

Industry
Bloomberg
BSE CODE

TECHNOLOGY
MPHL IN
526299

Direct core growth remain intact

RATING	BUY
CMP	936
Price Target	1079
Potential Upside	15%
Rating Change	↔
Estimate Change	↓
Target Change	↔

STOCK INFO	
52wk Range H/L	828/1060
Mkt Capital (Rs Cr)	17459
Free float (%)	40%
Avg. Vol 1M (,000)	6
No. of Shares (Crs)	19
Promoters Pledged %	0

Fig in Rs Cr

FINANCIAL	FY19	FY20E	FY21E
Net Sales	7,731	8,826	9,733
EBITDA	1,324	1,642	1,778
EBIT	1,248	1,414	1,528
PAT	1,073	1,133	1,253
EPS (Rs)	58	61	67
EPS growth (%)	33%	6%	11%
ROE (%)	20.4%	19.6%	19.5%
ROCE (%)	23.8%	24.5%	23.8%
BV	282	310	345
P/B (X)	4	3	3
P/E (x)	17	15	14

3QFY20 Result Update

- Mphasis reported mix set of numbers in 3QFY20 result. Revenue for the quarter came at USD317.8million, growth of 4%QoQ in cc terms(in line with our estimates)driven by Direct core which grew 4.5%QoQ .
- Ebit for the quarter stood at 369 crore, a growth of 6.4%QoQ. Margin improved 10 bps to 16.2% vs. 16.1% last quarter. The improvement in margin was supported by better mix, higher fixed price which was partially offset by wage increase.
- PAT during the quarter stood at Rs 294crore, a growth of 7.4%QoQ; primarily led by growth revenue growth

Momentum continued in Direct Core while DXC/HP growth moderated

- The 4% growth in revenue came on the back of growth in Direct International channel which grew 5.1% QoQ and 16.9% YoY in cc terms during the quarter. The growth in direct international came in due to healthy growth seen in direct core business which grew 4.5%QoQ. Growth in Direct Core was driven by a combination of strategic accounts, new logos (80% YoY growth) and Blackstone portfolio (grew at 50% YoY).
- Even digital risk posted a strong growth of 11%QoQ in cc terms which is highest in last 6 quarters.
- However DXC/HP channel which has growing strongly for the company in last few years, decelerated further in 3Q (grew 0.1%QoQ CC).

Impressive deal wins, maintain 15.5% to 17% margin guidance

- The company won TCV of USD189 mn net new in direct international in 3Q.Total YTD deal wins now constitutes of USD514million; more than 80% of deal wins are in new gen focus areas .
- Despite Company will see some acceleration in sales and marketing spends in next two quarters, it is confident of operating in the guided range of 15.5% to 17% for FY20.

View and Valuation

Mphasis has been among the few mid-tier IT companies which has been reporting steady growth QoQ despite macro issues. Revenue growth in 3Q was supported by strong traction from direct core(grew4.5%QoQ in 3Q) while DXC/HP business continued to decelerate. Momentum continued in net new TCV which stood at USD189million for the quarter (87% coming in New Gen Services). Going ahead, we expect strong traction in new deal wins, sustainable recovery in Digital Risk and acceleration in new logo/Blackstone portfolio (grew80%/50%YoY in 3Q) will drive growth for foreseeable future However increased uncertainty with new leadership change and divestments of business will moderate the Mphasis DXC growth(26.6% of rev) in coming quarters .

Post result, we have largely unchanged our FY20 estimates and reduced our FY21 Pat estimates marginally by 0.3%. Thus we largely maintain our BUY stance on the stock with target price of Rs 1079 .

Key Risks to our rating and target

- Delay in new client addition in Blackstone portfolio.
- Failure to grow Direct International channel faster than industry growth.

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3QFY20 Results

Mixed performance

Fig in Rs Cr

FINANCIALS	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	YoY%	QoQ%	FY18	FY19	YoY%
Net Sales	1,971	2,025	2,063	2,158	2,277	15.5%	5.5%	6546	7731	18.1%
Other Income	51	33	54	35	36	-28.6%	3.2%	162	177	9.0%
Employee Exp	1,089	1,112	1,154	1,188	1,259	15.7%	5.9%	3,818	4,299	12.6%
Other Expenses	552	572	534	564	591	7.1%	4.7%	1,666	2,108	26.6%
EBITDA	331	340	374	405	427	29.1%	5.4%	1062	1324	24.6%
Depreciation	20	20	55	58	58	193.7%	-1.1%	71	76	7.1%
EBIT	311	320	319	347	369	18.7%	6.4%	992	1,248	25.9%
Interest	3	6	20	22	19	450.4%	-12.2%	13	17	33.6%
PBT	358	348	354	360	387	7.9%	7.2%	1,141	1,407	23.4%
Tax	80	82	89	87	93	16.0%	6.8%	290	334	15.1%
PAT	278	266	265	273	294	5.6%	7.4%	837	1,073	28.2%

