

MindTree Ltd

HOLD
CMP Rs639
TP Rs650

28 Apr 2010

Good quarter, profitability to hit ahead

MindTree reported good growth of 5.7%QoQ in dollar revenue. Higher other income (forex gain) led to report higher than consensus PAT of Rs545mn and EPS of Rs13.4. The outlook for the IT services is robust but investments in NIW business will affect the profitability in FY11.

Growth led by realisation increase but margin decline

Revenue grew 3.8%QoQ to Rs3,444mn (PINCe Rs3445mn, consensus est. Rs3,361mn) largely led by improvement in realisation (6.5%QoQ offshore and 4%QoQ onsite). IT Services grew strongly by 8.2%QoQ to Rs1,835mn but Product Engineering Services declined 0.8%QoQ to Rs1,608mn. EBITDA margin declined ~150bpsQoQ to 18.4% due to currency appreciation, change in leave policy and investments in business. Forex gain was Rs165mn vs. Rs174mn in Q3.

BFSI and travel, ADM and IMS outperform

BFSI grew 15.7%QoQ and travel & transportation grew strongly by 20.1%QoQ; these two verticals will be primary growth drivers in FY11. Manufacturing grew 9.3%QoQ but it is expected to show modest growth. Application development, PI and IMS grew 7.6%, 20.9% and 17.2%QoQ, respectively.

Increased investments in NIW business

MindTree plans to invest USD10-11mn in H1FY11 into product development of mobile phones to cater to the India and the US market. The product is expected to be launched in H2FY11.

Outlook and recommendation

The growth in IT and R&D services is likely to be robust due to improvement in the discretionary IT spending ahead. But there will be pressure on margins due to investments in NIW business. Also, the product launch of high-end smartphone may delay or not result in expected outcome in a highly competitive market. From the date of initiating the coverage, the stock has risen 21% but incrementally the earnings are not likely to upgrade due to investments in NIW business and wage inflation higher than the industry average, which will put pressure on margins. We downgrade the rating from 'BUY' to 'HOLD' with a target price of Rs650 based on target PER multiple of 12x FY12E.

KEY FINANCIALS (Rs mn)

	FY08	FY09	FY10	FY11E	FY12E
Net Sales	7,398	12,375	12,960	15,188	18,806
YoY Gr. (%)	25.3%	67.3%	4.7%	17.2%	23.8%
Op. Profit	1,254	3,309	2,456	2,560	3,087
Op. Marg. (%)	16.9%	26.7%	18.9%	16.9%	16.4%
Adj. Net Profit	1,033	523	2,149	1,917	2,215
YoY Gr. (%)	14.7%	-49.4%	310.8%	-10.8%	15.5%

KEY RATIOS

Dil. EPS (Rs)	26.5	13.7	52.8	47.1	54.4
ROCE (%)	14.4	37.9	26.8	20.6	19.8
RoE (%)	19.4	9.5	32.0	22.1	20.4
PER (x)	23.3	46.2	11.7	13.1	11.3
EV/ Net Sales (x)	3.6	2.3	2.0	1.7	1.4
EV/EBDITA (x)	21.5	8.7	10.6	10.2	8.4

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QUARTERLY SNAPSHOT (Rs mn)

	Quarter Ended		
	Sep-09	Dec-09	Mar-10
Net sales	3,150	3,318	3,444
YoY Gr. (%)	23.7	-21.5	1.9
Op. Profit	659	657	632
OPM (%)	20.9	19.8	18.4
Adj. Net Profit	499	538	545
YoY Gr. (%)	35.8	487.3	162.5

STOCK DATA

Market cap	Rs26,006mn
Book Value per share	Rs165
Shares O/S	40.7mn
Free Float	42%
Avg Trade Value (6 months)	Rs85mn
52 week High/Low	730/236
Bloomberg Code	MTCL IN
Reuters Code	MINT.BO

PERFORMANCE (%)

