

India

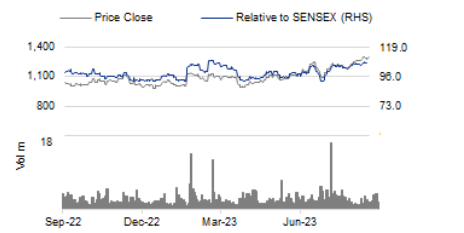
ADD (no change)

Consensus ratings*: Buy 15 Hold 13 Sell 15

| | |
|------------------------------|-----------------------------|
| Current price: | Rs1,305 |
| Target price: ▲ | Rs1,515 |
| Previous target: | Rs1,216 |
| Up/downside: | 16.1% |
| InCred Research / Consensus: | 34.8% |
| Reuters: | TEML.NS |
| Bloomberg: | TECHM IN |
| Market cap: | US\$15,345m Rs1,272,642m |
| Average daily turnover: | US\$36.1m Rs2997.4m |
| Current shares o/s: | 885.5m |
| Free float: | 64.0% |
| *Source: Bloomberg | |

Key changes in this note

- Introduce FY26F estimates.



Source: Bloomberg

| Price performance | 1M | 3M | 12M |
|-------------------|-----|------|------|
| Absolute (%) | 8.7 | 17.0 | 28.3 |
| Relative (%) | 6.8 | 11.6 | 12.9 |

| Major shareholders | % held |
|--------------------------------|--------|
| LIC | 9.5 |
| SBI-ETF Nifty 50 | 3.9 |
| ICICI Prudential Bluechip Fund | 1.8 |

Analyst(s)



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Tech Mahindra

The seeds are being sown...

- We expect a three-year journey with system & process maturity as key pillars.
- We adjust our estimates, introduce FY26F and increase the TP to Rs1,515.
- Customer attrition-led revenue decline could be a key risk to our thesis.

Restructuring may lead to earnings upgrade, P/E multiple expansion

In this report, we present the potential earnings scenarios from the ongoing leadership restructuring at Tech Mahindra. While the contours are not yet known, we believe historical anecdotes from Infosys and Wipro could provide the same. Further, MD & CEO Mr. Mohit Joshi could also lean on his first-hand experience of the restructuring at Infosys in 2018. We had turned constructive in Mar 2023 after Mr. Joshi's appointment & continue to believe that investors should not miss the potential earnings upgrade and P/E rerating cycle.

Generally, the blue print involves three stages

Previous restructuring at scale organizations suggests a potential three-year journey (of years 1/2/3) involving stabilization, consolidation & growth. Infosys, in its 2018 analyst meet, articulated FY19 being a year of stability, building momentum in FY20 & acceleration in FY21. News flow around leadership transition suggests that year-1 is likely underway.

What could be the broad contours of this restructuring?

Analyzing the past Analyst Day literature suggests the broad contours could hinge on key pillars such as 1) leadership, 2) structure, 3) top accounts, 4) large deals, 5) pipeline, 6) solutions/delivery, and 7) go-to-market (GTM), etc. Alongside, investments in systems and process maturity could be key to capturing and driving revenue growth and efficiency.

Customer attrition could decide the worst-case growth trajectory

Current restructuring may lead to potential revenue leakage given customer & leadership attrition. The scenarios to factor in the same assume a range of a 7% to 3% yoy fall in FY24F US\$ revenue, -3% to +3% in FY25F and 1% to 5% growth in FY26F (refer Fig. 3).

Jigsaw pieces are likely falling in place

Hiring of sales & support staff and a partial wage hike to junior staff in 1QFY24 suggests that the employee pyramid course correction and retention is underway. This, coupled with the centralized resource management, could help improve revenue and cost productivity while investments in capabilities and solutioning could improve go-to-market positioning.

