

Cognizant Technology (CTSH)

\$57.82 (As of 06/05/20)

Price Target (6-12 Months): **\$61.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 07/01/19)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:B

Value: B

Growth: A

Momentum: F

Summary

Cognizant's domain expertise and the ability to harness the ongoing digital transition are key catalysts. The company is witnessing strength in cloud and digital engineering services, and increased demand for interactive, IoT and analytics solutions. Moreover, acquisitions have strengthened the company's digital capabilities, clientele and international prospects. However, lackluster spending by large banks and ongoing stiff competition in the IT services market are concerns. Moreover, the company withdrew its 2020 guidance due to the negative impact of the coronavirus outbreak. Reduced client demand and delays in delivery on account of remote working in India and the Philippines are expected to affect Cognizant's top line. Notably, shares have underperformed the industry on a year-to-date basis.

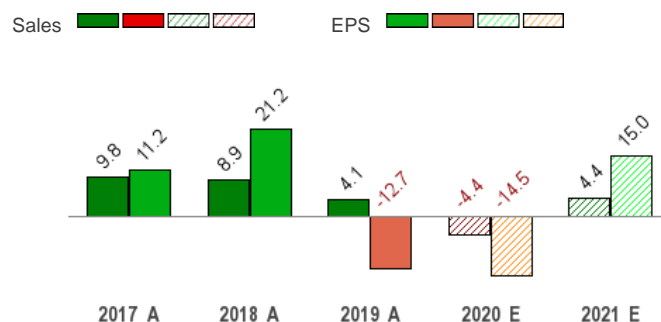
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$71.48 - \$40.01
20 Day Average Volume (sh)	3,785,801
Market Cap	\$31.3 B
YTD Price Change	-6.8%
Beta	1.15
Dividend / Div Yld	\$0.88 / 1.5%
Industry	Business - Software Services
Zacks Industry Rank	Bottom 45% (140 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	4.4%
Last Sales Surprise	-0.1%
EPS F1 Est- 4 week change	-6.9%
Expected Report Date	07/29/2020
Earnings ESP	-7.4%
P/E TTM	14.3
P/E F1	17.0
PEG F1	1.7
P/S TTM	1.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	4,094 E	4,117 E	4,174 E	4,273 E	16,735 E
2020	4,225 A	3,816 E	3,937 E	4,072 E	16,037 E
2019	4,110 A	4,141 A	4,248 A	4,284 A	16,783 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.89 E	\$0.92 E	\$0.96 E	\$1.01 E	\$3.92 E
2020	\$0.96 A	\$0.69 E	\$0.81 E	\$0.88 E	\$3.41 E
2019	\$0.91 A	\$0.94 A	\$1.08 A	\$1.07 A	\$3.99 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 06/05/2020. The reports text is as of 06/08/2020.

Overview

Headquartered in Teaneck, NJ, Cognizant Technology Solutions Corporation is a leading professional services company. The company was spun off from Dun & Bradstreet in 1996 and went public in 1998.

Cognizant's services include digital services and solutions, consulting, application development, systems integration, application testing, application maintenance, infrastructure services, and business process services.

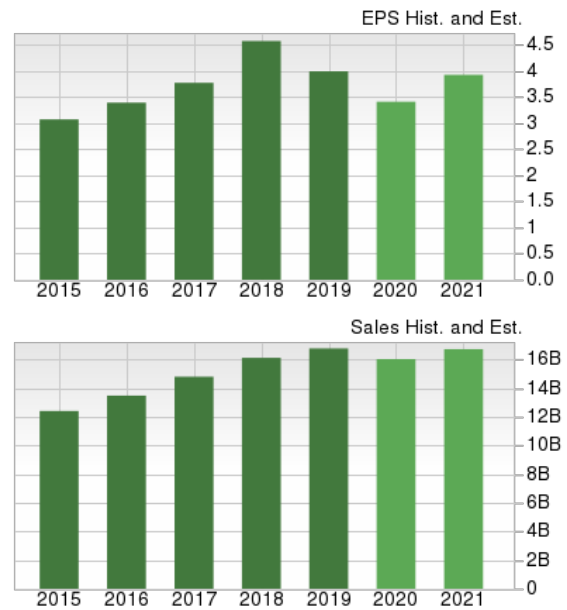
Cognizant reported revenues of \$16.78 billion in 2019.

