

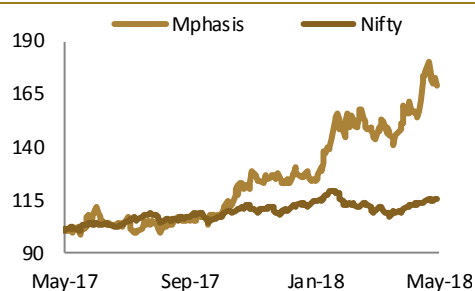
### Market statistics

Current stock price (₹)	985
Shares O/S (cr.)	19.3
Mcap (₹ cr)	19,037
52W H/L (₹)	1122/560
6m avg. volume	309,700
Bloomberg	MPHL.IN

### Shareholding pattern

Promoters	60.40
Domestic Institution	9.08
Foreign Institution	21.80
Non-institution	8.71
of which more than 1%	
Aberdeen Global Indian Equity Fund	4.63
LIC Market Plus 1 Growth Fund	2.17

### Mphasis vs Nifty



### Capital efficiency & valuations

Particulars	FY18	FY19E	FY20E
RoE (%)	14.6	16.6	17.1
EPS (₹)	44.0	49.0	54.5
CEPS (₹)	47.7	53.0	58.7
P/E (x)	19.2	20.1	18.1
P/BV (x)	3.0	3.2	3.0
EV/EBITDA (x)	16.3	16.9	14.7
Income growth (%)	7.7	10.7	11.0
EBITDA growth (%)	9.7	11.2	12.3
PAT growth (%)	4.2	13.2	11.3

**Mphasis at its analyst meet showcased its strength in each of its client bucket – Strategic, HP/DXC and Blackstone Portfolio, focus on geographies – Americas and Europe and bring deep domain expertise in verticals other than BFSI, where it is strong. It even showed various digital initiatives taken by the company to bring down the costs for its clients/partners. 4Q revenues increased 4.4% QoQ in cc terms –due to an increase in HP/DXC (up 8.3% QoQ). HP's enterprise services business is likely to uptick from here onwards. Margin was at 17.7% helped by revenue trajectory as well as one-time benefit from India Government Business. We maintain our SELL rating on the stock on account of underinvestment in business, increasing concentration of revenues and medium term risks to profitability.**

**Good quarter.** Mphasis reported US\$ revenues of US\$264.1mn (up 5.1% QoQ) on account of 8.3% cc QoQ growth in the HP channel; (2) 0.7% or ₹119mn contribution from one-off revenues from India government. EBIT margin of 16.8% increased 130bps and led by 67 bps gain from one-off India government business and 50 bps decline in SG&A spending as a percentage of revenues. Management indicated that HP channel revenues should see strength and would grow faster than the industry. Business mix of Direct vs HP moved to 73:27 QoQ from 74:26 in this quarter. The Direct Core segment should also see positive traction on account of US\$551mn of new deals wins (up 51% YoY) in FY18. EBIT margin of 15-17%, up from the earlier guidance band of 14-16%. This revision is based on – (1) optimization of S&M spending, (2) increasing component of FPP and (3) pyramid optimization.

**Operating metrics getting weaker, though cash supports downside:** Consolidated headcount decreased by 31 to 22,239 (net addition in 2Q18, 3Q18 of last 7 quarters). Mphasis added 5 clients this quarter (4 from the Direct channel). Net Cash & equivalents stand at ₹129/share (13.1% of the MCap is in form of cash). DSO's decreased 4 QoQ to 68 days this quarter. Utilisation and SG&A efficiencies are unlikely to provide much margin leverage going forward. Growth in the direct channel business going forward would be a positive.

