

BSE IT Index v/s BSE Sensex

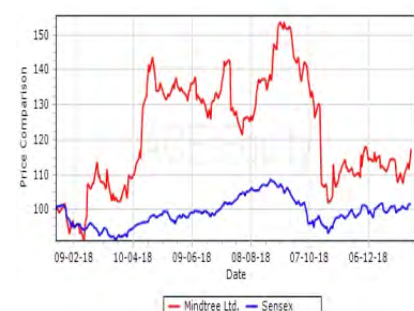


MINDTREE

Stock Performance (%)	3m	6m	12m
MINDTREE	9.4	16.5	29.3
SENSEX	4.6	0.04	3.2

Source: ACE Equity, Arihant Research

MINDTREE v/s SENSEX



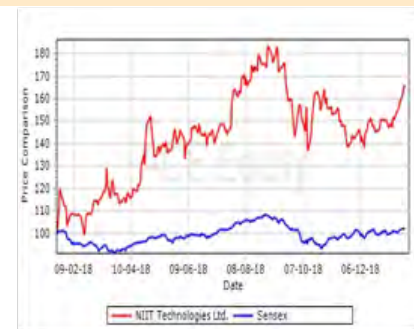
Source: ACE Equity, Arihant Research

NIIT TECHNOLOGIES

Stock Performance (%)	3m	6m	12m
NIIT TECHNOLOGIES	3.1	9.4	77.3
SENSEX	4.6	0.04	3.2

Source: ACE Equity, Arihant Research

NIIT TECHNOLOGIES v/s SENSEX

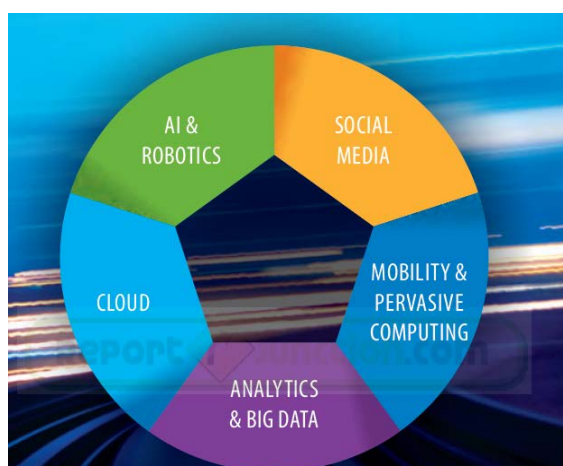


Source: ACE Equity, Arihant Research

Digital Transformation to drive growth momentum for Indian IT sector

Digital transformation involves using digital technologies to remake a process to become more efficient or effective. Digital transformation can involve many different technologies but the hottest topics are Cloud Computing, the Internet of Things, Big Data, and Artificial Intelligence. Digital technologies constitute over 20% of revenues for the Indian IT industry. With over 30% revenue growth, Digital is now the primary driver of growth. As per NASSCOM, 80% of the incremental IT spending by global companies is expected to be on the digital technologies. By the year 2025, the share of traditional technologies is expected to reduce to 40% from 80%, whereas share of digital technologies is expected to rise to 60%.

Digital Opportunity



Source: Company Annual Reports, Arihant Research

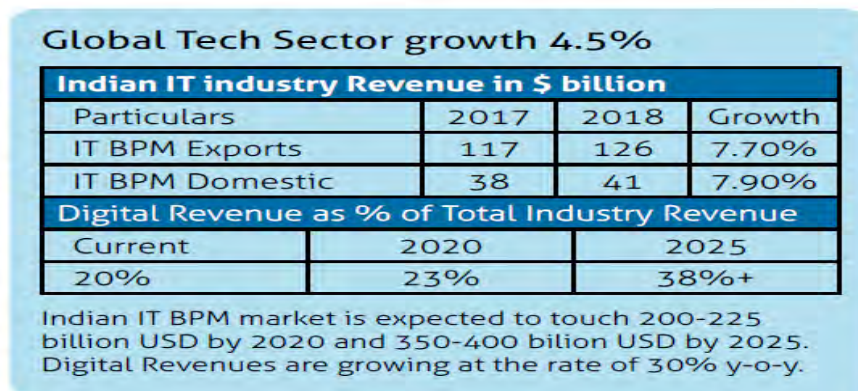
In the present report we have touched upon the key themes driving the Digital Transformation across different sectors with special focus on the IT sector. We are positive on the IT sector, which is the key beneficiary of this digital transformation and are addressing issues across their client companies on the digital platform, thereby driving the revenue momentum. We are especially positive on the Mid-Tier IT companies due to their reasonable valuation compared to their large cap peers and also due to their stupendous growth story, which is getting tailwind from this digital transformation. In this report, we covered two mid-cap IT companies, namely **Mindtree** and **NIIT Technologies**, and initiated coverage on them with 'BUY' rating.

Mindtree	NIIT Technologies
CMP : Rs 887	CMP : Rs 1225
Rating : BUY	Rating : BUY
Target : Rs 1141	Target : Rs 1570

Digital Boost to IT Sector

As per NASSCOM (National Association of Software and Services Companies), Digital revenues are growing at 30% in India (1.5 times global digital growth rate). The projects in Digital are more skill intensive than people intensive and require companies to focus on re-skilling their workforce to address these opportunities.

The digital market is well set to reach US\$ 200-225 bn by 2020 and US\$ 350-400 bn by 2025



Source: Nasscom, Arihant Research

Indian service providers face a significant opportunity as digital technologies continue to be embedded in an ever widening range of products and services. The market is well set to reach US\$ 200-225 bn by 2020 and US\$ 350-400 bn by 2025. At the same time, challenges around economic volatility, protectionism, competition, labour mobility and inertia will be the major factors to tackle by concerned stakeholders. Digital business, Blockchain, Internet of Things (IoT), AI/ML projects will be main drivers of growth going forward.

Digital Disruption

Digital technology is disrupting every aspect of people's lives and has become much more mainstream



Source: Nasscom, Arihant Research

Digital Marketing – Rising Demand

The need to offer personalized products to customers across almost all industries is another major trend that's driving demand for digital marketing software and IT services companies, that deploy these products. Whether it is retail or financial products, legacy enterprises have to figure out a way to better understand their customer's behaviour and needs, then create custom products or pricing.

Digital technology will help the cryptocurrency domain to create value of approx. US\$ 1 billion in the banking domain through blockchain

Search	Disruption	Blockchain	Trust	AI
30% Visual and Voice Search Drive Commerce Revenue	5 of 7 Digital Giants Self-Disrupt	\$1 Billion Cryptocurrency Value Created in Banking	50%+ Consuming More False Information Than True	Real or Fake? "Counterfeit Reality"

Source: Nasscom, Arihant Research

This task is achieved through various digital marketing and analytics software products, which are being offered by companies such as Adobe, SAS, IBM, Oracle, SAP and Salesforce.com.

Artificial Intelligence (AI) will help create 2.3 million new jobs by 2020 against 1.8 million redundant conventional jobs

50% Bot Development Over Mobile App Development	40% IT Versatility With People-Centric Roles	2.3M Net-New Jobs Versus 1.8M Eliminated	95% New Products Contain IoT	Half IoT Security Spend on Remediation
2021	2021	2020	2020	2022
AI	Talent	AI	IoT	Security

Source: Nasscom, Arihant Research

Digital Retail Industry

Retail digital transformation: Another industry ripe for disruption

Retail, one of the most competitive sectors, is up next for disruption. Consumers expect the latest technology and the best offers in the retail space. Everything has to be personalised, streamlined and overall, an enjoyable experience.

Key driver for the retail market will be the advantages of digital signages over traditional advertising tools



Source: Businesswire, Arihant Research

According to the Customers 2020 report, 86% of buyers will pay more for a better customer experience

Many of today's shoppers are digital natives and have high expectations for their digital experiences. On the positive side, they're increasingly showing that they're willing to pay more for a better customer experience (according to the Customers 2020 report, 86% of buyers will pay more for a better customer experience).

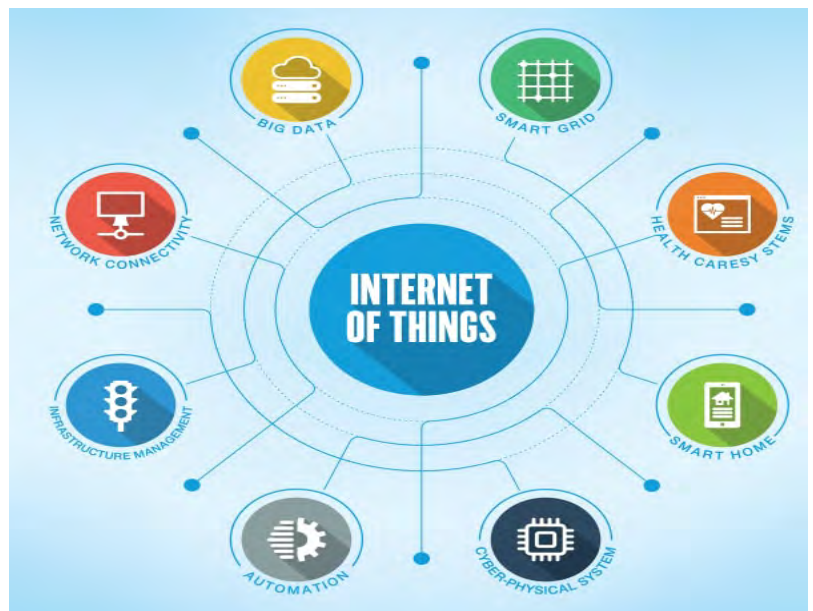
Retailers are starting to realise how important giving the customer a tailored, personalised experience is, and those who do not provide those services, will eventually lose even their most loyal customers.

Technologies to support digital transformation are the following,--

1) Use AI to Work Smarter in 2019

Rather than looking for ways to work harder, organisations are beginning to look for ways to work smarter. Using artificial intelligence is one of the best ways to develop insights and improve productivity. By deploying AI solutions organisations can utilise the data sets they accumulate and use them to refine everyday business practices. The retail industry, in particular, is embracing AI in attempt to improve their understanding of consumer preferences. It is estimated that global retailer spending on AI will reach US\$7.3 bn per year by 2022 as retailers attempt to develop their understanding of customer preferences.

It is estimated that global retailer spending on Artificial Intelligence (AI) will reach US\$ 7.3 billion per year by 2022



It is estimated that the global Internet of Things (IoT) market will be worth over US\$ 123 bn by 2021

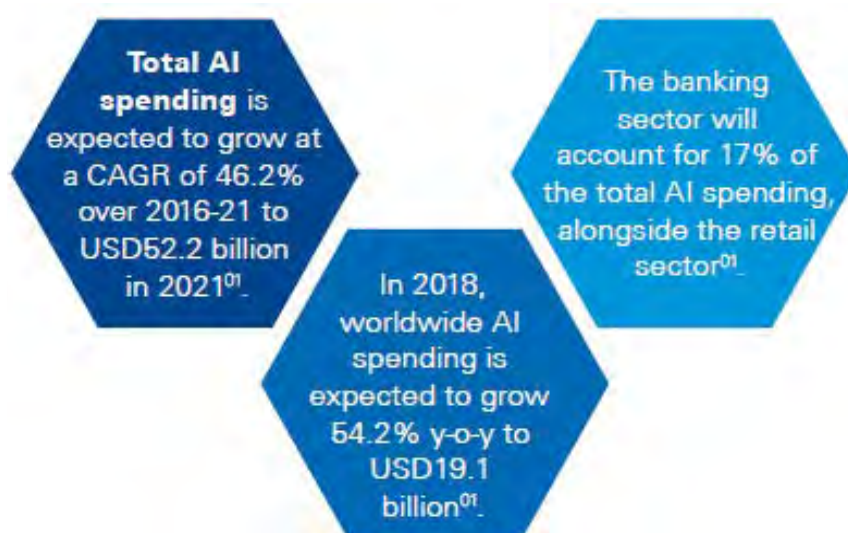
Source: Industry Reports, Arihant Research

2) Redefining local environment with IoT devices

Digital transformation is not just about changing insights. The borders between the physical world and the internet are slowly being erased as internet of things (IoT) devices continue to grow in popularity. IoT vendors will be able to connect everything from wearable devices and smart appliances to the internet for data collection. It is estimated that the global IoT market will be worth over US\$123 bn by 2021. The widespread adoption of IoT devices is slowly beginning to occur within the manufacturing industry, where goods need to be delivered from factory to consumer as fast and efficiently as possible. IoT devices are key resources for producing the data to make this possible.

Artificial Intelligence in BFSI Market

According to Nasscom reports, total Artificial Intelligence (AI) spending is expected to grow at a CAGR of 46.2% over 2016-21 to US\$ 52.2 billion in 2021. The banking sector alone (BFSI Market) will account for 17% of the total AI spending followed by retail sector.



Source: Nasscom, Arihant Research

Growth Drivers

The growth drivers for the above increased spending will be the following,---

- Exponentially growing digital data
- Rising investment in AI
- Increasing partnership between financial institutes and fintech companies
- Growing need to provide enhanced customer experience

Skilled-Labour Shortage Could Emerge as Major Issue in 2019

Next year could herald the emergence of a new thorn for the software sector -- a shortage of skilled labor. So far, this hasn't been a major issue holding back digital transformations. However, recent results from almost all services companies show rising employee attrition, which could mean slowing growth for both the software and service sectors if they don't reverse. Software companies depend on IT-services vendors to deploy their software and any labor issues in the latter could crimp product sales at the former.