Adjust our estimates & increase TP to Rs1,515; retain ADD rating

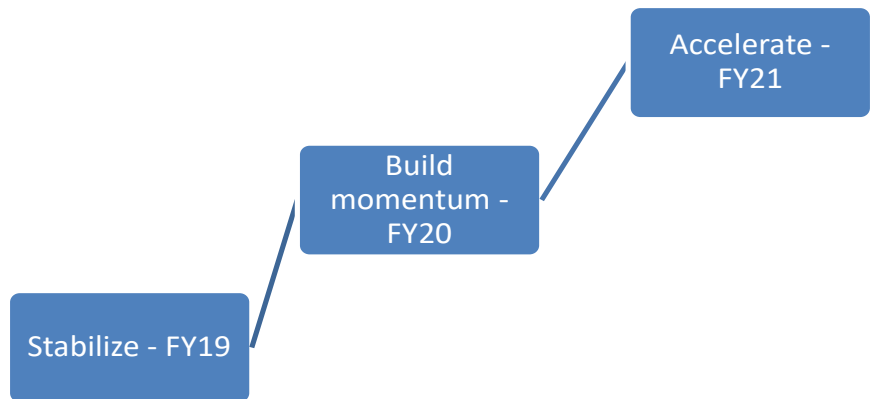
We adjust our estimates, introduce FY26F and shift valuations to FY26F as the FY24F low base distorts EPS CAGR. We now model a 4% US\$ revenue CAGR over FY24F-26F & ~30% PAT (Rs.) CAGR. We apply 1x PE/G to FY26F EPS growth (1.2x FY23-FY25F EPS CAGR) to arrive at our target multiple. The higher discount is to account for a longer time horizon. Retain ADD rating with a higher target price of Rs1,515. Downside risk: Weak revenue/EBIT margin execution led by customer and senior leadership attrition.

Financial Summary

| | Mar-22A | Mar-23A | Mar-24F | Mar-25F | Mar-26F |
|-----------------------------------|---------|---------|----------|----------|---------|
| Revenue (Rsm) | 446,460 | 532,902 | 529,426 | 553,185 | 594,787 |
| Operating EBITDA (Rsm) | 80,201 | 80,287 | 68,699 | 91,276 | 107,062 |
| Net Profit (Rsm) | 55,662 | 48,312 | 40,704 | 57,319 | 68,538 |
| Core EPS (Rs) | 63.0 | 57.2 | 46.0 | 64.7 | 77.4 |
| Core EPS Growth | 23.4% | (9.2%) | (19.7%) | 40.8% | 19.6% |
| FD Core P/E (x) | 20.71 | 23.92 | 28.40 | 20.17 | 16.86 |
| DPS (Rs) | 45.0 | 50.0 | 55.0 | 51.8 | 61.9 |
| Dividend Yield | 3.43% | 3.82% | 4.21% | 3.97% | 4.74% |
| EV/EBITDA (x) | 13.68 | 13.87 | 16.20 | 11.97 | 10.03 |
| P/FCFE (x) | 26.65 | 39.06 | 28.21 | 20.22 | 18.13 |
| Net Gearing | (22.3%) | (16.4%) | (17.3%) | (23.7%) | (28.9%) |
| P/BV (x) | 4.30 | 4.14 | 4.26 | 4.09 | 3.90 |
| ROE | 21.5% | 18.5% | 14.8% | 20.7% | 23.7% |
| % Change In Core EPS Estimates | | | (33.41%) | (11.88%) | |
| InCred Research/Consensus EPS (x) | | | | | |

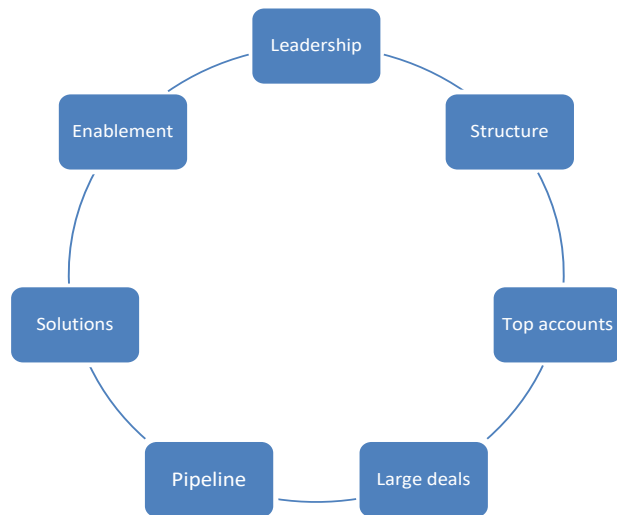
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 1: Infosys had set a three-year roadmap to achieve its restructuring objectives



