

Tech Mahindra (TECHM)

BUY

EBIT margin performance continues to surprise

Summary

While TECHM's Q4Y21 revenue was slightly lower than our forecast, EBIT margin was a beat. Revenue grew by 0.7% QoQ in CC (+1.6% QoQ in US\$ terms). EBIT margin improved by ~55bps QoQ to 16.5%, a 25-quarter high. However, recurring EPS of Rs13, -13.7%/+10.5% QoQ/YoY was a miss, impacted by FX loss and higher ETR.

In Q4FY21, TECHM has secured new deals with TCV of US\$1,043 mn and is confident of similar run-rate in Q1FY22. For FY22, TECHM has guided for a double-digit revenue growth and EBIT margin of 15%+, higher than our expectation and vs. 14.2% in FY21.

While we factor higher EBIT margin for FY22/23, it gets largely offset by higher ETR. We fine-tune our forecast to revenue/EPS CAGR of 9.5%/13.3% over FY21-23. We maintain BUY with new TP of Rs1,118 (vs. Rs1,108) based on PER of 17x FY23E.

Key Highlights and Investment Rationale

- Q4FY21 EBIT continues to see a QoQ improvement to a 25-quarter high**
 Q4FY21 revenue grew by 0.7% QoQ in CC (+1.6% in US\$) vs. our forecast of +1.7% QoQ. Enterprise segment (60.4% of revenue) has grown by 1.8% QoQ in US\$ with BFSI (16.5% of total revenue) outperforming with 4.9% QoQ growth and Retail, transport & logistics (7.5%) underperforming with QoQ decline of 3.2%. Communications vertical (39.6%) has grown by 1.4% QoQ in US\$. EBIT margin improved by ~55bps QoQ to 16.5%, at an 25-quarter high. The QoQ improvement was driven by operational efficiencies including increase in offshoring & utilization and lower D&A partly offset by increase in SG&A cost and variable payouts. Headcount continues to see QoQ decline (-0.7% to 121k) and attrition has inched up a bit to 13.3% vs. 12.4% in Q3.
- Large deal TCV an uptick; momentum to be maintained at least in Q1FY22**
 In Q4FY21, TECHM has secured new deal wins with TCV of US\$1,043 mn (US\$525 mn in Enterprise and US\$518 mn in Communications). TECHM confirmed that the deal-pipeline is robust and it is confident to maintain similar TCV in Q1FY22 as well.
- FY22 EBIT margin guidance of 15%+, last seen in FY19**
 TECHM's FY22 revenue growth guidance of double-digit growth includes double-digit growth for Enterprise segment and high sing-digit growth for Communications vertical. Importantly, it is confident of EBIT margin of 15%+ vs. 14.2% in FY21. It is confident of offsetting the headwinds from salary increase and partial rebound of travel and other costs through revenue growth and operational efficiencies.

TP	Rs1,118	
CMP	Rs963	
Potential upside / downside	16%	
Previous Rating	BUY	
V/s Consensus		
EPS (Rs)	FY22E	FY23E
IDBI Capital	61.4	65.8
Consensus	59.9	66.3
% difference	2.5	(0.8)

Shareholding Pattern (%)

Promoters	35.8
FII	39.1
DII	13.4
Public	11.7

Price Performance (%)

	-1m	-3m	-12m
Absolute	(2.8)	(0.9)	91.3
Rel to Sensex	(1.6)	(1.0)	36.8

Financial snapshot

Year	FY2019	FY2020	FY2021	FY2022E	FY2023E
Revenue	347,421	368,677	378,551	414,773	453,709
EBITDA	63,368	57,261	68,471	79,153	85,485
EBITDA (%)	18.2	15.5	18.1	19.1	18.8
Adj. PAT	42,975	42,505	44,788	53,630	57,496
EPS (Rs)	48.4	48.8	51.2	61.4	65.8
EPS Growth (%)	12.6	0.7	5.1	19.7	7.2
PE (x)	19.9	19.8	18.8	15.7	14.6
Dividend Yield (%)	1.5	1.6	4.7	5.2	5.5
EV/EBITDA (x)	11.8	13.6	10.7	9.2	8.3
RoE (%)	22.0	20.2	19.2	21.1	21.8
RoCE (%)	23.3	17.4	19.4	21.7	22.9

