

Estimate change

TP change

Rating change

CMP: INR1,661 TP: INR1,765 (+6%)
Neutral

Strong 3Q led by stellar margin performance

Risk-adjusted valuation remains unattractive

Bloomberg	MTCL IN
Equity Shares (m)	165
M.Cap.(INRb)/(USD\$b)	273.5 / 3.8
52-Week Range (INR)	1780 / 692
1, 6, 12 Rel. Per (%)	9/31/72
12M Avg Val (INR M)	1482

Financials & Valuations (INR b)

Y/E Mar	2021E	2022E	2023E
Sales	79.8	92.0	103.4
EBIT Margin (%)	17.4	17.6	17.5
PAT	10.9	12.4	13.9
EPS (INR)	65.9	75.3	84.1
EPS Gr. (%)	71.9	14.2	11.7
BV/Sh. (INR)	233	282	337

Ratios

RoE (%)	31.1	29.3	27.2
RoCE (%)	24.4	23.9	22.4
Payout (%)	37.4	35.0	35.0

Valuations

P/E (x)	25.2	22.0	19.7
P/BV (x)	7.1	5.9	4.9
EV/EBITDA (x)	15.1	12.5	10.9
Div Yield (%)	1.5	1.6	1.8

Shareholding pattern (%)

As On	Dec-20	Sep-20	Dec-19
Promoter	61.0	67.6	73.6
DII	10.6	12.0	6.2
FII	13.3	12.0	10.5
Others	15.1	8.4	9.7

FII Includes depository receipts

- Mindtree (MTCL) delivered strong revenue growth in 3Q (5.0% QoQ USD), above our estimate of 3.6% QoQ, on a broad-based performance across client buckets and industries (with the exception of BFSI). While deal wins (USD312m) were stable QoQ, they remain c20% below the highs seen some quarters ago.
- More importantly, we were surprised by further expansion in the EBIT margin (+290bp QoQ / +760bp YoY), led by a 430bp QoQ increase in utilization (all-time high) and 70bp increase in offshore mix (six-year high). For 9MFY21, sales (USD) / EBIT / PAT came in at -3%/74%/87%.
- We expect MTCL to continue to benefit from a strong demand environment, especially given the high exposure to cloud (19% of revenues) – USD revenue growth was in the low-to-mid teens. In addition to reporting strong revenue growth, the company should benefit from the massive margin expansion over 2QFY20–3QFY21 (10pp) – the majority of which the management expects to retain despite an increase in investments in sales and new employee additions.
- Hence, despite the near-term drag due to wage hikes in 4QFY21, along with the gradual resumption of travel next year, we raise our FY22 EBITDA margin expectation to 21.1% (19.0% earlier).
- However, we continue to see high exposure to the top client (28.5% of revenues) as a risk – despite modest growth seen over the last two quarters. While MTCL has been trying to diversify its client exposure for a long time, this has only increased (c10pp over FY19–21E), which remains a concern.
- We upgrade our FY22/FY23 EPS estimates by 10%/11% as we factor in 170bp margin expansion, apart from the strong beat during the quarter. The stock is trading at 20x FY23 EPS. It has been one of the best performers in CY20 in the IT sector, with returns of 88% over the past year. We believe the key positives are already captured, and we see limited upside hereafter. Our TP of INR1,765 implies 21x FY23 EPS (15% discount to LTI). **Maintain Neutral.**

Strong all-round beat

- MTCL's revenues grew 5.0% QoQ to USD274m, above our estimate of 3.6% QoQ growth.
- The EBIT margin expanded 290bp QoQ to 19.6%, above our expectations of 16.5%. This was largely led by a 430bp increase in utilization and 70bp increase in the offshore mix sequentially.
- PAT increased 28.7% QoQ to INR3.2b, against our expectation of INR2.5b; this was primarily owing to higher operational income.
- Growth in 3Q was driven by Travel & Hospitality (12.6% QoQ), Retail & Manufacturing (5.5% QoQ), and Technology, Media & Services (5.2% QoQ). The BFSI vertical posted muted growth of 0.9% QoQ.
- In terms of geography, growth was broad-based, with the US growing 4.7% QoQ, while Europe inched up 3.7% QoQ. RoW reported robust growth of 10.9% QoQ.

