

Industry
Bloomberg
BSE CODE

TECHNOLOGY
MAST IN
523704

Strong margin execution despite challenges

RATING	ACCUMULATE
CMP	420
Price Target	462
Potential Upside	10%

Rating Change	↑
Estimate Change	↑
Target Change	↑

STOCK INFO	
52wk Range H/L	509/295
Mkt Capital (Rs Cr)	1053
Free float (%)	52%
Avg. Vol 1M (,000)	14
No. of Shares (Crs)	2
Promoters Pledged %	0

Fig in Rs Cr

FINANCIAL	FY19	FY20E	FY21E
Net Sales	1,033	983	1,096
EBITDA	132	128	145
EBIT	114	106	121
PAT	100	104	120
EPS (Rs)	43	45	51
EPS growth (%)	43%	4%	15%
ROE (%)	12	14	16
ROCE (%)	18	15	16
BV	302	336	379
P/B (X)	1.5	1.2	1.1
P/E (x)	10.3	9.4	8.2

3QFY20 Result Update

Revenue in line, impressive cost management

- Mastek reported mix set of numbers in 3QFY20 result. Revenue came at Rs 243.6(in line), a flat QoQ growth in rupee terms and 4.1%QoQ decline in cc terms. The decline in revenue was primarily attributable to 1) seasonality across the market; 2) impact by UK general election (resulted in 6 week close down of government machinery); 3) shut downs in the major account of home office; 4) Also the weakness in Retail in US.
- EBITDA for the quarter stood at Rs 34 crore, growth of 17.4%QoQ. Margin expanded 120 bps to 13.8(beating our estimates of 13%), mainly owing to favorable currency ,better cost management and right shoring of cost structure.
- Attrition for the quarter increased to 24.9% as compared to 24.1% last quarter
- Pat for the quarter came at Rs 26crore; a growth of 5.6% primarily led by lower ETR and higher other income.
- The company added 9 new clients in 3QFY20. Total client count after the end of 3FY20 was 143 (LTM) as compared to 143(LTM) in 2QFY20 mainly impacted by macro challenges.

UK showed growth while US declined

Mastek reported a modest growth 1.4%QoQcc in UK market despite the shut down in UK home office (biggest contract) and impact of election. US business continued to struggle due to seasonality and timing of deal closure which resulted in 6%YoY decline in 3Q. The management expects to bring back growth from 4Q.

Elections impacted the order backlog

The company reported a 24.8%QoQ decline in order backlog to Rs471crore vs Rs626crore. The order backlog generally gets soft in 3Q, however this quarter was more pronounced on account of the local factors in UK which result in delay in deal closure.

View and Valuation

Mastek has been the one of the few Indian IT company which has enjoyed low exposure to legacy and have 84% above of digital Business. However FY20 so far have seemed to be tough year for the company with both the market majorly impacted. Uncertainty around Brexit and then further election dragged the UK growth in 3Q while slow down in retail in US added further impact. Going forward we expect the growth in UK business to revive post the Brexit outcome and completion of spending assessment. Also we see US business to recover itself in 4Q with the new deal ramp-up. On margin , we see steady margin improvement supported by favorable currency and recovery of the UK market .However some portion will offset by drag from India business where the client filed bankrupt.

Post result, we have revised our pat estimates by 4.8%/5.85 after the margin beat and rightward growth in UK. Thus we revised our target from Rs437 to 462 and recommend Accumulate.