	1M	3M	12M
Absolute	4.2	12.7	109.8
Relative	5.8	5.7	37.7

RELATIVE PERFORMANCE

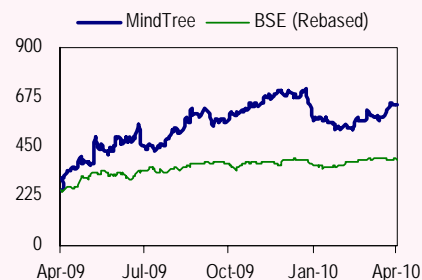


Exhibit 1 - Quarterly performance

	Q4FY09	Q3FY10	Consensus	Q4FY10(PINC EST)	Q4FY10	QoQ	YoY	Variance(PINC VS ACTUAL)
<i>Rs mn except EPS</i>								
Revenue (USDmn)	63.3	70.4	-	74.7	74.5	5.8%	17.7%	-0.3%
Revenue	3,381	3,318	3,361	3,445	3,444	3.8%	1.9%	0.0%
EBITDA	865	657	665	673	632	-3.8%	-26.9%	-6.0%
EBITDA Margin	25.6%	19.8%	19.8%	19.5%	18.4%	-144 bps	-722 bps	-117 bps
Pre Tax Income	179	691	550	513	665	-3.8%	270.3%	29.5%
Tax	-28	153	64	81	120	-21.7%	-527.2%	47.4%
Tax Rate	-16%	22%	12%	16%	18%	-412 bps	3359 bps	218 bps
PAT	184	538	486	432	545	1.3%	196.1%	26.2%
EPS	4.8	13.3	12.9	10.6	13.4	1.1%	177.9%	25.9%

Source: PINC Research, Company

Exhibit 2 - Significant improvement in realisation (6.6%QoQ) and flattish volumes

	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
<i>Effort - Service</i>					
- Onsite	285,755	293,906	305,207	3.8%	6.8%
- offshore	2,086,950	2,415,428	2,380,025	-1.5%	14.0%
Total	2,372,705	2,709,334	2,685,232	-0.9%	13.2%
<i>Fee revenue (USDmn)</i>					
- Onsite	18	19	20.4	8.0%	12.7%
- offshore	45	50	52.3	4.8%	15.7%
Total	65.7	68.9	72.8	5.7%	10.8%
<i>Pricing</i>					
Onsite	63.5	64.4	67.0	4.0%	5.5%
Offshore	21.7	20.7	22.0	6.4%	1.5%
Total	27.7	25.4	27.1	6.6%	-2.1%

Source: PINC Research, Company

Exhibit 3 - Segmental performance – IT Services shown strong growth

	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
<i>Revenue (Rs mn)</i>					
PE Services	1,409.1	1,621.7	1,608	-0.8%	14.1%
IT Services	1,972	1,697	1,836	8.2%	-6.9%
<i>Operating Income</i>					
PE Services	425	384	283	-26.4%	-33.5%
IT Services	452	245	312	27.6%	-30.9%
<i>Operating Margin</i>					
PE Services	30.2%	23.7%	17.6%	-611 bps	-1259 bps
IT Services	22.9%	14.4%	17.0%	259 bps	-590 bps
<i>Contribution to revenue</i>					
PE Services	41.7%	48.9%	46.7%	-217 bps	502 bps
IT Services	58.3%	51.1%	53.3%	217 bps	-502 bps

Source: PINC Research, Company

Onsite realisation increased 4%QoQ and offshore realisation increased 6.4%QoQ...

Volume declined due to lower working days (61 in Q4 compared to 63 in Q3)...

PE Services declined 0.8%QoQ and IT Services has shown robust growth of 8.2%QoQ...

Operating margin improved by 260bps in IT services but declined 600bpsQoQ for PE Services...

