

## Disappointing show

Information Technology ▶ Result Update ▶ February 2, 2024

**TARGET PRICE (Rs): 2,700**

**Mphasis reported weak operating performance in Q3 due to the miss on revenue. Gross revenue grew 1% QoQ (organic revenue declined 2.8%) to USD402.3mn, logging below our estimate of USD414.9mn. EBITM fell by 60bps QoQ to 14.9%, in line with our estimate and includes a 110bps impact from the Silverline integration. Higher than usual furloughs hit revenue growth in Q3, although Management highlighted signs of stability returning to business. BFS continues to face headwinds from weakness in some pockets, while stability is seen reappearing in the mortgage business. Mphasis signed net new deals worth USD241mn (85% of deal wins in new-gen services), taking the 9MFY24 deal intake to USD1.2bn, up 20% YoY. Company is observing pick up in conversion of TCV to revenue. It expects sequential revenue growth to resume from Q4, on account of reversal of furloughs, bottoming of mortgage, improving conversion from deal TCV to revenue, and deal wins & pipeline. We cut FY24-26E EPS by 2-3%, factoring-in the Q3 performance miss. We maintain REDUCE on Mphasis, with revised TP of Rs2,700/share at 26x its Dec-25E EPS.**

### Mphasis: Financial Snapshot (Consolidated)

Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Revenue	119,616	137,985	133,202	149,370	169,082
EBITDA	21,177	24,340	24,152	27,783	31,449
Adj. PAT	14,310	16,380	15,628	17,714	20,479
Adj. EPS (Rs)	76.3	86.9	82.8	93.8	108.5
EBITDA margin (%)	17.7	17.6	18.1	18.6	18.6
EBITDA growth (%)	17.5	14.9	(0.8)	15.0	13.2
Adj. EPS growth (%)	17.2	13.9	(4.8)	13.4	15.6
RoE (%)	21.2	22.0	19.0	19.9	21.1
RoIC (%)	31.6	32.6	25.5	25.5	29.2
P/E (x)	33.5	29.4	30.9	27.3	23.6
EV/EBITDA (x)	21.8	18.9	19.5	16.7	14.5
P/B (x)	6.9	6.1	5.6	5.2	4.8
FCFF yield (%)	3.3	2.8	2.5	3.7	4.3

Source: Company, Emkay Research

### Result summary

Gross revenue grew 1% QoQ to USD402.3mn, missing our estimate of USD414.9mn. DXC revenue declined 9.5% QoQ, while direct revenue grew 2% QoQ (organic declined 2%). EBITM fell by 60bps QoQ, in line with our estimates, impacted by the Silverline integration (110bps) and partially offset by operational rigor (50bps). Revenue growth was led by insurance (6.9% CC QoQ), logistics & transportation (3.2%), BFS (0.3%), and emerging industries (11.0%), while TMT declined 9.0%. Among geographies, Americas grew 2.9% QoQ, while EMEA, India, and RoW posted de-growth of 1.7%, 5.9%, and 4.5%, respectively. Mphasis signed net new deals worth USD241mn (USD1.2bn in 9MFY24, up 20% YoY), of which 85% are in new-gen services. The deal pipeline remains healthy (up sequentially, in double digits) and is well distributed across verticals, driven by data modernization, Agile IT Apps, and platforms. The company signed four large deals in Q3 (14 in 9MFY24). Its top-10 accounts declined 7.5% CC YoY, mainly due to higher than usual furloughs and regional banking issues in the USA. **What we like:** Healthy cash conversion (OCF/EBITDA at ~98%), margin defense, and healthy deal pipeline. **What we did not like:** Q3 revenue miss, delay in recovery in organic revenue growth recovery, softness in top clients.