**Other details from the Analyst Meet:** Mphasis focused on certain key points to drive growth going forward: 1) Strong Management: Infused new talent across levels, senior leaders in focus markets, 2) domain expertise in all verticals, 3) Focus on clients: Strategic customers, HP/DXC Technology, Blackstone Portfolio and New client acquisition, 4) Geography focus – Americas, Europe, 5) Strong TCV wins, 6) Margin expansion: Pyramid optimization, Increased pricing power and Business Model Shift

**HP channel revenue to become stable from here on, acquisition being used to prop up declining revenue:** HP channel (27% share) revenue should see traction from here onwards, after more than four years of decline. HP continued to lose contracts in services business which had impacted Mphasis. The company has started considering tuck-in acquisitions; after successful integration of Digital Risk.

**Valuation:** MPHL does not compare well versus some of the other mid-cap IT companies. Valuations, though being cheap compared to some of the performing mid-caps, the revenue growth story is weak, while risks to its margins are higher. We maintain our Sell recommendation on the stock. We have low comfort on sustainability of growth in Direct International business given Mphasis' underinvestment in digital and lack of differentiation. We maintain our SELL rating on the stock.

ANALYST

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**Exhibit 1: Quarterly details**

` mn	4QFY17	3QFY18	4QFY18	QoQ (%)	YoY (%)	Comments
<b>Revenues (In US\$m)</b>	<b>221.5</b>	<b>251.4</b>	<b>264.1</b>	<b>5.1</b>	<b>19.2</b>	Direct International increased by 2.1% QoQ. Won deals worth US\$115mn. HP business increased 8.3%.
<b>Revenues</b>	<b>15,059</b>	<b>16,607</b>	<b>17,445</b>	<b>5.0</b>	<b>15.8</b>	
- Operating costs	12,675	13,865	14,350	3.5	13.2	
<b>EBITDA</b>	<b>2,384</b>	<b>2,742</b>	<b>3,095</b>	<b>12.9</b>	<b>29.8</b>	Margins increased on better revenue trajectory and one-time India Government business
<b>EBITDA margin (%)</b>	<b>15.8</b>	<b>16.5</b>	<b>17.7</b>	<b>123bps</b>	<b>191bps</b>	
- Interest expense	17	29	43	48.3	152.9	
- Depreciation	184	176	171	(2.8)	(7.1)	Includes a forex gain of `12mn for the quarter vs `42mn in 3Q.
+ Other income, net (incl forex)	485	354	422	19.2	(13.0)	
<b>PBT</b>	<b>2,668</b>	<b>2,891</b>	<b>3,303</b>	<b>14.3</b>	<b>23.8</b>	
- Taxes	734	741	796	7.4	8.4	Tax rate to remain in the range of 27-28%
Effective tax rate (%)	27.5	25.6	24.1	(153)bps	(341)bps	
<b>PAT</b>	<b>1,934</b>	<b>2,150</b>	<b>2,507</b>	<b>16.6</b>	<b>29.6</b>	
Net margin (%)	12.8	12.9	14.4	142bps	153bps	
<b>Reported profits</b>	<b>1,841</b>	<b>2,150</b>	<b>2,376</b>	<b>10.5</b>	<b>29.1</b>	

Source: Company.

**Exhibit 2: Change in estimates**

` mn	FY18E			FY19E		
	Old	New	%Chg	Old	New	%Chg
Revenue (US\$ mn)	1,058	1,114	5.3	1,205	1,237	2.7
Revenue	71,100	72,433	1.9	78,348	80,418	2.6
EBITDA margin (%)	15.6	16.3	65bps	15.9	16.5	55bps
EPS (`)	45.8	49.0	7.0	50.8	54.5	7.3

Source: Trust Research

**Geography wise Revenues:** Business in Europe was up 17.2% QoQ while US increased 2.8%. RoW increased 3.6% QoQ.**Exhibit 3: Geographical wise Performance**

Geographical mix	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18
US	76.8	77.1	77.6	78.0	79.1	79.5	80.1	80.2	79.1
Europe	10.7	10.7	10.5	9.6	9.5	9.8	9.5	9.8	11.0
RoW	12.4	12.2	11.9	12.4	11.4	10.7	10.4	10.0	9.9
<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

