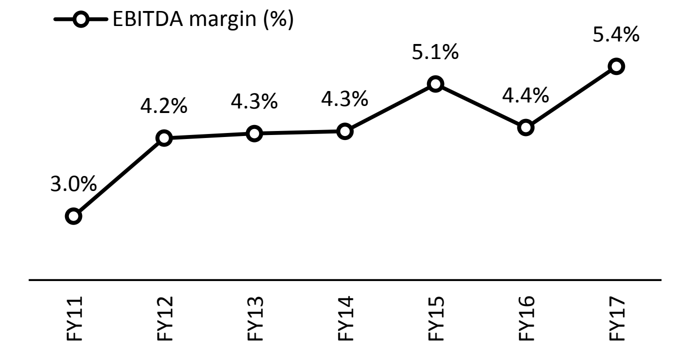
Story in charts

Exhibit 38: Revenue CAGR of 46% over the last five years



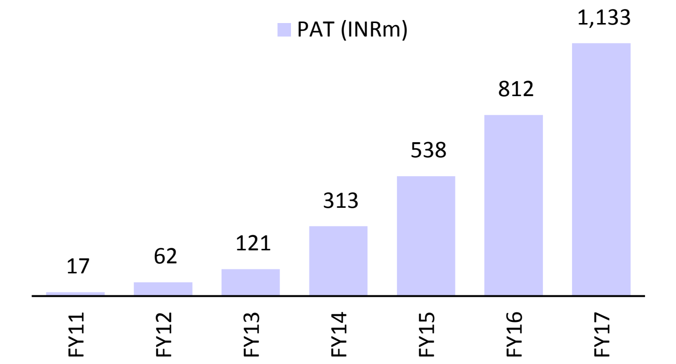
Source: MOSL, Company

Exhibit 39: Margins have expanded by 110bp over the same period



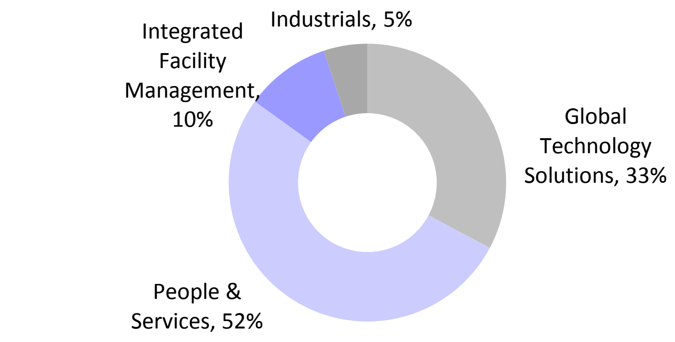
Source: MOSL, Company

Exhibit 40: Consequently, PAT has seen a CAGR of 79% over FY12-17



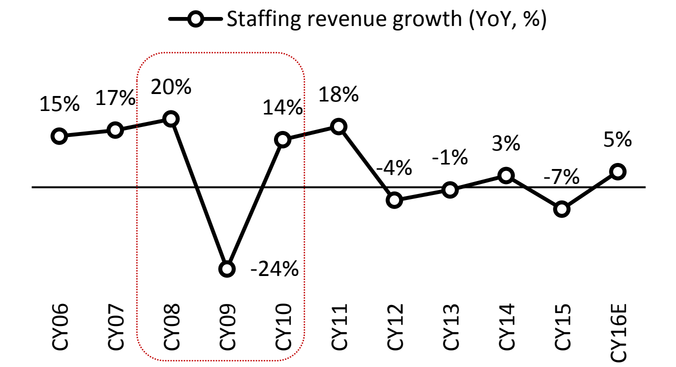
Source: MOSL, Company

Exhibit 41: Growth has been organic and driven by acquisitions, enabling presence in multiple segments…



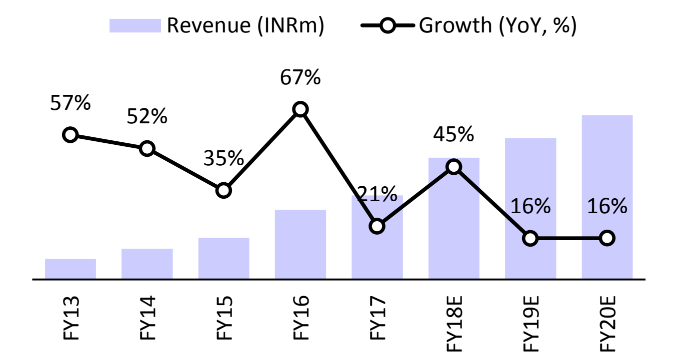
Source: Company

Exhibit 42: …which can shield the company from volatility during economic shocks…



Source: MOSL, Bloomberg

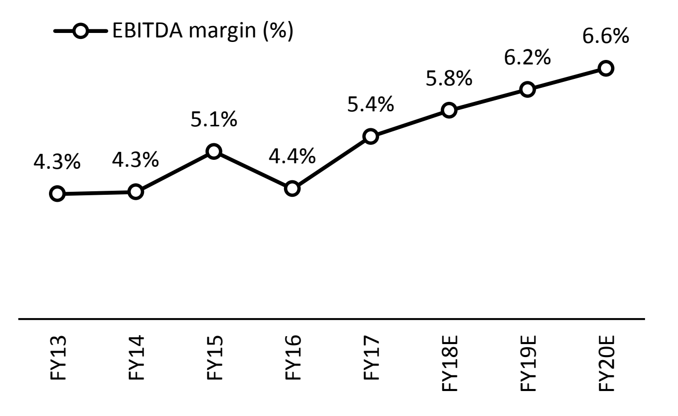
Exhibit 43: …and lead to continued momentum going forward (not factoring in additional acquisitions)



Source: MOSL, Company

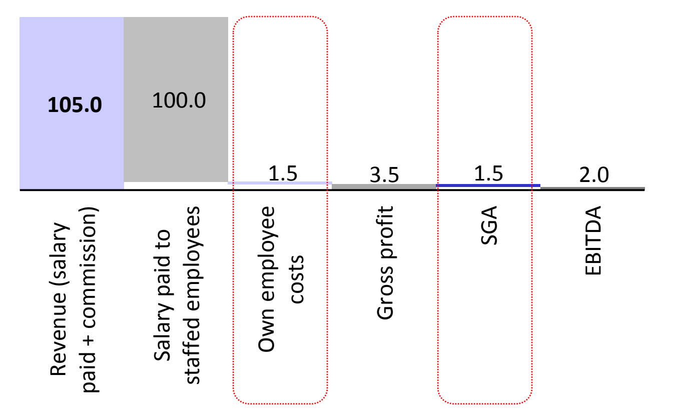
Story in charts

Exhibit 44: Expect improvement in margins, led by turnaround in acquisitions…



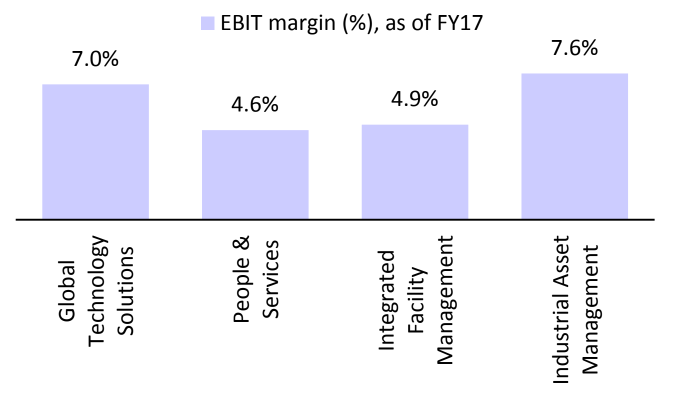
Source: MOSL, Company

Exhibit 45: …operational leverage in the Staffing business…



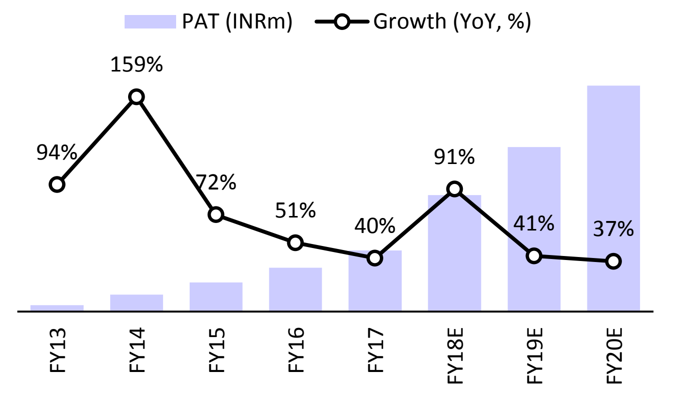
Source: MOSL

Exhibit 46: …and higher growth in higher-margin businesses…



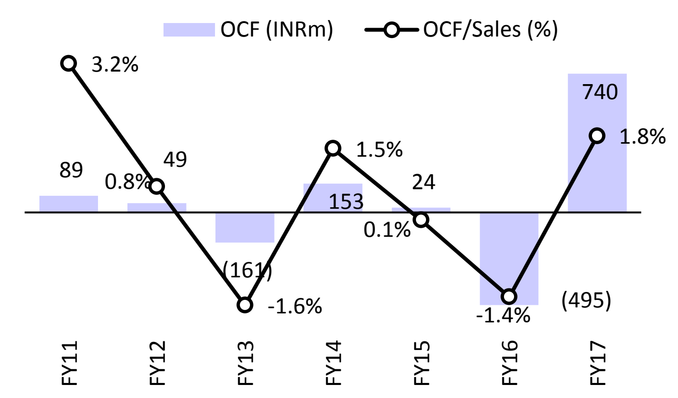
Source: Company

Exhibit 47: …leading to expectations of 55% PAT CAGR over the next three years



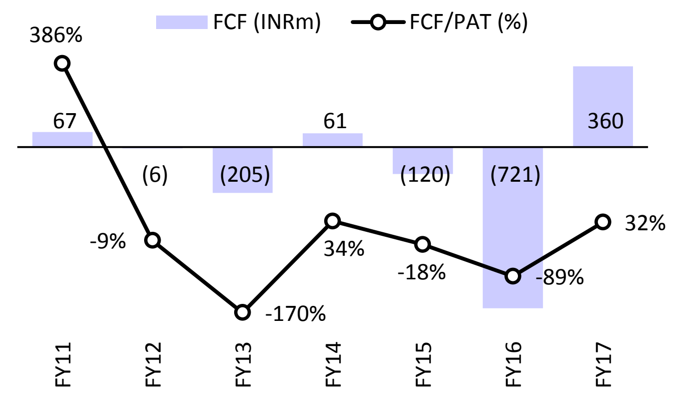
Source: MOSL, Company

Exhibit 48: Cash generation, however, has been dismal, even at the operating level…



Source: MOSL, Company

Exhibit 49: …let alone FCF (excluding acquisitions)



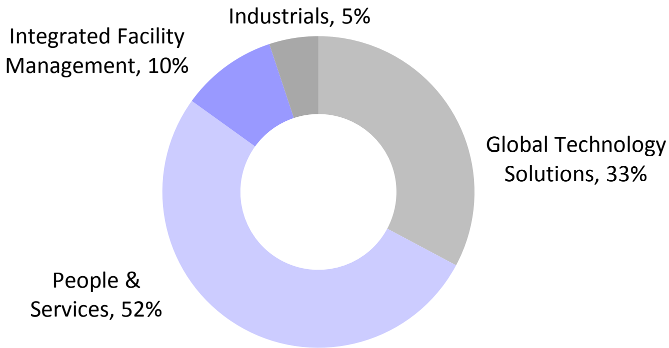
Source: MOSL, Company

Promising prsopects…

…Rightly positioned in multiple high-growth areas

Quess operates through four key business segments: [1] Global Technology Solutions (GTS), [2] People & Services (P&S), [3] Integrated Facility Management (IFM), and [4] Industrials. All of these areas have been witnessing high growth, which is expected to continue going forward as well.

Exhibit 50: Diversified business segments



Source: Company

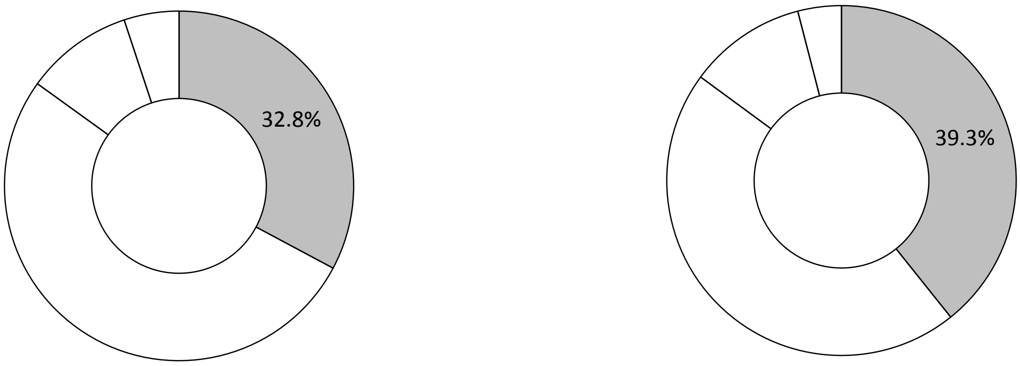
Exhibit 51: Strong growth exhibited across segments over the last five years (even organically)

	FY11	FY12	FY13	FY14	FY15	FY16	FY17
GTS							
Revenue (INR m)	462	2,049	2,687	4,097	5,898	9,217	11,830
Revenue growth (YoY, %)		343.6%	31.1%	52.5%	44.0%	56.3%	28.3%
P&S							
Revenue (INR m)	1,835	3,626	6,220	8,995	11,229	19,499	23,454
Revenue growth (YoY, %)		97.6%	71.6%	44.6%	24.8%	73.6%	20.3%
IFM							
Revenue (INR m)	462	713	1,123	1,863	2,421	3,724	4,046
Revenue growth (YoY, %)		54.6%	57.4%	65.8%	30.0%	53.8%	8.6%
Industrials							
Revenue (INR m)					1,038	1,934	2,244
Revenue growth (YoY, %)						86.4%	16.0%

Numbers for FY14 and FY15 have been normalized to 12 month periods; Source: Company

1. Global Technology Solutions

Exhibit 52: IT staffing | IT solutions | IT products (33% of revenue; 39% of EBIT)



Source: Company

Exhibit 53: 42/49% Revenue/EBITDA CAGR over the last five years

	FY12	FY13	FY14	FY15	FY16	FY17
Revenue (INRm)	2,049	2,687	4,097	5,898	9,211	11,830
Revenue growth (YoY, %)	*343.6%*	*31.1%*	*52.5%*	*44.0%*	*56.3%*	*28.3%*
EBITDA (INRm)	135	181	332	504	667	990
EBITDA margin (%)	*6.6%*	*6.7%*	*8.1%*	*8.5%*	*7.2%*	*8.4%*

Numbers for FY14 and FY15 have been normalized to 12 month periods; Source: Company

The Global Technology Solutions (GTS) segment contributed 32.8% of overall revenue and 39.3% of overall EBIT in 1QFY18. It has over 10,000 employees serving in over 300 clients. The group broadly classifies into three segments:

- **IT staffing – India (Magna Infotech)**

  Magna Infotech is the largest IT staffing company in India with a broad presence across verticals, and clientele that includes several leading Indian IT service providers and global captives set up in India. **Magna Infotech was acquired in December 2011.**

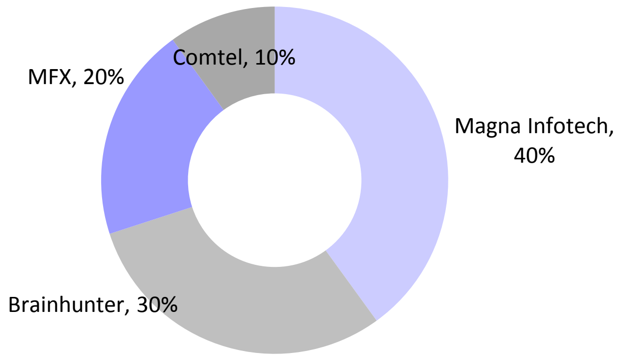
- **IT staffing – North America (Brainhunter)**

  Brainhunter is an IT and engineering professional staffing company headquartered in Canada. Apart from IT staffing, recruitment and payroll management, the company also provides software solutions to leverage technology for recruitment. **Brainhunter was acquired in October 2014.**

- **IT solutions and products (MFX)**

  MFX provides services and solutions in the P&C insurance space in North America. Offerings include system integration, application development and BPO, datacenter and infrastructure services including private cloud offerings. **MFX was acquired in November 2014.**

Exhibit 54: Revenue split within GTS



Source: Company, MOSL

Performance

The segment has seen strong growth over the last five years, posting 42% revenue CAGR and 49% EBITDA CAGR. EBITDA margin has improved from 6.6% in FY12 to 8.4% in FY17 despite the integration of Brainhunter and MFX, which have diluted overall profitability. The margin expansion has primarily come from an improvement in margins in the Indian professional staffing business (Magna Infotech), Brainhunter and MFX.

Growth prospects

The professional IT staffing market grew at a CAGR of 19% over 2009-14 to INR125b and is expected to grow at a CAGR of 22% over 2014-19. Faster growth in the market in the future is expected to be driven by:

- **Technology service providers:** The current flexi staff penetration in the Indian IT industry stands at 10% compared to ~20% in the developed nations. With increasing competition and margin pressures, IT companies are moving towards recruiting more temporary staff.
- **Captives:** According to NASSCOM, India houses 300-380 captives, which contribute 10-12% of the IT services industry revenue and 10-15% of the total employee base. Growth in the activity of captives, and consequently, in their use of temporary staffing would also result in an opportunity for staffing agencies.

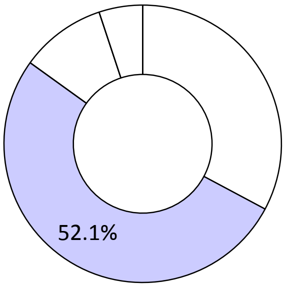
Automation may bring out non-linearity, reducing the required volume in the industry. This has the potential to slow growth in the medium term. However, there are several offsets against this, including [1] under-penetration of temporary staffing in Indian IT, compared to global average, and [2] Quess' presence in mid-experience jobs and not much exposure to categories exposed to the risk of automation.

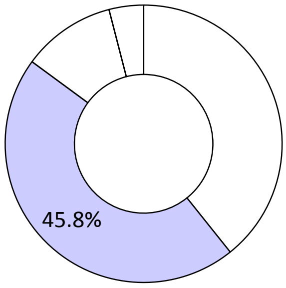
The US staffing market is expected to grow at 6-7%. Skill shortage, strong growth in US technology employment and increased adoption of the flexi staffing model by the industry are likely to be the key drivers for growth in North America.

We expect the segment to exhibit 25% revenue CAGR over FY17-20. Growth in FY18 would be further boosted by the integration of Comtel.

2. People & Services

Exhibit 55: General staffing | HR services | HR solutions (52% of revenues; 46% of EBIT)





Source: Company

Exhibit 56: 45/55% Revenue/EBITDA CAGR over the last five years

	FY12	FY13	FY14	FY15	FY16	FY17
Revenue (INRm)	3,626	6,220	8,995	11,229	19,499	23,454
Revenue growth (YoY, %)	*97.6%*	*71.6%*	*44.6%*	*24.8%*	*73.6%*	*20.3%*
EBITDA (INRm)	131	288	235	313	679	1,160
EBITDA margin (%)	*3.6%*	*4.6%*	*2.6%*	*2.8%*	*3.5%*	*4.9%*

Numbers for FY14 and FY15 have been normalized to 12 month periods; Source: Company

The People & Services (P&S) segment constituted 52.1% of overall revenue and 45.8% of overall EBIT in 1QFY18. The P&S business includes the following:

- Executive search (IKYA Search Partners)
- Recruitment (IKYA Recruitment & RPO)
- General staffing (IKYA)
- Workforce management solutions (PeopleNow)
- Technology solutions for the retail industry (InEdge Retail Solutions)
- Payroll and compliance (CoAchieve)
- Digital labor law compliance (Simpliance)
- Logistics solutions (Dependo)
- Skill development (Excelus)

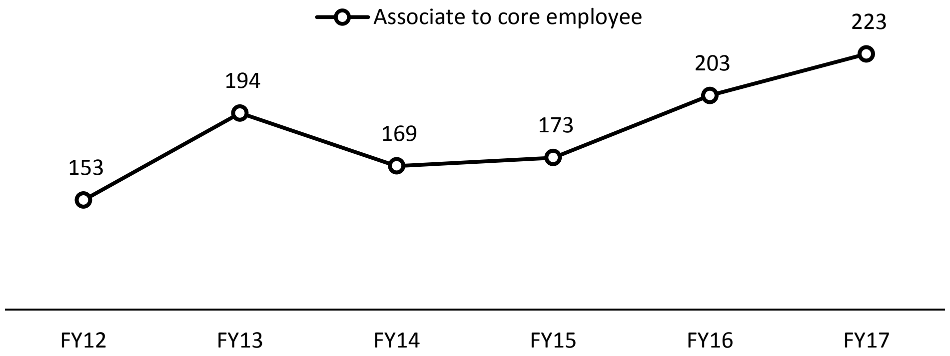
Majority of the revenue in this segment is contributed by the general staffing business. The business includes ~115,000 associates serving over 200 clients. Significant clients in this segment are Amazon, Bata, FMC, Hinduja Group, PNB Housing Finance and VF Brands.

Within general staffing, bulk of the revenue is contributed from India. The company also has presence in UAE and Sri Lanka, through the acquisitions of Styracorp and Randstad Sri Lanka, respectively.

Performance

The segment has seen strong growth over the last five years, posting 45% revenue CAGR and 55% EBITDA CAGR. EBITDA margin has improved over the last three years to 4.9% in FY17 from 2.7% in FY14. The improvement has largely been led by better portfolio mix, as the contribution of training and development in the overall revenue pie has increased. The general staffing business also tends to see gradual improvement, led by increase in the Associate / Core Employee ratio.