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Key pillars on which the contours of restructuring could best hinge on



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 3: Growth and EBIT margin scenarios

| Vertical growth assumptions | Bear | | | Base | | | Bull | | |
|-----------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| | FY24F | FY25F | FY26F | FY24F | FY25F | FY26F | FY24F | FY25F | FY26F |
| CME | -12.6% | -5.0% | 0.0% | -10.7% | 0.0% | 3.0% | -8.8% | 1.0% | 3.0% |
| Enterprise | -3.2% | -1.8% | 1.6% | -1.1% | 0.0% | 3.0% | 0.9% | 4.2% | 6.2% |
| Overall revenue | -7.0% | -3.0% | 1.0% | -5.0% | 0.0% | 3.0% | -3.0% | 3.0% | 5.0% |
| Revenue (US\$ m) | 6,146 | 5,962 | 6,022 | 6,278 | 6,278 | 6,466 | 6,407 | 6,599 | 6,931 |
| EBIT margin | 8.0% | 11.0% | 13.0% | 9.0% | 12.5% | 14.0% | 10.0% | 14.0% | 15.0% |
| PAT (Rs m) | 33,039 | 44,233 | 53,618 | 37,741 | 52,496 | 62,008 | 42,330 | 61,428 | 70,785 |
| EPS (Rs) | 37.3 | 50.0 | 60.6 | 42.6 | 59.3 | 70.0 | 47.8 | 69.4 | 79.9 |

SOURCE: COMPANY REPORTS, INCRED RESEARCH

Figure 4: Revenue productivity trend

| Revenue per average employee (US\$) | FY18 | FY19 | FY20 | FY21 | FY22 | FY23 |
|-------------------------------------|--------|--------|--------|--------|--------|--------|
| TCS | 48,807 | 51,052 | 50,489 | 47,324 | 47,568 | 46,275 |
| Infosys | 54,090 | 54,596 | 54,330 | 54,033 | 56,866 | 55,419 |
| Wipro | 48,526 | 49,014 | 46,604 | 42,757 | 46,983 | 44,786 |
| HCL Technologies | 66,406 | 66,906 | 68,907 | 63,711 | 60,769 | 57,890 |
| Tech Mahindra | 41,394 | 42,504 | 42,075 | 41,506 | 44,065 | 43,525 |
| LTI | 50,144 | 51,583 | 51,156 | 49,534 | 50,886 | 50,030 |
| Mindtree | 49,533 | 52,807 | 51,607 | 47,004 | 47,917 | NA |

SOURCE: INCRED RESEARCH, COMPANY REPORTS

NOTE: DATA FOR LTI IN FY23 IS OF THE MERGED ENTITY – LTIMINDTREE

Figure 5: Moderation in sub-contractor expenses could be a key tailwind

| Sub-contractor costs as a % of revenue | FY19 | FY20 | FY21 | FY22 | FY23 |
|--|-------|-------|-------|-------|-------|
| TCS | 7.7% | 8.2% | 8.0% | 9.1% | 9.5% |
| Infosys | 7.3% | 7.4% | 7.0% | 10.4% | 9.6% |
| Wipro | 16.2% | 14.8% | 13.5% | 13.7% | 12.8% |
| HCL Technologies | 16.2% | 15.1% | 13.5% | 14.6% | 14.7% |
| Tech Mahindra | 12.5% | 14.8% | 13.1% | 15.6% | 15.0% |
| LTI | 7.7% | 8.3% | 7.6% | 8.4% | 8.5% |
| Mindtree | 7.5% | 8.0% | 7.2% | 10.2% | NA |

