

October 26, 2020

Q2FY21 Result Update

Change in Estimates | Target | Reco

Change in Estimates

	Current		Previous	
	FY22E	FY23E	FY22E	FY23E
Rating	BUY		BUY	
Target Price	1,711		1,693	
Sales (Rs. m)	1,12,571	1,25,997	1,08,713	1,24,514
% Chng.	3.5	1.2		
EBITDA (Rs. m)	21,330	23,831	20,711	23,621
% Chng.	3.0	0.9		
EPS (Rs.)	80.3	90.8	78.6	90.7
% Chng.	2.1	0.2		

Key Financials - Standalone

Y/e Mar	FY20	FY21E	FY22E	FY23E
Sales (Rs. m)	88,436	98,664	1,12,571	1,25,997
EBITDA (Rs. m)	16,505	18,112	21,330	23,831
Margin (%)	18.7	18.4	18.9	18.9
PAT (Rs. m)	11,849	12,197	14,939	16,907
EPS (Rs.)	63.6	65.5	80.3	90.8
Gr. (%)	14.8	3.0	22.5	13.2
DPS (Rs.)	35.0	19.0	19.0	19.0
Yield (%)	2.5	1.4	1.4	1.4
RoE (%)	21.4	20.5	22.6	21.7
RoCE (%)	25.6	26.5	28.7	27.5
EV/Sales (x)	2.7	2.4	2.0	1.7
EV/EBITDA (x)	14.3	13.0	10.6	9.0
PE (x)	21.7	21.1	17.2	15.2
P/BV (x)	4.4	4.2	3.6	3.1

Key Data

MBFL.BO | MPHL IN

52-W High / Low	Rs.1,465 / Rs.612
Sensex / Nifty	40,686 / 11,930
Market Cap	Rs.258bn / \$ 3,505m
Shares Outstanding	187m
3M Avg. Daily Value	Rs.1427.07m

Shareholding Pattern (%)

Promoter's	56.16
Foreign	22.14
Domestic Institution	16.18
Public & Others	5.52
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	(0.1)	98.6	49.0
Relative	(7.6)	55.6	43.1

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Strong, Steady, Resilient!

Quick Pointers:

- Strong-** Revenue & margin performance, **Steady-** Cash Flow generation, **Resilient-** negligible exposure to directly COVID impacted verticals of travel, hospitality & energy.
- Strong growth in Direct Core business (+10.9% QoQ CC) & DXC continued decline of 15.5% QoQ CC & helping further de-rising the business profile (accounts to ~16% of revs).
- TCV now is at US\$1bn ttm up 70.2% YoY. Strong TCV of deal wins, improved pipeline and good conversion rates provide good growth visibility for FY22.

Mphasis reported strong beat in Q2 revenue of 327.4\$ Mn with growth of +6% QoQ CC / 18.4% YoY CC / 7.2% QoQ USD (Ple: 3% QoQ CC, 3.9% QoQ USD). Direct Channels grew at a robust 10.9% QoQ CC contributing 83.8% to revenues while DXC channel revenues declined 15.5% QoQ. Growth was led by banking and capital markets that grew a remarkable 17% QoQ. EBIT margin (pre-forex impact) at 16.2% grew at modest rate (+45 bps QoQ) and was in-line with our estimates (Ple: 16%). Margin band was maintained at 15.5-16.5% & aspiring to grow above that also.

Mphasis won new deals with TCV of USD 360 million in Q2 FY21 with 73 % of the deal wins in New-Gen Services, TCV on ttm basis is at US\$1 bn, up 75% YoY. Management is focusing on increasing wallet share in existing accounts and gaining new clients through differentiated cutting edge technology solutions. We continue to maintain our bullish stance on Mphasis as 1) Strong presence in mortgages, payments, consumer banking and wealth management, 2) Strong Leadership team, 3) Superior fundamentals than other midcaps. We were already ahead than street on estimates, so our estimates remains largely unchanged (avg 1.2% increase for FY22/23). We continue to value Mphasis on 20X earnings multiple on Sep-22 EPS of INR 85.6 to arrive at a changed TP of INR 1711 (earlier:1693). Mphasis is currently trading at attractive multiples of 17.2/15.2X on EPS of 80.3/91 on FY22/23 respectively. Maintain Buy.

