



In partnership. With trust.

# Mindtree

Sector: Technology

## 3QFY18 Result Update

CMP: ` 623

*Sustainable revenue growth; margin recovery*

Recommendation: Buy

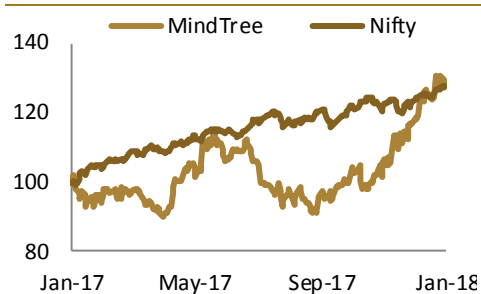
### Market statistics

Current stock price (`)	623
Shares O/S (cr.)	16.4
Mcap (` cr)	10,220
52W H/L (`)	644/435
6m avg. volume	616,298
Bloomberg	MTCL IN

### Shareholding pattern

Promoters	13.64
Domestic Institution	8.46
Foreign Institution	40.56
Non-institution	37.34
of which more than 1%	
Coffee Day	17.11
Nalanda India Fund Ltd	9.64

### Mindtree vs Nifty



### Capital efficiency & valuations

Particulars	FY18E	FY19E	FY20E
RoE (%)	19.7	20.4	21.2
EPS (`)	31.3	35.1	41.6
CEPS (`)	42.0	46.2	53.5
P/E (x)	19.9	17.7	15.0
P/BV (x)	3.9	3.4	3.0
EV/EBITDA (x)	12.9	10.1	8.5
Income growth (%)	3.8	13.4	11.2
EBITDA growth (%)	2.3	23.8	15.1
PAT growth (%)	22.5	12.2	18.4

**Mindtree's Q3FY18 performance was higher-than expected on both the margin and revenue front. Revenue increased 3.9% QoQ to US\$214.3mn (up 4% in cc terms). Margin was up 348bps to 15.5% primarily on account of tight SG&A costs, better operational efficiencies. TCV won in Q3 was US\$244mn (US\$207mn in 2QFY18, US\$314mn in 3QFY17) with digital comprising US\$132mn – which again was strong. Mindtree's comments regarding future business opportunities indicated a sustainable pick-up in revenue trajectory and margin recovery. We upgrade our recommendation on the stock to Buy on account of large deal ramp-ups and continued momentum in deal wins and pipeline courtesy improving positioning in digital. We believe that business challenges have bottomed out.**

**Higher-than-expected margins:** Mindtree's Q3FY18 revenue was up 3.9% QoQ in USD terms to US\$214.3mn. Volume decreased 1.9% QoQ (offshore decreased 1.2%, onsite decreased by 21%). Blended pricing increased 5.7% QoQ. The growth was primarily due to strong performance across verticals. Digital business grew 7.1% QoQ. Mindtree's comments regarding future business opportunities indicated a sustainable pick-up in revenue trajectory and margin recovery.

**Order signing healthy, provides lower revenue visibility:** Clients #2-5 increased 11.3% QoQ, while Top client (was up 7.1% QoQ). **Strong TCV signings:** Mindtree's total contract value signed during the quarter was at US\$244mn (US\$314mn in 3QFY17, US\$207mn in Q2FY18). Out of this, new deal wins accounted for US\$57mn, and contracts worth US\$206mn to be executed within a year. Travel and Hospitality grew by 9.3%; Retail, CPG and Manufacturing grew by 5.8%, Digital grew by 7.1%; BFSI grew by 3.7% and Independent Testing grew 8.4% QoQ. US (grew 7.3% QoQ) and RoW (+3.9%). EU declined by 4.8%. 290 employees (net) joined MTCL to take the employee base to 17,200 (a gross addition of 857). Utilization (excluding trainees) was down 30bps QoQ at 74.3%. Utilization (including trainees) was down 40bps QoQ at 72.8%.

**Digital—positioning and improving sales cycle:** Mindtree has made significant investments in digital over the past couple of years and developed domain expertise in Salesforce, SAP/S4 HANA, Adobe, Sitecore and Azure. These efforts are reflecting in increased deal flow. Digital deal wins TCV at US\$324mn was up ~25% yoy in 9MFY18. Factors working for Mindtree are (1) good work in pilot digital projects for marquee clients, and (2) more decisive clients; Mindtree is witnessing shorter decision cycles and increase in size of digital deals (median size up to US\$3-5 mn from sub-US\$1 mn earlier). Additionally, Mindtree is benefiting from the experience of its new digital business head, Sreedhar B (ex TCS).