Exhibit 57: Efficiency improvement with scale

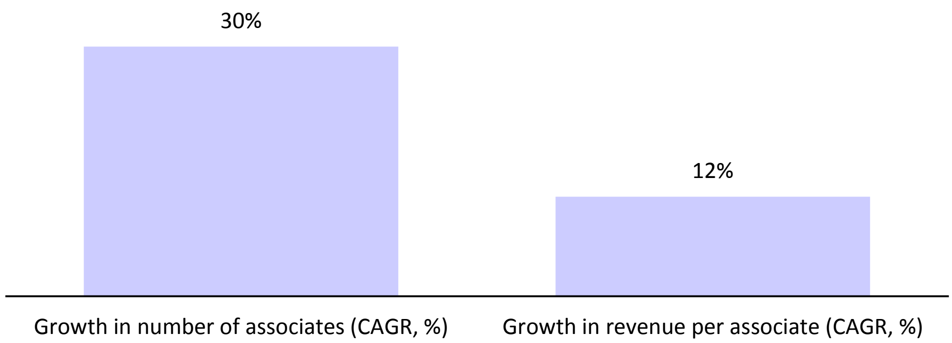


Source: Company, MOSL

Quess' 45% revenue CAGR (FY12-17) in the P&S business has been a good mix of volume and realization growth. Over the last five years, while the associate count has increased at a CAGR of 30%, realization per associate has increased at a 15% CAGR.

While the volume growth can be attributed to industry growth and Quess' expansion, the realization gain has been on account of wage inflation and improvement in employee mix.

Exhibit 58: 45% revenue CAGR over the last five years in P&S



Source: Company, MOSL

Growth prospects

The temporary general staffing market in India had revenue of INR385b in 2014 and is expected to exhibit 19% CAGR over 2019. The main drivers of the high industry growth rate for India are [1] under-penetration of temporary staffing in India, [2] non-linearity provided by an increase in employee productivity, and [3] shift of market from organized to unorganized.

In this backdrop, there are several advantages Quess has, apart from being amongst the top-5 players. These advantages are in the form of:

- Quess does 70-80% of the sourcing for its customers, compared to 20% for TeamLease.

- Quess has better revenue/customer and associate/customer ratios compared to TeamLease. It works with 200 customers (versus 1,200 for TeamLease), showing better client mining abilities.
- It extends funding to a larger proportion of its customer base (40% of revenue), versus 20% for TeamLease.
- It is able to provide additional ancillary services to its customers, thus seeing superior profitability in the business.

We are of the opinion that the general staffing business can see a sustained growth of ~20% over the coming years, and estimate Quess to deliver results in line with this macroeconomic tailwind. **We are factoring in 22% CAGR in the P&S business over FY17-20.**

Profitability improvement can also be expected, as scale-related efficiencies continue kicking in, and the smaller service lines of payroll, compliance, training and development, RPO, etc continue grabbing a larger share of the P&S pie. **We expect margins to inch towards 5.5% by FY20 from 4.9% in FY17.**

3. Integrated Facility Management

Exhibit 59: Facilities management | Catering | Security services (10% of revenue; 11% of EBIT)

Source: Company

Exhibit 60: 42/38% Revenue/EBITDA CAGR over the last five years

	FY12	FY13	FY14	FY15	FY16	FY17
Revenue (INRm)	713	1,123	1,863	2,421	3,719	4,046
Revenue growth (YoY, %)	*54.6%*	*57.4%*	*65.8%*	*30.0%*	*53.8%*	*8.6%*
EBITDA (INRm)	46	75	205	167	227	230
EBITDA margin (%)	*6.4%*	*6.6%*	*11.0%*	*6.9%*	*6.1%*	*5.7%*

Numbers for FY14 and FY15 have been normalized to 12 month periods; Source: Company

The Integrated Facility Management (IFM) segment contributed 10.0% of overall revenue and 10.9% of overall EBIT in 1QFY18. In this business, Quess provides facility management solutions to corporates, airports and other organizations such as hospitals and schools across India. Through this business, Quess manages 200m square feet of space across 550 locations in India, serving over 850 clients with around 20,000 associate employees.

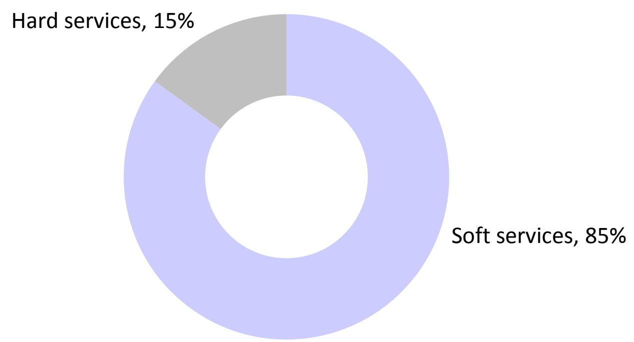
Its range of services includes janitorial services, electro-mechanical services, pest control, and food and hospitality services.

These services are provided under the brands, *Avon* and *Aravon*. They were acquired by Quess in May 2013 and April 2015, respectively. When acquired, Avon's offerings spanned across soft and hard services, pest control, and catering.

Aravon was a distinct facilities management player in Healthcare, Industrial and Hospitality segments. Service offerings for Aravon include healthcare and support, food and hospitality, guest house and hospitality management, and facility management for the verticals of BFSI and manufacturing.

The IFM business works on a cost plus model, with typical mark-up being ~10%.

Exhibit 61: Revenue split within IFM

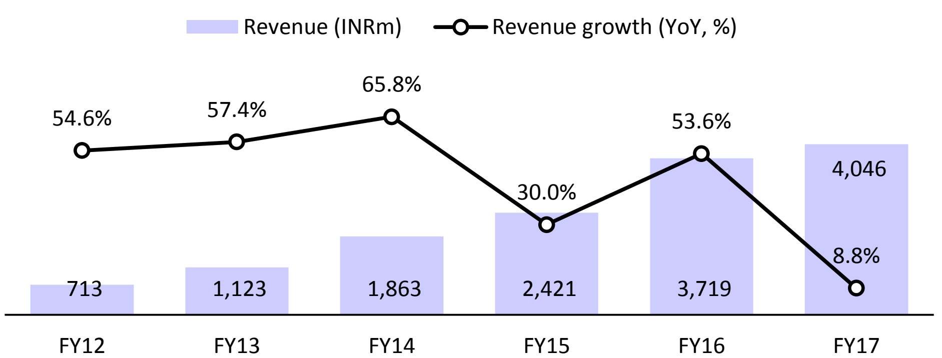


Source: Company, MOSL

Performance

The segment has seen strong growth over the last five years, posting 42% revenue CAGR and 38% EBITDA CAGR. EBITDA margin has been around 6% over the last five years. However, we expect this to improve as the company integrates the higher margin businesses of Manipal Integrated Services and Terrier Security Services going forward.

Exhibit 62: Strong growth seen in IFM over the last five years

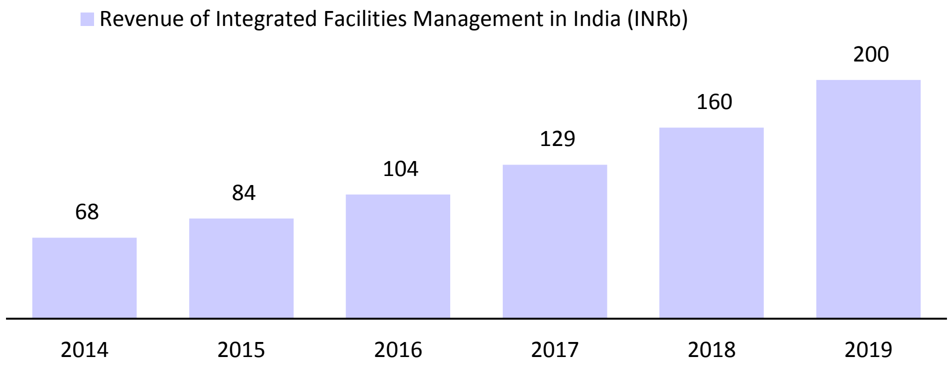


Numbers for FY14 and FY15 have been normalized to 12 month periods; Source: Company, MOSL

Growth prospects

The Financial Management (FM) services market is expected to grow from INR68.2b in 2014 to INR199.6b in 2019 (CAGR of 24%). Majority of the growth is expected to be driven by the consistent growth in demand from the commercial sector. In addition, the increasing preference for professional FM in the residential sector coupled with increased incidence of high rise residences that require unique FM solutions is expected to further drive growth.

Exhibit 63: 24% CAGR expected in the Facilities Management industry



Source: F&S Research

We expect this segment to exhibit 63% revenue CAGR over the next two three years. We expect margins to inch up from 5.7% in FY17 to 8.0% in FY20, driven by better business mix and higher growth in segments that have better profitability.

Exhibit 64: Gross margins better in select segments in the Facility Management space

	Gross margin
Healthcare / Hospitals	15-30%
Government owned properties and parks	4-8%
High profile govt. offices, assembly houses, ministers' house etc.	15-25%
Infrastructure (Airports)	5-10%
Industrial	18-20%
Commercial (Multi-tenanted/Individual Office Complexes)	10-35%

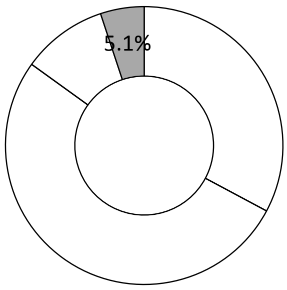
Source: F&S Research

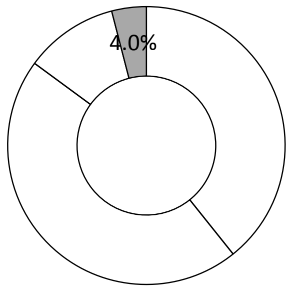
Visibility of the strong growth comes from the integration of Manipal Integrated Services and Terrier Security Services. Together, these are expected to add ~INR8b to revenue.

Manipal Integrated Services is a facilities management, food services and security services company. Terrier Security Services is present in the areas of manned guarding and security solutions.

4. Industrials

Exhibit 65: Operations and Maintenance | Consulting | Training (5% of revenue; 4% of EBIT)





Source: Company

Exhibit 66: Presence acquired through the acquisition of Hofincons in FY15

	FY12	FY13	FY14	FY15	FY16	FY17
Revenue (INRm)				1,038	1,934	2,244
Revenue growth (YoY, %)					*86.4%*	*16.0%*
EBITDA (INRm)	-	-	-	146	221	180
EBITDA margin (%)				*14.1%*	*11.4%*	*8.0%*

Numbers for FY14 and FY15 have been normalized to 12 month periods; Source: Company

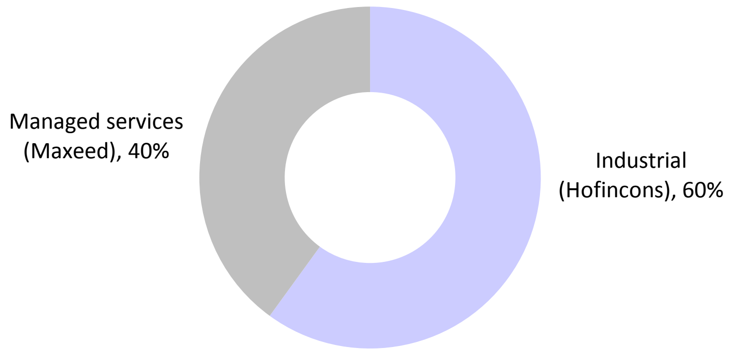
The Industrials segment contributed 5.1% of overall revenue and 4.0% of overall EBIT in 1QFY18. Quess has presence in this business on account of the acquisition of **Hofincons**, which it took over in June 2014. Hofincons operates in various industries including power, energy, oil & gas, chemicals, and ferrous and non-ferrous metal industries across India and the Middle East. The broad services offerings in this division are:

- **Industrial Operations and Maintenance (O&M):** These include solution-driven maintenance services in the areas of preventive maintenance, condition monitoring, shutdown services, breakdown repair and asset life extension. The services focus on minimizing maintenance costs and optimizing plant availability.
- **Technology and Consulting (T&C):** T&C provides clients with an integrated approach to Asset Management, delivering end-to-end ERP Data Solutions and EPC support services. The service focuses on the importance of managing asset data and achieving improved information management and asset performance.

In addition to this, Quess also provides managed services for utilities (meter reading services) and telecom companies (tower maintenance and network deployment services) under the **Maxeed** brand (own brand; operational since 2007).

Significant clients in this segment include L&T Special Steels and Heavy Forgings and other large energy and resources companies.

Exhibit 67: Revenue split within IAM



Source: Company, MOSL

Performance

Quess started separately disclosing revenue in this segment only after the acquisition of Hofincons in FY15. Revenue from IAM was INR2.2b in FY17, contributing to 5.4% of total revenue. Profitability is healthy in this business, with Quess reporting 8.0% EBITDA margin in FY17.

Growth prospects

We expect growth to moderate in this segment, given Quess' exposure in distressed sectors like power and metals. However, growth can be strong in the managed services business, which caters to telecom players as well. **We are factoring in 20% revenue CAGR over the next three years.** Although the income statement metrics can improve, high receivable days and cash flow issues have been impacting the business. A correction here would be correlated to improvement in the health of Quess' end customers.

Execution has been encouraging so far

Improvement metrics haven't reflected in a holistic manner

Quess has made multiple acquisitions since inception that have aided growth and diversification into the offerings it has today. The company started off as a general staffing agency and acquired most of the other businesses over time.

Exhibit 68: M&A – Quess Corp

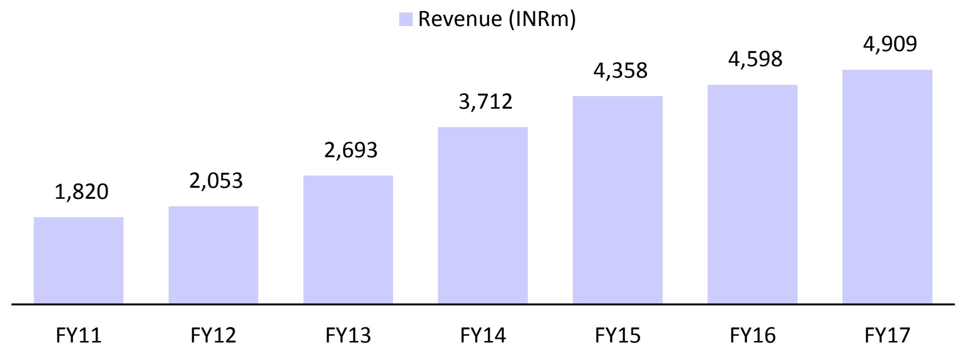
	Date	Target	Service
1	23-Dec-11	Magna Infotech	• IT staffing
2	13-May-13	Avon	• Facility management
3	27-Jun-14	Hofincons	• Industrial facilities management with an interest in electrical, mechanical and instrumentation services
4	23-Oct-14	Brainhunter	• IT staffing
5	3-Nov-14	MFX	• Service provider of cloud-based IT applications and outsourcing solutions in the commercial P&C industry
6	1-Apr-15	Aravon Services	• Integrated facility management service player, distinct in the field of Healthcare, Industrial and Hospitality sectors
7	1-Jun-15	Transfield Services*	• Oil and gas
8	5-Dec-15	Styracorp	• Human resources staffing solutions
9	5-Dec-15	IME Consultancy	• HR staffing solutions in the Middle East
10	26-Apr-16	Randstad Lanka	• General staffing in Sri Lanka
11	19-Oct-16	Comtel Solutions	• Staffing solutions, managed services solutions, and recruitment and search services in Singapore
12	19-Oct-16	Simpliance Technologies	• Solution for meeting labour compliance requirements of corporates
13	19-Oct-16	Terrier Security	• Provider of manned guarding services and electronic security solutions
15	28-Nov-16	Manipal Integrated Services*	• Facility management in healthcare and education
16	28-Nov-16	Inticore VJP Advanced Systems	• Engineering design and solutions
16	23-Jan-17	Heptagon	• Niche software development company working with machine learning and automation technologies

*Announced but not closed; Source: Company, Bloomberg, MOSL

Magna Infotech has seen high growth and profitability improvement post acquisition

Quess acquired Magna Infotech in FY11 when the revenue of the business was INR1.8b. Over the last six years, Magna Infotech has grown at a CAGR of 18%. It now is the largest professional IT staffing company in India, with revenue of INR4.9b as of FY17.

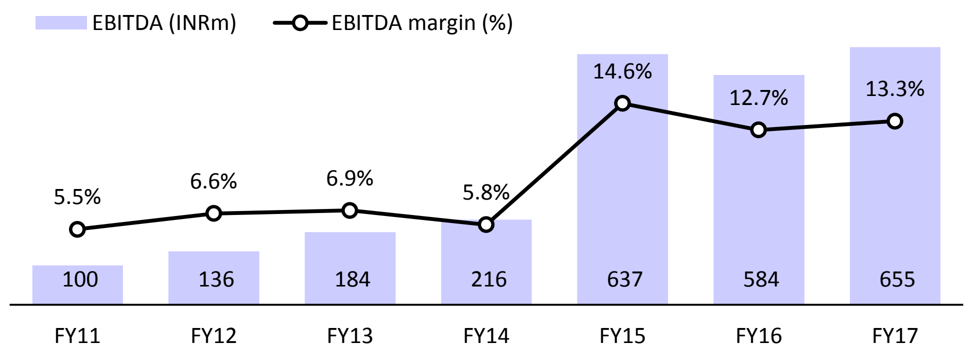
Exhibit 69: 18% CAGR in Magna Infotech post acquisition by Quess



Source: Company

Magna Infotech had an EBITDA margin of 5.5% in FY11, when it was acquired by Quess. Since then, profitability has improved; in FY17, EBITDA margin was 13.3%.

Exhibit 70: Sharp improvement in Magna Infotech's profitability

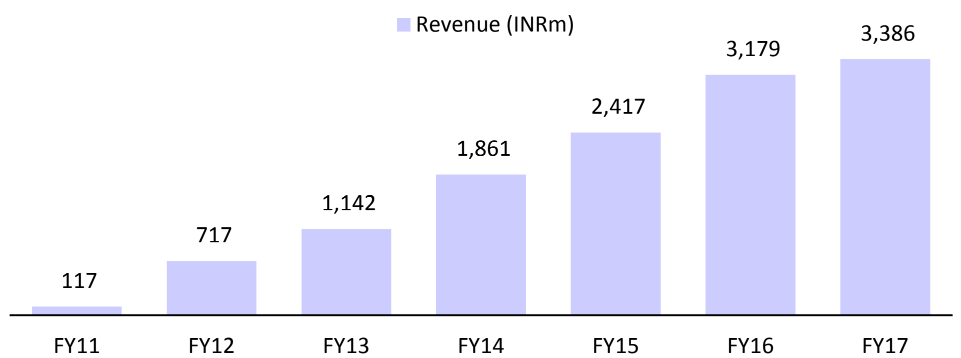


Source: Company

Similar story in Avon

The trajectory has been similar for Avon. In FY09, Avon had revenue of INR117m. Over the last eight years, it has seen 52% revenue CAGR, with revenue now at INR3.4b (as of FY17).

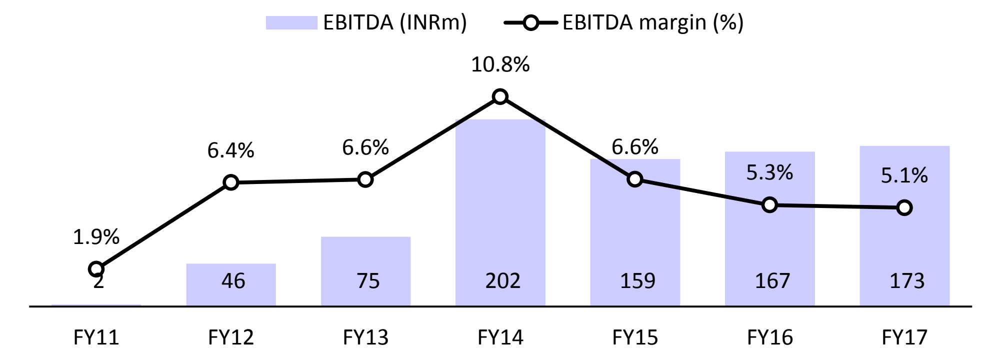
Exhibit 71: 52% CAGR in Avon over the last eight years



Source: Company

Profitability improvement too has been in tandem with revenue growth in the business. In FY09, Avon had an EBITDA margin of 1.7%. However, this has now increased to 5.1% (as of FY17).

Exhibit 72: Margins have improved from 1.9% to 5.1%



Source: Company

Recent acquisitions turning profitable

Multiple acquisitions were loss-making when Quess acquired them. Brainhunter and MFX were both loss-making till FY16. Some of the issues in the business were – high SGA, onsite-heavy teams and operational inefficiencies. Quess was able to turn both these businesses around by optimizing costs, tweaking the business model and increasing offshoring. Going forward, higher margins in these businesses are likely to result in improvement in overall margins.

Management bandwidth and breadth of operations

Quess has acquired several entities in different clusters that it operates across multiple geographies. Each of these companies is managed by independent and experienced professionals. The management doesn't get involved in day-to-day operations. Roadmaps are discussed with the subsidiaries regularly and strategic direction is decided by the owner management of the target company. Financing decisions, capital allocation and strategy are discussed at the group level.

M&A has been the name of the game

Staffing firms globally have undertaken a large number of M&A for more than half a century now. The primary areas for inorganic growth for these companies have been towards gaining scale, presence in ancillary services and geographical expansion as other markets started to evolve.

We see aggressive M&A in a human capital intensive industry as risky, with a likelihood of value destruction that cannot be ignored.

Disciplined approach towards inorganic growth

Globally, companies like Adecco and Randstad have been disciplined on their capital allocation.

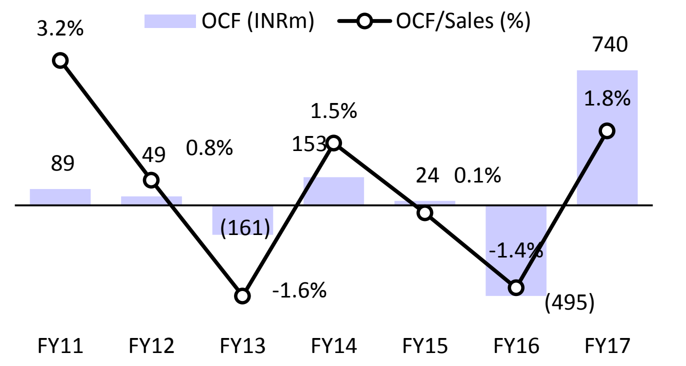
Similarly, Quess has been maintaining a disciplined approach while assessing and taking over businesses. The key points ensured by Quess are: [1] EBITDA payback of

4-5 years, [2] focus on cash generation abilities of the asset, [3] smaller acquisitions that give capabilities, rather than acquiring for scale, [4] management retention in order to ensure smooth integration and functioning of operations, [5] availability of currency to make the acquisition, and [6] focus on overall profitability improvement through acquisitions by getting into higher-margin businesses.