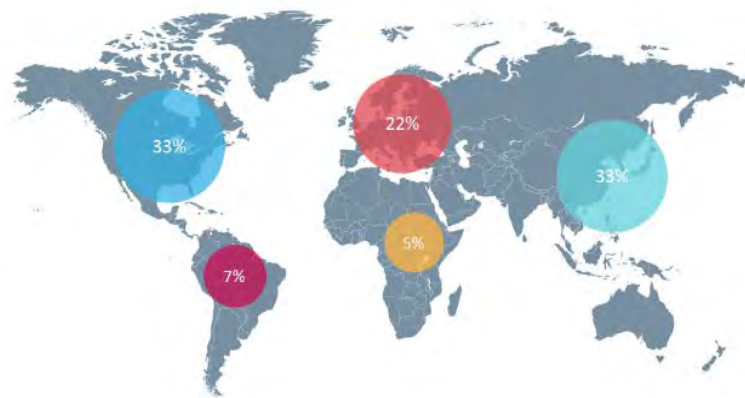
Source: Nasscom, Arianth Research

Acknowledging the above challenge of shortage of skilled labours, some IT companies like Mindtree has started investing heavily in re-skilling its employees. As a result Mindtree is not overtly worried about the effects of technology change (re-skilling) on the workforce. Thus consistent with its core philosophy of re-skilling its employees on a regular basis, the company invested in creating an internal platform called 'Yorbit' long back, which today has 1987 courses sourced from leading content providers all over the world as well as internally created content. Currently, 13641 Mindtree employees have completed 1,370,477 hours of training on the platform.

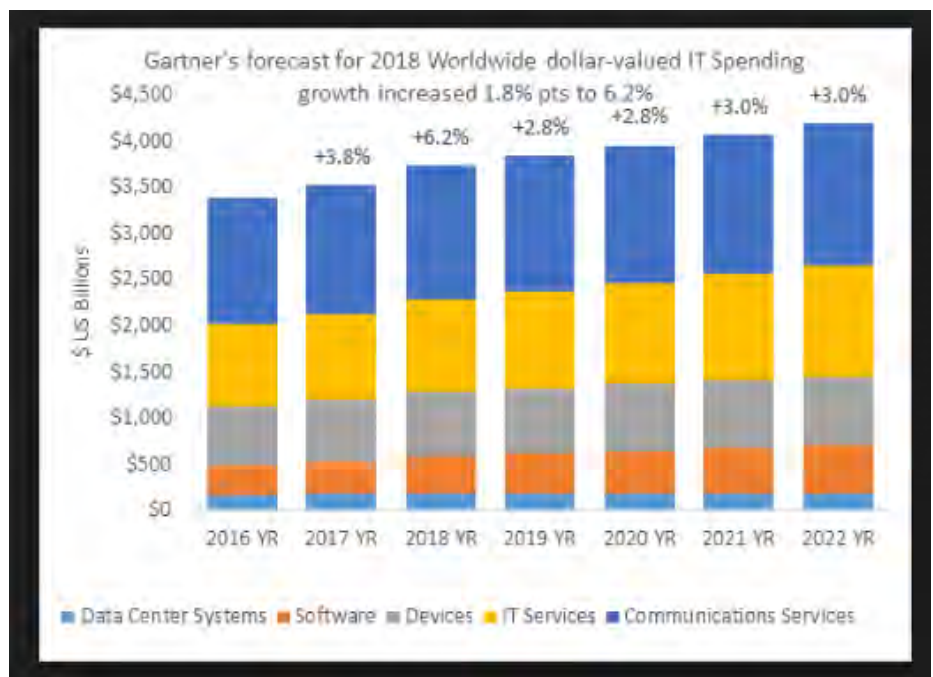
Regional Distribution of IT spending

The United States is the largest tech market in the world, representing 31% of the total, or approximately US\$1.5 trillion for 2018. In the U.S., as well as in many other countries, the tech sector is one of the most significant contributors to GDP. In the aggregate, the Asia-Pacific region, which encompasses Japan, China, Australia, India, and surrounding countries, accounts for one-third of the total. APEC has increased its share of the global IT pie, driven by the rise of countries such as China and India, and the slower growth rates experienced in parts of Europe and other markets. By 2032, China is projected to claim the mantle of world's largest economy.

Regional Distribution of IT Spending



Source: Gartner, Arihant Research



Source: Gartner, Arihant Research

Indian IT Services Industry

Traditional IT Services

The share of traditional IT services, account for the bulk of the US\$140 billion-a-year Indian IT industry. Overall IT revenue growth is expected at ~8% per annum until fiscal 2020, driven largely by digital services. Revenue growth in the industry slowed to below 10% between fiscals 2015 and 2017, from a very strong 27% compound annual growth rate (CAGR) seen in two decades through fiscal 2014. With bulk of the revenue coming from exports of services, lower IT spend by major global clients and a shift in demand towards digital services have led to the decline. Going forward in IT outsourcing, the pace of decline is expected to accelerate as enterprises close more data centres and embrace managed-cloud services. The offshore industry should show steady growth with localization of resources as the new theme in 2019.

Information Technology in India is an industry consisting of two major components,---

- **IT services and**
- **Business Process Outsourcing (BPO)**

With accelerated economic growth across geographies over 2017-2019 (figure below), the IT sector remains one of the major contributors to the GDP of the leading nations like US, Europe, China and India. The IT sector has increased its contribution to India's GDP from 1.2% in 1998 to 7.7% in 2017. According to NASSCOM, the sector aggregated revenues of US\$160 billion in 2017, with export revenues at US\$99 billion and domestic revenues at US\$48 billion, growing by over 13%. The United States accounts for two-thirds of India's IT services exports.

Economic growth across geographies:

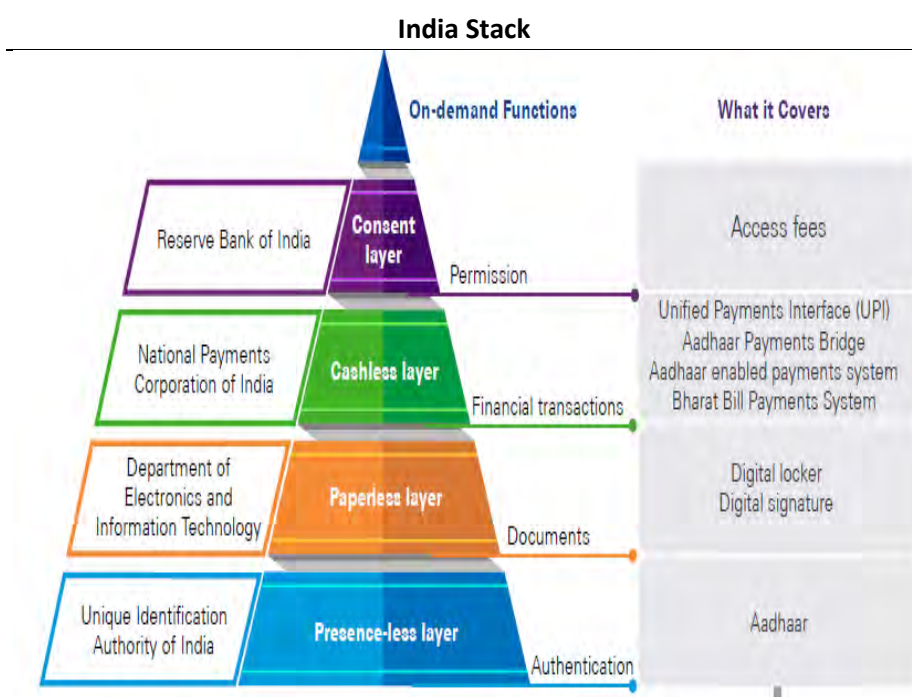
Area	2017	2018	2019
US	2.3%	2.7%	2.5%
Europe	2.4%	2.2%	2.0%
China	6.8%	6.6%	6.4%
India	6.7%	7.4%	7.8%

Source: Mindtree Annual Report, Arian Research

India – Growing towards an open Digital Economy

Over the past few years, India has essayed several guidelines and reforms such as granting multiple licences for differentiated banking to small finance banks, payment banks and introduced the unified payment interface to include the unbanked population of India in the formal financial services folder, strengthening the payments ecosystem. To embrace open banking architecture and unleash the true potential of shared ecosystem, a foundation has to be formed on four pedestals,--

1) government, 2) regulators, 3) traditional institutions and 4) fintech.



Source: Nasscom, Arianth Research

For open digital economy to thrive, strong government support is a critical component. To propel India towards a digital economy, the government along with the support of regulators, is working aggressively towards creating a progressive digital ecosystem. The government is expediting the move towards a 'presence, paper, and cash – less service delivery' system popularly known as '**India Stack**'.

An upsurge is evident as a result of these reforms and initiatives across several key indicators. Around 878 million bank accounts have been linked with Aadhaar till March 2018. Transaction volume using Unified Payments Interface grew from 0.1 million in October 2016 to 312 million in August 2018 and transactions in value terms rose from Rs 0.5 million to over Rs 542 billion during the same period.

Share of digital services in IT exports to double in 3 years

The share of digital services in Indian's IT exports is expected to double to ~30% by FY20, as the segment grows at a healthy 30-35% a year. This will be supported by re-skilling of employees and increased M&As by Indian IT players, seeking to enhance the digital pie in revenues. The increasing share of digital services in new global outsourcing contracts will drive revenue growth going forward. For major IT players based outside India, more than a third of revenue already comes from digital services. Besides in-house digital skill building, IT firms are likely to undertake more acquisitions that will accelerate revenue growth from digital services.

As the share of digital services in IT exports is expected to double in 3 years, we believe companies which are winning large deals in the digital space and have excellent competency in successfully executing digital projects, will be the prime beneficiaries. In this report we have covered two mid-cap IT companies, **1) Mindtree** and **2) NIIT Technologies**, which we believe will benefit from this digital upsurge and initiated coverage on them with 'BUY'.

Mindtree

We expect Mindtree to report 18.4% CAGR in its revenues over FY18-21E, while PAT will witness a CAGR of 21.1% over the same period. EBITDA margin is expected to be steady around 16-16.5% level. We are positive on Mindtree's future growth prospects, and initiate coverage on the stock with a BUY rating and a target price of Rs 1141 (18.5x FY21E earnings), giving an upside potential of 28.6%.

Financial Performance

YE March (Rs Mn)	Net Sales	EBITDA	PAT	EPS (Rs)	EBITDA Margin %	RoE (%)	P/E (x)	P/BV (x)
FY16	46730	8210	5525	32.9	17.6	22.9	26.9	6.2
FY17	52364	7181	4186	24.9	13.7	16.2	35.6	5.8
FY18	54628	7405	5701	34.8	13.6	20.8	25.5	5.3
FY19E	70692	11108	7373	44.9	15.7	23.1	19.8	4.6
FY20E	81434	13336	8896	54.2	16.4	23.9	16.4	3.9
FY21E	90629	14939	10131	61.7	16.5	23.1	14.4	3.3

Source: Company, Arianth Research

NIIT Technologies

We expect N-Tech to report 20.3% CAGR in its revenues over FY18-21E, while PAT will witness a CAGR of 27.8% over the same period. EBITDA margin is expected to be steady around 17-18% level. We are positive on N-Tech's future growth prospects, and initiate coverage on the stock with a BUY rating and a target price of Rs 1570 (16.5x FY21E earnings), giving an upside potential of 28.2%.

Financial Performance

YE March (Rs Mn)	Net Sales	EBITDA	PAT	EPS (Rs)	EBITDA Margin %	RoE (%)	P/E (x)	P/BV (x)
FY17	28021	4795	2722	44.3	17.1	16.1	27.6	4.5
FY18	29915	5014	2803	45.6	16.8	15.8	26.9	4.2
FY19E	37287	6451	4039	65.7	17.3	20.0	18.7	3.7
FY20E	45053	7929	4981	81.0	17.6	22.5	15.1	3.4
FY21E	52042	9264	5854	95.2	17.8	24.0	12.9	3.1

Source: Company, Arianth Research

COMPANY SECTION

CMP : Rs 887

Rating : BUY

Target : Rs 1141

STOCK INFO

INDEX	
BSE	532819
NSE	MINDTREE
Bloomberg	MTCL IN
Reuters	MINT.BO
Sector	IT
Face Value (Rs)	10
Equity Capital (Rsmn)	1642
Mkt Cap (Rsmn)	145645
52w H/L (Rs)	1182/ 670
Avg Weekly Vol (BSE+NSE)	22277350

SHAREHOLDING PATTERN

	%
(as on Dec, 2018)	
Promoters	13.3
Public & Others	86.7

Source: ACE Equity, Arihant Research

STOCK PERFORMANCE(%)	3m	6m	12m
Mindtree	-9.4	-16.5	29.3
SENSEX	6.0	0.0	3.2

Source: ACE Equity, Arihant Research

Mindtree v/s SENSEX



Source: ACE Equity, Arihant Research

Mindtree Limited is a global technology consulting and services company headquartered in Bengaluru, India and New Jersey, USA. With strong deal pipeline and encouraging demand environment, we expect Mindtree to continue its industry leading growth momentum going forward. We expect Mindtree to report 18.4% CAGR in its revenues over FY18-21E, while PAT will witness a CAGR of 21.1% over the same period. EBITDA margin is expected to be steady around 16-16.5% level. We are positive on Mindtree's future growth prospects, and initiate coverage on the stock with a BUY rating and a target price of Rs 1141 (18.5x FY21E earnings), giving an upside potential of 28.6%.

