

ADD

TP: Rs 1,540 | ▲ 7%

MINDTREE

| IT Services

| 04 December 2020

Analyst meet takeaways – 4×4×4 strategy laid out

Mindtree (MTCL) is optimistic about achieving above-industry growth, aided by a new three-year '4×4×4' strategy aimed at narrowing its focus on four verticals, service lines and markets each. With margins now at a comfortable level, management will not shy away from acquisitions. The L&T management clarified that an LTI-MTCL merger is not on the cards in the midterm. We see limited valuation upside given flattish growth in the CMT vertical (0.7% QoQ in Q2FY21). Retain ADD with a Sep'21 TP of Rs 1,540 on a target P/E of 21.5x.

Ruchi Burde | Seema Nayak

research@bobcaps.in

4×4×4 strategy over three years: Management intends to follow a broad strategic path of (1) building on existing strengths, (2) enhanced focus on growth opportunities, and (3) developing strategic relationships. As part of its 4x4x4 roadmap, MTCL's focus will be narrowed to four industry groups (retail-CPG-manufacturing, BFSI, TTHL, and communication, media & technology or CMT), four service lines (customer service, data & intelligence, cloud, and enterprise IT) and four geographies (US, Continental Europe, UK & Ireland, and APAC (mostly Australia, New Zealand and India)).

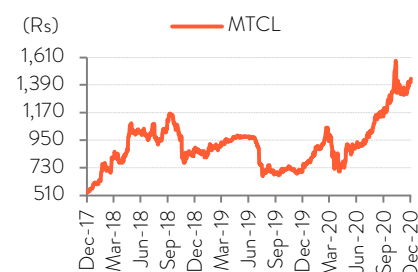
Management plans to rejuvenate the consulting arm to stitch together service lines for large deals. It also intends to align the delivery engine to the four new focus geographies.

New healthcare vertical: To tap into increased demand coming from the healthcare sector post the Covid outbreak, MTCL will be carving out a new vertical that is currently in its incubation phase. This healthcare vertical will focus on payers, device manufacturers and insurance providers, but will stay away from life sciences. Work here has already begun with a few large deals coming from insurance providers and medical device manufacturers.

Ticker/Price	MTCL IN/Rs 1,442
Market cap	US\$ 3.2bn
Shares o/s	165mn
3M ADV	US\$ 29.3mn
52wk high/low	Rs 1,606/Rs 692
Promoter/FPI/DII	74%/11%/15%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	70,215	77,643	79,171	91,883	100,695
EBITDA (Rs mn)	10,645	10,623	15,286	18,377	19,650
Adj. net profit (Rs mn)	7,542	6,309	9,698	11,511	12,354
Adj. EPS (Rs)	45.8	38.3	58.9	69.9	75.0
Adj. EPS growth (%)	32.1	(16.3)	53.7	18.7	7.3
Adj. ROAE (%)	24.9	19.5	28.2	28.4	26.1
Adj. P/E (x)	31.5	37.6	24.5	20.6	19.2
EV/EBITDA (x)	22.2	22.2	15.3	12.4	11.3

Source: Company, BOBCAPS Research

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Other analyst meet takeaways

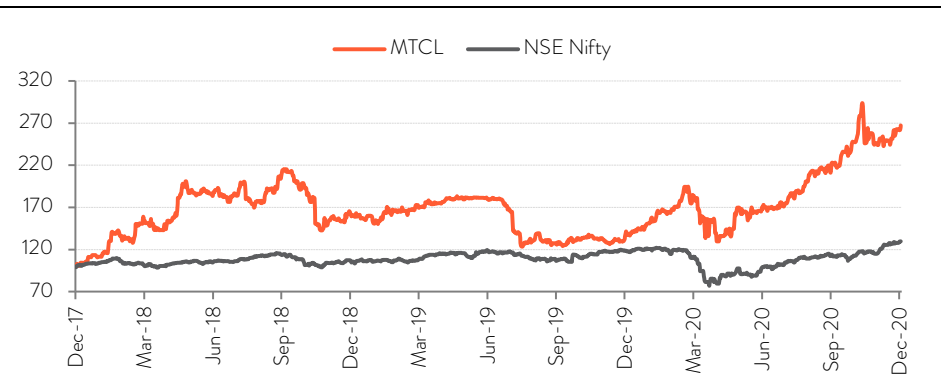
- Client priorities have shifted in the wake of the pandemic to cash conservation, business resilience, digital acceleration and cost realignment. IT services is seeing a shift from a capex to opex model. Vendor consolidation, cloud migration, process automation, remote working evolution, no-shore agile projects, remote project transition, and focus on cybersecurity are some of the key trends.
- MTCL continues to focus on profitable growth through top account mining, enterprise-level digital transformation, multiyear annuity deals, seamless delivery, targeted partnerships, and M&A. Its current pipeline consists of large deals cutting across service lines.
- To increase efficiency, MTCL focuses on using bots for manual and repetitive tasks in the BFSI vertical.
- More top-level management personnel are being hired from tier-I IT companies in an effort to bring scalability.
- Two-third of total employees have shown increased productivity during remote work.