The company primarily serves four domains: Financial Services (Banking and Insurance), Healthcare (Healthcare and Life Sciences), Products & Resources (Manufacturing & Logistics, Retail & Consumer Goods, Travel & Hospitality and Energy & Utilities) and Communications, Media & Technology (Communications & Media and Technology).

In 2019, Financial Services accounted for 35% of revenues. Healthcare, Products & Resources, Communications, and Media & Technology accounted for 28%, 22.4% and 14.6% of revenues, respectively.

At the end of 2019, Cognizant had roughly 292,500 employees.

Cognizant faces significant competition from the likes of Accenture, Atos, Capgemini, Deloitte Digital, DXC Technology, EPAM Systems, Genpact, HCL Technologies, IBM Global Services, Infosys Technologies, Tata Consultancy Services, Wipro and numerous local providers.



Reasons To Buy:

- ▲ Cognizant is consistently developing its capabilities to benefit from the ongoing digital transition especially when it comes to integration of the new digital framework with legacy technology platforms. Its Digital Works platform is designed to aid such business transformations. The company's continuing investments to extend its digital capabilities, including the extensive training and re-skilling of its technical teams, is a key catalyst. Cognizant is also expected to continue expansion of its local workforces in the United States and other markets around the world. These efforts are expected to boost organic revenue growth. Moreover, increasing revenue contribution from the higher margin digital services is expected to drive profitability in the long haul.
- ▲ Over the past few years, Cognizant outpaced its Tier-1 peers as it has more exposure to the fast-growing verticals, like Financial Services and Healthcare. The company has gained deep industry expertise and knowledge of the domain through partnerships with top firms. This strategy has enabled it to deliver more value to clients and capitalize on new opportunities. Additionally, the new slate of domestic and international regulations, particularly in the financial services and healthcare industries, is a key catalyst.
- ▲ Moreover, acquisitions of Bolder Healthcare, Hedera Consulting, Softvision, Advanced Technology Group (ATG), and SaaSfocus are strengthening the company's digital capabilities and clientele. Additionally, these acquisitions have helped the company expand in countries like Belgium, the Netherlands, Romania and Australia. The acquisition of Meritsoft not only strengthens Cognizant's SaaS portfolio but also expands its footprint among financial institutions. Notably, Meritsoft's FINBOS platform for post-trade processing, an automation solution for managing taxes, fees, commissions and cash flows, is popular among financial institutions.
- ▲ Cognizant is expected to continue to benefit from strong demand for high quality, lower cost technology services. Based on its global delivery model and expanding capacity in low cost areas in India, Philippines and Latin America, the company remains well-positioned in the outsourcing market. Moreover, its realignment program and other margin enhancement initiatives are expected to boost profitability.
- ▲ Notably, Cognizant drew \$1.74 billion from its revolving credit facility on Mar 23 to strengthen the company's financial flexibility. This brought total cash and investment balance as of Mar 31 to \$4.7 billion or net cash of \$2.2 billion. The company had cash and cash equivalents (and short-term investments) of \$3.42 billion as of Dec 31, 2019. The improved liquidity will help Cognizant easily meet its working capital requirements. Notably, the company has no significant debt maturities until 2023. Additionally, times interest earned is 99.8X much higher than industry's 19X as of Mar 31, 2020.

Cognizant benefits from domain expertise, expanding clientele and accretive acquisitions that are strengthening its digital capabilities.