■ **Scaling up of digital revenues to boost growth going forward**

Digital business is estimated to provide the Indian IT companies a US\$ 48bn market by 2020 and thereby making it a great market opportunity for Mindtree for next several years. For Mindtree, digital revenue has grown at a CQGR (compounded quarterly growth rate) of 4.6% over Q1FY17-Q3FY19 period. Mindtree expects to maintain its revenues from Digital services to 50% of its total revenues.

■ **Stable utilisation rate and low attrition will be beneficial in medium term**

Employee addition remains strong for Mindtree with stable utilisation level and lower attrition rate. Attrition Rate fell to a low of 12.5% in FY18 from 15.1% in FY17, which is lowest in last 5 years. Mindtree's investment in reskilling its people was the biggest reason for the multiyear low attrition levels. Going forward low attrition level and stable employee utilisation rate will be beneficial for Mindtree in the medium term.

■ **PAT to witness 21.1% CAGR over FY18-21E**

With 18.4% CAGR revenue growth over FY18-21E and stable EBITDA margin around 16-16.5% level, we expect Mindtree's consolidated PAT to grow from Rs 5701mn in FY18 to Rs 10131mn in FY21E, thereby registering a CAGR of 21.1% over FY18-21E.

Valuations

At CMP of Rs 887, Mindtree is trading at FY19E, FY20E and FY21E, P/E multiples of 19.8x, 16.4x and 14.4x respectively, which is reasonable. We value the stock at a FY21E target P/E multiple of 18.5x, which yields a target price of Rs 1141 per share. We are bullish on the future prospects of Mindtree and initiate coverage on the stock with a BUY rating and a target price of Rs 1141 (18.5x FY21E earnings), which gives an upside potential of 28.6%.

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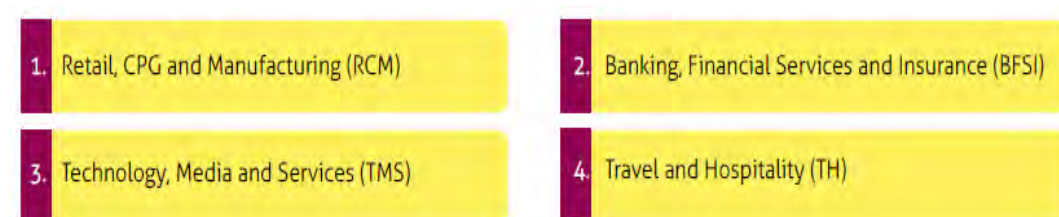
Source: Company, Arihant Research

Company Background

Mindtree Limited is a global technology consulting and services company headquartered in Bengaluru, India and New Jersey, USA. Founded in 1999, the company employs approximately 19,000 employees with annual revenue of \$846mn in FY18. Mindtree deals in e-commerce, mobile applications, cloud computing, digital transformation, data analytics, enterprise application integration and enterprise resource planning, with more than 340 active clients and 43 offices in over 17 countries, as of 31 July 2018. Its largest operations are in India and major markets are United States and Europe. Mindtree has formed successful business and technology alliances with big companies like Microsoft, Salesforce, Hewlett Packard, Oracle, Bluetooth SIG, Intel, IBM, SAP, Orange, Sun Microsystems and many more.

Business Verticals

The key verticals of the company are Retail, CPG and Manufacturing (RCM), Banking, Financial Services & Insurance (BFSI), Technology, Media & Services (TMS) and Travel & Hospitality (TH).



Mindtree provides various research and development services including Bluetooth Solutions, Digital Video Surveillance, an integrated test methodology called MindTest, an IT infrastructure management and service platform called MWatch, the application management service, Atlas, SAP Insurance and OmniChannel. Some of the top clients are Microsoft, AIG, Unilever, Avis, Southwest Airlines, Fly Dubai, Getronics, P&G, Marriott, Adidas, Symantec, Samsung, etc.

Service Offerings

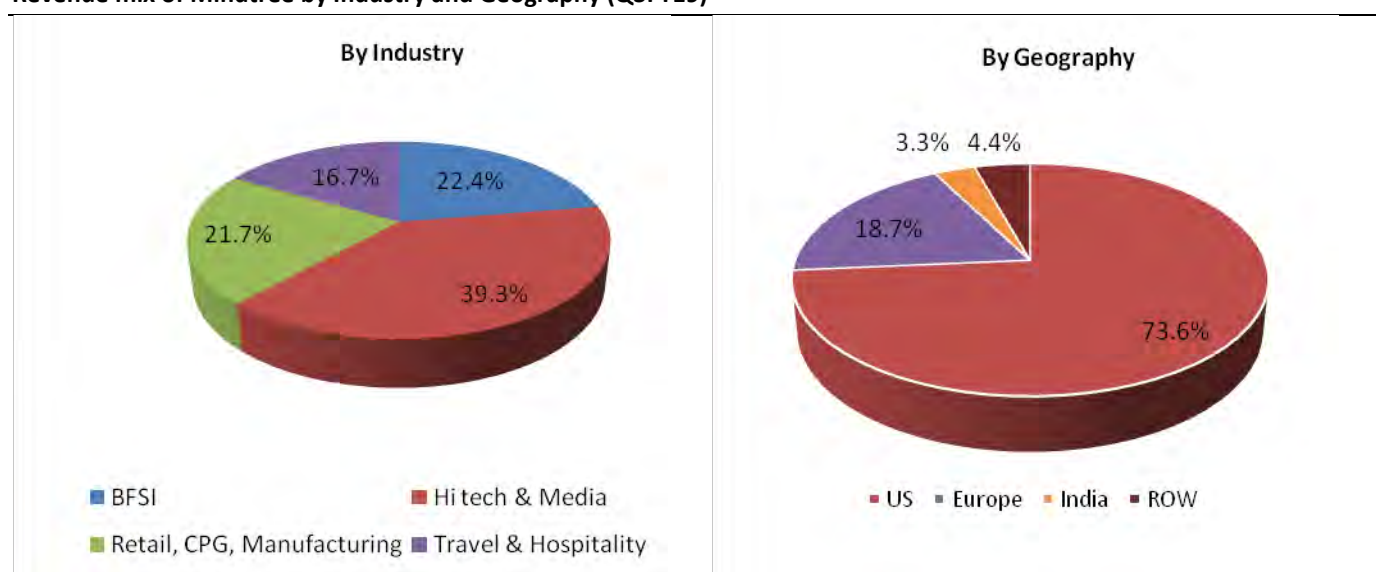


Source: Company, Arianth Research

Diversity of Revenues

The company works in Application Development and Maintenance, Data Analytics, Digital Services, Enterprise Application Integration & Business Process Management, Engineering R&D, Enterprise Application Services, Testing, and Infrastructure Management Services. Mindtree's revenue stream is diversified by Industry as well as Geography. In the following figure Mindtree's revenue mix has been given for the latest reported quarter of Q3FY19. As per industry mix, Retail, CPG and Manufacturing contributed 21.7% of Q3FY19 revenues, BFSI contributed 22.4% of revenues, Hi-Tech & Media contributed 39.3% of revenues while the rest 16.7% contribution came from Travel & Hospitality. As far as Geographical break-up is concerned, US contributed 73.6% of revenues, Europe contributed 18.7% of revenues, while the rest came from India (3.3%) and ROW (4.4%).

Revenue mix of Mindtree by Industry and Geography (Q3FY19)



Source: Company, Arianth Research

Hi-Tech & Media Services

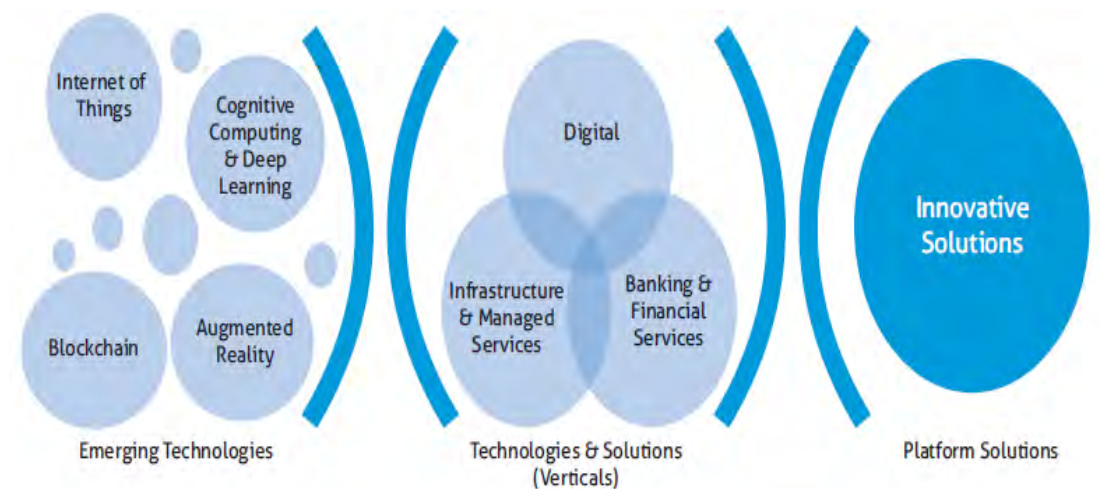
The media industry is in the midst of enormous reinvention at the hands of digital. Technology is erasing the lines between content creators and consumers. Powerful online communities are pushing news and events into real time viral storms. New distribution channels and partnerships are creating unprecedented business opportunities. Mindtree uses its expertise to enable broadcasters, publishers, gamers, out-of-home services, advertising agencies and sports/entertainment businesses to quickly adapt and align to customer needs. Solutions that have helped align business with customer needs to ensure two clear goals,--

- Customisation and personalisation of content to create delight/engagement
- Continued protection of advertising/subscription revenues mainly from non-traditional players

BFSI

Mindtree's Banking vertical, over several years, has successfully leveraged on its domain and technical expertise to deliver solutions for leading Banks and Financial Institutions across the world. Mindtree has strong banking analytics, sound and stable infrastructure, which help transform the world's leading banks and financial institutions. By delivering scalable services, Mindtree was able to manage and execute strategic initiatives, creating innovative delivery models like omnidirectional banking. Mindtree supports mission-critical infrastructure and banking software applications that pull insights from data to help banks engage in a better fashion with their users and customers. Mindtree has decent track record in providing Banking solutions, having worked with more than 14+ clients across the globe. With more than 600+ people in banking among which 155 are FLIP certified, across various role like, business analysts, architects, tech leads, developers etc, Mindtree was able to bring to its clients a credible and experienced global leadership team driving service delivery through the next generation global delivery model.

Mindtree is working on using innovative technologies to solve challenges in niche areas in the banking and capital markets value chain. The company has focused on the developing solutions in disruptive technologies aimed at helping banks and financial institutions address regulatory obligations and other path breaking solutions in the banking, securities and payment industry.



Source: Company, Arianth Research

Retail, CPG & Manufacturing

Today's consumers use many different channels to compare and buy products and services. They expect retailers to provide fast, consistent and seamless interactions in stores, online and via mobile devices. Mindtree helps retailers transform their technology to gain a 360-degree view of consumers and serve them across the entire purchase process using retail supply management and retail consulting. With greater visibility into the customer experience, Mindtree helps to improve operational efficiencies, increase order fulfilment and encourage collaboration between stores and supply chain partners.

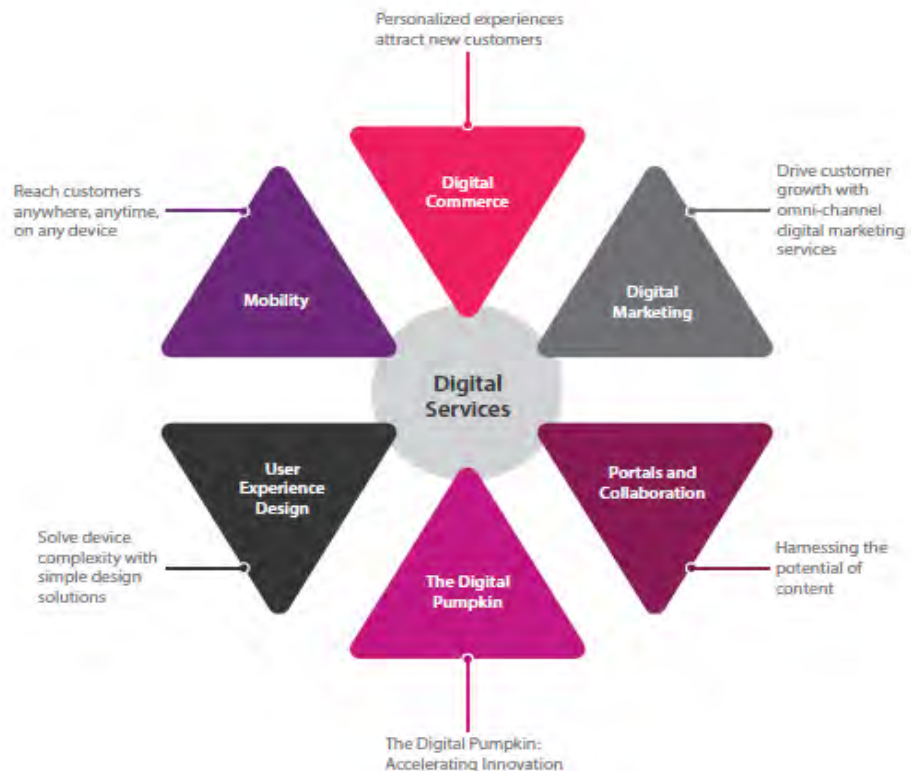
Travel & Hospitality

Mindtree delivers digital transformation and technology solutions and services for the 'Travel, Hospitality and Leisure' industry which includes Air Transport, Hotel & Lodging, Resorts & Vacations, Car & Truck Rental, Travel Management & Services, Recreation & Leisure and Health & Wellness for its clients all over the world. There is a growing need to think beyond selling seats and rooms in the industry. eHailing for car rentals, unbundling of inventory and ancillary sales have become the mainstay of offerings in the travel industry, owing to the growing customer demands. Mindtree has strong understanding of the Travel & Hospitality industry and unlike most of its competitors, Mindtree has instituted a dedicated leadership group for this industry, which has resulted in several large multi-year client partnerships for the company.