Valuation methodology

Management is confident of its pipeline for the next couple of quarters. After flattish dollar revenue growth of 0.7% QoQ in CMT (~50% of revenues) in Q2FY21, MTCL expects the vertical to regain momentum. However, we see limited possibility for growth outside the top client in the CMT vertical. In our view, demand from the top client will also normalise following the spike in Q1FY21.

We keep our EPS estimates unchanged and maintain our Sep'21 target price of Rs 1,540, set at a target one-year forward P/E of 21.5x. Retain ADD considering limited upside on current rich trading valuations of 27x.

FIG 1 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Key downside risks to our estimates are:

- revenue contraction from large clients,
- sell-off in mid-caps, and
- operating margin reverting to previous levels.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	70,215	77,643	79,171	91,883	100,695
EBITDA	10,645	10,623	15,286	18,377	19,650
Depreciation	1,641	2,754	2,422	2,813	3,119
EBIT	9,004	7,869	12,863	15,564	16,532
Net interest income/(expenses)	(29)	(529)	(563)	(680)	(720)
Other income/(expenses)	894	948	890	885	1,228
Exceptional items	0	0	0	0	0
EBT	9,869	8,288	13,191	15,768	17,040
Income taxes	2,327	1,979	3,493	4,257	4,686
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
Reported net profit	7,542	6,309	9,698	11,511	12,354
Adjustments	0	0	0	0	0
Adjusted net profit	7,542	6,309	9,698	11,511	12,354

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	0	0	0	0	0
Other current liabilities	7,330	17,690	19,522	22,656	24,829
Provisions	1,399	2,304	1,735	2,014	2,207
Debt funds	0	0	0	0	0
Other liabilities	0	0	0	0	0
Equity capital	1,642	1,642	1,642	1,642	1,642
Reserves & surplus	31,419	29,926	35,543	42,205	49,355
Shareholders' fund	33,061	31,568	37,185	43,847	50,997
Total liabilities and equities	41,790	51,562	58,442	68,517	78,033
Cash and cash eq.	2,562	5,870	11,365	19,946	28,365
Accounts receivables	13,356	14,389	16,268	17,621	19,311
Inventories	0	0	0	0	0
Other current assets	6,634	5,107	5,423	6,293	6,897
Investments	8,036	7,748	7,748	7,748	7,748
Net fixed assets	9,966	13,469	12,550	11,297	9,739
CWIP	297	136	136	136	136
Intangible assets	4,732	4,732	4,732	4,732	4,732
Deferred tax assets, net	388	1,835	1,835	1,835	1,835
Other assets	848	3,148	3,254	3,776	4,138
Total assets	41,790	51,566	58,442	68,518	78,034

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	6,927	9,063	12,120	14,324	15,472
Interest expenses	(117)	(419)	(327)	(205)	(508)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(2,360)	9,459	(1,037)	667	(290)
Other operating cash flows	1,855	(10,349)	0	0	0
Cash flow from operations	6,305	7,754	10,756	14,786	14,675
Capital expenditures	(1,708)	(1,496)	(1,504)	(1,560)	(1,560)
Change in investments	(301)	0	0	0	0
Other investing cash flows	209	419	327	205	508
Cash flow from investing	(1,800)	(1,077)	(1,176)	(1,355)	(1,052)
Equities issued/Others	3	0	0	0	0
Debt raised/repaid	(3,004)	0	0	0	0
Interest expenses	(37)	0	0	0	0
Dividends paid	(2,180)	(3,369)	(4,085)	(4,849)	(5,204)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(5,218)	(3,369)	(4,085)	(4,849)	(5,204)
Changes in cash and cash eq.	(713)	3,308	5,494	8,582	8,419
Closing cash and cash eq.	2,562	5,870	11,365	19,946	28,365

