

MASTEK LTD.

Industry	IT
Bloomberg	MAST:IN
BSE CODE	523704

Strong order backlog to drive growth, Margin in 12% range as investment plan continues in FY19

RATING	BUY
CMP	439
Price Target	541
Potential Upside	23%

Rating Change	↔
Estimate Change	↓
Target Change	↔

Stock Info

52wk Range H/L	644/321
Mkt Capital (Rs Cr)	1,044
Free float (%)	52%
Avg. Vol 1M (,000)	227
No. of Shares (Cr)	2
Promoters Pledged %	NA

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Key Highlights-

- ❑ Company reported in line performance with revenue growth of 5%QoQ (vs. our estimates of 4.8% QoQ) however margin declined 50bps impacted by wage revision and emigration expenses.
- ❑ The Company posted an impressive growth in its order backlog in 2QFY19 which now stand at 599.2 crore (66.3mn pound) as compared 501crore last quarter.
- ❑ With New leadership team (appointment of CEO Mr. John Owen), strong performance by UK and robust order backlog, the management expects the growth to continue in FY19 too.
- ❑ Under capital allocation policy, the board has declared 70% as interim dividend (Rs3.5 per share).

2Q FY19 Result Update

Company posted stable set of numbers in 2QFY19. Revenue for the quarter stood at Rs257 (growth of 5%QoQ) led by strong performance in UK market and continued traction from strategic account. EBITDA for the quarter stood at Rs31.30 crore (growth of 1.2%). EBITDA Margin declined by 50 bps from 12.7% to 12.2% mainly due to wage revision and expenses in emigration in US. Pat stood at Rs25.10crore, growth of 12%QoQ. Other income increased from Rs3.13crore to Rs 8.70 crore due to income coming from one of the company folded. Thus leading to improved pat margin of 60bps.

View and Valuation

Mastek continued to report strong growth of 30 % in 1HFY19 (from Rs384 crore in 1FY18 to Rs501crore) led by continued performance in its mature market (UK) and robust growth in the new market. Even the margins improved in 1HFY19 by 40 bps showing the continued improvement in operational parameters.

Going forward, we expect company to post better performance in FY19 led by strong order book, continued growth in the mature market and strong traction from public sector (growth of 29% in 2QFY19). As order backlog increased 20% QoQ (from Rs 501 crore to Rs599)and 33%YoY in 1HFY19, we are confident of seeing the momentum to continue in 2HFY19 on the back of continued client addition and increase in wallet share with existing customer. On mature market (UK), since the company has strongly positioned in the UK market for long time, continued growth in UK quarter on quarter (grew 7%QoQ in 2QFY19) and strong pipeline gives us confidence strong performance in FY19 too. Even the US market which has started 24 months back is expected to post robust growth led by continued growth in digital business.

On the margin front, we have reduced margin by 20 bps in FY19 as the management continues to plan to invest addition income back in the company. Thus resulting in near term impact in margin but profitable for long term business position

We expect Mastek to post 23% revenue CAGR over FY18 to FY20E. We value the stock at a target price of Rs541 (11x FY20EPS) and recommend BUY

Key Risks to our rating and target

- ❑ Slower than expected growth in UK Market.
- ❑ Delay in order execution.

KEY FINANCIAL/VALUATIONS	FY16	FY17	FY18	FY19E	FY20E
Net Sales	527	562	817	1040	1242
EBITDA	18	53	100	130	159
EBIT	2	40	81	112	136
PAT	14	37	70	99	115
EPS (Rs)	6	16	30	42	49
EPS growth (%)	165%	164%	90%	41%	17%
ROE (%)	4	7	12	15	16
ROCE (%)	4	10	15	19	19
BV	139	190	235	270	312
P/E (x)	24	11	17	10	9
P/B (X)	1	1	2	2	1

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2QFY19 Results
In Line with the Estimates

Financials	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	YoY %	QoQ%	FY17	FY18	YoY %
Net Sales /	198	210	224	244	257	30%	5%	562	817	45.3%
Other Income	6	6	7	3	9	55%	178%	10	21	116%
COGS	-	-	-	-	-			-	-	
Employee	116	126	130	140	150	29%	7%	321	481	49.6%
Other Expenses	58	57	66	73	76	30%	4%	188	237	25.8%
EBITDA	24	26	28	31	31	32%	1%	53	100	88.5%
Depreciation	5	5	4	4	5	-6%	21%	13	19	45.9%
EBIT	19	21	24	27	27	42%	-2%	40	81	102.2%
Interest	1	1	2	1	2	68%	92%	3	6	127.2%
PROFIT BEFORE	23	25	30	29	33	44%	14%	47	96	103.7%
Tax	5	7	10	6	8	45%	20%	7	26	280.8%
PAT	17	18	19	22	25	44%	12%	37	70	89.6%

Strong growth continued in UK market

Revenue for the quarter stood at Rs257 (growth of 5%QoQ) led by strong performance in UK market and continued traction from strategic account.UK continued to be strong and grew 7%QoQ and 36.6%YoY.Even US which was started 24 months back have shown a steady growth of 2.4%QoQ and YoY14.4%.However other market declined by 15.9%QoQ.

