

Tech Mahindra Ltd. (TECHM)

CMP: Rs. 994 | TARGET PRICE: Rs. 1187 (19.4%)

Company Profile

Tech Mahindra is leading provider of solutions and services to the telecommunications industry with a majority stake owned by Mahindra & Mahindra Ltd. The Company since 2022 has operations in China with Offices in Beijing, Shanghai Etc. It offers various services such as integration, application development and management, application management Consulting, Infrastructure management and revenue management services.

Investment Rationale

Operations into Growing 5G and Cloud Segment: Tech Mahindra has Operations into fast growing 5G and cloud segments. It drives 40% of its revenue (FY22) from Communications and allied services segments. Tech Mahindra has invested USD 300 Mn+ in 5G segments. The 5G revenue jumped from USD 125 Mn in FY21 to USD 600 Mn in FY22 (5x), as it reported a five fold jump in 5G revenue in single fiscal year of FY22. Globally, 5G adaption to witness rapid growth and company is well place to benefit from the tailwind.

Significant Deal Win in Q4FY22: Tech Mahindra hits USD 1.04 Bn. mark of new deal win in Q4FY22. The deal wins remained muted during the last three qtrs. and it witnessed meaningful jump as total new deal wins for the Q4FY22 stands at USD 1041 Mn. The Bid pipeline remained healthy in Q4FY22. Deal Momentum in Communication, media & entertainment (CME) vertical is expected to sustain given the strong pipeline. It is bidding actively for deals in the CME (5G related) and BFSI space.

Recent Acquisitions to strengthen Technical Capabilities: Tech Mahindra made 26 Acquisition in FY22 to fuel up its technical capabilities across 5G, BFSI, Retail etc. the acquired companies includes leading companies such as DigitalOnUs, Eventus solutions group, Brain scale Inc. Company have adapted required technologies by acquiring firms in the same space.

Stabilized Attrition rates to Aid EBITDA Margins : Employee cost accounts for ~49.5% of the revenues and has direct impact on the EBITDA margins. Over the past 2 year the Attrition rate have improve on sequential basis for IT companies. The factor for higher attrition rates are higher Demand, Work from Home Etc. The Attrition rates of Tech Mahindra stabilized at 24% in Q3 & Q4 FY22. the uptrend in the jumped from 12% in Q3FY21 to 24% in Q4FY22. We believe the EBITDA margins to aid fro H2FY23.

Robust Sequential Top line growth: Tech Mahindra is reporting healthy sequential Constant Currency revenue growth of 6%, beating the growth rates of its peers. The higher attributable to the BFSI and technology space which saw a rebound and grew in double digit growth rates. The BFSI grew 18.5% QoQ and technology grew 16.1%.

Company Valuations: TECHM's high exposure to the Communications especially in 5G is a potential opportunity as a broader 5G rollout to lead to a new spending cycle revolving around 5G ecosystem in this space. We estimate Revenue/ PAT CAGR of 17%/13% over FY22-FY24E period. TECHM's historical earning multiple median is 16.5. The stocks is trading at a Forward PE of 13 (X). We value the Stocks at 16X of FY24E PAT. We recommend Buy on **TECHM** with a target price of Rs 1187 (19.4%).

Company Detail

Industry	IT-Software
BSE Code	532755
NSE Code	TECHM
Bloomberg Code	TECHM IN
Market Cap (INR Cr)	96,649
Promoter Holding (%)	35.2%
52wk Hi/Lo	1838 / 944
Avg. 20 Daily Volume (NSE)	555,063

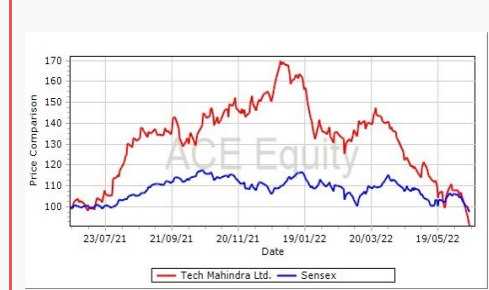
Shareholding Pattern (%)

Category	Dec-2021	Mar-2022
Promoter	35.67	35.26
Public	64.33	64.74

Public Holding More than 1% (Mar-22)

Name	% of Shares
First Sentier Investors ICVC	2.06%
Government Pension Fund	1.44%
ICICI Pru. Technology Fund	2.38%
LIC	4.84%
UTI Retirement Pension Fund	1.08%
SBI-ETF Nifty 50	2.84%