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- In terms of Services, growth was largely skewed toward Data & Intelligence (10.2% QoQ). Other services lines – Cloud (6.1% QoQ), Enterprise IT (4.6% QoQ), and Customer Success (2.9% QoQ) – also reported robust growth.
- Growth was broad-based. Revenues from the top customer grew 3.6% QoQ and 22.9% YoY.
- Total TCV was USD312m (+51% YoY) for 3QFY21. On a YTD basis, MTCL exceeded deal wins of USD1b.

Largely in-line revenue; beat on margins

- The management continues to see strong demand across geographies and service lines, and the pipeline remains healthy.
- Among the verticals, Travel is still some quarters away from a full recovery. It has reached bottom levels and would only grow from hereon.
- The management intends to invest in growth in the coming quarters, which would be a headwind to margins.
- The company expects wage hikes to impact margins in the next quarter (-250bps). Despite this, the management is confident of sustaining margins in the 20%+ range on a sequential basis.
- This was possible owing to reduced travel cost on account of COVID-19, but largely because of company-specific optimization levers.
- The company has embarked on a rigorous re-skilling program, which has led to increased utilization. Now that utilization has reached ~83% levels, the management intends to hire aggressively.
- The company actively seeks inorganic opportunities, apart from significant organic traction.

Valuation and view – fair valuations; limited upside

- Since Jul'19, post the disruption pertaining to ownership change, Mindtree has been undertaking encouraging steps toward achieving stability in both its client and employee counts.
- The strategy change to increase focus on annuity revenue and tail account rationalization is already reflected in the revenue and client mixes.
- (1) A stable outlook for the Top account, (2) decent deal signings, and (3) the ability to sustain improved margins are key positives.
- Consistent margin expansion and a positive outlook on the same are key positives. High exposure to Travel, Transport, and Hospitality remains a drag on overall recovery.
- The stock is currently trading at 20x FY23E EPS. The stock has been one of the best performers in the IT sector in CY20, with returns of 87%. We believe the key positives are already captured, and we see limited upside hereafter. Our TP of INR1,765 implies 21x FY23 EPS (15% discount to LTI). **Maintain Neutral.**

Quarterly Performance

(INR m)

Y/E March	FY20				FY21E				FY20	FY21E	Est. 3QFY21	Var. (% / bp)
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE				
Revenue (USD m)	264	271	275	278	253	261	274	283	1,089	1,072	270	1.4
QoQ (%)	0.8	2.6	1.5	1.2	-9.1	3.1	5	3.4	8.7	-1.6	3.6	141bp
Revenue (INR m)	18,342	19,143	19,653	20,505	19,088	19,260	20,237	21,256	77,643	79,841	19,958	1.4
YoY (%)	11.9	9.1	10	11.5	4.1	0.6	3	3.7	10.6	2.8	1.6	142bp
GPM (%)	26.6	26.9	29.1	30.4	26.3	27.5	30.6	29.2	28.3	28.5	31.6	-96bp
SGA (%)	14	13.9	13.5	13.2	8.1	7.9	7.5	7.7	13.6	7.8	12	-448bp
EBITDA (INR M)	2,318	2,482	3,063	3,512	3,478	3,784	4,679	4,580	11,375	16,521	3,912	19.6
EBITDA Margin (%)	12.6	13	15.6	17.1	18.2	19.6	23.1	21.5	14.7	20.7	19.6	352bp
EBIT (INR M)	1,649	1,775	2,364	2,833	2,881	3,215	3,962	3,836	8,621	13,894	3,293	20.3
EBIT Margin (%)	9	9.3	12	13.8	15.1	16.7	19.6	18	10.5	16.4	16.5	308bp
Other income	-387	59	215	-220	17	232	489	149	-333	887	111	341.5
ETR (%)	26.5	26.4	23.6	21.1	26.5	26.4	26.6	26.5	23.9	26.5	26	65bp
PAT	927	1,350	1,970	2,062	2,130	2,537	3,265	2,929	6,309	10,861	2,519	29.6
QoQ (%)	-53.3	45.6	45.9	4.7	3.3	19.1	28.7	-10.3			-0.7	2941bp
YoY (%)	-41.4	-34.6	3	3.9	129.8	87.9	65.7	42	-16.3	72.1	27.9	3788bp
EPS (INR)	5.6	8.2	12	12.5	12.9	15.4	19.8	17.8	38.3	65.9	15.3	29.4