Reasons To Sell:

- ▼ Cognizant is exposed to significant geographic concentration risks. North America contributes most of the revenues. Hence, any slowdown in the region's economic environment will hurt the company's revenue growth. Moreover, Cognizant earns more than 35% of revenues from the financial services industry. Sluggish spending by top banking customers negatively impacted financial services segment growth throughout 2019. As the trend is expected to continue in the near term, Cognizant's top-line growth is anticipated to suffer.
- ▼ Competition is intense in the IT services industry. The company's direct competitors, including Infosys Technologies, Tata Consultancy Services and Wipro, utilized an integrated global delivery business model as opposed to the hybrid-model used by Cognizant. The company also competes with large IT service providers with greater resources, such as Accenture, HP Enterprise and IBM Global Services.
- ▼ Employees are the primary resource for a company like Cognizant. But there is significant competition for highly skilled and efficient personnel, so the company remains under pressure to raise wages and control the attrition rate. Though Cognizant is investing heavily to retain the best talent around the world, we think employee turnover remains a concern as the offshore staff continues to expand. Though the company has been taking initiatives to retain employees, its attrition rates are still higher than preferred.
- ▼ An additional concern for the company relates to the nature of its business, which necessitates bringing employees into the U.S. for on-site application maintenance work. With continuous pressure from the U.S. government under Donald Trump to limit immigration, there has been an increase in the number of H1-B visa application rejections and delays in processing such applications. This doesn't bode well for Cognizant's operations.

Cognizant is exposed to significant geographic, domain concentration risks amid a stiff competition from peers.

Last Earnings Report

Cognizant Q1 Earnings Beat, Revenues Rise Y/Y

Cognizant Technology Solutions reported first-quarter 2020 non-GAAP earnings of 96 cents per share that beat the Zacks Consensus Estimate by 4.3%. Moreover, the figure increased 5.5% from the year-ago quarter.

First-quarter revenues of \$4.22 billion matched the consensus mark. The figure improved 3.5% year over year at constant currency (cc).

COVID-19-related disruptions reduced revenues in March, reflecting delays in project fulfillment as Cognizant rapidly enabled the shift to work-from-home capabilities across its delivery teams.

Quarter Ending **03/2020**

Report Date	May 07, 2020
Sales Surprise	-0.05%
EPS Surprise	4.35%
Quarterly EPS	0.96
Annual EPS (TTM)	4.05

Quarter Details

Segment-wise, Financial services (34.3% of revenues) grew 1.8% on a year-over-year basis at cc to \$1.45 billion, primarily driven by insurance.

Moreover, growth in banking sector was stable, driven by the partnership with three Finnish financial institutions to transform and operate a shared core banking platform and regional banks in North America. The growth was partially offset by softness at some of Cognizant's largest banking and insurance clients.

Healthcare (28.3% of revenues) increased 2.7% year over year at cc to \$1.19 billion. The upside was driven by double-digit growth in life sciences and the contribution of Zenith Technologies, which was acquired in July 2019.

However, healthcare growth was partially offset by the negative impact of industry consolidation and the movement of work to a captive at a large North American client.

Products and Resources' (22.6% of revenues) momentum continued. Revenues increased 5.3% year over year at cc to \$954 million, driven by growth in retail and consumer goods, and manufacturing, logistics, energy and utilities, partially offset by softness in the travel and hospitality industries.

Communications, Media and Technology revenues (14.8% of revenues) were \$626 million, up 6.3% from the year-ago quarter at cc, driven by broad-based growth across all industries in this segment.

However, technology revenue growth was hurt by the company's decision to exit certain portions of its content services business.

Consulting & Technology services accounted for 60.3% of revenues. Outsourcing services contributed 39.7% of revenues. Additionally, roughly 36.8% of Cognizant's revenues were from fixed-price contracts.

Region-wise, revenues from North America increased 2.2% year over year at cc and represented 75.5% of total revenues.

Revenues from Europe increased 7.6% from the year-ago quarter at cc and accounted for 18.3% of total revenues. Rest of the World revenues rose 3.5% at cc and represented 6.2% of total revenues.

Operating Details

Selling, general & administrative (SG&A) expenses, as a percentage of revenues, contracted 290 basis points (bps) from the year-ago quarter to 18.2%.

Headcount increased 2.1% year over year. Quarterly annualized attrition was 22%, up 3% year over year and 1% sequentially.

