

Tech Mahindra

Disappointing; can remain weaker for longer

Tech Mahindra's (TECHM) disappointing Q1 performance has elements that could take longer to recover. While the dismal levels of margin are the bottom, its recovery trajectory can be protracted. The slip in Q1 revenue of -4% QoQ was largely led by the CME vertical (38% of revenue) which dropped 9.5% QoQ, while the Enterprise segment delivered in line with peers (flat sequentially). The decline in the CME vertical was a combination of impact on network services, lower discretionary spend, and transition-delay between project completion and project/phase starts. The margin was impacted by certain one-offs pertaining to provision towards client-specific situations (-200bps impact). We downgrade TECHM to Reduce (ADD earlier) with a TP at INR 1,020 (14x Jun-25E EPS) as recovery in growth/margin may be protracted on sub-par bookings and near-term challenges in CME vertical may persist for longer (recent instances of deals from large customers going to competition as well as business challenges for telcos).

- Q1FY24 highlights:** (1) TECHM's Q1 revenue came at USD 1,601mn, -4% QoQ and -2% YoY (HSIE est. USD 1,650mn). (2) CME vertical led the decline at 9.5% QoQ while enterprise was flat at -0.3% QoQ—Manufacturing vertical (17% of revenue) led the growth at 2% QoQ, supported by the Auto, Aero and Industrial segments. (3) Net new deal TCV declined sharply at USD 359mn, -40/-50% QoQ/YoY which will also impact near-term growth. (4) Within geographies, the decline was led by Europe and RoW with a 6.7% and 8.2% QoQ decline, while Americas was flat (-0.5% QoQ). (5) EBITM dropped 438bps QoQ, impacted by -200bps from provision for client bankruptcy, -50bps from Comviva seasonality, wage increase (-130bps QoQ) and on revenue decline; Q2 will be impacted by wage increase of senior workforce (~100bps impact).
- Outlook:** We have factored USD revenue growth at -2.0%, 10.5%, and 10.5% for FY24/25/26E with revenue CAGR at 6% over FY23-26E factoring CME growth at -9.5%, +5.7%, +7.7% and Enterprise growth at 3%, 13.3%, 12% over FY24/25/26E. Factored EBITM at 9.3/12.7/13.9% over FY24/25/26E resulting in earnings acceleration in FY25E, following a 20% decline in FY24E. Nearly half of the earnings cut for FY24E is attributable to the Q1 miss and FY24E has more downside risk.

Quarterly Financial summary

YE March (INR bn)	Q1FY24	Q1FY23	YoY (%)	Q4FY23	QoQ (%)	FY22	FY23	FY24E	FY25E	FY26E
Revenue (USD mn)	1,601	1,633	(1.9)	1,668	(4.0)	5,998	6,606	6,473	7,151	7,899
Revenue	131.59	127.08	3.5	137.18	(4.1)	446.46	532.90	535.17	600.71	671.42
EBIT	8.91	14.03	(36.5)	15.30	(41.7)	65.00	60.72	49.77	76.04	93.25
APAT	6.93	11.32	(38.8)	13.30	(47.9)	55.66	50.68	40.48	61.13	74.42
Diluted EPS (INR)	7.9	12.8	(38.8)	15.1	(47.9)	63.1	57.5	45.9	69.3	84.4
P/E (x)						18.1	19.9	24.9	16.5	13.5
EV / EBITDA (x)						11.7	11.9	13.9	10.0	8.4
RoE (%)						21.5	18.5	14.3	20.8	24.2

Source: Company, HSIE Research, Consolidated Financials

Change in Estimates

YE Mar (INR bn)	FY24E Old	FY24E Revised	Change %	FY25E Old	FY25E Revised	Change %
Revenue (USD mn)	6,765	6,473	(4.3)	7,425	7,151	(3.7)
Revenue	559.32	535.17	(4.3)	623.71	600.71	(3.7)
EBIT	66.96	49.77	(25.7)	83.37	76.04	(8.8)
EBIT margin (%)	12.0	9.3	-267bps	13.4	12.7	-71bps
APAT	52.38	40.48	(22.7)	65.21	61.13	(6.2)
EPS (INR)	59.4	45.9	(22.7)	73.9	69.3	(6.2)

Source: Company, HSIE Research

REDUCE

CMP (as on 26 Jul 2023) INR 1,143

Target Price INR 1,020

NIFTY 19,778

KEY CHANGES	OLD	NEW
Rating	ADD	REDUCE
Price Target	INR 1,150	INR 1,020
EPS %	FY24E	FY25E
	-23	-6

KEY STOCK DATA

Bloomberg code	TECHM IN
No. of Shares (mn)	975
MCap (INR bn) / (\$ mn)	1,114/13,626
6m avg traded value (INR mn)	3,061
52 Week high / low	INR 1,271/968

STOCK PERFORMANCE (%)

	3M	6M	12M
Absolute (%)	14.7	8.8	16.4
Relative (%)	4.1	(2.0)	(4.3)

SHAREHOLDING PATTERN (%)

	Mar-23	Jun-23
Promoters	35.18	35.16
FIs & Local MFs	25.85	26.96
FPIs	26.87	25.69
Public & Others	12.10	12.19

Pledged Shares - -

Source : BSE

Pledged shares as % of total shares

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Disclosure:

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