Key Performance Indicators

Y/E March	FY20				FY21				FY20	FY21
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q		
Margins										
Gross Margin	26.6	26.9	29.1	30.4	26.3	27.5	30.6	29.2	28.3	28.5
EBIT Margin	9.0	9.3	12.0	13.8	15.1	16.7	19.6	18.0	11.1	17.4
Net Margin	5.1	7.1	10.0	10.1	11.2	13.2	16.1	13.8	8.1	13.6
Operating metrics										
Headcount	20,935	21,267	21,561	21,991	21,955	21,827	22,195		21,991	
Attrition (%)	15.1	16.5	17.2	17.4	16.6	13.8	12.5		17.4	
Utilization	77.2	77.0	75.9	75.3	75.5	78.8	83.1		76.4	
Deal Win TCV (USD m)	324.0	307.0	207.0	393.0	391.0	303.0	312.0		1231.0	
Top Client (YoY %)										
Top Client	13.3	12.2	26.4	33.1	43.5	35.1	22.9		21.5	
Outside Top 10	10.4	13.4	6.5	-2.1	-19.3	-14.4	-6.6		6.8	
Key Geographies (YoY%)										
North America	10.9	10.1	11.2	10.9	2.7	1.1	3.1		10.8	

Management commentary highlights

Revenues, deal wins, and demand outlook

- The company reported growth of 5% QoQ in 3QFY21 – the highest sequential growth in a decade. Growth was broad-based.
- In terms of order book, the company signed TCV worth USD1b on a YTD basis. Going forward, the management expects it to be robust.
- The management continues to witness strong demand across geographies and service lines, and the pipeline remains healthy.
- The growth momentum is expected to continue in the coming quarters, and the management is confident of sustaining strong growth.
- Among the verticals, Travel is still some quarters away from a full recovery. It has reached bottom levels and would only grow from hereon.

Top client

- MTCL has a very strategic relationship with its Top client, and the management is highly optimistic about the relationship; growth is expected to continue.

- The company has been working on multiple areas with this client and is well-spread across various services.

Margin drivers and outlook

- The company reported a 350bp expansion in its EBITDA margins to 23.1% – the highest margins witnessed in a decade.
- Robust expansion was led by operational growth and efficiency.
- The management intends to invest in growth in the coming quarters, which would be a headwind to margins.
- The company expects wage hikes to impact margins in the next quarter (-250bps). Despite this, the management is confident of sustaining margins in the 20%+ range on a sequential basis.
- This was possible owing to reduced travel cost on account of COVID-19, but largely because of company-specific optimization levers.
- The company has embarked on a rigorous re-skilling program, which has led to increased utilization. Now that utilization has reached ~83% levels, the management intends to hire aggressively.

Other highlights

- Attrition stood at 12.5% in 3Q and DSO was reduced by 4 days to 61 days.
- The company has honored all campus selections and has completed its promotion cycle as well.
- It actively seeks inorganic opportunities, apart from the significant organic traction.