Source: Company; IDBI Capital Research

Q4FY21 Result Review

Key Stock Data

Bloomberg / Reuters	TECHM IN /TEML.BO
Sector	IT Services
Shares o/s (mn)	968
Market cap. (Rs mn)	932,792
Market cap. (US\$ mn)	12,483
3-m daily average value (Rs mn)	2,239.3
52-week high / low	Rs1,081 / 490
Sensex / Nifty	48,387 / 14,485

Relative to Sensex (%)

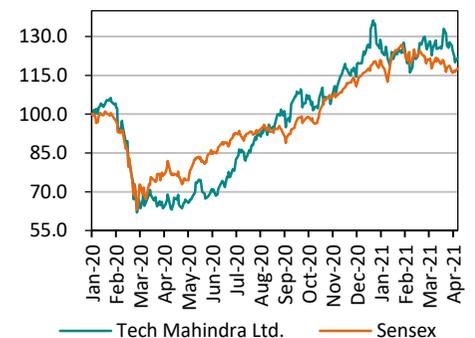


Exhibit 1: Financial snapshot

(Rs mn)

Q4FY21 revenue growth of 0.7%
QoQ CC was slightly lower than our
forecast

EBIT margin of 16.5%, +55bps QoQ
was a beat to our forecast and at an
25 quarter high.

Year-end: March	Q4FY21	Q3FY21	QoQ (%)	Q4FY20	YoY (%)
Revenues (US\$ mn)	1,330	1,309	1.6	1,295	2.7
Revenues	97,299	96,471	0.9	94,902	2.5
COGS	64,497	64,708	(0.3)	66,896	(3.6)
Gross profit	32,802	31,763	3.3	28,006	17.1
SG&A	13,321	12,808	4.0	14,528	(8.3)
EBITDA	19,481	18,955	2.8	13,478	44.5
Depreciation & amortization	3,444	3,584	(3.9)	3,982	(13.5)
EBIT	16,037	15,371	4.3	9,496	68.9
Other income	(91)	1,788	n.m.	2,320	(103.9)
PBT	15,946	17,159	(7.1)	11,816	35.0
Tax	4,998	4,263	17.2	2,392	108.9
Adjusted net profit	373	202	n.m.	790	n.m.
Minority interest	11,321	13,098	(13.6)	10,214	10.8
Exceptional items	(507)	0	n.m.	(2,175)	n.m.
Reported net profit	10,814	13,098	(17.4)	8,039	34.5
Diluted EPS (Rs)	13.0	15.0	(13.7)	11.7	10.5
As % of net revenue					
Gross profit	33.7	32.9		29.5	
SG&A	13.7	13.3		15.3	
EBITDA	20.0	19.6		14.2	
EBIT	16.5	15.9		10.0	
Reported net profit	11.1	13.6		8.5	
Tax rate	31.3	24.8		20.2	

Source: Company; IDBI Capital Research

Exhibit 2: Actual vs. estimates

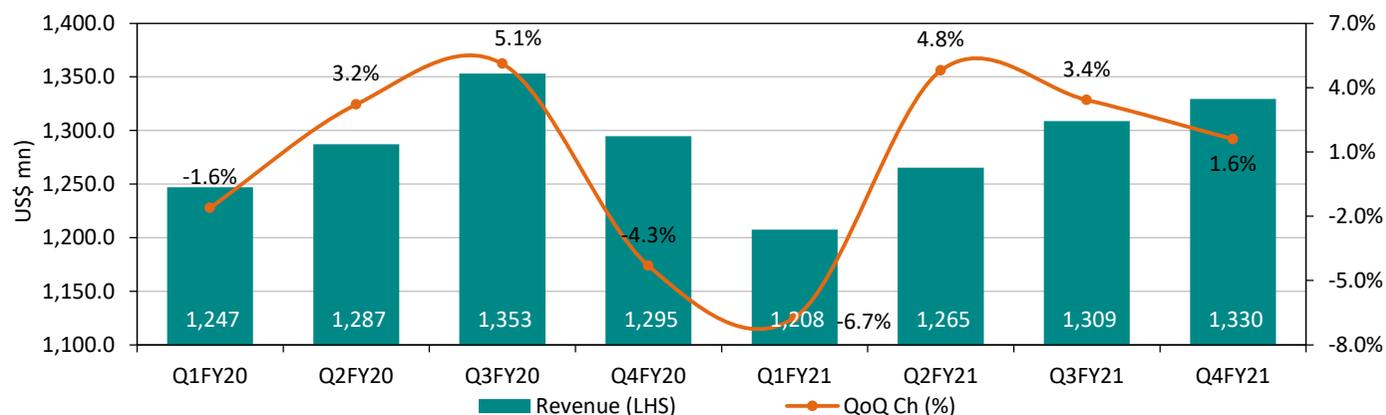
Year to March	Q4FY21	Q4FY21E	Variance (%)
Revenue (US\$ mn)	1,330	1,341	(0.8)
Revenue (Rs mn)	97,299	97,737	(0.4)
EBIT (Rs mn)	16,037	15,294	4.9
EBIT margin (%)	16.5	15.6	83bps
PAT (Rs mn)	11,321	12,859	(12.0)
PAT margin (%)	11.6	13.2	(152)bps
EPS (Rs)	13.0	14.7	(12.1)