- Strong beat in revenue:** Mphasis reported strong beat in Q2 revenue of 327.4\$ Mn with growth of +6% QoQ CC / 18.4% YoY CC / 7.2% QoQ USD (Ple: 3% QoQ CC, 3.9% QoQ USD). Direct Channels grew at a robust 10.9% QoQ CC contributing 83.8% to revenues while DXC channel revenues declined 15.5% QoQ. Within this Direct channel, New Gen services grew at 17.6% YoY on reported basis. DXC is not a concern for management as its share in revenue has further declined to 16.2%. They are also working on building visibility of revenues from DXC and intend to continue their partnership (Q1: 61\$ mn, Q2: 53\$ mn). Mphasis is confident of DXC partnership continuing beyond Sep 2021 despite indications that DXC will reduce spend on third-party contractors. DXC has ~US\$200 mn committed spending to Mphasis till Sep 2021.

- Growth was led by **Banking & Capital Markets (BCM)** vertical (53% of revenues) which grew at 17.4% QoQ USD followed by recovery in Insurance vertical up 2.5% QoQ USD. Vendor consolidations in BCM segment contributing to market share gains in this vertical. Kind of vendors displaced due to market share gains range from large global peers, Indian peers to local firms underscores their competence in the business. They have strong outlook for BCM with good growth driven by DCM and digital risk offerings. They saw spend re-alignment in **logistics** vertical (-8.7% QoQ INR) and is expected to recover in Q3. Logistics vertical. **Insurance** pipeline was robust in last few quarters which will be converted to revenue in coming quarters.
- Europe (contributing to 11% of revenues) continues to be the focus area and Direct channel revenues in Europe have grown by 23% YoY in CC terms and deal pipeline continues to be strong. **Cloud focused partnerships** now form 36% of their revenues and there has been 3x increase of cloud pipeline in last one year.
- **Stable operating margins:** EBIT margin (pre-forex impact) at 16.2% grew at modest rate (+45 bps QoQ) and was in-line with our estimates (Ple: 16%). Gross margins improved by 200 bps due to significant improvement in segmental gross margins for all the verticals while G&A costs increased by 100 bps QoQ due to bench cost (lower utilization), ramp up costs & transition costs. They are prioritizing converting deals into revenues so in the short run offshoring may not improve but they target is to improve it in the long terms. They also faced pressure in onsite local hiring due to visa related restrictions and prioritize to build robust supply chain and gain market share over further cost optimization in the short term.
- Management indicated that they will maintain margins in the narrow band of 15.5% - 16.5% going forward and focus on investing in skilling talent and building competencies in next generation growth areas. Net Income was 2.99 INR Bn up 8.8% on QoQ.
- **Highest ever deal wins and continued strong deal momentum:** Mphasis won new deals with TCV of USD 360 million in Q2 FY21 with 73 % of the deal wins in New-Gen Services. This includes one large deal win of over USD 200+ million TCV. Net new TCV exceeded 1Bn \$ on trailing 12-month basis. Pipeline has increasing component of large integrated deals in nature. Deal pipeline is at record high up 75% YoY with multiple large deals to be expected in Q3. 80% of new deal wins are garnered due to proactively identifying problems and offering solutions for their customers. In coming quarters, they will have large deal wins with longer tenures. They have achieved healthy conversion of clients at each stage to the next (50% conversion rate) and consistent new client wins.
- In the past twelve months they have added 2 new clients in +75 Mn bucket, 1 new client in +20Mn bucket and 3 new clients in +10 Mn bucket. Revenue share from new clients was 30%. **Historically they have seen strong correlation of 0.85 of revenues with TCV.** We expect strong deal flow to continue which will provide pivot for growth in FY21/22E. Management is focusing on increasing wallet share in existing accounts and gaining new clients through differentiated cutting edge technology solutions.

