

HOLD
TP: Rs 2,266 | ▼ 1%

MPHASIS

| Technology & Internet

| 08 May 2024

Modest growth; BFSI yet to pick up

- Regional banks and mortgages business will continue to draw down the overall BFSI segment
- Expertise in Microsoft Dynamics and Salesforce through acquisition likely to impact positively in improving deal pipeline
- We assume coverage on Mphasis with a HOLD rating and TP of Rs 2,266 based on 22x P/E on FY26E EPS (in line with current P/E)

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Growth headwinds expected in FY25: The company's revenue performance remained volatile over the last few quarters. Banking forms ~47% of the total portfolio, majorly relying on higher discretionary spending, which is impacting near-term growth visibility. Mortgage business (Digital Risk) and DXC channel impacted revenue by 10% over the last two years. We believe higher exposure in regional banks, coupled with uncertainty over US interest rates, will create continued headwinds in critical/major accounts (Top-10 accounts). Tight budgets, insourcing and layoffs likely to disrupt growth for Mphasis, in our view. In this situation, the company needs better discretionary spending and share gains in vendor consolidation.

Reshuffle/hire in senior management team: The company has hired Ashish Devalekar to head the Europe operations and Anurag Bhatia has been transferred to the BPS business.

Building enterprise business through M&A: Mphasis is building capabilities in Microsoft Dynamics/Salesforce through acquisitions of eBecs and Silverline. The company is trying to improve the large client mining through new services offerings. Mphasis has partnered with Kore.AI especially for the infusion of generative AI and the implementation of the product to improve the company's revenue stream.

Moderated deal TCV but stability in margin remains intact: FY24 revenue stood at USD 1.6bn, down 16% in BFS but non-BFS was up 5% YoY. EBIT margin in Q4 was 14.9% (including Silverline integration cost of 110bps QoQ). Margin guidance stood at 14.6-16% in FY25. New total contract value stood at USD 177mn in Direct business and 77% of the deal wins are coming from Next-Gen services.

Valuation outlook: Despite weakness in the mortgage business and tight budgets in key verticals/top accounts, we expect reduction in near-term leakage and recovery in Digital Risk. Mphasis trades at 25.2x FY25E and 22.2x FY26E EPS. We assume coverage with HOLD rating with a TP of Rs 2,266 based on 22x P/E of FY26E EPS in line with current P/E.

Key changes

Target	Rating
▼	◀ ▶

Ticker/Price	MPHL IN/Rs 2,287
Market cap	US\$ 5.2bn
Free float	40%
3M ADV	US\$ 15.6mn
52wk high/low	Rs 2,838/Rs 1,808
Promoter/FPI/DII	52%/29%/14%

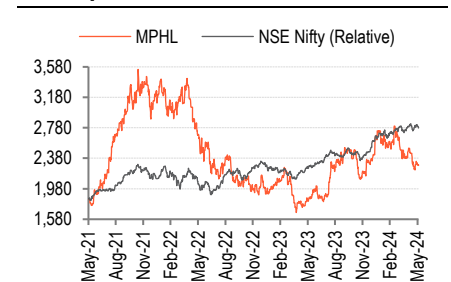
Source: NSE | Price as of 7 May 2024

Key financials

Y/E 31 Mar	FY24A	FY25E	FY26E
Total revenue (Rs mn)	1,32,785	1,41,349	1,48,186
EBITDA (Rs mn)	24,220	26,291	28,896
Adj. net profit (Rs mn)	15,548	17,125	19,469
Adj. EPS (Rs)	82.4	90.6	103.0
Consensus EPS (Rs)	82.4	91.2	105.5
Adj. ROAE (%)	18.6	18.7	19.8
Adj. P/E (x)	27.7	25.2	22.2
EV/EBITDA (x)	17.5	16.2	14.8
Adj. EPS growth (%)	(5.3)	9.9	13.7