Cash conversion has been weak…

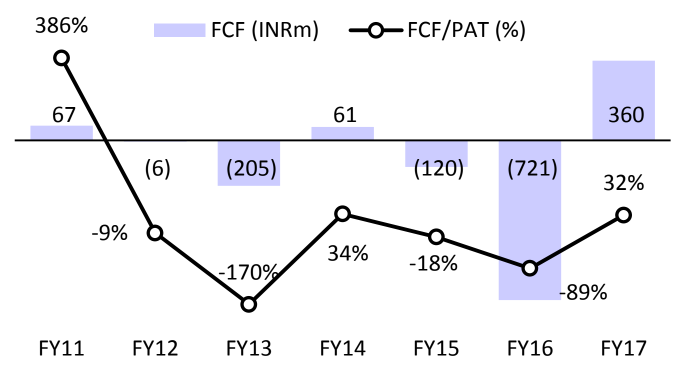
Despite the successful integration of acquisitions, Quess has failed to generate cash, even at an operating level, on a consistent and sustained basis. The cumulative OCF over the last seven years has been INR398m.

Exhibit 73: Cumulative OCF over the last six years has been negative…



Source: Company

Exhibit 74: …and so has cumulative FCF



Source: Company

…Except in FY17

In FY17, Quess made an operating cash flow of INR740. This was led by a 44% jump in profitability led by an increase in PBT margins to 4.0% in FY17, from 3.3% in the year before; and a reduction in working capital needs.

Exhibit 75: Improved cash generation in FY17

	FY11	FY12	FY13	FY14	FY15	FY16	FY17
PBT	30	129	234	288	1,049	1,147	1,652
Adjustments	32	62	94	79	119	222	307
Interest income	(8)	(13)	(12)	(2)	(9)	(70)	(124)
Finance costs	48	126	176	88	218	310	465
OCF before WC changes	102	304	493	454	1,378	**1,609**	**2,300**
Changes in WC	71	(163)	(454)	(52)	(942)	**(1,622)**	**(759)**
Income tax paid	(84)	(93)	(200)	(249)	(412)	(482)	(802)
OCF before WC changes	89	49	(161)	153	24	(495)	740

Source: Company

If we were to exclude certain one-off factors, OCF would be even higher in FY17 at ~INR950m or 2.3% of sales, versus an average of -0.2% in the five years prior to that (FY12-16).

[1] Income tax liabilities: For current tax liabilities of INR82m, there is no legally enforceable right to set off against the non-current tax assets and disclosed separately.

[2] Payable for acquisition of business: Other current financial liabilities consist of INR151m towards consideration payable and INR43m towards contingent consideration payable.

[3] Provision for bonus and incentive: Other current financial liabilities include an amount of INR454m as a provision for the payment of bonus as per the circular issued by Ministry of Law and Justice dated December 31, 2015.

Exhibit 76: Cash flows excluding some non-repeatable items look even better

		Reported	Adjusted	Effect on OCF	
	FY16	FY17	FY17	FY17 - R	FY17 - A
Current assets					
Inventories	18	57	57	(39)	39
Trade receivables	4,053	4,468	4,468	(416)	416
Cash and cash equivalents	1,066	3,013	3,013	na	na
Bank balances other than cash and cash equivalents	27	1,583	1,583	na	na
Current loans	174	230	230	(56)	56
Other current financial assets	2	26	26	(24)	24
Unbilled revenue	2,873	3,868	3,868	(995)	995
Other current assets	235	262	262	(27)	27
Total current assets	**8,449**	**13,508**	**13,508**	**(1,556)**	**1,556**
Current liabilities					
Bank overdraft	39	3	3	(35)	(35)
Current borrowings	3,390	4,557	4,557	na	na
Trade payables	674	631	631	(42)	(42)
Other current financial liabilities	2,630	2,864	3,124	234	494
Income tax liabilities	-	82	-	82	-
Current provisions	197	227	227	30	30
Other current liabilities	1,217	1,770	1,770	553	553
Total	**8,146**	**10,135**	**10,313**	**822**	**1,000**
Working capital	**2,600**	**3,334**	**3,156**	**(734)**	**(556)**

Source: MOSL, Company

While performance on the cash front in FY17 has been starkly different from that in the previous years; sustenance of this positive trend would be crucial in determining consistent growth performance, and triggering re-rating.

Expect a continued high-growth phase

Revenue CAGR of 25% isn't out of the way

With the strategy in place, and execution being impeccable, we expect 25% revenue CAGR over FY17-20. This would be fueled by the current portfolio, and any inorganic activity will only add to these expectations.

These expectations don't seem to carry much risk given the fact that historical growth rates have been superior, and there is visibility on account of recent acquisitions. Over the last year, Quess has acquired Comtel Solutions, Heptagon, Manipal Integrated Services, Simpliance and Terrier Security Services.

Together, these are expected to contribute to ~INR10b in revenue for FY18: Comtel Solutions (INR2b), Heptagon (negligible), Manipal Integrated Services (INR5b), Simpliance (negligible) and Terrier Security Services (INR3b).

Exhibit 77: Expect revenue growth momentum to continue

	Revenue (INR m)				Growth (YoY, %)			
	FY17	FY18E	FY19E	FY20E	FY17	FY18E	FY19E	FY20E
GTS	11,830	15,970	18,366	21,120	28%	35%	15%	15%
P&S	23,454	29,318	33,715	38,773	20%	25%	15%	15%
IFM	4,046	12,138	14,566	17,479	9%	200%	20%	20%
Industrials	2,244	2,692	3,231	3,877	17%	20%	20%	20%
Overall	**41,574**	**60,118**	**69,878**	**81,249**	**21%**	**45%**	**16%**	**16%**

Source: Company, MOSL

Visibility on profitability improvement exists too

Over the same period, we also expect cumulative EBITDA margin expansion of 125bp to 6.6%. The visibility for this comes from:
[1] Continued improvement in profitability in Brainhunter and MFX, which were loss-making entities,
[2] Growth in Global Technology Solutions (33% of revenue), which has higher margins than the rest of the portfolio,
[3] Improvement in margins in the People & Services business, led by operational leverage and higher share of revenue from Training & Development, and
[4] Integration of higher EBITDA margin businesses, going forward: Comtel Solutions (~7%), Manipal Integrated Services (~10%) and Terrier Security Services (~6%).

Exhibit 78: Expect 125bp EBITDA margin expansion over FY17-20

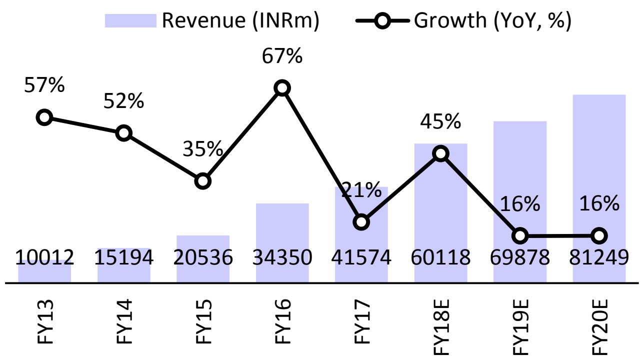
	EBITDA (INRm)				EBITDA margin (%)			
	FY17	FY18E	FY19E	FY20E	FY17	FY18E	FY19E	FY20E
GTS	990	1,416	1,721	2,084	8.4%	8.9%	9.4%	9.9%
P&S	1,160	1,509	1,802	2,150	4.9%	5.1%	5.3%	5.5%
IFM	230	850	1,092	1,398	5.7%	7.0%	7.5%	8.0%
Industrials	180	215	291	388	8.0%	8.0%	9.0%	10.0%
Overall	**2,228**	**3,510**	**4,348**	**5,372**	**5.4%**	**5.8%**	**6.2%**	**6.6%**

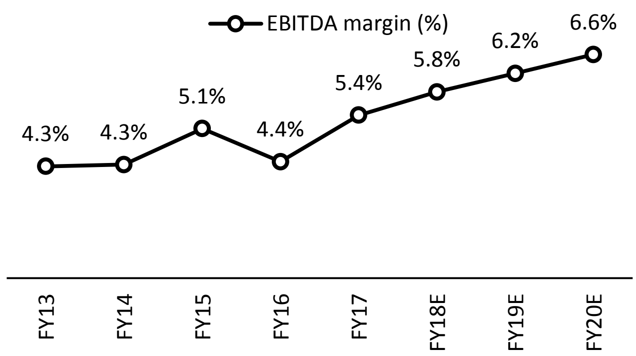
Source: Company, MOSL

Expected revenue CAGR of 28% and EBITDA margin expansion of 125bp over FY17-20 should result in EBITDA CAGR of 58%. We also expect ETR to reduce from 31.4% in FY17 to 27.4/21.8/17.7% in FY18/19/20E. This would be led by a lower tax rate in MFX and incremental profits from Comtel, which operates in a lower tax rate geography.

Moreover, Quess is also eligible to draw the benefits of Section 80JJAA, relating to a 30% deduction on wages paid to new workmen (in excess of 50) in the previous year, for three assessment years. We have also factored that into our ETR estimates.

Exhibit 79: Expect strong financial performance over the next three years





Source: Company, MOSL

Valuations are as steep; but so is growth!

A leading integrated business services provider

- Quess operates through four key business segments: [1] Global Technology Solutions (GTS), [2] People & Services (P&S), [3] Integrated Facility Management (IFM), and [4] Industrials. All of these areas have been witnessing high growth, which is expected to continue going forward as well.
- In terms of penetration, it has barely scratched the surface in its core staffing business as well as other areas. In general staffing, India's low penetration of 0.5% of working population (versus global average of 1.5%) itself will drive high velocity growth.
- In business services, Quess intends to be part of anything that is non-core to a business, and that can be outsourced to a third party. While it has touched upon the areas of facilities management, catering, security and industrial asset management, the directions for further growth are ample.

Successful track record on acquisitions

- Inorganic growth has been a key component for Quess' growth, improvement in profitability and diversification. It has demonstrated successful integration with payback periods of ~5 years, margin accretion and retention of management personnel.
- The diversification it has achieved over the years makes it a stable bet in case of volatility in the economic cycle. Staffing companies across the globe witnessed a 40% gap between the peak and trough during the CY08-09 global financial meltdown.
- Validation also comes from the following examples:
- [1] Over the last eight years, revenue at Avon has grown at a CAGR of 52% and EBITDA margin has improved to 5% from 2% at the time of acquisition.
- [2] Magna has grown at a CAGR of 18% over the last six years and its margins have improved to 13% from 6% at the time of acquisition.
  [3] Profitability has been gradually improving in both Brainhunter and MFX since they have been acquired.

Strong growth expectations going ahead…

- With the strategy in place, and execution being impeccable, we expect 28% revenue CAGR over FY17-20. This would be largely fueled by the current portfolio and the integration of recent acquisitions. Further inorganic activity will only add to these expectations.
- Over the same period, we also expect cumulative EBIDTA margin expansion of 125bp to 6.6%. The visibility for this comes from [1] continued improvement in profitability in Brainhunter and MFX, which were loss-making entities, [2] growth in Global Technology Solutions (33% of revenue), which has higher margins than the rest of the portfolio, [3] improvement in margins in the People & Services business, led by operational leverage and higher share of revenue from Training & Development, and [4] integration of higher margin Manipal Integrated Services, Terrier and Comtel.

...but sustained cash flow improvement necessary too

- Quess' cumulative OCF/FCF over the last six years are negative (INR309m / -INR630m). Debtor days are worse (45 v/s 20 for TeamLease) because of its presence in GTS, IFM and Industrials (60-65 days). Moreover, in the P&S business, it extends funding for 40% of its revenue compared to 20% for TeamLease.
- An improvement in cash flow generation would be a necessary factor for valuations to sustain at current levels. Although the turn has been positive in FY17, the continued momentum in this direction, in our view would be necessary; whereas high growth at the cost of cash generation would be value-dilutive.

Valuation and view: Multi-dimensional growth opportunity

- We value Quess using DCF to reach a price target of INR990. While we observe a direct relation between P/E multiples of staffing companies with their growth and the value of services offered, there is an inverse relationship with risk of inorganic activity and a broad portfolio.
- Over FY17-19, we expect 28% revenue CAGR, 37% EBITDA CAGR and 58% PAT CAGR, which make these valuations seem sustainable.
- Over a longer time horizon, the multiple opportunities opened up because of inorganic foray, and the flawless execution exhibited over the past many years make this an attractive opportunity despite steep valuations.

Exhibit 80: Fair value of INR990/share based on DCF

Discount rate	12.0%
Terminal growth rate	5.0%
PV FCF	36,343
PV of terminal value	90,440
NPV	126,782
Cash and cash equivalents	9,408
Deployed in acquisitions	7,526
Sales acquired	6,272
EBITDA acquired	470
EBITDA in FY19	564
Value of acquired EBITDA	11,289
Cash not deployed	1,882
Less: Debt	6,530
Total equity value	133,423
Per share	
PV FCF	268
PV of terminal value	668
NPV	936
Cash deployed in acquisitions	83
Cash not utilized	14
Less: Debt	48
Total equity value	985
NOSH m	135
CMP	830
Target price	990
Upside (%)	**19%**

Source: MOSL

Exhibit 81: We assume 12% WACC and 5% terminal growth rate

WACC/g	Sensitivity analysis				
990	3.0%	4.0%	5.0%	6.0%	7.0%
10%	1,130	1,270	1,460	1,760	2,240
11%	960	1,050	1,180	1,360	1,630
12%	830	900	990	1,100	1,270
13%	720	770	840	920	1,030
14%	640	680	730	790	860

Scenario analysis

We don't see much risk to our FY18/19 estimates, given the visibility provided by existing momentum in the business, integration of announced acquisitions, material improvement in the financials of lagging assets, and steady state of economic conditions. Quess was also able to largely mitigate the impact of demonetization because of its diversified portfolio, giving few reasons to worry about as far as near-term growth is concerned.

We have analyzed scenarios based on our medium-long-term estimates considered in our DCF valuation. Broadly, our scenario assumptions differ on the parameters of revenue growth, margins and working capital requirements.

Exhibit 82: Assumptions – differences across scenarios

	Bull	Base	Bear
Revenue growth (YoY, %)			
FY20-22	22%	20%	15%
FY23-25	22%	20%	15%
FY26-27	22%	20%	15%
EBIT margin (%)			
FY20-22	20bp	20bp	0bp
FY23-25	20bp	20bp	0bp
FY26-27	20bp	20bp	0bp
Working capital / Sales (%)			
FY20-22	10.0%	11.6%	13.0%
FY23-25	9.2%	11.2%	13.2%
FY26-27	8.8%	10.8%	12.8%

Source: MOSL

Exhibit 83: Value across scenarios

		Base case	Bull case	Bear case
Discount rate	12.0%			
Terminal growth rate	5.0%			
PV FCF		36,343	42,289	24,839
PV of terminal value		90,440	107,691	48,796
NPV		126,782	149,980	73,634
Add: Cash deployed in acquisitions		11,289	11,289	11,289
Add: Cash not utilized		1,882	1,882	1,882
Less: Debt		6,530	6,530	6,530
Total equity value		133,423	156,620	80,275
Per share				
PV FCF		268	312	183
PV of terminal value		668	795	360
NPV		936	1107	544
Add: Cash deployed in acquisitions		83	83	83
Add: Cash not utilized		14	14	14
Less: Debt		48	48	48
Total equity value		985	1156	593
NOSH m	135			
CMP	830			
Target price		990	1,156	593
Upside (%)		19%	39%	-29%

Source: MOSL

Bull case suggests ~40% upside from current levels

Our bull case assumes 2pp higher growth than we have assumed in our DCF valuation, along with steady 20bp EBIT margin expansion through the time frame. These assumptions aren't far-fetched, given the industry's structural prospects.

As highlighted in our sector analysis, in the staffing business, growth would hinge on

- Volume growth, led by an increase in penetration of the temporary staffing industry in India to the global average of 1.5% (from 0.5% currently)
- Increase in India's per capita GDP, resulting in higher realization per temporary employee
- Shift of the market away from the unorganized segment, which currently comprises of ~70% of the total industry

An analysis of these variables threw up the likelihood of 22.9% CAGR in the organized staffing market over the next five years, and 16.3% CAGR post that. Our assumptions clearly seem within limits, given the high ceiling!

Over and above this, Quess is present in the areas of professional staffing, HR solutions and facility management – all of which have been exhibiting higher growth compared to general staffing. This heightens the probability of achievement of both revenue and margin assumptions, especially given that the other businesses command better profitability compared to general staffing.

Moreover, given the aggression shown by Quess so far in inorganic growth, the probability of overall financial performance being towards the higher end is greater.

Bear case analysis indicates 30% downside from current levels

Our bear case assumes 5pp lower growth than we have assumed in our DCF valuation, along with no EBIT margin change along the time frame.

Key assumptions to our growth estimates are structural in nature. However, certain risks that would push growth lower would be:

- Economic downturn, leading to lower growth across all segments that Quess is present in
- Slower than anticipated increase in penetration of temporary staffing in India
- GST implementation not resulting in a shift of the temporary staffing market from unorganized players to organized
- Slowdown in IT hiring impacting Magna Infotech and elevated pain in the Power and Metals verticals, leading to slower growth in IAM
- Failure of one or more acquisitions, negatively impacting financial performance
- Quess losing one of its top customers

Any of these risks playing out would result in a sharp deterioration in performance of the impacted business. However, given the company's diversification, we see low risk of overall financial performance going downhill. Hence, we have made lower growth assumptions for our base case rather than taking steep cuts periodically.

SWOT Analysis

Strengths

- **Customer relationships:** Quess has been able to penetrate deeper into clients because of its wide array of service offerings. This has led to higher revenue per customer compared to peers. Moreover, given the higher profitability in services excluding general staffing, Quess demonstrates higher blended profitability versus competition.
- **Execution:** The company has successfully demonstrated its ability to integrate and grow companies after acquiring them. Avon's 52% revenue CAGR and Magna's 18% CAGR are classic examples. It has also been able to turn profitability around in Brainhunter and MFX, further showing execution prowess.
- **Identifying opportunities**: Opportunities in the business services industry are endless. Quess has historically been able to identify these areas, make a presence in them and manage to scale them up to become one of the leaders. This gives it the ability to demonstrate growth as a multiplier to the GDP growth.

Weaknesses

- **Weak cash flow:** Quess' cash flow generation has been weak, resulting out of the acquisition-fuelled growth. Even at an operating level, as it enters businesses with higher receivable days, it has been seeing a deterioration of working capital, resulting in low operating cash flow.

Opportunities

- **Staffing:** On account of the under-penetration of temporary staffing in India (0.5% in general staffing v/s 1.6% globally; and 10% in IT services v/s 20% globally), there lies tremendous opportunity for volume growth. Moreover, wage inflation and improved business mix would result in further growth. Together, this creates an opportunity for sustained 20%+ growth in these areas. Furthermore, key triggers like GST implementation and the move of the industry from unorganized to organized can further boost growth in the coming years.
- **Other business services:** While Quess has expanded into several business services, there are multiple other dimensions of growth in the form of [1] additional services, [2] geographies, and [3] verticals. This has the potential of resulting in sustained high-double-digit growth for Quess.
- **Other geographies:** On increasing maturity of developed countries, global peers started spreading their wings into emerging markets. Though India is still far from that point, other countries in the Middle East, Africa and Asia are witnessing similar trends in this business.

Threats

- **Acquisition-related risks:** Quess has completed multiple acquisitions in areas that it has historically no experience in managing. Failure of integration and management poses a significant threat, as inorganic growth remains the focus.
- **Loss of key clients:** Key customers have accounted for a significant proportion of Quess' revenue. Its top-10 clients contribute to 30% of total revenue. Loss of a major client would result in stress on financials. Magna Infotech recently saw a decline in revenue because of a project completion.
- **Correlation with economic cycles:** The staffing business (both general and professional) has high dependency on economic cycles. Although India is an under-penetrated market, and there are structural opportunities for growth, any significant downturn in economic activity could result in a severe impact on financial performance as it contributes to 80% of Quess' revenue.

Company description

Quess Corp is a leading integrated business services provider established in 2007. It has a pan-India presence, with 65 offices across 34 cities. It also has operations in North America, the Middle East and South East Asia. In all, it operates in nine countries – the US, Canada, Sri Lanka, UAE, India, Malaysia, Philippines and Singapore.

Quess is a step down subsidiary of Fairfax Financial Holdings Group (FFH CN), held through its Indian listed subsidiary, Thomas Cook India Limited (TC IN). It has annualized revenue of INR41.04b as of 3QFY17.

It serves over 1,300 customers globally. Its business is broadly divided into four key segments:

- **Global Technology Solutions**
  Through Magna, Quess is India's largest IT staffing provider, with ~9,000 associates.
- **People & Services**
  Quess is India's third-largest general staffing player, with ~100,000 associates across 5,000 locations.
- Integrated **Facility Management**
  Through Avon, Quess is a leading facility management provider, with more than 17,000 associates. Its services include soft services, electro-mechanical maintenance, specialized services, and pest control.
- **Industrials**
  Hofincons, a 39 year old brand with 3,200 personnel on the rolls, is a recognized service provider in power, energy, oil & gas refining, chemicals, ferrous & non-ferrous industry segments. Quess acquired Hofincons in June 2014.

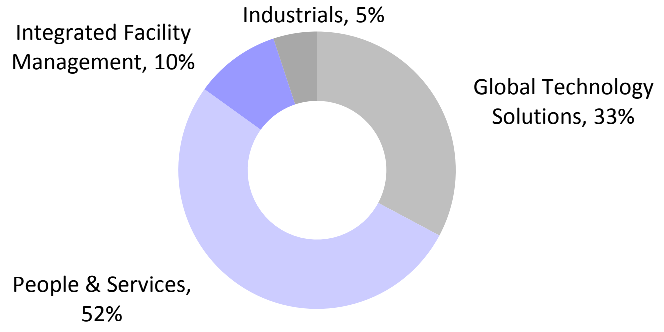
Quess has been actively acquiring business over the last eight years, and has a successful track record of integrating and running these businesses. It has acquired 11 businesses over the last eight years.

Through both organic and inorganic means, Quess has grown at a 66% CAGR over the last five years. Over the same period, on account of its entry into higher-value-add businesses, its PAT has growth at a CAGR of 120%.

A success for Fairfax!