**Exhibit 4: Operating mix (%)**

Details	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18
Application maintenance	34.1	35.8	35.4	37.0	36.9	35.6	34.6	33.1	31.2
Application development	24.5	23.2	23.9	23.1	24.5	24.7	24.0	26.3	26.2
Customer service	2.0	1.9	1.8	1.9	1.8	1.5	1.7	1.4	1.3
Service/ technical help desk	2.3	2.1	2.4	2.3	2.2	5.4	7.2	7.6	7.4
Transaction processing service	7.1	7.0	7.0	6.2	6.5	7.0	6.8	7.0	6.9
Infrastructure management services	13.6	13.6	13.6	14.2	13.8	13.8	13.4	13.2	15.2
Knowledge processes	16.4	16.4	15.9	15.4	14.3	12.1	12.3	11.4	11.8
<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



**Human Resources:** Consolidated headcount decreased by 31 to 22,239 (net addition in 2Q18, 3Q18 of last 7 quarters).

Details	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18
Applications (onsite)	2,322	2,340	2,357	2,299	2,353	2,373	2,363	2,392	2,456
BPO (onsite)	1,359	1,236	1,189	1,127	1,040	1,044	998	981	950
ITO (onsite)	212	215	281	251	274	277	676	1,106	1,120
Applications (offshore)	8,441	8,495	8,468	8,615	8,807	8,668	8,486	8,228	8,281
BPO (offshore)	5,511	5,682	5,561	5,351	5,176	5,191	5,360	5,304	5,139
ITO (offshore)	3,209	3,158	3,196	3,136	3,074	3,055	3,011	3,062	3,121
S&M	300	289	300	315	325	346	330	300	278
G&A	948	943	939	940	945	943	932	897	894
<b>Total</b>	<b>22,302</b>	<b>22,358</b>	<b>22,291</b>	<b>22,034</b>	<b>21,994</b>	<b>21,897</b>	<b>22,156</b>	<b>22,270</b>	<b>22,239</b>

Source: Company

**Client Concentration:** Mphasis added 5 clients this quarter (4 from the Direct channel). MPHL added 2 clients in Emerging Industries and added 1 client in Banking and Capital Market & 2 in Insurance.

#### Exhibit 5: Client details

Details	Q4FY16	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18
Top client (%)	11.0	11.0	12.0	11.0	11.0	12.0	12.0	12.0	13.0
Top 5 clients (%)	38.0	39.0	40.0	40.0	40.0	40.0	40.0	39.0	40.0
Top 10 clients (%)	51.0	53.0	54.0	55.0	55.0	55.0	54.0	55.0	56.0
Top 20 clients (%)	61.0	63.0	65.0	65.0	66.0	65.0	66.0	66.0	69.0
US\$1mn+	103	102	98	92	90	90	90	88	90
US\$5mn+	35	28	28	30	36	39	37	38	37
US\$10mn+	14	15	14	14	14	15	15	17	17
US\$20mn+	8	9	14	8	7	7	7	8	8
Client added	11	3	6	6	5	12	5	6	5

Source: Company

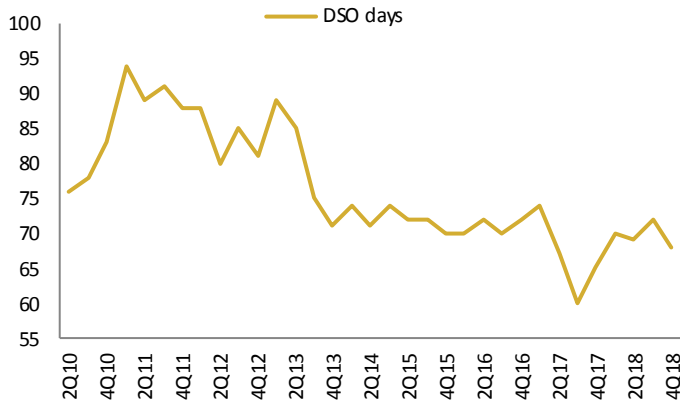
#### Exhibit 6: Billing rates (US\$/hr)