Digital Services

From an IT services industry perspective, Digital business is estimated to touch US\$225 bn by 2020 with US\$48 bn predicted for Indian IT Services firms. But the excitement stems from the optimistic view that 90% of all incremental spend in the next five years on IT will be on Digital. Mindtree has a vision to "Make Businesses digital". In order to achieve this vision, the company has positioned its Digital Business across six areas,---

- Digital commerce
- Digital marketing
- Mobility
- User experience design
- Portals and collaborations
- The digital pumpkin



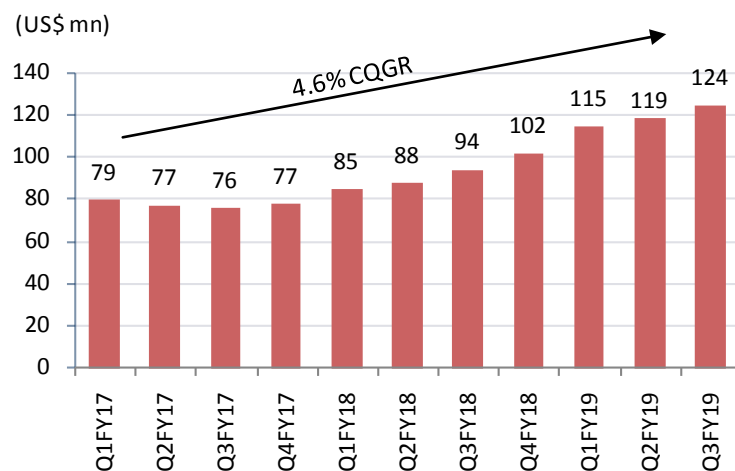
Source: Company, Arianth Research

Investment Rationale

■ Scaling up of digital revenues to boost growth going forward

Digital business is estimated to provide the Indian IT companies a US\$ 48bn market by 2020 and thereby making it a great market opportunity for Mindtree for next several years. Mindtree's digital strategy is pivoted on multiple solutions, IPs and frameworks cutting across several service offerings, covering areas such as real time recommendations, social media intelligence, workforce productivity, customer analytics and sales enablement etc. In the digital space, deal size is increasing and the market is opening up. For Mindtree, Retail, CPG and travel are expected to grow at a faster rate and will lead the growth for Digital revenue.

Digital revenue trend of Mindtree over the quarters



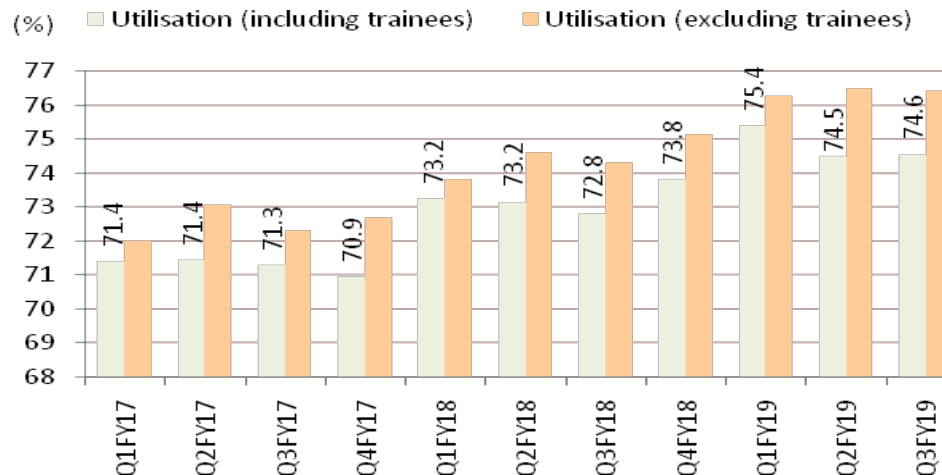
Source: Company, Arianth Research

Digital, now contributing nearly half of its revenue (49.5% in Q3FY19), grew 5% sequentially and 32.3% YoY for the quarter ended Q3FY19. For Mindtree, digital revenue has grown at a CQGR (compounded quarterly growth rate) of 4.6% over Q1FY17-Q3FY19 period. Mindtree's competency in digital space is visible from its digital contribution to its total revenue (~50%) and strong double-digit YoY growth in digital business. However, due to lower adoption of digital pick-up in BFSI unlike other verticals, the management sounded cautious on BFSI. For the last reported quarter of Q3FY19, BFSI vertical continued to see pressure, as digital spend is as yet on the rise and its key services include mainly run-the-business services.

We believe the near-term BFSI weakness notwithstanding, going forward, FY20E could see improving growth given higher digital spend in this vertical and Mindtree's increasing focus on change-the-business services. Also with the acquisitions of Magnet 360 LLC, Bluefin Solutions and Relational Solutions Inc., Mindtree further strengthened its digital capabilities. Over the next 2-3 years, Mindtree expects to maintain its revenues from Digital services to 50% of its total revenues.

- **Stable utilisation rate and low attrition level will be beneficial in the medium term**
Although large IT companies have alluded to supply-side constraints leading to higher costs of subcontracting, Mindtree management did not sound worried in the latest quarterly concall for Q3FY19. As clients are looking to transform their core businesses, Mindtree is getting deals which are having more digital share, especially in the consumer facing businesses, also deal sizes are getting larger. Hence, management is in a position to move more work offshore.

Utilisation level of Mindtree over the quarters



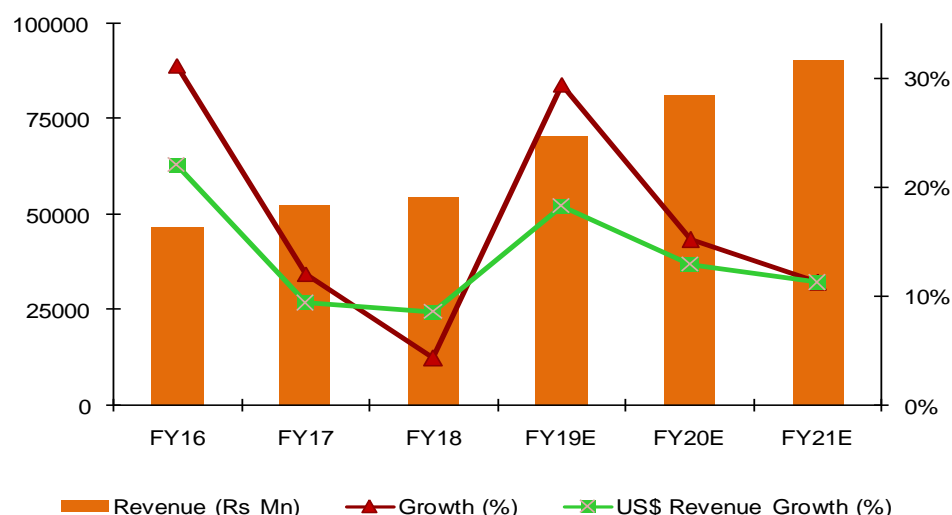
Source: Company, Arianth Research

Employee addition remains strong for Mindtree with stable utilisation level and lower attrition rate. Attrition Rate fell to a low of 12.5% in FY18 from 15.1% in FY17, which is lowest in last 5 years. As a result Mindtree is not overtly worried about the effects of technology change (reskilling) on the workforce. Thus consistent with its core philosophy of reskilling its employees on a regular basis, the company invested in creating an internal platform called 'Yorbit' long back, which today has 1987 courses sourced from leading content providers all over the world as well as internally created content. Currently, 13641 Mindtree employees have completed 1,370,477 hours of training on the platform. This investment in reskilling its people was perhaps the biggest reason for the multiyear low attrition levels in Mindtree.

Financial Performance Analysis

■ Revenue to witness 18.4% CAGR over FY18-21E

In its latest reported quarter of Q3FY19 Mindtree reported strong revenue growth of 17.8% YoY in constant currency terms, reversing the weakness it witnessed in the preceding quarter. Mindtree's competency in digital space is visible from its digital contribution to its total revenue (~50%) and strong double-digit YoY growth in digital business over the quarters. In Q3FY19, digital revenue grew 32% YoY and 5% QoQ and contributed 49.5% to its total revenue.



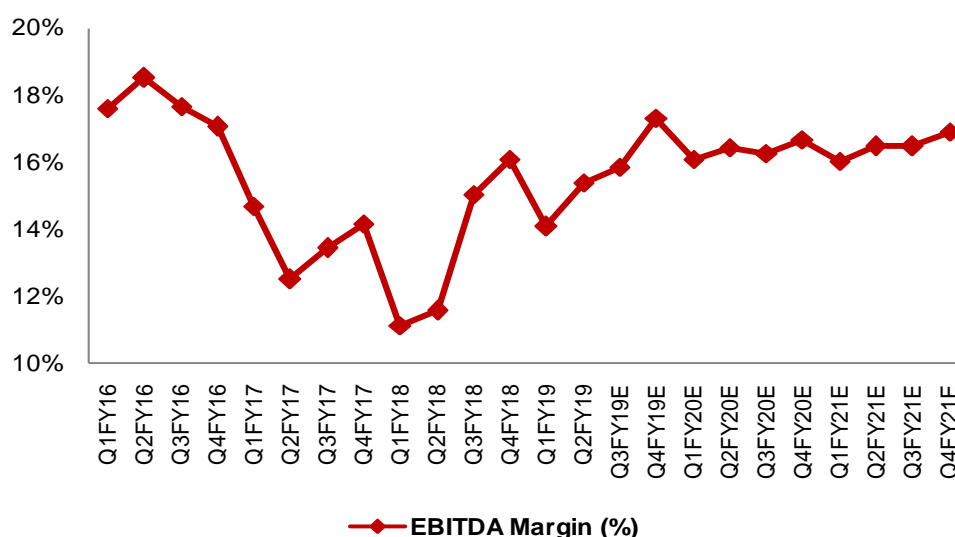
Source: Company, Arian Research

Over the last few years Mindtree has been able to deliver industry leading growth in its revenues. Even in the latest reported quarter of Q3FY19, the company reported robust 17.8% YoY in CC terms. This was despite tepid growth in its top client account. In the Q3FY19 concall, management has given encouraging commentary on demand environment and steady deal wins; which reflects strong end-market demand. We expect Mindtree to report 29.4%, 15.2% and 11.3% YoY revenue growth (in rupee terms) for FY19E, FY20E and FY21E respectively. While on constant currency terms, we expect Mindtree to report 18.3%, 12.9% and 11.3% YoY revenue growth for FY19E, FY20E and FY21E respectively.

We expect Mindtree to continue reporting industry leading growth going forward and have modeled a revenue growth of 18.4% CAGR (in rupee terms) and 14.1% CAGR (in constant currency terms) over FY18-21E.

■ EBITDA margin to remain stable around 16-16.5% level

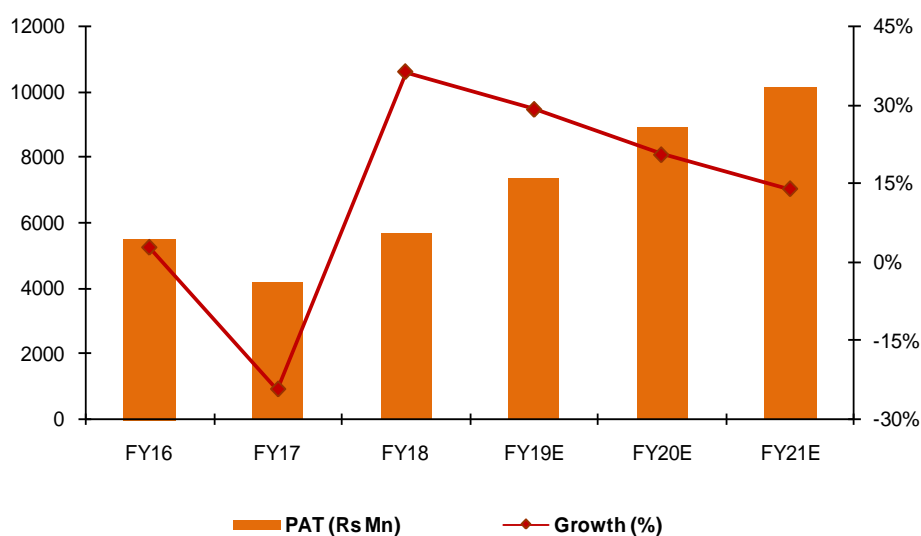
Mindtree has improved its EBITDA margin by 50 basis points sequentially to 15.9% in Q3FY19 due to operational efficiency. Management expects margin to remain stable going forward. We believe Mindtree would be able to further improve its margins in the near-term led by operational efficiency, employee pyramid and judicious pricing. In our model we have factored in stable EBITDA margin of 15.7%, 16.4% and 16.5% for FY19E, FY20E and FY21E respectively.



