

Industry	IT
Bloomberg	MAST IN
BSE CODE	523704

Continued traction in UK market to drive growth in FY20

RATING	BUY
CMP	429
Price Target	570
Potential Upside	33%

Rating Change	↔
Estimate Change	↔
Target Change	↔

Stock Info

52wk Range H/L	366/644
Mkt Capital (Rs Cr)	1024
Free float (%)	52%
Avg. Vol 1M (,000)	53
No. of Shares (Cr)	2
Promoters Pledged (Cr)	0

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Key Highlights-

- ❑ Mastek 3QFY19 performance reflected a continued growth momentum where the revenue grew 3.1%QoQ in rupee term and 1.4% in CC terms (in line with the estimates) whereas the margin improved 60 bps (above expectation).
- ❑ UK market posted a strong growth of 6.8%QoQ in 3QFY19 driven by government led contracts in UK. However US market declined 6.7%QoQ due to seasonality.
- ❑ Order backlog was softer in 3QFY19 to Rs517.3 crore as compared to 599.2 crore in 2QFY19. However we are confident of continued growth in order backlog in 4QFY19 and FY20 on the back of continued client addition and increase in wallet share with existing customer.
- ❑ Management expects US market to improve in next quarter as they have started to build a recovery plan to bring back the growth by not only dependent on oracle but also re-orientating the business and working on different modes to cushion the impact of seasonality.

3Q FY19 Result Update

Company's 3QFY19 revenue performance was in line with the estimates. Revenue for the quarter stood at Rs265 crore, a growth of 3.1% QoQ led by strong growth in government segment in UK. In constant currency term, revenue grew 1.4%QoQ. Ebitda for the quarter came at Rs34 crore, a growth of 8.6%QoQ and 32.3%YoY. Margin improved 60 bps to 12.8% as compared to 12.2% in last quarter. Margin improved mainly due to operational efficiency. However utilization decline to 76% (normally at 80%) due to seasonality. PAT stood at Rs26.5 crore in 3QFY19 a growth of 5.7%QoQ.

View and Valuation

Going forward, we expect company to post better performance in FY20 led by strong order book, continued growth in the mature market and strong traction from public sector. Order backlog for the quarter stood at Rs517 crore as compared to 599 crore last quarter. Though on QoQ basis order book decline 14% due to seasonality, however we expect it is to improve in 4QFY19 and FY20 led by strong pipeline and no impact of brexit. Mature market for the company (UK) continued to post strong growth in 3QFY19 (6.8%QoQ) led by robust growth in government segment. We expect momentum in UK to continue as pipeline looks very strong. Even the management expects healthy pipeline as they are well poised to continue to be preferable vendors for UK government. However some concern lies in US market which declined below expectation of the company however the management is working on recovery plan by expanding in different modes than entirely depended on oracle. On margin front, we expect better performance going forward led by operational efficiency however US recovery will be gradual thus offsetting some portion of the margin.

We expect Mastek to post revenue growth of 24% CAGR over FY18 - FY20E. We maintain our target price of Rs570 (11 x FY20E EPS) and recommend BUY.

Key Risks to our rating and target

- ❑ Execution issue continued in US business

KEY FINANCIAL/VALUATIONS	FY16	FY17	FY18	FY19E	FY20E
Net Sales	527	562	817	1043	1248
EBITDA	18	53	100	131	159
EBIT	2	40	81	113	140
PAT	14	37	70	102	121
EPS (Rs)	6	16	30	43	52
EPS growth (%)	-24%	164%	90%	45%	19%
ROE (%)	4	7	12	15	16
ROCE (%)	4	10	15	20	22
BV	139	201	235	267	311
P/B (X)	1	1	2	2	1
P/E (x)	24	11	17	10	8

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3QFY19 Results

Revenue in line with estimates

Financials	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	YoY %	QoQ%	FY17	FY18	YoY %
Net Sales	210	224	244	257	265	26.5%	3.1%	562	817	45.3%
Other Income	6	7	3	9	6	3%	-31%	10	21	116%
Employee	126	130	140	150	149	18%	0%	321	481	50%
Other Expenses	57	66	73	76	82	42%	7%	188	237	25.8%
EBITDA	26	28	31	31	34	32%	9%	53	100	88.5%
Dep and	5	4	4	5	4	-13%	-10%	13	19	45.9%
EBIT	21	24	27	27	30	43%	12%	40	81	102.2%
Interest	1	2	1	2	1	0%	0%	3	6	0.0%
PBT	25	30	29	33	34	37%	5%	47	96	103.7%
Tax	7	10	6	8	8	18%	2%	7	26	280.8%
Exceptional	-	-	-	-	-	0%	0%	3	-	0.0%
PAT	18	19	22	25	27	44%	5.7%	37	70	89.6%

