

**ADD**

TP: Rs 1,850 | ▲ 11%

**MINDTREE**

| IT Services

| 18 January 2021

## Good growth; onset of a positive cycle

**Mindtree (MTCL) reported a strong Q3FY21 performance with dollar revenue growth of 5% QoQ and EBIT margin at an all-time high of 19.6% (+230bps QoQ). Management expects continued margin resilience in the near term despite impending wage hikes. Deal wins were healthy at US\$ 312mn. We raise FY21/FY22/FY23 EPS by 12%/11%/8% on higher margin assumptions and hike our target P/E to 23.4x (vs. 21x). Rolling valuations over, we have a revised Dec'21 TP of Rs 1,850 (vs. Rs 1,540). Retain ADD.**

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**Travel and manufacturing recovery:** MTCL's dollar revenue increased 5% QoQ vs. 3.6% estimated, its highest third-quarter growth in a decade, driven by 12.6% growth in travel, media and services and a 5.5% uptick in manufacturing. Q3 marked a large deal win from a large airline. BFSI was flattish, up ~1%. TCV at US\$ 312mn rose 3% QoQ and 51% YoY. The 9M order book has crossed the US\$ 1bn mark. Overall, MTCL delivered growth on par with tier-I IT players.

Ticker/Price	MTCL IN/Rs 1,664
Market cap	US\$ 3.7bn
Shares o/s	165mn
3M ADV	US\$ 23.9mn
52wk high/low	Rs 1,780/Rs 692
Promoter/FPI/DII	74%/11%/15%

Source: NSE

**Margins surprise:** EBIT margin was at an all-time high of 19.6% (+230bps QoQ) aided by good topline growth and higher gross margins. Utilisation was also at an all-time high of 83.4%, up 430bps QoQ. Q4 will see headwinds from pending salary hikes, but management is confident of delivering a 20%+ EBITDA margin nevertheless. MTCL has embarked on a positive cycle following new CEO takeover, resulting in elevated margins due to an aggressive focus on profitable growth (using levers such as utilisation, offshoring, deep account mining and rationalisation of long-tail).

## STOCK PERFORMANCE



Source: NSE

**Healthy pipeline; positive outlook:** Per management, demand has grown in the areas of simplification of operations, cost takeout, vendor consolidation and customer experience. MTCL's new 4\*4\*4 strategy has received a good client response. Management anticipates a healthy deal win ratio and pipeline.

## KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	70,215	77,643	80,109	94,876	105,993
EBITDA (Rs mn)	10,645	10,623	16,449	20,011	20,930
Adj. net profit (Rs mn)	7,542	6,309	10,867	12,816	13,330
Adj. EPS (Rs)	45.8	38.3	66.0	77.8	81.0
Adj. EPS growth (%)	32.1	(16.3)	72.3	17.9	4.0
Adj. ROAE (%)	24.9	19.5	31.3	30.8	27.1
Adj. P/E (x)	36.3	43.4	25.2	21.4	20.5
EV/EBITDA (x)	25.6	25.6	16.4	13.2	12.3

Source: Company, BOBCAPS Research

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## Other highlights

- Top client revenues grew 3.6% QoQ (23% YoY) vs. a 1% decline in Q2FY21. Management plans to broaden growth outside the top client by way of strong account mining among the rest of the top-10 bracket. MTCL expects to expand growth through inorganic means as well.
- DSO decreased to 61 days, declining by 4 days QoQ due to strong collections.
- Attrition at 12.5% declined 130bps QoQ.