Share Price Performance



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91-22-66142685

Exhibit 1: Meaningful Deal win in Q4FY22 reverted downtrend of deals

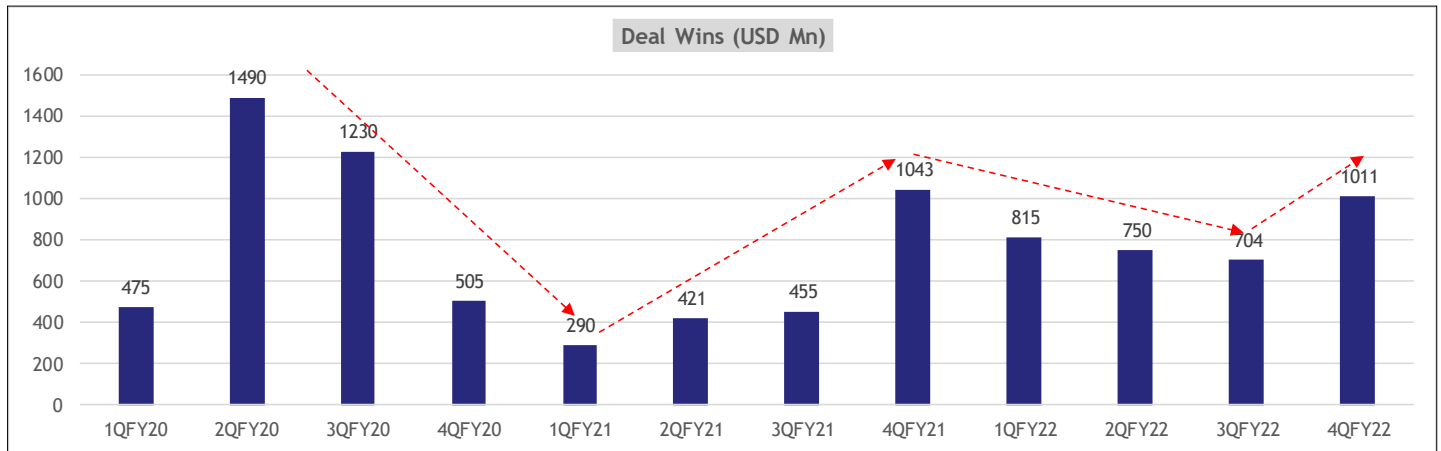


Exhibit 2: Attrition Rates stabilized at 24% in Q3 and Q4FY22 and Paused the

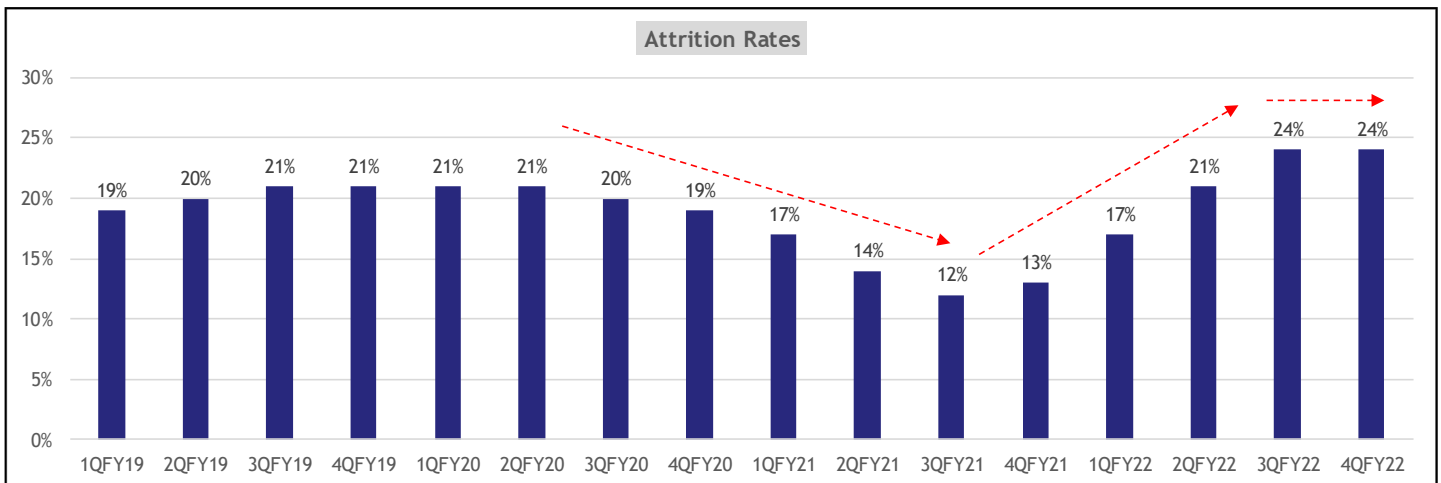


Exhibit 3: Employee Addition Remained in Uptick Driven by Robust Demand and skills

