



DALAL & BROACHA
STOCK BROKING PVT. LTD.

Analyst: Mayank Babla (022) 67141412

Q2 FY20 Result Update@ Dalal&Broacha

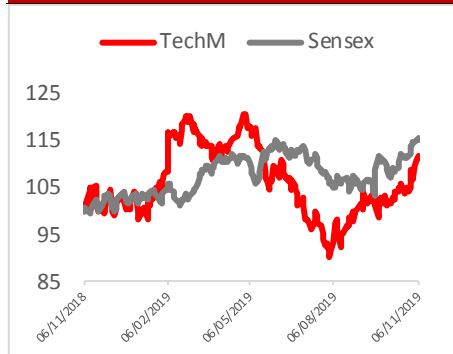
Buy on Dips

Current Price	771
Target Price	825
Upside	7%
52 Week Range	608/846

Key Share Data

Market Cap (Rs.Bn)	744.17
Market Cap (US\$ Mn)	10481.26
No of o/s shares (Mn)	964.84
Face Value	5
Monthly Avg.	
Vol(BSE+NSE) '000	2,740
BSE Code	532755
NSE Code	TECHM
Bloomberg	TECHM:IN

Price performance



% Shareholding	Sept-19	Jun-19
Promoters	35.88	35.90
Public	64.11	64.09
Others	0.01	0.01
Total	100	100

Consolidated Financials (In INR Mn)

INR Mn	Net Sales	% Growth	EBITDA	EBITDA Margin (%)	PAT	PAT Margin (%)	EPS	% Growth	P/E (x)	ROE (%)	ROCE (%)
FY18	3,07,730	5.6%	47,170	15.3%	38,001	12.3%	43.0	33.8%	18.0x	20.7%	19.0%
FY19	3,47,421	12.9%	63,368	18.2%	43,630	12.6%	49.4	14.8%	15.7x	20.5%	18.9%
FY20e	3,66,154	5.4%	61,879	16.9%	44,721	12.2%	50.6	2.5%	15.3x	18.3%	17.2%
FY21e	3,95,140	7.9%	73,278	18.5%	52,061	13.2%	59.0	16.4%	13.1x	18.6%	17.5%

Source: Company, Dalal&Broacha Research

TechM Q2FY20 performance was a beat on our estimates on all fronts

- USD Revenue came in at \$1,287 Mn, +3.2% qoq / +5.7% yoy and 1.4% above our estimate of \$1,269 Mn
 - Revenue in INR terms came in at INR 90,699 Mn, +4.8% qoq / +5.1% yoy and 1.5% above our estimate of INR 89,336 Mn
 - EBITDA stood at INR 15,009 Mn, +14.2% qoq / -7.3% yoy and 0.5% above our estimate of INR 14,938 Mn. EBITDA margins stood at INR 16.5%, +136 bps qoq / -221 bps yoy and 17 bps below our est. of 16.7%
 - EBIT stood at INR 11,594 Mn, +16.8% qoq / -12.4% yoy and 1.1% below our est. of INR 11,725 Mn. EBIT margins at 12.8%, +131 bps qoq / -256 bps yoy and 34 bps below our est. of INR 13.1%
 - PAT was reported at INR 11,236 Mn, +17.1% qoq / +5.6% yoy and 15% above our est. of INR 9,750 Mn. Reported PAT was largely a beat on estimates due to lower Tax Rate of 17%. However, this is a one-off and tax rate is expected to return to 25% henceforth.
 - EPS in Q2FY20 at INR 12.7 vs 10.9 / 12.1 in Q1FY20 / Q2FY19 respectively.
 - Industry-wise Read Through: Communications (41.1% of rev), BFSI (13% of rev), TMT (8.1%) and Retail (7% of rev) led the growth with 4.8% / 2% / 17.4% and 14% yoy growth in reported terms
 - Geography-wise Read Through: North America (48.5% of rev) and ROW (24.9% of rev) drove growth with a 9.2% and 12.6% yoy growth.
- Company added 1 client in the >\$50 Mn client bucket during the quarter