### Earnings call KTAs

i) Company continues to witness bottoming of revenue, which is playing out even if the seasonality hit is ruled out. Pressure on discretionary spend as well as seasonality impacted growth QoQ in the Applications segment. While macro headwinds persist, clients are also fast-tracking to newer sources of value, such as AI, to stay ahead. ii) Mortgage business is stable, aided by new deal wins. iii) The deal pipeline remains healthy across BFS and non-BFS, backed by proactive pursuits that contributed to 81% of the pipeline. Large deals continue to bob up in the pipeline, even as an uptick is also being seen in smaller deals, thus providing better visibility to revival in discretionary deals, while also boosting the pace of revenue conversion. The healthy mix of large deals in the pipeline reflects in the ongoing digital transformation, and the accelerating digital adoption remains the core theme for clients. iv) Management expects revenue growth to recover from Q4, led by BFS and TMT. It expects growth rebound to be beyond seasonality. v) Revenue growth on YoY basis was impacted by softness in discretionary spending, regional banking issues, weakness in mortgage business, and insourcing challenges. vi) Excluding M&A charges, Management retains its target EBITM range of 15.25-16.25%. vii) Silverline contributed ~USD15mn in Q3, and was lower than the previously disclosed CY22 revenue run-rate, as MPHL is more focused on the enterprise segment, while Silverline focus is a combination of both, enterprise and mid-market.

Target Price – 12M	Dec-24
<b>Change in TP (%)</b>	<b>(3.6)</b>
Current Reco.	REDUCE
Previous Reco.	REDUCE
Upside/(Downside) (%)	5.5
CMP (02-Feb-24) (Rs)	2,560.2

Stock Data	Ticker
52-week High (Rs)	2,789
52-week Low (Rs)	1,660
Shares outstanding (mn)	188.8
Market-cap (Rs bn)	483
Market-cap (USD mn)	5,830
Net-debt, FY24E (Rs mn)	-12,372
ADTV-3M (mn shares)	1
ADTV-3M (Rs mn)	1,379.2
ADTV-3M (USD mn)	16.6
Free float (%)	44.0
Nifty-50	21,854
INR/USD	82.9
<b>Shareholding, Dec-23</b>	
Promoters (%)	55.5
FPIs/MFs (%)	15.7/23.8

Price Performance			
(%)	1M	3M	12M
Absolute	(4.2)	17.0	22.2
Rel. to Nifty	(5.1)	2.5	(1.6)

### 1-Year share price trend (Rs)



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**Exhibit 1: Quarterly snapshot**

(Rs mn)	Q3FY24	Q2FY24	QoQ (%)	Q3FY23	YoY (%)
Gross Sales (USD mn)	387.1	398.4	-2.8%	429.4	-9.8%
Net Sales (USD mn)	400.8	396.0	1.2	425.9	-5.9
Net sales	33,380	32,765	1.9	35,062	-4.8
Operating expenses	27,373	26,809		28,887	
EBITDA	6,007	5,956	0.9	6,175	-2.7
Margins (%)	18.0	18.2	-20.0	17.6	40.00
Depreciation	1,035	889		821	
EBIT	4,972	5,067	-1.9	5,354	-7.1
Margins (%)	14.9	15.5	-60.0	15.3	(40)
Other income	14	150		156	
Pre-tax profit	4,986	5,217		5,510	
Tax provided	1250	1298		1387	
Profit after tax	3,736	3,919	-4.7	4,123	-9.4
Emkay Net profit	3,736	3,919	-4.7	4,123	-9.4
EPS (Rs)	19.8	20.8	-4.8	21.9	-9.6