Exhibit 4 - Growth from all geographies

By Geography	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
North America	43.4	45.3	46.8	3.2%	7.7%
Europe	10.0	13.0	13.9	7.5%	39.3%
India	5.1	4.5	4.7	4.2%	-7.3%
Rest of World	4.8	7.6	9.1	19.5%	88.9%
Total	63.3	70.4	74.5	5.8%	17.7%

US grew 3.2%QoQ and Europe grew 7.5%QoQ...

as % of Total

US	68.6%	64.4%	62.8%	-160 bps	-580 bps
Europe	15.8%	18.4%	18.7%	30 bps	290 bps
India	8.0%	6.4%	6.3%	-10 bps	-170 bps
Rest of World	7.6%	10.8%	12.2%	140 bps	460 bps

Source: PINC Research, Company

Exhibit 5 - Discretionary spend picking up – ADM and PI outperform

By Service Offerings	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
Development	29.4	36.5	39.3	7.6%	33.4%
Maintenance	15.2	14.6	14.1	-3.9%	-7.3%
Consulting	2.3	1.8	1.9	5.8%	-20.5%
Package Implementation	2.2	3.0	3.6	20.9%	61.4%
Independent Testing	12.0	12.0	12.7	5.8%	5.3%
Infrastructure Management & Tech Support	2.1	2.6	3.1	17.2%	46.2%
Total	63.3	70.4	74.5	5.8%	17.7%

Application development grew strongly by 7.6%QoQ and package implementation grew 20.9% on a small base, signaling uptick in discretionary spending...

as % of Total

Development	46.5%	51.8%	52.7%	90 bps	620 bps
Maintenance	24.0%	20.8%	18.9%	-190 bps	-510 bps
Consulting	3.7%	2.5%	2.5%	0 bps	-120 bps
Package Implementation	3.5%	4.2%	4.8%	60 bps	130 bps
Independent Testing	19.0%	17.0%	17.0%	0 bps	-200 bps
Infrastructure Management & Tech Support	3.3%	3.7%	4.1%	40 bps	80 bps

Source: PINC Research, Company

Exhibit 6 - Sharp increase in FPP revenue

Revenue by Project Type	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
Fixed Price	10.6	17.4	23.2	33.7%	118.5%
Time & Material	52.7	53.0	51.3	-3.3%	-2.7%
Total	63.3	70.4	74.5	5.8%	17.7%

A few projects won in Q4 and project ramp ups happened in FPP, leading to overall 650bps increase in FPP revenue...

% of Total Revenue

Fixed Price	16.8%	24.7%	31.2%	650 bps	1440 bps
Time & Material	83.2%	75.3%	68.8%	-650 bps	-1440 bps

Source: PINC Research, Company

Exhibit 7 - BFSI and Travel lead the pack

By Industry	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
Manufacturing	14.6	8.5	9.3	9.3%	-36.3%
BFSI	15.1	11.3	13.0	15.7%	-13.8%
Travel and Transportation	12.2	8.9	10.7	20.1%	-12.4%
R&D Services (RDS)	0.0	10.1	10.7	5.8%	-
Software Product Engineering (SPE)	0.0	19.6	19.4	-0.7%	-
MindTree Wireless Products	0.0	4.7	4.6	-2.1%	-
Others	0.0	7.3	6.7	-8.4%	-
Total	63.3	70.4	74.5	5.8%	17.7%

BFSI and travel will continue to perform good in FY11

R&D Services will pick up in H2FY11...

as % of Total	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
Manufacturing	23.1%	12.1%	12.5%	40 bps	-1060 bps
BFSI	23.9%	16.0%	17.5%	150 bps	-640 bps
Travel and Transportation	19.2%	12.6%	14.3%	170 bps	-490 bps
R&D Services (RDS)	0.0%	14.4%	14.4%	0 bps	1440 bps
Software Product Engineering (SPE)	0.0%	27.8%	26.1%	-170 bps	2610 bps
MindTree Wireless Products	0.0%	6.7%	6.2%	-50 bps	620 bps
Others	0.0%	10.4%	9.0%	-140 bps	900 bps

Source: PINC Research, Company

Exhibit 8 - Ex-10 clients grew better than top 10 clients

Client Concentration	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
US\$ 1mn +	64	58	60	3.4%	-6.3%
US\$ 5mn +	13	13	13	0.0%	0.0%
US\$ 10mn +	3	5	5	0.0%	66.7%
Fortune 500 accounts	37	40	40	0.0%	8.1%
New client added	22	35	27	-22.9%	22.7%
Repeat Business	99.2%	98.2%	99.1%	-2150 bps	-1930 bps
DSO	70	65	68		

27 new clients added in the quarter...