Details	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18
Applications (onsite)	76	77	78	78	80	83	84	85
ITO (onsite)	68	68	71	73	74	77	86	88
Applications (offshore)	21	22	21	22	21	21	22	22
BPO (offshore)	10	10	11	11	11	11	11	11
ITO (offshore)	19	19	18	18	19	19	20	22

Source: Company

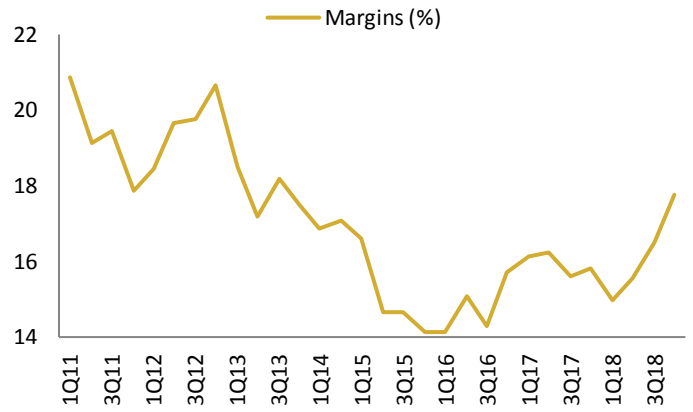


Exhibit 7: DSO days was down 4 days QoQ to 68



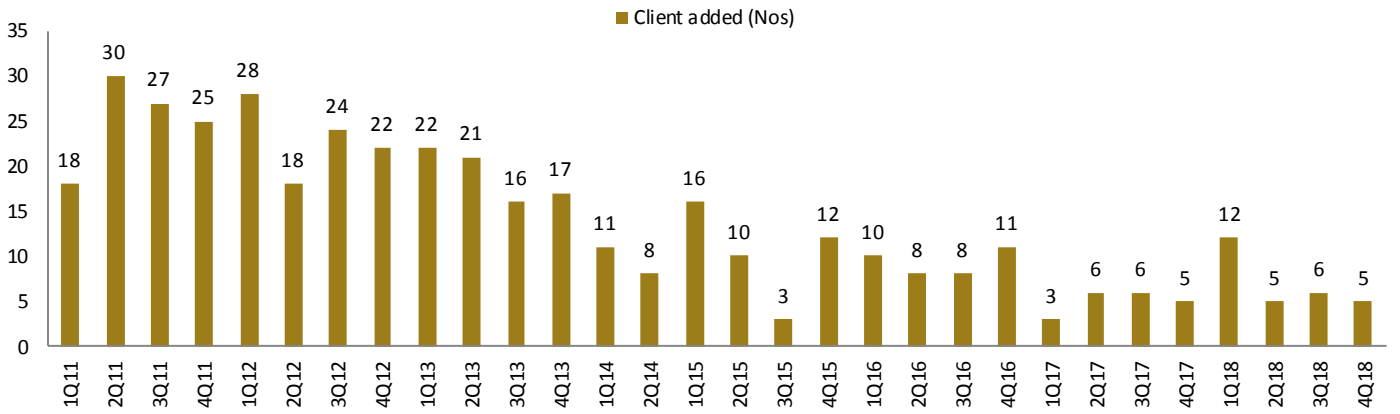
Source: Company, Trust

Exhibit 8: Margin up QoQ on better operational efficiencies



Source: Company, Trust

Exhibit 9: Client addition at MPHL has been weak over the past 7-8 quarters compared to the past