- Fairfax Financial Holdings Group invested USD172.7m in Thomas Cook, purchasing shares from Thomas Cook UK and others.
- Thomas Cook acquired Quess Corp in May 2013 for USD47m, making Fairfax's holding in Quess 77%, thereby valuing the company at USD60m.
- Three years later, in 2016, Quess raised USD60m by selling 10% in the IPO, valuing the company at USD600m. ***(10x in three years)***
- The company is now trading at a valuation of USD1.4b! ***(23x in four years)***

Exhibit 84: Revenue split between the four segments



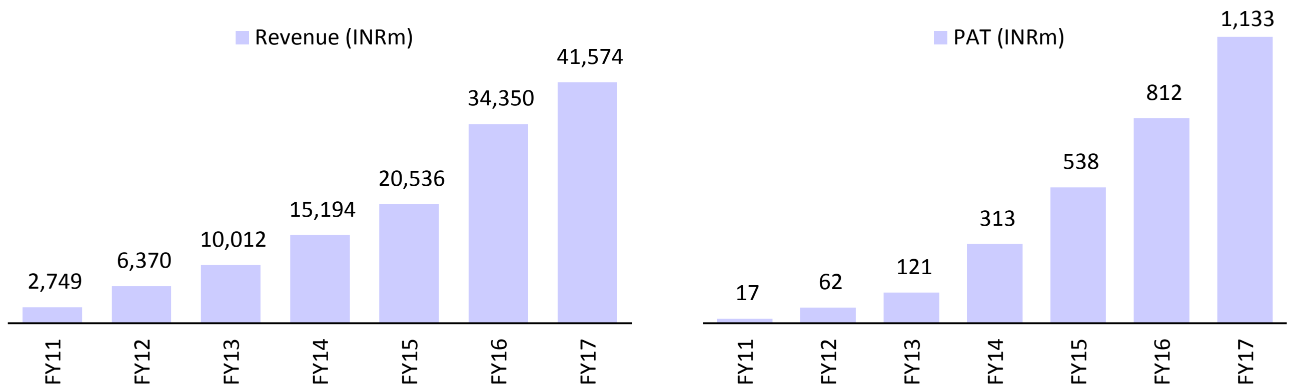
Source: Company, MOSL

Exhibit 85: Several acquisitions across business segments

Global Technology Solutions	People & Services	Integrated Facility Management	Industrial Asset Management
MFX	IKYA	Avon	Hofincons
Brainhunter	Coachieve	Aravon	Maxeed
Magna Infotech	excelus	Terrier Security	Transfield
Mindwire	Styracorp	Manipal Integrated Services	Inticore
	Randstad Lanka		
	Comtel Solutions		

Source: Company, MOSL

Exhibit 86: Revenue CAGR of 46% over the last five years; PAT CAGR of 79% over the same period



Numbers for FY14 and FY15 have been normalized to 12 month periods; Source: Company, MOSL

Key management personnel

Mr Ajit Isaac, Chairman & Managing Director and CEO

Mr Isaac is responsible for the company's daily operations and strategic decisions. He has 25 years of experience in Human Resources and Corporate Management. Prior to joining Quess, he was the Country Manager, India and Middle East for Adecco Peopleone India Limited.

Mr Subrata Nag, Executive & Wholetime Director and CFO

Mr Nag is responsible for the overall Finance and Accounts functions of Quess Corp. He has 27 years of experience in Finance. Prior to joining Quess, he was the Vice President – Finance and Company Secretary of Ilantus Technologies Private Limited.

Mr Amitabh Jaipuria, President and CEO – Global Services

Mr Jaipuria has over 27 years of corporate experience with organizations such as Reliance Jio Infocomm, AGS Transact, Monsanto India, Pepsico India and GE Lighting. Prior to joining Quess, he was President and Head of Mobility Business at Reliance Jio Infocomm for over two years. Prior to that, he was the CEO of AGS Transact Technologies (2013-14), and the MD of Monsanto India (2007-13).

Mr Satyakam Basu, President and CEO – Industrials

Mr Basu is the CEO & President – Industrials, heading Hofincons and Maxeed businesses. He is also charged with the responsibility of leading the Industrials Business globally. He has 36 years of varied experience in the Engineering industry. He has previously worked with Arcelor Mittal, Tata Steel and Essar Steel, with deep expertise in Production, Marketing, Industrial Business, and Mergers & Acquisitions.

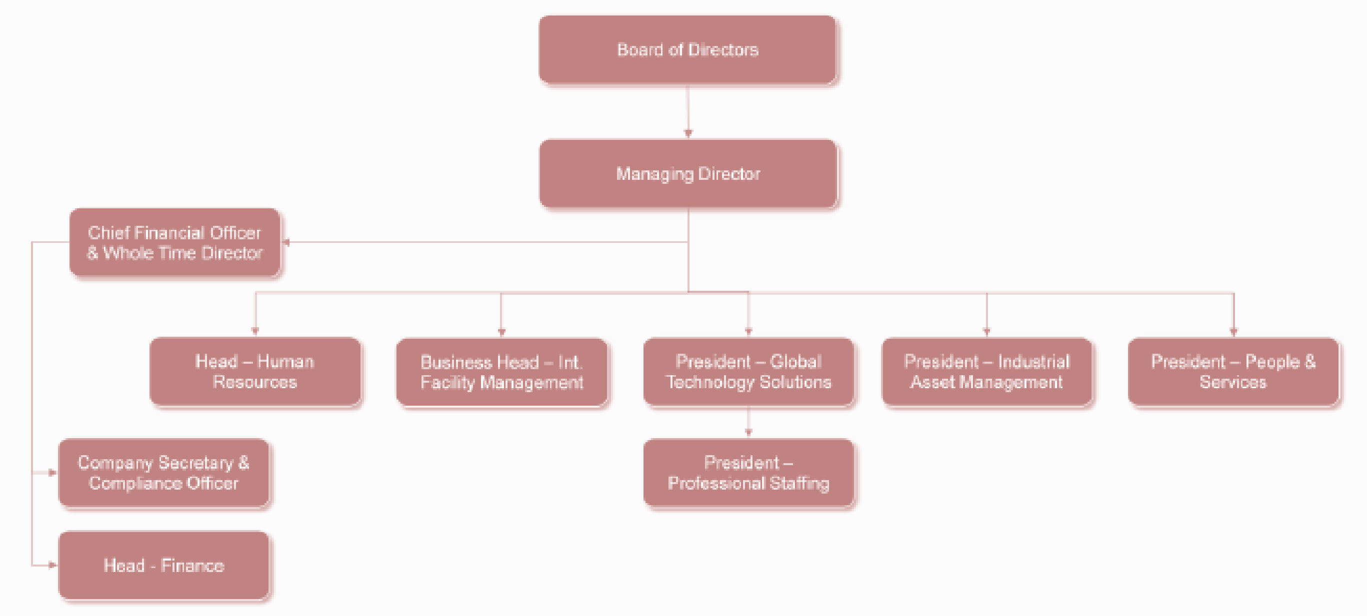
Mr Guruprasad Srinivasan, President – Special Projects and Logistics

Mr Srinivasan is President – Special Projects and Logistics and has been associated with Quess since 2007. He has over 18 years of experience in Healthcare and Services. He heads the People and Services business at Quess. Prior to joining Quess, he worked with Adecco Flexione Workforce Solutions Limited as GM – Payroll & Services.

Mr Vikram Gulati, President – Global Technology Solutions

Mr Gulati is President – Global Technology Solutions and has been associated with Quess since 2014. Prior to this, he was the CEO and Co-Founder of Happiest Minds, prior to which he was the CEO for Intelligroup and has had multiple roles at Wipro. He has over 25 years of experience in the IT services industry.

Exhibit 87: Organization structure (to be revised)



Source: Company

Exhibit 88: Board of Directors

Name	Designation	Comments
Ajit Isaac	Chairman and MD and CEO	■ 25 years of experience ■ Was the Country Manager, India and Middle East for Adecco Peopleone ■ Director since April 2009
Subrata Kumar Nag	Executive and Whole time Director and CFO	■ 27 years of experience ■ Was the VP – Finance and Company Secretary of Ilantus Technologies ■ Director since July 2013
Madhavan Karunakaran Menon	Non-Executive, Nominee Director	■ 34 years of experience ■ Is the Chairman and MD of Thomas Cook India ■ Director since May 2013
Chandran Ratnaswami	Non-Executive, Nominee Director	■ 23 years of experience ■ Is a Nominee Director at Thomas Cook India ■ Director since January 2016
Pravir Kumar Vohra	Non-Executive, Independent Director	■ 38 years of experience ■ Was the Group Chief Technical Officer at ICICI Bank, and has held various positions with SBI ■ Director since July 2015
Revathy Ashok	Non-Executive, Independent Director	■ 30 years of experience ■ Was the Director – Finance and Administration of TSI Ventures and the CFO of Syntel ■ Director since July 2015
Pratip Chaudhuri	Non-Executive, Independent Director	■ 40 years of experience ■ Was the Chairman of SBI ■ Director since July 2015
Sanjay Anandaram	Non-Executive, Independent Director	■ 25 years of experience ■ Director since December 2015

Source: Company

Key risks

Acquisition-related risks: Quess has completed multiple acquisitions in areas that it has historically had no experience in managing. Failure of integration and management poses a significant threat, as inorganic growth remains the focus.

Loss of key clients: Key customers have accounted for a significant proportion of Quess' revenue. Its top-10 clients contribute 30% of total revenue. Loss of a major client could result in stress on financials. Magna Infotech recently saw a decline in revenue because of a project completion.

Correlation with economic cycles: The staffing business (both general and professional) has high dependency on economic cycles. Though India is an underpenetrated market, and there are structural growth opportunities, a downturn in economic activity could impact financial performance as Quess gets 80% of its revenue from this geography.

Financials and valuations

Consolidated - Income Statement (INR Million)

Y/E March	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Total Income from Operations	**6,370**	**10,012**	**10,060**	**25,671**	**34,350**	**41,574**	**60,118**	**72,142**	**86,571**
Change (%)	131.7	57.2	0.5	155.2	33.8	21.0	44.6	20.0	20.0
Total Expenditure	**6,101**	**9,581**	**9,662**	**24,366**	**32,839**	**39,346**	**56,608**	**67,659**	**80,865**
% of Sales	95.8	95.7	96.0	94.9	95.6	94.6	94.2	93.8	93.4
EBITDA	**269**	**431**	**398**	**1,305**	**1,511**	**2,228**	**3,510**	**4,483**	**5,706**
Margin (%)	4.2	4.3	4.0	5.1	4.4	5.4	5.8	6.2	6.6
Depreciation	37	44	42	101	144	264	361	433	519
EBIT	**233**	**387**	**356**	**1,203**	**1,367**	**1,964**	**3,149**	**4,050**	**5,186**
Int. and Finance Charges	126	176	88	218	310	465	392	347	304
Other Income	24	32	21	57	91	153	220	324	512
PBT bef. EO Exp.	**131**	**243**	**289**	**1,042**	**1,147**	**1,651**	**2,978**	**4,027**	**5,395**
PBT after EO Exp.	**131**	**243**	**289**	**1,042**	**1,147**	**1,651**	**2,978**	**4,027**	**5,395**
Total Tax	48	72	97	370	335	518	816	878	955
Tax Rate (%)	36.5	29.6	33.7	35.5	29.2	31.4	27.4	21.8	17.7
Minority Interest	21	50	13	0	0	0	0	0	0
Reported PAT	**62**	**121**	**179**	**672**	**812**	**1,133**	**2,162**	**3,149**	**4,440**
Adjusted PAT	**62**	**121**	**179**	**672**	**812**	**1,133**	**2,162**	**3,149**	**4,440**
Change (%)	258.4	94.1	48.0	276.3	20.8	39.6	90.8	45.7	41.0
Margin (%)	1.0	1.2	1.8	2.6	2.4	2.7	3.6	4.4	5.1

Consolidated - Balance Sheet (INR Million)

Y/E March	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Equity Share Capital	300	300	962	258	1,133	1,268	1,377	1,377	1,377
Total Reserves	231	383	884	2,267	2,433	7,094	17,995	21,144	25,584
Net Worth	**531**	**682**	**1,846**	**2,525**	**3,566**	**8,362**	**19,372**	**22,521**	**26,961**
Minority Interest	114	164	0	0	0	9	9	9	9
Total Loans	556	879	641	2,170	3,783	7,304	6,530	5,783	5,061
Deferred Tax Liabilities	-76	-66	-50	-35	-1,345	-1,658	-1,658	-1,658	-1,658
Capital Employed	**1,126**	**1,660**	**2,437**	**4,660**	**6,005**	**14,017**	**24,253**	**26,655**	**30,373**
Gross Block	191	244	319	604	1,043	1,363	1,913	2,463	3,013
Less: Accum. Deprn.	117	159	201	415	541	779	1,140	1,573	2,092
Net Fixed Assets	**74**	**85**	**118**	**189**	**502**	**583**	**773**	**890**	**920**
Goodwill on Consolidation	250	250	729	1,104	2,020	3,788	3,788	3,788	3,788
Capital WIP	0	0	4	0	24	77	97	117	137
Total Investments	**0**	**0**	**0**	**0**	**37**	**2,976**	**2,976**	**2,976**	**2,976**
Curr. Assets, Loans&Adv.	**2,143**	**2,909**	**3,080**	**5,869**	**8,573**	**13,721**	**25,007**	**28,950**	**34,630**
Inventory	1	4	4	4	18	57	57	57	57
Account Receivables	1,177	1,580	1,246	2,755	6,926	8,337	12,227	14,672	17,606
Cash and Bank Balance	291	234	291	818	1,094	3,013	9,408	10,256	12,222
Loans and Advances	673	1,091	1,539	2,292	536	2,314	3,316	3,965	4,744
Curr. Liability & Prov.	**1,341**	**1,583**	**1,496**	**2,502**	**5,151**	**7,128**	**8,388**	**10,066**	**12,079**
Account Payables	43	57	48	414	674	631	913	1,096	1,315
Other Current Liabilities	1,279	1,491	1,413	1,941	4,138	6,044	6,820	8,184	9,821
Provisions	19	36	35	147	339	453	655	786	943
Net Current Assets	**802**	**1,325**	**1,585**	**3,367**	**3,423**	**6,593**	**16,619**	**18,884**	**22,551**
Appl. of Funds	**1,126**	**1,660**	**2,437**	**4,660**	**6,005**	**14,017**	**24,253**	**26,655**	**30,373**

E: MOSL Estimates

Financials and valuations

Ratios									
Y/E March	**FY12**	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18E**	**FY19E**	**FY20E**
Basic (INR)									
EPS	**0.5**	**1.1**	**1.6**	**5.9**	**7.2**	**10.0**	**19.1**	**27.8**	**39.2**
Cash EPS	0.9	1.5	1.9	6.8	8.4	12.3	22.3	31.6	43.8
BV/Share	4.7	6.0	16.3	22.3	31.5	73.8	170.9	198.7	237.9
Valuation (x)									
P/E					140.0	115.9	83.0	43.5	29.9
Cash P/E					121.6	98.4	67.3	37.3	26.3
P/BV					37.3	26.4	11.3	4.9	4.2
EV/Sales					3.7	2.8	2.4	1.5	1.2
EV/EBITDA					73.1	64.1	44.2	26.0	20.0
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
FCF per share	0.0	-1.8	0.5	-1.1	-6.4	3.3	-9.4	20.0	30.9
Return Ratios (%)									
RoE	12.5	19.9	14.1	30.8	26.7	19.0	15.6	15.0	17.9
RoCE	17.0	22.3	12.4	22.6	17.1	12.6	11.8	12.6	15.5
RoIC	20.1	24.1	13.2	25.9	22.3	21.1	23.2	25.3	30.1
Working Capital Ratios									
Asset Turnover (x)	5.7	6.0	4.1	5.5	5.7	3.0	2.5	2.7	2.9
Debtor (Days)	67	58	45	39	74	73	74	74	74
Creditor (Days)	2	2	2	6	7	6	6	6	6
Leverage Ratio (x)									
Net Debt/Equity	0.5	0.9	0.2	0.5	0.7	0.2	-0.3	-0.3	-0.4

Cash Flow Statement									(INR Million)
Y/E March	**FY12**	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18E**	**FY19E**	**FY20E**
OP/(Loss) before Tax	129	234	288	1,049	1,147	1,652	2,978	4,027	5,395
Depreciation	37	44	42	101	144	264	361	433	519
Interest & Finance Charges	126	176	88	218	310	465	392	347	304
Direct Taxes Paid	-93	-200	-249	-412	-482	-802	-816	-878	-955
(Inc)/Dec in WC	-163	-454	-52	-942	-1,622	-759	-3,632	-1,417	-1,700
CF from Operations	**36**	**-199**	**118**	**15**	**-503**	**821**	**-717**	**2,512**	**3,562**
Others	13	38	35	9	8	-66	220	324	512
CF from Operating incl EO	**49**	**-161**	**153**	**24**	**-495**	**756**	**-497**	**2,836**	**4,075**
(Inc)/Dec in FA	-54	-44	-92	-145	-226	-379	-570	-570	-570
Free Cash Flow	**-6**	**-205**	**61**	**-120**	**-721**	**376**	**-1,067**	**2,266**	**3,505**
(Pur)/Sale of Investments	0	0	-657	-525	0	0	0	0	0
Others	11	0	15	375	129	-5,457	0	0	0
CF from Investments	**-43**	**-44**	**-734**	**-295**	**-97**	**-5,836**	**-570**	**-570**	**-570**
Issue of Shares	0	0	965	0	34	3,704	8,848	0	0
Inc/(Dec) in Debt	193	323	-237	1,015	1,137	3,726	-774	-747	-722
Interest Paid	-126	-174	-90	-217	-304	-430	-392	-347	-304
Dividend Paid	0	0	0	0	0	0	0	0	0
Others	0	0	0	0	0	0	-220	-324	-512
CF from Fin. Activity	67	148	638	798	867	7,000	7,462	-1,418	-1,538
Inc/Dec of Cash	**73**	**-57**	**58**	**527**	**275**	**1,920**	**6,395**	**848**	**1,967**
Opening Balance	217	290	233	291	818	1,093	3,013	9,408	10,256
Closing Balance	**290**	**233**	**291**	**818**	**1,093**	**3,013**	**9,408**	**10,256**	**12,223**

TeamLease Services

BSE SENSEX	S&P CNX
30,465	9,428

CMP: INR1,635 TP: INR 1,990 (+22%) Buy

A straight-forward GDP multiplier…

…Propelled by scale and reforms

- **TeamLease is India's largest general staffing company, with more than 130k associates across the country. It has seen 30% revenue CAGR over the last five years. From a negative 6.4% in FY11, EBITDA margin expanded to a positive 1.5% in FY17.**
- **With an industry-leading market share, it is a structural play on the increasing penetration of temporary staffing in India and formalization of employment.**
- **Despite it having gained scale, we forecast revenue CAGR of 25% over the next two years, as the industry has barely scratched the surface in terms of potential. We expect the organized staffing market to expand 3x in five years, and 6x in 10 years.**
- **We value TeamLease on a DCF basis at INR1,990 per share (22% upside), implying a forward P/E of 54x (FY18E) and 36x (FY19E).**

Market leadership in staffing industry

- TeamLease is a market leader in the highly fragmented temporary staffing industry, with a 6% market share.
- Its extensive geographic reach, presence in multiple industries and functions, scale, ability to fill positions, and sourcing capabilities reflect in its operational prowess, which is a key determinant of success in this industry.
- It has been able to rapidly scale up its apprentice skilling initiative – NETAP (National Employability through Apprenticeship Program), and has now acquired capabilities in IT staffing by acquiring ASAP Info Systems.

Staffing industry on a structural growth path

- Temporary staffing across the globe has gained prominence in the last few years, as companies seek flexibility and better cost management. This segment constitutes 2-4% of the total workforce for developed countries, and averages at 1.6% for the world. However, this constitutes 0.5% of the workforce in India. A convergence to the global average itself can triple the industry.
- The growth story improves for organized players, as they constitute ~30% of the overall market. We expect these to gain a larger share of the market post GST implementation, which would force unorganized players to pay service tax, erasing the ~15% benefit they enjoy due to non-compliance.
- The market would also see wage-inflation-led growth, resulting in higher revenue for the industry, as commissions are a mark-up on the salary paid to associate employees.
- We expect a convergence of these factors to result in sustained 20%+ growth for the organized staffing industry.

Financial performance to remain strong, going forward…

- We expect the high-double digit growth CAGR that TeamLease has witnessed over the last five years to continue. Our assumptions bake in 16% CAGR in associate employees, and 8% CAGR in average realization per associate. Growth is also likely to be supported by the IT staffing business gaining scale.

Stock Info

~~Bloomberg~~	~~TCOM IN~~
~~Equity Shares (m)~~	~~285.0~~
~~52-Week Range (INR)~~	~~784 /427~~
~~1, 6, 12 Rel. Per (%)~~	~~-9/-6/32~~
~~M.Cap. (INR b)~~	~~192.6~~
~~M.Cap. (USD b)~~	~~2.9~~
~~Avg Val, INRm~~	~~530~~
~~Free float (%)~~	~~25.0~~

~~Financials Snapshot (INR b)~~

~~Y/E MARCH~~	~~FY17~~	~~FY18E~~	~~FY19E~~
~~Sales~~	~~176.2~~	~~178.8~~	~~190.9~~
~~EBITDA~~	~~24.1~~	~~28.6~~	~~36.2~~
~~NP~~	~~7.4~~	~~5.2~~	~~10.3~~
~~EPS (INR)~~	~~26.0~~	~~18.1~~	~~36.0~~
~~EPS Gr.(%)~~	~~1,573.9~~	~~-30.3~~	~~98.7~~
~~BV/Sh (INR)~~	~~55.9~~	~~74.0~~	~~110.0~~
~~P/E (x)~~	~~26.0~~	~~37.3~~	~~18.8~~
~~P/BV (x)~~	~~12.1~~	~~9.1~~	~~6.1~~
~~RoE (%)~~	~~126.2~~	~~27.9~~	~~39.1~~
~~RoCE (%)~~	~~9.7~~	~~6.0~~	~~9.9~~

~~Shareholding pattern (%)~~

~~As On~~	~~Mar-17~~	~~Dec-16~~	~~Mar-16~~
~~Promoter~~	~~75.0~~	~~75.0~~	~~75.0~~
~~DII~~	~~8.0~~	~~9.1~~	~~14.7~~
~~FII~~	~~11.4~~	~~11.1~~	~~3.3~~
~~Others~~	~~5.6~~	~~4.9~~	~~7.0~~

~~FII Includes depository receipts~~

Stock Performance (1-year)

- We expect profitability improvement, led by [1] operational leverage because of an improvement in the Associate/Core Employee ratio, and [2] higher proportion of revenue from IT staffing, training and other HR solutions, which command better margins. We are baking in cumulative margin expansion of 40bp over the next three years.
- This would result in 25% revenue CAGR, 35% EBITDA CAGR, and 26% PAT CAGR over FY17-20.