Strong growth continued in UK market

Revenue for the quarter stood at Rs265 (growth of 3.1%QoQ) led by strong performance in UK market in government segment. UK continued to be strong and grew 6.8%QoQ and 39.2%YoY. However US which was started 24 months back have shown de growth of 6.4%QoQ due to seasonality and delay in decision making .Also other market declined by 12.5%QoQ. Industry wise, Government and IT led the growth in the industry by growing 1.4% and 43.6% QoQ. However, retail service declined 1.2%QoQ.

Robust growth in UK continued while US declined more than anticipated

VERTICALS(in crore)	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	QoQ%	YoY %
UK	123	136	143	161	174	186	199	6.8%	39.2%
US	57	58	62	60	65	67	62	-6.4%	0.0%
Others	6	4	4	2	5	4	4	-12.5%	-17.4%

Softness seen in retail due to seasonality.

Industry (in crore)	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	QoQ%	YoY %
Government	64	69	70	71	77	99	101	1.4%	43.6%
Other Financial Services	36	34	45	51	54	49	50	1.4%	9.8%
Retail Services	70	77	78	80	90	93	92	-1.2%	18.7%
IT & Other services	16	18	17	21	23	16	23	43.6%	32.5%

Margin beat despite seasonality

Ebitda for the quarter came at Rs34 crore, a growth of 8.6%QoQ and 32.3%YoY .Margin improved 60 bps in 3QFY19 to 12.8% as compared to 12.2% last quarter led by operational efficiency however utilization decline to 76% (normally at 80%) due to seasonality. The management has given new base for utilization in 76% to 80 % (earlier was 84%).

Concall Highlights

- ❑ Operational metrics: Added 14 new logos in 3QFY19. Total active client became 165. Top 5 Client revenue contribution was at 42.6% and Top 10 Client revenue was at 57.1%. Total Employee stood at 2,088 (offshore: 1,287; onsite: 801) in 3QFY19 .
- ❑ Decline in Order backlog: 12Months Backlog was Rs 517.3 crore (£ 58.1 m) on 3QFY19 as compared to Rs 599.2 crore (£ 63.3m) in Q2FY19.The order backlog dipped 14%QoQ driven by seasonality and delay in decision making due to holiday season.
- ❑ Macro front: Market is stable , digital is robust and two particular strategic market of UK and US and the focus on building strategic account is really providing platform of sustained financial performance for last 11 quarters . The management is seeing benefit from brexit as the UK government is aggressively working on program of digitalization and as the company is among the top 10 supplier for the UK government thus it is seeing more revenue resilience in next few quarters as the budget for digital spending is expected to improve by UK government.
- ❑ M&A plan: Management continues to be open for inorganic growth and if got the chance will utilize the majesco stake (18%).
- ❑ Hedge book: Forex hedges for next twelve month are at 8.3mn pound (average rate of 94.3).
- ❑ Outlook: US market declined 6.8%QoQ which was below anticipated due to issue in execution in H1 .However the management expects to improve in next quarter as they have build a recovery plan to bring back the growth in 4QFY19 by not only dependent on oracle but also re -orientating the business and working on different modes to cushion the impact of seasonality.

Exhibit: Revenue trend

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

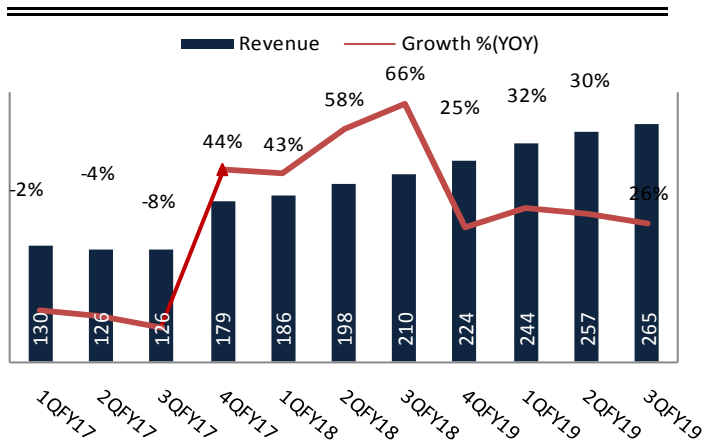


Exhibit: Service line

Application continued to post robust growth in 3QFY19.

