

October 25, 2023

RESULT REPORT Q2 FY24 | Information Technology

Tech Mahindra Ltd

Muted financial performance led by subdued performance across verticals

Result Synopsis

Tech Mahindra (TECHM) reported weak financial performance for the quarter. The sequential revenue growth and EBIT margin were below expectation. Revenue declined by 2.4% QoQ in cc terms. (down 2.2% QoQ in INR terms, down 2.9% QoQ in USD terms), led by CME segment (down 4.9% QoQ). There was sequential decline in EBIT margin (down 206bps QoQ) on lower revenue. Employee attrition continues to moderate as LTM attrition was down ~2 percentage points QoQ to 11%.

The near term demand environment remains challenging as the clients remain cautious regarding the evolving macroeconomic situation and that is reflected in slowdown in discretionary spending and it continues to impact near term revenue performance. The continued weakness in Telecom vertical is expected to result in muted revenue growth for FY24. Falling employee attrition, improving employee pyramid and focus on better revenue mix is expected to support operating margin going ahead. We estimate revenue CAGR of 8.1% over FY23-25E with average EBIT margin of 11.5% over the period. We maintain our NEUTRAL rating on the stock with revised target price of Rs 1,190/share at 16.0x on FY25E EPS. The stock trades at PER of 25.5x/15.4x on FY24E/FY25E EPS.

Result Highlights

- Reported revenue of Rs 128.6bn (down 2.2% QoQ in INR terms, down 2.9% QoQ in USD terms). The muted performance of various verticals include Manufacturing (up 2.3% QoQ), CME (down 4.9% QoQ), BFSI (down 2.9% QoQ), TME (down 0.2% QoQ) and Retail & Transport (up 0.8% QoQ), other vertical (down 8.4% QoQ). Overall, the revenue decreased by 2.4% QoQ in cc terms.
- EBIT margin decreased by 206 bps QoQ to 4.7%, led by lower revenue and increase in Cost of Services (up 2.0% QoQ).
- Signed net new deals of \$640mn vs \$359mn in Q1FY24 and \$716mn in Q2FY23.
- Offshore effort mix was up 30 bps QoQ to 73.4%. Total number of Active clients decreased by 3 QoQ to 1252.
- Total headcount increased by around 2,307 QoQ to 150,604. LTM attrition was down 2.0 percent points QoQ to 11%. Utilization excluding trainees was down 100 bps QoQ to 86.0%.
- The Board approved interim dividend of Rs. 12 per share.

Exhibit 1: Actual vs estimates

Rs mn	Actual	Estimate		% Variation	
		YES Sec	Consensus	YES Sec	Consensus
Sales	128,639	131,693	132,450	-2.3%	-2.9%
EBITDA	10,723	15,803	16,180	-32.1%	-33.7%
EBITDA Margin (%)	8.34%	12.00%	12.22%	-366 bps	-388 bps
Adjusted PAT	4,939	9,091	8,000	-45.7%	-38.3%

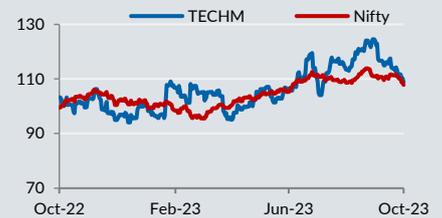
Source: Company, YES Sec

Reco	: NEUTRAL
CMP	: Rs 1,142
Target Price	: Rs 1,190
Potential Return	: + 4.2%

Stock data (as on October 25, 2023)

Nifty	19,122
52 Week h/l (Rs)	1320 / 981
Market cap (Rs/USD mn)	1127700 / 13562
Outstanding Shares (mn)	976
6m Avg t/o (Rs mn):	3,037
Div yield (%):	4.3
Bloomberg code:	TECHM IN
NSE code:	TECHM

Stock performance



	1M	3M	1Y
Absolute return	-12.1%	-1.2%	5.5%

Shareholding pattern (As of Sep'23 end)