### FIG 1 – QUARTERLY PERFORMANCE

(Rs mn)	Q3FY21	Q3FY20	YoY (%)	Q2FY21	QoQ (%)	9MFY21	9MFY20	YoY (%)
<b>Revenues (US\$ mn)</b>	<b>274.1</b>	<b>275.2</b>	<b>(0.4)</b>	<b>261.0</b>	<b>5.0</b>	<b>788</b>	<b>810</b>	<b>(2.7)</b>
<b>Revenue</b>	<b>20,237</b>	<b>19,653</b>	<b>3.0</b>	<b>19,260</b>	<b>5.1</b>	<b>58,585</b>	<b>57,138</b>	<b>2.5</b>
Operating Expenditure	15,558	16,590	(6.2)	15,357	1.3	46,785	49,752	(6.0)
Cost of revenues	12,610	12,535	0.6	12,623	(0.1)	38,011	37,714	0.8
as % of sales	62.3	63.8	-	65.5	-	64.9	66.0	-
SG&A expenses	2,948	4,055	(27.3)	2,734	7.8	8,774	12,038	(27.1)
as % of sales	14.6	20.6	(29.4)	14.2	-	15.0	21.1	-
<b>EBITDA</b>	<b>4,679</b>	<b>3,063</b>	<b>52.8</b>	<b>3,903</b>	<b>19.9</b>	<b>11,800</b>	<b>7,386</b>	<b>59.8</b>
Depreciation	717	699	2.6	569	26.0	1,883	2,075	(9.3)
<b>EBIT</b>	<b>3,962</b>	<b>2,364</b>	<b>67.6</b>	<b>3,334</b>	<b>18.8</b>	<b>9,917</b>	<b>5,311</b>	<b>86.7</b>
Other Income	489	215	127.4	113	332.7	877	364	140.9
PBT	4,451	2,579	72.6	3,447	29.1	10,794	5,675	90.2
Total Tax	1,186	609	94.7	910	30.3	2,864	1,428	100.6
<b>Adjusted PAT</b>	<b>3,265</b>	<b>1,970</b>	<b>65.7</b>	<b>2,537</b>	<b>28.7</b>	<b>7,930</b>	<b>4,247</b>	<b>86.7</b>
Other comprehensive income/(loss)	714	77	-	1402	-	3,010	(15)	-
APAT after MI	3,979	2,047	94.4	3,939	1.0	10,940	4,232	158.5
Extra ordinary items	0	0	-	0	-	0	0	-
Reported PAT	3,979	2,047	94.4	3,939	1.0	10,046	4,324	132.3
Reported EPS	19.8	12.0	65.7	15.4	28.7	48	26	86.7
<b>Margins (%)</b>			<b>(bps)</b>		<b>(bps)</b>			<b>(bps)</b>
EBITDA	23.1	15.6	750	20.3	290	20.1	12.9	720
EBIT	19.6	12.0	750	17.3	230	16.9	9.3	760
EBT	22.0	13.1	890	17.9	410	18.4	9.9	850
PAT	19.7	10.4	920	20.5	(80)	18.7	7.4	1,130
Effective Tax rate	26.6	23.6	300	26.4	20	26.5	25.2	140

Source: BOBCAPS Research

**FIG 2 – OPERATING METRICS**

(in US\$ terms)	Q3FY21 (% Contr. to Revenue)	QoQ (%)	YoY (%)
Deal wins	312	3.0	50.7
<b>Revenue breakup by Geography</b>			
North America	77.2	4.7	3.1
Europe	15.2	3.7	(10.9)
<b>Revenue breakup by Vertical</b>			
Communications, media and technology	49.9	5.2	19.8
BFSI	19.6	0.9	(8.3)
Manufacturing & Retail	21.6	5.5	4.4
Travel, Media and Services	8.9	12.6	(46.6)
<b>Client concentration</b>			
Top Client	28.5	3.6	22.9
Top 5 Clients	39.8	2.9	9.8
Top 10 Clients	49.0	4.2	7.0
Non-Top 10 Clients	51.0	5.8	(6.6)

Source: BOBCAPS Research

## Valuation methodology

MTCL's operating margin recovery following change of ownership is tracking ahead of expectations. We raise our FY21/FY22/FY23 EPS estimates by 12%/11%/8% as we believe the company is embarking on a phase of stable, high margins due to its aggressive focus on profitable growth. EBITDA margin is forecast to remain at 20%+ levels as management is focused on reskilling (instead of increasing hiring) and boosting utilisation (to be maintained at 80%+).

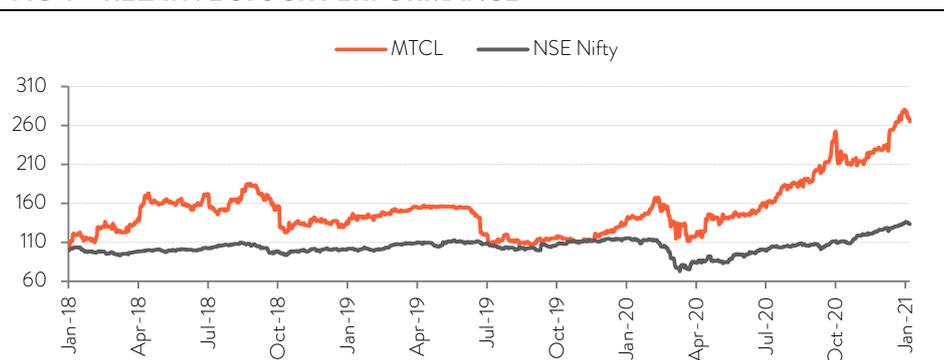
Rolling valuations forward, we have a revised Dec'21 target price of Rs 1,850 (Rs 1,540 earlier), set at a new target P/E of 23.4x (21x earlier) which is +1sd to the last five-year average. MTCL has substantial exposure to the technology vertical (~50% of revenue with a chunk coming from the top client), which is less vulnerable to Covid-19 headwinds and has helped it maintain growth momentum. Reiterate ADD.