Concall KTAs

- Enterprise business had a very strong quarter with 5.1% growth qoq in cc terms and Comms grew 2.1% qoq.* Enterprise growth will continue to remain steady going ahead, albeit at a softer rate compared to this quarter.
- Recorded the highest ever quarterly deal wins in Q2FY20 at \$1.49bn*. Comms contributed \$1 Bn to the deal wins and balance was Enterprise.
- EBITDA margin walk:* Tailwinds – Operational Efficiency: +100 bps and others such as lower visa costs and synergies with portfolio companies. Headwinds: Balance salary hikes in Q2 – 20-30 bps impact.
- Normalized SGA at 13.5-14%
- DSO increased by 4 days – should come down by next 3-4 quarters. Management focusing on converting unbilled DSO to Billed
- FCF at \$73 Mn (50% of PAT), which was low on account of acquisition of Mad*Pow.
- The tax rate was lower as the company received a tax refund on account of old Tax dispute. The tax rate would be around 25% as guided earlier by the management.
- Company added 5750 employees during the quarter. The headcount addition was more on account of BPO Professionals. Software Professional headcount drop of 2,000 was due to completion of certain short projects for which headcounts were also temporary.



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(viii) Manufacturing segment was soft in the quarter mainly due to the automotive segment, which was de-grew in the Q1 and Q2. However the management eye revival post Q3FY20.

(ix) Growth in BFSI, Travel & Transport and other verticals will even out over the rest of the year. This quarter was particularly strong due to healthy deal wins.

(x) Telecom space largely being driven by opportunities in 5G space and modernization of network and systems and processes. See healthy trends in Communications space. For example, when 4G started, only 4 operators were active. In 5G, more than 30 operators are currently active in trials or deployment.

(xi) EBIT margins may soften by 150-250 bps in H2FY20 vs last year (H2FY19 EBIT margin was ~15.7%) due to certain ramp-ups. However, EBIT margins to come up to 15% in FY21.

(xii) Broad-based deal wins across segments and geographies. For example, deals were won in Digital Transformation, Cloud Migration, IMS, Healthcare (synergies between HCI and TechM brought about 2 deal wins) and Hi-Tech has shown one large deal.

(xiii) Retail segment outperformed in the quarter, contrary to weak performance by peers, as TechM serves smaller sized customers compared to peers and performance was driven by Peninfarina.

Q2FY20 Performance Highlights:

YE March (Rs. mn)	Q2 FY20	Q1 FY20	Q-o-Q change %	Q2 FY19	Y-o-Y change %	Q2 FY20 Estimates	Deviation %
Net Sales (USD Mn)	1,287	1,247	3.2%	1,218	5.7%	1,269	1.4%
Net Sales (INR Mn)	90,699	86,530	4.8%	86,298	5.1%	89,336	1.5%
Less:							
Employees Remuneration & Benefits	63,893	61,642	3.7%	56,923	12.2%	62,270	2.6%
Administrative & Other Expenses	11,797	11,747	0.4%	13,189	(10.6%)	12,128	(2.7%)
Total Operating Expenditure	75,690	73,389	3.1%	70,112	8.0%	74,398	1.7%
EBITDA	15,009	13,141	14.2%	16,186	(7.3%)	14,938	0.5%
Less: Depreciation	3,415	3,213	6.3%	2,944	16.0%	3,213	6.3%
EBIT	11,594	9,928	16.8%	13,242	(12.4%)	11,725	(1.1%)
Less: Interest	383	454	(15.6%)	388	(1.3%)	452	(15.2%)
Add: Other income	2,163	3,413	(36.6%)	1,751	23.5%	1,787	21.1%
Profit Before Tax	13,374	12,887	3.8%	14,605	(8.4%)	13,059	2.4%
Adjusted Profit Before Tax	13,374	12,887	3.8%	14,605	(8.4%)	13,059	2.4%
Less: Total Tax	2,265	3,318	(31.7%)	3,914	(42.1%)	3,265	(30.6%)
Minority Interest	127	102		84		-45	
Reported PAT	11,239	9,593	17.2%	10,642	5.6%	9,750	15.3%
Adjusted PAT	11,236	9,593	17.1%	10,642	5.6%	9,750	15.2%
Reported Diluted EPS (Rs.)	12.7	10.9	17.2%	12.1	5.6%	11.0	15.3%
Adjusted Diluted EPS (Rs.)	12.7	10.9	17.1%	12.1	5.6%	11.0	15.2%
No of Shared Diluted (mn)	883.0	883.0		883.0		883.0	
Margin Analysis %			Change in bps		Change in bps		Change in bps
EBIT Margin	12.8%	11.5%	131	15.3%	(256)	13.1%	(34)
EBIDTA Margin	16.5%	15.2%	136	18.8%	(221)	16.7%	(17)
NPM	12.4%	11.1%	131	12.3%	6	10.9%	148
Adjusted NPM	12.4%	11.1%	130	12.3%	6	10.9%	147
Effective Tax Rate %	16.9%	25.7%	(881)	26.8%	(986)	25.0%	(806)
Cost Analysis %			Change in bps		Change in bps		Change in bps
Employee Cost/Net Sales	70.4%	71.2%	(79)	66.0%	448	69.7%	74
SG&A/Net sales	13.0%	13.6%	(57)	15.3%	(228)	13.6%	(57)