Exhibit 1: BFSI was flat, while other verticals reported sequential growth

Verticals	Contribution to rev (%)	Growth (QoQ %)	Growth (YoY %)
Communications, Media & Technology	49.9	5.2	19.8
BFSI	19.6	0.9	-8.3
Manufacturing, CPG & Retail	21.6	5.5	4.4
Travel & Hospitality	8.9	12.6	-46.6

Source: Company, MOFSL

Exhibit 2: Growth was broad-based, with Asia-Pacific leading the pack

Geographies	Contribution to rev (%)	Growth (QoQ %)	Growth (YoY %)
North America	77.2	4.7	3.1
Continental Europe	7.4	3.6	-11.2
UK and Ireland	7.8	3.7	-10.7
Asia Pacific	7.6	10.9	-9.9

Source: Company, MOFSL

Exhibit 3: Data & Intelligence reported strong growth sequentially

Service Offerings	Contribution to rev (%)	Growth (QoQ %)	Growth (YoY %)
Customer success	38.1	2.9	-4.7
Data & Intelligence	14.9	10.2	6.0
Cloud	19.2	6.1	20.3
Enterprise IT	27.8	4.6	-8.6

Source: Company, MOFSL

Valuation and view – fair valuations; limited upside

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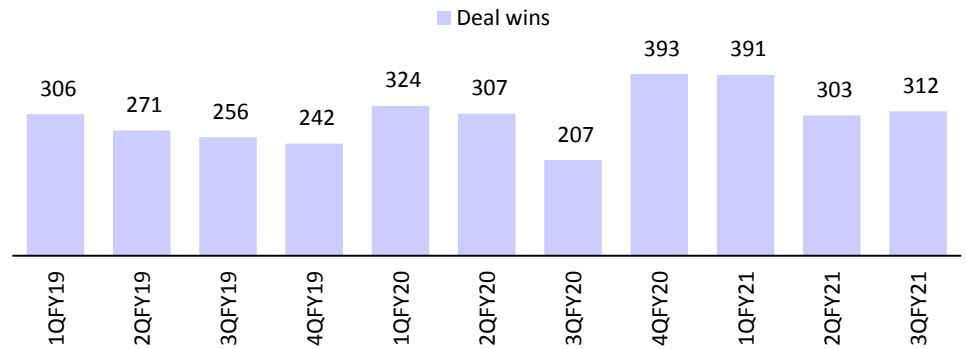
Exhibit 4: Revisions to our estimates

	Revised			Earlier			Change		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
INR/USD	74.5	75.0	75.0	74.5	75.0	75.0	0.0%	0.0%	0.0%
USD Revenue - m	1,072	1,227	1,378	1,064	1,217	1,362	0.7%	0.8%	1.2%
Growth (%)	(1.6)	14.5	12.3	(2.3)	14.4	12.0	70bps	10bps	40bps
EBIT margin (%)	17.4	17.6	17.5	16.0	15.9	15.8	140bps	170bps	170bps
PAT (INR M)	10,861	12,405	13,859	9,689	11,216	12,482	12.1%	10.6%	11.0%
EPS	65.9	75.3	84.1	58.9	68.2	75.8	11.9%	10.4%	10.9%

