

28 February 2022

Mindtree Ltd. – BUY

CMP : Rs.3,830.0
Target Price : Rs.4,598.0
Upside : 20%+
Stop Loss : Rs.3,321.0 (Closing basis)

Investment Thesis

Recently, the stock price of Mindtree Ltd. (Mindtree) corrected by ~24% from 52-week high of Rs.5,060.00 as it has reported lower-than-expected margin on higher headcount addition and high visa cost in last quarter.

Mindtree has recently acquired the NxT Digital Business, the cloud based IoT and AI platform for Industry 4.0 of L&T Group. The acquisition is in sync with Mindtree's strategy of building deep domain expertise to deliver differentiated customer experience, positioning as one of the leading partners for leveraging data and analytics to drive insights and deliver transformational services. Acquisition will also enable it to cater emerging growth areas such as Industry 4.0, smart supply chain processes, end-to-end contactless experience across travel, logistics and manufacturing industries. Current revenue of NxT Digital is only Rs.376mn in FY21, which is 0.5% of Mindtree's total revenue but NxT Digital's deep domain expertise in Industrial IoT combined with Mindtree's scale and ability to cross-sell and up-sell is expected to unlock huge growth potential for Mindtree.

Mindtree has presence in select verticals like, BFSI, Retail, Travel, Hi-Tech and services like, Digital, IMS and ADM. Its success is largely on its niche positioning and strong management pedigree. Its strategy has been backed by strong execution, which helped it grow above industry rate in IT Services business in the last five years. Mindtree remains focused on digital, which continues to grow ahead of company average. Proportion of digital to overall revenue is the highest amongst peers. Mindtree has been investing to bolster its early mover advantage in digital through acquisitions like, P&C Insurance, SAP HANA, CPG analytics and Salesforce. We believe digital will help Mindtree to grow at a healthy pace with cross selling services to existing client and need to outsource due to reducing time to market and increased product launches.

Financials

- During the past 5 years, revenue of Mindtree grew at a CAGR of 11.3% while PAT grew at a CAGR of 15.0% in the same period.

Consol. (Rs.Mn.)	FY19	FY20	FY21	FY22E	FY23E
Revenue	70,215	77,643	79,678	99,598	114,537
EBITDA	10,645	10,815	16,567	20,709	23,815
% growth	43.8	1.6	53.2	25.0	15.0
PAT	7,541	6,309	11,105	15,547	17,817
EPS (INR)	45.9	38.3	67.4	94.4	108.2
P/E (x)	83.4	99.9	56.8	40.6	35.4
RoE (%)	22.9%	20.0%	25.8%	32.9%	34.4%

- Mindtree has reported 4.7% QoQ growth in revenue in US\$ term to \$366.0mn in Q3FY22 led by Technology, BFSI and travel verticals which grew 6.1%, 4.7%, 7.0% QoQ, respectively.

Stock Data

Market Cap (Rs. Mn)	6,29,915
Market Cap (\$ Mn)	8,345.2
Shares O/S (in Mn)	164.7
Avg. Volume (3 month)	12,15,000
52-Week Range (Rs.)	5,060.00 / 1,712.60

Shareholding Pattern

Promoters	61.00%
FII's	15.72%
Institutions	9.71%
Others (incl. body corporate)	13.57%

Performance (%)	1M	6M	1Yr
Absolute	-2.0%	3.1%	122.9%
BSE IT	-3.7%	-2.1%	30.5%

Key Ratios

Div Yield	0.7%
TTM PE	42.1x
ROE	30.8%
TTM EPS (Rs.)	90.8/-

- Mindtree's EBITDA grew by 11.6% QoQ in Q3FY22 to Rs.5,911mn. As a result, EBITDA margin also improved by 100bps QoQ to 21.5% in Q3FY22 mainly due to 60bps on account of business growth while 40bps was due to currency tailwinds.
- Mindtree is looking to scale up the fresher hiring run rate. Mindtree has added 1500 freshers for the quarter and looking to keep up this pace for the next few quarters to cater to the increasing demand.

Key Business Highlights

- Mindtree is a global IT consulting and implementation company that delivers business solutions through global software development. It operates in five segments, viz, Retail, Consumer Packaged Goods & Manufacturing; BFSI; Hitech & Media Services; Travel & Hospitality.
- Mindtree offers services in areas of agile, analytics and information management, application development and maintenance, business process management, business technology consulting, cloud, digital business's, mobility and independent testing.
- Mindtree generated 73.0% of its total revenue from the US while Europe contributed 18.6% and remaining (8.4%) came from rest of world including India in Q3FY22.