Concall highlights

- 3QFY20 Performance:** Direct international grew 6.9%QoQ and 17.9%YoY in reported basis. Direct core now constitutes 83% of direct international business grew 6.3%sequentially and 15.6%YoY aided by consistent deal wins. Growth in direct core has been broad based around strategic accounts, Blackstone portfolio and new client segment. Black stone and new client segment continue to post strong growth momentum YOY , growing 50% and 80% respectively .Digital Risk continue to witness strong growth and reported a sequential growth of above 13% in cc terms
- Black stone portfolio:** Blackstone now constitutes about 7% of Direct Core revenue which is up from low to mid-single digits last year. It is growing at 50%YoY.The company expects to grow it to 10% in coming quarters as pipeline is very strong .2 of black stone clients have now become part of top 20 clients list of Mphasis .
- Strong deal wins:** The company won TCv of USD189mn net new in direct international in 3Q.Total YTD deal now constitutes of USD514million ;more than 80% of deal wins are in new gen focus areas . The deal wins have again been broad-based across strategic accounts, new clients and Blackstone portfolio. The company is able to pull through some longer-term revenue along with the transformation deals that gives the ability to see some longer term visibility going ahead.
- DXC relationship:** With the recent change of guard at DXC (new leadership), strategy is now moving towards an enterprise technology stack. Through this DXC is harnessing significant opportunity not only in their core foundational business of IPO but identifying significant opportunities with customers in applying transformation across the stack. Thus resulting in opportunities for Mphasis .The management seeing minimum overlap and is confident of industry level growth for foreseeable future
- Verticals**
 - BCM segment:** Despite the challenging environment and seasonal softness , the company continued to witness strong growth momentum and positive outlook in its focus verticals of banking and capital market. The segment has reported a strong revenue growth of 16%YoY for the quarter ; broad based across BCM as well as direct core and digital business.
 - Insurance** segment also reported strong sequential growth aided by strong deal wins announced in last few quarter .While the industry narrative will be bearish for the segment, Majority of sub segment of company's BCM is less focus to cyclical trend as they are B2C focus and digital disruption prone.
 - Emerging vertical** is growing above 18%over the past 8 quarters .Logistic and transportation which is sub segment and comprises 50% of this segment has grown above 33%YoY .
- Geography:** Europe region which has been focus area for the company has shown 18.6%sequential revenue growth in this quarter .This is highest reported growth for region in last 5 years .The sales affect and investment have started to yield good results for the company and is expected to continue to grow in coming quarters .
- Operating margin performance:** Operating margin improved 10 bps sequentially and 30 bps YoY to 16.2% despite a typically seasonally challenging quarter for the sector. During the quarter, The Company was able to pull some operating levers including fixed-price projects as well as automation initiatives and using IP platform which supported the margins. The management is confident of operating in the guided range of 15.5% to 17% for FY 20.
- Demand environment:** Despite having some uncertainty especially around interest rates, elections, global macro, and of course on the new uncertainty with global growth concerns around the outbreak with the China, the management sees demand fairly stable .There is no further acceleration in the spend number, but there is definitely further acceleration in the shift of the spend from legacy to the transformation initiative.

Revenue Mix

DIRECT CORE CONTINUED TO DRIVE GROWTH

SEGMENTAL (IN USD MN)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	QoQ%	YoY%
Direct International	186	187	190	199	203	211	223	5.5%	16.8%
DXC / HP Business	74	78	82	83	84	84	84	0.5%	2.8%
Others	9	10	10	10	10	10	11	12.3%	7.4%

Revenue by verticals

STRONG GROWTH CONTINUED IN BCM SEGMENT AND EMERGING VERTICAL

VERTICAL(USD MN)	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	QoQ%	YoY%
Banking &Capital Mkt	126	127	125	129	133	140	145	3.6%	16.0%
Market Insurance	30	31	33	35	35	34	36	4.9%	7.2%
IT, Comm	46	47	47	50	49	49	50	1.8%	5.2%
Emerging Industries	66	71	77	77	80	82	88	7.1%	13.4%

Exhibit: Direct Core

Continued uptick in revenue growth led by strong growth in strategic account and client addition in Blackstone portfolio.