Key Risks to our rating and target

- Slow down in order booking.
- Prolonged weakness in US business

RESEARCH ANALYST

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3QFY20 Results

Mixed quarter

Fig in Rs Cr

FINANCIALS	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	265	267	248	244	244	-8.0%	0.0%	817	1,033	26.4%
Other Income	6	7	5	9	10	58.6%	4.7%	21	25	18.1%
Employee Exp	149	149	135	135	137	-8.5%	1.1%	481	587	22.1%
Other Expenses	82	83	80	80	73	-10.1%	-8.0%	237	315	32.9%
EBITDA	34	35	33	29	34	-1.1%	17.4%	100	132	32.0%
Deprication	4	4	6	6	6	35.0%	3.4%	19	17	-7.5%
EBIT	30	31	27	23	28	-6.3%	20.8%	81	114	41.1%
Interest	1	1	1	1	1	-40.7%	-7.0%	6	6	4.6%
PBT	34	37	31	31	37	6.4%	16.9%	96	133	38.3%
Tax	8	10	7	7	6	-23.2%	-9.3%	26	32	22.4%
Exceptional Items	-	(1)	-	-	5			-	1	
PAT	27	27	24	25	26	-1.9%	5.6%	70	100	43.5%

Concall Highlights

- **Major impacts:** 3QFY20 was dominated by 1)seasonally soft quarter across the market; 2)UK general election which resulted in 6 week close down of government machinery into December ;3)shut downs in the major account of home office (massive revenue generator for the company)4)Also the weakness in Retail in US From furlough and restructuring impact the revenue .
- **Market performance:** The company reported a modest growth 1.4%QoQcc in UK market despite the shut down in UK home office (biggest contract).It was further exaggerated by the election resulting delay in deal closures.US business continued to struggle due to seasonality and timing of deal closure which resulted in 6%YoY decline in 3Q.The company is confident as internal transformation in US will bring back growth in 4Q and will continue to flow in Fy21.
- **Margin performance:** The Company reported EBITDAAT 13.8%, a growth of 120bps in margins .The cost management as well as operating efficiency initiates as well as right shoring of cost structure, all of these contributed to EBITDA improvement. The company will continue to build on it and use it as the lever to invest in growth of the business going ahead.
- **Provisions:** The Company has created a provision for bad debts of Rs 4 .5crore in current quarter on account of C&K bankruptcy its India client .The Company sees no more provision needed further.
- **Order backlog:** The company reported a 24.8%QoQ decline in order backlog to Rs471crore.The order backlog generally get soft in 3Q , however this quarter was more pronounced on account of the local factors in UK. In all the company acquired 9 new logos and LTM client stood at 143.Going forward, the company sees the order backlog getting positive seeing the January trend.
- **Challenges in India business:** India is struggling in 3Q due to bankruptcy of Cox and king (long time customer) which impact cash and revenues of the company .These impact will continue in near term.
- **Divestment of asset:** the company has successfully divested 60% of legacy shareholding in Majesco through two tranche of sales , thus creating USD24million cash to Mastek .Going forward the company will continue to divest the balance of the remaining 2million shares at the appropriate time .the company will completely exit this investment in near term. Also the company will sell its noncore real estate assets within the next few quarters.
- **Appointment:** To further strengthen the board, the company has appointed Mr Rajiv Grover as an independent director.
- **Headcount:** the company has been reducing the headcount in that few quarters. Now the headcount stands at 1880 vs1937 last quarter .The management now expects to increase the headcount from 4Q.
- **US visibility:** Though the project got over, the company saw a impact in Man and services as it did not materialize in 3Q.However the company had 5 new logo addition during the quarter .Thus expects upward trajectory in US geography going ahead.
- **Outlook:** The company expects favorable exchange rate will yield better returns for Mastek in the future due to significant business mix .The company continues to focus to grow in cc terms in every market .the management sounded more confidence of returning modest growth in 4Q and maintain the trajectory in FY21 seeing improved condition in core market of UK and absences of furlough.