Exhibit 1: Q2FY21: Quick view on results

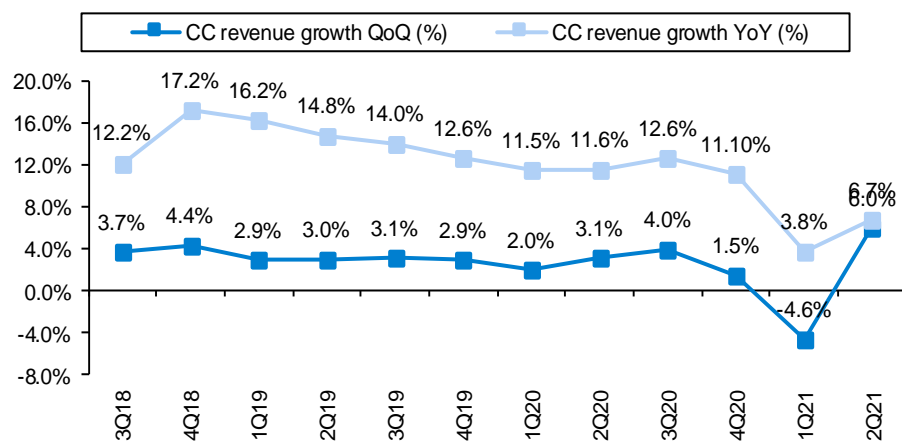
Y/e March	2Q21	1Q21	QoQ gr.	2Q20	YoY gr.	% var from est	Pl e
Consolidated Sales - pre forex (US\$ m)	327	305	7.2%	304.7	7.4%	3.4%	316.7
Consolidated Sales - post forex (Rs m)	24,354	22,882	6.4%	21,581	12.8%	4.1%	23,404
EBITDA	4524	4178	8.3%	4052	11.6%		
EBIT	3,924	3,583	9.5%	3,470	13.1%	4.8%	3,745
<i>EBIT margin</i>	<i>16.1%</i>	<i>15.7%</i>	<i>45 bps</i>	<i>16.1%</i>	<i>3 bps</i>	<i>11 bps</i>	<i>16.0%</i>
PBT (Rs m)	4,038	3,765	7.3%	3,604	12.0%	0.9%	4,001
Tax (Rs m)	1,046	1,015	3.1%	871	20.1%	2.5%	1,021
PAT (Rs m)	2,992	2,750	8.8%	2,733	9.5%	0.4%	2,980
EPS (Rs)	16.0	14.7	8.3%	14.54	9.8%	0.4%	15.89

Source: Company, PL

Exhibit 2: Change in Estimates

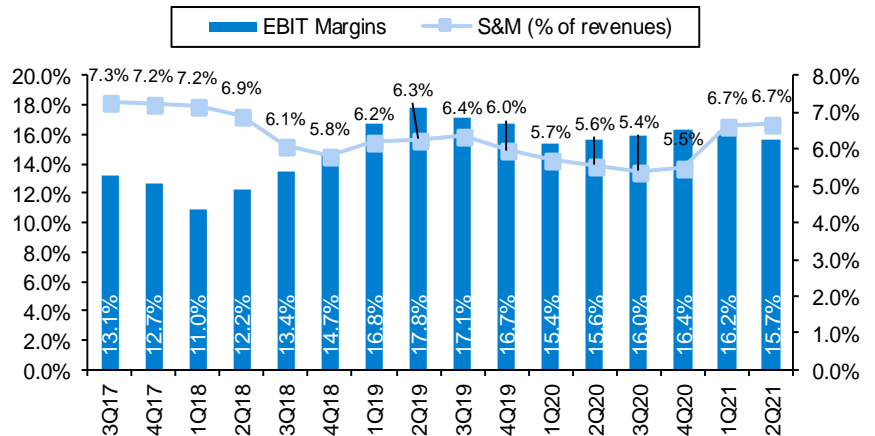
Y/e March	FY21E	FY22E	FY23E
USD revenues (US\$ m)			
- New	1,325	1,495	1,652
- Old	1,281	1,458	1,665
<i>Change (%)</i>	<i>3.4%</i>	<i>2.5%</i>	<i>-0.8%</i>
EBIT Margin			
- New	15.9%	16.8%	16.9%
- Old	15.9%	16.8%	17.0%
<i>Change (%)</i>	<i>3 bps</i>	<i>0 bps</i>	<i>-1 bps</i>
Recurring EPS - Fully diluted (Rs)			
- New	65.1	79.7	90.2
- Old	63.3	78.0	91.0
<i>Change (%)</i>	<i>2.8%</i>	<i>2.1%</i>	<i>-0.9%</i>