■ Direct Channel revenue (in Usd mn)

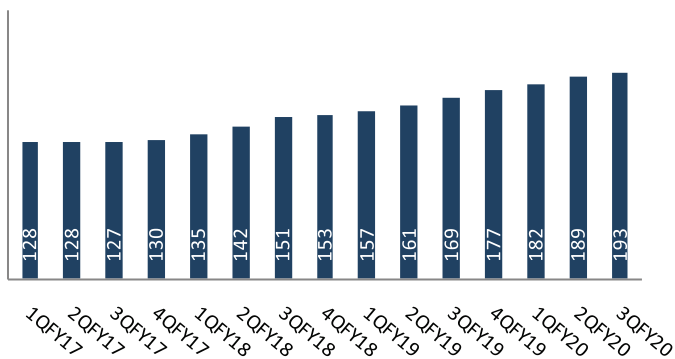


Exhibit: HP/DCX Revenue

DCX issue may impact HP /DCX business.

■ Revenues from HP channel - USDm ▲ QoQ growth

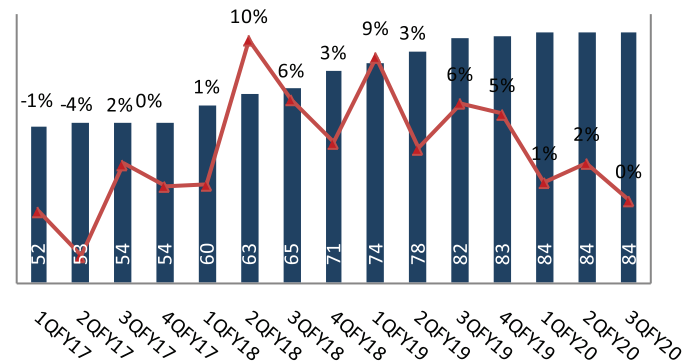


Exhibit: Deal wins

Continued growth in net new wins.

■ TCV

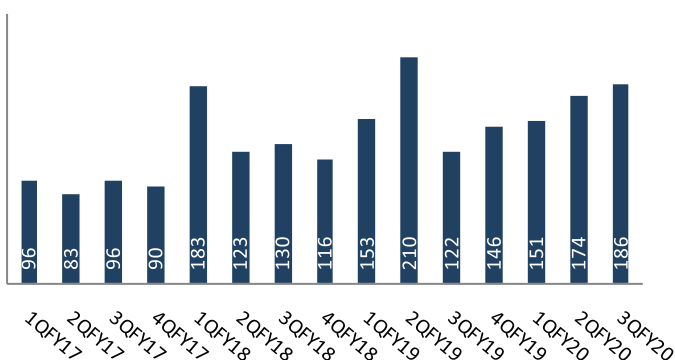


Exhibit: EBIT margin

Despite wage hike, EBIT margin managed to be within guided range of 15.5 % to 17%.

■ EBIT ▲ EBIT MARGIN

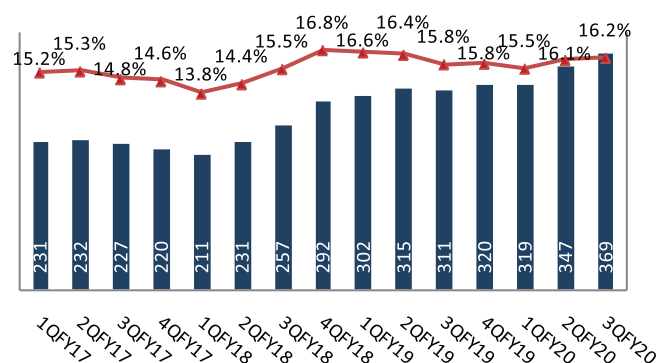
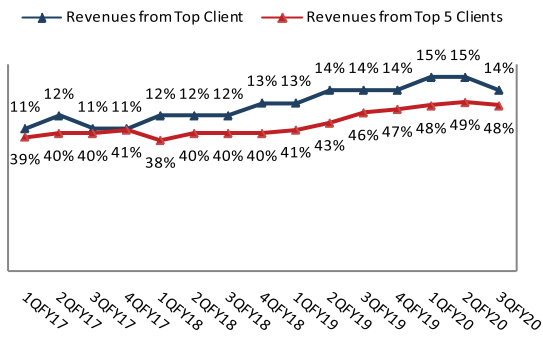


Exhibit: Top Client contribution

Seasonality impacted top client .



