

**RESEARCH**
**Mindtree | TARGET: Rs 2,270 | -9% | SELL**

Demand robust; margin weighed down by supply constraints

**SUMMARY**
**Mindtree**

- Mindtree (MTCL) reported a strong Q1FY22 performance with revenue growth of 7.7% QoQ USD, ahead of our (5.4%) and street estimates
- Despite a record-high gross margin of 40%, EBIT margin declined 80bps QoQ due to elevated SG&A, indicating supply constraints
- Downgrade to SELL on margin headwinds; TP revised to Rs 2,270 (vs. Rs 2,180) on rollover

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**Daily macro indicators**

Indicator	Current	2D (%)	1M (%)	12M (%)
US 10Y yield (%)	1.36	1bps	(9bps)	75bps
India 10Y yield (%)	6.22	4bps	21bps	43bps
USD/INR	74.58	0.1bps	(2.1bps)	0.8bps
Brent Crude (US\$/bbl)	75.16	(0.5)	3.4	75.9
Dow	34,996	0.4	1.5	34.2
Shanghai	3,548	0.7	(1.2)	3.0
Sensex	52,373	0.0	(0.2)	42.7
<b>India FII (US\$ mn)</b>	<b>09-Jul</b>	<b>MTD</b>	<b>CYTD</b>	<b>FYTD</b>
FII-D	10.8	(4.3)	(3,171.1)	(1,143.8)
FII-E	(134.4)	(284.4)	7,799.7	473.4

Source: Bank of Baroda Economics Research

**BOBCAPS Research**

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**SELL**  
 TP: Rs 2,270 | ▼ 9%

**MINDTREE**

| IT Services

| 13 July 2021

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**Stellar growth; margins a drag:** MTCL reported an above-expected Q1 operating performance driven by a revenue beat. Dollar revenue growth at 7.7% QoQ was well ahead of our (5.4%) and consensus estimates. EBITDA margin at 20.3% declined 160bps QoQ, largely in line with our expectations. Gross margin at 40.3% (+260bps QoQ) was at a five-year high due to a higher mix of offshore business, but this was more than offset by a rise in SG&A to 20% of sales (five-quarter high) as subcontracting expenses hit a record high at 11.3% of revenue. Net profit at Rs 3.7bn was boosted by Rs 366mn in forex gains. A margin rebound looks unlikely as management announced sustained high hiring levels and another round of wage hikes.

**Secular growth beyond top client:** Revenue from the top client increased 5.4% QoQ, marking higher growth over the prior two quarters. Revenue ex-top client grew 8.6% QoQ, highlighting the company’s success in client mining beyond its top account. MTCL plans to lower its top-client concentration going forward. The company clocked record deal wins in Q1 with TCV worth US\$ 504mn, up 34% QoQ and 29% YoY, crossing the half billion mark for the first time and signaling healthy future demand. TCV was broad-based, tilting slightly towards the CMT and RCM verticals and consisting mostly of annuity deals with increasing tenure.

**Covid-hit verticals make a comeback:** While BFSI grew 6.6% QoQ USD in Q1 (rebounding after two weak quarters), verticals adversely affected by Covid-19 such as manufacturing & retail/travel grew 6.3%/12.8% QoQ USD. MTCL has also bagged a major cloud migration deal in the travel space.

**Downgrade to SELL:** MTCL’s strong results herald good demand for Indian IT, as indicated by (1) robust TCV, (2) rebound in Covid-hit verticals, and (3) growth in non-top clients. Weak execution, however, remains a concern as SG&A grew 38% QoQ (mostly driven by increased subcontracting costs), causing the EBIT margin to contract 80bps QoQ despite peak gross margins. We expect subdued margins to play spoilsport as more hiring and wage hikes get underway. Consequently, we downgrade the stock from ADD to SELL. On rollover, our new Jun’22 TP stands at Rs 2,270 (vs. Rs 2,180), based on an unchanged one-year forward P/E of 23.4x.

**Key changes**

	Target	Rating
	▲	▼

Ticker/Price	MTCL IN/Rs 2,496
Market cap	US\$ 5.5bn
Free float	87%
3M ADV	US\$ 25.8mn
52wk high/low	Rs 2,618/Rs 963
Promoter/FPI/DII	74%/11%/15%

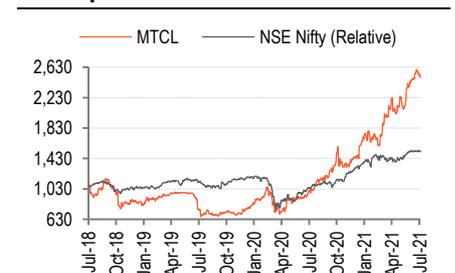
Source: NSE | Price as of 13 Jul 2021

**Key financials**

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	79,678	98,486	112,947
EBITDA (Rs mn)	16,426	20,603	22,874
Adj. net profit (Rs mn)	11,103	14,436	15,453
Adj. EPS (Rs)	67.4	87.7	93.9
Consensus EPS (Rs)	67.4	82.3	92.7
Adj. ROAE (%)	29.7	31.0	28.4
Adj. P/E (x)	37.0	28.5	26.6
EV/EBITDA (x)	24.8	19.6	17.5
Adj. EPS growth (%)	76.0	30.0	7.0

Source: Company, Bloomberg, BOBCAPS Research

**Stock performance**



Source: NSE



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### Recommendation scale: Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

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