Source: PL

Exhibit 3: Revenue growth momentum to improve


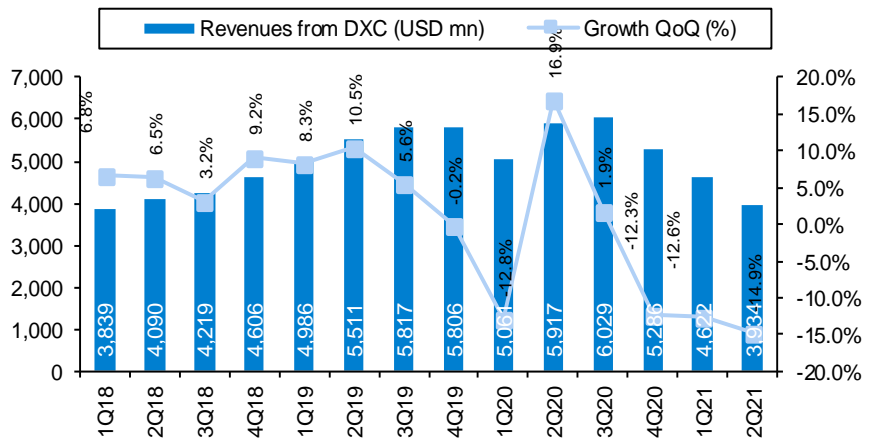
Source: Company, PL

Exhibit 4: Stable Margin Performance



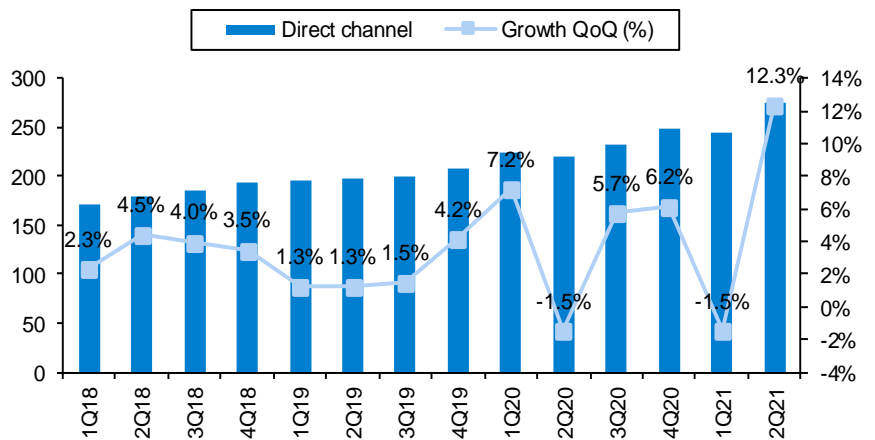
Source: Company, PL

Exhibit 5: DXC decline was steep



Source: Company, PL

Exhibit 6: Direct channel continued growth momentum



Source: Company, PL

Exhibit 7: Revenue by service offerings

(Rs m)	2Q21	1Q21	QoQ gr.	2Q20	YoY gr.
Application Services	14,300	14,695	-2.7%	6,502	119.9%
Business Process Services	6,434	4,852	32.6%	2,694	138.8%
Infrastructure Services	3,504	3,490	0.4%	1,907	83.7%
% of Total					
Application Services	58.7%	64.2%	-550 bps	30.1%	2859 bps
Business Process Services	26.4%	21.2%	521 bps	12.5%	1394 bps
Infrastructure Services	14.4%	15.3%	-86 bps	8.8%	555 bps

Source: Company, PL

Exhibit 8: Vertical-wise revenues

(Rs m)	2Q21	1Q21	QoQ gr.	2Q20	YoY gr.
Banking and Capital Market	12,950	11,240	15.2%	9,834	31.7%
Insurance	2,308	2,293	0.7%	2,414	-4.4%
Information, Communication & Entertainment	2,860	3,258	-12.2%	3,459	-17.3%
Emerging Industries	6,120	6,248	-2.0%	5,754	6.4%
% of Total					
Banking and Capital Market	53.2%	49.1%	405 bps	45.6%	761 bps
Insurance	9.5%	10.0%	-54 bps	11.2%	-171 bps
Information, Communication & Entertainment	11.7%	14.2%	-249 bps	16.0%	-428 bps
Emerging Industries	25.1%	27.3%	-218 bps	26.7%	-153 bps
Gross Profit Margin					
Banking and Capital Market	25.1%	24.4%	70 bps	25.1%	7 bps
Insurance	32.4%	28.5%	389 bps	27.8%	465 bps
IT, Communication & Entertainment	19.7%	18.5%	115 bps	19.4%	32 bps
Emerging Industries	36.4%	36.7%	-33 bps	30.4%	598 bps