**FY19 Outlook:** We expect a revival in both, revenue trajectory and margin expansion on account of (1) An improvement in client IT spends, healthy deal pipeline and increasing win-rates (pipeline ~20% higher and ~30% win-rate), (2) Multiplicity of service offerings and supplementing revenue growth with digital (highest share amongst peers at 44% of revenue, with an increasing deal size), (3) Stability in acquisitions, and (4) No pricing pressure from large clients expected in the coming future.. MTCL has maintained its high single-digit revenue growth for FY18.

**Valuation & Outlook:** Mindtree's margin recovery commenced in 2Q with 50bps expansion in EBITDA margin led by tightening of execution. Continued tightening of execution, improvement in revenue growth trajectory and reduction in loss of acquired entities offer significant headroom for margin expansion. We estimate EBITDA margin of 13.1%/14.3% in FY2018/19E. We upgrade our recommendation on the stock to Buy on account of large deal ramp-ups and continued momentum in deal wins and pipeline courtesy improving positioning in digital. We believe that business challenges have bottomed out.

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**Exhibit 1: Quarterly details (IND-AS)**

` mn	3QFY17	2QFY18	3QFY18	QoQ (%)	YoY (%)	Comments
<b>Revenues (in US\$ mn)</b>	<b>192.2</b>	<b>206.2</b>	<b>214.3</b>	<b>3.9</b>	<b>11.5</b>	Volumes decreased 1.9%, pricing increased 5.7%.
Revenues	12,953	13,316	13,777	3.5	6.4	
- Operating costs	11,213	11,775	11,703	(0.6)	4.4	
<b>EBITDA</b>	<b>1,740</b>	<b>1,541</b>	<b>2,074</b>	<b>34.6</b>	<b>19.2</b>	
<b>EBITDA margin (%)</b>	<b>13.4</b>	<b>11.6</b>	<b>15.1</b>	<b>348bps</b>	<b>162bps</b>	<b>Up on account of tight SG&amp;A control and efficiencies</b>
- Interest expense	46	25	46	84.0	-	
- Depreciation	459	454	419	(7.7)	(8.7)	
+ Other income, net (incl forex)	144	598	59	(90.1)	(59.0)	
<b>PBT</b>	<b>1,379</b>	<b>1,660</b>	<b>1,668</b>	<b>0.5</b>	<b>21.0</b>	
- Taxes	348	413	253	(38.7)	(27.3)	
Effective tax rate (%)	25.2	24.9	15.2	(971)bps	(1,007)bps	Effective tax rate for FY19 to be between 24-25%
<b>PAT</b>	<b>1,031</b>	<b>1,247</b>	<b>1,415</b>	<b>13.5</b>	<b>37.2</b>	
Net margin (%)	8.0	9.4	10.3	91	231	

Source: Company

**Exhibit 2: Change in estimates**

` mn	FY18E			FY19E		
	Old	New	% Chg	Old	New	% Chg
Revenue (US\$ mn)	838	842	0.5	939	948	1.0
Revenue	54,283	54,346	0.1	61,064	61,606	0.9
EBITDA margin (%)	11.7	13.1	135bps	12.2	14.3	185bps
EPS (`)	30.6	31.3	2.3	34.1	35.1	2.9

Source: Trust Research

**Geography wise Revenues:** US (grew 7.3% QoQ) and RoW (+3.9%). EU declined by 4.8%.

**Exhibit 3: Geographical wise Performance**

Geographical mix	Q3FY16	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
US	63.5	65.9	66.7	67.6	68.7	69.8	69.6	67.5	69.7
Europe	26.4	24.5	23.1	21.4	20.8	20.8	21.1	22.8	20.9
India	2.7	2.8	3.1	3.5	3.1	2.8	3.0	3.5	3.2
RoW	7.4	6.8	7.1	7.5	7.4	6.6	6.3	6.2	6.2
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

Source: Company

**Vertical Performance:** Travel and Hospitality grew by 9.3%; Retail, CPG and Manufacturing grew by 5.8%, Digital grew by 7.1%; BFSI grew by 3.7% and Independent Testing grew 8.4% QoQ

