

IT

Tech Mahindra

Q2FY23 Result Update

November 01, 2022

CMP	1072
Sensex	61121

Stock Statistics

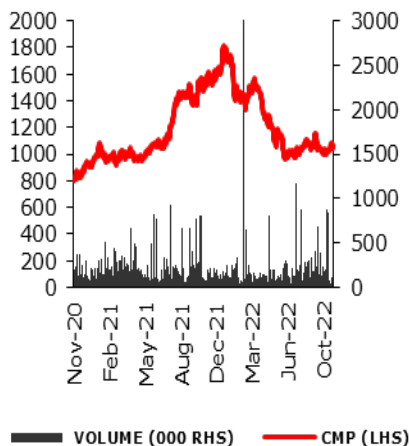
Reuters code	TEML.BO
Bloomberg code	TECHM IN

Equity Cap (INR cr)	440
Face Value (INR)	5
INR / USD	82.8
Market cap (INR cr)	1,04,298
Market cap (USD bn)	12.6
52 Wk High/Low (INR)	1838/944

Shareholding Pattern (%) – Sep'22

Promoter	35.2
Foreign Institutional Investor	29.2
MF / FI / UTI / Banks	23.8
Public & Others	11.0
Bodies & Corporate	0.8

2 yr Price and Volume Chart



Analyst

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Strategic pruning of low margin operations slows growth

Tech M has reported 0.3% qoq growth in reported terms to US\$1638mn for Q2FY23, while in CC terms growth was 2.9% qoq. Further growth was restricted due to pruning of non-strategic and non-scalable low margins business in BFSI vertical. In INR terms Top-line grew 3.3% qoq to Rs13,129cr.

CME de-grew 1.3% qoq (but grew 3.1% in CC terms), while Enterprise segment grew 1.5% qoq (grew 2.8% in CC terms). TCV of net new deal wins was down 11% qoq to US\$716mn despite of some slow down seen in later part of quarter end.

Though in reported term Europe de-grew 3.5% qoq, however in CC terms it grew 3.6% qoq. US grew 2.4% qoq in CC terms. Only ROW de-grew 0.2% in CC terms, due to pruning of non-strategic low margins business in BFSI vertical.

EBIT margin was up 32bps qoq in Q2FY23 to 11.4% despite of salary hikes. 60bps qoq benefit came from improved Utilization, 20bps qoq benefit from pruning of non-strategic low margins business in BFSI vertical, 45bps qoq benefit from SG&A and 30bps qoq currency benefit.

Tech M has taken the pruning exercise of the non-strategic low margins and non-scalable business of its portfolio companies, which it expects to have revenue loss of US\$100-120mn from discontinued business operations in FY23, out of which 60% has been executed in H1FY23 and balance will be done in H2FY23. This initiative is in order to uplift margins from current levels and this initiative might be continued even for FY24.

Other Income was up 138% qoq in Q2FY23 due to both higher Interest and Dividend income as well as Forex Gain. Forex gain stood at Rs127cr in Q2 (v/s Rs54cr in Q1FY23). Thus, led by stable operational performance and higher other income resulted in 13.6% qoq spike in Tech Ms PAT to Rs1285cr.

Tech M witnessed 5877 net employee additions on stable basis during Q2FY23 taking the total headcount to 1,63,912. LTM Attrition rate was down 260bps qoq at 19.6%, which is positive as its second consecutive quarter of easing of rate.

Key Financials (IND AS Consolidated)				
Y/E March (Rs cr)	FY2021	FY2022	FY2023E	FY2024E
Net Sales	37,855	44,646	53,994	59,018
% chg	2.7	17.9	20.9	9.3
Net Profit	4,428	5,566	5,612	6,543
% chg	9.8	25.7	0.8	16.6
EBITDA Margin (%)	18.1	18.0	16.0	16.9
FDEPS (Rs)	50.2	63.3	63.4	73.9
P/E (x)	15.4	21.4	16.9	14.5
P/BV (x)	2.7	4.4	3.5	3.4
RoE (%)	17.8	20.7	20.8	23.8
RoCE (%)	13.9	14.8	14.8	16.7
EV/Sales (x)	1.7	2.5	1.6	1.4
EV/EBITDA (x)	9.2	14.0	10.0	8.5
Net Debt/Equity	(0.0)	(0.1)	(0.1)	(0.2)