Promoter	35.1%
FII+DII	53.5%
Others	11.3%

Δ in stance

(1-Yr)	New	Old
Rating	NEUTRAL	NEUTRAL
Target Price	1,190	1,199

Δ in earnings estimates

	FY24E	FY25E
EPS (New)	44.7	74.4
EPS (Old)	58.5	79.9
%Change	-23.5%	-6.9%

Financial Summary

(Rs mn)	FY23	FY24E	FY25E
Net Revenue	530,537	539,565	618,280
YoY Growth	18.7%	1.7%	14.6%
EBIDTA	77,922	69,315	105,726
YoY Growth	-3.3%	-11.0%	52.5%
PAT	45,947	39,509	65,689
YoY Growth	-18.1%	-14.0%	66.3%
ROE	16.8%	14.2%	22.5%
EPS	52	45	74
P/E	21.9	25.5	15.4
BV	316	316	345
P/BV	3.6	3.6	3.3

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Exhibit 2: Quarterly snapshot Console: Witnessed sequential dip in margin during the quarter

Particulars(Rs mn)	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	yoy%	qoq%	H1FY24	H1FY23	yoy %
Sales (\$ mn)	1,638	1,668	1,668	1,601	1,555	-5.1	-2.9	3,156	3,270	-3.5
Sales	131,295	137,346	137,182	131,590	128,639	-2.0	-2.2	260,229	258,374	0.7
EBITDA	19,841	21,440	20,205	13,380	10,723	-46.0	-19.9	24,103	38,642	-37.6
EBITDA %	15.1	15.6	14.7	10.2	8.3	-678 bps	-183 bps	9.3	15.0	-569 bps
Depreciation	4,917	4,981	4,902	4,466	4,657	-5.3	4.3	9,123	9,684	-5.8
EBIT	14,924	16,459	15,303	8,914	6,066	-59.4	-31.9	14,980	28,958	-48.3
EBIT Margin %	11.4	12.0	11.2	6.8	4.7	-665 bps	-206 bps	5.8	11.2	-545 bps
Other income	2,505	2,382	3,005	1,995	2,642	5.5	32.4	4,637	3,729	24.3
Interest	790	1,129	3,060	1,197	2,555	223.4	113.5	3,752	1,193	214.5
PBT	16,639	17,712	15,248	9,712	6,153	-63.0	-36.6	15,865	31,494	-49.6
Tax	3,647	4,859	3,999	2,676	1,100	-69.8	-58.9	3,776	7,027	-46.3
Reported PAT	12,854	12,966	11,176	6,925	4,939	-61.6	-28.7	11,864	24,170	-50.9
Adjusted PAT	12,854	12,966	11,176	6,925	4,939	-61.6	-28.7	11,864	24,170	-50.9
NPM (%)	9.8	9.4	8.1	5.3	3.8	-595 bps	-142 bps	4.6	9.4	-480 bps