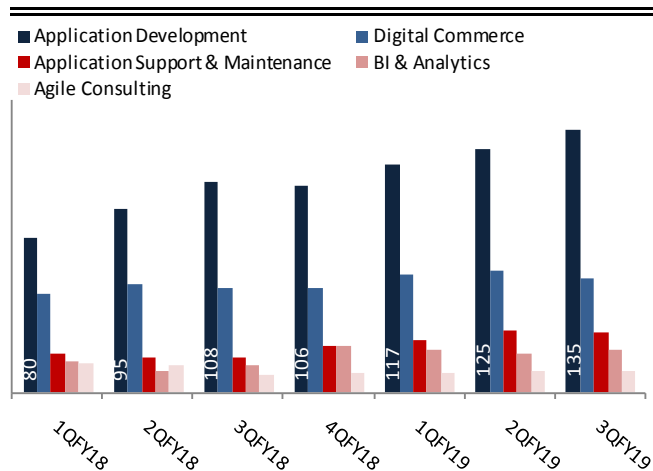


Exhibit: EBITDA and EBITDA margin

Margin expanded by 60bps led by operational efficiency.

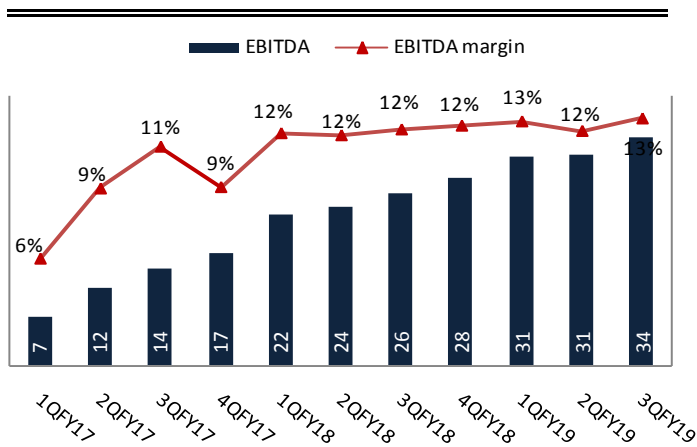


Exhibit: Fixed Price and Time & Material

Continued growth in fixed price contracts.

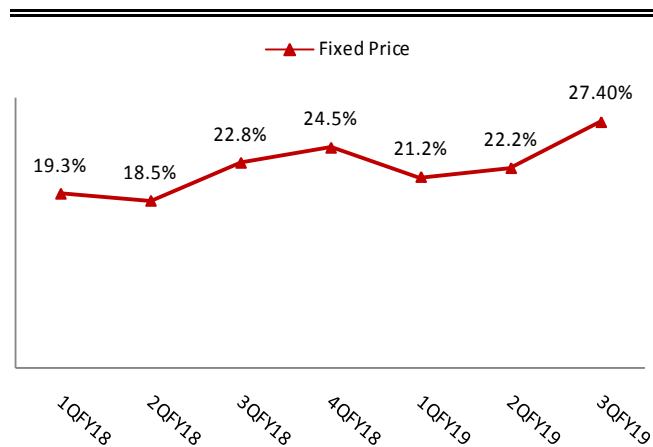


Exhibit: Top Client

Growth seen in top client after been stagnant for last few quarters.

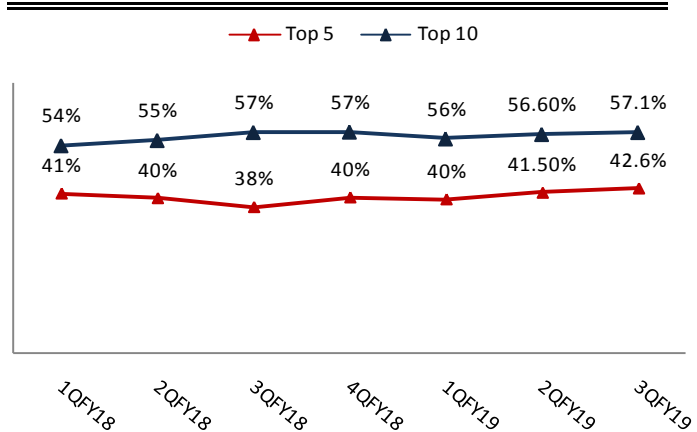
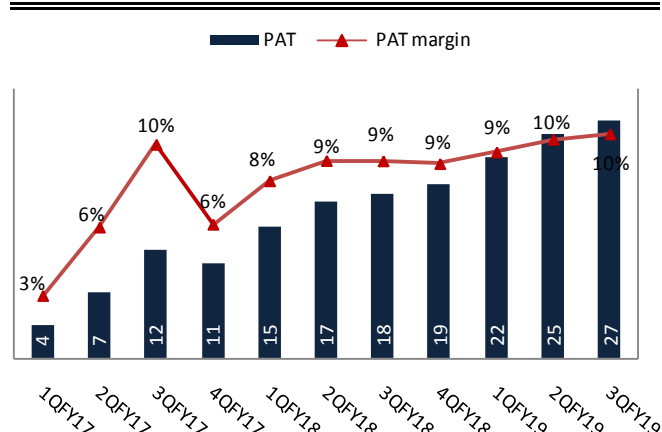