Source: Company, Emkay Research

**Exhibit 2: Actuals vs estimates**

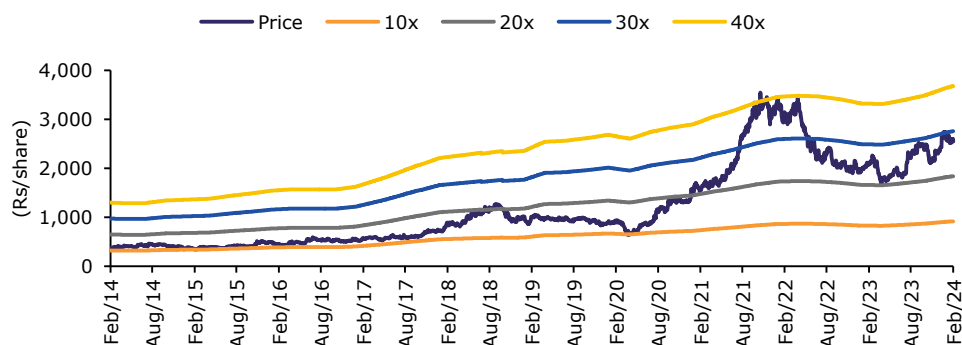
(Rs mn)	Actual	Estimates		Variation		Comment
		Emkay	Consensus	Emkay	Consensus	
Gross Revenues (in US\$ mn)	402	415	413	-3.0%	-2.7%	Revenue performance missed expectations
Sales	33,380	34,504	34,433	-3.3%	-3.1%	
EBIT	4,972	5,128	5,085	-3.0%	-2.2%	
EBIT margin	14.9%	14.9%	14.8%	0 bps	10 bps	EBITM was in line with our estimates
PAT	3,736	3,917	3,915	-4.6%	-4.6%	Profit came lower than expectations due to the revenue miss

Source: Company, Emkay Research

**Exhibit 3: Changes in estimates**

(Rs mn)	FY24E			FY25E			FY26E		
	Old	New	Change	Old	New	Change	Old	New	Change
Reported Revenue (USD mn)	1,640	1,615	-1.6%	1,837	1,777	-3.3%	2,057	1,989	-3.3%
YoY change	-4.5%	-6.0%		12.0%	10.0%		12.0%	12.0%	
Revenue	135,340	133,202	-1.6%	154,205	149,370	-3.1%	174,727	169,082	-3.2%
EBIT	20,583	20,286	-1.4%	23,984	23,239	-3.1%	27,395	26,520	-3.2%
EBIT margin (%)	15.2	15.2		15.6	15.6		15.7	15.7	
Net Profit	15,911	15,628	-1.8%	18,263	17,714	-3.0%	21,126	20,479	-3.1%
EPS (Rs)	84.4	82.8	-1.9%	96.8	93.8	-3.1%	112.0	108.5	-3.2%

Source: Company, Emkay Research

**Exhibit 4: MPHL – One-year forward P/E**

Source: Company, Emkay Research

## Mphasis: Consolidated Financials and Valuations

Profit & Loss					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
<b>Revenue</b>	<b>119,616</b>	<b>137,985</b>	<b>133,202</b>	<b>149,370</b>	<b>169,082</b>
Revenue growth (%)	23.0	15.4	(3.5)	12.1	13.2
<b>EBITDA</b>	<b>21,177</b>	<b>24,340</b>	<b>24,152</b>	<b>27,783</b>	<b>31,449</b>
EBITDA growth (%)	17.5	14.9	(0.8)	15.0	13.2
Depreciation & Amortization	2,908	3,252	3,866	4,544	4,929
<b>EBIT</b>	<b>18,269</b>	<b>21,088</b>	<b>20,286</b>	<b>23,239</b>	<b>26,520</b>
EBIT growth (%)	17.0	15.4	(3.8)	14.6	14.1
Other operating income	0	0	0	0	0
Other income	1,605	1,616	1,883	1,436	1,908
Financial expense	744	973	1,324	900	940
<b>PBT</b>	<b>19,130</b>	<b>21,731</b>	<b>20,845</b>	<b>23,775</b>	<b>27,488</b>
Extraordinary items	0	0	0	0	0
Taxes	4,820	5,351	5,217	6,061	7,008
Minority interest	0	0	0	0	0
Income from JV/Associates	0	0	0	0	0
<b>Reported PAT</b>	<b>14,310</b>	<b>16,380</b>	<b>15,628</b>	<b>17,714</b>	<b>20,479</b>
PAT growth (%)	17.6	14.5	(4.6)	13.4	15.6
<b>Adjusted PAT</b>	<b>14,310</b>	<b>16,380</b>	<b>15,628</b>	<b>17,714</b>	<b>20,479</b>
<b>Diluted EPS (Rs)</b>	<b>76.3</b>	<b>86.9</b>	<b>82.8</b>	<b>93.8</b>	<b>108.5</b>
Diluted EPS growth (%)	17.2	13.9	(4.8)	13.4	15.6
<b>DPS (Rs)</b>	<b>46.0</b>	<b>50.0</b>	<b>50.0</b>	<b>55.0</b>	<b>65.0</b>
<b>Dividend payout (%)</b>	<b>60.3</b>	<b>57.5</b>	<b>60.4</b>	<b>58.6</b>	<b>59.9</b>
EBITDA margin (%)	17.7	17.6	18.1	18.6	18.6
EBIT margin (%)	15.3	15.3	15.2	15.6	15.7
Effective tax rate (%)	25.2	24.6	25.0	25.5	25.5
<b>NOPLAT (pre-IndAS)</b>	<b>13,666</b>	<b>15,895</b>	<b>15,209</b>	<b>17,315</b>	<b>19,758</b>
Shares outstanding (mn)	187.5	188.4	188.8	188.8	188.8