…resulting in improvement in multiple other metrics

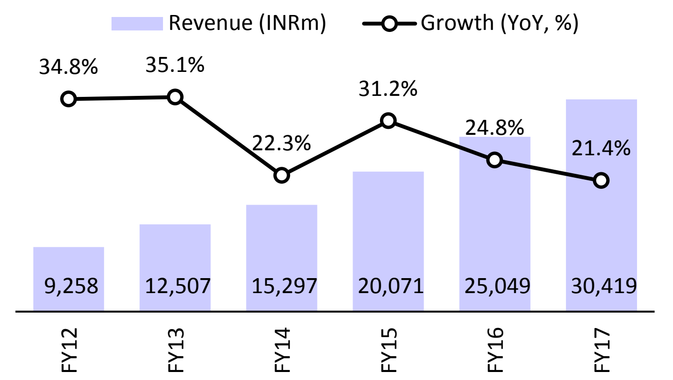
- The staffing business is asset-light, which leads to strong cash generation, return ratios and asset turnover, once it gains scale.
- Profitability keeps improving, as scale and technology lead to a higher Associate/Core Employee ratio. TeamLease has seen its Associate/Core Employee ratio improving from 149 in FY11 to 203 in FY17 – there's still tremendous room for improvement.
- We see continued improvement in profitability, leading to a RoIC of 34.4% in FY20 (up from 32.9% in FY17). Asset turnover should increase to 9.0x by FY20 (from 8.3x in FY17).
- These ratios will only get better with time, as the company continues gaining scale at a velocity that is disproportionately higher than the investments required in the business, either in the form of capital expenditure or in the form of employees to run the business.

Valuation and view: Scale will be the key driver of value creation

- We value TeamLease using DCF to reach a price target of INR1,990, implying an upside of 22%.
- We see TeamLease as a key beneficiary to industry trends, and expect it to demonstrate a high-growth trajectory over the next three years. Consequently, prospective improvement in return ratios and cash generation, led by the business model, would be a key driver of value creation for TeamLease.
- **Key risks:** [1] Economic downturn leading to a proportionate and direct impact on business, [2] Loss of business or issues with a top client (top-5 contribute 14% of revenue; top-10 contribute 20% of revenue), [3] Inability to have a higher proportion of revenue from other HR services and professional staffing, leading to lower realizations and profitability.

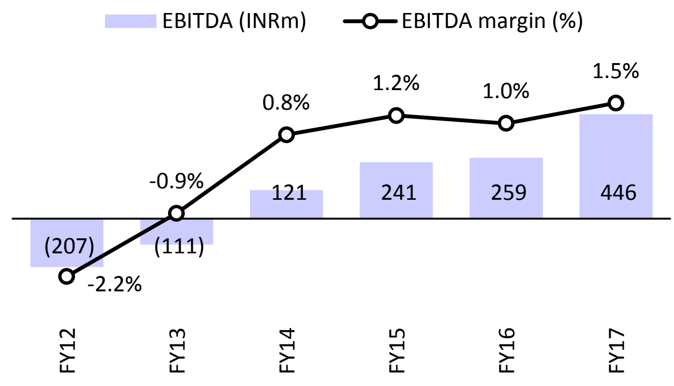
Story in charts

Exhibit 89: Revenue CAGR of 27% over the last five years



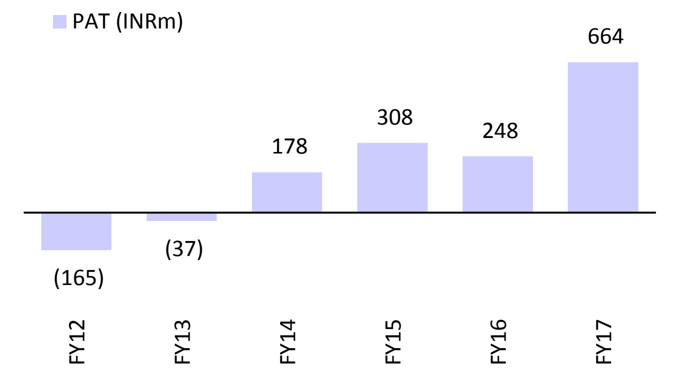
Source: MOSL, Company

Exhibit 90: Profitability has turned from negative to positive



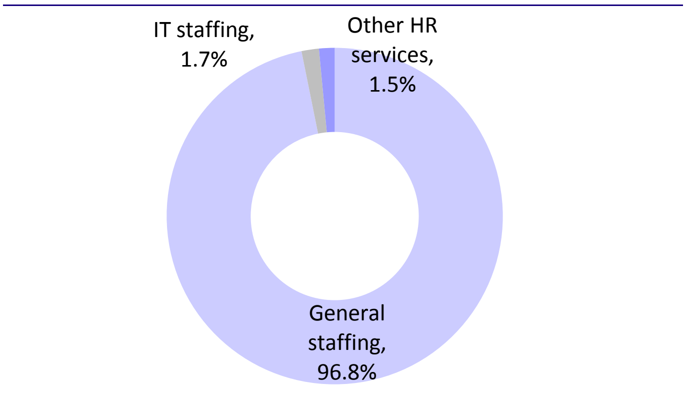
Source: MOSL, Company

Exhibit 91: Consequently, PAT too has turned 360 degrees



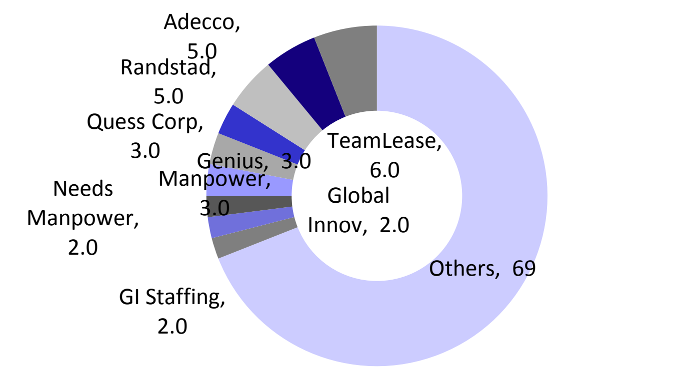
Source: MOSL, Company

Exhibit 92: Portfolio for TeamLease is dominated by staffing (96.8% of revenue)…



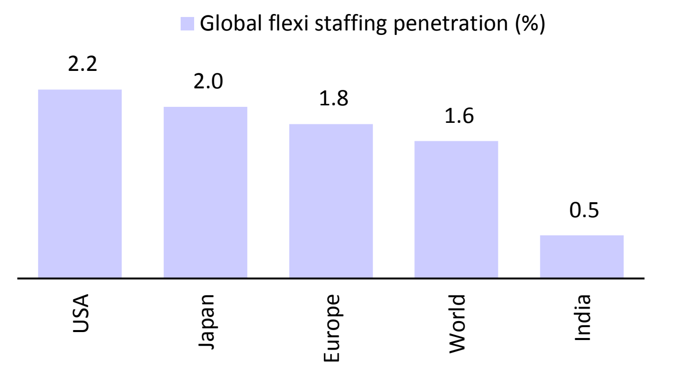
Source: Company

Exhibit 93: …where it has the highest market share



Source: CRISIL Research

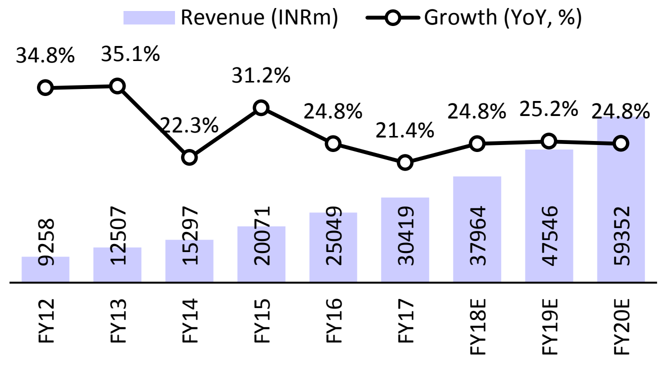
Exhibit 94: India's staffing market still nascent



Source: CIETT economic report 2016

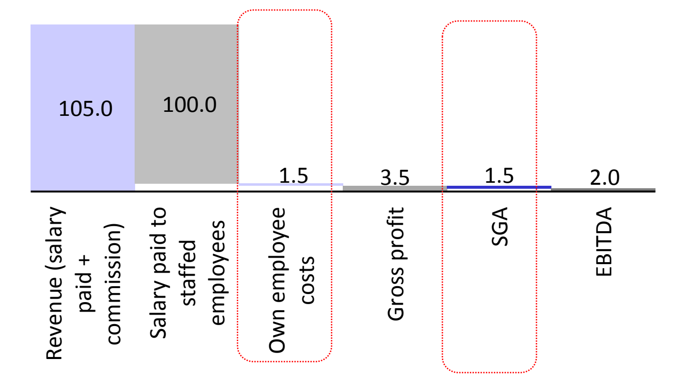
Story in charts

Exhibit 95: This will keep growth momentum intact



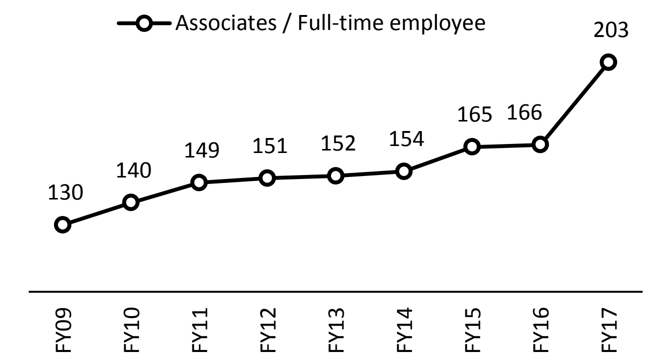
Source: MOSL, Company

Exhibit 96: Scale will bring operational leverage



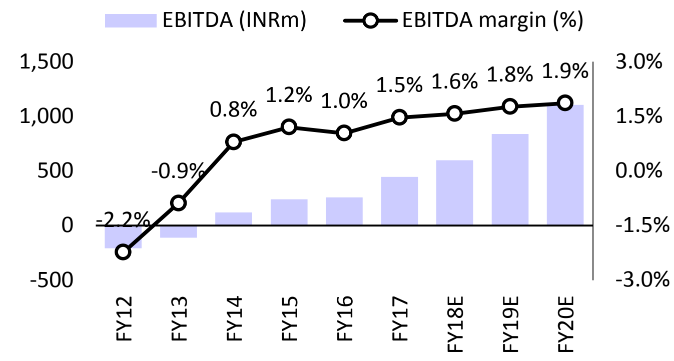
Source: MOSL

Exhibit 97: TeamLease has already demonstrated steady improvement in operational efficiency



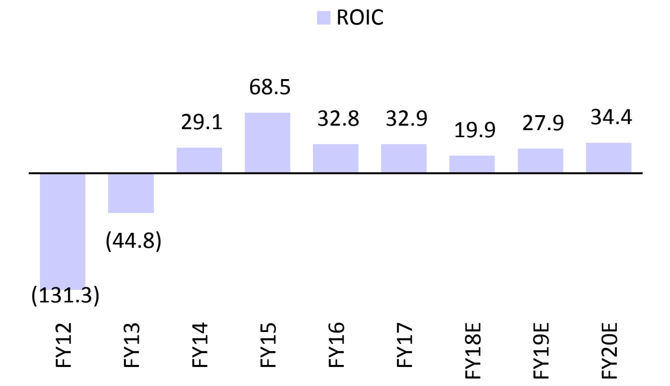
Source: Company

Exhibit 98: This will continue driving margin expansion…



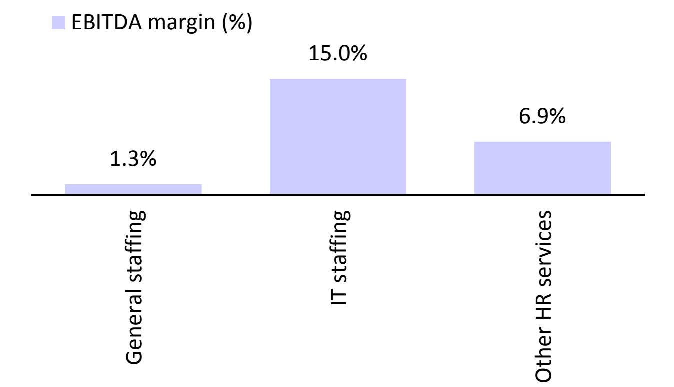
Source: MOSL, Company

Exhibit 99: …which will also improve return ratios



Source: MOSL, Company

Exhibit 100: Margins are also higher for other businesses it is now entering



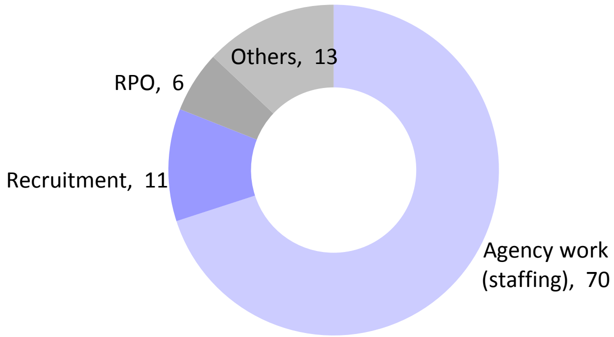
Source: Company

Leadership in staffing business...

...to drive growth, going forward

TeamLease is a pure-play HR service player, with a leadership in the staffing business. The global workforce solutions ecosystem has staffing (70% of revenue) at its heart, and supports businesses in multiple other ways including, recruitment, payroll/compliance, contracting/consulting, talent acquisition technology, process outsourcing, and other workforce solutions.

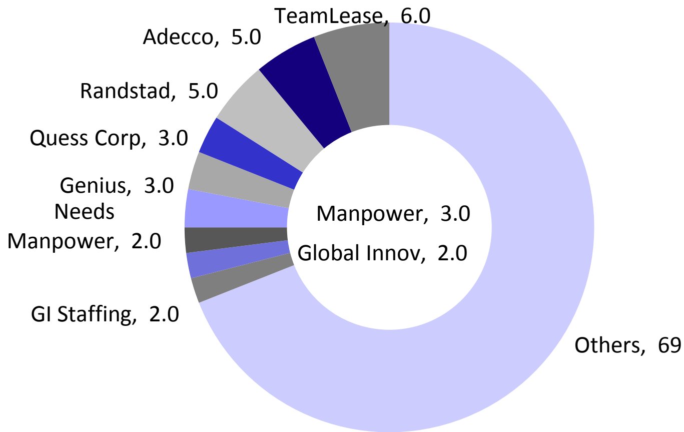
Exhibit 101: Composition of the global HR solutions market (by revenue, %)



Source: CIETT economic report 2016

TeamLease has a clear lead in the staffing market, with a 5-6% market share. It has ~130,000 associates deployed over 1,900+ customers across sectors.

Exhibit 102: TeamLease has 5-6% market share in the staffing business



Source: CRISIL Research

TeamLease's 27% revenue CAGR over the last five years has been primarily dominated by its core staffing business. Investments in people, optimization of processes and investments in technology have led to a gain of scale and efficiency.

TeamLease's core business is providing staffing solutions across industry sectors and diverse functional areas. The majority of its associate employees are engaged in sales, logistics and customer service functions.

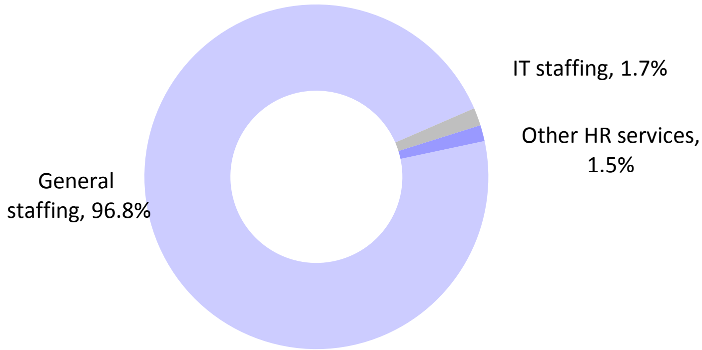
The key factors that put TeamLease in a position to capture the market opportunity successfully are:

[1] A focused player

Globally, staffing agencies have spread their wings across the HR solutions value chain, and haven't restricted themselves to staffing. Some companies like Quess Corp are diversified business services companies, with presence in areas like facilities management and industrial asset maintenance, along with staffing.

TeamLease sees ample opportunity in staffing (general and specialist) and intends to stick to this market. It already has presence in the HR value chain (apart from staffing) through recruitment services, regulatory compliance services, retail learning solutions, institutional learning solutions, apprenticeship programs, skill development, and payroll processing.

Exhibit 103: Most of TeamLease's revenue comes from staffing



Source: Company

[2] Variable mark-ups, an effortless growth vector

The key vectors for growth in revenue for staffing agencies are: [1] Volume – increase in the number of associates placed, and [2] Realization – commission earned per associate placed.

Volume is largely a function of growth in the industry (working population and temporary workforce) and market share changes. However, realization can be moved by a number of factors:

- Higher commissions on temporary staffing
- Wage inflation
- Mix of associates (higher proportion of skilled)

While commissions are largely stable on account of it being a fragmented industry and TeamLease having reached best-in-class scale and operation efficiency, they can either be fixed or variable. In a fixed mark-up, an absolute rupee amount is decided as commission for the agency. However, in a variable mark-up, a fixed percentage is charged on the associate's salary.

Variable mark-up results in an increase in commissions commensurate to wage inflation. This is easier to do on new contracts than having to renegotiate older ones. The company has laid its focus on getting a higher mix of variable contracts. These contracts now account for ~30% of TeamLease's total revenue.

Over time, TeamLease will continue reaping the benefits of 6-8% wage inflation on its employee base, thus having to put in less volume effort, as the base increases!

[3] Operational excellence achieved through strong back-end

The staffing business is an asset-light model, and sees disproportionate benefits when it gains scale. This is because of the diminishing incremental capital expenditure and manpower required to get those additional dollars. However, the focus of the business is more on operational excellence, as this would be a crucial factor for improving profitability and for being able to source and place associates at customer locations swiftly and optimally.

The company manages ~130,000 associates across 1,900+ clients. Given that the nature of employment is temporary, the business sees 60%+ attrition, making it a continuous and revolving process to manage an increasingly large number of people. It is thus of utmost importance to have a strong technology background to manage operational excellence.

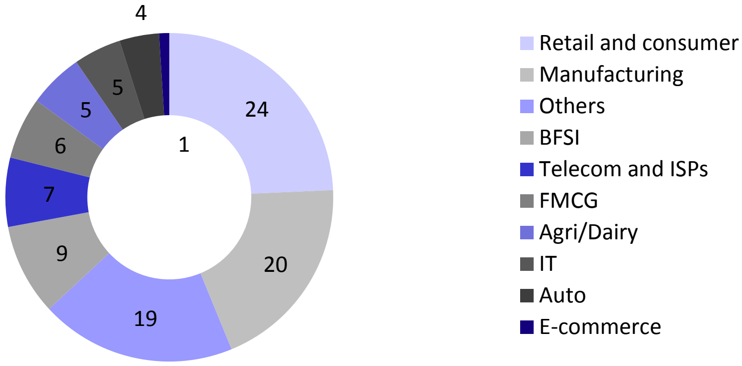
TeamLease has a team of 70+ engineers that have developed technology in-house to efficiently manage procurement, compliance and placement of its associates.

[4] Stability achieved by diversification

The staffing business, because of its direct linkage to employment, is highly correlated with economic activity. This causes the industry to move in a direction (and quantum) similar to that of overall macroeconomic factors. The perils of this were witnessed over the period 2008-10, when TeamLease had more than 50% of its revenue coming from the BFSI and Telecom verticals. This resulted in its associate count (and consequently revenue) reducing to half. Because of the wafer-thin operating margins in the business, profitability took a further hit.

TeamLease has now managed to create a buffer by diversifying its presence in various other verticals. Now, no vertical contributes to more than 20% of its overall revenue. The benefit of this was evident from the fact that TeamLease saw higher growth post demonetization. The demand for temporary staffing to meet the surge in footfalls in banks was enough to more than offset the decline in hiring demand seen in other verticals.