Source: MOFSL

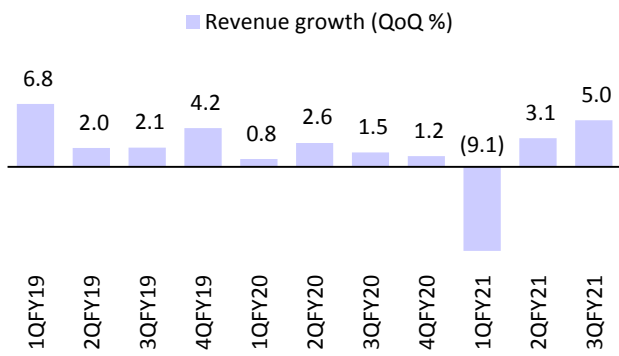
Story in charts

Exhibit 5: Total TCV signed grew 51% YoY during the quarter



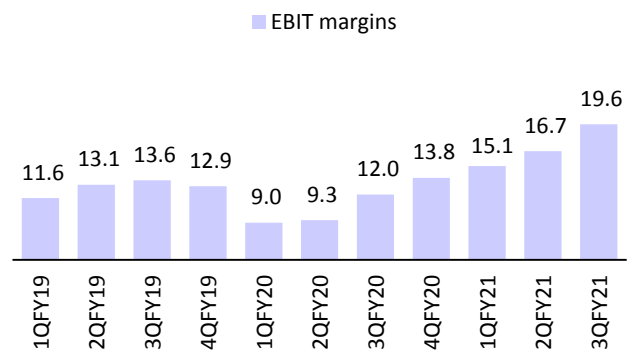
Source: Company, MOFSL

Exhibit 6: Company reported robust growth in 3QFY21



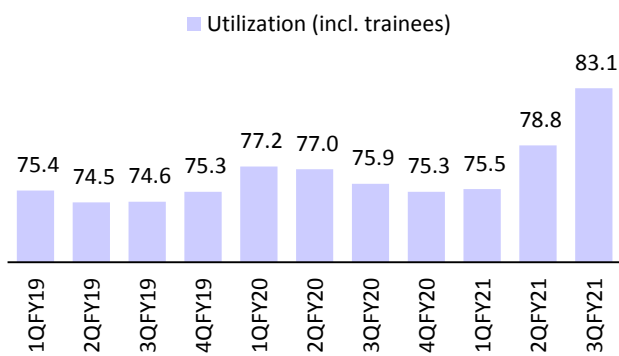
Source: Company, MOFSL

Exhibit 7: Margin expansion of 290bps was seen on the back of...



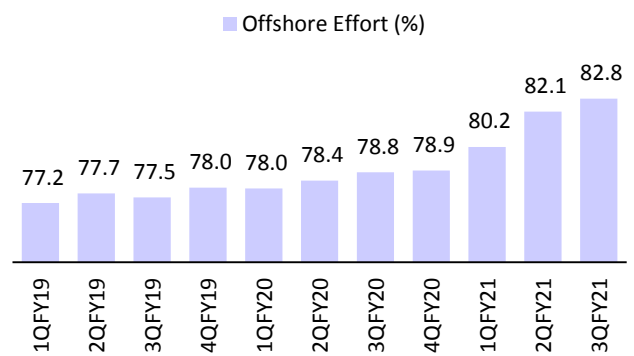
Source: Company, MOFSL

Exhibit 8: ...increased utilization levels (430bps) and...



Source: Company, MOFSL

Exhibit 9: ...increased offshoring efforts (70bps)



Source: Company, MOFSL

Operating metrics

Exhibit 10: Operating metrics

	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21	2QFY21	3QFY21
Geographic Mix (%)*											
North America						73.7	74.6		79.0	77.4	77.2
Continental Europe						8.9	8.3		6.6	7.5	7.4
UK and Ireland						8.7	8.7		6.5	7.9	7.8
Asia Pacific						8.7	8.4		7.9	7.2	7.6
Vertical Mix (%)											
Hi-Tech & Media	38.9	39.3	39.4	39.6	39.4	39.8	41.5	43.1	51.0	49.8	49.9
BFSI	22.3	22.4	21.7	21.8	21.6	21.6	21.3	20.4	20.3	20.4	19.6
Manufacturing, CPG & Retail	23.1	21.7	22.3	22.2	22.2	21.7	20.6	20.3	20.6	21.5	21.6
Travel & Hospitality	15.8	16.7	16.7	16.4	16.8	16.9	16.6	16.2	8.1	8.3	8.9
Utilization (%)											
Including trainees	75.4	74.5	74.6	75.3	77.2	77.0	75.9	75.3	75.5	78.8	83.1
Client Metrics											
No. of Active clients	339	341	340	349	346	343	320	307	292	283	276
New clients added	24	18	23	15	12	14	7	5	6	8	8
Client buckets											
US\$1mn clients	117	111	116	120	122	130	134	134	127	125	120
US\$5mn clients	39	44	44	45	46	47	47	47	44	43	43
US\$10mn clients	19	21	21	23	23	21	22	23	23	24	21
US\$25mn clients	4	4	4	4	4	4	5	5	5	5	4
US\$50mn clients	1	1	1	1	1	1	1	1	1	1	1
US\$100mn clients	1	1	1	1	1	1	1	1	1	1	1
Client contribution (%)											
Top client	19.4	20.2	20.0	19.8	20.1	20.6	23.1	24.8	30.1	28.9	28.5
Top 5	32.3	33.8	33.8	33.2	33.6	33.2	36.1	37.9	42.9	40.6	39.8
Top 10	43.5	44.8	44.1	42.9	43.0	43.1	45.6	47.4	52.0	49.4	49.0
Service lines (%)*											
Customer success						41.8	39.8		39.8	38.9	38.1
Data & Intelligence						12.1	14.0		13.9	14.2	14.9
Cloud						14.5	15.9		20.1	19.0	19.2
Enterprise IT						31.6	30.3		26.2	27.9	27.8