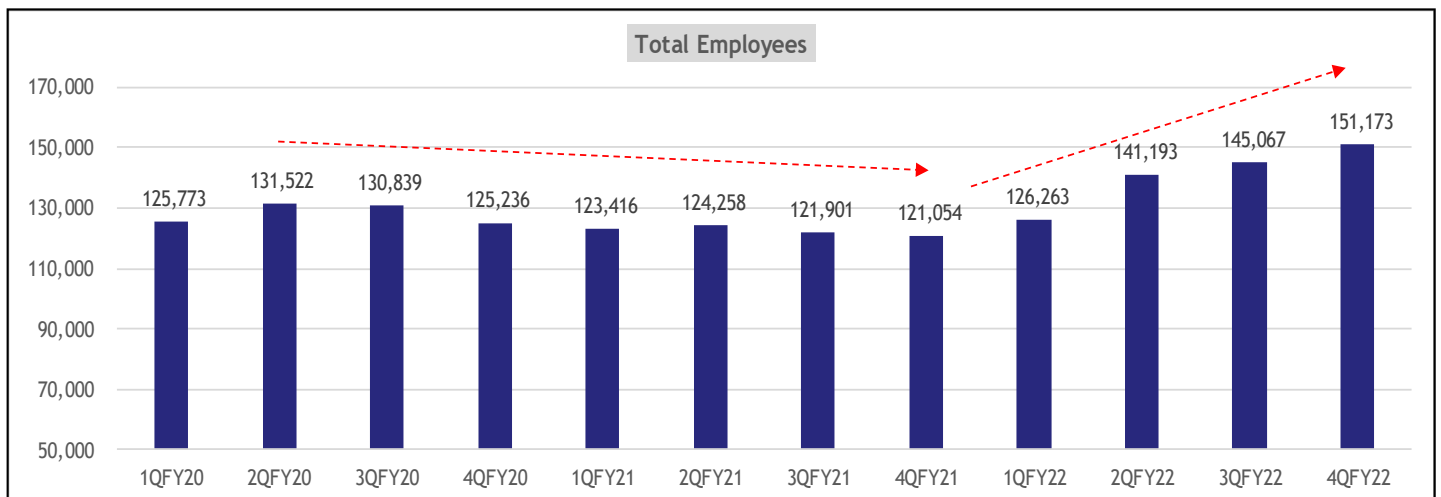


Exhibit 4: Meaningful Deal win in Q4FY22 reverted downtrend of deals

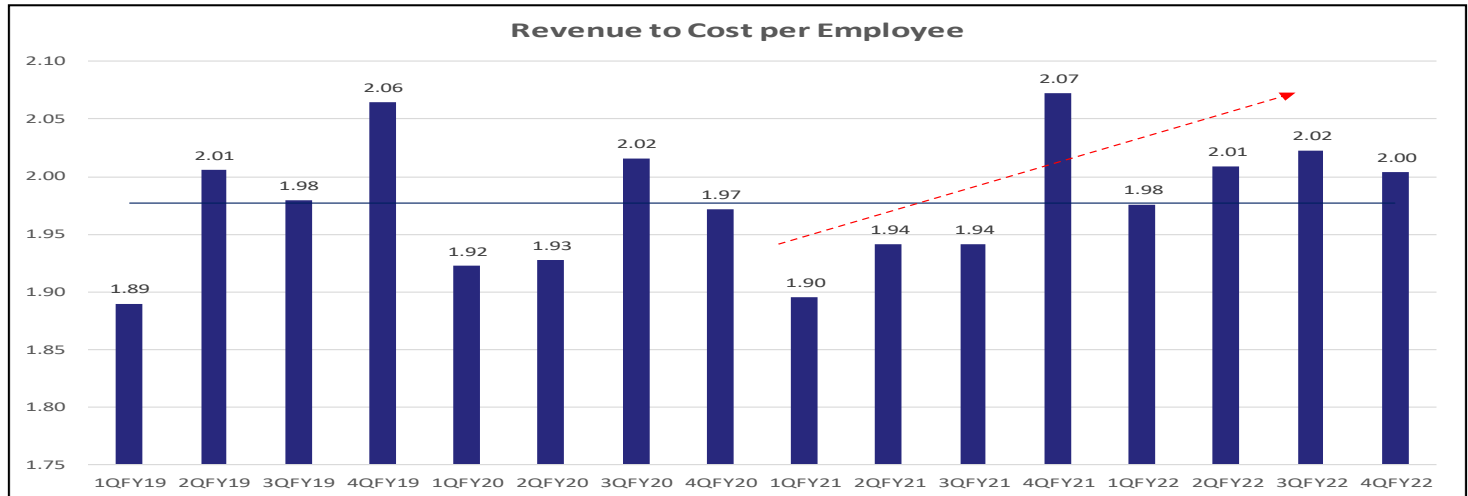


Exhibit 5: highest Exposure of 41% to telecom space

(% Revenue)	1QFY20	2QFY20	3QFY20	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22
Telecom	42	41	43	41	40	39	40	40	40	40	41	41
Manufacturing	19	18	17	18	17	16	16	16	17	16	16	15
BFSI	13	13	13	15	16	16	16	17	16	16	15	17
Others	12	13	12	12	11	11	11	11	11	11	11	10
Technology, Media & Entertmt.	8	8	8	7	9	10	9	9	9	9	9	9
Retail, Transport & Logistics	6	7	7	7	7	8	8	7	8	8	9	8