**FIG 3 – REVISED ESTIMATES**

(Rs mn)	FY21E			FY22E			FY23		
	Old	New	Change (%)	Old	New	Change (%)	Old	New	Change (%)
Overall Revenues (US\$ mn)	1,053	1,075	2.1	1,178	1,240	5.3	1,291	1,359	5.3
YoY growth (%)	(3.3)	(1.2)	-	11.9	15.3	-	9.6	9.6	-
Revenues	79,171	80,109	1.2	91,883	94,876	3.3	100,695	105,993	5.3
EBITDA	15,286	16,449	7.6	18,377	20,011	8.9	19,650	20,930	6.5
EBITDA margins (%)	19.3	20.5	-	20.0	21.1	-	19.5	19.7	-
Net profits	9,698	10,867	12.1	11,511	12,816	11.3	12,354	13,330	7.9
EPS (Rs)	58.9	66.0	12.1	69.9	77.8	11.3	75.0	81.0	7.9

Source: BOBCAPS Research

**FIG 4 – 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
- margin reverting to previous levels.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
<b>Total revenue</b>	<b>70,215</b>	<b>77,643</b>	<b>80,109</b>	<b>94,876</b>	<b>105,993</b>
EBITDA	10,645	10,623	16,449	20,011	20,930
Depreciation	1,641	2,754	2,511	2,807	3,110
EBIT	9,004	7,869	13,938	17,203	17,820
Net interest income/(expenses)	(29)	(529)	(540)	(680)	(720)
Other income/(expenses)	894	948	1,387	914	1,286
Exceptional items	0	0	0	0	0
EBT	9,869	8,288	14,785	17,437	18,386
Income taxes	2,327	1,979	3,918	4,621	5,056
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	0	0	0	0	0
<b>Reported net profit</b>	<b>7,542</b>	<b>6,309</b>	<b>10,867</b>	<b>12,816</b>	<b>13,330</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>7,542</b>	<b>6,309</b>	<b>10,867</b>	<b>12,816</b>	<b>13,330</b>

### 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	19,753	23,394	26,135
Provisions	1,399	2,304	1,756	2,079	2,323
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	36,220	43,638	51,352
Shareholders' fund	33,061	31,568	37,862	45,280	52,994
<b>Total liabilities and equities</b>	<b>41,790</b>	<b>51,562</b>	<b>59,370</b>	<b>70,753</b>	<b>81,453</b>
Cash and cash eq.	2,562	5,870	12,100	21,407	30,306
Accounts receivables	13,356	14,389	16,461	18,195	20,327
Inventories	0	0	0	0	0
Other current assets	6,634	5,107	5,487	6,498	7,260
Investments	8,036	7,748	7,748	7,748	7,748
Net fixed assets	9,966	13,469	12,448	11,171	9,621
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	3,292	3,899	4,356
<b>Total assets</b>	<b>41,790</b>	<b>51,566</b>	<b>59,371</b>	<b>70,754</b>	<b>81,453</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	6,927	9,063	13,378	15,624	16,440
Interest expenses	(117)	(419)	(847)	(234)	(566)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(2,360)	9,459	(1,081)	612	(365)
Other operating cash flows	1,855	(10,349)	0	0	0
<b>Cash flow from operations</b>	<b>6,305</b>	<b>7,754</b>	<b>11,450</b>	<b>16,002</b>	<b>15,508</b>
Capital expenditures	(1,708)	(1,496)	(1,490)	(1,530)	(1,560)
Change in investments	(301)	0	0	0	0
Other investing cash flows	209	419	847	234	566
<b>Cash flow from investing</b>	<b>(1,800)</b>	<b>(1,077)</b>	<b>(643)</b>	<b>(1,296)</b>	<b>(994)</b>
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)	(4,578)	(5,399)	(5,615)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(5,218)</b>	<b>(3,369)</b>	<b>(4,578)</b>	<b>(5,399)</b>	<b>(5,615)</b>
<b>Changes in cash and cash eq.</b>	<b>(713)</b>	<b>3,308</b>	<b>6,230</b>	<b>9,307</b>	<b>8,900</b>
<b>Closing cash and cash eq.</b>	<b>2,562</b>	<b>5,870</b>	<b>12,100</b>	<b>21,407</b>	<b>30,306</b>