PAT was up 17% qoq and beat our estimates by 15% due to lower Tax Rate at 17% vs 25.7% in the previous quarter. However, this is a one-off and tax rate is expected to return to 25% henceforth

Despite softening of EBIT margins due to certain ramp ups in H2FY20, margins will still be above the 12.8% reported in Q2FY20

Valuation & Outlook

TechM reported a healthy Q2FY20 performance driven by broad-based growth across Verticals and Geographies. Management has given healthy growth guidance for Communications and Enterprise segment going ahead. Although EBIT margins are expected to be softer (150—250 bps YoY) in H2FY20 due to certain ramp ups, they are still expected to improve steadily on a QoQ basis in H2FY20 and in FY21. The stock is currently trading at 15.3x / 13.1x FY20e / FY21e EPS. We recommend a “Buy on Dips” strategy with a revised target price of INR 825, based on 14x FY21e EPS.



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Profit & Loss Statement

YE March (Rs. mn)	FY18	FY19	FY20E	FY21E
Net Sales	3,07,730	3,47,421	3,66,154	3,95,140
Growth %	5.6%	2.9%	5.4%	7.9%
Total Revenue	3,07,730	3,47,421	3,66,154	3,95,140
Less:				
Software development expenses	2,15,299	2,33,590	2,54,268	2,66,543
Selling, Mktg & General expenses	45,261	50,463	50,006	55,320
Total Operating Expenditure	2,60,560	2,84,053	3,04,275	3,21,863
EBIDTA	47,170	63,368	61,879	73,278
Growth %	2.7%	34.3%	-2.3%	18.4%
Less: Depreciation	10,849	11,292	13,458	14,103
EBIT	36,321	52,076	48,421	59,174
Growth %	13.3%	43.4%	-7.0%	22.2%
EBIT Margin (%)	11.8%	15.0%	13.2%	15.0%
Non-operating Income	14,092	5,342	11,315	12,004
Extraordinary Income	0	0	0	0
Extraordinary Expense	0	0	0	0
Profit Before tax	48,789	56,086	58,139	69,678
Tax	10,925	12,544	13,552	17,419
Minority Interest	137	88	135	-198
Net Profit	38,001	43,630	44,721	52,061
Adjusted Profit	38,001	43,630	44,721	52,061
Reported Diluted EPS Rs	43.0	49.4	50.6	59.0
Growth %	33.8%	14.8%	2.5%	16.4%
Adjusted Diluted EPS Rs	43.0	49.4	50.6	59.0
Growth %	33.8%	14.8%	2.5%	16.4%