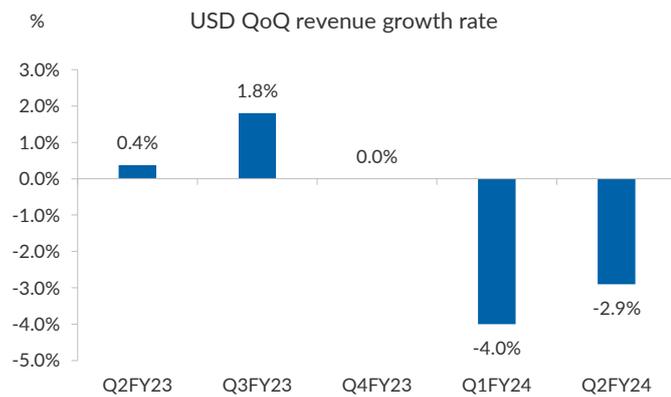
Source: Company, YES Sec

KEY CON-CALL HIGHLIGHTS

- Telecom will be the focused vertical for TECHM going ahead.
- A few of the customers have cut down their budget on 5G related transformation due to tough macro conditions
- No near-term bounce back visible in CME vertical. There are delay in the closure of the deals. CME vertical is witnessing headwinds and remains sluggish.
- Trained 10,000 employees during the quarter in new generative AI platform across various hyperscalers. 60+ clients are using Gen AI at their workplace for efficient operations.
- Top 5 client concentration was down 16.3% YoY. DSO reduced by 1 day QoQ to 97 days.
- Working on margin levers such as lower subcon cost, improving employee pyramid and increase in offshoring to drive margin improvement
- Insurance vertical grew sequentially and shows signs of uptick, however, BFS is dragging down the overall vertical.
- H2FY24 deal pipeline remains strong. Management focus remains on Margin improvement in the medium term.
- The management has introduced a new organization structure with effect from 1st Jan 2024
- The new management would be coming out with detailed plans with regard to revenue growth, margin improvement and organization in April'2024.

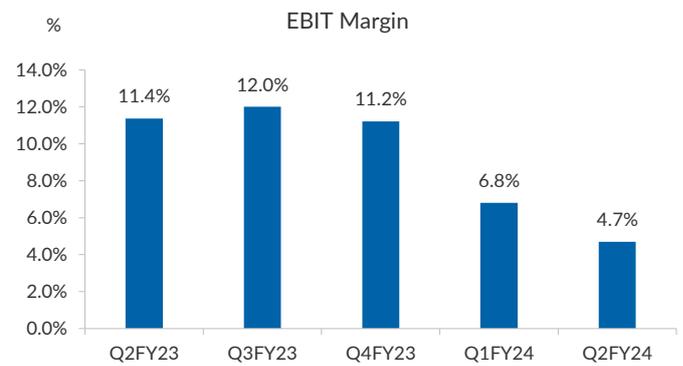
STORY IN CHARTS

Exhibit 3: Sequential growth in USD terms decreased due to near term demand concerns