Source: Company & Anvil Research

Quarterly Financial Statement

Q2FY23 Consolidated IND AS								
Y/E March (Rs cr)	Q2FY23	Q1FY23	% chg qoq	Q2FY22	% chg yoy	H1FY23	H1FY22	% chg
Net Revenues	13,129	12,708	3.3	10,881	20.7	25,837	21,079	22.6
Cost of Revenues	8,920	8,616	3.5	7,084	25.9	17,536	13,755	27.5
Gross Profit	4,210	4,092	2.9	3,798	10.9	8,302	7,324	13.3
SG&A Expenses	2,226	2,212	0.6	1,802	23.5	4,438	3,453	28.5
EBITDA	1,984	1,880	5.5	1,995	(0.6)	3,864	3,872	(0.2)
Other Income	290	122	137.7	282	-	412	569	(27.6)
Impairment of Goodwill & non- current assets	24	-	-	-	-	24	-	-
Interest Cost	79	40	96.0	35	123.2	119	74	62.3
Depreciation	492	477	3.1	343	43.4	968	674	43.7
PBT	1,679	1,485	13.1	1,899	(11.6)	3,164	3,693	(14.3)
Tax	365	338	7.9	557	(34.5)	703	986	(28.7)
Minority Interest	(14)	(16)	-	(2)	-	(30)	(15)	-
Share of Profits/Exceptional items	(15)	0	-	(1)	-	(15)	(1)	-
Net Income	1,285	1,132	13.6	1,339	(4.0)	2,417	2,692	(10.2)
Diluted EPS (Rs)	14.5	12.8	13.6	15.1	(4.1)	27.3	30.4	(10.3)
Gross Profit Margin (%)	32.1	32.2	(0.1)	34.9	(2.8)	32.1	34.7	(2.6)
EBITDA Margin (%)	15.1	14.8	0.3	18.3	(3.2)	15.0	18.4	(3.4)
EBIT Margin (%)	11.4	11.0	0.3	15.2	(3.8)	11.2	15.2	(4.0)
Net Profit Margin (%)	9.8	8.9	0.9	12.3	(2.5)	9.4	12.8	(3.4)
Tax rate	21.7	22.8	(1.0)	29.3	(7.6)	22.2	26.7	(4.5)

Source: Company and Anvil Research

Key Operational Matrix

Revenue break-up (\$mn)	Q2FY23	Q1FY23	% chg qoq	Q2FY22	% chg yoy
Communications, Media & Entertainment (CME)	651	660	(1.3)	590	10.3
Enterprise Services	987	973	1.5	882	11.9
Net Revenues	1,638	1,633	0.3	1,473	11.2

Source: Company and Anvil Research

Vertical Split (USD mn)	Q2FY23	Q1FY23	Q2FY22	% chg qoq	% chg yoy
CME	651	660	590	(1.3)	10.3
Manufacturing	262	249	236	5.1	11.1
Technology	166	159	132	4.5	25.5
BFSI	267	272	240	(2.0)	11.0
Retail, Transport & Logistics	133	130	114	2.3	16.4
Others	160	163	160	(1.9)	(0.1)
Net Revenues	1,638	1,633	1,473	0.3	11.2

Source: Company and Anvil Research

Goographical Split (USD mn)	Q2FY23	Q1FY23	Q2FY22	% chg qoq	% chg yoy
North America	832	809	705	2.8	18.1
Europe	401	416	382	(3.5)	5.1
ROW	405	406	388	(0.3)	4.4
Net Revenues	1,638	1,633	1,473	0.3	11.2

Source: Company and Anvil Research

Revenues (USD mn)	Q2FY23	Q1FY23	Q2FY22	Chg qoq	Chg yoy
Active Clients	1,279	1,262	1,123		
Top 5 client	310	335	330	-7.6%	-6.1%
% of revenues	18.9%	20.5%	22.4%		
Top 10 clients	459	489	462	-6.1%	-0.8%
% of revenues	28.0%	29.9%	31.4%		
Top 20 clients	654	673	629	-3.0%	3.9%
% of revenues	39.9%	41.3%	42.7%		

Source: Company and Anvil Research

Outlook

- Focusing on Data, new competencies, new tech developments resulted in profitable growth for Tech M in Q2.
- Tech Ms investments on Metaverse, network operations, customer mgmt. are all yielding good results.
- As far as Telecom Network equipment business is concerned, the company wants to continue to stay focused on core purpose. Thus, software integration engineering around software devices and operations continues to be dominant area for Tech M. It will continue to be working with key telecom services providers in India, which is a voluminous game and in sync with its network related strategy in communication segment.
- Tech M has been witnessing good growth in Hi-tech vertical compared to peers as it has been investing both on organic as well as inorganic capabilities in Cloud computing, which is helping it in getting better customer coverage and wallet share. It is giving better deal wins and better penetration in existing customers accounts, which will continue to see traction even in near term. More so due to its strategy with Hyperscalers, more so in areas of Product development and Engineering, which will continue to see momentum going ahead.
- There was sharp decline in Top5 client revenue contribution as one project got closed in Q2.
- Pricing continues to be very strong lever and Tech M will continue to go for opportunities that will drive margin improvement.
- The company has articulated actions from structural and long-term perspective which will drive change not only in FY24 but beyond. These actions include geography mix with focus on growth mainly in US as well as in Europe markets, which will also help in driving better margin outcomes in long run.