**Per Share**

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	45.8	38.3	66.0	77.8	81.0
Adjusted EPS	45.8	38.3	66.0	77.8	81.0
Dividend per share	33.0	17.0	23.1	27.2	28.3
Book value per share	200.8	191.7	230.0	275.0	321.9

**Valuations Ratios**

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	3.9	3.5	3.4	2.8	2.4
EV/EBITDA	25.6	25.6	16.4	13.2	12.3
Adjusted P/E	36.3	43.4	25.2	21.4	20.5
P/BV	8.3	8.7	7.2	6.0	5.2

**DuPont Analysis**

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	76.4	76.1	73.5	73.5	72.5
Interest burden (PBT/EBIT)	109.6	105.3	106.1	101.4	103.2
EBIT margin (EBIT/Revenue)	12.8	10.1	17.4	18.1	16.8
Asset turnover (Revenue/Avg TA)	177.4	166.3	144.4	145.8	139.3
Leverage (Avg TA/Avg Equity)	1.3	1.4	1.6	1.6	1.5
Adjusted ROAE	24.9	19.5	31.3	30.8	27.1

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

**Ratio Analysis**

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
<b>YoY growth (%)</b>					
Revenue	28.5	10.6	3.2	18.4	11.7
EBITDA	43.8	(0.2)	54.8	21.7	4.6
Adjusted EPS	32.1	(16.3)	72.3	17.9	4.0
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	15.2	13.7	20.5	21.1	19.7
EBIT margin	12.8	10.1	17.4	18.1	16.8
Adjusted profit margin	10.7	8.1	13.6	13.5	12.6
Adjusted ROAE	24.9	19.5	31.3	30.8	27.1
ROCE	31.2	27.9	54.0	69.1	76.3
<b>Working capital days (days)</b>					
Receivables	61	65	70	67	66
Inventory	0	0	0	0	0
Payables	40	68	107	105	106
<b>Ratios (x)</b>					
Gross asset turnover	7.2	6.6	6.2	8.0	10.2
Current ratio	2.7	1.4	1.7	2.0	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

## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

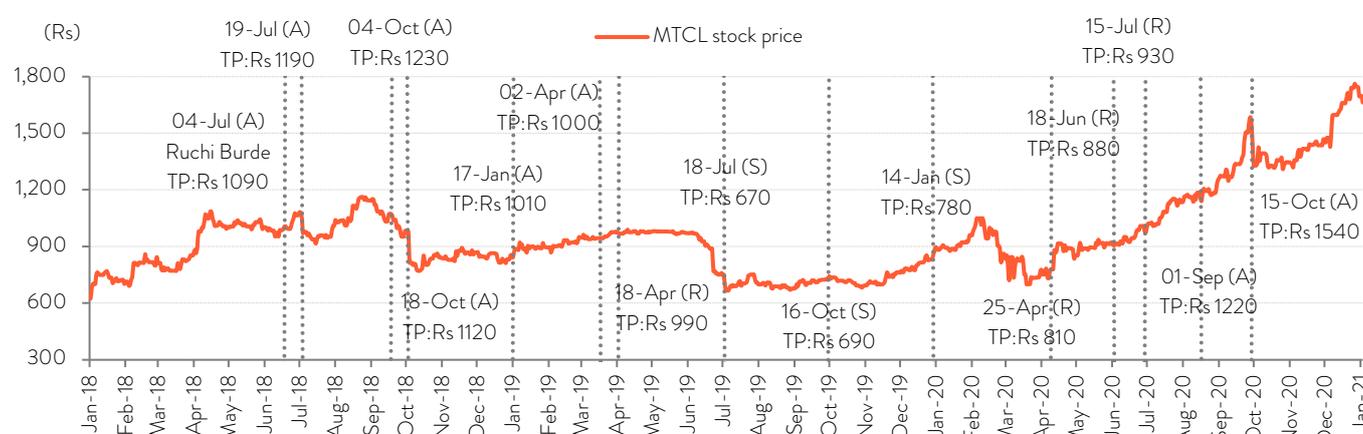
**ADD** – Expected return from >+5% to +15%

**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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