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

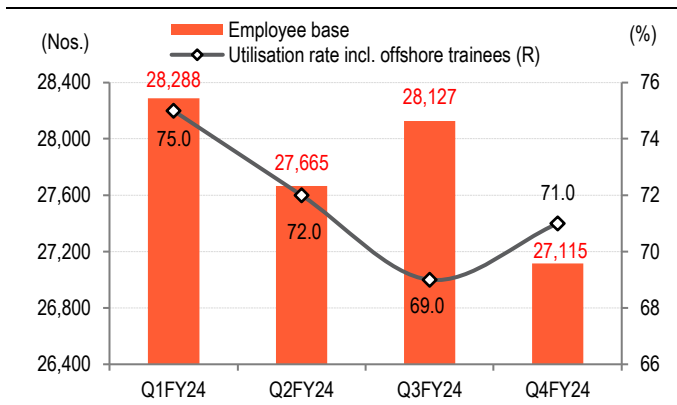


Fig 1 – Quarterly performance

(Rs mn)	Q4FY24	Q3FY23	Q4FY23	QoQ (%)	YoY (%)
US\$ Revenue	411	402	412	2.1	(0.3)
INR Revenue	34,150	33,507	33,893	1.9	0.8
EBIT	5,080	4,972	5,152	2.2	(1.4)
PAT	3,932	3,736	4,052	5.2	(3.0)
EBIT Margin (%)	14.9	14.8	15.2	4bps	(33bps)
PAT Margin (%)	11.5	11.1	12.0	36bps	(44bps)