Total	100	100	100	100	100	100	100	100	100	100	100	100

Exhibit 6: America remains Major Contributor to Revenue

Revenue By Geography (%)	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22
Americas	47.7	49.3	48.4	46.8	45.5	46.7	47.8	48.9	48.3
Europe	26.5	25.8	25.2	26.4	26.5	27.2	25.9	25.5	26.4
Rest of the World	25.8	24.9	26.4	26.8	28	26.1	26.3	25.6	25.3
Total	100	100	100	100	100	100	100	100	100

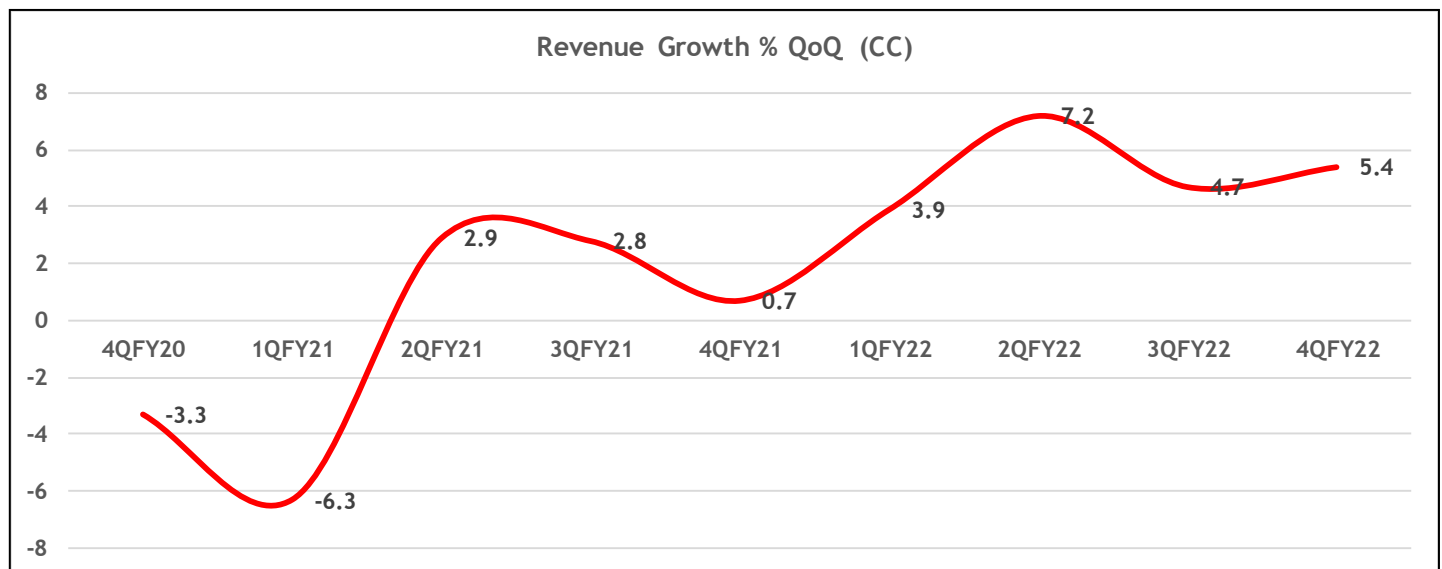
Exhibit 7: High Churn of Software Professional in Last 2 qtr lead Attrition rate to 24%