Source: Company, Arianth Research

■ PAT to grow at 21.1% CAGR over FY18-FY21E

With 18.4% CAGR revenue growth over FY18-21E and stable EBITDA margin around 16-16.5% level, we expect Mindtree's consolidated PAT to grow from Rs 5701mn in FY18 to Rs 10131mn in FY21E, thereby registering a CAGR of 21.1% over FY18-21E.



Source: Company, Arianth Research

Q3FY19 and 9MFY19 Financial Performance

Rs Mn (consolidated)	Q3FY19	Q2FY19	Q3FY18	Q-o-Q	Y-o-Y	9MFY19	9MFY18	Y-o-Y
Net Revenue	17,872	17,554	13,777	1.8%	29.7%	51,821	39,988	29.6%
Employee cost	11,142	11,171	8,946	-0.3%	24.5%	32,708	26,340	24.2%
Other Expenses	3,897	3,684	2,757	5.8%	41.3%	11,271	8,598	31.1%
EBITDA	2,833	2,699	2,074	5.0%	36.6%	7,842	5,050	55.3%
<i>EBITDA margin %</i>	<i>15.9%</i>	<i>15.4%</i>	<i>15.1%</i>	<i>48</i>	<i>80</i>	<i>15.1%</i>	<i>12.6%</i>	<i>250</i>
Other Income	-200	524	59	NA	NA	603	1,311	-54.0%
Depreciation	410	403	419	1.7%	-2.1%	1,213	1,332	-8.9%
EBIT	2,223	2,820	1,714	-21.2%	29.7%	7,232	5,029	43.8%
Finance cost	-	1	46	NA	NA	29	111	-73.9%
Exceptional Item	-	-	-	-	-	-	-	-
PBT	2,223	2,819	1,668	-21.1%	33.3%	7,203	4,918	46.5%
Tax Expense	311	756	253	-58.9%	22.9%	1,646	1,039	58.4%
<i>Effective tax rate %</i>	<i>14.0%</i>	<i>26.8%</i>	<i>15.2%</i>	<i>-1,283</i>	<i>-118</i>	<i>22.9%</i>	<i>21.1%</i>	<i>173</i>
PAT	1,912	2,063	1,415	-7.3%	35.1%	5,557	3,879	43.3%
MI & Associates	-	-	-	-	-	-	-	-
Consolidated PAT	1,912	2,063	1,415	-7.3%	35.1%	5,557	3,879	43.3%
<i>PAT margin %</i>	<i>10.7%</i>	<i>11.8%</i>	<i>10.3%</i>	<i>-105</i>	<i>43</i>	<i>10.7%</i>	<i>9.7%</i>	<i>102</i>
EPS (Rs)	11.6	12.6	8.6	-7.3%	35.1%	33.8	23.6	43.3%

Source: Company, Arianth Research

Future Outlook

Mindtree was an early adopter of digital theme (as depicted by the company's tagline 'Born Digital'). This early embracing of digital, has enabled the company to clock industry leading growth with digital contributing nearly 50% of its total consolidated revenue. With strong deal pipeline and encouraging demand environment, we expect Mindtree to continue its industry leading growth momentum going forward.

Business Metrics of Mindtree over the Quarters

	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19
Vertical Mix									
BFSI	24%	25%	25%	25%	25%	23%	22%	22%	22%
Hi-Tech & Media Services	37%	38%	38%	38%	37%	38%	39%	39%	39%
Retail, CPG & Manufacturing	24%	23%	23%	23%	23%	24%	23%	22%	22%
Travel & Hospitality	15%	15%	14%	15%	15%	16%	16%	17%	17%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%

Service Line Mix									
ADM	49%	49%	51%	50%	50%	50%	51%	51%	51%
Consulting	4%	4%	3%	4%	4%	4%	3%	3%	3%
Package Implementation	12%	13%	12%	11%	11%	11%	11%	9%	9%
IP Led Revenue	1%	1%	1%	1%	1%	1%	1%	1%	1%
Independent Testing	13%	13%	12%	12%	13%	13%	13%	13%	13%
Infra Mgmt. & Tech Support	20%	20%	21%	22%	21%	21%	22%	23%	23%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%

Geography Mix									
US	69%	70%	70%	68%	70%	71%	73%	74%	73%
Europe	21%	21%	21%	23%	21%	21%	20%	19%	19%
India	3%	3%	3%	3%	3%	3%	3%	3%	4%
Rest of World (ROW)	7%	7%	6%	6%	6%	5%	4%	4%	4%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%

Total Contract Value (US\$ mn)									
Renewals	170	135	219	130	187	256	255	222	184
New	144	74	43	77	57	42	51	49	72
Total	314	209	262	207	244	298	306	271	256
Expiring within 1 year	234	182	198	166	206	237	259	198	212
Expiring > 1 year	80	27	64	41	38	61	47	73	44
Digital	103	50	108	84	132	102	139	162	136

Client Concentration									
Top client	14%	14%	15%	16%	17%	18%	19%	20%	20%
Top 5 clients	30%	31%	30%	30%	32%	32%	32%	34%	34%
Top 10 clients	42%	42%	42%	42%	44%	44%	44%	45%	44%

Number of Client									
Between US\$ (1mn - 5mn)	106	111	113	114	114	118	117	111	116
Between US\$ (5mn-10mn)	30	30	33	38	37	38	39	44	44
> US\$ 10mn	23	22	22	21	20	23	25	27	27

Utilisation									
Including Trainees	71%	71%	73%	73%	73%	74%	75%	75%	75%
Excluding Trainees	72%	73%	74%	75%	74%	75%	76%	77%	76%

Source: Company, Arianth Research

Valuations

At CMP of Rs 887, Mindtree is trading at FY19E, FY20E and FY21E, P/E multiples of 19.8x, 16.4x and 14.4x respectively. If we look at the average P/E band of Mindtree for the last 10 years then the stock has traded at an average P/E of 17x. IT stocks have always been reasonably valued by the street despite their secular growth oriented business model and ability to generate positive free cash flows. Mindtree due to its industry leading growth momentum and digital focus has commanded better multiple than its midcap IT peers like NIIT Tech, Hexaware, etc. However due to stagnant margin and limited scope to increase its margins in future despite strong revenue growth, we assign a target P/E multiple of 18.5x (slight premium to its 10 years average) to its FY21E earnings to value the stock. We value the stock at a FY21E target P/E multiple of 18.5x, which yields a target price of Rs 1141 per share. We are bullish on the future prospects of Mindtree and initiate coverage on the stock with a BUY rating and a target price of Rs 1141 (18.5x FY21E earnings), which gives an upside potential of 28.6%.

PE Band - Mindtree Ltd.



Source: Company, ACE Equity, Arihant Research

Peer Comparison

Mindtree's closest peer companies are Hexaware, Mphasis, NIIT Technologies and Tech Mahindra. In the following table we have compared Mindtree with its peers on key parameters.

Company Name (FY20E estimates)	Price (Rs)	Sales (Rs Mn)	EBITDA (Rs Mn)	EBITDA Margin (%)	PAT (Rs Mn)	EPS (Rs)	P/E (x)	P/BV (x)	ROE (%)
Hexaware Tech	333	59180	9649	16.3	7333	23.7	14.0	3.3	25.8
Mphasis Tech	868	88280	15566	17.6	12023	63.4	13.7	2.8	21.1
Mindtree	887	81434	13336	16.4	8896	54.2	16.4	3.9	23.9
NIIT Technologies	1225	45053	7929	17.6	4981	81.0	15.1	3.4	22.5
Tech Mahindra	719	386074	70439	18.2	47539	53.3	13.5	2.6	20.8

Source: Company, Bloomberg, Arihant Research

Consolidated Financials

Income Statement (Rs mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
Revenues	46,730	52,364	54,628	70,692	81,434	90,629
Change (%)	31.2%	12.1%	4.3%	29.4%	15.2%	11.3%
Employee Costs	27,991	34,125	35,641	44,022	50,173	56,035
Other Expenses	10,529	11,058	11,582	15,562	17,925	19,654
Total Expenses	38,520	45,183	47,223	59,584	68,098	75,690
EBITDA	8,210	7,181	7,405	11,108	13,336	14,939
Other Income	839	417	1,902	790	796	1,042
Depreciation	1,658	1,858	1,715	1,673	1,842	2,077
Interest	160	191	169	138	103	120
PBT	7,231	5,549	7,423	10,087	12,187	13,784
Tax	1,706	1,363	1,722	2,714	3,290	3,653
Rate (%)	23.6%	24.6%	23.2%	26.9%	27.0%	26.5%
PAT	5,525	4,186	5,701	7,373	8,896	10,131
MI & Associates	0	0	0	0	0	0
Consolidated PAT	5,525	4,186	5,701	7,373	8,896	10,131
Change (%)	3%	-24.2%	36.2%	29.3%	20.7%	13.9%

Source: Company, Arianth Research

Balance Sheet (Rs mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
Sources of Funds						
Share Capital	1,678	1,680	1,639	1,642	1,642	1,642
Reserves & Surplus	22,471	24,091	25,775	30,284	35,633	42,218
Net Worth	24,149	25,771	27,414	31,926	37,275	43,860
Loan Funds	433	991	3,009	1,605	1,873	2,202
MI, Deferred Tax & other Liabilities	432	-323	-233	-233	-233	-233
Capital Employed	25,014	26,439	30,190	33,298	38,915	45,829
Application of Funds						
Net Block	6,805	5,750	5,029	6,028	7,051	8,270
CWIP	232	192	92	110	129	151
Other Non-current Assets	6,990	6,672	6,837	7,311	7,735	8,240
Net Fixed Assets	14,027	12,614	11,958	13,450	14,914	16,661
Investments	62	58	58	58	58	58
Debtors	9,728	8,962	10,155	13,364	15,618	17,381
Cash & Bank Balance	4,598	8,377	10,495	9,434	11,668	15,458
Loans & Advances & other CA	3,948	3,271	4,381	5,765	6,738	7,498
Total Current Assets	18,274	20,610	25,031	28,563	34,023	40,337
Current Liabilities & Provisions	7,349	6,843	6,857	8,773	10,080	11,227
Net Current Assets	10,925	13,767	18,174	19,791	23,943	29,109
Total Assets	25,014	26,439	30,190	33,298	38,915	45,829

Source: Company, Arianth Research

Cash Flow Statement (Rs mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
PBT	7,231	5,549	7,423	10,087	12,187	13,784
Depreciation	1,658	1,858	1,715	1,673	1,842	2,077
Interest & others	454	-404	202	17	-85	-183
Cash flow before WC changes	9,343	7,003	9,340	11,776	13,944	15,678
(Inc)/dec in working capital	-2,995	1,095	-2,397	-3,030	-2,155	-1,579
Operating CF after WC changes	6,348	8,098	6,943	8,746	11,790	14,099
Less: Taxes	-1,706	-1,363	-1,971	-2,714	-3,290	-3,653
Operating Cash Flow	4,642	6,735	4,972	6,033	8,499	10,446
(Inc)/dec in F.A + CWIP	-1,584	-871	-1,020	-2,691	-2,883	-3,319
(Pur)/sale of investment	0	0	0	0	0	0
Cash Flow from Investing	-1,584	-871	-1,020	-2,691	-2,883	-3,319
Free Cash Flow (FCF)	3,058	5,864	3,952	3,342	5,616	7,128
Loan raised/(repaid)	410	558	2,018	-1,404	267	329
Equity raised	841	2	-41	3	0	0
Interest & others	-6,738	-464	-1,254	151	-103	-120
Dividend	-2,079	-2,181	-2,557	-3,153	-3,547	-3,547
Cash Flow from Financing Activities	-7,566	-2,085	-1,834	-4,403	-3,383	-3,338
Net inc /(dec) in cash	-4,508	3,779	2,118	-1,061	2,233	3,790
Opening balance of cash	9,106	4,598	8,377	10,495	9,434	11,668
Closing balance of cash	4,598	8,377	10,495	9,434	11,668	15,458

Source: Company, Arianth Research

Key Ratios

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
Per share (Rs)						
EPS	32.9	24.9	34.8	44.9	54.2	61.7
CEPS	42.8	36.0	45.2	55.1	65.4	74.3
BVPS	143.9	153.4	167.2	194.4	227.0	267.1
DPS	10.5	11.0	13.0	16.0	18.0	18.0
Valuation (x)						
P/E	26.9	35.6	25.5	19.8	16.4	14.4
P/CEPS	20.7	24.7	19.6	16.1	13.6	11.9
P/BV	6.2	5.8	5.3	4.6	3.9	3.3
EV/EBITDA	17.2	19.2	18.6	12.4	10.2	8.8
Return ratio (%)						
EBIDTA Margin	17.6%	13.7%	13.6%	15.7%	16.4%	16.5%
PAT Margin	11.8%	8.0%	10.4%	10.4%	10.9%	11.2%
ROE	22.9%	16.2%	20.8%	23.1%	23.9%	23.1%
ROCE	26.2%	20.1%	18.8%	28.3%	29.5%	28.1%
Dividend Yield	1.2%	1.2%	1.5%	1.8%	2.0%	2.0%
Leverage Ratio (%)						
Total D/E	0.0	0.0	0.1	0.1	0.1	0.1
Net D/E	-0.2	-0.3	-0.3	-0.2	-0.3	-0.3
Turnover Ratios						
Asset Turnover (x)	4.5	4.7	4.5	5.1	4.9	4.6
Receivable Days	76	62	68	69	70	70
Payable days	15	12	11	11	11	11

Source: Company, Arianth Research

CMP : Rs 1225
Rating : BUY
Target : Rs 1570
STOCK INFO

INDEX	
BSE	532541
NSE	NIITTECH
Bloomberg	NITEC IN
Reuters	NITT.BO
Sector	IT - Software
Face Value (Rs)	10
Equity Capital (Rs mn)	615
Mkt Cap (Rs mn)	75,338
52w H/L (Rs)	1425 / 679
Avg Weekly Vol (BSE+NSE)	5,899,960

SHAREHOLDING PATTERN

	%
(As on September, 2018)	
Promoters	30.6
Public & Others	69.4

Source: BSE, Arihant Research

STOCK PERFORMANCE(%)	3m	6m	12m
NIIT Tech	3.1	9.4	77.3
SENSEX	4.6	0.04	3.2

Source: ACE Equity, Arihant Research

NIIT Tech v/s SENSEX


Source: ACE Equity, Arihant Research

NIIT Technologies (N-Tech) is a leading global IT solutions organization, enabling its clients to achieve real world business impact through unparalleled domain expertise working at the intersection of emerging technologies. N-Tech will witness robust growth mainly driven by digital (25% of revenue) as well as sustained uptick in fresh order intake. We expect N-Tech to report 20.3% CAGR in its revenues over FY18-21E, while PAT will witness a CAGR of 27.8% over the same period. EBITDA margin is expected to be steady around 17-18% level. We are positive on N-Tech's future growth prospects, and initiate coverage on the stock with a BUY rating and a target price of Rs 1570 (16.5x FY21E earnings), giving an upside potential of 28.2%.