Source: MOFSL, Company. Note: Geography and Service Line mix has been reclassified from 2QFY21.

Financials and valuations

Income Statement								(INR m)
Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Sales	46,730	52,365	54,628	70,215	77,643	79,841	92,027	1,03,384
Change (%)	31.8	12.1	4.3	28.5	10.6	2.8	15.3	12.3
Cost of Services	31,591	36,500	38,192	47,997	55,686	57,106	65,398	73,674
SG&A Expenses	7,054	8,681	9,021	11,522	10,582	6,215	7,175	7,961
EBITDA	8,085	7,184	7,415	10,696	11,375	16,521	19,454	21,750
% of Net Sales	17.3	13.7	13.6	15.2	14.7	20.7	21.1	21.0
Depreciation & Amortization	1,523	1,850	1,715	1,692	2,754	2,627	3,221	3,618
Other Income	652	216	1,723	864	-333	887	644	724
PBT	7,214	5,550	7,423	9,868	8,288	14,781	16,877	18,855
Tax	1,691	1,390	1,722	2,327	1,979	3,920	4,472	4,997
Rate (%)	23.4	25.0	23.2	23.6	23.9	26.5	26.5	26.5
PAT	5,523	4,160	5,701	7,541	6,309	10,861	12,405	13,859
Change (%)	3.8	-24.7	37.0	32.3	-16.3	72.1	14.2	11.7

Balance Sheet								(INR m)
Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Share Capital	1,678	1,680	1,639	1,642	1,646	1,646	1,646	1,646
Other components	1,353	1,019	0	993	0	0	0	0
Reserves	21,148	23,072	25,775	30,430	29,922	36,717	44,781	53,789
Net Worth	24,179	25,771	27,414	33,065	31,568	38,363	46,427	55,435
Loans	829	991	3,009	10	0	0	0	0
Long term liabilities	832	301	85	174	6,762	6,953	8,015	9,004
Capital Employed	25,840	27,063	30,508	33,249	38,330	45,317	54,441	64,438
Gross Block	13,342	14,288	15,988	12,321	14,321	16,421	18,921	21,421
Less : Depreciation	6,327	7,995	9,710	889	3,643	6,270	9,491	13,109
Net Block	7,015	5,942	5,121	5,234	9,496	8,969	8,248	7,130
Goodwill	4,815	4,470	4,539	4,732	4,732	4,732	4,732	4,732
Other LT Assets	2,578	2,826	2,616	2,952	3,985	4,098	4,723	5,306
Investments	62	58	58	1,200	804	804	804	804
Curr. Assets	18,278	20,610	25,031	27,672	32,549	40,833	51,056	62,524
Current Investments	2,016	5,869	10,287	6,920	8,905	8,047	7,189	6,331
Debtors	11,860	11,187	10,155	16,347	17,194	15,957	18,393	23,580
Cash & Bank Balance	2,332	2,508	3,289	2,562	3,909	14,833	23,174	30,029
Other Current Assets	2,070	1,046	1,283	1,843	2,541	1,996	2,301	2,585
Current Liab. & Prov	6,908	6,843	6,857	8,541	13,236	14,119	15,123	16,058
Trade payables	1,889	1,651	1,710	2,131	2,587	3,382	3,899	4,380
Other liabilities	4,269	4,087	3,929	5,666	8,925	8,964	9,181	9,383
Provisions	750	1,105	1,218	744	1,724	1,773	2,043	2,296
Net Current Assets	11,370	13,767	18,174	19,131	19,313	26,714	35,934	46,467
Application of Funds	25,840	27,063	30,508	33,249	38,330	45,317	54,441	64,438