Revenues by Client Geography

FLAT GROWTH IN UK MARKET WHILE US SAW SHARP DECLINE

VERTICALS (GBP MN)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	QoQ%	YoY%
UK	19.2	20.4	21.5	22.3	20.2	20.1	20.1	0.4%	-6.2%
US	7.2	7.3	6.7	6.4	7.1	7.5	6.1	-17.9%	-8.8%
Others	0.5	0.4	0.4	0.4	0.4	0.5	0.3	-50.2%	-33.7%

Revenues by Business Segments

GOVERNMENT LED THE GROWTH, RETAIL REMAINED SOFT

INDUSTRY WISE (GBP MN)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	QoQ%	YoY%
Government	8	11	11	12	11	11	12	4.2%	6.5%
Financial Services	6	5	5	5	5	5	5	-7.0%	-14.1%
Retail Services	10	10	10	10	10	11	9	-15.0%	-10.1%
Others	3	2	2	2	2	1	1	-3.6%	-41.0%

Revenues by Offering

BARRING SUPPORT , ALL OTHER SERVICES REMAINED SOFT

SERVICES (GBP MN)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	QoQ%	YoY%
ADM	13	14	15	12	11	12	12	0.0%	-15.2%
Digital Commerce	7	7	6	6	7	7	6	-19.2%	-6.3%
Application Support	3	3	3	6	5	5	5	10.7%	52.3%
BI & Analytics	2	2	2	3	3	2	2	-20.5%	-18.2%
Agile Consulting	1	1	1	1	1	1	1	-8.0%	-16.5%
Assurance & Testing	1	1	1	1	0	0	0	-5.4%	-68.0%

Revenues by Project type

STEEP DECLINE IN FIXED PRICE CONTRACTS

SERVICES (CRORE)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	QoQ%	YoY%
Fixed Price	6	6	8	8	7	5	5	-5.9%	-36.3%
Time & Material	21	22	21	21	21	23	22	-5.3%	3.8%

Client Metrics

Nos	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	QoQ%	YoY%
Active Clients (TTM)	7	9	14	7	9	11	9	-18.2%	-35.7%
Active Clients (during the qtr)	166	162	165	157	154	144	143	-0.7%	-13.3%
Top 5 Client	0	0	0	0	0	0	0	8.3%	1.6%
Top 10 Client	1	1	1	1	1	1	1	11.2%	11.0%

Exhibit: Revenue trend

YoY growth impacted by slowdown in US geography.

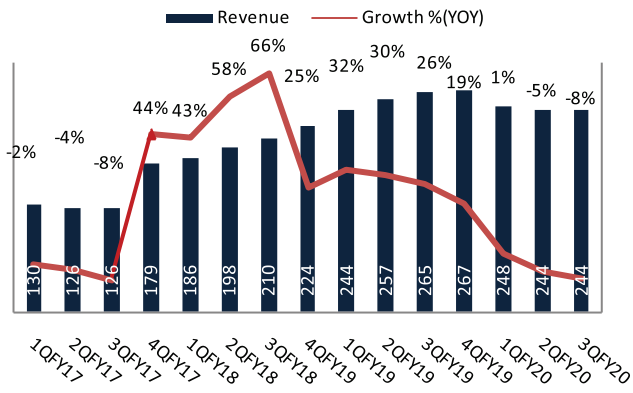


Exhibit: Service line

Most of service line soft due macro challenges.