■ Impressive growth driven by digital revenue

Over the quarters N-Tech has consistently maintained stable growth in its BFSI segment due to continued ramp up in top accounts in US and Europe and also due to digital engagements especially in Cloud, Artificial Intelligence (AI), Data & Automation, which will be the new growth drivers for the company going forward.

■ Sustained uptick in fresh order intake

N-Tech has a robust order book to the tune of US \$375mn at the end of Q3FY19. The company had consistently increased its fresh order intake over the last few quarters.

■ Organisation restructuring to put thrust on growth and performance

N-Tech has undertaken massive restructuring exercise with special focus on large deal wins to drive sales momentum. With this restructuring, N-Tech has transformed itself from a geo-centric organisation to a vertical-centric organisation, which has been formed around three key verticals of 1) Travel & Transportation, 2) Insurance and 3) BFS.

■ PAT to witness 27.8% CAGR over FY18-21E

With 20.3% CAGR revenue growth over FY18-21E and stable EBITDA margin of 17-18%, we expect N-Tech's PAT to grow from Rs 2803mn in FY18 to Rs 5854mn in FY21E, thereby registering a CAGR of 27.8%.

Valuations

At CMP of Rs 1225, N-Tech trades at FY19E, FY20E and FY21E, P/E multiples of 17.8x, 14.4x and 12.3x respectively which is attractive. We value the stock at FY21E target P/E multiple of 16.5x, which yields a target price of Rs 1570 per share. We initiate coverage on N-Tech with a BUY rating and a TP of Rs 1570 (16.5x FY21E EPS), an upside of 28.2%.

Financial Performance

YE March (Rs Mn)	Net Sales	EBITDA	PAT	EPS (Rs)	EBITDA Margin %	RoE (%)	P/E (x)	P/BV (x)
FY17	28021	4795	2722	44.3	17.1	16.1	27.6	4.5
FY18	29915	5014	2803	45.6	16.8	15.8	26.9	4.2
FY19E	37287	6451	4039	65.7	17.3	20.0	18.7	3.7
FY20E	45053	7929	4981	81.0	17.6	22.5	15.1	3.4
FY21E	52042	9264	5854	95.2	17.8	24.0	12.9	3.1

Source: Company, Arihant Research

Company Background

NIIT Technologies (N-Tech) is a leading global IT solutions organization, enabling its clients to achieve real world business impact through unparalleled domain expertise working at the intersection of emerging technologies. With nearly 10,000 people serving clients across Americas, Europe, Asia, and Australia, N-Tech fosters a culture that promotes innovation and constantly seeks to find new yet simple ways to add value for its clients.

Business Verticals

The company focuses on three key verticals,--- 1) Banking and financial services (BFSI), 2) Insurance and 3) Travel and Transportation (T&T). This domain strength combined with leading-edge capabilities in Data & Analytics, Automation, Cloud, and Digital, helps clients to innovate business, automate process and industrialize artificial intelligence (AI).



Source: Company, Arianth Research

■ Banking & Financial Services (BFSI) Vertical

With the emergence of new digital economy, it is imperative for financial institutions to keep pace. Operating at the intersect of emerging technologies, N-Tech drives collaborative transformation across Retail and Corporate Banking, and Asset and Wealth Management for larger, established players as well as Fintechs. Working for more than 30 clients through 1000 domain specialists, the Company has enabled USD 1.5 trillion AUM, more than 6000 advisors, and managed platform services for over 200 financial institutions. Apart from larger BFS institutions, NIIT Technologies also addresses the requirements of smaller community, cooperative and rural banks through its cloud-based, customized banking solutions.

■ Insurance Vertical

N-Tech enables its clients in the insurance segment to seamlessly integrate platforms for unified experience and adopt cognitive solutions to expand revenue streams, improve time-to-market, and increase profitability. The Company has transformed more than 15 million policies, USD 100 billion premium payments written by clients, and 5X savings delivered through legacy modernization for over 50 active Insurers. It has developed deep domain expertise in Property & Casualty, Life & Annuities, Reinsurance and Large Commercial sub verticals in Insurance. NIIT Technologies also has an innovative commercial insurance and reinsurance product family – AdvantageGo which enables insurers and reinsurers to fuse the traditional with digital, helping them to rapidly adapt, drive change and succeed with agile software and Micro-services.

■ Travel & Transportation Vertical

Evolving customer demands, growing economies, increased competition, and disruptive technology is driving rapid transformation in the Travel and Transportation industry. Responding to these dynamic changes the Company is leveraging emerging technologies like Automation, AI, and Analytics effectively to enable its clients address the key industry needs of personalization and seamless operations. Working with over 100 customers, NIIT Technologies has built deep focus, and expertise in the airlines, airports, travel distribution, surface transport, travel technology, and hospitality segments.

The company offers the following services,---

- Cloud Services
- Geographic Information Systems
- Digital Process Transformation
- Application Services
- Intelligent Automation
- Data & Analytics
- Business Process Services
- Infrastructure Management Services
- Digital Services

■ Cloud Services

NIIT Technologies' Cloud services include digital transformation, Integrated Platform Hubs, Building Future Ready Infrastructure and Enabling Smart Operations for the clients. The Company has a strong partner ecosystem for cloud enablement and proven templates for design, implementation, and management, which enables clients to seamlessly move their business applications to the Cloud while managing and operating at scale.

■ Data & Analytics

The Data & Analytics services enable clients to drive agility in their business operations, attain competitive advantage, and offer proactive response to emerging opportunities. NIIT Tech helps businesses leverage enterprise and external data sources to drive better outcomes by implementing advanced analytics techniques and technologies. With an integrated approach to data management capabilities, ranging from Master Data Management to Data Quality and Data Governance, the company creates an enterprise view of data for its clients, enabling them to make informed decisions. Its Advanced Analytics Incubation Services enabled by state of the art data lab for rapid prototyping, helps organizations to see immediate ROI and jumpstart their data initiatives. The Company provides industry specific and cross industry data management and advanced analytics solutions. Data and Analytics service catalogue offers a suite of following services as 4M Approach,---

- Manage - Enterprise Data Management, Data Integration and Managed Services
- Modernise - Data Lakes, Cloud Migration and Data Virtualisation
- Moonetise - Visualization and Insights, Informative Asset Monetization
- Machine Learning - Predictive Analytics

■ Digital Services

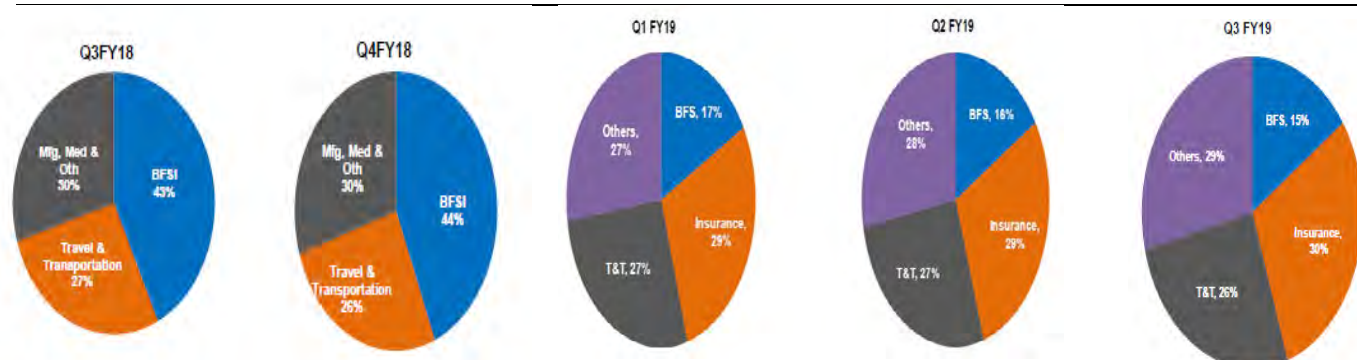
This stack enables businesses to strategize, build, and leverage new technologies and create market-ready solutions with revolutionary benefits. The company has clearly articulated offerings that spread across the digital services value chain. The Company delivers digital experience through e-commerce, user experience design, portals, social integration, multichannel offerings and mobility solutions.

Investment Rationale

■ **Cloud, Automation and Data to be the new growth drivers going forward**

While N-Tech already has a formidable presence and well-regarded position in industry verticals such as Travel & Transport (T&T), Insurance and Financial Services, it is focusing on build-outs along two dimensions on the capability front. This includes structuring of technologies that present an immediate opportunity to scale and differentiate as Service Lines capable of replicating the success N-Tech had in the fields of IMS and ADM. N-Tech expects to achieve this by building up two service lines around the following axes – Data/Automation and Cloud. In addition, N-Tech is also strengthening its Centres of Competence (CoCs) to advance and accelerate its capabilities in the areas of Block-chain and Artificial Intelligence (AI). Together all these (cloud/automation/data) will act as future growth drivers of N-Tech.

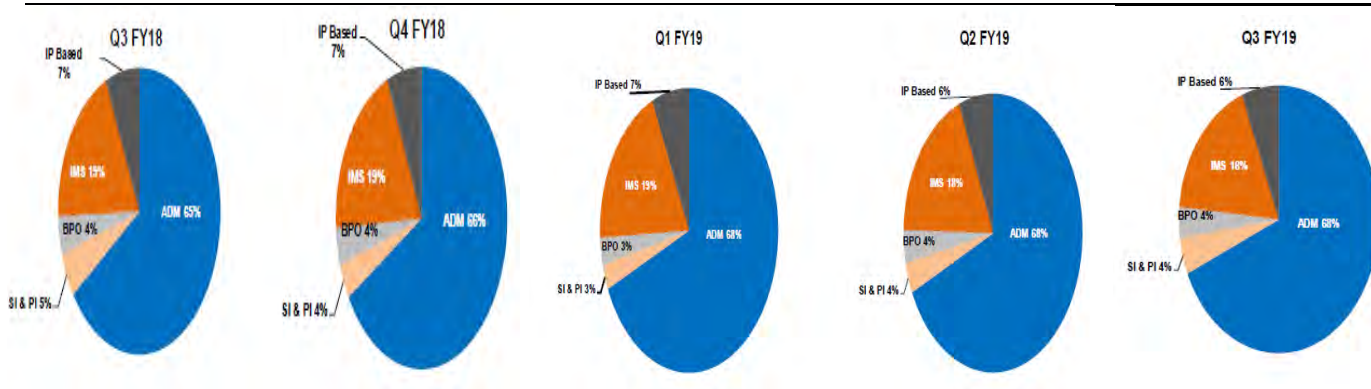
Business Vertical Mix of N-Tech over the quarters



Source: Company, Arianth Research

Over the quarters N-Tech has consistently maintained stable growth in its BFSI segment due to continued ramp up in top accounts in US and Europe and also due to digital engagements. In its last reported quarter of Q3FY19, BFSI revenue was up 1.7% QoQ. It has also added 1 new account and signed a large US\$20mn+ deal in US. The quarter also saw decent growth of 9.8% QoQ in its Insurance revenues contributing 29.6% of its total revenue for Q3FY19. N-Tech saw stable growth in its key accounts in US with signing of US\$20mn+ deal in US and added 3 new accounts. T&T revenue also continued its growth trajectory by registering 5.4% QoQ growth. N-Tech also added two new accounts in its T&T vertical.