Source: Company, Emkay Research

Cash flows					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
PBT	19,130	21,731	20,845	23,775	27,488
Others (non-cash items)	3,215	4,592	4,311	4,786	4,975
Taxes paid	(3,686)	(5,926)	(5,217)	(6,061)	(7,008)
Change in NWC	(1,501)	(5,779)	(56)	(1,017)	(1,328)
<b>Operating cash flow</b>	<b>17,157</b>	<b>14,618</b>	<b>19,883</b>	<b>21,483</b>	<b>24,126</b>
Capital expenditure	(1,192)	(1,112)	(8,006)	(3,450)	(3,450)
Acquisition of business	(5,219)	0	(11,850)	0	0
Interest & dividend income	321	286	879	658	894
<b>Investing cash flow</b>	<b>(1,594)</b>	<b>1,918</b>	<b>(11,298)</b>	<b>(8,792)</b>	<b>(10,556)</b>
Equity raised/(repaid)	442	271	0	0	0
Debt raised/(repaid)	32	(3,557)	15	0	0
Payment of lease liabilities	(1,443)	(1,493)	0	0	0
Interest paid	(741)	(970)	(1,324)	(900)	(940)
Dividend paid (incl tax)	(12,177)	(8,652)	(9,438)	(10,382)	(12,270)
Others	0	0	0	0	0
<b>Financing cash flow</b>	<b>(13,887)</b>	<b>(14,402)</b>	<b>(10,747)</b>	<b>(11,282)</b>	<b>(13,210)</b>
Net chg in Cash	1,676	2,134	(2,162)	1,409	361
OCF	17,157	14,618	19,883	21,483	24,126
Adj. OCF (w/o NWC chg.)	18,658	20,397	19,939	22,500	25,454
FCFF	15,966	13,506	11,877	18,033	20,676
FCFE	15,542	12,820	11,432	17,791	20,630
OCF/EBITDA (%)	81.0	60.1	82.3	77.3	76.7
FCFE/PAT (%)	108.6	78.3	73.1	100.4	100.7
<b>FCFF/NOPLAT (%)</b>	<b>116.8</b>	<b>85.0</b>	<b>78.1</b>	<b>104.1</b>	<b>104.6</b>