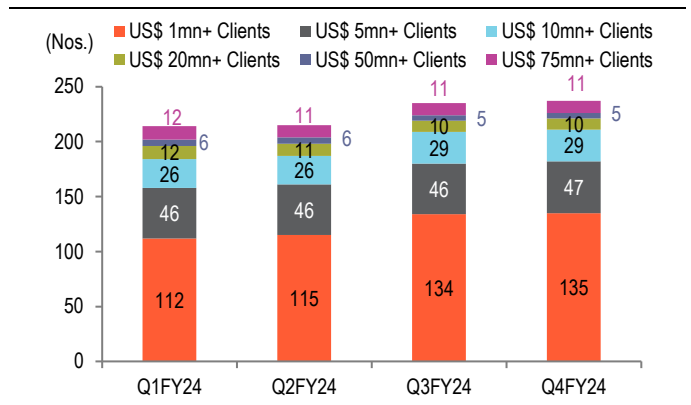
Source: Company, BOBCAPS Research

Fig 2 – Employee metrics



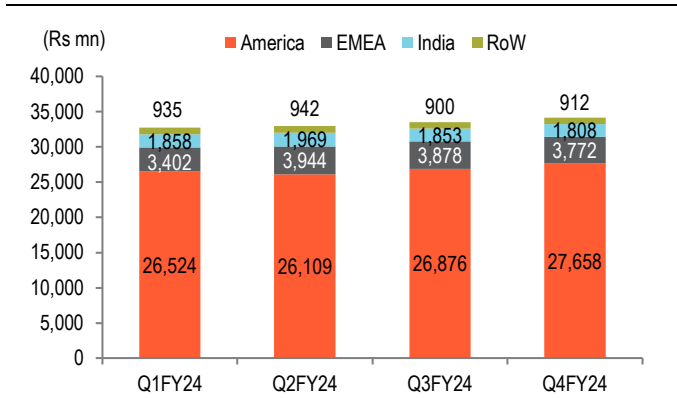
Source: Company, BOBCAPS Research

Fig 3 – Client composition



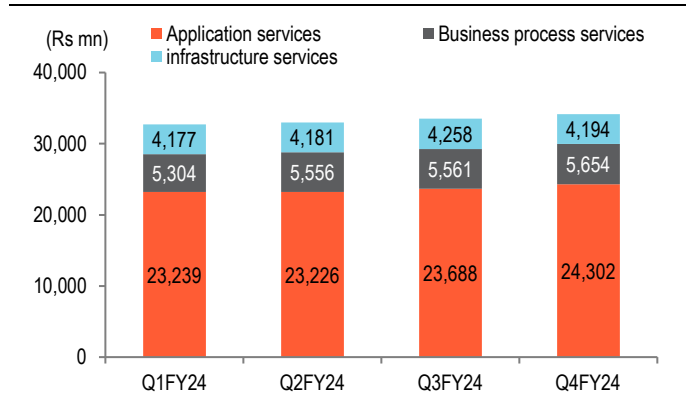
Source: Company, BOBCAPS Research

Fig 4 – Revenue by geography



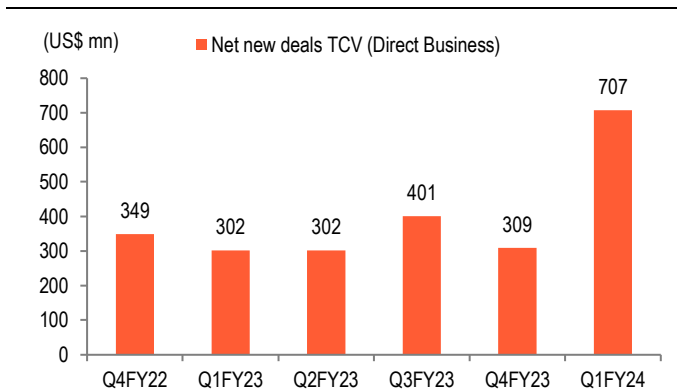
Source: Company, BOBCAPS Research

Fig 5 – Revenue by service type



Source: Company, BOBCAPS Research

Fig 6 – Net new deal TCV (Direct business)



Source: Company, BOBCAPS Research | TCV: Total contract value

Valuation outlook

Despite weakness in the mortgage business and tight budgets in key verticals/top accounts, we expect reduction in near-term leakage and recovery in Digital Risk. Mphasis trades at 25.2x FY25E and 22.2x FY26E EPS. We assume coverage with HOLD rating with a TP of Rs 2,266 based on 22x P/E of FY26E EPS (in line with current P/E.).

Risks

- Decrease in interest rates may lead to higher deal wins in BFSI, and,
- an elongated decision-making cycle could lead to lower transformational deal wins.

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24A	FY25E	FY26E
Total revenue	1,19,614	1,37,984	1,32,785	1,41,349	1,48,186
EBITDA	21,175	24,339	24,220	26,291	28,896
Depreciation	2,906	3,253	4,106	4,240	4,149
EBIT	18,269	21,086	20,114	22,050	24,747
Net interest inc./(exp.)	0	0	0	0	0
Other inc./(exp.)	861	645	570	700	1,040
Exceptional items	0	0	0	0	0
EBT	19,130	21,731	20,684	22,750	25,787
Income taxes	4,821	5,351	5,136	5,626	6,318
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	14,309	16,380	15,548	17,125	19,469
Adjustments	0	0	0	0	0
Adjusted net profit	14,309	16,380	15,548	17,125	19,469

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24A	FY25E	FY26E
Accounts payables	8,496	8,640	7,983	8,094	8,269
Other current liabilities	16,956	14,707	28,536	30,632	32,330
Provisions	2,272	2,797	3,480	3,873	4,060
Debt funds	6,900	7,145	9,173	9,173	9,173
Other liabilities	3,507	3,458	4,184	4,184	4,184
Equity capital	1,878	1,884	1,890	1,890	1,890
Reserves & surplus	67,553	77,464	86,056	92,906	99,720
Shareholders' fund	69,431	79,348	87,946	94,796	1,01,610
Total liab. and equities	1,07,561	1,16,095	1,41,302	1,50,751	1,59,625
Cash and cash eq.	8,268	10,441	8,049	9,124	10,943
Accounts receivables	22,269	26,540	27,027	29,819	32,073
Inventories	0	0	0	0	0
Other current assets	12,896	12,332	10,015	10,456	10,962
Investments	19,356	17,620	30,994	35,994	39,994
Net fixed assets	8,693	9,718	9,215	9,357	9,653
CWIP	110	55	137	137	137
Intangible assets	29,043	31,149	46,588	46,588	46,588
Deferred tax assets, net	6,925	8,240	9,276	9,276	9,276
Other assets	0	0	0	0	0
Total assets	1,07,561	1,16,095	1,41,302	1,50,751	1,59,625

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24A	FY25E	FY26E
Cash flow from operations	17,157	14,618	21,797	20,032	21,879
Capital expenditures	(1,192)	(1,112)	(916)	(4,382)	(4,446)
Change in investments	1,085	1,354	(11,898)	(5,000)	(4,000)
Other investing cash flows	(2,713)	1,582	(12,006)	700	1,040
Cash flow from investing	(2,820)	1,825	(24,821)	(8,682)	(7,406)
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(16,164)	(13,517)	(13,120)	0	0
Interest expenses	14,919	8,245	23,887	0	0
Dividends paid	(465)	(478)	(569)	(10,275)	(12,655)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(1,710)	(5,750)	10,198	(10,275)	(12,655)
Chg in cash & cash eq.	12,627	10,693	7,174	1,075	1,818
Closing cash & cash eq.	8,268	10,441	8,049	9,124	10,943