- Tech M has been investing on large deals structure and hence large deals won 12-18mths back are now getting mainstream and will also help in improving margins. The company's competency in Digital engineering is also giving better returns.
- Nothing to be of threat from customer behavior until now, however the company will continue to monitor carefully macro-economic situation mainly the inflation in Europe. Decision making and deal closure is expected to slowdown in Europe, however sustainability spends will continue. The Pipeline remains robust and deal momentum continues.
- Clarity on client budgets for spends in FY24 will come at the Q4FY23 ending. But overall pipeline depending on clients' conversations continues to stay robust. **There could be some reprioritization of spend areas by clients. Open architecture, creating and converting network asserts into platform play will start seeing spends. Hence Tech M spends to start coming either in Network or Digital side.**
- Furloughs for H2FY23 are expected to be marginally higher on yoy basis.
- **Cash & Equivalents was down 14% qoq to Rs7254cr. Gross Debt was down 3.3% qoq to Rs1681cr in Q2FY23. DSO was down 2 days qoq to 98 days.**
- **Board approves Special Dividend of Rs18/share (up 20% yoy).**

Thus, we expect Tech M to register Top-line growth of 20.9% yoy in INR (growth of 12% yoy in USD terms) in FY23E led by strong TCV booking in FY22. However, PAT is expected to be up 0.8% yoy (led by margin pressure on account of supply constraints) and EPS to be at Rs63 in FY23E. For FY24E Top-line growth is expected to be 9.3% yoy in INR (growth of 9% yoy in USD terms) as we expect demand to ease down a bit yoy. However, PAT is expected to up 16.6% yoy (as margin pressure on account of supply constraints eases down a little) and EPS to be at Rs74.

Assumptions for Revenue projection	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Volume growth	6.6%	3.7%	4.5%	-2.0%	15.7%	15.0%	9.1%
Pricing growth	2.7%	0.8%	-0.6%	0.5%	1.8%	-2.2%	-0.1%
USD/INR impact	-3.7%	8.4%	2.2%	4.1%	0.4%	8.0%	0.3%
Revenues growth (in INR)	5.6%	12.9%	6.1%	2.7%	17.9%	20.9%	9.3%
Revenues growth (in USD)	9.6%	4.2%	4.3%	-1.4%	17.3%	12.0%	9.0%

Source: Company and Anvil Research

P&L (Rs cr)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Net sales	30,773	34,742	36,868	37,855	44,646	53,994	59,018
Other income	1,416	534	1,192	787	1,112	1,163	1,461
Total income	32,189	35,276	38,060	38,642	45,758	55,158	60,479
Cost of revenue	20,512	21,858	24,251	24,272	29,243	36,189	39,318
SG&A	5,551	6,548	7,108	6,737	7,383	9,146	9,738
Cost of sales	26,063	28,405	31,359	31,008	36,626	45,334	49,056
EBIDTA (Excl Other Income)	4,710	6,337	5,509	6,847	8,020	8,660	9,962
Interest,net	162	133	192	174	163	276	308
PBDT	4,547	6,204	5,317	6,673	7,857	8,384	9,654
Depreciation	1,085	1,129	1,446	1,458	1,520	1,996	2,125
PBT	4,879	5,609	5,063	6,002	7,449	7,552	8,990
Provision for tax	1,093	1,254	1,160	1,599.9	1,822	1,837	2,337
PAT	3,786	4,354	3,903	4,403	5,627	5,715	6,652
Pref div							
Exceptional Items	0	(66)	(6)	(50)	3	(46)	(61)
Minority Interest/ Others	14	9	136	75	(64)	(57)	(48)
Adjusted PAT	3,800	4,298	4,033	4,428	5,566	5,612	6,543