Source: Company, Emkay Research

Balance Sheet					
Y/E Mar (Rs mn)	FY22	FY23	FY24E	FY25E	FY26E
Share capital	1,878	1,884	1,884	1,884	1,884
Reserves & Surplus	67,553	77,464	83,654	90,986	99,196
<b>Net worth</b>	<b>69,431</b>	<b>79,348</b>	<b>85,538</b>	<b>92,870</b>	<b>101,080</b>
Minority interests	0	0	0	0	0
Deferred tax liability (net)	(898)	(1,393)	(1,393)	(1,393)	(1,393)
<b>Total debt</b>	<b>5,272</b>	<b>1,985</b>	<b>2,000</b>	<b>2,000</b>	<b>2,000</b>
<b>Total liabilities &amp; equity</b>	<b>73,806</b>	<b>79,940</b>	<b>86,145</b>	<b>93,477</b>	<b>101,687</b>
Net tangible fixed assets	2,456	2,249	1,969	1,815	1,532
Net intangible assets	1,695	1,563	5,788	4,754	3,686
Net ROU assets	6,236	7,469	7,668	7,763	7,634
Capital WIP	110	324	50	50	50
Goodwill	27,348	29,586	41,436	41,436	41,436
Investments [JV/Associates]	3,778	3,848	3,848	3,848	3,848
<b>Cash &amp; equivalents</b>	<b>23,846</b>	<b>24,213</b>	<b>14,372</b>	<b>21,781</b>	<b>30,141</b>
Current assets (ex-cash)	40,475	44,690	44,831	48,120	52,109
Current Liab. & Prov.	32,139	33,732	33,818	36,089	38,749
<b>NWC (ex-cash)</b>	<b>8,335</b>	<b>10,958</b>	<b>11,014</b>	<b>12,031</b>	<b>13,359</b>
<b>Total assets</b>	<b>73,806</b>	<b>79,940</b>	<b>86,145</b>	<b>93,477</b>	<b>101,687</b>
Net debt	(18,574)	(22,229)	(12,372)	(19,781)	(28,141)
Capital employed	73,806	79,940	86,145	93,477	101,687
<b>Invested capital</b>	<b>46,072</b>	<b>51,555</b>	<b>67,875</b>	<b>67,799</b>	<b>67,648</b>
BVPS (Rs)	370.4	421.2	453.1	492.0	535.5
Net Debt/Equity (x)	(0.3)	(0.3)	(0.1)	(0.2)	(0.3)
Net Debt/EBITDA (x)	(0.9)	(0.9)	(0.5)	(0.7)	(0.9)
Interest coverage (x)	0.0	0.0	0.1	0.0	0.0
<b>RoCE (%)</b>	<b>27.7</b>	<b>29.5</b>	<b>26.7</b>	<b>27.5</b>	<b>29.1</b>

Source: Company, Emkay Research

Valuations and key Ratios					
Y/E Mar	FY22	FY23	FY24E	FY25E	FY26E
P/E (x)	33.5	29.4	30.9	27.3	23.6
P/CE(x)	27.9	24.6	24.8	21.7	19.0
P/B (x)	6.9	6.1	5.6	5.2	4.8
EV/Sales (x)	3.9	3.3	3.5	3.1	2.7
EV/EBITDA (x)	21.8	18.9	19.5	16.7	14.5
EV/EBIT(x)	25.3	21.8	23.2	19.9	17.2
EV/IC (x)	10.0	8.9	6.9	6.8	6.7
FCFF yield (%)	3.3	2.8	2.5	3.7	4.3
FCFE yield (%)	3.2	2.7	2.4	3.7	4.3
Dividend yield (%)	1.8	2.0	2.0	2.1	2.5
<b>DuPont-RoE split</b>					
Net profit margin (%)	12.0	11.9	11.7	11.9	12.1
Total asset turnover (x)	1.7	1.8	1.6	1.7	1.7
Assets/Equity (x)	1.1	1.0	1.0	1.0	1.0
<b>RoE (%)</b>	<b>21.2</b>	<b>22.0</b>	<b>19.0</b>	<b>19.9</b>	<b>21.1</b>
<b>DuPont-RoIC</b>					
NOPLAT margin (%)	11.4	11.5	11.4	11.6	11.7
IC turnover (x)	2.8	2.8	2.2	2.2	2.5
<b>RoIC (%)</b>	<b>31.6</b>	<b>32.6</b>	<b>25.5</b>	<b>25.5</b>	<b>29.2</b>
<b>Operating metrics</b>					
Core NWC days	25.4	29.0	30.2	29.4	28.8
<b>Total NWC days</b>	<b>25.4</b>	<b>29.0</b>	<b>30.2</b>	<b>29.4</b>	<b>28.8</b>
Fixed asset turnover	2.8	2.8	2.1	2.0	2.2
Opex-to-revenue (%)	82.3	82.4	81.9	81.4	81.4