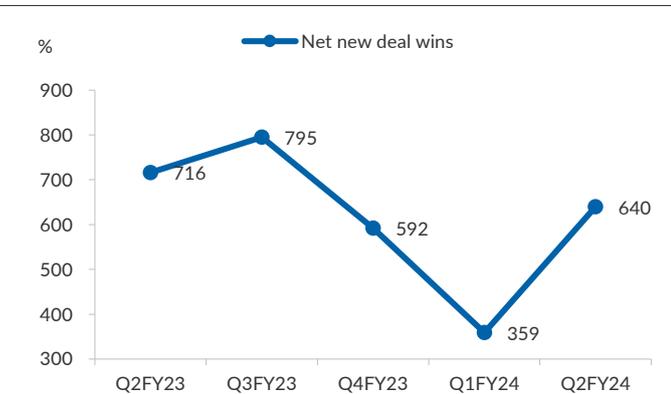
Source: Company, YES Sec

Exhibit 4: EBIT Margins declined sequentially due to higher Employee Expenses



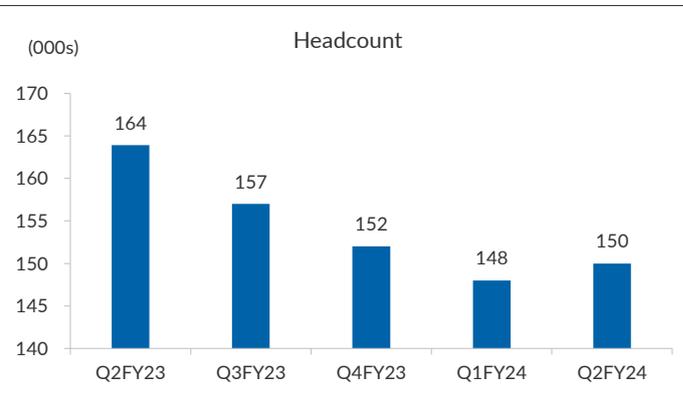
Source: Company, YES Sec

Exhibit 5: Net new deal wins remained strong



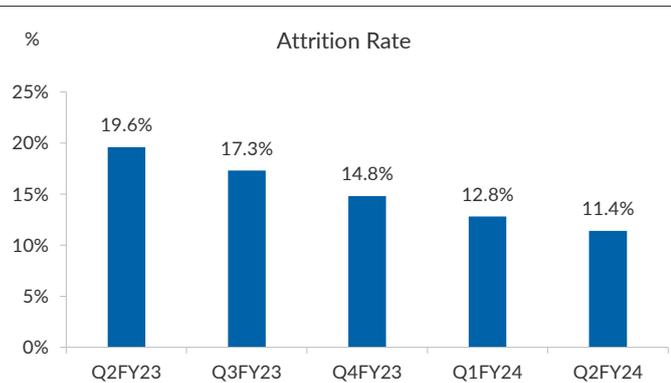
Source: Company, YES Sec

Exhibit 6: Total employee count increased during the quarter



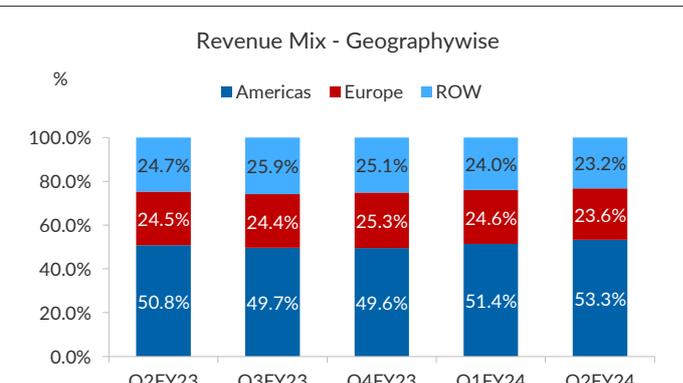
Source: Company, YES Sec

Exhibit 7: LTM Attrition rate declined during the quarter



Source: Company, YES Sec

Exhibit 8: Europe geography saw softness due to macro-economic uncertainties



Source: Company, YES Sec

FINANCIALS

Exhibit 9: Balance Sheet

Y/e March 31 (Rs mn)	FY20	FY21	FY22	FY23	FY24E	FY25E
Share capital	4,359	4,370	4,388	4,400	4,400	4,400
Reserves & surplus	213,772	244,280	264,469	274,845	274,619	300,571
Shareholders' funds	218,131	248,650	268,857	279,245	279,019	304,971
Non-current liabilities	29,910	29,256	37,544	32,072	32,379	32,742
Long-term borrowings	10,326	9,735	8,620	9,191	8,731	8,295
Other non-current liabilities	19,584	19,521	28,924	22,881	23,648	24,447
Current liabilities	121,561	115,079	137,352	145,514	152,220	161,845
ST borrowings, Curr maturity	25,954	18,963	17,564	18,211	18,757	19,320
Other current liabilities	95,607	96,116	119,788	127,303	133,463	142,525
Total (Equity and Liabilities)	373,535	396,780	448,707	461,533	468,320	504,260
Non-current assets	141,812	144,227	204,150	217,206	216,140	215,561
Fixed assets (Net block)	55,344	51,286	75,229	73,855	76,153	78,724
Non-current Investments	2,360	5,757	4,479	6,049	6,351	6,669
Other non-current assets	59,874	66,824	99,160	106,705	103,038	99,571
Current assets	231,723	252,553	244,557	244,327	252,180	288,699
Cash & current investment	87,606	124,971	84,104	70,379	58,859	71,763
Other current assets	144,117	127,582	160,453	173,948	193,321	216,936
Total (Assets)	373,535	396,780	448,707	461,533	468,320	504,260