Cognizant reported non-GAAP operating margin of 15.1%, which was flat year over year.

Balance Sheet

Notably, Cognizant drew \$1.74 billion from its revolving credit facility on Mar 23 to strengthen the company's financial flexibility. This brought total cash and investment balance as of Mar 31 to \$4.7 billion or net cash of \$2.2 billion.

The company had cash and cash equivalents (and short-term investments) of \$3.42 billion as of Dec 31, 2019.

Cognizant generated \$497 million in cash from operations compared with \$938 million reported in the previous quarter.

Notably, the company has no significant debt maturities until 2023. As of Mar 31, 2020, the company had a long-term debt of \$2.43 billion, up from \$700 million as of Dec 31, 2019.

Free cash flow was \$385 million compared with \$845 million reported in the previous quarter.

Cognizant bought back 8.5 million shares in the first quarter.

Guidance

Management expects revenues to remain volatile and uncertain, with particular weakness in demand in the second quarter, given additional impact of the ransomware incident of around \$50-70 million.

In late April, the company announced a security incident involving its internal systems resulting from a Maze ransomware attack.

On Apr 9, Cognizant withdrew its 2020 guidance for revenues and earnings in anticipation of the long-term impact of coronavirus outbreak on its business.

The company expects adjusted operating margin below 16-17% in 2020 and a strong balance sheet, including net cash of \$1.8 billion.

Recent News

On Jun 1, Cognizant announced completion of the acquisition of the French operations of EI-Technologies, a Paris-based digital technology consulting firm and Salesforce specialist.

On May 27, Cognizant was named a Leader by Gartner in its 2020 Magic Quadrant for Public Cloud Infrastructure Professional and Managed Services, Worldwide report, based on its completeness of vision and ability to execute.

On May 7, Cognizant announced that it had contained the ransomware attack announced in April 2020.

On May 5, Cognizant entered into an agreement to acquire Collaborative Solutions, a privately-held global consultancy specializing in Workday enterprise cloud applications for finance and human resources. The transaction is expected to close in the second quarter of 2020, subject to the satisfaction of certain closing conditions, including regulatory clearance. The financial details were not disclosed.

On Apr 1, Cognizant announced an initial \$10 million philanthropic commitment to support communities across the globe in addressing the immediate and long-term impacts of COVID-19.

On Mar 23, Cognizant announced that it has entered into an agreement to acquire Lev, a privately-held, digital marketing consultancy in the United States to further expand Cognizant's Salesforce practice.

Valuation

Cognizant shares are down 6.8% in the year-to-date period and 8.3% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Computer & Technology sector are up 7.2% and 8% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 8.9% and 23.5%, respectively.

The S&P 500 index is down 1% in the year-to-date period while up 10.5% in the past year.

The stock is currently trading at 15.92X forward 12-month earnings, which compares to 25.39X for the Zacks sub-industry, 25.07X for the Zacks sector and 23.07X for the S&P 500 index.

Over the past five years, the stock has traded as high as 23.05X and as low as 10.04X, with a 5-year median of 17.37X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$61 price target reflects 16.72X forward 12-month earnings.

The table below shows summary valuation data for CTSH

Valuation Multiples - CTSH					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	15.92	25.39	25.07	23.07
	5-Year High	23.05	25.39	25.07	23.07
	5-Year Low	10.04	7.29	16.72	15.23
	5-Year Median	17.37	21.77	19.28	17.49
P/S F12M	Current	1.91	10.44	3.82	3.59
	5-Year High	3.11	10.44	3.82	3.59
	5-Year Low	1.29	6.88	2.32	2.53
	5-Year Median	2.43	8.45	3.11	3.02
EV/EBITDA TTM	Current	8.84	47.27	12.32	11.82
	5-Year High	16.78	51.42	12.72	12.85
	5-Year Low	6.34	33.43	7.57	8.25
	5-Year Median	10.75	42.38	10.73	10.8