Headcounts	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22
Software Professionals	71,515	71,020	69,512	68,734	68,427	69,877	76,800	81,115	85,830
BPO	46,816	45,554	48,462	46,832	46,125	49,668	57,058	56,297	57,315
Sales and Support	6,905	6,842	6,284	6,335	6,502	6,718	7,335	7,655	8,028
Total	125,236	123,416	124,258	121,901	121,054	126,263	141,193	145,067	151,173
Headcount QoQ Growth%									
Software Professionals		-0.7%	-2.1%	-1.1%	-0.4%	2.1%	9.9%	5.6%	5.8%
BPO		-2.7%	6.4%	-3.4%	-1.5%	7.7%	14.9%	-1.3%	1.8%
Sales and Support		-0.9%	-8.2%	0.8%	2.6%	3.3%	9.2%	4.4%	4.9%
Total		-1.5%	0.7%	-1.9%	-0.7%	4.3%	11.8%	2.7%	4.2%
IT Attrition Rate									
	19%	17%	14%	12%	13%	17%	21%	24%	24%
Employee Cost									
	4,813	4,805	4,828	4,969	4,696	5,162	5,417	5,660	6,048
Employee Cost growth %									
		-0.2%	0.5%	2.9%	-5.5%	9.9%	4.9%	4.5%	6.8%

Exhibit 8: Client Metric of Tech Mahindra

Client Metrics	4QFY20	1QFY21	2QFY21	3QFY21	4QFY21	1QFY22	2QFY22	3QFY22	4QFY22
No. of Active Clients	973	981	988	997	1,007	1,058	1,123	1,191	1,191
No. of USD Mn Clients									
USD 1 Mn +	446	451	460	454	451	466	488	502	502
USD 5 Mn +	160	161	165	162	169	168	169	173	173
USD 10 Mn +	85	81	82	83	85	86	90	96	96
USD 20 Mn +	49	48	50	50	50	51	50	50	50
USD 50 Mn +	22	21	21	21	21	22	22	22	22
Client Concentration (%)									
Top 5	21	22	22	22	22	22	22	23	22
Top 6-10	10	9	8	9	9	9	9	8	9
Top 11-20	13	12	13	11	12	12	12	11	12