Industry wise, Government and Retail led the growth in the industry by growing 29% and 3.6% QoQ. However, financial service declined 9%QoQ.

VERTICALS(in crore)	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	QoQ%	YoY %
UK	123	136	143	161	174	186	7.0%	36.6%
US	57	58	62	60	65	67	2.4%	14.4%
Others	6	4	4	2	5	4	-15.9%	9.7%

Government showed robust performance;Softness seen in financial service

Industry (in crore)	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	QoQ%	YoY %
Government	64	68	70	78	77	99	29.0%	45.1%
Other Financial Services	36	34	45	43	54	49	-9.1%	42.5%
Retail Services	70	77	78	80	90	93	3.6%	20.8%
IT & Other services	16	18	17	19	23	16	-33.1%	-15.1%

Margin continued to remain in 12% range

Operating EBITDA stood at Rs31.3 crore(12.2 %) vs.30.9 crore(12.7%) in last quarter mainly reflecting the impact of wage hike(80 bps) and also impacted by emigration related expenses that was incurred in US geography(20 to 25 bps).

Concall Highlights:

- ❑ Order book: The Company posted a impressive growth in its order backlog, a barometer to sustain financial growth at 33%. It stand at now 599.2 crore (66.3mn pound) as compared 501crore last quarter
- ❑ Operational metrics: 9 clients were added during the quarter. Total customer for last 12 months now stands at 162. Top 5 client revenue is at 41.5% and top 10 contributes 56.6%.Total employee base 2104 at the end of 2QFY19. Split of employee on onsite/offshore (1317/787).
- ❑ On margin been stagnant, the management stated that to dive higher growth in the business, it is required to continue to invest in the market. Thus investment will continue for next few quarters, so operational efficiency will play to improve the margin.
- ❑ Vertical outlook: The management expect public sector to still be strong and brand recognition in UK is helping to start to pull more project which giving confidence of robust growth in FY19.Credibility on Retail continues to be strong and the management have started to see the new capabilities moving across business to business making them relatively confident of growth coming from this business segment .pipeline is strong and management continues to reinvestment in this business.
- ❑ Outlook for FY19: Management feels that the pipeline of UK and US is all very robust as the kind of investments that they had made for market coverage is now coming.
- ❑ Hedge book: Forex hedges for next twelve month are at 9.1mn pound (average rate of 92.9).

Exhibit: Revenue trend

Strong performance in UK market and continued traction from strategic account led the revenue growth.

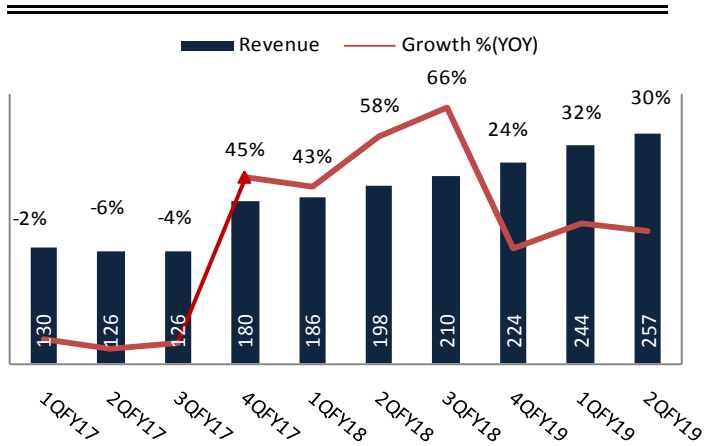


Exhibit: Service line

Application and digital showed a robust growth in 2QFY19.

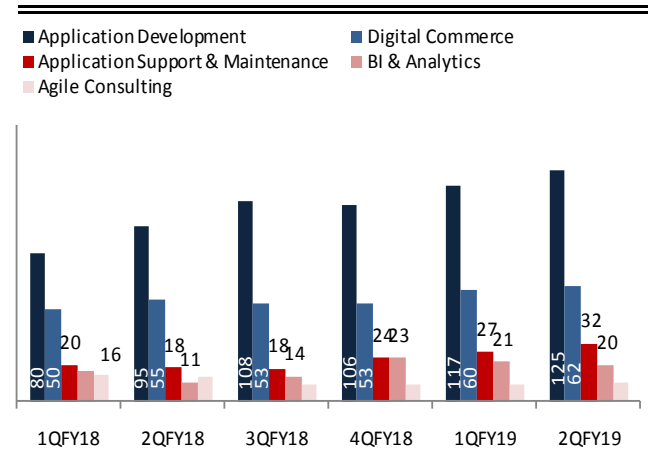


Exhibit: EBITDA and EBITDA margin

Wage revision and emigration impacted margins; Management continued to be in 12% range.