Source: Company, Emkay Research

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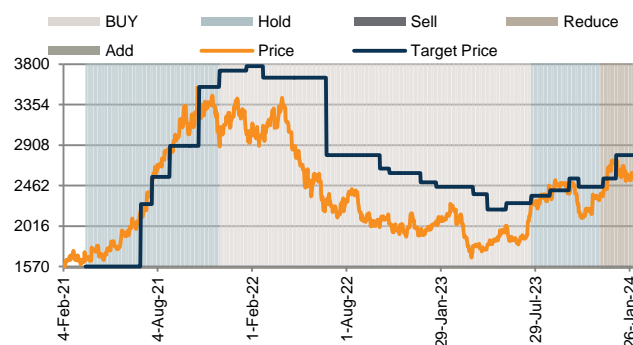
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## RECOMMENDATION HISTORY - DETAILS

Date	Closing Price (INR)	TP (INR)	Rating	Analyst
31-Dec-23	2,740	2,800	Reduce	Dipeshkumar Mehta
06-Dec-23	2,384	2,540	Reduce	Dipeshkumar Mehta
30-Nov-23	2,355	2,450	Reduce	Dipeshkumar Mehta
20-Oct-23	2,170	2,450	Hold	Dipeshkumar Mehta
02-Oct-23	2,377	2,540	Hold	Dipeshkumar Mehta
26-Aug-23	2,392	2,410	Hold	Dipeshkumar Mehta
21-Jul-23	2,331	2,350	Hold	Dipeshkumar Mehta
02-Jul-23	1,895	2,270	Buy	Dipeshkumar Mehta
03-Jun-23	2,018	2,270	Buy	Dipeshkumar Mehta
28-Apr-23	1,814	2,200	Buy	Dipeshkumar Mehta
01-Apr-23	1,796	2,370	Buy	Dipeshkumar Mehta
20-Jan-23	2,025	2,450	Buy	Dipeshkumar Mehta
02-Jan-23	1,969	2,500	Buy	Dipeshkumar Mehta
21-Dec-22	1,959	2,500	Buy	Dipeshkumar Mehta
22-Oct-22	2,043	2,600	Buy	Dipeshkumar Mehta
04-Oct-22	2,068	2,650	Buy	Dipeshkumar Mehta
23-Aug-22	2,265	2,800	Buy	Dipeshkumar Mehta
22-Jul-22	2,276	2,800	Buy	Dipeshkumar Mehta
23-Jun-22	2,311	2,800	Buy	Dipeshkumar Mehta
29-Apr-22	2,843	3,650	Buy	Dipeshkumar Mehta
01-Apr-22	3,344	3,650	Buy	Dipeshkumar Mehta
22-Feb-22	3,122	3,650	Buy	Dipeshkumar Mehta
21-Jan-22	3,025	3,780	Buy	Dipeshkumar Mehta
01-Jan-22	3,397	3,730	Buy	Dipeshkumar Mehta
30-Nov-21	2,895	3,730	Buy	Dipeshkumar Mehta
22-Oct-21	3,255	3,550	Hold	Dipeshkumar Mehta
02-Oct-21	3,026	2,900	Hold	Dipeshkumar Mehta
22-Sep-21	3,251	2,900	Hold	Dipeshkumar Mehta
27-Aug-21	2,895	2,900	Hold	Dipeshkumar Mehta
24-Jul-21	2,530	2,560	Hold	Dipeshkumar Mehta
02-Jul-21	2,155	2,260	Hold	Dipeshkumar Mehta
14-May-21	1,789	1,570	Hold	Dipeshkumar Mehta
26-Apr-21	1,724	1,570	Hold	Dipeshkumar Mehta
05-Apr-21	1,755	1,570	Hold	Dipeshkumar Mehta
18-Mar-21	1,638	1,570	Hold	Dipeshkumar Mehta

Source: Company, Emkay Research

## RECOMMENDATION HISTORY - TREND



Source: Company, Bloomberg, Emkay Research

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<b>SELL</b>	<15% downside

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