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Investors' delight – Tech Mahindra Ltd.

Jan. 03, 2020

CMP: Rs. 777, FV: Rs. 5, Market Cap: Rs. 76,532 crores, EPS (TTM): Rs. 44.16, P/E: 18x, Target price: Rs. 936, Upside: 20%

Price movement chart



Source: Moneycontrol website

It is one of the best companies in IT space both on business model and management competency and integrity front. Tech Mahindra Ltd. is a leading provider of digital transformation, consulting and business reengineering services and solutions. The Company aims to being a Next Gen Services Partner through TechMNxt. The Company is working with some of the best startups in emerging technology areas like Artificial Intelligence, Machine Learning, IoT, Blockchain etc.

Tech Mahindra has once again retained its ranking in the Dow Jones Sustainability Index under both the DJSI World category and the DJSI Emerging Markets 2019. Tech Mahindra is one of three Indian companies to be included in the DJSI World Index.

Q2FY20 result highlights

The Company had a great record quarter in deal wins, one of the largest deals in Tech Mahindra's history. It ended H1 with the highest TCV across both Enterprise and Communications vertical. Its pipeline remains robust. Overall, the Company enjoyed robust broad-based revenue growth, practically across all the geography in constant currency terms. Digital transformation in the Company was worth appreciating. The digital revenue has crossed half a billion mark in Q2FY20 quarter. Contribution from digital revenue stood at 39% of the quarter's revenue. Clearly, the Company's focus on gen technologies, its focus on TechMNxt has put it in a good position. On a constant currency basis, the Company witnessed revenues growth of 4.1% on QoQ basis to touch US\$ 1,287 million and about 7.3% YoY on a constant currency basis. Within that, Enterprise business had a very strong quarter of 5.6% growth in CC terms and Communications grew about 2% in CC terms sequentially.



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Financial highlights

Revenue at Rs. 9,070 crore; up 4.8% QoQ; EBITDA at Rs.1,501 crore; up 14.2% QoQ;
Margins at 16.5%; up 130 bps QoQ
Profit after tax (PAT) at Rs. 1,124 crore; up 17.2% QoQ
Earnings per share (EPS) stood at Rs. 12.88

Q2FY20 Financial highlights in (USD)

Revenue at USD 1,287.2 mn; up 3.2% QoQ
Revenue growth at 4.1% in constant currency terms
Digital revenues grew 11.8% QoQ, at 39.0% of Revenues
EBITDA at USD 211.8 mn; up 11.5% QoQ
Consolidated PAT at USD 158.6 mn, up 14.3% QoQ
Total headcount at 131,522; up 5,749 QoQ

CP Gurnani, Managing Director & Chief Executive Officer, Tech Mahindra, said, "We are thankful to our customers for believing in our capabilities despite a tough demand environment. Our consistent large deal wins is a testimony of our differentiation in the

marketplace. We are confident of our growth outlook for both Communications and Enterprise businesses. 'Digital' continues to be a strong growth driver, as we help our customers in their transformation journey."

Manoj Bhat, Chief Financial Officer, Tech Mahindra, said, "We have witnessed a broad based growth across geographies and across our customers. We continue to focus on margin improvement while transitioning some of the large deals in a volatile macro economic environment."

The Company had earlier delivered a decent performance in FY19. The Company reported revenue growth of 12.9 percent to touch Rs. 34,742 crores. In dollar terms, the Company witnessed growth of 4.2 percent and in constant currency terms it was 5.8 percent. It was heartening to see margin expansion in FY19. FY19 EBITDA margin witnessed an improvement of 290 bps on yoy basis. PAT clocked yoy growth of 18 percent to Rs. 4,298 crores. PAT margin stood at 12.37 percent.

The Company's focus has been to deepen its presence in other verticals besides Communications. The strategy has worked well for the Company which was displayed in the robust performance of the with the Manufacturing vertical which crossed one billion dollars in Revenue in FY19.

The Company is strong in generating Operating Cashflows and Free Cashflows. For FY19, the Company generated record free cash flows of Rs. 3,708 crores. The Company also initiated its maiden Share Buyback FY19 as part of its capital allocation policy.

The Company continues to expand its industry leading capabilities in Communication business as it positions itself to capture the '5G Wave'. The Company has been investing in developing capabilities and partnerships addressing multiple facets of 5G roll-out and its



investments in Altiostar or Rakuten 5G testing lab are examples of its commitment in this area.

Recently, the Company announced expansion of its strategic collaboration with AT&T to accelerate AT&T's IT network application, shared systems modernization and movement to the cloud. Tech Mahindra will assume management of many of the applications which support AT&T's network and shared systems. The multi-year agreement will enable AT&T to focus on core objectives, including having the most advanced software defined 5G network, and migrate the majority of its non-network workloads to the public cloud by 2024. This comprehensive program will help drive sustainable operational improvement across the network and software development domains. Together, AT&T and Tech Mahindra aims to improve the agility in rolling out and supporting networks of the future, while improving returns on investment through technology—led transformation AT&T and Tech Mahindra will integrate several world class technologies and platforms in areas like artificial intelligence, DevOps, data analytics and 5G.

Other key wins in Q2FY20

- 1) Engaged with an American managed-cloud computing company to enhance customer experience and operational efficiencies through technology transformation.
- 2) Selected by one of the largest healthcare organization based in the US as their infrastructure managed services partner to drive transformation of IT operations deploying AI ML based Automation.
- 3) Selected by a leading European telecom provider for Network Operations transformation and NOC (Network Operations Center) managed services.
- 4) Selected by an Australian superannuation firm as a strategic partner for a multi-year digital engagement for Salesforce implementation, analytics, cyber-security and application modernization.
- 5) Signed a deal with Asia Pacific based regulator to digitally transform its operations and drive business agility.

We recommend to **"Buy"** the Company with a target price of Rs. 936 (18x at estimated FY21 EPS of Rs. 52) for investors with a horizon of 9 -12 months.



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Recommendation parameters for fundamental reports:

Buy – Absolute return of 20% and above

Accumulate – Absolute return between 15% and above

Book profits: On achieving the price target given in the research report for a particular Company or on a occurrence of a specific event leading to change in fundamentals of the Company recommended

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