Operational Details

BY GEOGRAPHY	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
AMERICAS	79%	80%	80%	78%	78%	78%	80%	78%
EMEA	11%	11%	11%	11%	11%	11%	10%	12%
INDIA	6%	6%	6%	6%	5%	5%	5%	5%
ROW	4%	3%	3%	5%	6%	6%	5%	5%

BY PROJECT TYPE (%)	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Time and Material	74%	73%	75%	76%	77%	76%	74%	73%
Fixed Price	26%	27%	25%	24%	23%	24%	26%	27%

SERVICE TYPE	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Application Maintenance	31%	30%	34%	36%	34%	33%	30%	29%
Application Development	26%	28%	28%	30%	31%	33%	33%	32%
Customer Service	1%	1%	1%	1%	1%	1%	1%	1%
Service / Technical	8%	8%	6%	7%	8%	7%	9%	9%
Transaction Processing	7%	7%	7%	6%	6%	6%	7%	8%
IMS	15%	15%	14%	13%	7%	8%	7%	8%
Knowledge Processes	12%	11%	10%	7%	13%	12%	13%	13%
License Income	0%	0%	0%	0%	0%	0%	0%	0%

CLIENT	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Top Client	13%	13%	14%	14%	14%	15%	15%	14%
Top 5 Clients	40%	41%	43%	46%	47%	48%	49%	48%
Top 10 Clients	56%	56%	58%	59%	60%	61%	60%	60%

HEADCOUNT	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Onsite								
Application Services	2456	2550	2991	3539	3277	3246	3309	3298
ITO Services / IS	1120	1087	1312	1210	1293	1522	1547	1399
BPO Services	950	914	914	884	851	951	1080	1398
Offshore								
Application Services	8281	8680	8962	9286	9742	10312	10995	10980
ITO Services	3121	3075	2994	2843	2723	2789	2867	2927
BPO Services	5139	5092	5140	5236	5384	5474	5958	6078

TOTAL CLIENT ADDITIONS	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
Direct Channel	4	7	5	18	19	12	7	13
HP / DXC Channel	1	5	7	2	4	7	8	2
Total client additions	5	12	12	20	23	19	15	15

Financial Details

Balance Sheet

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	210	210	210	210	193	186	186	186
Reserves	4,905	5,270	6,083	5,942	5,289	5,064	5,593	6,243
Networth	5,115	5,480	6,293	6,152	5,482	5,250	5,780	6,429
Debt	431	434	311	260	390	543	543	543
Other Non Current Liab	60	111	153	76	102	128	128	128
Total Capital Employed	5,606	6,025	6,758	6,489	5,973	5,920	6,450	7,099
Net Fixed Assets (incl CWIP)	224	176	173	224	185	214	78	62
Non Current Investments	541	250	375	126	317	259	259	259
Other Non Cur Asst	25	105	104	198	151	96	96	96
Non Current Assets	3,721	3,469	3,733	2,868	3,039	3,268	3,132	3,116
Current investment	1,275	1,193	1,736	2,270	1,465	1,070	1,430	1,698
Inventories	-	-	4	-	-	-	-	-
Trade receivables	778	625	649	628	812	955	1,091	1,203
Other current assets	545	558	682	270	280	351	401	442
Other financial assets	-	-	-	597	600	66	66	66
Short term loans and advances	214	251	251	71	82	126	143	158
Cash & Bank balance	458	1,321	855	614	707	642	754	992
Current assest	3,269	3,948	4,177	4,449	3,946	4,103	4,905	5,684
Trade payables	451	406	453	388	502	785	896	988
Other curr liab & provisions	932	985	699	137	169	187	212	233
employee defined benefit liabilities	-	-	-	78	73	64	64	64
Other financial liabilities	-	-	-	160	180	279	279	279
Income tax liabilities (Net)	-	-	-	65	87	137	137	137
Curr Liabilities	1,384	1,392	1,152	828	1,012	1,451	1,588	1,701
Net Curr Assets	1,886	2,556	3,025	3,621	2,934	2,652	3,318	3,983
Total Assets	6,990	7,417	7,909	7,317	6,985	7,371	8,037	8,800