Financials and valuations

Ratios

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Basic (INR)								
EPS	32.9	24.7	34.2	45.8	38.3	65.9	75.3	84.1
Cash EPS	41.9	35.7	44.5	56.1	55.1	81.8	94.8	106.0
Book Value	144.2	153.5	164.9	201.5	191.9	232.9	281.8	336.5
DPS	10.5	10.0	9.0	33.0	16.0	24.7	26.3	29.4
Payout %	32.0	40.4	26.3	72.0	41.7	37.4	35.0	35.0
Valuation (x)								
P/E	50.5	67.0	48.5	36.2	43.2	25.2	22.0	19.7
Cash P/E	39.6	46.4	37.2	29.5	30.1	20.3	17.5	15.6
EV/EBITDA	33.9	37.7	35.7	24.6	22.8	15.1	12.5	10.9
EV/Sales	5.9	5.2	4.9	3.7	3.3	3.1	2.6	2.3
Price/Book Value	11.5	10.8	10.1	8.2	8.6	7.1	5.9	4.9
Dividend Yield (%)	0.6	0.6	0.5	2.0	1.0	1.5	1.6	1.8
Profitability Ratios (%)								
RoE	24.3	16.7	21.4	24.9	19.5	31.1	29.3	27.2
RoCE	21.5	15.6	16.3	22.7	18.3	24.4	23.9	22.4
Turnover Ratios								
Debtors (Days)	93	78	68	85	81	73	73	83
Fixed Asset Turnover (x)	6.7	8.8	10.7	13.4	8.2	8.9	11.2	14.5

Cash Flow Statement

(INR m)

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
CF from Operations	6,651	5,318	6,477	8,716	9,396	12,601	14,981	16,753
Cash for Working Capital	-2,451	1,217	-833	-2,360	-1,145	2,743	-1,301	-4,130
Net Operating CF	4,200	6,535	5,644	6,356	8,251	15,344	13,681	12,624
Net Purchase of FA	-1,315	-846	-1,011	-1,759	-1,220	-2,100	-2,500	-2,500
Free Cash Flow	2,885	5,689	4,633	4,597	7,031	13,244	11,181	10,124
Net Purchase of Invest.	-2,928	-3,687	-989	-225	991	1,745	1,502	1,582
Net Cash from Invest.	-4,243	-4,533	-2,000	-1,984	-229	-355	-998	-918
Proc. from equity issues	24	8	1	3	4	0	0	0
Proceeds from LTB/STB	407	550	1,906	-3,044	-1,024	0	0	0
Dividend Payments	-2,151	-1,934	-4,782	-2,180	-5,940	-4,065	-4,342	-4,851
Cash Flow from Fin.	-1,720	-1,376	-2,875	-5,221	-6,960	-4,065	-4,342	-4,851
Exchange difference	92	-135	-2	133	285	0	0	0
Net Cash Flow	-1,671	491	767	-716	1,347	10,924	8,341	6,855
Opening Cash Bal.	3,763	2,092	2,583	3,350	2,634	3,981	14,904	23,246
Add: Net Cash	-1,671	491	767	-716	1,347	10,924	8,341	6,855
Closing Cash Bal.	2,092	2,583	3,350	2,634	3,981	14,904	23,246	30,100

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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