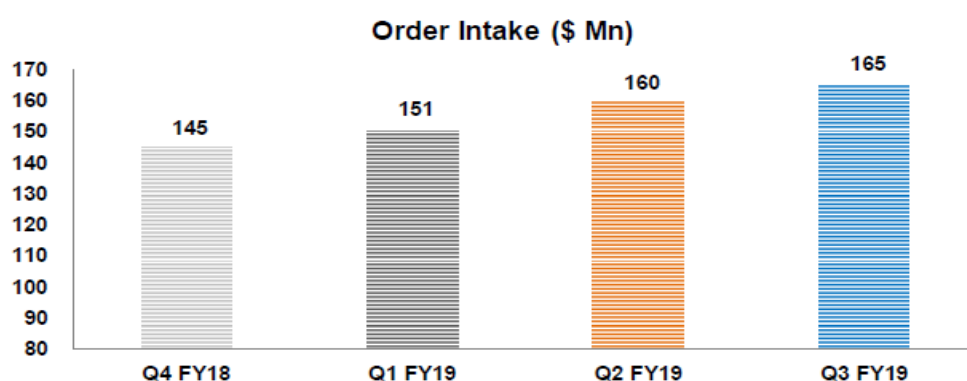
Service Mix of N-Tech over the quarters



Source: Company, Arianth Research

■ Strong order book and impressive future order pipeline

N-Tech has a robust order book to the tune of US \$375mn at the end of Q3FY19. The company had consistently increased its fresh order intake over the last few quarters. N-Tech's total fresh order intake during FY18 was US \$507mn. This was led by multiple new engagements secured by the company during the year, as well as 7 large multiyear deals. A total of 31 new clients were acquired during FY18, which is more than twice the number of new customers added by the company in FY17. In FY19 also the order inflow momentum continued (figure below). N-Tech added orders of US \$151mn, US \$160mn and US \$165mn in Q1, Q2 and Q3 of FY19 respectively. This has led to US \$375mn of firm business (order book) for N-Tech executable over next 1 year.



Source: Company, Arianth Research

During the last concluded quarter of Q3FY19, N-Tech added 10 new customers, with 8 in US and 2 in APAC (Asia Pacific). NIIT Technologies has a relatively diversified geographic and client mix and the company has been able to ensure that it does not become too dependent on any particular geography or client.

Client concentration of N-Tech over the quarters



Source: Company, Arianth Research

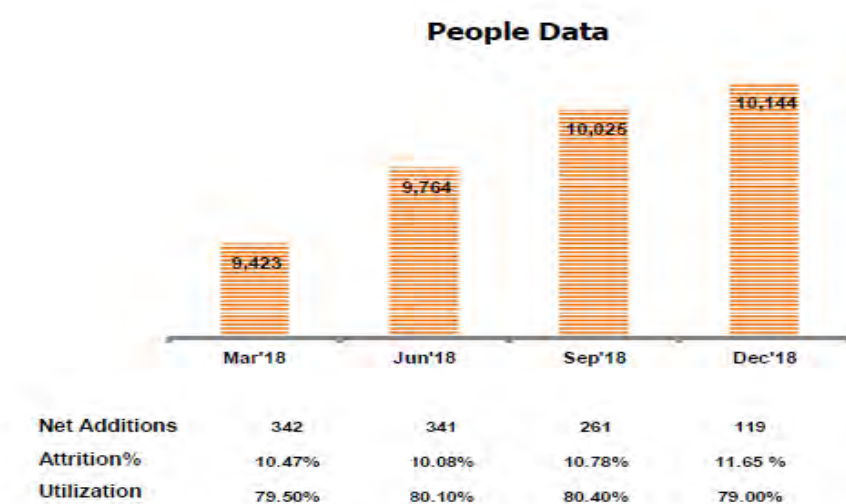
N-Tech also has a broad based clientele, with the top 10 customers contributing about 40% of revenues. The company also increased its number of US \$1mn+ clients over the quarters, which increased to 90 in Q3FY19 from 78 in Q3FY18. Also worth mentioning that while large deal wins improved, client concentration came down to 28% in Q3FY19 for top 5 clients from 30% in Q3FY18.

■ Organisation restructuring to put emphasis on growth and performance

During FY18, N-Tech inducted new leaders, mainly drawn from Tier 1 organisations to lead major industry segments globally and further sharpen the focus on select industry segments. With a view to ensure better connect with the marketplace, these leaders are based in the major markets they serve. The company also inducted a new CEO Mr. Sudhir Singh who joined in May 2017 and was appointed as CEO in January 2018. He is based in New Jersey, USA. The fundamental principles underpinning this reorganization, effective from the start of FY18, were centred around the following,--

- To further accelerate revenue growth
- Enhancing market impact
- Moving the centre of gravity of the leadership team to the markets &
- Creating new growth vectors

With the above restructuring, N-Tech has transformed itself from a geo-centric organisation to a vertical-centric organisation, which has been formed around three key verticals of 1) Travel & Transportation, 2) Insurance and 3) BFS.



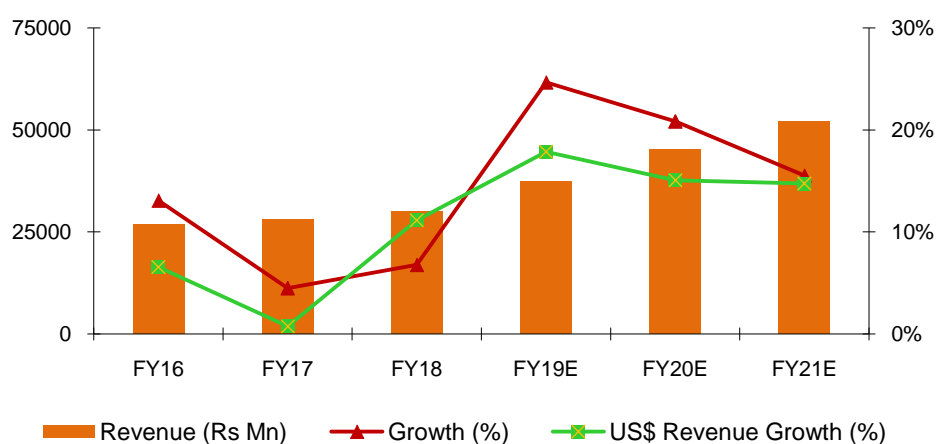
Source: Company, Arianth Research

As far as people induction is concerned, N-Tech has also added new teams that will focus on increasing its sales momentum. Its sales force is now concentrating more on large deal (US \$ 20mn qualifies for one large deal) wins. N-Tech has an internal target of winning two large deals per quarter and has revised its incentive structure in a suitable way so that its sales team remain committed enough to win these large deals. It has increased the bonus component for an employee to 4x more than that obtained earlier for these large deal wins. Also, from now on there will be discontinuous variable increases for revenue and margin upsides. Lastly, as far as increments are concerned, N-Tech has introduced more active differentiation, with the spread of the band getting wider. All these have already started showing its impact as employee utilisation level has increased over the last four quarters, from 79% in Q3FY18 to 80.4% in Q2FY19, before stabling around 79% in Q3FY19 (see figure above). Also the attrition rate has remained constant within the 10-10.5% range (barring Q3FY19, which saw some unusual spike), indicating that employees are now more happy and not leaving the organisation and N-Tech has been successful in retaining the talent.

Financial Performance Analysis

■ Revenue to witness 20.3% CAGR over FY18-21E

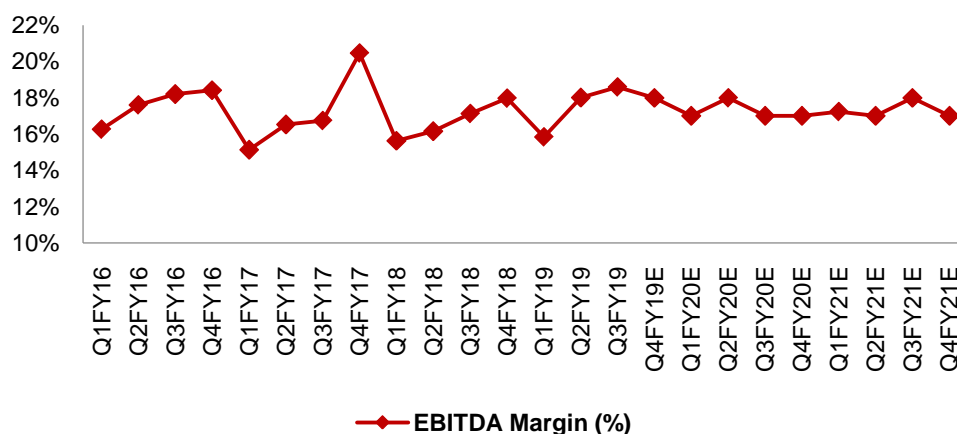
N-Tech is aiming for a sales growth of 15-16% in constant currency terms. The company is focusing on two large deal wins (US \$ 20mn each) every quarter and has adequately incentivised its sales team by raising the incentive structure by 4x from earlier level. N-Tech has increased its headcount by 900 in last 1-year, and its current employee strength stands at approx. 10,000 with some high level recruits from competitor organizations to drive its sales growth. If we look at past few quarter's results this restructuring initiative has already started showing its results and going forward also we believe all these will help the company to achieve its desired sales growth. We expect N-Tech to clock a revenue growth of 20.3% CAGR over FY18-21E.



Source: Company, Arihant Research

■ EBITDA margin to be maintained around 17-18% level with upside trigger

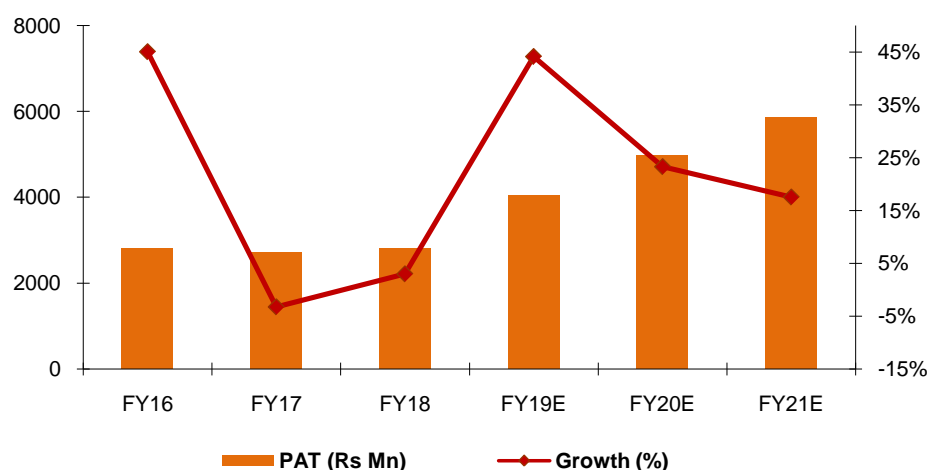
The restructuring exercise undertaken by N-Tech management, has enabled the company to increase its margins from 15.6% in Q1FY18 to 18.6% in its last reported quarter of Q3FY19. N-Tech expects this 18% margin to be the new normal for the company going forward with upside trigger. We expect N-Tech's EBITDA margin to be maintained in a band of 17-18% over the medium term.



Source: Company, Arihant Research

■ PAT to grow at 27.8% CAGR over FY18-FY21E

With 20.3% CAGR revenue growth over FY18-21E and stable EBITDA margin around 17-18% level, we expect N-Tech's PAT to grow from Rs 2803mn in FY18 to Rs 5854mn in FY21E, thereby registering a CAGR of 27.8% over FY18-21E. During the current financial year of FY19, N-Tech has continued to generate steady cash. In the last reported quarter of Q3FY19, the company added Rs 704mn in its cash balance.



Source: Company, Arianth Research

Q3FY19 and 9MFY19 Financial Performance

Rs Mn (consolidated)	Q3FY19	Q2FY19	Q3FY18	Q-o-Q	Y-o-Y	9MFY19	9MFY18	Y-o-Y
Net Revenue	9,717	9,074	7,565	7.1%	28.4%	27,040	22,026	22.8%
Employee cost	6,280	5,897	4,811	6.5%	30.5%	16,463	13,395	22.9%
Other Expenses	1,632	1,543	1,458	5.8%	11.9%	5,750	4,808	19.6%
EBITDA	1,805	1,634	1,296	10.5%	39.3%	4,827	3,823	26.3%
EBITDA margin %	18.6%	18.0%	17.1%	57	144	17.9%	17.4%	49
Other Income	5	215	5	-97.7%	0.0%	451	180	150.6%
Depreciation	314	319	311	-1.6%	1.0%	945	968	-2.4%
PBT	1,496	1,530	990	-2.2%	51.1%	4,333	3,035	42.8%
Tax Expense	445	363	163	22.6%	173.0%	1,107	661	67.5%
Effective tax rate %	29.7%	23.7%	16.5%	602	1,328	25.5%	21.8%	377
PAT	1,051	1,167	827	-9.9%	27.1%	3,226	2,374	35.9%
MI & Associates	-49	-49	-70			-144	-173	
Consolidated PAT	1,002	1,118	757	-10.4%	32.4%	3,082	2,201	40.0%
PAT margin %	10.3%	12.3%	10.0%	-201	31	11.4%	10.0%	141
EPS (Rs)	16.3	18.2	12.3	-10.4%	32.4%	50.2	35.8	40.0%