Exhibit 9: Robust Constant Currency growth on Sequential basis

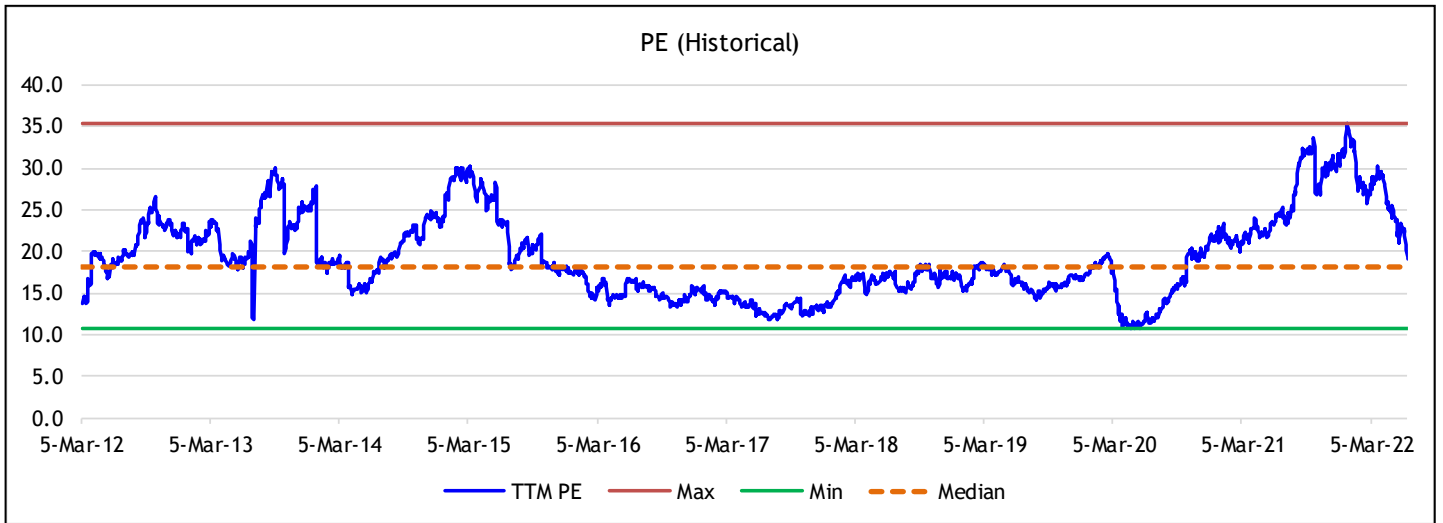


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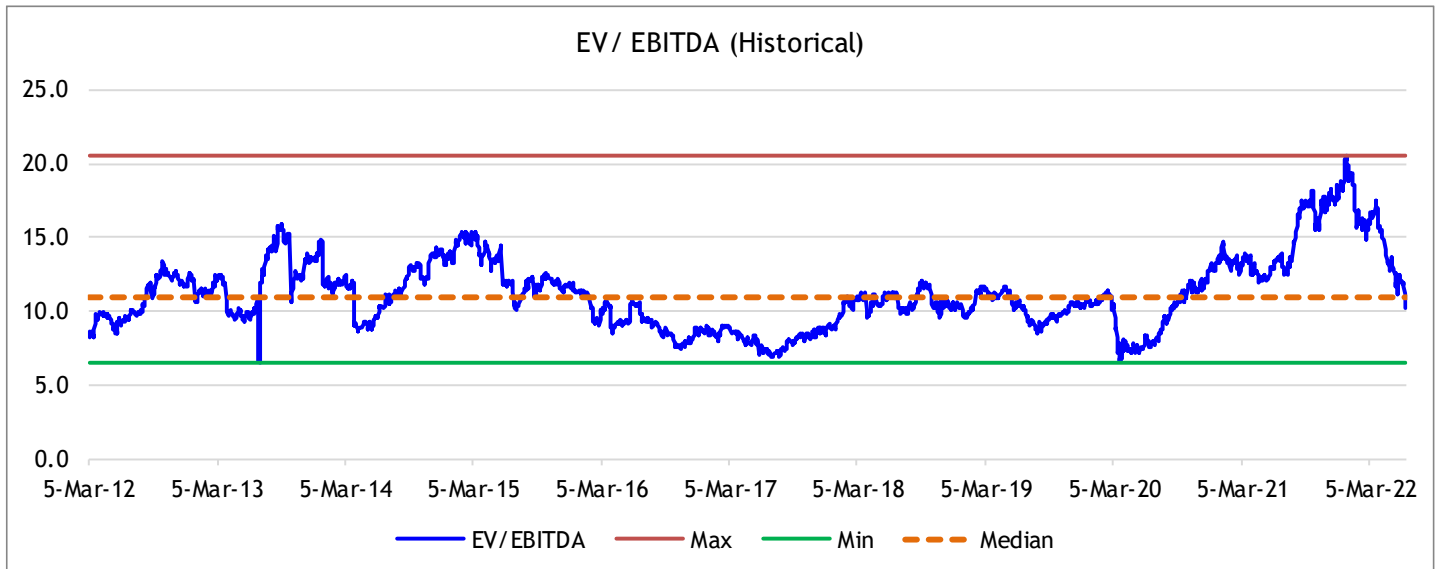