Source: Company, PL

Exhibit 9: Geography-wise revenues

(Rs m)	2Q21	1Q21	QoQ gr.	2Q20	YoY gr.
Americas	18,929	17,696	7.0%	17,005	11.3%
EMEA	2,624	2,749	-4.5%	2,176	20.6%
India	1,101	948	16.1%	1,131	-2.7%
RoW	1,584	1,644	-3.6%	1,150	37.7%
Total	24,238	23,037	5.2%	21,462	12.9%
% of Total					
America	78.1%	76.8%	128 bps	79.2%	-114 bps
EMEA	10.8%	11.9%	-111 bps	10.1%	69 bps
India	4.5%	4.1%	43 bps	5.3%	-73 bps
RoW	6.5%	7.1%	-60 bps	5.4%	118 bps
Total	100.0%	100.0%		100.0%	

Source: Company, PL

Exhibit 10: Client Metrics

	2Q21	1Q21	QoQ gr.	2Q20	YoY gr.
>1mn	80	79	1.3%	104	-23.1%
>5mn	31	32	-3.1%	35	-11.4%
>10mn	17	16	6.3%	17	0.0%
>20mn	8	7	14.3%	8	0.0%
Top Customer	2,922	2,746	6.4%	3,237	-9.7%
Top 5	9,498	8,924	6.4%	10,575	-10.2%
Top 2-5	6,576	6,178	6.4%	7,338	-10.4%
Top 6-10	5,601	4,805	16.6%	5,611	-0.2%
Top 10	12,177	10,983	10.9%	12,949	-6.0%
Non Top 10 customers	12,177	11,899	2.3%	8,632	41.1%
% of Revenue					
Top Customer	12.0%	12.0%	0 bps	15.0%	-300 bps
Top 5	39.0%	39.0%	0 bps	49.0%	-1000 bps
Top 10	50.0%	48.0%	200 bps	60.0%	-1000 bps
Non Top 10 customers	50.0%	52.0%	-200 bps	40.0%	1000 bps

Source: Company, PL

Exhibit 11: Segment-wise revenues

(Rs m)	2Q21	1Q21	QoQ gr.	2Q20	YoY gr.
Direct International	19,823	18,075	9.7%	14,864	33.4%
HP Channel	3,934	4,622	-14.9%	5,917	-33.5%
Direct Others	481	340	41.5%	681	-29.4%
% of Total					
Direct International	81.4%	79.0%	240 bps	68.9%	1252 bps
HP Channel	16.2%	20.2%	-405 bps	27.4%	-1126 bps
Direct Others	2.0%	1.5%	49 bps	3.2%	-118 bps

Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Net Revenues	88,436	98,664	1,12,571	1,25,997
YoY gr. (%)	14.4	11.6	14.1	11.9
Employee Cost	62,951	70,109	80,089	89,080
Gross Profit	25,485	28,555	32,482	36,916
Margin (%)	28.8	28.9	28.9	29.3
SG&A Expenses	4,093	4,265	5,162	6,073
Other Expenses	-	-	-	-
EBITDA	16,505	18,112	21,330	23,831
YoY gr. (%)	24.7	9.7	17.8	11.7
Margin (%)	18.7	18.4	18.9	18.9
Depreciation and Amortization	2,317	2,376	2,414	2,475
EBIT	14,188	15,735	18,917	21,356
Margin (%)	16.0	15.9	16.8	16.9
Net Interest	-	-	-	-
Other Income	967	720	1,122	1,328
Profit Before Tax	15,155	16,455	20,038	22,684
Margin (%)	17.1	16.7	17.8	18.0
Total Tax	3,306	4,258	5,099	5,777
Effective tax rate (%)	21.8	25.9	25.4	25.5
Profit after tax	11,849	12,197	14,939	16,907
Minority interest	-	-	-	-
Share Profit from Associate	-	-	-	-
Adjusted PAT	11,849	12,197	14,939	16,907
YoY gr. (%)	10.6	2.9	22.5	13.2
Margin (%)	13.4	12.4	13.3	13.4
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	11,849	12,197	14,939	16,907
YoY gr. (%)	10.6	2.9	22.5	13.2
Margin (%)	13.4	12.4	13.3	13.4
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	11,849	12,197	14,939	16,907
Equity Shares O/s (m)	186	186	186	186
EPS (Rs)	63.6	65.5	80.3	90.8