Source: Company and Anvil Research; Note: Financials in IND AS format

Balance Sheet (Rs cr)	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Equity capital	442	444	436	437	439	440	440
Reserve & Surplus	18401	19841	21377	24428	26447	26481	27024
Networth	18843	20284	21813	24865	26886	26920	27463
Long-Term Debt	771	209	179	166	142	132	122
Short-Term Debt	955	1196	2250	1496	1440	1549	1459
Total Debt	1726	1405	2428	1662	1582	1681	1581
Deferred tax liability	(571)	(608)	(809)	(837)	(364)	(964)	(1264)
Other long-term liab./Minority Int./ Amt pending Investigation	2346	2042	3731	3513	4002	2602	2102
Capital Employed	22344	23123	27164	29202	32105	30239	29883
Goodwill & IPR's	2773	2816	3388	4008	7426	7926	8626
Net block	4659	4074	4167	3914	6341	5841	5741
Capital WIP	240	276	50	118	165	365	505
Total fixed assets (incl Goodwill)	7672	7167	7605	8041	13932	14132	14872
Non-current Investments & Assets	4082	4105	5732	5469	5664	6464	6664
Inventory	66	75	36	24	41	0	0
Sundry Debtors	6498	6959	7577	6473	7468	7396	7600
Cash & bank	3044	2359	3148	2835	3975	5590	6890
Short-term Investments	2465	6590	5612	3500	4000	4000	4001
Loans & advances	4072	2906	3736	9490	5577	2077	76
Other current assets	1962	2677	3063	2933	3396	5396	6796
Sundry Creditors	2037	2489	3257	2785	4095	4495	4695
Other liabilities	4522	6251	4983	5465	6299	8799	10799
Provisions	958	975	1106	1312	1553	1523	1523
Net current assets	10590	11851	13827	15693	12510	9643	8347
Capital Deployed	22344	23123	27164	29202	32105	30239	29883

Source: Company and Anvil Research; Note: Financials in IND AS format

Key Ratios	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Absolute Growth (%)							
Revenue	5.6	12.9	6.1	2.7	17.9	20.9	9.3
EBITDA	12.6	34.6	-13.1	24.3	17.1	8.0	15.0
PAT	35.1	13.1	-6.2	9.8	25.7	0.8	16.6
Profitability Ratios (%)							
EBITDA margins	15.3	18.2	14.9	18.1	18.0	16.0	16.9
EBIT margins	11.8	15.0	11.0	14.2	14.6	12.3	13.3
PAT margins	12.3	12.4	10.9	11.7	12.5	10.4	11.1
ROCE	12.1	15.9	11.1	13.9	14.8	14.8	16.7
ROIC	16.7	28.5	17.0	17.3	20.3	24.4	30.5
ROA	12.0	12.5	10.2	10.6	11.2	11.2	12.4
ROE	20.2	21.2	18.5	17.8	20.7	20.8	23.8
Valuation Ratio (x)							
P/E (on FDEPS)	11.1	14.6	16.0	15.4	21.4	16.9	14.5
P/CEPS	8.6	11.6	11.7	11.5	16.7	12.4	10.9
P/BV	2.2	3.1	2.9	2.7	4.4	3.5	3.4
Dividend yield (%)	3.3	2.0	3.3	2.9	3.4	5.9	6.4
EV/Sales	1.2	1.6	1.6	1.7	2.5	1.6	1.4
EV/EBITDA	8.1	8.7	10.5	9.2	14.0	10.0	8.5
EV / Total Assets	1.3	1.9	1.7	1.6	2.4	1.8	1.6
Per Share Data (Rs)							
EPS (Basic)	43.0	48.4	46.3	50.7	63.4	63.8	74.4
EPS (fully diluted)	42.7	48.5	45.9	50.2	63.3	63.4	73.9
Cash EPS	55.3	61.2	62.8	67.3	80.7	86.5	98.6
Cash Per Share	161.3	145.7	203.7	190.0	219.7	274.3	308.4
DPS	15.5	14.1	23.9	22.1	45.5	63.2	68.3
Book Value per share	213.3	228.6	250.2	284.5	306.4	306.3	312.4
Liquidity ratios (x)							
Avg. Debtors days	70	71	72	68	57	50	46
Avg. Creditors days	29	32	38	33	41	36	35
Working capital cycle (ex-cash days)	90	100	106	124	70	27	9
Leverage ratios (x)							
Gross Debt to Equity	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Net Debt to Equity	(0.1)	(0.0)	(0.0)	(0.0)	(0.1)	(0.1)	(0.2)
Net Debt to EBITDA	(0.3)	(0.2)	(0.1)	(0.2)	(0.3)	(0.5)	(0.5)
Interest Coverage	31.0	43.1	27.4	35.5	46.8	28.4	30.2

Source: Company and Anvil Research; Note: Financials in IND AS format

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