Valuation

- Mindtree is planning to capture the increasing growth opportunity in Europe and it more open to outsourcing opportunities. It has hired significant client partners and business development managers (BDMs) to expand its presence in Nordics (Finland and Norway) and DACH region. It has added sales team to expand in Australia and will leverage Parent's strong presence to expand in Japan. It also plans to expand in travel & hospitality and BFSI segment in Middle East.
- Mindtree's expertise in cloud is expected to drive its industry leading growth. Each \$1 spent by client on cloud, Mindtree aims to maximize its revenue to 1.5x led by multiple value-added cloud offerings ranging from enterprise workload transformation, cloud security, Data modernization to Industry Platforms. All 4 service lines leverage cloud in a big way. Mindtree has also built service line focused sales team over last two years which also fits well for 'hyper scalar hyper growth' strategy as all four service lines involve cloud in a big way.
- Mindtree's margins dipped 160bps in Q1FY22 due to headcount addition and visa cost. We believe the margin will be impacted due to selective wage hike, investments to drive growth and return of few cost (which was saved due to Covid-19) in the next few quarters. However, Mindtree is expected to maintain margins at over 20% going ahead led by fixed price projects, higher offshoring, lower sub con cost, annuity type revenues and revenue growth.
- With recently acquired the NxT Digital Business, niche positioning & strong management pedigree, remains focused on digital, planning to capture increasing growth opportunity in Europe, expertise in cloud will drive industry leading growth and expected to maintain margins at over 20%, we value Mindtree at 42.5x FY23E EPS of Rs.108.20 to arrive at target price of Rs.4,598.00, an upside of ~20%.

Risk & Concern

- Mindtree generates ~93% of revenues from US and Europe, any economic slowdown in these regions may affect IT spending negatively and may affect revenue growth of Mindtree.
- Any project ramp downs of any of the vertical may alter the product mix and overall revenue of Mindtree.
- Mindtree faces supply side constraints as it directly competes with tier-1 companies for specialized manpower.

Graphs & Charts

Figure 1: Net Sales Trend

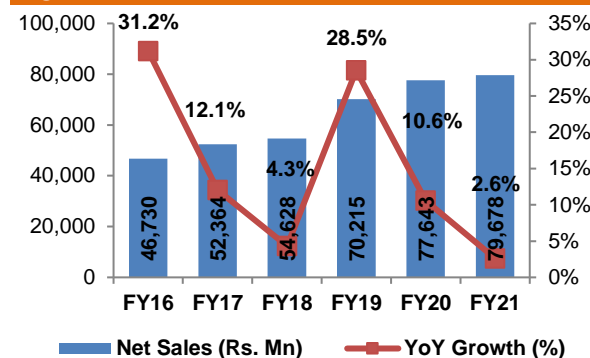


Figure 2: EBITDA & EBITDA Margin Trend

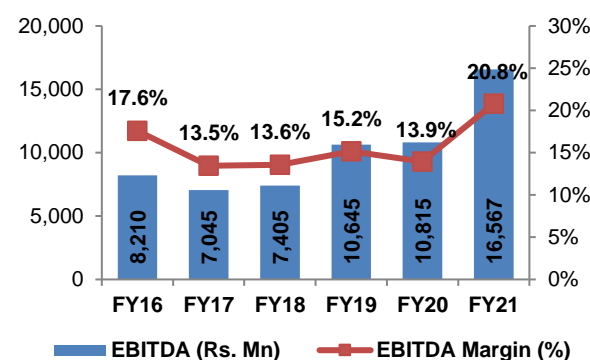


Figure 3: PAT Trend

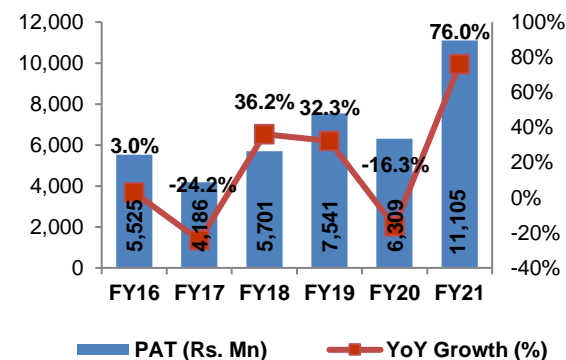
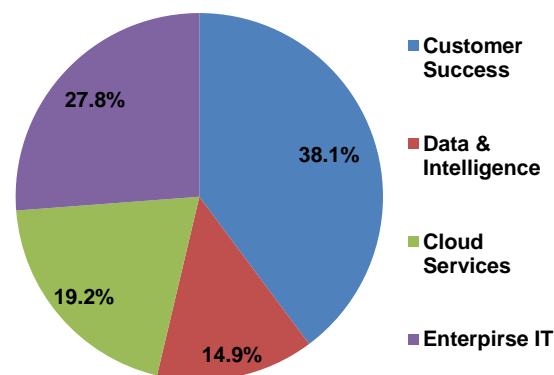


Figure 4: Service-wise Revenue (Q3FY22)



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