USD mn	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
Top client	4.2	5.1	5.4	5.8%	26.4%
Top 5 clients	15.6	20.0	20.8	3.9%	33.4%
Top 10 clients	23.6	28.5	29.8	4.5%	26.5%
Non Top 10	39.8	41.9	44.7	6.7%	12.4%
Total	63.3	70.4	74.5	5.8%	17.7%
Top client	6.7%	7.2%	7.2%	0 bps	50 bps
Top 5 clients	24.6%	28.4%	27.9%	-50 bps	330 bps
Top 10 clients	37.2%	40.5%	40.0%	-50 bps	280 bps

Source: PINC Research, Company

Exhibit 9 - Improved net addition but attrition increased sharply

Employee metrics	Q4FY09	Q3FY10	Q4FY10	QoQ	YoY
Total employees	7,866	8,127	8,297	2.1%	5.5%
Software Professionals	7,281	7,460	7,651	2.6%	5.1%
Sales & support	585	667	646	-3.1%	10.4%
Gross addition	539	462	668	44.6%	23.9%
Net addition	217	41	170	314.6%	-21.7%
Utilisation					
Including trainees	65.3%	71.4%	71.4%	0.0	610.0
Excluding trainees	67.1%	72.9%	72.6%	-30.0	550.0
Attrition	13.7%	10.7%	14.1%	31.8%	2.9%

Source: PINC Research, Company

TTM attrition has shot up sharply to 14.1% from 10.7% in Q3...

Utilisation remained stable...

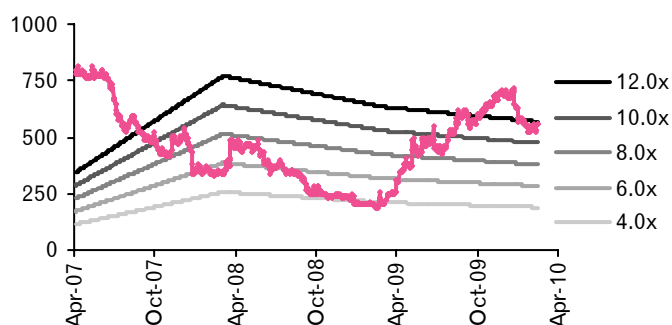
Income Statement					
Year end 31 Mar (Rs mn)	FY08	FY09	FY10	FY11E	FY12E
Net sales	7,398	12,375	12,960	15,188	18,806
<i>growth (%)</i>	25.3	67.3	4.7	17.2	23.8
Gross profit	2,673	5,407	4,977	5,579	6,742
Other operating charges	1,419	2,097	2,522	3,019	3,656
EBITDA	1,254	3,309	2,456	2,560	3,087
<i>growth (%)</i>	14.4	163.9	-25.8	4.2	20.6
Depreciation	356	570	652	778	936
Other income	238	(1,974)	770	200	350
EBIT	1,177	766	2,574	2,282	2,701
Interest paid	59	162	27	0	0
Pre-tax profit (before E/o items)	1,118	604	2,547	2,282	2,701
Tax Provision	85	67	398	365	486
E/o loss / (Income)	0	41	0	0	0
Net profit	1,033	537	2,149	1,917	2,215
Adjusted net profit	1,033	523	2,149	1,917	2,215
<i>growth (%)</i>	14.7	-49.4	310.8	-10.8	15.5
Diluted EPS (Rs)	26.5	13.7	52.8	47.1	54.4
<i>Diluted EPS Growth (%)</i>	-4.3	-48.3	285.3	-10.8	15.5