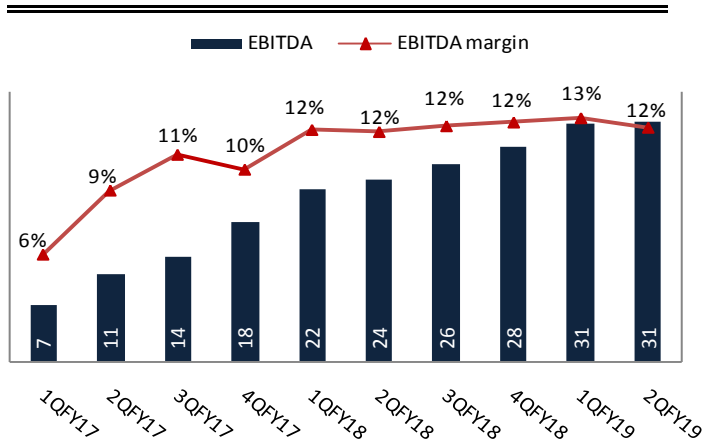


Exhibit: Fixed Price and Time & Material

Continued growth in fixed price contracts.

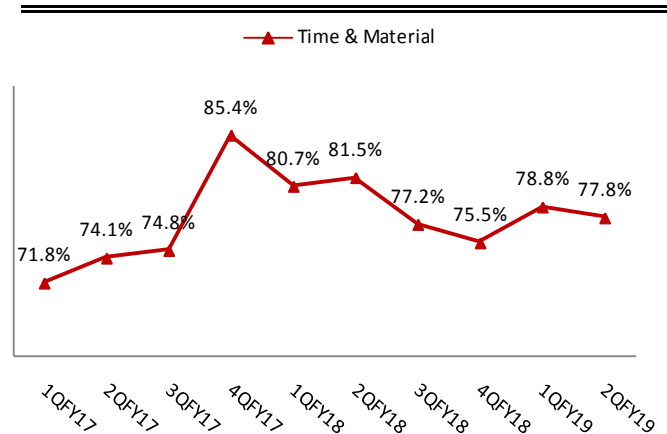


Exhibit: Top Client

Stagnant growth in top client

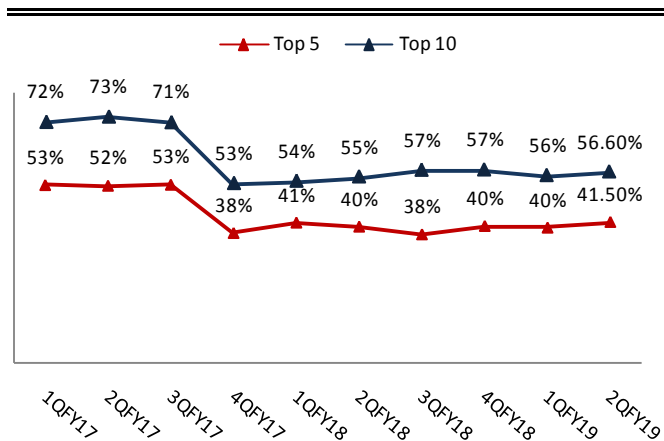
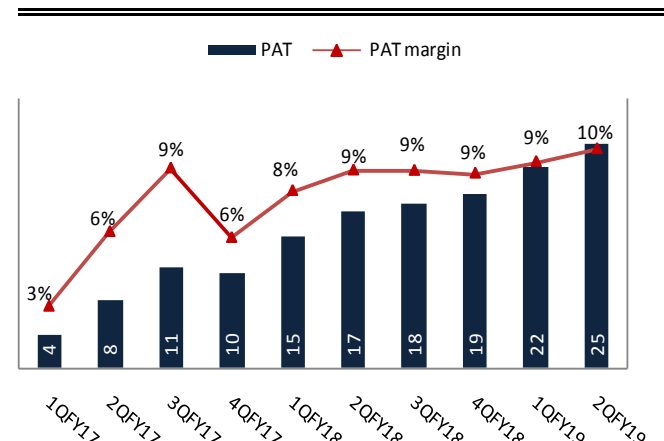


Exhibit: PAT and PAT margin

Other income led to growth in Pat in 2QFY19.