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 6: EBIT margin trend

| EBIT Margin | FY19 | FY20 | FY21 | FY22 | FY23 |
|------------------|-------|-------|-------|-------|-------|
| TCS | 25.6% | 24.6% | 25.1% | 25.3% | 24.1% |
| Infosys | 22.8% | 21.3% | 24.5% | 23.0% | 21.1% |
| Wipro | 17.9% | 18.1% | 20.3% | 17.7% | 15.7% |
| HCL Technologies | 19.6% | 19.6% | 21.4% | 18.9% | 18.2% |
| Tech Mahindra | 15.0% | 11.6% | 14.2% | 14.6% | 10.9% |
| LTIM | NA | NA | NA | 17.8% | 16.2% |

SOURCE: COMPANY REPORTS, INCRED RESEARCH

Figure 7: Scope to improve client productivity exists

| Client metric - 1QFY24 | TCS | Infosys | Wipro | HCLT | TechM |
|---|-----|---------|-------|------|-------|
| US\$10m+ clients | 468 | 312 | 207 | 237 | 115 |
| US\$50m+ clients | 137 | 79 | 51 | 48 | 26 |
| Revenue per active client on TTM basis - US\$ m | NA | 10.0 | 7.8 | NA | 5.1 |
| Revenue per top 5 clients on TTM basis - US\$ m | NA | 479 | 289 | 261 | 232 |
| Revenue per top 6-10 clients on TTM basis - US\$ m | NA | 267 | 177 | 198 | 126 |
| Revenue per top 11-20 clients on TTM basis - US\$ m | NA | NA | NA | 128 | 83 |

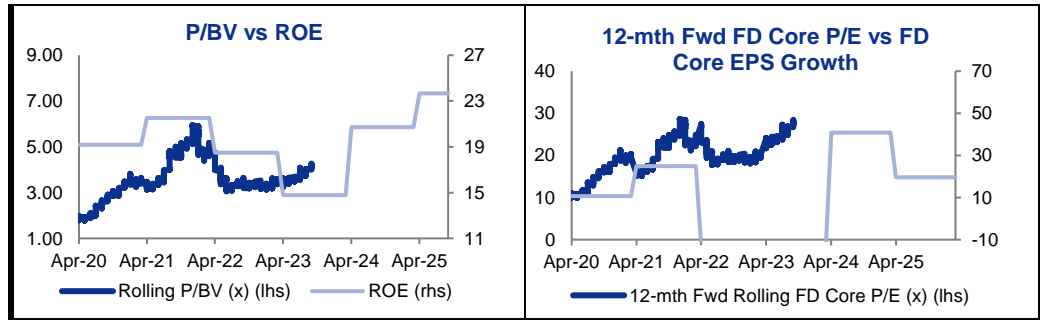
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 8: Valuation scenarios

| | Bear | Base | Bull |
|---------------------------|--------|-------|-------|
| PE/G | 0.90 | 1.10 | 1.35 |
| Multiple (x) | 19.1 | 19.9 | 20.6 |
| CMP (Rs) | 1,305 | 1,305 | 1,305 |
| EPS (Rs) | 60.6 | 70.0 | 79.9 |
| Target price (Rs) | 1,156 | 1,396 | 1,646 |
| Potential upside/downside | -11.5% | 6.9% | 26.1% |