Exhibit: PAT and PAT margin

Other income and margin beat led to growth in Pat in 3QFY19.



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	622	726
Networth	533	560	596	319	444	549	634	738
Debt	1	1	20	0	65	50	0	0
Other Non Cur Liab	36	25	27	6	103	52	52	52
Total Capital Employed	570	586	643	325	611	651	686	790
Net Fixed Assets (incl CWIP)	250	261	280	66	75	73	75	81
Non Cur Investments	3	3	2	19	169	166	166	166
Other Non Cur Asst	334	346	357	133	245	245	247	253
Non Curr Assets	337	348	359	151	414	412	414	420
Inventory	0	0	0	0	0	0	0	0
Debtors	149	117	133	97	85	135	173	206
Cash & Bank	122	90	163	89	48	88	94	173
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	476	591
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	56	67
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	221
Net Curr Assets	234	238	292	174	197	243	272	370
Total Assets	742	754	832	428	734	840	889	1011

Income Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Revenue from Operation	683	923	1013	527	562	817	1043	1248
Change (%)	-6%	35%	10%	-48%	7%	45%	28%	20%
	0	0	0	0	0	0	0	0
EBITDA	57	90	56	18	53	100	131	159
Change (%)	179%	58%	-38%	-67%	191%	89%	32%	21%
Margin (%)	8%	10%	5%	3%	9%	12%	13%	13%
Depr & Amor.	22	33	37	16	13	19	18	19
EBIT	35	57	18	2	40	81	113	140
Int. & other fin. Cost	0	1	1	1	3	6	6	5
Other Income	9	11	17	17	10	21	25	25
EBT	44	68	34	19	47	96	132	159
Exp Item	0	0	12	3	3	0	0	0
Tax	9	16	5	3	7	26	30	38
Minority Int & P/L share of Ass.	0	0	0	0	0	0	0	0
Reported PAT	34	52	18	14	37	70	102	121
Adjusted PAT	34	52	18	14	37	70	102	121
Change (%)	6760%	51%	-66%	-22%	169%	90%	45%	19%
Margin(%)	5%	6%	2%	3%	7%	9%	10%	10%

Financial Details

Key Ratios

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
ROE	6	9	4	4	7	12	15	16
ROCE	8	12	6	4	10	15	20	22
Asset Turnover	3	4	4	8	8	11	14	15
Debtor Days	80	46	48	67	55	60	60	60
BV	216	253	264	139	201	235	267	311
Payable Days	2	2	5	7	13	8	8	8
Earnings Per Share	14	23	8	6	16	30	43	52
P/E	9	9	54	24	11	17	10	8
Price / Book Value	1	1	2	1	1	2	2	1
EV/EBITDA	3	4	15	13	8	11	7	5
EV/Sales	0	0	1	0	1	1	1	1

Cash Flow Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
PBT	44	68	34	19	47	70	132	159
(inc)/Dec in Working Capital	28	16	-8	7	-10	-45	-20	-18
Non Cash Op Exp	18	28	42	13	10	48	18	19
Int Paid (+)	0	0	0	0	0	0	0	0
Tax Paid	-9	-23	1	-8	-4	-9	-30	-38
others	0	0	0	0	0	0	0	0
CF from Op. Activities	80	89	68	31	43	64	100	121
(inc)/Dec in FA & CWIP	-18	-27	-49	-13	-15	-15	-20	-25
Free Cashflow	62	63	19	19	28	49	79	97
(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	-21	-25
inc/(dec) in NW	0	0	0	0	0	0	0	0
inc/(dec) in Debt	0	0	19	-1	67	4	-54	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	-70	-17
Inc(Dec) in Cash	29	-48	66	43	-12	34	6	79
Add: Opening Balance	82	119	67	25	59	54	88	94
Closing Balance	111	71	134	67	48	88	94	173

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