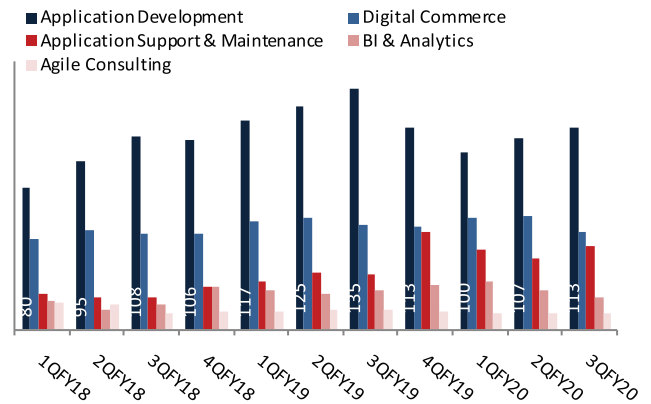


Exhibit: Margin Trend

EBIT margin witnessed recovery led by cost control and currency benefit

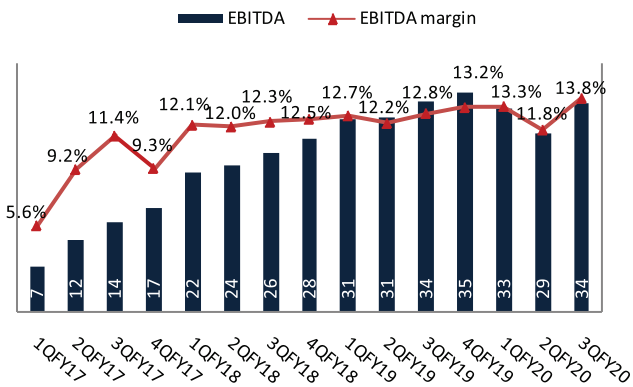


Exhibit: Fixed Price and Time & Material

Decline in fixed price contracts due to weakness in UK market.

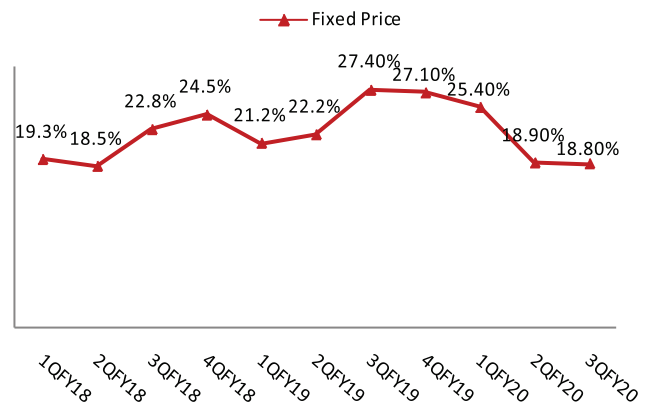
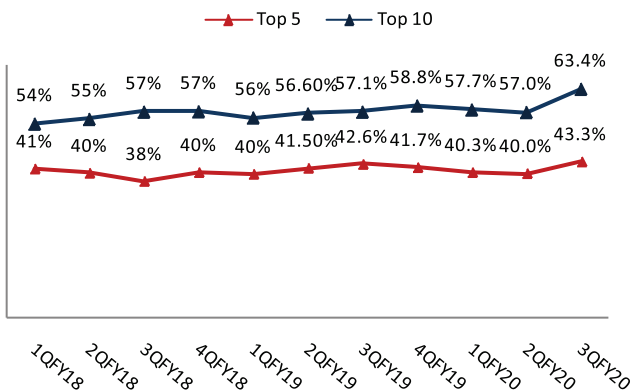


Exhibit: Top Client

Uptick in top client revenue.



Financial Details

Balance Sheet

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	11	11	11	12	12	12	12	12
Reserves	549	585	308	432	537	704	792	895
Networth	560	596	319	444	549	716	804	907
Debt	1	20	0	65	50	69	69	69
Other Non Current Liab	25	27	6	103	52	32	59	59
Total Capital Employed	586	643	325	611	651	818	932	1,035
Net Fixed Assets (incl CWIP)	261	280	66	75	73	71	61	52
Non Current Investments	3	2	19	169	166	282	282	282
Other Non Cur Asst	346	357	133	245	245	220	210	201
Non Current Assets	348	359	151	414	412	503	492	483
Inventory	-	-	-	-	-	-	-	-
Debtors	117	133	97	85	135	208	198	221
Cash & Bank	90	163	89	48	88	93	128	179
Other Curr Assets	94	89	44	14	10	49	47	52
Other financial assets	-	-	-	68	77	19	19	19
Short-term loans and advances	24	35	16	0	0	0	0	0
Current Assets	406	472	277	320	428	484	606	724
Creditors	4	13	9	20	19	9	9	10
Provisions	24	17	6	32	5	12	12	13
Other Curr Liab	140	151	88	3	44	36	34	38
Other financial liabilities	-	-	-	39	27	0	27	27
Other long-term liabilities	-	-	-	4	9	6	6	6
Curr Liabilities	167	180	103	122	185	169	166	172
Net Curr Assets	238	292	174	197	243	315	440	552
Total Assets	754	832	428	734	840	987	1,098	1,207