Source: Company, Trust



## Financials

### Income Statement (` mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E
<b>Revenues</b>	<b>60,879</b>	<b>60,763</b>	<b>65,459</b>	<b>72,433</b>	<b>80,418</b>
Op. Expenses	51,909	51,075	54,834	60,615	67,143
<b>EBITDA</b>	<b>8,970</b>	<b>9,688</b>	<b>10,625</b>	<b>11,818</b>	<b>13,275</b>
Other Income	1,954	2,385	1,620	1,938	2,138
Depreciation	744	592	709	771	820
<b>EBIT</b>	<b>10,180</b>	<b>11,481</b>	<b>11,536</b>	<b>12,985</b>	<b>14,593</b>
Interest	242	139	130	172	138
<b>PBT</b>	<b>9,938</b>	<b>11,342</b>	<b>11,406</b>	<b>12,813</b>	<b>14,455</b>
Tax	2,696	3,155	2,900	3,331	3,903
<b>PAT</b>	<b>7,242</b>	<b>8,187</b>	<b>8,506</b>	<b>9,482</b>	<b>10,552</b>
Ex. ordinary	495	152	131	-	-
<b>Adj Pat</b>	<b>6,747</b>	<b>8,035</b>	<b>8,375</b>	<b>9,482</b>	<b>10,552</b>

### Key Parameters

Year End-March	FY16	FY17	FY18	FY19E	FY20E
<b>Per share (`)</b>					
EPS	34.4	38.9	44.0	49.0	54.5
CEPS	38.0	41.7	47.7	53.0	58.7
BVPS	299.3	292.4	283.6	306.8	331.9
DPS	20.0	17.0	20.0	22.0	25.0
Payout (%)	67.9	51.1	53.2	52.5	53.7
<b>Valuation (x)</b>					
P/E	13.7	14.9	19.2	20.1	18.1
P/BV	1.6	2.0	3.0	3.2	3.0
EV/EBITDA	10.5	12.1	16.3	16.9	14.7
Dividend Yield (%)	4.0	2.9	2.4	2.2	2.5
<b>Return ratio (%)</b>					
EBITDA Margin	14.7	15.9	16.2	16.3	16.5
PAT Margin	11.9	13.5	13.0	13.1	13.1
ROAE	12.3	13.2	14.6	16.6	17.1
ROACE	15.9	17.5	18.8	21.3	22.2
<b>Leverage Ratios (x)</b>					
Long Term D/E	0.0	0.0	0.0	0.0	0.0
Net Debt/Equity	(0.4)	(0.5)	(0.4)	(0.4)	(0.4)
Current ratio	3.3	3.7	2.8	2.9	3.0
<b>Growth Ratios (%)</b>					
Income growth	5.1	(0.2)	7.7	10.7	11.0
EBITDA growth	3.1	8.0	9.7	11.2	12.3
PAT growth	(0.8)	20.0	4.2	13.2	11.3
<b>Turnover Ratios</b>					
Inventor Days	0	0	0	0	0
Debtors Days	38	38	40	39	38
Payable days	9	8	9	9	9