**Exhibit 4: Service offering segmentation**

Service offerings	Q3FY16	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
Development	23.7	23.0	22.7	22.0	22.3	21.4	22.6	23.1	24.5
Engineering	8.3	9.8	9.8	9.8	9.5	9.5	9.6	9.2	9.1
Maintenance	19.8	18.0	17.3	17.8	17.6	18.3	19.0	17.7	16.6
Consulting & IP Licensing	2.6	4.0	4.1	3.8	3.9	4.0	3.4	4.0	4
Package Implementation	12.9	13.6	13.9	13.1	12.4	12.6	11.5	11.2	11.3
Independent Testing	12.8	12.6	12.8	12.4	12.6	12.5	11.8	12.1	12.6
IMS	18.1	17.5	18.4	19.9	20.3	20.4	21.0	21.8	21.1
IP Licensing	1.8	1.3	1.0	1.2	1.4	1.3	1.1	1.0	0.8
<b>Total revenue</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

Source: Company



**Human Resources:** 290 employees (net) joined MTCL to take the employee base to 17,200 (a gross addition of 857). Utilization (excluding trainees) was down 30bps QoQ at 74.3%. Utilization (including trainees) was down 40bps QoQ at 72.8%.

**Exhibit 5: Employee strength at MTCL**

Vertical Mix	Q3FY16	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
Software Professionals	15,296	15,623	15,092	15,189	15,068	15,413	15,441	15,782	16,068
Sales and Support	947	1,000	1,018	1,030	1,031	1,057	1,120	1,128	1,132
<b>Total employees</b>	<b>16,243</b>	<b>16,623</b>	<b>16,110</b>	<b>16,219</b>	<b>16,099</b>	<b>16,470</b>	<b>16,561</b>	<b>16,910</b>	<b>17,200</b>
Gross Addition	1,306	1,020	210	744	470	914	645	856	857
Net Addition	661	380	(513)	109	(120)	371	91	349	290
Attrition (LTM, %)	16.0	15.7	16.5	16.4	16.1	15.1	14.0	13.0	12.6

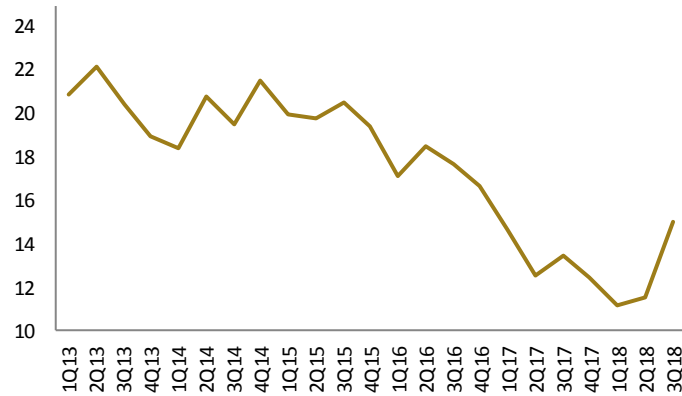
Source: Company, Trust Research

**Exhibit 6: Client details**

Employees	Q3FY16	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18
Top client	10.9	11.7	13.1	14.4	14.1	14.3	15.3	16.1	16.6
Top 5 clients	32.1	29.7	29.6	30.0	30.1	30.7	30.1	30.1	31.6
Top 10 clients	46.2	42.7	42.6	42.5	42.3	41.9	41.5	41.9	43.7
Number Of Active Clients	294	348	343	337	348	328	336	327	344
New Client Additions	23	37	17	18	21	20	20	24	28
\$1 Mn Clients	93	101	98	107	106	111	113	114	114
\$5 Mn Clients	29	31	31	30	30	30	33	38	37
\$10 Mn Clients	13	15	16	16	17	16	16	16	15
\$25 Mn Clients	5	6	5	6	4	4	3	3	3
\$50 Mn Clients	2	2	2	2	1	1	1	1	1
\$100 Mn Clients	0	0	0	0	1	1	1	1	1