Source: Company; IDBI Capital Research

Exhibit 3: Earnings Revision

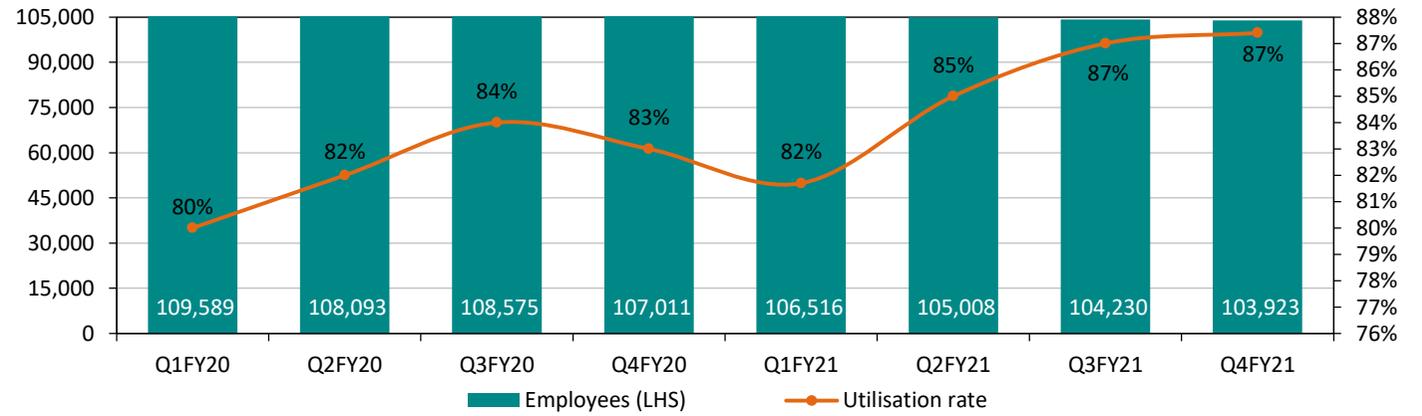
Year-end: March	FY22F			FY23F		
	New	Old	Chg (%)	New	Old	Chg (%)
Revenue (US\$ mn)	5,605	5,556	0.9	6,131	6,066	1.1
Revenue (Rs bn)	414.8	411.2	0.9	453.7	448.9	1.1
EBIT margin (%)	15.3	14.2	109bps	15.1	14.1	101bps
EPS (Rs/sh)	61.4	59.5	3.0	65.8	65.2	0.9