Financial Details

Balance Sheet

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Share Capital	12	11	11	11	12	12	12	12
Reserves	521	549	585	308	432	537	619	718
Networth	533	560	596	319	444	549	631	729
Debt	1	1	20	0	65	50	50	50
Other Non Cur Liab	36	25	27	6	103	52	52	52
Total Capital Employed	570	586	643	325	611	651	732	831
Net Fixed Assets (incl CWIP)	250	261	280	66	75	73	106	133
Non Cur Investments	3	3	2	19	169	166	166	166
Other Non Cur Asst	334	346	357	133	245	245	278	305
Non Curr Assets	337	348	359	151	414	412	444	471
Inventory	0	0	0	0	0	0	0	0
Debtors	149	117	133	97	85	135	172	205
Cash & Bank	122	90	163	89	48	88	115	167
Other Curr Assets	76	94	89	44	14	10	13	16
other financial asset	0	0	0	0	68	77	77	77
Short-term loans and advances	21	24	35	16	0	0	0	0
Curr Assets	405	406	472	277	320	428	496	584
Creditors	5	4	13	9	20	19	24	29
Provisions	32	24	17	6	32	5	6	7
Other Curr Liab	135	140	151	88	3	44	55	66
Other financial liabilities	0	0	0	0	39	27	27	27
Other long-term liabilities	0	0	0	0	4	9	9	9
Curr Liabilities	171	167	180	103	122	185	204	220
Net Curr Assets	234	238	292	174	197	243	292	363
Total Assets	742	754	832	428	734	840	940	1055

Income Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Revenue from Operation	683	923	1,013	527	562	817	1,040	1,242
Change (%)	-6%	35%	10%	-48%	7%	45%	27%	19%
EBITDA	57	90	56	18	53	100	130	159
Change (%)	179%	58%	-38%	-67%	191%	89%	31%	22%
Margin (%)	8%	10%	5%	3%	9%	12%	13%	13%
Depr & Amor.	22	33	37	16	13	19	19	23
EBIT	35	57	18	2	40	81	112	136
Int. & other fin. Cost	0	1	1	1	3	6	9	10
Other Income	9	11	17	17	10	21	25	25
EBT	44	68	34	19	47	96	128	151
Exp Item	-	-	12	3	3	-	-	-
Tax	9	16	17	3	7	26	30	36
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	34	52	5	14	37	70	99	115
Adjusted PAT	34	52	5	14	37	70	99	115
Change (%)		51%	-90%	170%	169%	90%	41%	17%
Margin(%)		6%	1%	3%	7%	9%	9%	9%

Financial Details

Key Ratios

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
ROE	6	9	1	4	7	12	15	16
ROCE	8	12	6	4	10	15	19	19
Asset Turnover	3	4	4	8	8	11	10	9
Current Ratio	2	2	3	3	3	2	2	3
Debtor Days	80	46	48	67	55	60	60	60
Book Value Per Share	216	253	264	139	190	235	270	312
Payable Days	2	2	5	7	13	8	8	8
Earnings Per Share	14	23	2	6	16	30	42	49
P/E	9	9	189	24	11	17	10	9
Price / Book Value	1	1	2	1	1	2	2	1
EV/EBITDA	0	0	1	0	1	1	1	1
EV/Sales	3	4	15	13	8	11	7	6
Dividend payout	22%	19%	111%	42%	22%	20%	14%	12%

Cash Flow Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
PBT	44	68	34	19	47	70	128	151
(inc)/Dec in Working Capital	28	16	-8	7	-10	-45	-20	-18
Non Cash Op Exp	18	28	42	13	10	48	19	23
Int Paid (+)	0	0	0	0	0	0	0	0
Tax Paid	-9	-23	1	-8	-4	-9	-30	-36
others	0	0	0	0	0	0	0	0
CF from Op. Activities	80	89	68	31	43	64	98	120
(inc)/Dec in FA & CWIP	-18	-27	-49	-13	-15	-15	-52	-50
Free Cashflow	62	63	19	19	28	49	46	70
(Pur)/Sale of Inv	-256	-570	-494	0	0	-113	0	0
others	0	0	0	0	0	0	0	0
CF from Inv. Activities	-9	-70	-24	16	-119	-24	-52	-50
inc/(dec) in NW	0	0	0	0	0	0	0	0
inc/(dec) in Debt	0	0	19	-1	67	4	0	0
Int. Paid	0	-1	-1	0	-3	-3	0	0
Div Paid (inc tax)	0	-12	-10	-9	-2	-11	-17	-17
others	-42	-55	14	6	2	3	0	0
CF from Fin. Activities	-43	-67	22	-4	64	-7	-17	-17
Inc(Dec) in Cash	29	-48	66	43	-12	34	27	52
Add: Opening Balance	82	119	67	25	59	54	88	115
Closing Balance	111	71	134	67	48	88	115	167

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