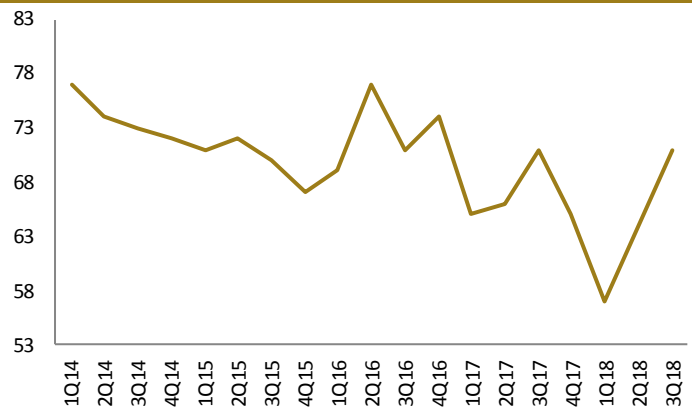
Source: Company

**Exhibit 7: Margin was better than we had expected**



Source: Company, Trust

**Exhibit 8: DSO increased by 7 days QoQ to 71**



Source: Company, Trust



## Financials

### Income Statement (` mn)

Year End-March	FY16	FY17	FY18E	FY19E	FY20E
<b>Revenues</b>	<b>46,730</b>	<b>52,364</b>	<b>54,346</b>	<b>61,606</b>	<b>68,520</b>
Op. Expenses	38,520	45,183	47,234	52,800	58,383
<b>EBITDA</b>	<b>8,210</b>	<b>7,181</b>	<b>7,112</b>	<b>8,806</b>	<b>10,137</b>
Other Income	839	417	1,386	800	1,000
Depreciation	1,658	1,858	1,761	1,816	1,956
<b>EBIT</b>	<b>7,391</b>	<b>5,740</b>	<b>6,737</b>	<b>7,790</b>	<b>9,181</b>
Interest	160	191	152	114	91
<b>PBT</b>	<b>7,231</b>	<b>5,549</b>	<b>6,585</b>	<b>7,676</b>	<b>9,090</b>
Tax	1,706	1,363	1,456	1,919	2,272
<b>PAT</b>	<b>5,525</b>	<b>4,186</b>	<b>5,129</b>	<b>5,757</b>	<b>6,817</b>
Ex. ordinary	-	-	-	-	-
<b>Adj Pat</b>	<b>6,033</b>	<b>4,186</b>	<b>5,129</b>	<b>5,757</b>	<b>6,817</b>

### Key Parameters

Year End-March	FY16	FY17	FY18E	FY19E	FY20E
<b>Per share (`)</b>					
EPS	32.9	24.9	31.3	35.1	41.6
CEPS	42.8	36.0	42.0	46.2	53.5
BVPS	143.9	153.4	160.7	183.0	209.0
DPS	10.5	8.0	10.0	11.0	14.0
Payout (%)	37.3	37.6	37.4	36.7	37.5
<b>Valuation (x)</b>					
P/E	19.9	18.2	19.9	17.7	15.0
P/BV	4.6	3.0	3.9	3.4	3.0
EV/EBITDA	12.3	9.0	12.9	10.1	8.5
Dividend Yield (%)	1.6	1.8	1.6	1.8	2.2
<b>Return ratio (%)</b>					
EBITDA Margin	17.6	13.7	13.1	14.3	14.8
PAT Margin	11.8	8.0	9.4	9.3	9.9
ROAE	24.7	16.8	19.7	20.4	21.2
ROACE	32.4	22.2	24.1	25.4	26.5
<b>Leverage Ratios (x)</b>					
Long Term D/E	0.0	0.0	0.0	0.0	0.0
Net Debt/Equity	(0.2)	(0.3)	(0.4)	(0.4)	(0.4)
Debt/EBITDA	0.1	0.0	0.0	0.0	0.0
Interest Coverage	-	-	-	-	-
Current ratio	2.4	2.6	3.0	3.1	3.2
<b>Growth Ratios (%)</b>					
Income growth	31.2	12.1	3.8	13.4	11.2
EBITDA growth	15.8	(12.5)	2.3	23.8	15.1
PAT growth	3.0	(24.2)	22.5	12.2	18.4
<b>Turnover Ratios</b>					
F.A Turnover x	6.6	8.8	10.4	11.4	12.5
Debtors Days	65	65	63	61	61
Payable days	5	4	4	4	4