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	45.8	38.3	58.9	69.9	75.0
Adjusted EPS	45.8	38.3	58.9	69.9	75.0
Dividend per share	33.0	17.0	20.6	24.5	26.3
Book value per share	200.8	191.7	225.8	266.3	309.7

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	3.4	3.0	2.9	2.5	2.2
EV/EBITDA	22.2	22.2	15.3	12.4	11.3
Adjusted P/E	31.5	37.6	24.5	20.6	19.2
P/BV	7.2	7.5	6.4	5.4	4.7

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	76.4	76.1	73.5	73.0	72.5
Interest burden (PBT/EBIT)	109.6	105.3	102.5	101.3	103.1
EBIT margin (EBIT/Revenue)	12.8	10.1	16.2	16.9	16.4
Asset turnover (Revenue/Avg TA)	177.4	166.3	143.9	144.7	137.4
Leverage (Avg TA/Avg Equity)	1.3	1.4	1.6	1.6	1.5
Adjusted ROAE	24.9	19.5	28.2	28.4	26.1

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	28.5	10.6	2.0	16.1	9.6
EBITDA	43.8	(0.2)	43.9	20.2	6.9
Adjusted EPS	32.1	(16.3)	53.7	18.7	7.3
Profitability & Return ratios (%)					
EBITDA margin	15.2	13.7	19.3	20.0	19.5
EBIT margin	12.8	10.1	16.2	16.9	16.4
Adjusted profit margin	10.7	8.1	12.2	12.5	12.3
Adjusted ROAE	24.9	19.5	28.2	28.4	26.1
ROCE	31.2	27.9	49.8	62.4	70.9
Working capital days (days)					
Receivables	61	65	71	67	67
Inventory	0	0	0	0	0
Payables	40	68	106	105	107
Ratios (x)					
Gross asset turnover	7.2	6.6	6.1	7.7	9.6
Current ratio	2.7	1.4	1.7	1.9	2.2
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	(0.1)	(0.2)	(0.3)	(0.5)	(0.6)

Source: Company, BOBCAPS Research

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

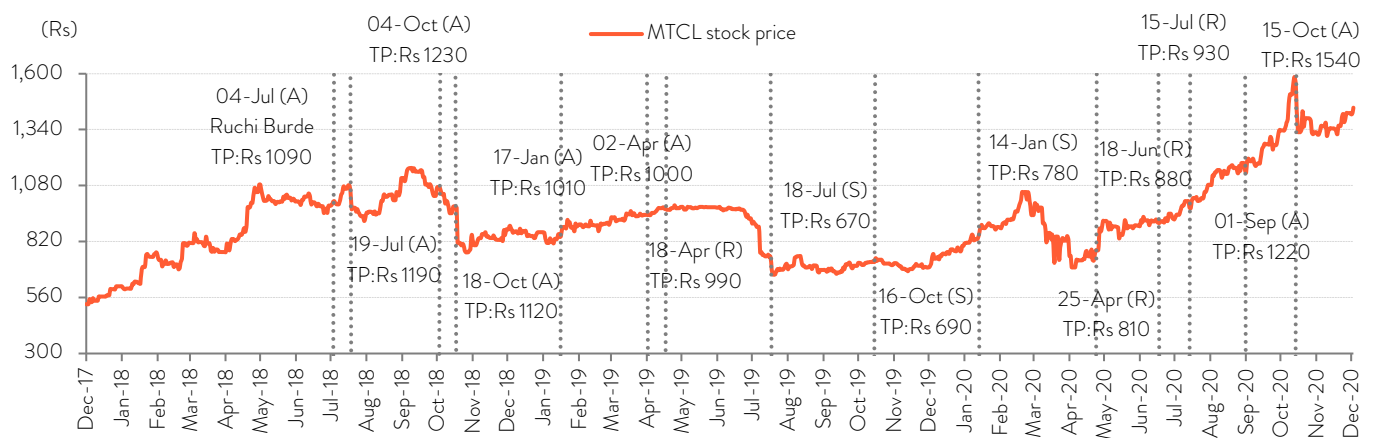
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): MINDTREE (MTCL IN)



B – Buy, A – Add, R – Reduce, S – Sell

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