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Non-Current Assets				
Gross Block	8,897	8,888	9,788	10,587
Tangibles	8,897	8,888	9,788	10,587
Intangibles	-	-	-	-
Acc: Dep / Amortization	-	-	-	-
Tangibles	-	-	-	-
Intangibles	-	-	-	-
Net fixed assets	8,897	8,888	9,788	10,587
Tangibles	8,897	8,888	9,788	10,587
Intangibles	-	-	-	-
Capital Work In Progress	-	-	-	-
Goodwill	21,405	20,885	20,885	20,885
Non-Current Investments	-	-	-	-
Net Deferred tax assets	2,157	1,349	1,349	1,349
Other Non-Current Assets	10,945	9,748	9,748	9,748
Current Assets				
Investments	-	-	-	-
Inventories	-	-	-	-
Trade receivables	8,353	9,461	10,794	12,082
Cash & Bank Balance	21,035	21,831	31,631	42,315
Other Current Assets	-	-	-	-
Total Assets	87,535	85,975	99,956	1,14,605
Equity				
Equity Share Capital	1,865	1,866	1,866	1,866
Other Equity	56,431	58,693	69,495	82,264
Total Network	58,296	60,559	71,361	84,131
Non-Current Liabilities				
Long Term borrowings	-	-	-	-
Provisions	-	-	-	-
Other non current liabilities	7,567	7,398	7,398	7,398
Current Liabilities				
ST Debt / Current of LT Debt	-	-	-	-
Trade payables	21,672	18,018	21,197	23,077
Other current liabilities	-	-	-	-
Total Equity & Liabilities	87,535	85,975	99,956	1,14,605

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
PBT	15,155	16,455	20,038	22,684
Add. Depreciation	2,317	2,376	2,414	2,475
Add. Interest	813	382	80	400
Less Financial Other Income	967	720	1,122	1,328
Add. Other	-	-	-	-
Op. profit before WC changes	18,285	19,214	22,532	25,559
Net Changes-WC	2,825	(2,804)	(102)	(1,287)
Direct tax	(3,306)	(4,258)	(5,099)	(5,777)
Net cash from Op. activities	17,804	12,151	17,331	18,494
Capital expenditures	(5,677)	(1,847)	(3,314)	(3,274)
Interest / Dividend Income	-	-	-	-
Others	-	-	-	-
Net Cash from Invt. activities	(5,677)	(1,847)	(3,314)	(3,274)
Issue of share cap. / premium	3	1	-	-
Debt changes	-	-	-	-
Dividend paid	(7,621)	(4,137)	(4,137)	(4,137)
Interest paid	(813)	(382)	(80)	(400)
Others	223	(4,990)	-	-
Net cash from Fin. activities	(8,208)	(9,508)	(4,217)	(4,537)
Net change in cash	3,918	796	9,800	10,683
Free Cash Flow	12,126	10,304	14,017	15,220

Source: Company Data, PL Research

Quarterly Financials (Rs m)