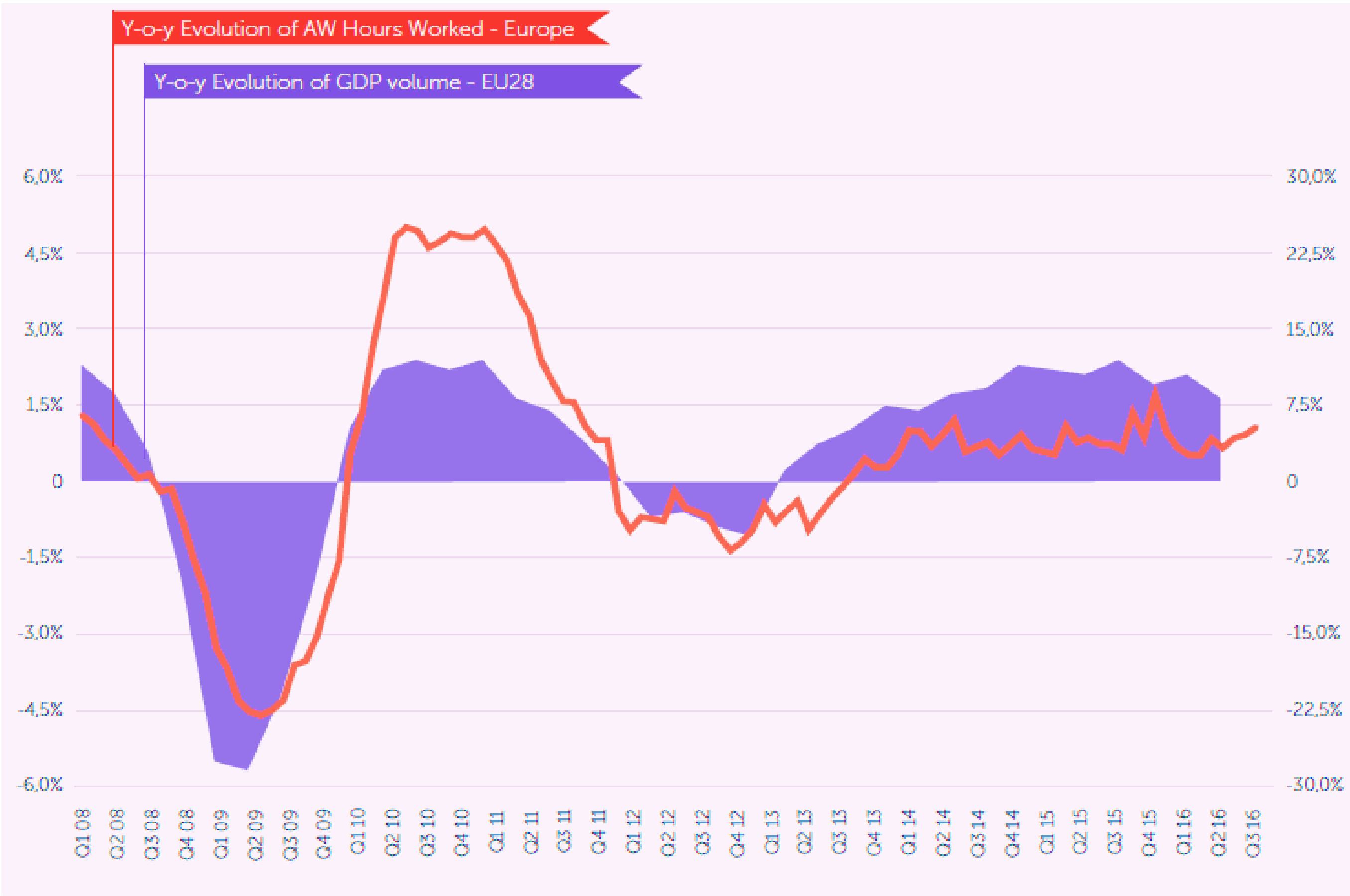
Exhibit 104: Well diversified revenue stream



Source: Company

The company has been quick to respond to market and demand changes. It has been able to leverage its operational prowess and pan-India reach to swiftly adjust to changes in terms of both vertical-specific and geographical demand.

Exhibit 105: Staffing highly dependent on economic cycles (EU in the chart)



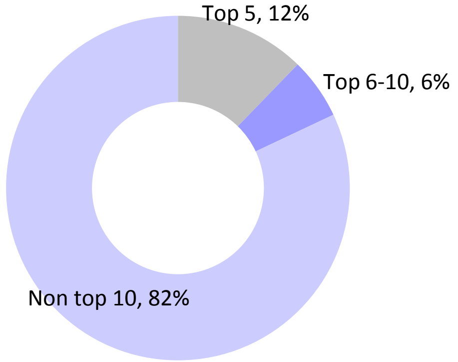
Source: CIETT economic report 2016

[5] Client mining can lead to further growth

TeamLease has a long tail, as it has more than 1,900 customers, but the top 10 contributing to 18% of total revenue. This compares with Quess having 80,000 associates spread across 200 customers.

Actively mining clients can lead to increased revenue per customer and potential for higher growth, with lower investments in sales and marketing.

Exhibit 106: 80% revenue comes from ~1,900 customers

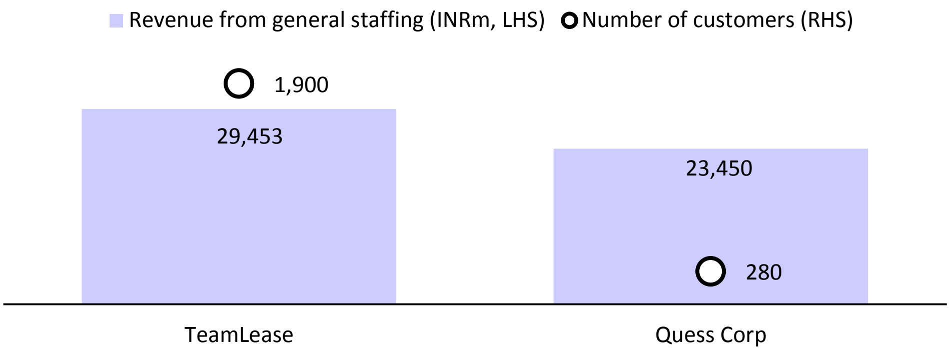


Source: Company

When the market starts to rapidly shift from the unorganized to the organized segment, TeamLease is likely to benefit to a larger extent because of its spread. It has consciously approached the market from a broad perspective, as opposed to Quess, which has focused on a smaller number of large players.

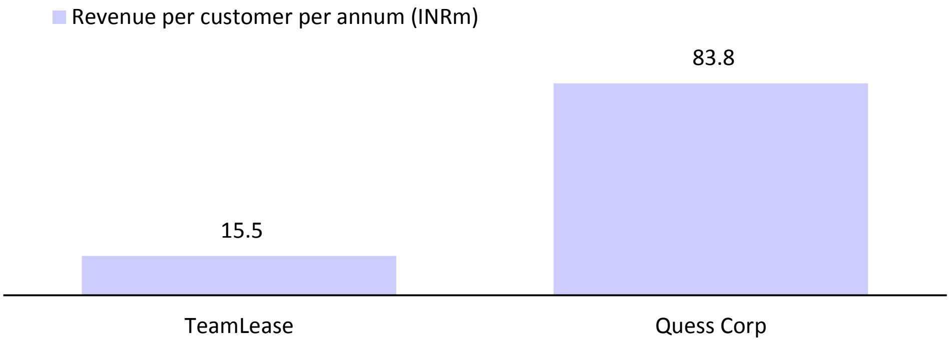
This is reflected in the fact that TeamLease made INR29.5b from 1,900 customers (INR15.5m per customer per annum) opposed to Quess, which made INR23.5b in staffing from ~280 customers (INR83.8m per customer per annum).

Exhibit 107: TeamLease has focused on broadening its presence



Source: Company

Exhibit 108: Larger customer base offers potential without much hunting effort



Source: Company

TeamLease has already been contacted, and is in discussion with 40% of its customers on resource procurement changes post GST implementation. It has also prepared its IT systems to cope with the process and operational changes that will follow suit.

At the same time, its business model has been agile enough to adapt to rapid market changes swiftly. This would enable it to cater to demand upswings from its customer base on GST rollout.

[6] Business mix improvement has a direct impact on yield

TeamLease has relatively lower exposure to high-yield sectors like Healthcare, Hospitality and Information Technology. These require specialized skill sets, and hence, command higher realization per associate. Commissions too can be higher in these verticals, leading to better blended profitability.

The company has started increasing its footprint in these areas to achieve higher profitable growth. Its recent acquisitions of ASAP Infosystems and Nichepro Technologies will only aid faster transition into these areas.

[7] Currency available for future growth

TeamLease has been less aggressive than Quess on the inorganic front. Its growth so far has been in the staffing business and organic. However, it has been open to acquisitions, especially to enter and gain scale in newer sectors.

Over the last year, IT has been a focus area – TeamLease acquired two companies. Given the multiple opportunities present in other high-yield sectors, it is likely to acquire specialized staffing agencies to expand.

Its balance sheet is healthier than peers, giving it the ability to make acquisitions without adding debt or diluting equity. Post the IPO, TeamLease has cash of INR1.6b on its books, which can be utilized to expand.

Broadening avenues

Adding specialist capabilities and broadening offerings

Agencies have spread their wings across multiple service lines, given their association with staffing, and the fact that customers would be likely to opt for these ancillary services from a third party.

Multiple service lines have helped diversify from concentrated offerings…

- The direct linkage of the staffing business to employment results in high correlation with economic activity. The perils of this were witnessed during 2008-10, when TeamLease had more than 50% of its revenue coming from the BFSI and Telecom verticals. This resulted in its associate count (and consequently revenue) reducing to half. Because of the wafer-thin operating margins in the business, profitability took a further hit.
- TeamLease has now created a buffer by diversifying to various other verticals. Now, no vertical contributes more than 20% of its overall revenue. The benefit of this was evident in TeamLease's higher growth post demonetization. The demand for temporary staffing to address the surge in footfalls in banks was enough to more than offset the decline in hiring demand seen in other verticals.
- Greater diversification can further cushion the impact of such cyclicality, thus reducing risk and also resulting in increased margin of safety.

…and also improve growth rates and profitability

- The HR solutions market in India has been growing at a CAGR of 28% for the last five years. As the share of organized employment increases, so will the velocity of growth in HR solutions.
- Similarly, the professional IT staffing market grew at a CAGR of 19% over 2009-14 to INR125b and is expected to grow at a CAGR of 22% during 2014-19.
- Profitability in the general staffing business in India has been in the range of 2-4%, making companies operate at thin margins with little safety during downturns. In other ancillary businesses, despite smaller scale, profitability is higher. Professional staffing, recruitment and HR solutions command double-digit margins, thereby improving overall profitability.

We can broadly divide the staffing market into two key areas: general and professional. While growth rates have been similar for both these categories, we see a difference in their margins and return ratios. Specialist staffing companies have been historically enjoying higher profitability than general staffing companies. This is also getting reflected in their RoEs, which are significantly superior.

This has also resulted in superior valuations for specialist staffing companies compared to general staffing companies. **On average, specialists have traded at a 25-30% premium to general staffing companies.**

ASAP acquisition gives entry into higher-margin IT staffing

ASAP was established in 1998 as an IT training business and subsequently converted into an IT staffing company in 2003. It is a tier-1 staffing provider to reputed MNCs and is ranked among the top 10 Indian IT staffing companies. Its services span across Staff Augmentation, Direct Hiring, Payroll, Transitioning, and SOW-Project Services.

ASAP operates through its offices across India, Bangalore being its corporate office. It has branches across Chennai, Hyderabad, Gurgaon, and Pune. ASAP operates all its corporate services from one centralized office in Bangalore.

Exhibit 109: ASAP has superior financials compared to the general staffing business (FY16)

No. of Employees (Core + Associates)	1,100
Revenue	**64**
YoY Revenue growth	**127%**
Mark-up %	26%
Gross margin	14
Gross margin %	**24%**
EBITDA	11
EBIDTA %	**18%**
PBT	9
PBT %	14%
PAT	5
PAT %	**11%**
Other ratios:	
RoE (%)	**51%**
Debtor days	54

Source: Company

The acquisition marks an entry for TeamLease into the higher-margin IT staffing vertical, in line with its strategy for margin expansion. The acquisition would be EBITDA and EPS-accretive from year-1, thereby improving financial performance immediately. Moreover, it is a high-growth business. While FY16 revenue growth was 127%, the business has grown at 50-70% over the last 2-3 years.

Has also acquired Nichepro

In September 2016, TeamLease also acquired Nichepro for an enterprise value of INR295m through its wholly-owned subsidiary, TeamLease Staffing Services Private Limited. The company offers IT staffing solutions to various IT product companies. It has over 150 associates and 30 core employees.

The acquisition strengthened TeamLease’s IT staffing vertical, and has been complementary to ASAP Info Systems. In FY16, Nichepro Technologies had revenue of INR260m and EBITDA of INR68m (26% EBITDA margin).

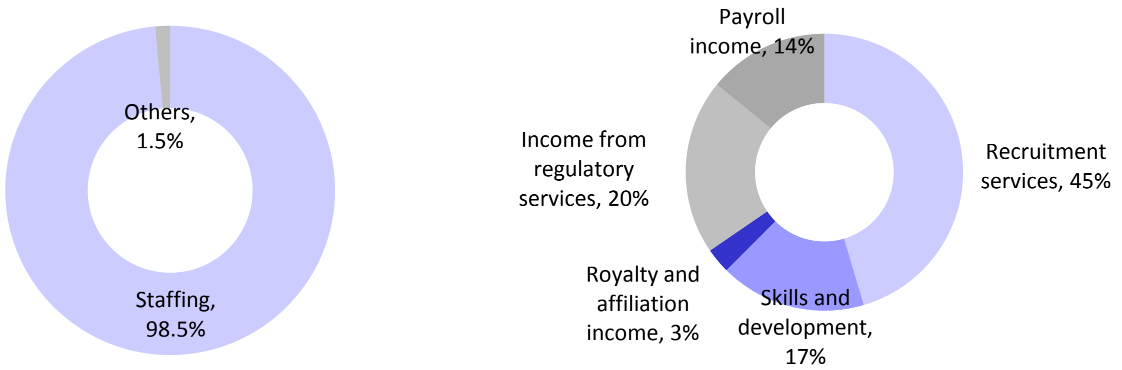
Nichepro is a tier-1 staffing provider to reputed MNCs and niche product companies. The transaction was EPS-accretive for TeamLease from the first year.

Ancillary businesses link HR value chain fully

Apart from staffing, TeamLease is present in the areas of recruitment services, regulatory compliance services, retail learning solutions, institutional learning solutions, apprenticeship programs, skills development, and payroll processing.

Staffing accounts for 98.5% of TeamLease’s gross revenue and ~70% of its net revenue. Ancillary businesses, however, help add offerings to existing customers, gain access into newer ones, and also give the company presence in areas that have high growth prospects and better margins.

Exhibit 110: Revenue split by services



Source: Company

[1] Recruitment services

TeamLease offers lateral hiring to over 500 clients across the country. Its services include RPO, search, selection and talent export, and have been on offer for the last 10 years. Repeat business tends to be high, and so does client referencing. Over the last three years, growth has been significant in this business at 22% YoY.

[2] Regulatory compliance services

As part of its daily operations, TeamLease has to deal with compliance and regulations across the country. It has capitalized this activity to address requirements in the domain of regulatory and labor law compliance of companies. The scope of services in this area includes:

Exhibit 111: Regulatory compliance services

Consulting and Advisory Services	Audit and Assesment Services	Maintenance Services	Liaison Services
• Review Labor Laws compliance Practices • Study industry specific practices • Suggest areas of risk and mitigation step. • Training on Labor law compliances and guidelines	• Review Labor Laws compliance Practices • Review of Client and vendor compliances • Audit of records (Localized/ PAN India) • Detailed Audit report on compliances applicable, risk areas and mitigation steps • Due Diligence (for labour laws) in Mergers and Acqusitions • Due Diligence of Contractors /Service Providers	• Comprehensive assistance in record upkeep and maintenance • Onsite and Offsite Service Delivery Model • Payroll, Establishment , CLRA and Factory Compliances • Statutory Remittances , Returns and Challans. • Labor Law Advisory services • Assistance in Inspections and Audits	• Registration/Renewals under various labor laws / acts • Special exemptions and approval • Inspections closures under referred acts

Source: Company

The company has a team of >150 people operating out of 20 locations, servicing 250+ customers, with solutions ranging from standard to customized to cater to their varying requirements.

[3] Retail learning solutions
TeamLease has presence in this segment on account of the acquisition of IIJT, which it acquired in FY11. In this business, it offers training programs in IT, Finance and Retail, following a franchisee model. The business identifies franchisees, sources and provides training to associates, and then offers them placement services.

Earlier, TeamLease also provided training by itself, by leasing space. It is now, however, moving to a franchisee model, completely. It has also partnered with the National Skill Development Corporation (NSDC) to offer various training programs.

As at the end of FY15, it had provided training to 17,691 persons under the NSDC scheme, and is entitled to receive ~INR9,000 per person, subject to certain conditions set by NSDC.

[4] Institutional learning solutions
TeamLease provides skill development services under various government schemes. Its clients in this line of business are state governments or government agencies. On account of its partnership with NSDC, TeamLease is prequalified to bid for tenders. In addition, it also receives grants from state governments to offer skills training programs, which it offers through third parties or through its retail learning solutions infrastructure.

In FY15, this business had revenue of INR88m, exhibiting a growth of 42%.

[5] Apprenticeship programs (NETAP)
National Employability through Apprenticeship Program (NETAP) is an on-the-job training program offered by TeamLease Skills University in Public Private Partnership with the Ministry of Skill Development & Entrepreneurship, AICTE under the Ministry of HRD, CII and NSDC. The program seeks to help unemployed youth build skills through “learning by doing” and “learning while earning”, thus making them job-ready. NETAP proposes to appoint 200k apprentices every year for the next 10 years. At peak capacity, it will be the world’s largest apprenticeship program.

[6] Payroll processing
TeamLease has a well-established and robust payroll processing system in place; it is a combination of technology and domain expertise. It had introduced Payroll Process Outsourcing services as a standalone offering a few years ago.

This expertise too is acquired courtesy its staffing business, for which it already manages payrolls at a large scale and in a complex mesh of operations, for multiple clients across sectors and states, in varying numbers.

Financial performance expectations

Expect 25% revenue CAGR over the next two years

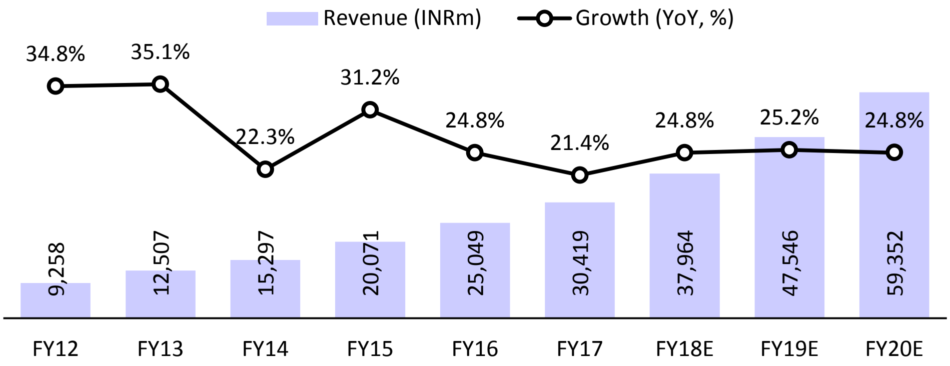
We expect strong growth in the staffing industry over the next few years, led by:
[1] Under-penetration of temporary staffing in India,
[2] Non-linearity provided by an increase in employee productivity, and
[3] Shift of market from unorganized to organized.

Led by these factors, we anticipate 20%+ sustained growth in the industry for organized players. TeamLease being a market leader, with the highest market share in terms of number of associates, can ride this wave, going forward.

TeamLease has a consistent track record, and has sustainably grown its revenue by 27% CAGR over the last five years. This has been led by 15% volume CAGR, and the rest has been a result of wage inflation and improvement in business mix. Most of the growth for TeamLease has been the organic way.

Over the next three years, we expect revenue growth to be a combination of 16% CAGR in associate employees and 8% CAGR in average realization per associate.

Exhibit 112: Revenue CAGR of 25%+ throughout



Source: MOSL, Company

Visibility on profitability improvement exists too

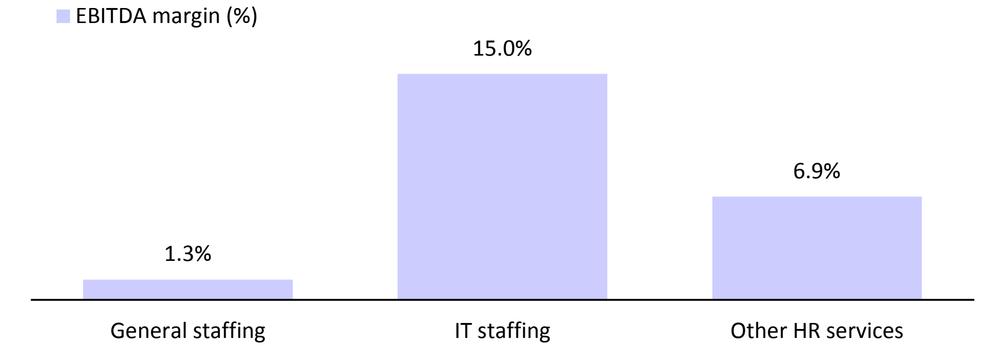
Over the next five years, the management is targeting revenue of USD1b, with EBITDA margin of around 3%. This would be driven by revenue CAGR of 25%, which would be a combination of organic and inorganic growth.

Operating leverage as the business gains scale, combined with higher realization per associate is expected to drive up margins in the staffing business by 10bp each year. This would get a further boost from the increasing share of other businesses (HR services and IT staffing) that command higher margins.

TeamLease recently acquired ASAP Infosystems, marking its entry into IT staffing. As of FY17, this business had an EBITDA margin of 15%, which is materially higher than the 1.3% margin in the general staffing business. The higher margin business led to a 30bp accretion for TeamLease in FY17 on EBITDA margins.

Revenue CAGR of 25% and 40bp EBITDA margin expansion over FY17-20 are expected to result in EBITDA CAGR of 35%.

Exhibit 113: Other businesses have better margins compared to general staffing



Source: MOSL, Company

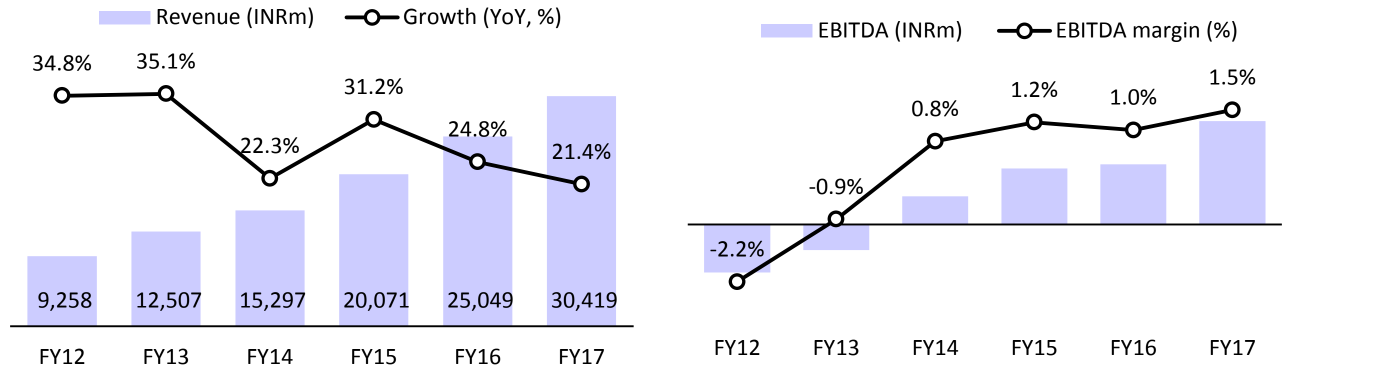
Return ratios to reflect improvement

FY14 and FY15 are good examples of how steady-state improvement in business metrics can result in better financials. The staffing business is asset-light and needs minimal capital expenditure and operational investments for incremental growth.