Source: Company, YES Sec

Exhibit 10: Income Statement

Y/e March 31 (Rs mn)	FY20	FY21	FY22	FY23	FY24E	FY25E
Net sales	368,677	379,350	446,867	530,537	539,565	618,280
Operating expenses	(311,416)	(310,080)	(366,259)	(452,615)	(470,250)	(512,554)
EBITDA	57,261	69,270	80,608	77,922	69,315	105,726
Depreciation	(14,458)	(14,577)	(15,204)	(19,567)	(18,897)	(21,640)
EBIT	42,803	54,693	65,404	58,355	50,418	84,086
Other income	11,924	7,883	11,151	9,116	10,001	11,053
Finance cost	(1,919)	(1,740)	(1,626)	(5,382)	(7,316)	(6,710)
Profit before tax	52,808	60,836	74,929	62,089	53,102	88,429
Tax (current + deferred)	(11,604)	(15,999)	(18,220)	(15,885)	(13,140)	(22,284)
Reported Profit / (Loss)	42,505	45,587	56,069	45,947	39,509	65,689
Adjusted net profit	42,505	45,587	56,069	45,947	39,509	65,689

Source: Company, YES Sec

Exhibit 11: Cash Flow Statement

Y/e March 31 (Rs mn)	FY20	FY21	FY22	FY23	FY24E	FY25E
Profit before tax	52,808	60,836	74,929	62,089	53,102	88,429
Depreciation	14,458	14,577	15,204	19,567	18,897	21,640
Change in working capital	(21,956)	21,099	(12,418)	(15,782)	(12,749)	(14,065)
Total tax paid	(13,581)	(15,346)	(14,189)	(16,986)	(13,140)	(22,284)
Others	(10,005)	(6,143)	(9,525)	(3,734)	(2,685)	(4,342)
Cash flow from operations (a)	21,724	75,023	54,001	45,154	43,426	69,377
Capital expenditure	(24,590)	(10,519)	(39,147)	(18,193)	(21,195)	(24,211)
Change in investments	14,936	(43,893)	53,538	14,957	(2,251)	(2,402)
Others	4,692	7,828	12,049	8,744	9,835	10,878
Cash flow from investing (b)	(4,962)	(46,584)	26,440	5,508	(13,611)	(15,734)
Free cash flow (a+b)	16,762	28,439	80,441	50,662	29,815	53,643
Equity raised/(repaid)	(78)	11	18	12	0	0
Debt raised/(repaid)	16,325	(7,582)	(2,514)	1,218	87	126
Dividend (incl. tax)	(24,917)	(17,594)	(39,813)	(42,633)	(39,736)	(39,736)
Others	(196)	(6,405)	(26,739)	(6,457)	(3,634)	(3,213)
Cash flow from financing (c)	(8,866)	(31,570)	(69,048)	(47,860)	(43,283)	(42,823)
Net change in cash (a+b+c)	7,896	(3,131)	11,393	2,802	(13,468)	10,819

Source: Company, YES Sec

Exhibit 12: Ratio Analysis

Y/e March 31	FY20	FY21	FY22	FY23	FY24E	FY25E
Growth(%)						
Revenue Growth	6.1	2.9	17.8	18.7	1.7	14.6
EBITDA Growth	(9.6)	21.0	16.4	(3.3)	(11.0)	52.5
EBIT Growth	(17.8)	27.8	19.6	(10.8)	(13.6)	66.8
Net Profit Growth	(1.1)	7.3	23.0	(18.1)	(14.0)	66.3
Profitability Ratios(%)						
EBITDA Margin	15.5	18.3	18.0	14.7	12.8	17.1
EBIT margin	11.6	14.4	14.6	11.0	9.3	13.6
Net Profit margin	11.5	12.0	12.5	8.7	7.3	10.6
RoA	12.1	14.2	15.5	12.8	10.8	17.3
RoE	20.2	19.5	21.7	16.8	14.2	22.5
RoCE	16.6	18.9	20.8	17.6	15.1	24.1
Liquidity Ratios						
Net debt/Equity (x)	(0.2)	(0.4)	(0.2)	(0.2)	(0.1)	(0.1)
Current ratio (x)	1.9	2.2	1.8	1.7	1.7	1.8
Quick ratio (x)	1.9	2.2	1.8	1.7	1.7	1.8
Valuation Ratios						
PER(x)	NA	NA	NA	21.9	25.5	15.4
PCE(x)	NA	NA	NA	15.4	17.3	11.5
Price/Book(x)	NA	NA	NA	3.6	3.6	3.3
EV/EBITDA(x)	NA	NA	NA	12.4	14.1	9.1