Income Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	923	1013	527	562	817	1033	983	1096
Change (%)	35%	10%	-48%	7%	45%	26%	-5%	11%
EBITDA	90	56	18	53	100	132	128	145
Change (%)	58%	-38%	-67%	191%	88%	32%	-3%	13%
Margin (%)	10%	5%	3%	9%	12%	13%	13%	13%
Depr & Amor.	33	37	16	13	19	17	22	24
EBIT	57	18	2	40	81	114	106	121
Int. & other fin. Cost	1	1	1	3	6	6	3	3
Other Income	11	17	17	10	21	25	29	36
EBT	68	34	19	47	96	133	131	154
Exp Item	-	12	3	3	-	1	-	-
Tax	16	5	3	7	26	32	27	34
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	52	18	14	37	70	100	104	120
Adjusted PAT	52	18	14	37	70	100	104	120
Change (%)	51%	-66%	-22%	169%	90%	43%	4%	15%
Margin(%)	6%	2%	3%	7%	9%	10%	11%	11%

Financial Details

Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	9	4	4	7	11	12	14	16
ROCE	12	6	4	10	15	18	15	16
Asset Turnover	4	4	8	8	11	14	16	21
Current Ratio	2	3	3	3	2	3	4	4
Debtor Days	46	48	67	55	60	74	74	74
Book Value Per Share	253	264	139	201	235	302	336	379
Payable Days	2	5	7	13	8	3	3	3
Earnings Per Share	23	8	6	16	30	43	45	51
P/E	9	54	24	11	17	10	9	8
Price / Book Value	1	2	1	1	2	1	1	1
EV/EBITDA	4	15	13	8	11	8	7	6
EV/Sales	0	1	0	1	1	1	1	1

Cash Flow Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	68	34	19	47	70	101	131	154
(inc)/Dec in Working Capital	16	(8)	7	(10)	(45)	(51)	34	(18)
Non Cash Op Exp	28	42	13	10	48	55	22	24
Int Paid (+)	-	-	-	-	-	-	-	-
Tax Paid	(23)	1	(8)	(4)	(9)	(31)	(27)	(34)
others	-	-	-	-	-	-	-	-
CF from Op. Activities	89	68	31	43	64	76	161	126
(inc)/Dec in FA & CWIP	(27)	(49)	(13)	(15)	(15)	(16)	(12)	(15)
Free Cashflow	63	19	19	28	49	60	149	111
(Pur)/Sale of Inv	(570)	(494)	-	-	(113)	(153)	(99)	(40)
others	-	-	-	-	-	-	-	-
CF from Inv. Activities	(70)	(24)	16	(119)	(24)	(53)	(111)	(54)
inc/(dec) in NW	-	-	-	-	-	-	-	-
inc/(dec) in Debt	-	19	(1)	67	4	1	-	-
Int. Paid	(1)	(1)	(0)	(3)	(3)	(2)	-	-
Div Paid (inc tax)	(12)	(10)	(9)	(2)	(11)	(18)	(17)	(17)
others	(55)	14	6	2	3	3	-	-
CF from Fin. Activities	(67)	22	(4)	64	(7)	(16)	(17)	(17)
Inc(Dec) in Cash	(48)	66	43	(12)	34	6	35	51
Add: Opening Balance	119	67	25	59	54	87	93	128
Closing Balance	71	134	67	48	88	93	128	179

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