Income Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	5,728	5,795	6,088	6,076	6,546	7,731	8,826	9,733
Change (%)	-1%	1%	5%	0%	8%	18%	14%	10%
EBITDA	992	870	896	969	1,062	1,324	1,642	1,778
Change (%)	-4%	-12%	3%	8%	10%	25%	24%	8%
Margin (%)	17%	15%	15%	16%	16%	17%	19%	18%
Depr & Amor.	122	98	74	79	71	76	228	250
EBIT	870	772	822	890	992	1,248	1,414	1,528
Int. & other fin. Cost	37	28	24	14	13	17	80	76
Other Income	117	197	196	239	162	177	163	207
EBT	950	941	994	1,114	1,141	1,407	1,497	1,659
Exp Item	6	3	55	15	13	-	-	-
Tax	258	263	270	308	290	334	364	406
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	686	675	669	792	837	1,073	1,133	1,253
Adjusted PAT	686	675	669	792	837	1,073	1,133	1,253
Change (%)	-8%	-2%	-1%	18%	6%	28%	6%	11%
Margin(%)	12%	12%	11%	13%	13%	14%	13%	13%

Financial Details

Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	13%	12%	11%	13%	15%	20%	20%	19%
ROCE	16%	13%	13%	14%	18%	24%	24%	24%
Asset Turnover	25	29	35	31	32	39	60	138
Current Ratio	2	3	3.6	5.4	3.9	2.8	3.1	3.3
Debtor Days	50	39	39	38	45	45	45	45
Book Value Per Share	243	261	299	292	284	282	310	345
Payable Days	29	26	27	23	28	37	37	37
Earnings Per Share	33	32	32	38	43	58	61	67
EPS growth%	-8%	-2%	-1%	18%	15%	33%	6%	11%
P/E	12	12	15	15	19	17	15	14
Price / Book Value	2	1	2	2	3	4	3	3
EV/EBITDA	9	8	11	12	15	14	11	10
EV/Sales	1	1	2	2	2	2	2	2

Cash Flow Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	428	941	945	1114	1141	1407	1497	1659
(inc)/Dec in Working Capital	-121	-20	52	-105	-150	-142	-193	-160
Non Cash Op Exp	21	-22	-21	-54	21	27	228	250
Int Paid (+)	0	0	0	0	0	0	0	0
Tax Paid	-130	-279	-234	-290	-278	-343	-364	-406
others	0	-3	-11	-1	0	0	0	0
CF from Op. Activities	198	616	731	664	733	950	1168	1343
(inc)/Dec in FA & CWIP	-36	-72	-127	-118	-33	-85	-92	-234
Free Cashflow	162	544	603	546	700	865	1076	1109
(Pur)/Sale of Inv	115	460	-562	-126	737	572	-360	-268
others	141	-755	531	512	-211	-29	0	0
CF from Inv. Activities	220	-366	-158	268	493	289	-453	-503
inc/(dec) in NW	0	0	0	0	0	10	0	0
inc/(dec) in Debt	0	8	-146	-197	128	125	0	0
Int. Paid	-11	-22	-18	-7	-10	-16	0	0
Div Paid (inc tax)	-418	-172	-404	-505	-395	-465	-603	-603
others	0	0	0	0	-1103	-995	0	0
CF from Fin. Activities	-429	-186	-568	-710	-1380	-1342	-603	-603
Inc(Dec) in Cash	-11	64	5	222	-154	-103	113	238
Add: Opening Balance	364	340	388	391	618	455	352	464
Closing Balance	353	403	393	613	464	352	465	702

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Analyst's ownership of the stocks mentioned in the Report	NIL
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Registration Details of Group entities: G. Raj & Company Consultants Ltd (G RAJ)-BSE Broker INZ260010731; NSDL DP: IN-DP-NSDL-371-2014 || Narnolia Commerce Limited (Formerly Microsec Commerce Ltd.)-MCX/NCDEX Commodities Broker: INZ000051636 || NarnoliaVeloX Advisory Ltd.- SEBI Registered PMS: INP000005109 || Eastwind Capital Advisors Pvt Ltd. (EASTWIND)-SEBI Registered Investment Adviser: INA300005439 || Narnolia Insurance Brokers Limited (Formerly Microsec Insurance Brokers Ltd.)-IRDA Licensed Direct Insurance Broker (Life & Non-Life) Certificate No. 134, License No. DB046/02 || Narnolia Securities Ltd. (NSL)-AMFI Registered Mutual Fund distributor: ARN 20558, PFRDA NPS POP: 27092018 || Narnolia Capital Advisors Pvt. Ltd. - RBI Registered NBFC: B.05.02568.

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