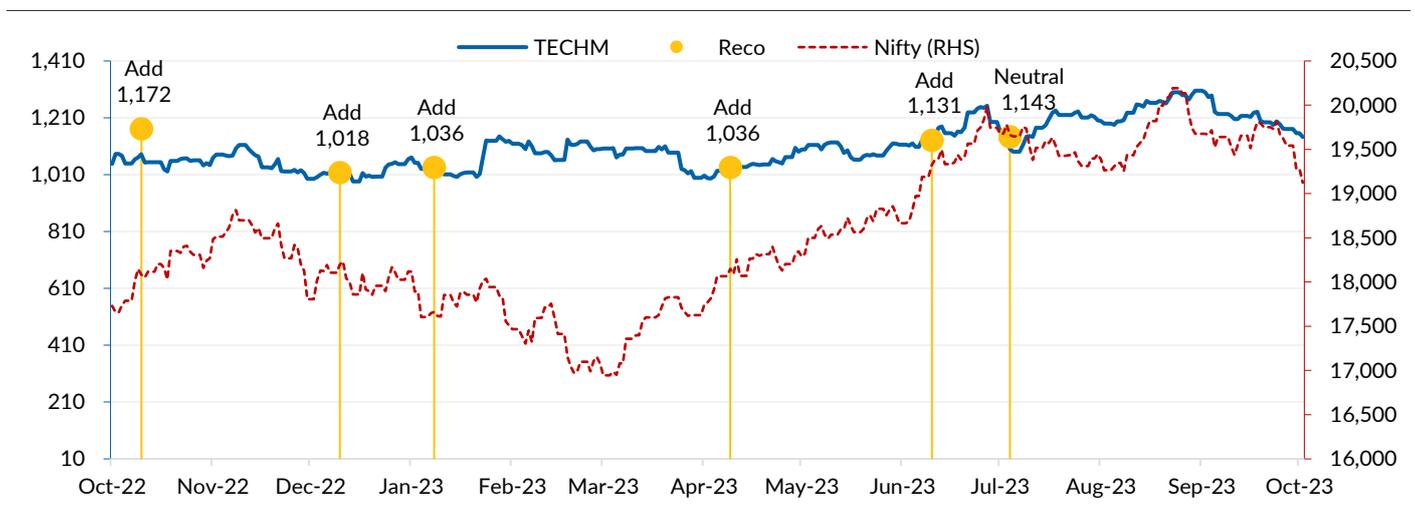
Source: Company, YES Sec

Exhibit 13: Dupont Analysis

Dupont Analysis	FY20	FY21	FY22	FY23	FY24E	FY25E
Net margin(%)	11.5	12.0	12.5	8.7	7.3	10.6
Asset turnover (x)	1.0	1.0	1.1	1.2	1.2	1.3
Leverage factor (x)	1.7	1.7	1.6	1.7	1.7	1.7
Return on Equity(%)	20.2	19.5	21.7	16.8	14.2	22.5

Source: Company, YES Sec

Recommendation Tracker



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YES Securities (India) Limited ("YSL") is a wholly owned subsidiary of YES BANK LIMITED. YSL is a Securities and Exchange Board of India (SEBI) registered Stock broker holding membership of National Stock Exchange (NSE), Bombay Stock Exchange (BSE), Multi Commodity Exchange (MCX) & National Commodity & Derivatives Exchange (NCDEX). YSL is also a SEBI-registered Category I Merchant Banker, Investment Adviser and Research Analyst. YSL is also a Sponsor and Investment Manager of Alternate Investment Fund - Category III (YSL Alternates) and AMFI registered Mutual Fund Distributor. The Company is also a registered Depository Participant with CDSL and NSDL. YSL offers, inter alia, trading/investment in equity and other financial products along with various value added services. We hereby declare that there are no disciplinary actions taken against YSL by SEBI/Stock Exchanges.