Date: 21 June, 2022

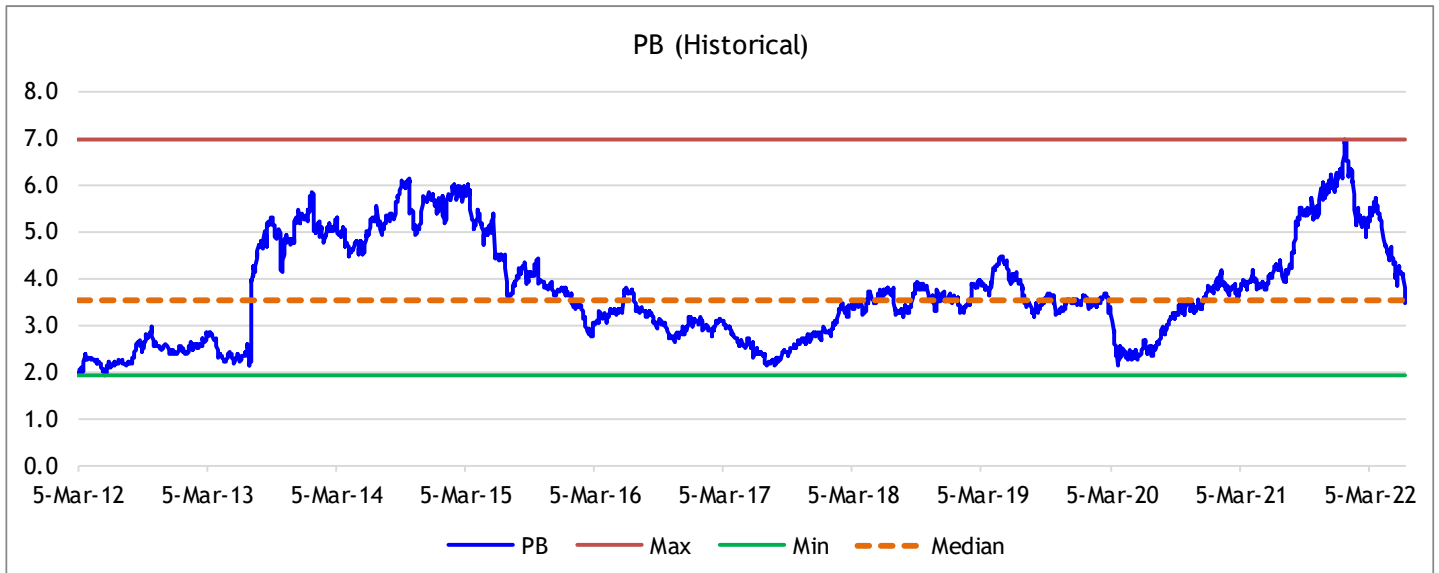
All time high valuations corrected to historical median levels aids comfort.



EV/ EBITDA trading below historical levels



Premium to equity has corrected to 3.6 (X) from Highs of 7 (x)



Profit and Loss Statement

Particulars (INR Cr)	FY 17	FY 18	FY 19	FY 20	FY 21	FY 22	FY 23E	FY 24E
Sales	29,100	30,800	34,700	36,900	37,900	44,600	53,609	61,114
change (%)		5.8%	12.7%	6.3%	2.7%	17.7%	19.0%	15.0%
COGS	20,600	21,500	23,400	26,000	25,900	31,000	37,500	42,200
SGA Expenses	4,400	4,500	5,000	5,200	5,200	5,700	6,900	7,800
Total Expenses	25,000	26,000	28,400	31,200	31,100	36,700	44,400	50,000
EBITDA	4,100	4,800	6,300	5,700	6,800	7,900	9,209	11,114
EBITDAM %	14.1%	15.6%	18.2%	15.4%	17.9%	17.7%	17.2%	18.2%
D&A	1,000	1,100	1,100	1,400	1,500	1,500	1,800	2,350
Other Income	600	1,200	300	1,000	600	1,000	1,005	1,050
PBT	3,700	4,900	5,500	5,300	5,900	7,400	8,414	9,814
Tax	1,000	1,100	1,300	1,200	1,500	1,800	2,200	2,600
Rate (%)	27%	22%	24%	23%	25%	24%	26%	26%
PAT	2,700	3,800	4,200	4,100	4,400	5,600	6,214	7,214
Minority Interest	0	0	0	-100	-100	100	0	0
Share of Associates	0	0	0	0	0	0	0	0
PAT before EI	2,700	3,800	4,200	4,000	4,300	5,700	6,214	7,214
Extraordinary Items (EI)	0	0	0	-200	-100	0	0	0
Reported PAT	2,700	3,800	4,200	3,800	4,200	5,700	6,214	7,214
PATM %	9%	12%	12%	10%	11%	13%	12%	12%
growth (YoY)		41%	11%	-10%	11%	36%	9%	16%