\* MPHL had a 5-month FY14

### Balance Sheet (` mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E
<b>Sources of Funds</b>					
Equity Share Capital	2,102	2,104	1,933	1,935	1,937
Reserves & Surplus	60,829	59,420	52,885	57,433	62,359
<b>Total Shareholders Fund</b>	<b>62,931</b>	<b>61,524</b>	<b>54,818</b>	<b>59,368</b>	<b>64,296</b>
<b>Non- current liabilities</b>	<b>2,378</b>	<b>(2,766)</b>	<b>(41)</b>	<b>(139)</b>	<b>(49)</b>
Long term Borrowings	1,789	11	38	38	38
Deferred tax liabilities	(211)	(3,369)	(1,007)	(1,007)	(1,007)
Other LT liabilities & prov	801	592	928	830	920
<b>Current Liabilities</b>	<b>12,844</b>	<b>10,886</b>	<b>14,020</b>	<b>15,025</b>	<b>16,224</b>
Short-term borrowings	1,325	2,602	3,899	3,899	3,899
Trade payables	4,525	3,878	5,024	5,480	6,070
Other cur liabilities & Prov	6,993	4,406	5,097	5,646	6,254
<b>Total Liabilities</b>	<b>78,153</b>	<b>69,644</b>	<b>68,796</b>	<b>74,254</b>	<b>80,470</b>
<b>Assets</b>					
<b>Non- current Assets</b>	<b>36,385</b>	<b>25,120</b>	<b>29,336</b>	<b>30,575</b>	<b>31,551</b>
Fixed assets	1,728	2,244	1,848	2,254	2,334
Non-current investments	26,696	15,324	20,184	20,184	20,184
Long-term loans & adv	6,881	1,111	1,140	1,389	1,542
Other non-current assets	1,079	6,441	6,164	6,747	7,491
<b>Current assets</b>	<b>41,768</b>	<b>44,523</b>	<b>39,460</b>	<b>43,681</b>	<b>48,920</b>
Current investments	17,364	22,701	14,651	14,651	14,651
Trade receivables	6,489	6,310	8,116	7,541	8,372
Inventories	41	-	-	-	-
<b>Cash &amp; bank balances</b>	<b>8,549</b>	<b>6,133</b>	<b>4,642</b>	<b>10,177</b>	<b>13,337</b>
Short-term loans & adv	2,508	707	824	992	1,102
Other current assets	6,817	8,672	11,227	10,319	11,457
<b>Total Assets</b>	<b>78,153</b>	<b>69,644</b>	<b>68,796</b>	<b>74,254</b>	<b>80,470</b>

### Cash flow Statement

Year End-March	FY16	FY17	FY18	FY19E	FY20E
<b>PBT</b>	<b>9,938</b>	<b>11,342</b>	<b>11,406</b>	<b>12,813</b>	<b>14,455</b>
Depreciation	859	(2,566)	3,071	771	820
Others	(495)	(152)	(131)	-	-
<b>CF before W.cap</b>	<b>10,302</b>	<b>8,624</b>	<b>14,346</b>	<b>13,584</b>	<b>15,275</b>
Inc/dec in W.cap	3,861	2,870	2,057	(1,391)	1,688
<b>Op CF after W.cap</b>	<b>6,440</b>	<b>5,755</b>	<b>12,289</b>	<b>14,975</b>	<b>13,588</b>
Less Taxes	2,696	3,155	2,900	3,331	3,903
<b>Net CF From Operations</b>	<b>3,744</b>	<b>2,600</b>	<b>9,389</b>	<b>11,643</b>	<b>9,685</b>
Inc/(dec) in F.A + CWIP	712	1,108	313	1,177	900
(Pur)/sale of Investments	7,847	(6,034)	(3,190)	-	-
<b>CF from Invest Activities</b>	<b>(8,559)</b>	<b>4,926</b>	<b>2,877</b>	<b>(1,177)</b>	<b>(900)</b>
Loan Raised/(repaid)	(1,230)	(501)	1,324	-	-
Equity Raised	1,385	(5,256)	(10,559)	49	42
Dividend	-	4,185	4,523	4,981	5,666
<b>CF from Fin Activities</b>	<b>155</b>	<b>(9,943)</b>	<b>(13,757)</b>	<b>(4,932)</b>	<b>(5,624)</b>
Net inc/(dec) in cash	(4,660)	(2,417)	(1,491)	5,535	3,161
<b>Op. bal of cash</b>	<b>13,209</b>	<b>8,550</b>	<b>6,133</b>	<b>4,642</b>	<b>10,177</b>
<b>Cl. balance of cash</b>	<b>8,549</b>	<b>6,133</b>	<b>4,642</b>	<b>10,177</b>	<b>13,337</b>



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**Recommendation**      **Expected absolute returns (%) over 12 months**

Buy                      More than 15%

Hold                     15% to -15%

Sell                      Less than -15%

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