Source: Company; IDBI Capital Research

Exhibit 4: Q4FY21 revenue was slightly lower than our forecast


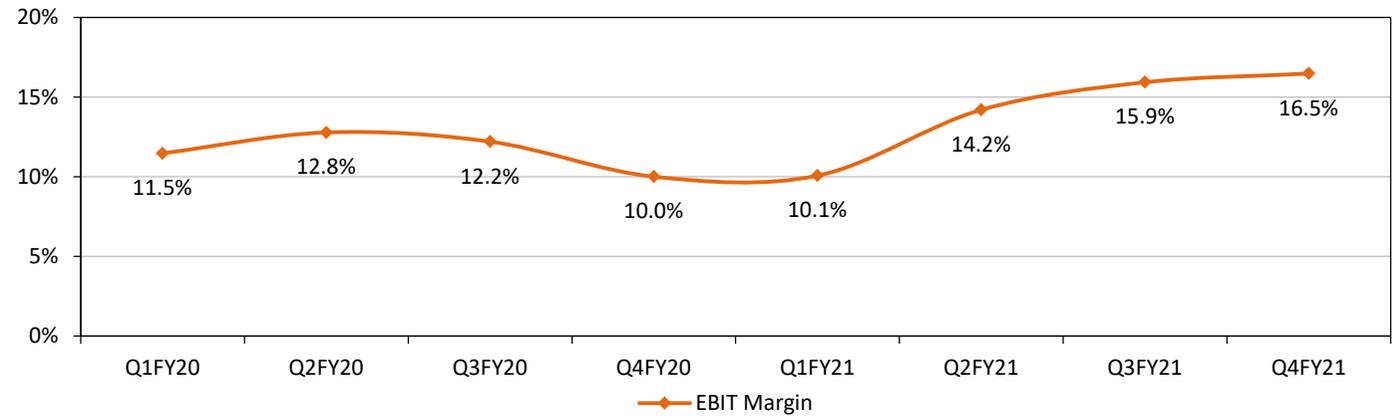
Source: Company; IDBI Capital Research

Exhibit 5: Utilisation remains at all-time high



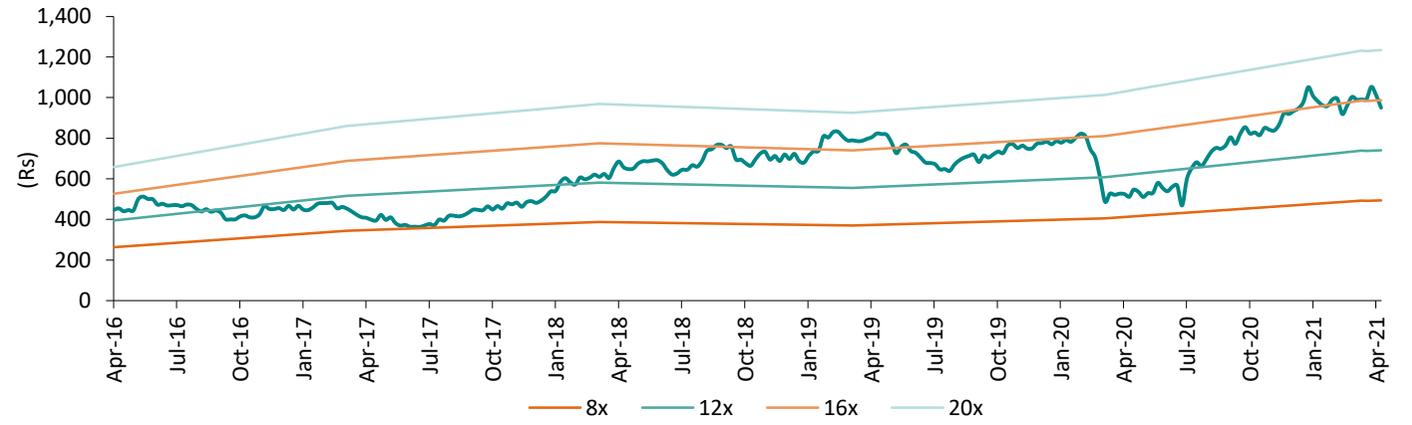
Source: Company; IDBI Capital Research

Exhibit 6: EBIT Margin was a beat to our forecast



Source: Company; IDBI Capital Research

Exhibit 7: One-year forward PER trend



Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Net sales	368,677	378,551	414,773	453,709
<i>Growth (%)</i>	6.1	2.7	9.6	9.4
Operating expenses	(311,416)	(310,080)	(335,620)	(368,224)
EBITDA	57,261	68,471	79,153	85,485
<i>Growth (%)</i>	-9.6	19.6	15.6	8.0
Depreciation	(14,458)	(14,577)	(15,708)	(16,758)
EBIT	42,803	53,894	63,444	68,726
Interest paid	(1,919)	(1,740)	(1,406)	(1,226)
Other income	11,924	7,871	8,561	8,254
Pre-tax profit	52,808	60,025	70,600	75,755
Tax	(11,604)	(15,999)	(17,650)	(18,939)
<i>Effective tax rate (%)</i>	22.0	26.7	25.0	25.0
Minority Interest	(874.0)	255.0	680.0	680.0
Net profit	40,330	44,281	53,630	57,496
Exceptional items	(2,175)	(507)	-	-
Adjusted net profit	42,505	44,788	53,630	57,496
<i>Growth (%)</i>	(1.1)	5.4	19.7	7.2
<i>Shares o/s (mn nos)</i>	872	874	874	874