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS



Profit & Loss

| (Rs mn) | Mar-22A | Mar-23A | Mar-24F | Mar-25F | Mar-26F |
|---|----------------|----------------|----------------|----------------|----------------|
| Total Net Revenues | 446,460 | 532,902 | 529,426 | 553,185 | 594,787 |
| Gross Profit | 136,741 | 151,705 | 141,159 | 160,424 | 175,462 |
| Operating EBITDA | 80,201 | 80,287 | 68,699 | 91,276 | 107,062 |
| Depreciation And Amortisation | (15,204) | (19,567) | (18,191) | (19,361) | (20,818) |
| Operating EBIT | 64,997 | 60,720 | 50,508 | 71,914 | 86,244 |
| Financial Income/(Expense) | 3,855 | 3,404 | 2,459 | 2,957 | 3,480 |
| Pretax Income/(Loss) from Assoc. | | | | | |
| Non-Operating Income/(Expense) | 5,642 | 2,990 | 1,837 | 1,936 | 2,082 |
| Profit Before Tax (pre-EI) | 74,494 | 67,114 | 54,804 | 76,807 | 91,805 |
| Exceptional Items | | | | | |
| Pre-tax Profit | 74,494 | 67,114 | 54,804 | 76,807 | 91,805 |
| Taxation | (18,220) | (15,885) | (13,969) | (19,355) | (23,135) |
| Exceptional Income - post-tax | | (2,370) | | | |
| Profit After Tax | 56,274 | 48,859 | 40,836 | 57,451 | 68,670 |
| Minority Interests | (612) | (547) | (132) | (132) | (132) |
| Preferred Dividends | | | | | |
| FX Gain/(Loss) - post tax | | | | | |
| Other Adjustments - post-tax | | | | | |
| Net Profit | 55,662 | 48,312 | 40,704 | 57,319 | 68,538 |
| Recurring Net Profit | 55,662 | 50,682 | 40,704 | 57,319 | 68,538 |
| Fully Diluted Recurring Net Profit | 55,662 | 50,682 | 40,704 | 57,319 | 68,538 |

Cash Flow

| (Rs mn) | Mar-22A | Mar-23A | Mar-24F | Mar-25F | Mar-26F |
|----------------------------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| EBITDA | 80,201 | 80,287 | 68,699 | 91,276 | 107,062 |
| Cash Flow from Invt. & Assoc. | | | | | |
| Change In Working Capital | (14,343) | (18,451) | 262 | (1,035) | (6,448) |
| (Incr)/Decr in Total Provisions | | | | | |
| Other Non-Cash (Income)/Expense | 11,758 | 1,094 | 264 | 264 | 264 |
| Other Operating Cashflow | | | | | |
| Net Interest (Paid)/Received | (1,626) | (3,256) | (4,788) | (4,788) | (4,788) |
| Tax Paid | (23,137) | (19,931) | (13,969) | (19,355) | (23,135) |
| Cashflow From Operations | 52,853 | 39,743 | 50,469 | 66,361 | 72,954 |
| Capex | (9,584) | (10,152) | (9,500) | (9,200) | (9,200) |
| Disposals Of FAs/subsidiaries | | | | | |
| Acq. Of Subsidiaries/investments | | | | | |
| Other Investing Cashflow | 14,399 | 7,367 | 9,084 | 9,681 | 10,349 |
| Cash Flow From Investing | 4,815 | (2,785) | (416) | 481 | 1,149 |
| Debt Raised/(repaid) | | | | | |
| Proceeds From Issue Of Shares | | | | | |
| Shares Repurchased | | | | | |
| Dividends Paid | (39,808) | (42,633) | (48,705) | (45,856) | (54,831) |
| Preferred Dividends | | | | | |
| Other Financing Cashflow | (6,858) | (8,148) | (4,788) | (4,788) | (4,788) |
| Cash Flow From Financing | (46,666) | (50,781) | (53,493) | (50,644) | (59,619) |
| Total Cash Generated | 11,002 | (13,823) | (3,440) | 16,198 | 14,485 |
| Free Cashflow To Equity | 43,269 | 29,591 | 40,969 | 57,161 | 63,754 |
| Free Cashflow To Firm | 59,294 | 40,214 | 54,841 | 71,629 | 78,892 |