Balance Sheet

Particulars (INR Cr)	FY 17	FY 18	FY 19	FY 20	FY 21	FY 22	FY 23E	FY 24E
Share Capital	400	400	400	400	400	400	400	400
Reserves & Surplus	16,000	18,400	19,800	21,400	24,400	26,400	28,100	30,000
Shareholders Funds	16,400	18,800	20,200	21,800	24,800	26,800	28,500	30,400
Minority Interest	500	500	500	400	400	500	500	500
Long term borrowings	1,200	1,700	1,400	2,400	1,700	1,600	1,600	1,600
Other LT Loans	1,200	1,200	900	2,800	2,800	3,600	4,300	4,800
Amount Pending Investem.	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
Current Liabilities & prov.	5,600	7,000	9,100	8,700	8,800	11,100	13,100	14,700
Total Sourced of Funds	26,100	30,400	33,300	37,300	39,700	44,800	49,200	53,200
Assets	6,800	7,900	7,300	8,900	9,100	14,900	13,700	12,400
Investments	700	1,500	1,200	200	600	400	400	400
Other Non-Current Invest.	2,200	3,000	3,300	5,000	4,700	5,000	6,000	6,900
Current Assets	16,300	18,100	21,600	23,200	25,300	24,500	29,000	33,600
Trade Receivables	5,300	6,500	7,000	7,600	6,500	7,500	9,000	10,300
Cash & Bank Balance	2,000	2,000	2,000	3,000	2,700	3,800	2,600	1,900
Short term Investments	6,300	7,500	9,800	5,700	9,800	4,600	7,100	9,600
Other Current Aseets	2,700	2,200	2,800	6,800	6,300	8,600	10,300	11,700
Total Application of Funds	26,000	30,600	33,400	37,200	39,700	44,800	49,100	53,200

Cash Flow Statement

Particulars (Rs Bn)	FY 17	FY 18	FY 19	FY 20	FY 21	FY 22	FY 23E	FY 24E
Cash Flow from operations	3,500	4,300	5,500	4,900	6,500	6,700	8,300	9,700
Change in Working Capital	600	(800)	(1,100)	(500)	1,600	(1,400)	(1,600)	(1,500)
Net Operating Cash Flows	4,100	3,600	4,400	4,400	8,100	5,300	6,800	8,300
Net Purchase of F. Assets	(800)	(800)	(800)	(800)	(800)	(800)	(800)	(800)
Free Cash Flows	3,300	2,800	3,700	3,500	7,500	4,500	5,900	7,300
Net Purchase of Investment	(2,100)	(2,600)	(1,300)	1,900	(4,900)	1,300	(2,500)	(2,500)
Cash from Investing Act.	(2,900)	(3,400)	(2,100)	1,000	(5,500)	500	(3,400)	(3,500)
Inc/(Dec) in equity	-	-	-	-	100	100	-	-
Proceeds from borrowings	(400)	600	(600)	(2,000)	(1,300)	(800)	-	-
Dividend Payments	(1,200)	(900)	(1,700)	(2,500)	(1,800)	(4,000)	(4,600)	(5,500)
Cash Flows from Financial act.	(1,600)	(300)	(2,300)	(4,500)	(3,000)	(4,700)	(4,600)	(5,500)
Other Adjustments	-	-	-	100	-	-	-	-
Net Cash Flows	(400)	-	100	1,000	(300)	1,100	(1,200)	(700)
Opening Cash Balance	2,400	2,000	2,000	2,000	3,000	2,700	3,800	2,600
Add; Net Cash	(400)	-	100	1,000	(300)	1,100	(1,200)	(700)
Closing Cash Balance	2,000	2,000	2,000	3,000	2,700	3,800	2,600	1,900

View and Recommendation

Comfortable valuations with Mid-teens Growth Ahead:

- TECHM's high exposure to the Communications (40% of FY22 revenue) especially in 5G is a potential opportunity as a broader 5G rollout to lead to a new spending cycle revolving around 5G ecosystem in this space. Company has widened its technical capabilities and has track record of successfully completing projects in 5G space. The 5G rollout to bring Web 3.0 and newer ecosystem in UI. Thus it opens up new opportunity for Tech Mahindra.
- The Valuations have corrected from All time high levels amid FII's selling across all stocks. The peak FII Stake in TECHM from 39.05% in Dec-20 fell to 34.27% in Mar-22. In parallel way DII's holding improved from 13.5% to 18.05% in same period. The valuation multiples moderated to median levels gives comfort as we estimate the company to grow earnings in Mid teens.
- The uptrend in churn in employee headcount has stabilized at 24% since last 2 Qtrs. We expect moderation in Attrition rate going ahead and improvement in EBITDA margins from H2FY23.
- We estimate Revenue/ PAT CAGR of 17%/13% over FY22-FY24E period. TECHM's historical earning multiple median is 16.5. The stocks is trading at a Forward PE of 13 (X). We value the Stocks at 16X of FY24E PAT. We recommend Buy on TECHM with a target price of Rs 1187 (19.4%).

Notes

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for stock and our recommendation.

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