Source: Company, Arianth Research

Business Metrics of N-Tech over the Quarters

	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19
Vertical Mix									
BFS	18%	18%	17%	17%	17%	16%	17%	16%	15%
Insurance	24%	24%	25%	25%	26%	28%	29%	29%	30%
Travel and Transport	32%	31%	29%	27%	27%	26%	27%	27%	26%
Manufacturing and Media	26%	25%	29%	31%	27%	29%	27%	28%	29%
Government		2%			3%	1%	0%		
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%
Service Line Mix									
ADM	67%	66%	66%	64%	65%	66%	68%	68%	68%
IP assets	7%	6%	6%	7%	7%	7%	7%	6%	6%
Managed services	17%	17%	18%	18%	19%	19%	19%	18%	18%
SI and PI	4%	6%	5%	6%	5%	4%	3%	4%	4%
BPO	5%	5%	5%	4%	4%	4%	3%	4%	4%
Total	100%	100%	100%	99%	100%	100%	100%	100%	100%
Geography Mix									
USA	48%	48%	49%	50%	50%	48%	50%	49%	49%
EMEA	34%	33%	32%	29%	30%	32%	32%	34%	33%
ROW	18%	19%	19%	21%	20%	20%	18%	17%	18%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%
Billable People									
Onsite	1857	1877	1984	2040	2018	2088	2217	2369	2408
Offshore	6180	6189	6164	6156	6217	6500	6684	6815	6881
Total	8037	8066	8148	8196	8235	8588	8901	9184	9289
Sales and marketing (Ex-GIS)	139	133	137	135	147	145	131	123	114
sales and marketing (GIS)	82	81	85	85	85	85	90	94	94
Others	551	573	593	606	614	605	642	624	647
Total	8809	8853	8963	9022	9081	9423	9764	10025	10144
New Client Addition									
USA	1	1	5	2	4	2	5	5	8
EMEA	1	3	1	2	2	4	3	3	0
APAC	1	1	3	3	2	1	1	2	2
India							0	0	0
Total	3	5	9	7	8	7	9	10	10
Between 1 mn - 5mn	55	55	52	55	59	60	63	63	62
5mn-10 mn	10	10	14	13	12	13	14	18	20
>10mn	8	8	6	6	7	7	7	7	8
Total	73	73	73	74	78	80	84	88	90
Repeat business	90%	88%	96%	91%	91%	89%	96%	89%	88%

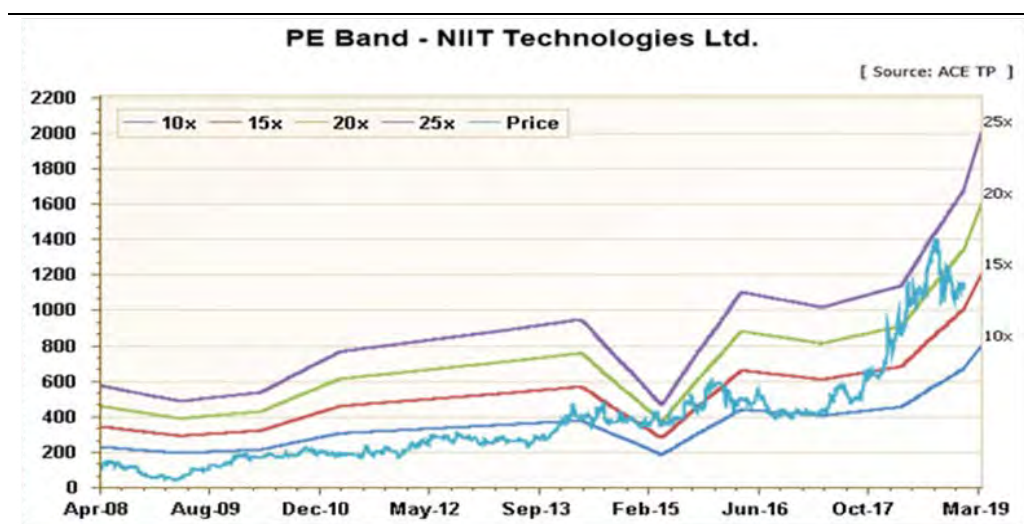
Future Outlook

The Indian IT industry's sustained and profitable growth in the face of a challenging environment is, to a large extent, due to the talent, skills and delivery capabilities that industry players have been able to build over the years, as well as the willingness to embrace change and adapt to evolving industry and technology trends. The outlook for the Indian IT Services sector remains positive, with NASSCOM expecting continued growth in IT-BPM exports during FY19, in the range of about 7% to 9%.

N-Tech's differentiated business model, recognition in the market place as a competent solutions provider, domain specialisation, IP assets and long-standing relationships with several key clients has been enabling it to deliver growth in a highly competitive environment. The company intends to stay the course in terms of following its strategy to 'Focus and Differentiate'. N-Tech is also well-regarded for its people practices and has significantly restructured its operations from a geo-centric to a vertical-centric organisation. These factors are expected to support the company's efforts to maintain its competitive edge in the market.

Valuations

At CMP of Rs 1225, N-Tech is trading at FY19E, FY20E and FY21E, P/E multiples of 18.7x, 15.1x and 12.9x respectively. If we look at the average P/E band of N-Tech for the last 10 years then the stock has traded at an average P/E of 10x. IT stocks have always been reasonably valued by the street despite their secular growth oriented business model and ability to generate positive free cash flows. The top tier IT companies like TCS, Infosys, and Wipro had commanded relatively better multiples in the range of 18-20x compared to their mid cap peers. Only in CY18, IT stocks have started outperforming the market due to US\$ tailwind (rupee depreciation) and robust US economy. As a result, mid cap IT stocks like N-Tech, MindTree etc. got re-rated and started commanding relatively better multiples of 15-20x compared to 10x earlier. This is mainly due to their superior growth outlook and improving margins. We believe N-Tech will get further re-rated going forward due to the recent steps the company has taken to improve its sales momentum through large deal wins and significant expansion in its margin profile. Based on this rationale, we value the stock at a FY21E target P/E multiple of 16.5x, which yields a target price of Rs 1570 per share. We are bullish on the future prospects of N-Tech and initiate coverage on the stock with a BUY rating and a target price of Rs 1570 (16.5x FY21E earnings), which gives an upside potential of 28.2%.



Source: Company, ACE Equity, Arihant Research

Peer Comparison

N-Tech's closest peer companies are Hexaware, Mphasis, MindTree and Tech Mahindra. In the following table we have compared NIIT Technologies with its peers on key parameters.

Company Name (FY20E estimates)	Price (Rs)	Sales (Rs Mn)	EBITDA (Rs Mn)	EBITDA Margin (%)	PAT (Rs Mn)	EPS (Rs)	P/E (x)	P/BV (x)	ROE (%)
Hexaware Tech	333	59180	9649	16.3	7333	23.7	14.0	3.3	25.8
Mphasis Tech	868	88280	15566	17.6	12023	63.4	13.7	2.8	21.1
NIIT Technologies	1225	45053	7929	17.6	4981	81.0	15.1	3.4	22.5
Mindtree	887	81434	13336	16.4	8896	54.2	16.4	3.9	23.9
Tech Mahindra	719	386074	70439	18.2	47539	53.3	13.5	2.6	20.8

Source: Company, Bloomberg, Arihant Research

Consolidated Financials

Income Statement (Rs mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
Revenues	26,824	28,021	29,915	37,287	45,053	52,042
<i>Change (%)</i>	13.1%	4.5%	6.8%	24.6%	20.8%	15.5%
Operating Costs	391	140	317	186	451	520
Gross Profit	26,433	27,881	29,598	37,101	44,602	51,522
Employee Costs	15,386	16,513	17,601	21,813	26,446	30,497
Other Expenses	6,288	6,573	6,983	8,837	10,227	11,762
Total Expenses	22,065	23,226	24,901	30,837	37,124	42,779
EBITDA	4,759	4,795	5,014	6,451	7,929	9,264
Other Income	205	269	391	559	541	520
Depreciation	1,101	1,277	1,274	1,184	1,354	1,482
Interest	49	60	94	87	102	110
PBT	3,814	3,727	4,037	5,739	7,014	8,191
Extra-ordinary	13	221	0	0	0	0
PBT after ext-ord.	3,801	3,506	4,037	5,739	7,014	8,191
Tax	832	785	949	1,435	1,754	2,048
<i>Rate (%)</i>	21.9%	22.4%	23.5%	25.0%	25.0%	25.0%
PAT	2,970	2,721	3,088	4,304	5,261	6,144
MI & Associates	-170	-220	-285	-265	-280	-290
Consolidated PAT	2,813	2,722	2,803	4,039	4,981	5,854
<i>Change (%)</i>	45.0%	-3.2%	3.0%	44.1%	23.3%	17.5%

Source: Company, Arianth Research

Balance Sheet (Rs mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
Sources of Funds						
Share Capital	612	614	615	615	615	615
Reserves & Surplus	15,296	16,251	17,125	19,581	21,522	23,775
Net Worth	15,907	16,865	17,740	20,196	22,137	24,390
Loan Funds	64	214	179	129	109	89
MI, Deferred Tax & other Liabilities	645	2,040	2,191	2,191	2,191	2,191
Capital Employed	16,616	19,119	20,110	22,516	24,437	26,670
Application of Funds						
Gross Block	12,863	10,880	12,540	13,540	15,040	17,040
Less: Depreciation	4,659	2,404	3,108	4,292	5,646	7,128
Net Block	8,205	8,476	9,432	9,248	9,394	9,912
CWIP	167	0	7	7	7	7
Other Non-current Assets	170	120	134	134	134	134
Deferred Tax Assets	259	971	1,231	1,231	1,231	1,231
Net Fixed Assets	8,801	9,567	10,804	10,620	10,766	11,284
Investments	740	3,236	3,066	2,966	2,866	2,766
Debtors	5,901	4,680	5,858	7,151	8,640	9,981
Inventories	3	3	3	3	6	7
Cash & Bank Balance	3,362	4,075	4,183	6,095	7,327	8,568
Loans & Advances & other CA	3,685	2,895	2,784	3,575	4,320	4,990
Total Current Assets	12,950	11,653	12,828	16,824	20,294	23,546
Current Liabilities	3,686	3,837	5,138	7,662	9,257	10,694
Provisions	2,189	1,500	1,450	232	232	232
Net Current Assets	7,076	6,316	6,240	8,930	10,804	12,620
Total Assets	16,616	19,119	20,110	22,516	24,437	26,670

Source: Company, Arianth Research

Cash Flow Statement (Rs mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
PBT	3,814	3,727	4,037	5,739	7,014	8,191
Depreciation	1,101	1,277	1,274	1,184	1,354	1,482
Interest & others	-327	-429	-582	-737	-719	-700
Cash flow before WC changes	4,589	4,575	4,729	6,186	7,649	8,974
(Inc)/dec in working capital	-485	1,860	252	-778	-642	-575
Operating CF after WC changes	4,104	6,435	4,981	5,408	7,007	8,398
Less: Taxes	-832	-785	-949	-1,435	-1,754	-2,048
Operating Cash Flow	3,272	5,650	4,032	3,973	5,254	6,350
(Inc)/dec in F.A + CWIP	-1,465	-766	-1,237	-1,000	-1,500	-2,000
(Pur)/sale of investment	-186	-2,496	170	100	100	100
Cash Flow from Investing	-1,651	-3,262	-1,067	-900	-1,400	-1,900
Free Cash Flow (FCF)	1,682	5,546	3,069	2,973	3,754	4,350
Loan raised/(repaid)	15	150	-35	-50	-20	-20
Equity raised	1	2	1	0	0	0
Interest & others	-356	-1,089	-2,013	101	-1,107	-1,434
Dividend	-612	-738	-810	-1,212	-1,494	-1,756
Cash Flow from Financing Activities	-951	-1,674	-2,857	-1,161	-2,622	-3,210
Net inc /(dec) in cash	670	713	108	1,912	1,232	1,241
Opening balance of cash	2,692	3,362	4,075	4,183	6,095	7,327
Closing balance of cash	3,362	4,075	4,183	6,095	7,327	8,568

Source: Company, Arianth Research

Key Ratios

Year End-March	FY16	FY17	FY18	FY19E	FY20E	FY21E
Per share (Rs)						
EPS	46.0	44.3	45.6	65.7	81.0	95.2
CEPS	64.0	65.1	66.3	84.9	103.0	119.3
BVPS	260.0	274.7	288.5	328.4	359.9	396.6
DPS	10.0	12.0	13.2	19.7	24.3	28.6
Div. Payout (%)	0.2	0.3	0.3	0.3	0.3	0.3
Valuation (x)						
P/E	26.6	27.6	26.9	18.7	15.1	12.9
P/CEPS	19.1	18.8	18.5	14.4	11.9	10.3
P/BV	4.7	4.5	4.2	3.7	3.4	3.1
EV/EBITDA	15.1	14.9	14.2	10.8	8.6	7.2
Dividend Yield (%)	0.8%	1.0%	1.1%	1.6%	2.0%	2.3%
Return ratio (%)						
EBITDA Margin	17.7%	17.1%	16.8%	17.3%	17.6%	17.8%
PAT Margin	10.5%	9.7%	9.4%	10.8%	11.1%	11.2%
ROE	17.7%	16.1%	15.8%	20.0%	22.5%	24.0%
ROCE	22.0%	18.4%	18.6%	23.4%	26.9%	29.2%
Leverage Ratio (%)						
Total D/E	0.0	0.0	0.0	0.0	0.0	0.0
Net D/E	-0.2	-0.2	-0.2	-0.3	-0.3	-0.3
Turnover Ratios						
Asset Turnover (x)	1.6	1.5	1.5	1.7	1.8	2.0
Inventory Days	2	8	3	5	5	5
Receivable Days	80	61	71	70	70	70
Payable days	80	70	80	75	75	75

Source: Company, Arianth Research

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Stock Rating Scale

BUY
ACCUMULATE
HOLD
NEUTRAL
REDUCE

Absolute Return

>20%
12% to 20%
5% to 12%
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