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

| Balance Sheet | | | | | |
|--------------------------------------|----------------|----------------|----------------|----------------|----------------|
| (Rs mn) | Mar-22A | Mar-23A | Mar-24F | Mar-25F | Mar-26F |
| Total Cash And Equivalents | 84,104 | 70,379 | 71,331 | 91,921 | 110,797 |
| Total Debtors | 119,334 | 128,816 | 127,062 | 129,998 | 139,775 |
| Inventories | 405 | 236 | 236 | 236 | 236 |
| Total Other Current Assets | 40,714 | 44,896 | 44,896 | 44,896 | 44,896 |
| Total Current Assets | 244,557 | 244,327 | 243,525 | 267,051 | 295,704 |
| Fixed Assets | 37,846 | 40,430 | 31,739 | 21,577 | 9,960 |
| Total Investments | 10,153 | 10,175 | 10,175 | 10,175 | 10,175 |
| Intangible Assets | 110,844 | 109,334 | 109,334 | 109,334 | 109,334 |
| Total Other Non-Current Assets | 45,307 | 57,267 | 57,267 | 57,267 | 57,267 |
| Total Non-current Assets | 204,150 | 217,206 | 208,515 | 198,353 | 186,736 |
| Short-term Debt | 14,397 | 14,494 | 14,494 | 14,494 | 14,494 |
| Current Portion of Long-Term Debt | | | | | |
| Total Creditors | 40,947 | 43,846 | 42,354 | 44,255 | 47,583 |
| Other Current Liabilities | 82,008 | 87,174 | 87,174 | 87,174 | 87,174 |
| Total Current Liabilities | 137,352 | 145,514 | 144,022 | 145,923 | 149,251 |
| Total Long-term Debt | 1,420 | 1,288 | 1,288 | 1,288 | 1,288 |
| Hybrid Debt - Debt Component | | | | | |
| Total Other Non-Current Liabilities | 36,124 | 30,784 | 30,784 | 30,784 | 30,784 |
| Total Non-current Liabilities | 37,544 | 32,072 | 32,072 | 32,072 | 32,072 |
| Total Provisions | | | | | |
| Total Liabilities | 174,896 | 177,586 | 176,094 | 177,995 | 181,323 |
| Shareholders Equity | 268,857 | 279,245 | 271,243 | 282,707 | 296,415 |
| Minority Interests | 4,954 | 4,702 | 4,702 | 4,702 | 4,702 |
| Total Equity | 273,811 | 283,947 | 275,945 | 287,409 | 301,117 |

| Key Ratios | | | | | |
|---------------------------|----------------|----------------|----------------|----------------|----------------|
| | Mar-22A | Mar-23A | Mar-24F | Mar-25F | Mar-26F |
| Revenue Growth | 17.9% | 19.4% | (0.7%) | 4.5% | 7.5% |
| Operating EBITDA Growth | 17.1% | 0.1% | (14.4%) | 32.9% | 17.3% |
| Operating EBITDA Margin | 18.0% | 15.1% | 13.0% | 16.5% | 18.0% |
| Net Cash Per Share (Rs) | 68.99 | 52.73 | 53.81 | 77.06 | 98.38 |
| BVPS (Rs) | 303.66 | 315.36 | 306.32 | 319.27 | 334.75 |
| Gross Interest Cover | 39.97 | 18.65 | 10.55 | 15.02 | 18.01 |
| Effective Tax Rate | 24.5% | 23.7% | 25.5% | 25.2% | 25.2% |
| Net Dividend Payout Ratio | 71.1% | 87.2% | 119.7% | 80.0% | 80.0% |
| Accounts Receivables Days | 85.70 | 84.98 | 88.20 | 84.81 | 82.78 |
| Inventory Days | 0.38 | 0.31 | 0.22 | 0.22 | 0.21 |
| Accounts Payables Days | 40.54 | 40.60 | 40.52 | 40.24 | 39.97 |
| ROIC (%) | 30.6% | 20.0% | 15.1% | 22.3% | 27.8% |
| ROCE (%) | 17.1% | 15.3% | 12.4% | 17.6% | 20.3% |
| Return On Average Assets | 12.6% | 10.7% | 8.5% | 12.0% | 13.9% |

SOURCES: INCRED RESEARCH, COMPANY REPORTS

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| served as an officer, director or employee of the subject company | NO | NO |
| been engaged in market making activity for the subject company | NO | NO |

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