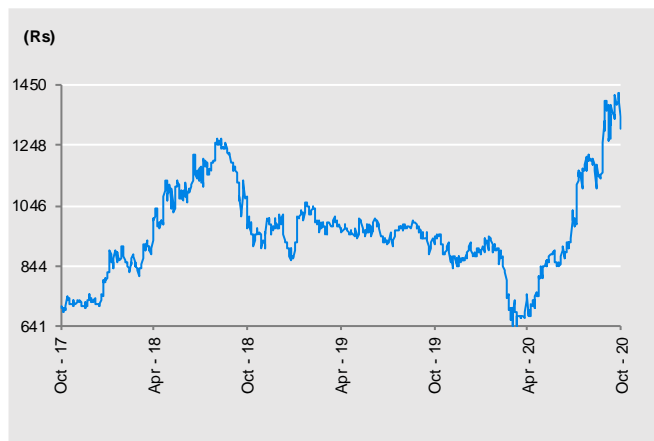
Y/e Mar	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Net Revenue	22,767	23,462	22,882	24,354
YoY gr. (%)	12.4	13.7	6.0	7.0
Raw Material Expenses	16,228	16,591	16,261	16,974
Gross Profit	6,539	6,871	6,621	7,380
Margin (%)	28.7	29.3	28.9	30.3
EBITDA	4,269	4,441	4,178	4,524
YoY gr. (%)	25.4	18.6	3.1	6.0
Margin (%)	18.8	18.9	18.3	18.6
Depreciation / Depletion	575	610	595	600
EBIT	3,694	3,831	3,583	3,924
Margin (%)	16.2	16.3	15.7	16.1
Net Interest	-	-	-	-
Other Income	172	319	182	114
Profit before Tax	3,866	4,150	3,765	4,038
Margin (%)	17.0	17.7	16.5	16.6
Total Tax	929	618	1,015	1,046
Effective tax rate (%)	24.0	14.9	27.0	25.9
Profit after Tax	2,937	3,532	2,750	2,992
Minority interest	-	-	-	-
Share Profit from Associates	-	-	-	-
Adjusted PAT	2,937	3,532	2,750	2,992
YoY gr. (%)	10.3	33.4	0.6	1.9
Margin (%)	12.9	15.1	12.0	12.3
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	2,937	3,532	2,750	2,992
YoY gr. (%)	10.3	33.4	0.6	1.9
Margin (%)	12.9	15.1	12.0	12.3
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	2,937	3,532	2,750	2,992
Avg. Shares O/s (m)	186	186	187	186
EPS (Rs)	15.8	18.9	14.7	16.1

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY20	FY21E	FY22E	FY23E
Per Share(Rs)				
EPS	63.6	65.5	80.3	90.8
CEPS	76.0	78.3	93.2	104.1
BVPS	312.8	325.2	383.4	452.1
FCF	65.1	55.3	75.3	81.8
DPS	35.0	19.0	19.0	19.0
Return Ratio(%)				
RoCE	25.6	26.5	28.7	27.5
ROIC	37.1	34.6	34.1	29.9
RoE	21.4	20.5	22.6	21.7
Balance Sheet				
Net Debt : Equity (x)	(0.4)	(0.4)	(0.4)	(0.5)
Debtor (Days)	34	35	35	35
Valuation(x)				
PER	21.7	21.1	17.2	15.2
P/B	4.4	4.2	3.6	3.1
P/CEPS	76.0	78.3	93.2	104.1
EV/EBITDA	14.3	13.0	10.6	9.0
EV/Sales	2.7	2.4	2.0	1.7
Dividend Yield (%)	2.5	1.4	1.4	1.4

Source: Company Data, PL Research

Price Chart
Recommendation History


No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	05-Oct-20	BUY	1,693	1,345
2	01-Oct-20	BUY	1,693	1,383
3	27-Jul-20	BUY	1,302	1,118
4	04-Jul-20	Accumulate	943	887
5	15-May-20	Accumulate	852	803
6	12-Apr-20	Accumulate	839	676
7	10-Feb-20	Accumulate	1,094	929
8	03-Jan-20	Accumulate	1,010	884

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Coforge	BUY	2,784	2,457
2	Cyient	BUY	456	379
3	HCL Technologies	BUY	1,101	830
4	Hexaware Technologies	BUY	495	466
5	Infosys	BUY	1,436	1,137
6	L&T Technology Services	Accumulate	1,860	1,754
7	Larsen & Toubro Infotech	BUY	3,465	3,100
8	Mindtree	BUY	1,625	1,438
9	Mphasis	BUY	1,693	1,345
10	Persistent Systems	BUY	1,304	1,304
11	Redington (India)	BUY	146	117
12	Sonata Software	BUY	436	311
13	Tata Consultancy Services	BUY	3,200	2,736
14	TeamLease Services	BUY	2,753	2,265
15	Tech Mahindra	BUY	966	823
16	Wipro	BUY	415	376
17	Zensar Technologies	BUY	216	192

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly

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