Balance Sheet

YE March (Rs. mn)	FY18	FY19	FY20E	FY21E
Liabilities				
Equity Capital	4,839	4,839	4,839	4,839
Reserves & Surplus	186,535	2,17,076	2,48,381	2,84,823
Equity	1,91,374	2,21,915	2,53,220	2,89,662
Preference Share Capital	0	0	0	0
Net Worth	1,91,374	2,21,915	2,53,220	2,89,662
Minority Interest	2,034	2,034	2,034	2,034
Net Deferred tax liability/(Asset)	280	307	338	372
Total Loans	1,767	1,567	1,367	1,167
Long term Provisions	6,426	7,069	7,776	8,553
Amount Pending Investigation	12,304	12,304	12,304	12,304
Capital Employed	2,14,185	2,45,197	2,77,039	3,14,093
Assets				
Net Block	89,407	92,407	95,407	98,407
Capital WIP	3,729	2,399	2,399	2,399
Investments	13,244	13,244	13,244	13,244
Intangible Assets	911	911	911	911
Others - A	27,388	30,127	33,140	36,454
Current Assets				
Inventories	414	414	414	414
Sundry Debtors	69,823	76,805	84,486	92,934
Cash and Bank Balance	29,146	49,599	68,636	91,874
Loans and Advances	20,672	22,739	25,013	27,514
Other Current Assets	40,296	43,802	47,617	51,769
Total Current Assets	1,60,350	1,93,359	2,26,166	2,64,505
Less: Current Liabilities & Provisions				
Sundry Creditors	26,541	28,665	30,958	33,435
Provisions	29,153	32,068	35,275	38,802
Other Current Liabilities	25,151	26,519	27,996	29,591
Total Current Liabilities & Provisions	80,845	87,251	94,228	1,01,828
Capital Applied	2,14,185	2,45,197	2,77,039	3,14,093

Free Cash Flow Statement

YE March (Rs. mn)	FY18	FY19	FY20E	FY21E
EBIDTA	36,321	52,076	48,421	59,174
Less: Adjusted Taxes	8,133	11,647	11,287	14,794
NOPLAT	28,188	40,429	37,134	44,381
Plus: Depreciation	10,849	11,292	13,458	14,103
Less: Increase in Working Capital	5,894	6,944	7,167	8,082
Operating Cashflow	33,143	44,777	43,424	50,402
Less: Net Capex	14,341	12,962	16,458	17,103
Less: Increase in Net Other Assets	2,464	2,711	2,982	3,280
Total FCF	16,338	29,104	23,984	30,019

Valuation Ratios

YE March (Rs. mn)	FY18	FY19	FY20E	FY21E
P/E (x)	18.0x	15.7x	15.3x	13.1x
P/BV (x)	3.6x	3.1x	2.7x	2.4x
EV/EBIDTA (x)	13.9x	10.0x	10.0x	8.1x
EV/Sales	2.1x	1.8x	1.7x	1.5x
Market Cap./ Sales (x)	2.2x	2.0x	1.9x	1.7x
Dividend Yield (%)	1.7%	1.9%	2.0%	2.3%

Key Ratios

YE March (Rs. mn)	FY18	FY19	FY20E	FY21E
Key Operating Ratios				
EBITDA Margin (%)	15.3%	18.2%	16.9%	18.5%
Tax / PBT (%)	22.4%	22.4%	23.3%	25.0%
Net Profit Margin (%)	12.3%	12.6%	12.2%	13.2%
RoE (%)	20.7%	20.5%	18.3%	18.6%
RoCE (%)	19.0%	18.9%	17.2%	17.5%
Current Ratio (x)	2.0x	2.2x	2.4x	2.6x
Dividend Payout (%)	30.0%	30.0%	30.0%	30.0%
Book Value Per Share (Rs.)	216.7	251.3	286.8	328.0
Growth Indicators %				
Growth in Gross Block (%)				
Sales Growth (%)	5.6%	12.9%	5.4%	7.9%
EBITDA Growth (%)	12.7%	34.3%	(2.3%)	18.4%
Net Profit Growth (%)	33.8%	14.8%	2.5%	16.4%
Diluted EPS Growth (%)	33.8%	14.8%	2.5%	16.4%
Turnover Ratios				
Debtors (Days of net sales)	83	81	84	86



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