Systems, technology and process are already in place, and associates work at client locations. This gives the company the advantage of focusing solely on operations and flawless delivery, especially as market conditions are conducive for growth, led more by industry factors and less by company-specific efforts.

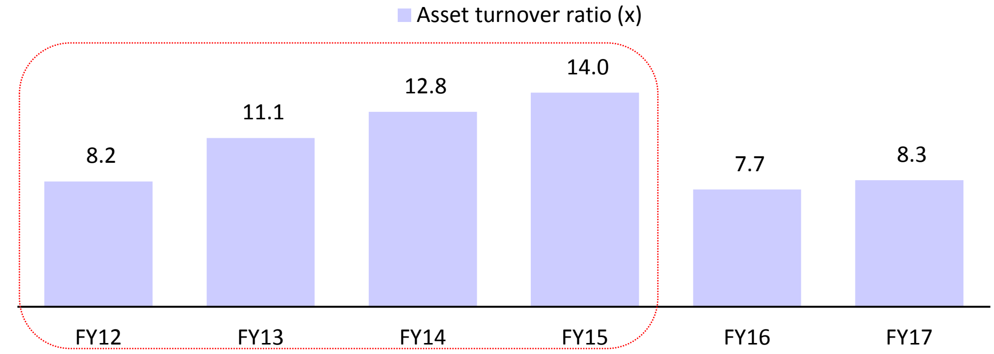
By FY14, TeamLease had a positive EBITDA, and made a margin of 0.8%, compared to -0.9% in the previous year. EBITDA margin further improved to 1.2% in FY15. In both these years, revenue growth was strong at 22% and 31%, respectively.

Exhibit 114: Stark improvement in metrics in FY14/FY15



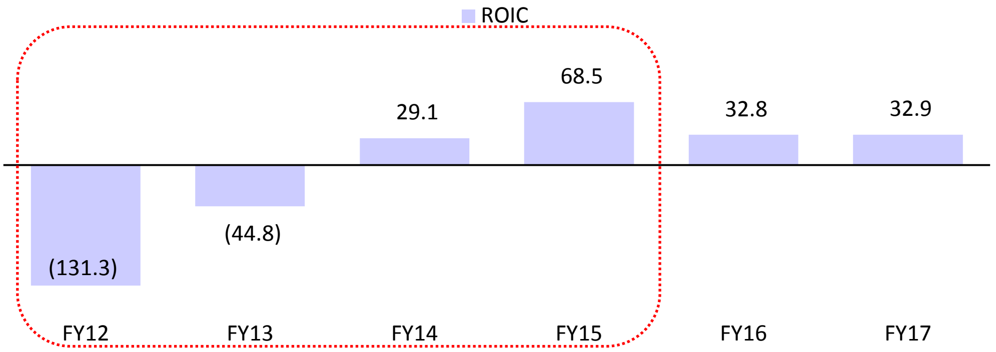
Source: Company

Exhibit 115: Turnover ratio reflects the leverage on existing assets



Source: MOSL, Company

Exhibit 116: Return ratios improve materially during such periods



Source: MOSL, Company

In FY14 and FY15, return ratios too saw stark improvement, with RoIC jumping from a negative 45% to positive 29% in FY14 and to 68% in FY15.

We expect steady improvement in profitability to continue, reflecting in gradually increasing return ratios and steadily improving cash conversion as capex intensity gradually reduces.

Initiate coverage with Buy; TP of INR1,990 per share

Market leadership in staffing industry

- TeamLease is a market leader in the highly fragmented temporary staffing industry, with a 6% market share.
- Its extensive geographic reach, presence in multiple industries and functions, scale, ability to fill positions and sourcing capabilities reflect in its operational prowess, which is a key determinant of success in this industry.
- It has been able to rapidly scale up its apprentice skilling initiative – NETAP (National Employability through Apprenticeship Program), and has now acquired capabilities in IT staffing through the acquisition of ASAP Info Systems.

Staffing industry on a structural growth path

- Temporary staffing across the globe has gained prominence in the last few years, as companies seek flexibility and better cost management. This segment constitutes 2-4% of the total workforce for developed countries, and averages at 1.6% for the world. However, this constitutes only 0.5% of the workforce in India. A convergence to global average itself can triple the industry.
- The growth story improves for organized players, as they constitute ~30% of the overall market. We expect these to gain a larger share of the market post the implementation of GST, which would force unorganized players to pay service tax, erasing the ~15% benefit that non-payment of tax gives them.
- The market would also see wage-inflation-led growth, resulting in higher revenue for the industry, as commissions are a mark-up on the salary paid to associate employees.
- We expect a convergence of these factors to result in sustained 20%+ growth for the organized staffing industry.

Financial performance expected to remain strong, going forward…

- We expect the 25%+ CAGR that TeamLease has witnessed over the last five years to continue, going forward. Our assumptions bake in 16% CAGR in associate employees and 8% CAGR in average realization per associate. Growth is also likely to be supported by the IT staffing business gaining scale.
- We expect profitability improvement, led by [1] Operational leverage because of an improvement in the Associate/Core Employee ratio, and [2] Higher proportion of revenue from IT staffing, training and other HR solutions, which command better margins. We are baking in cumulative margin expansion of 40bp over the next three years.
- This would result in 25% revenue CAGR, 35% EBITDA CAGR, and 26% PAT CAGR over FY17-20.
- TeamLease is eligible to draw the benefits of Section 80JJAA, relating to a 30% deduction on wages paid to new workmen (in excess of 50) in the previous year, for three assessment years. We expect this to be a material earnings booster given the fact that employee expenses account for ~96% of total revenue, and the addition of associates has been 15%+ over the last five years.

…thereby improving multiple other metrics

- The staffing business is asset-light, which leads to strong cash generation, return ratios and asset turnover once it gains scale and reaches steady profitability.
- We expect continued improvement in profitability to lead to a RoIC of 34.4% in FY20 (from 32.9% in FY17). Asset turnover should increase to 9.0x by FY20 (from 8.3x in FY17).
- These ratios will only get better with time, as the company continues gaining scale at a velocity that is disproportionately higher than the investments required in the business, either in the form of capital expenditure or in the form of employees to run the business.

Better placed in general staffing compared to listed competition

- TeamLease is a market leader in the temporary staffing industry, with a 6% market share. Scale has its benefits in this market, as it drives higher operational efficiency and superior financial performance.
- Despite its scale, TeamLease has a lower Associate/Core Employee ratio than Quess (203 for TeamLease versus 223 for Quess). The primary reason for this is the difference in approach towards the business.
- While Quess is focused on higher revenue from a smaller number of large customers, TeamLease has diversified its presence across multiple customers to extend reach. It has ~1,900 customers in the staffing business, compared to 280 for Quess, resulting in a higher number of account managers and support staff.
- Though this seems negative from an efficiency point of view, when the time horizon is extended further, in the future, TeamLease would require lesser effort to gather new customers, and will focus on mining existing customers for growth. Moreover, GST implementation has been triggering a shift in the market towards organized players, because of which there will be higher velocity witnessed in the smaller players because of the under-penetration of organized temporary staffing, in turn positively impacting TeamLease to a larger extent.

Valuation and view: Scale will be the key driver of value creation

- We value TeamLease using DCF to reach a price target of INR1,990, implying an upside of 22%.
- We see TeamLease as a key beneficiary to industry trends, and expect it to demonstrate a high-growth trajectory over the next three years. Consequently, prospective improvement in return ratios and cash generation, led by the business model, would be a key driver of value creation for TeamLease.

Exhibit 117: Fair value of INR1,990 based on DCF

Discount rate	12.0%
Terminal growth rate	5.0%
PV FCF	9,193
PV of terminal value	22,880
NPV	32,073
Less: Debt	11
Add: Cash and cash equivalents	1,979
Total equity value	34,041
Per share	
PV FCF	538
PV of terminal value	1338
NPV	1876
Less: Debt	1
Add: Cash and cash equivalents	116
Total equity value	1991
NOSH m	17
CMP	1,637
Target price	1,990
Upside (%)	22%

Source: MOSL

Exhibit 118: We assume 12% WACC and 5% terminal growth rate

WACC/g	Sensitivity analysis				
1990	**3.0%**	**4.0%**	**5.0%**	**6.0%**	**7.0%**
10%	2,280	2,560	2,950	3,540	4,510
11%	1,940	2,130	2,390	2,750	3,290
12%	1,670	1,810	1,990	2,230	2,560
13%	1,470	1,570	1,700	1,860	2,080
14%	1,300	1,380	1,470	1,590	1,740

Source: MOSL

Scenario analysis

We don't see much risk to our FY18/19 estimates, given the visibility provided by existing momentum in the business, integration of announced acquisitions, and steady state of economic conditions. TeamLease was also able to largely mitigate the impact of demonetization because of its diversified portfolio, thereby giving few reasons to worry about, as far as near-term growth is concerned.

The business was showed resilience even after demonetization. Revenue growth in the staffing business in 3QFY17 saw acceleration (25% YoY versus 11% YoY in the previous quarter), as demand for temporary staff in the BFSI space following demonetization more than offset the decline in sectors with a direct negative impact (like Retail). Associate headcount grew by 8,700 in 3QFY17, compared to a growth of 2,700 in the previous quarter.

Our bull and bear case assumptions both build in margin expansion, as scale would lead to efficiency improvement, defined by better Associate/Core Employee ratio. Only the quantum of expansion varies across these scenarios.

We have analyzed scenarios based on our medium-long-term estimates considered in our DCF. Broadly, our scenario assumptions differ on the parameters of revenue growth and margins.

The scenario analysis highlights the kind of benefits that would flow into the company's financial performance because of the model it is based on. We haven't been proportional in our assumptions in a bull case (+2pp growth on base) and a bear case (-5pp growth on base). However, note that cash generation becomes disproportionately superior compared to the increase in growth estimates.

Exhibit 119: Assumptions – differences across scenarios

	Bull	Base	Bear
Revenue growth (YoY, %)			
FY21-22	25%	23%	18%
FY23-25	22%	20%	15%
FY26-28	19%	17%	12%
EBIT margin (%)			
FY20-22	15bp	10bp	5bp
FY23-25	15bp	10bp	5bp
FY26-27	15bp	10bp	5bp

Source: MOSL

Exhibit 120: Assumptions – differences across scenarios

		Base case	Bull case	Bear case
Discount rate	12.0%			
Terminal growth rate	5.0%			
PV FCF		9,193	10,985	7,167
PV of terminal value		22,880	30,505	14,178
NPV		32,073	41,490	21,344
Less: Debt		11	11	11
Add: Cash and cash equivalents		1,979	1,979	1,979
Total equity value		34,041	43,458	23,312
Per share				
PV FCF		538	642	419
PV of terminal value		1338	1784	829
NPV		1876	2426	1248
Less: Debt		1	1	1
Add: Cash and cash equivalents		116	116	116
Total equity value		1991	2541	1363
NOSH m	17			
CMP	1,637			
Target price		1,990	2,541	1,363
Upside (%)		22%	55%	-17%

Source: MOSL

Bull case suggests ~60% upside from current levels

Our bull case assumes 2pp higher growth than we have assumed in our DCF, along with steady 15bp EBIT margin expansion through the time frame.

As highlighted in our sector analysis, in the staffing business, growth would hinge on:

- Volume growth, led by an increased penetration of the temporary staffing industry in India to the global average of 1.5% (from 0.5% currently),
- Increase in India's per capita GDP resulting in higher realization per temporary employee, and
- Shift of the market away from the unorganized segment, which currently comprises ~70% of the total industry.

An analysis of these variables threw up the likelihood of 23% CAGR in the organized staffing market over the next five years, and 16% CAGR post that. Our assumptions seem within limits, given the high ceiling and TeamLease's superior positioning in this space.

Moreover, the focus is on gaining a higher profitability profile by entering high-value businesses like staffing in the IT, healthcare and hospitality sectors. This doesn't only result in better margins (and consequently higher cash generation), but also better valuations, as observed in some of the global peers we analyzed earlier.

Bear case analysis indicates ~15% downside from current levels

Our bear case assumes 5pp lower growth than we have assumed in our DCF, along with no EBIT margin change along the timeframe.

Key assumptions to our growth estimates are structural in nature. However, certain risks that would push growth lower would be:

- Economic downturn leading to lower growth in staffing. Down-cycles are usually accompanied by a direct hit on employment and contract staffing.
- Slower increase in the penetration of temporary staffing in India despite the headroom.
- GST implementation not resulting in a shift of the temporary staffing market from unorganized players to organized players, thus not accelerating growth for players like TeamLease.
- Issues in one or more of the top customers, given the long tail that TeamLease has and the fact that it depends on its top-10 customers for 18% of its revenue.
- Issues in top clients won't be restricted plainly to TeamLease's performance and execution with that customer, or competitive dynamics. This would be exposed to multiple other risk factors at various levels – macroeconomic, sectoral, functional, and idiosyncratic.

Any of these risks playing out would result in sharp deterioration in performance. However, our assumptions in the bear case are still factoring in 5bp margin expansion each year. This is resulting out of the fact that economies of scale would continue benefiting the company till the time revenue grows.

SWOT analysis

Strengths

- **Scale:** TeamLease is well placed to capture the opportunities in the Indian staffing market because of its scale, operational abilities and geographical presence. The staffing industry is highly fragmented, with the largest player having a 6% market share. This would make TeamLease a direct beneficiary of any upward trend in the industry.
- **Execution prowess:** The company manages 130,000 associates across 1,900 customers all over the country. These associates have 60%+ attrition and the company has to constantly maintain efficiency in procuring, processing and managing. So far, it has excelled at execution, which puts it in a better position than peers in an operations-centric business.
- **Monetization**: Because of its business and operations, TeamLease goes through compliance and regulation, payroll, and training and development at a large scale. As it has mastered these processes for running itself, it has also started monetizing these areas by selling solutions and services around them to other customers.

Weaknesses

- **Lack of diversification:** TeamLease has been late in capitalizing opportunities in specialist staffing. It has been focused on general staffing, which is reflecting in low margins and large scale. Specialist staffing tends to have better yields and profitability. This also gets reflected in superior financial position, and consequently, higher valuations too.

Opportunities

- **Staffing:** On account of the under-penetration of temporary staffing in India (0.5% in general staffing v/s 1.6% globally, and 10% in IT services v/s 20% globally), there lies tremendous opportunity for volume growth. Moreover, wage inflation and improved business mix would result in further growth. Together, this creates an opportunity for sustained 20%+ growth in these areas.
- **Other business services:** While TeamLease gets a majority of its revenue from general staffing, other HR solutions pose an opportunity for high growth, and improved profitability. Higher growth is anticipated in the areas on a small base and TeamLease is well positioned to capitalize on those.
- **Client mining:** TeamLease gets 80% of its business from over 1,900 clients. This makes it a long tail marked by low revenue per customer. An opportunity exists to actively mine these clients better and get a higher wallet share amongst them. A strong customer base also implies not deploying a heavy S&M team to hunt for additional revenue.

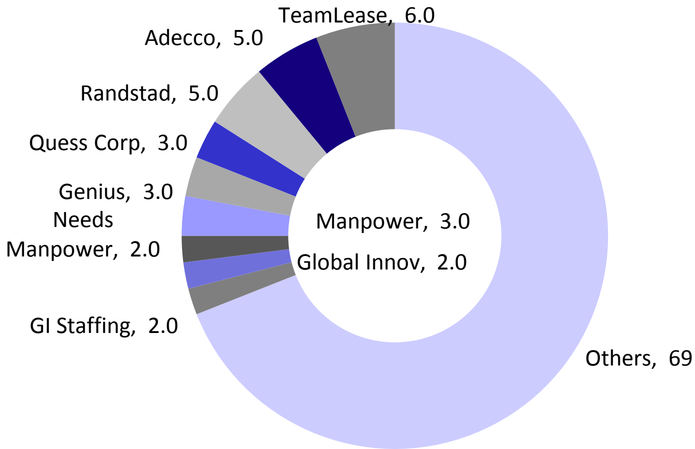
Threats

- **Loss of key clients:** Top 5/10 accounts contribute to 12/18% of TeamLease's revenue. While this doesn't reflect much dependency compared to the 30% from top-10 clients for Quess, TeamLease has more concentrated services in each of its customers and it has a longer tail (80% revenue distributed amongst 1,900 customers), making the risk larger compared to Quess. Loss of any top client would materially impact financial performance.
- **Correlation with economic cycles:** The staffing business (both general and professional) has high dependency on economic cycles. Although India is an under-penetrated market, and there are structural opportunities for growth, any significant downturn in economic activity could result in a severe impact on financial performance. For TeamLease, no sector contributes over 20% of total revenue, and that is well-diversified. However, in case of overall economic downturn, this spread would be of little help.

Company description

TeamLease is India's largest general staffing company. It was established in 2002 by Mr Manish Sabharwal, Mr Ashok Reddy, and Mr Mohit Gupta. Apart from general staffing, it also provides other human resource services like payroll processing, recruitment, compliance, learning and assessment. It has 130k associates serving over 1,900 customers across the country. TeamLease operates out of nine offices and has 1,467 full-time employees.

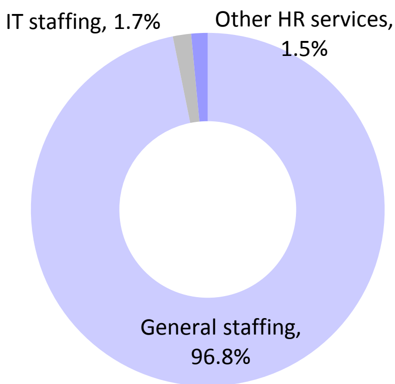
Exhibit 121: TeamLease is the largest general staffing company in India



Source: CRISIL Research

TeamLease's core business is providing staffing solutions across industry sectors and diverse functional areas. Most of its associate employees are engaged in sales, logistics and customer service functions. The company focuses on people, processes and technology to enhance business productivity for its end-customers, who can outsource the staffing function to better focus on their core business.

Exhibit 122: Staffing is TeamLease's core business



Source: Company

Key management personnel

Mr Manish Sabharwal, Chairman and Co-Founder

Mr Manish Sabharwal is the Chairman of TeamLease. Prior to co-founding the company, he co-founded India Life, a human resource outsourcing company that was acquired by Hewitt Associates in 2002. Consequently, he was the CEO of Hewitt Outsourcing based in Singapore. Mr Sabharwal also serves on various state and central government committees on education, employment and employability.

Mr Ashok Reddy, Managing Director and Co-Founder

Mr Ashok Reddy is the Co-Founder and Managing Director of TeamLease. He oversees operations and represents the company in forums with major clients. He has 17 years of experience in human resource services. Prior to this, he was a Director at India Life Capital Private Limited.

Ms Rituparna Chakraborty, Executive Vice President

Ms Chakraborty has been with TeamLease since inception. She is responsible for staffing and also drives the NETAP (National Employability through Apprenticeship Program) initiative. Prior to this, she was Client Manager at India Life Pension Services Private Limited and Key Accounts Manager at Monster.com (India). She is also the Founding Trustee and President of Indian Staffing Federation.

Ms Neeti Sharma, Senior Vice President Learning Services

Ms Sharma is Senior Vice President, Institutional Learning Services and Distance Learning. She has over 15 years of experience in the field of human resources. Prior to this, she was Assistant Manager at APTECH India.

Mr N Ravi Vishwanath, Chief Financial Officer

Mr Vishwanath is the CFO of TeamLease. He has over 21 years of experience in the finance sector. Prior to this, he worked at Sun Microsystems India and was the Vice President – Finance at Global Symphony Software.

Mr Kunal Sen, Sr Vice President, Permanent Recruitment

Mr Sen is a Senior Vice President in the Sourcing department. He has over 15 years of experience in sales and marketing. Prior to this, he was the Director of Sales and Marketing at Stovekraft Private Limited.

Mr Sharanabasappa Shirol, Sr Vice President, Information Technology

Mr Shirol is Vice President-IT. He has 12 years of experience. Prior to this, he was Senior Software Engineer at Hewitt Outsourcing India.

Mr Mruthunjaya Murthy, Company Secretary

Mr Mruthunjaya Murthy is the Company Secretary. He has over 18 years of professional experience in corporate governance and statutory compliance. Prior to this, he was the Company Secretary of NSL Sugars Limited.

Mr Santosh Thangavelu, Vice President and Head - Human Resources

Mr Santosh Thangavelu is Vice President, Human Resources. He has over 17 years of experience in human resource management. Prior to this, he was Senior Director – Human Resources with Cognizant Technology Solutions India. Prior to that, he has worked with Infosys, Motor Industries, and P4P Consulting.

Exhibit 123: Organization structure

Source: Company

Exhibit 124: Board of Directors

Name	Designation	Comments
Manish Sabharwal	Chairman	■ Prior to this, co-founded India Life Capital, a pension and provident fund asset management company that was acquired by Hewitt Associates ■ Serves on various state and central government committees on education, employment and employability
Ashok Reddy	Managing Director	■ 17 years of experience in human resource services ■ Prior to this, co-founded India Life Capital, a pension and provident fund asset management company that was acquired by Hewitt Associates
Gopal Jain	Non-Executive, Nominee Director	■ One of the co-founders of Gaja Capital ■ Director since November 2009
Latika Prakash Pradhan	Independent Director	■ 35 years of experience ■ Independent Director on the board of Mafatlal Industries ■ In the past, she has been associated with Voltas, Blue Star, Cummins, Park Davis India and Pidilite ■ Director since July 2015
Narayan Ramachandran	Independent Director	■ Was the country head of and CEO of Morgan Stanley India, prior to which he was the co-head of emerging markets division of Morgan Stanley Investment Management, Singapore ■ Director since July 2015
V. Raghunathan	Independent Director	■ CEO of GMR Varalakshmi Foundation ■ Was a Fellow of IIM, Calcutta; Professor at IIM, Ahmedabad for two decades ■ Director since July 2015

Source: Company

Key risks

Loss of key clients: Top 5/10 accounts contribute 12%/18% of TeamLease's revenue. While this doesn't reflect much dependency compared to 30% from top-10 clients for Quess, TeamLease has more concentrated services in each of its customers and it has a longer tail (80% revenue distributed amongst 1,900 customers), making the risk larger compared to Quess. Loss of any top client would result in a material impact on financial performance.