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24A	FY25E	FY26E
Reported EPS	76.4	87.1	82.4	90.6	103.0
Adjusted EPS	76.4	87.1	82.4	90.6	103.0
Dividend per share	42.1	47.8	45.2	54.4	66.9
Book value per share	371.6	420.9	465.2	501.5	537.5

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24A	FY25E	FY26E
EV/Sales	3.6	3.1	3.2	3.0	2.9
EV/EBITDA	20.3	17.6	17.5	16.2	14.8
Adjusted P/E	29.9	26.3	27.7	25.2	22.2
P/BV	6.2	5.4	4.9	4.6	4.3

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24A	FY25E	FY26E
Tax burden (Net profit/PBT)	74.8	75.4	75.2	75.3	75.5
Interest burden (PBT/EBIT)	104.7	103.1	102.8	103.2	104.2
EBIT margin (EBIT/Revenue)	15.3	15.3	15.1	15.6	16.7
Asset turnover (Rev./Avg TA)	119.4	123.4	103.2	96.8	95.5
Leverage (Avg TA/Avg Equity)	1.5	1.5	1.5	1.6	1.6
Adjusted ROAE	21.2	22.0	18.6	18.7	19.8

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24A	FY25E	FY26E
YoY growth (%)					
Revenue	23.0	15.4	(3.8)	6.4	4.8
EBITDA	17.5	14.9	(0.5)	8.6	9.9
Adjusted EPS	17.3	14.0	(5.3)	9.9	13.7
Profitability & Return ratios (%)					
EBITDA margin	17.7	17.6	18.2	18.6	19.5
EBIT margin	15.3	15.3	15.1	15.6	16.7
Adjusted profit margin	12.0	11.9	11.7	12.1	13.1
Adjusted ROAE	21.2	22.0	18.6	18.7	19.8
ROCE	19.9	21.0	17.5	17.3	18.4
Working capital days (days)					
Receivables	46	65	74	73	76
Inventory	0	0	0	0	0
Payables	67	59	69	99	100
Ratios (x)					
Gross asset turnover	13.6	15.0	14.0	15.2	15.6
Current ratio	1.6	1.9	1.1	1.2	1.2
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	0.0	0.0	0.0	0.0	0.0

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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BUY – Expected return >+15%

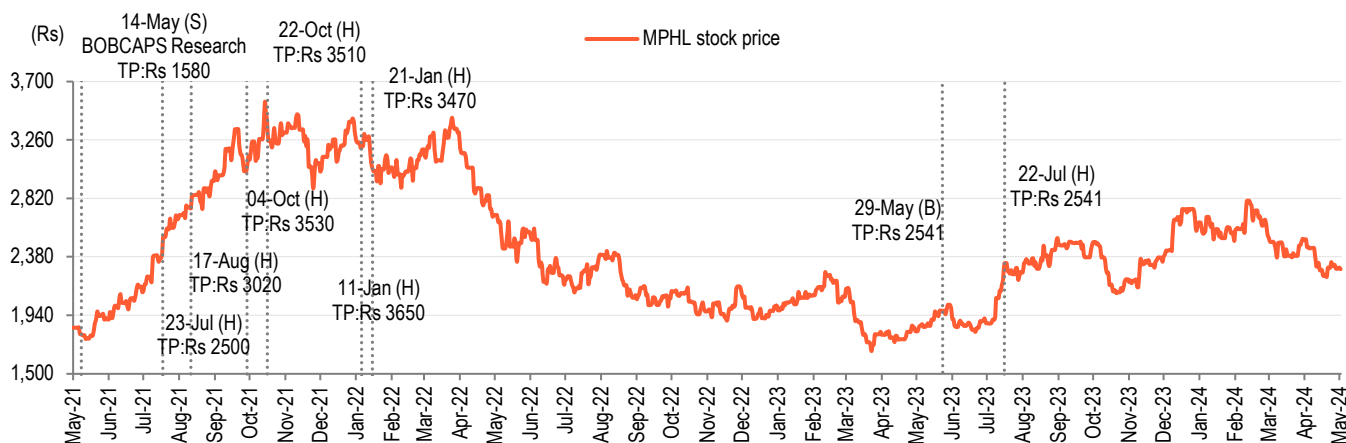
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

Ratings and Target Price (3-year history): MPHASIS (MPHL IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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