### Balance Sheet (` mn)

Year End-March	FY16	FY17	FY18E	FY19E	FY20E
Equity Share Capital	1,678	1,680	1,639	1,639	1,644
Reserves & Surplus	22,471	24,091	26,358	29,374	32,577
<b>Total Shareholders Fund</b>	<b>24,149</b>	<b>25,771</b>	<b>27,997</b>	<b>31,013</b>	<b>34,221</b>
<b>Non- current liabilities</b>	<b>450</b>	<b>(310)</b>	<b>(303)</b>	<b>(294)</b>	<b>(285)</b>
Long term borrowings	765	243	243	243	243
Deferred tax liabilities	(406)	(624)	(624)	(624)	(624)
Other LT liabilities & prov	91	71	78	87	96
<b>Current Liabilities</b>	<b>7,764</b>	<b>7,821</b>	<b>7,916</b>	<b>8,689</b>	<b>9,465</b>
Short term borrowings	415	978	928	878	828
Trade payables	1,890	1,651	1,682	1,881	2,079
Other cur liabilities & Prov	5,459	5,192	5,306	5,931	6,558
<b>Total Liabilities</b>	<b>32,363</b>	<b>33,282</b>	<b>35,610</b>	<b>39,409</b>	<b>43,401</b>
<b>Assets</b>					
<b>Non- current Assets</b>	<b>14,089</b>	<b>12,672</b>	<b>12,000</b>	<b>12,483</b>	<b>12,811</b>
Fixed assets	7,037	5,942	5,239	5,423	5,467
Non-current investments	4,877	4,528	4,528	4,528	4,528
Long-term loans & adv	844	876	893	1,013	1,126
Other non-current assets	1,331	1,326	1,340	1,519	1,690
<b>Current assets</b>	<b>18,274</b>	<b>20,610</b>	<b>23,610</b>	<b>26,926</b>	<b>30,591</b>
Current investments	2,266	5,869	6,869	7,869	8,869
Trade receivables	9,728	8,962	9,231	10,465	11,639
Cash & Bank balances	2,332	2,508	4,234	4,879	5,953
Short term loans & adv.	2,799	2,237	2,233	2,532	2,816
Other current assets	1,149	1,034	1,042	1,181	1,314
<b>Total Assets</b>	<b>32,363</b>	<b>33,282</b>	<b>35,610</b>	<b>39,409</b>	<b>43,401</b>

### Cash flow Statement

Year End-March	FY16	FY17	FY18E	FY19E	FY20E
PBT	7,231	5,549	6,585	7,676	9,090
Depreciation	1,701	1,640	1,761	1,816	1,956
Interest Exp	160	191	152	114	91
<b>CF before W.cap</b>	<b>9,092</b>	<b>7,380</b>	<b>8,498</b>	<b>9,606</b>	<b>11,137</b>
Inc/dec in W.cap	3,732	(890)	154	1,137	1,040
<b>Op CF after W.cap</b>	<b>5,360</b>	<b>8,270</b>	<b>8,344</b>	<b>8,470</b>	<b>10,097</b>
Less Taxes	1,706	1,363	1,456	1,919	2,272
<b>Net CF From Operations</b>	<b>3,654</b>	<b>6,907</b>	<b>6,888</b>	<b>6,551</b>	<b>7,824</b>
Inc/(dec) in F.A + CWIP	3,708	763	1,058	2,000	2,000
(Pur)/sale of Investments	870	3,254	1,000	1,000	1,000
Others	(160)	(191)	(152)	(114)	(91)
<b>CF from Invst Activities</b>	<b>(4,738)</b>	<b>(4,208)</b>	<b>(2,210)</b>	<b>(3,114)</b>	<b>(3,091)</b>
Loan Raised	1,157	41	(50)	(50)	(50)
Equity Raised	557	(992)	(984)	(628)	(1,055)
Dividend	2,061	1,572	1,919	2,113	2,554
<b>CF from Fin Activities</b>	<b>(347)</b>	<b>(2,523)</b>	<b>(2,953)</b>	<b>(2,791)</b>	<b>(3,660)</b>
<b>Net inc /(dec) in cash</b>	<b>(1,431)</b>	<b>176</b>	<b>1,726</b>	<b>645</b>	<b>1,074</b>
Op. bal of cash	3,763	2,332	2,508	4,234	4,879
<b>Cl. balance of cash</b>	<b>2,332</b>	<b>2,508</b>	<b>4,234</b>	<b>4,879</b>	<b>5,953</b>



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