Correlation with economic cycles: The staffing business (both general and professional) have a very high dependency on economic cycles. Although India is an under-penetrated market, and there are structural opportunities of growth, any significant downturn in economic activity could result in a severe impact on financial performance. For TeamLease, no sector contributes more than 20% of total revenue; it is well-diversified. However, in case of overall economic downturn, this spread would be of little help.

High attrition amongst associates: The temporary staffing industry is associated with high attrition (60%+) on account of the nature of the job, and the constant shift of employees from temporary to permanent employment. This makes it necessary for companies to constantly add associates in numbers much larger than the net requirement. Despite demand, it could become difficult for a company with this scale to keep adding people because of supply or procurement issues.

Financials and valuation

Consolidated - Income Statement (INR Million)

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Total Income from Operations	**12,507**	**15,297**	**20,071**	**25,049**	**30,419**	**37,964**	**47,546**	**59,352**
Change (%)	35.1	22.3	31.2	24.8	21.4	24.8	25.2	24.8
Employees Cost	12,165	14,839	19,445	24,391	29,377	36,607	45,804	57,179
Selling & Admin Expenses	265	193	315	305	439	561	666	787
Other Expenses	189	144	70	94	157	200	238	281
Total Expenditure	**12,618**	**15,175**	**19,829**	**24,790**	**29,972**	**37,368**	**46,707**	**58,247**
% of Sales	100.9	99.2	98.8	99.0	98.5	98.4	98.2	98.1
EBITDA	**-111**	**121**	**241**	**259**	**446**	**597**	**839**	**1,105**
Margin (%)	-0.9	0.8	1.2	1.0	1.5	1.6	1.8	1.9
Depreciation	36	19	27	30	43	47	51	55
EBIT	**-147**	**102**	**214**	**229**	**403**	**550**	**788**	**1,050**
Int. and Finance Charges	5	2	2	5	14	2	2	2
Other Income	115	79	114	154	224	279	350	437
PBT bef. EO Exp.	**-37**	**178**	**326**	**378**	**613**	**828**	**1,137**	**1,485**
EO Items	0	0	0	0	0	0	0	0
PBT after EO Exp.	**-37**	**178**	**326**	**378**	**613**	**828**	**1,137**	**1,485**
Total Tax	0	0	18	130	-50	198	178	146
Tax Rate (%)	0.0	0.0	5.5	34.4	-8.2	23.9	15.7	9.8
Minority Interest	0	0	0	0	0	0	0	0
Reported PAT	**-37**	**178**	**308**	**248**	**664**	**630**	**958**	**1,340**
Adjusted PAT	**-37**	**178**	**308**	**248**	**664**	**630**	**958**	**1,340**
Change (%)	-77.6	-581.9	72.6	-19.4	167.6	-5.1	52.1	39.8
Margin (%)	-0.3	1.2	1.5	1.0	2.2	1.7	2.0	2.3

Consolidated - Balance Sheet (INR Million)

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Equity Share Capital	5	5	5	171	171	171	171	171
Total Reserves	1,005	1,183	1,483	2,945	3,640	4,270	5,228	6,568
Net Worth	**1,010**	**1,188**	**1,488**	**3,116**	**3,811**	**4,441**	**5,399**	**6,739**
Minority Interest	0	0	0	0	0	0	0	0
Total Loans	121	9	0	194	11	11	11	11
Deferred Tax Liabilities	0	0	-57	-45	-149	-149	-149	-149
Capital Employed	**1,131**	**1,197**	**1,431**	**3,264**	**3,673**	**4,303**	**5,261**	**6,601**
Gross Block	282	276	221	309	349	373	404	443
Less: Accum. Deprn.	205	199	222	252	302	349	399	455
Net Fixed Assets	**77**	**77**	**-1**	**57**	**47**	**25**	**5**	**-12**
Goodwill on Consolidation	30	30	54	54	982	982	982	982
Total Investments	0	0	42	0	0	0	0	0
Curr. Assets, Loans&Adv.	**2,135**	**2,326**	**2,974**	**5,629**	**5,641**	**7,062**	**9,017**	**11,576**
Inventory	5	3	2	2	2	2	2	3
Account Receivables	618	595	813	1,205	1,872	2,368	3,005	3,800
Cash and Bank Balance	780	847	1,147	2,590	1,593	1,979	2,611	3,531
Loans and Advances	732	881	1,012	1,832	2,174	2,714	3,399	4,243
Curr. Liability & Prov.	**1,111**	**1,236**	**1,638**	**2,476**	**3,101**	**3,870**	**4,846**	**6,049**
Account Payables	12	72	69	88	105	131	163	203
Other Current Liabilities	970	976	1,303	2,013	2,469	3,081	3,858	4,816
Provisions	130	188	266	375	528	658	825	1,029
Net Current Assets	**1,023**	**1,090**	**1,336**	**3,153**	**2,540**	**3,193**	**4,171**	**5,527**
Appl. of Funds	**1,131**	**1,197**	**1,431**	**3,264**	**3,673**	**4,303**	**5,261**	**6,601**

E: MOSL Estimates

Financials and valuation

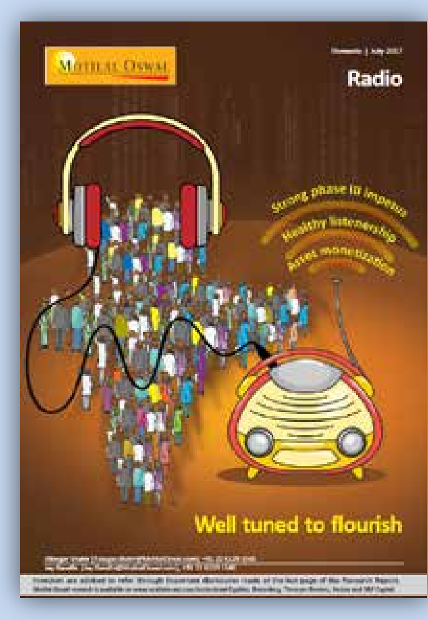
Ratios

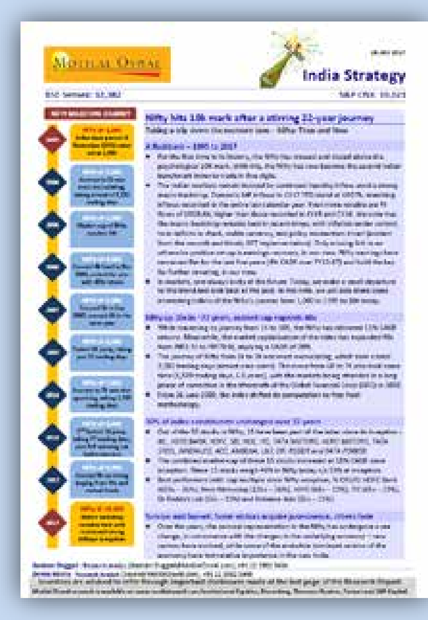
Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Basic (INR)								
EPS	**-2.2**	**10.4**	**18.0**	**14.5**	**38.8**	**36.8**	**56.0**	**78.3**
Cash EPS	0.0	11.5	19.6	16.3	41.3	39.6	59.0	81.6
BV/Share	59.1	69.5	87.0	182.2	222.9	259.7	315.8	394.1
DPS	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Payout (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Valuation (x)								
P/E			91.0	112.9	42.2	44.5	29.2	20.9
Cash P/E			83.6	100.7	39.6	41.4	27.7	20.1
P/BV			18.8	9.0	7.3	6.3	5.2	4.2
EV/Sales			1.3	1.0	0.9	0.7	0.5	0.4
EV/EBITDA			111.2	98.7	59.2	43.6	30.3	22.1
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
FCF per share	-6.1	8.0	17.9	-8.9	18.4	6.3	16.6	28.3
Return Ratios (%)								
RoE	-3.6	16.2	23.0	10.8	19.2	15.3	19.5	22.1
RoCE	-2.8	15.5	23.1	10.5	19.0	15.2	19.5	22.1
RoIC	-44.8	29.1	68.5	32.8	32.9	19.9	27.9	34.4
Working Capital Ratios								
Asset Turnover (x)	11.1	12.8	14.0	7.7	8.3	8.8	9.0	9.0
Debtor (Days)	18	14	15	18	22	23	23	23
Creditor (Days)	0	2	1	1	1	1	1	1
Leverage Ratio (x)								
Net Debt/Equity	-0.7	-0.7	-0.8	-0.8	-0.4	-0.5	-0.5	-0.5

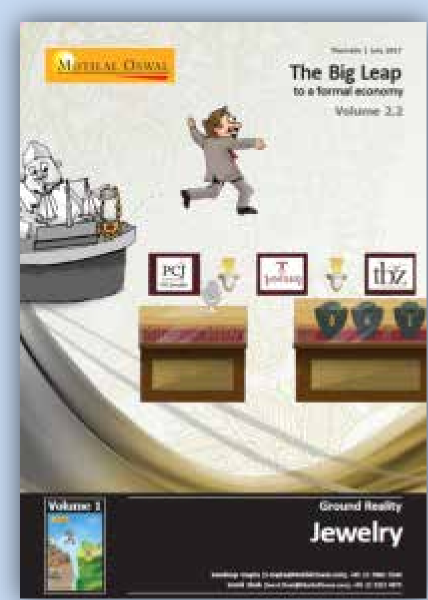
Consolidated - Cash Flow Statement **(INR Million)**

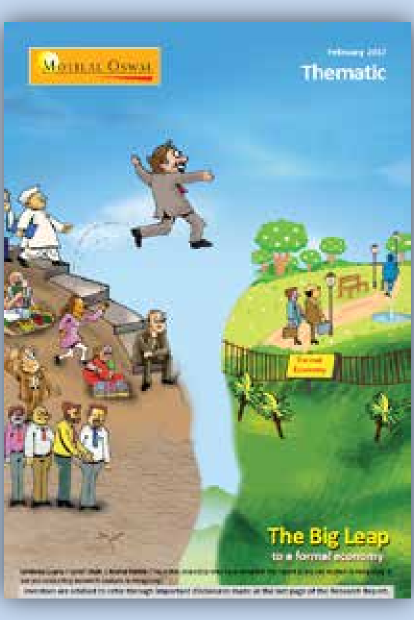
Y/E March	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
OP/(Loss) before Tax	-37	179	326	378	613	828	1,137	1,485
Depreciation	36	19	27	30	43	47	51	55
Interest & Finance Charges	-65	-69	-97	-95	-157	-278	-348	-435
Direct Taxes Paid	-86	-78	17	-265	-191	-198	-178	-146
(Inc)/Dec in WC	-17	58	38	-150	-19	-266	-346	-436
CF from Operations	**-168**	**108**	**311**	**-102**	**289**	**133**	**315**	**523**
Others	75	55	32	-3	43	0	0	0
CF from Operating incl EO	**-93**	**164**	**343**	**-105**	**332**	**133**	**315**	**523**
(Inc)/Dec in FA	-11	-26	-37	-47	-18	-25	-31	-39
Free Cash Flow	**-104**	**137**	**306**	**-152**	**314**	**108**	**284**	**485**
(Pur)/Sale of Investments	1	2	3	2	-85	0	0	0
Others	26	43	0	23	-814	279	350	437
CF from Investments	**16**	**19**	**-34**	**-22**	**-917**	**255**	**319**	**398**
Issue of Shares	0	0	0	1,500	0	0	0	0
Inc/(Dec) in Debt	40	-113	-8	0	0	0	0	0
Interest Paid	-5	-2	-1	-4	-11	-2	-2	-2
Dividend Paid	0	0	0	0	0	0	0	0
Others	0	0	0	73	-401	0	0	0
CF from Fin. Activity	**35**	**-115**	**-10**	**1,569**	**-412**	**-2**	**-2**	**-2**
Inc/Dec of Cash	**-42**	**67**	**300**	**1,443**	**-997**	**386**	**632**	**920**
Opening Balance	822	780	847	1,147	2,590	1,593	1,979	2,611
Closing Balance	**780**	**847**	**1,147**	**2,590**	**1,593**	**1,979**	**2,611**	**3,531**

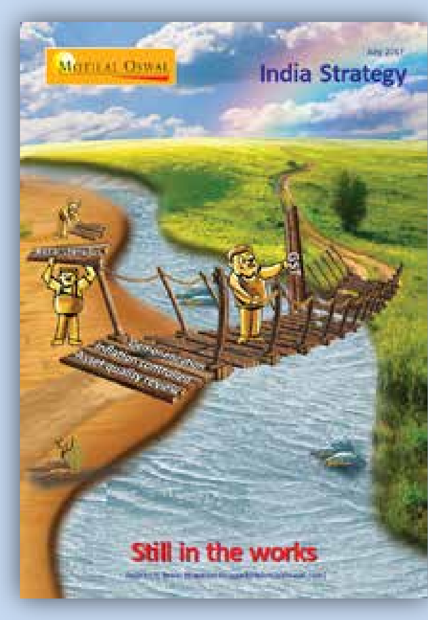
THEMATIC/STRATEGY RESEARCH GALLERY











NOTES

Disclosures:

The following Disclosures are being made in compliance with the SEBI Research Analyst Regulations 2014 (herein after referred to as the Regulations).

Motilal Oswal Securities Ltd. (MOSL) is a SEBI Registered Research Analyst having registration no. INH000000412. MOSL, the Research Entity (RE) as defined in the Regulations, is engaged in the business of providing Stock broking services, Investment Advisory Services, Depository participant services & distribution of various financial products. MOSL is a subsidiary company of Motilal Oswal Financial Service Ltd. (MOFSL). MOFSL is a listed public company, the details in respect of which are available on www.motilaloswal.com. MOSL is registered with the Securities & Exchange Board of India (SEBI) and is a registered Trading Member with National Stock Exchange of India Ltd. (NSE) and Bombay Stock Exchange Limited (BSE), Metropolitan Stock Exchange Of India Ltd. (MSE) for its stock broking activities & is Depository participant with Central Depository Services Limited (CDSL) & National Securities Depository Limited (NSDL) and is member of Association of Mutual Funds of India (AMFI) for distribution of financial products. Details of associate entities of Motilal Oswal Securities Limited are available on the website at http://onlinereports.motilaloswal.com/Dormant/documents/Associate%20Details.pdf

Pending Regulatory Enquiries against Motilal Oswal Securities Limited by SEBI:

SEBI pursuant to a complaint from client Shri C.R. Mohanraj alleging unauthorized trading, issued a letter dated 29th April 2014 to MOSL notifying appointment of an Adjudicating Officer as per SEBI regulations to hold inquiry and adjudge violation of SEBI Regulations; MOSL requested SEBI to provide all documents, records, investigation report relied upon by SEBI which were referred in Show Cause Notice and also sought personal hearing. The matter is currently pending.

MOSL, it's associates, Research Analyst or their relative may have any financial interest in the subject company. MOSL and/or its associates and/or Research Analyst may have beneficial ownership of 1% or more securities in the subject company at the end of the month immediately preceding the date of publication of the Research Report. MOSL and its associate company(ies), their directors and Research Analyst and their relatives may; (a) from time to time, have a long or short position in, act as principal in, and buy or sell the securities or derivatives thereof of companies mentioned herein. (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company(ies) discussed herein or act as an advisor or lender/borrower to such company(ies) or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.; however the same shall have no bearing whatsoever on the specific recommendations made by the analyst(s), as the recommendations made by the analyst(s) are completely independent of the views of the associates of MOSL even though there might exist an inherent conflict of interest in some of the stocks mentioned in the research report. Research Analyst may have served as director/officer, etc. in the subject company in the last 12 month period. MOSL and/or its associates may have received any compensation from the subject company in the past 12 months.

In the last 12 months period ending on the last day of the month immediately preceding the date of publication of this research report, MOSL or any of its associates may have:

a) managed or co-managed public offering of securities from subject company of this research report,
b) received compensation for investment banking or merchant banking or brokerage services from subject company of this research report,
c) received compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company of this research report.
d) Subject Company may have been a client of MOSL or its associates during twelve months preceding the date of distribution of the research report.

MOSL and it's associates have not received any compensation or other benefits from the subject company or third party in connection with the research report. To enhance transparency, MOSL has incorporated a Disclosure of Interest Statement in this document. This should, however, not be treated as endorsement of the views expressed in the report. MOSL and / or its affiliates do and seek to do business including investment banking with companies covered in its research reports. As a result, the recipients of this report should be aware that MOSL may have a potential conflict of interest that may affect the objectivity of this report. Compensation of Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

Terms & Conditions:

This report has been prepared by MOSL and is meant for sole use by the recipient and not for circulation. The report and information contained herein is strictly confidential and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of MOSL. The report is based on the facts, figures and information that are considered true, correct, reliable and accurate. The intent of this report is not recommendatory in nature. The information is obtained from publicly available media or other sources believed to be reliable. Such information has not been independently verified and no guaranty, representation of warranty, express or implied, is made as to its accuracy, completeness or correctness. All such information and opinions are subject to change without notice. The report is prepared solely for informational purpose and does not constitute an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments for the clients. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. MOSL will not treat recipients as customers by virtue of their receiving this report.

Analyst Certification

The views expressed in this research report accurately reflect the personal views of the analyst(s) about the subject securities or issues, and no part of the compensation of the research analyst(s) was, is, or will be directly or indirectly related to the specific recommendations and views expressed by research analyst(s) in this report.

Disclosure of Interest Statement	Companies where there is interest
▪ Analyst ownership of the stock	No

A graph of daily closing prices of securities is available at www.nseindia.com, www.bseindia.com. Research Analyst views on Subject Company may vary based on Fundamental research and Technical Research. Proprietary trading desk of MOSL or its associates maintains arm's length distance with Research Team as all the activities are segregated from MOSL research activity and therefore it can have an independent view with regards to subject company for which Research Team have expressed their views.

Regional Disclosures (outside India)

This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject MOSL & its group companies to registration or licensing requirements within such jurisdictions.

For Hong Kong:

This report is distributed in Hong Kong by Motilal Oswal capital Markets (Hong Kong) Private Limited, a licensed corporation (CE AYY-301) licensed and regulated by the Hong Kong Securities and Futures Commission (SFC) pursuant to the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) "SFO". As per SEBI (Research Analyst Regulations) 2014 Motilal Oswal Securities (SEBI Reg No. INH000000412) has an agreement with Motilal Oswal capital Markets (Hong Kong) Private Limited for distribution of research report in Hong Kong. This report is intended for distribution only to "Professional Investors" as defined in Part I of Schedule 1 to SFO. Any investment or investment activity to which this document relates is only available to professional investor and will be engaged only with professional investors." Nothing here is an offer or solicitation of these securities, products and services in any jurisdiction where their offer or sale is not qualified or exempt from registration. The Indian Analyst(s) who compile this report is/are not located in Hong Kong & are not conducting Research Analysis in Hong Kong.

For U.S.

Motilal Oswal Securities Limited (MOSL) is not a registered broker - dealer under the U.S. Securities Exchange Act of 1934, as amended (the"1934 act") and under applicable state laws in the United States. In addition MOSL is not a registered investment adviser under the U.S. Investment Advisers Act of 1940, as amended (the "Advisers Act" and together with the 1934 Act, the "Acts), and under applicable state laws in the United States. Accordingly, in the absence of specific exemption under the Acts, any brokerage and investment services provided by MOSL, including the products and services described herein are not available to or intended for U.S. persons. This report is intended for distribution only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the Exchange Act and interpretations thereof by SEC (henceforth referred to as "major institutional investors"). This document must not be acted on or relied on by persons who are not major institutional investors. Any investment or investment activity to which this document relates is only available to major institutional investors and will be engaged in only with major institutional investors. In reliance on the exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act") and interpretations thereof by the U.S. Securities and Exchange Commission ("SEC") in order to conduct business with Institutional Investors based in the U.S., MOSL has entered into a chaperoning agreement with a U.S. registered broker-dealer, Motilal Oswal Securities International Private Limited. ("MOSIPL"). Any business interaction pursuant to this report will have to be executed within the provisions of this chaperoning agreement.

The Research Analysts contributing to the report may not be registered /qualified as research analyst with FINRA. Such research analyst may not be associated persons of the U.S. registered broker-dealer, MOSIPL, and therefore, may not be subject to NASD rule 2711 and NYSE Rule 472 restrictions on communication with a subject company, public appearances and trading securities held by a research analyst account.

For Singapore

Motilal Oswal Capital Markets Singapore Pte Limited is acting as an exempt financial advisor under section 23(1)(f) of the Financial Advisers Act(FAA) read with regulation 17(1)(d) of the Financial Advisors Regulations and is a subsidiary of Motilal Oswal Securities Limited in India. This research is distributed in Singapore by Motilal Oswal Capital Markets Singapore Pte Limited and it is only directed in Singapore to accredited investors, as defined in the Financial Advisers Regulations and the Securities and Futures Act (Chapter 289), as amended from time to time. In respect of any matter arising from or in connection with the research you could contact the following representatives of Motilal Oswal Capital Markets Singapore Pte Limited:

Disclaimer:

Registered Office Address: Motilal Oswal Tower, Rahimtullah Sayani Road, Opposite Parel ST Depot, Prabhadevi, Mumbai-400025; Tel No.: 022-3980 4263; www.motilaloswal.com. Correspondence Address: Palm Spring Centre, 2nd Floor, Palm Court Complex, New Link Road, Malad (West), Mumbai- 400 064. Tel No: 022 3080 1000. Compliance Officer: Neeraj Agarwal, Email Id: na@motilaloswal.com, Contact No.:022-30801085.

Registration details of group entities.: MOSL: NSE (Cash): INB231041238; NSE (F&O): INF231041238; NSE (CD): INE231041238; BSE (Cash): INB011041257; BSE(F&O): INF011041257; BSE(CD); MSE(Cash): INB261041231; MSE(F&O): INF261041231; MSE(CD): INE261041231; CDSL: IN-DP-16-2015; NSDL: IN-DP-NSDL-152-2000; Research Analyst: INH000000412. AMFI: ARN 17397. Investment Adviser: INA000007100. Motilal Oswal Asset Management Company Ltd. (MOAMC): PMS (Registration No.: INP000000670) offers PMS and Mutual Funds products. Motilal Oswal Wealth Management Ltd. (MOWML): PMS (Registration No.: INP000004409) offers wealth management solutions. *Motilal Oswal Securities Ltd. is a distributor of Mutual Funds, PMS, Fixed Deposit, Bond, NCDs, Insurance and IPO products. * Motilal Oswal Commodities Broker Pvt. Ltd. offers Commodities Products. * Motilal Oswal Real Estate Investment Advisors II Pvt. Ltd. offers Real Estate products. * Motilal Oswal Private Equity Investment Advisors Pvt. Ltd. offers Private Equity products