As of 06/05/2020

Industry Analysis Zacks Industry Rank: Bottom 45% (140 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Accenture PLC (ACN)	Neutral	3
Automatic Data Processing, Inc. (ADP)	Neutral	3
EPAM Systems, Inc. (EPAM)	Neutral	4
Genpact Limited (G)	Neutral	3
International Business Machines Corporation (IBM)	Neutral	3
Infosys Limited (INFY)	Neutral	3
Wipro Limited (WIT)	Neutral	3
DXC Technology Company. (DXC)	Underperform	5

Industry Comparison Industry: Business - Software Services				Industry Peers		
	CTSH	X Industry	S&P 500	ACN	INFY	WIT
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	4	-	-	3	3	3
VGM Score	B	-	-	A	A	B
Market Cap	31.26 B	7.68 B	23.09 B	132.53 B	39.78 B	18.95 B
# of Analysts	10	4	14	11	8	4
Dividend Yield	1.52%	0.00%	1.82%	1.53%	2.19%	0.42%
Value Score	B	-	-	B	B	A
Cash/Price	0.15	0.08	0.06	0.04	0.08	0.24
EV/EBITDA	9.74	13.31	13.17	18.10	11.15	7.07
PEG Ratio	1.70	1.74	3.13	2.75	1.88	1.74
Price/Book (P/B)	2.95	5.10	3.15	8.32	4.57	2.55
Price/Cash Flow (P/CF)	11.48	24.67	12.43	23.39	14.53	12.11
P/E (F1)	17.18	33.38	22.80	27.53	18.76	15.67
Price/Sales (P/S)	1.85	3.11	2.52	2.97	3.11	2.22
Earnings Yield	5.90%	2.67%	4.19%	3.63%	5.33%	6.31%
Debt/Equity	0.30	0.28	0.76	0.17	0.00	0.01
Cash Flow (\$/share)	5.04	2.23	7.01	8.91	0.65	0.28
Growth Score	A	-	-	A	A	C
Hist. EPS Growth (3-5 yrs)	10.74%	16.78%	10.87%	11.33%	5.16%	1.99%
Proj. EPS Growth (F1/F0)	-14.59%	-14.07%	-10.79%	2.90%	-9.09%	-3.41%
Curr. Cash Flow Growth	-2.96%	9.60%	5.48%	8.06%	4.82%	-1.07%
Hist. Cash Flow Growth (3-5 yrs)	10.46%	14.18%	8.55%	9.75%	4.59%	-3.45%
Current Ratio	2.90	1.62	1.29	1.38	2.62	2.40
Debt/Capital	22.97%	22.97%	44.75%	14.34%	0.00%	0.86%
Net Margin	10.46%	4.35%	10.59%	11.13%	18.24%	15.95%
Return on Equity	20.90%	9.99%	16.26%	32.87%	27.34%	17.57%
Sales/Assets	1.04	0.74	0.55	1.43	1.05	0.74
Proj. Sales Growth (F1/F0)	-4.44%	-2.97%	-2.61%	2.81%	-3.30%	-6.71%
Momentum Score	F	-	-	A	B	B
Daily Price Chg	3.99%	1.45%	2.89%	2.65%	1.19%	0.60%
1 Week Price Chg	3.01%	2.33%	4.60%	4.08%	0.55%	11.82%
4 Week Price Chg	-1.60%	8.31%	15.60%	11.43%	3.76%	10.63%
12 Week Price Chg	18.05%	30.48%	29.34%	36.69%	16.52%	15.63%
52 Week Price Chg	-6.59%	11.26%	2.76%	15.57%	-10.92%	-25.17%
20 Day Average Volume	3,785,801	563,336	2,537,324	2,011,713	10,215,892	1,092,411
(F1) EPS Est 1 week change	-0.93%	0.00%	0.00%	0.00%	0.00%	1.19%
(F1) EPS Est 4 week change	-6.94%	0.00%	-0.08%	0.02%	0.00%	1.19%
(F1) EPS Est 12 week change	-16.15%	-21.49%	-16.19%	-3.27%	-16.25%	-12.37%
(Q1) EPS Est Mthly Chg	-17.16%	0.00%	0.00%	-0.05%	0.00%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	A
Momentum Score	F
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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