Cash Flow Statement					
Year end 31 Mar (Rs mn)	FY08	FY09	FY10	FY11E	FY12E
Pre-tax profit	1,118	604	2,547	2,282	2,701
Depreciation	356	570	652	778	936
Total tax paid	(188)	(287)	(685)	(365)	(486)
Chg in working capital	(252)	(668)	892	(1,089)	(727)
Other operating activities	(122)	1,579	(1,134)	(200)	(350)
Cash flow from operations (a)	912	1,798	2,273	1,406	2,074
Capital expenditure	(2,176)	(369)	(473)	(1,337)	(1,316)
Chg in investments	845	1,003	(248)	0	0
Other investing activities	(170)	(2,857)	(242)	200	350
Cash flow from investing (b)	(1,501)	(2,224)	(964)	(1,137)	(966)
Free cash flow (a+b)	(588)	(426)	1,309	269	1,107
Equity raised/(repaid)	(119)	6	94	0	0
Debt raised/(repaid)	662	507	(1,363)	(31)	0
Change in Minorities Interest	(23)	(38)	0	0	0
Dividend (incl. tax)	(88)	(90)	(46)	(118)	(118)
Other financing activities	(59)	(159)	(27)	0	0
Cash flow from financing (c)	373	226	(1,342)	(148)	(118)
Net chg in cash (a+b+c)	(215)	(200)	(33)	120	990

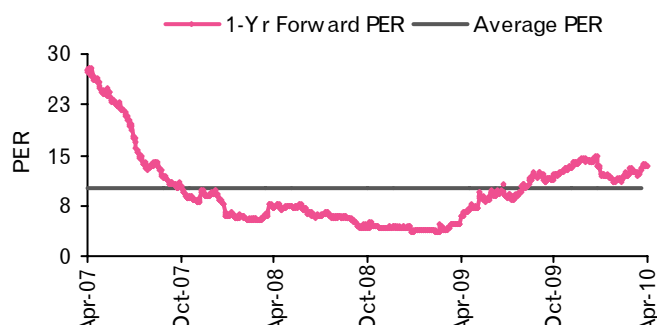
Balance Sheet					
Year end 31 Mar (Rs mn)	FY08	FY09	FY10	FY11E	FY12E
Equity Share capital	379	380	395	395	395
Reserves & surplus	4,952	5,133	6,311	8,265	10,480
Shareholders' funds	5,331	5,513	6,706	8,660	10,875
Minorities interests	0	328	0	0	0
Total Debt	919	1,394	31	0	0
Capital Employed	6,250	7,234	6,737	8,660	10,875
Net fixed assets	2,840	4,422	3,013	3,629	4,082
Net Current Assets (excl Cash & Cash eq.)	1,373	1,121	1,715	2,746	3,400
Cash & Cash Eq.	553	488	523	799	1,906
Investments	1,395	1,013	1,272	1,272	1,272
Net Deferred Tax Assets	90	190	214	214	214
Total assets	6,250	7,234	6,737	8,660	10,875

Key ratios					
Year end 31 Mar (Rs mn)	FY08	FY09	FY10	FY11E	FY12E
OPM (%)	16.9	26.7	18.9	16.9	16.4
Net margin (%)	14.0	4.2	16.6	12.6	11.8
Yield (%)	0.4	0.4	0.5	0.5	0.5
Net debt/Equity (x)	17.2	23.6	0.0	0.0	0.0
Net Working Capital (days)	79	37	55	73	73
Asset turnover (x)	0.3	0.3	0.3	0.2	0.2
ROCE (%)	14.4	37.9	26.8	20.6	19.8
RoE (%)	19.4	9.5	32.0	22.1	20.4
EV/Net sales (x)	3.6	2.3	2.0	1.7	1.4
EV/EBITDA (x)	21.5	8.7	10.6	10.2	8.4
PER (x)	23.3	46.2	11.7	13.1	11.3
Price/Book (x)	4.7	4.4	3.9	3.0	2.4

P/E Band



1-year fwd PER



T E A M

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PINC bright thinking

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