Cash Flow Statement

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Pre-tax profit	52,808	60,025	70,600	75,755
Depreciation	9,343	14,577	15,708	16,758
Tax paid	(13,611)	(16,284)	(17,650)	(18,939)
Chg in working capital	(13,353)	14,633	(3,072)	615
Other operating activities	(50,579)	33,059	(3,185)	(3,423)
Cash flow from operations (a)	(15,392)	106,010	62,402	70,767
Capital expenditure	(13,723)	(18,935)	(10,000)	(10,000)
Chg in investments	5,424	(2,844)	-	-
Other investing activities	-	-	-	-
Cash flow from investing (b)	(8,299)	(21,779)	(10,000)	(10,000)
Equity raised/(repaid)	(78)	11	-	-
Debt raised/(repaid)	10,235	(7,664)	(2,000)	(2,000)
Dividend (incl. tax)	(15,692)	(39,330)	(43,700)	(46,322)
Chg in minorities	(1,718)	117	-	-
Other financing activities	-	-	-	-
Cash flow from financing (c)	(7,253)	(46,866)	(45,700)	(48,322)
Net chg in cash (a+b+c)	(30,944)	37,365	6,702	12,445

Balance Sheet

(Rs mn)

Year-end: March	FY20	FY21	FY22E	FY23E
Net fixed assets	76,047	80,405	74,697	67,938
Investments	3,804	6,648	6,648	6,648
Other non-curr assets	61,605	56,413	56,413	56,413
Current assets	231,723	252,553	274,085	299,899
Inventories	358	242	265	290
Sundry Debtors	75,772	64,728	73,864	80,797
Cash and Bank	87,606	124,971	131,673	144,117
Loans and advances	30,632	29,331	31,818	34,805
Total assets	373,179	396,019	411,843	430,898
Shareholders' funds	218,131	248,650	258,580	269,754
Share capital	4,359	4,370	4,370	4,370
Reserves & surplus	213,772	244,280	254,210	265,384
Total Debt	24,282	16,618	14,618	12,618
Secured loans	-	-	-	-
Unsecured loans	24,282	16,618	14,618	12,618
Other liabilities	21,076	19,027	19,027	19,027
Curr Liab & prov	105,757	107,929	116,503	127,064
Current liabilities	72,193	71,361	76,730	83,557
Provisions	33,564	36,568	39,773	43,506
Total liabilities	151,115	143,574	150,148	158,709
Total equity & liabilities	373,179	396,019	411,843	430,898
Book Value (Rs)	250	284	296	309

Source: Company; IDBI Capital Research

Financial Ratios

Year-end: March	FY20	FY21	FY22E	FY23E
Adj. EPS (Rs)	48.8	51.2	61.4	65.8
Adj. EPS growth (%)	0.7	5.1	19.7	7.2
EBITDA margin (%)	15.5	18.1	19.1	18.8
Pre-tax margin (%)	14.3	15.9	17.0	16.7
ROE (%)	20.2	19.2	21.1	21.8
ROCE (%)	17.4	19.4	21.7	22.9
Turnover & Leverage ratios (x)				
Asset turnover (x)	1.0	1.0	1.0	1.1
Leverage factor (x)	1.7	1.6	1.6	1.6
Net margin (%)	11.5	11.8	12.9	12.7
Net Debt/Equity (x)	(0.3)	(0.4)	(0.5)	(0.5)
Working Capital & Liquidity ratio				
Inventory days	0	0	0	0
Receivable days	75	62	65	65
Payable days	38	33	32	32

Valuation

Year-end: March	FY20	FY21	FY22E	FY23E
P/E (x)	19.8	18.8	15.7	14.6
Price / Book value (x)	3.8	3.4	3.3	3.1
PCE (x)	14.7	14.2	12.1	11.3
EV / Net sales (x)	2.1	1.9	1.7	1.6
EV / EBITDA (x)	13.6	10.7	9.2	8.3
Dividend Yield (%)	1.6	4.7	5.2	5.5



Notes

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Key to Ratings Stocks:

BUY: Absolute return of 15% and above; **ACCUMULATE:** 5% to 15%; **HOLD:** Upto ±5%; **REDUCE:** -5% to -15%; **SELL:** -15% and below.

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