

Tech Mahindra

6 November 2019

Reuters: TEMPL.BO; Bloomberg: TECHM IN

Strong TCV due to the AT&T win; Decent 2Q: Cashflow strained

Tech Mahindra (TML) has presented a good set of numbers for 2QFY20 with a constant currency (CC) revenue growth of 4.1% QoQ (our estimate +2.3%). USD revenue was 1.5% above our estimate. The 'Enterprise' segment showed a strong growth of 5.6% QoQ in CC with broad-based traction coming from all verticals driven by Digital transformation. This is after a few quarters of fairly poor growth from this segment. Communication segment grew by 2% QoQ in CC terms. TML recorded an all-time high TCV of \$1.49bn (largely driven by the AT&T deal of ~US\$800mn over 6.5 years. See our note [AT&T deal, A showcase deal for the 5G Telco world?](#)). In enterprise segment, growth came from verticals like TME (Technology, media and entertainment) and RTL (Retail, Transport & Logistics) that grew by 10%/16.5%, QoQ, in USD, respectively. BFSI also recovered, growing 4.8% QoQ after de-growth in 1QFY20. All the verticals showed good growth except Manufacturing which de-grew by 4.2% QoQ due to slowdown in Automobile industry, especially in Europe. The EBIT margin performance was good at 12.8% (100bps higher than our estimate), up 130bps QoQ driven by operational efficiency (lower SG&A), lower visa costs and synergy benefits (HCI and Healthcare vertical). With incremental revenue from the new AT&T deal and continued traction in enterprise (though not at 2Q levels) 2H growth looks robust. But, with a relatively poor EBIT margin performance in 1H (~12%) and likely transition costs connected with AT&T and other large deals in 2HFY20, we think EBIT margin in FY20 may fall short of that of FY19 by 100bps at least (~14% versus 15% in FY19). TML has given a FY21 guidance of pulling up margins to the 15% level clocked in FY19 without committing to a specific revenue number that year. TML expects both Communication and Enterprise segments to show market rate growth in FY21. Delivering on both growth and margins in our view is going to be a challenge for TML as it has not been able to do that in the recent past. Post 2QFY20, we have tweaked our revenue and margin estimates upwards (for FY20/FY21/FY22) but still remain below the company guidance on the latter. We maintain Sell rating on TML with a target price (TP) of Rs575 based on a target multiple of 9.9x September 2021E EPS. The target multiple is at a 40% discount to TCS and reflects TML's structural weakness because of its less diversified revenue mix, higher client concentration, slower organic growth, lower margins, lower RoIC and behind-the-curve investments in automation and digital. Our Sell rating is driven by the view that industry will witness P/E de-rating in a no-growth year we expect in FY21.

5G pick-up by FY21: TML commentary around 5G has been that that B2B firms will be the first beneficiaries of 5G and consumer-centric adoption may be slower. TML is of the view that the contribution of 5G will be fairly small in FY20 (a warm-up year). But the management is optimistic on the prospects of 5G going forward and sees it as a big opportunity. According to the management, while during the introduction of 4G, there were 2-3 telecom operators who were deploying the technology, now there are ~30 operators across the world who have started the trials and partially deploying 5G technology. The main traction is coming from the US where the Telecom companies have a clear roadmap for the next two years while the companies in Europe are still working out their strategy around 5G. TML expects both new investments as well as repurposing of current spends to drive 5G growth going forward from the customer's side.

SELL

Sector: Information Technology

CMP: Rs775

Target price: Rs575

Downside: 26%

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Key Data

Current Shares O/S (mn)	965.0
Mkt Cap (Rsbn/US\$bn)	747.4/10.6
52 Wk H / L (Rs)	847/607
Daily Vol. (3M NSE Avg.)	3,049,725

Price Performance (%)

	1 M	6 M	1 Yr
Tech Mahindra	9.4	(5.2)	11.2
Nifty Index	6.6	1.7	13.2

Source: Bloomberg

Y/E March (Rsmn)	2QFY19	1QFY20	2QFY20	YoY (%)	QoQ (%)	2QFY20E	Dev (%)
Net Sales (USD mn)	1,218	1,247	1,287	5.7	3.2	1,268	1.5
Net Sales	86,298	86,530	90,699	5.1	4.8	89,110	1.8
Direct Cost	56,923	61,642	63,893	12.2	3.7	62,881	1.6
Gross Margin	29,375	24,888	26,806	(8.7)	7.7	26,229	2.2
% of Sales	34.0	28.8	29.6	-	-	29.4	-
SG&A	13,189	11,747	11,797	(10.6)	0.4	12,461	(5.3)
% of Sales	15.3	13.6	13.0	-	-	14.0	-
EBITDA	16,186	13,141	15,009	(7.3)	14.2	13,768	9.0
EBITDA Margin (%)	18.8	15.2	16.5	-	-	15.5	-
Depreciation & Amortisation	2,944	3,213	3,415	16.0	6.3	3,232	5.6
EBIT	13,242	9,928	11,594	(12.4)	16.8	10,535	10.1
EBIT Margin (%)	15.3	11.5	12.8	-	-	11.8	-
Interest	388	454	383	(1.3)	(15.6)	433	(11.5)
Other Income	1,751	3,413	2,163	23.5	(36.6)	1,693	27.8
PBT	14,605	12,887	13,374	(8.4)	3.8	11,795	13.4
Exceptional Item (as Reported)	(133)	-78	3	-	-	(150)	-
Provision for Tax	3,914	3,318	2,265	(42.1)	(31.7)	2,831	(20.0)
Effective Tax Rate	26.8	25.7	16.9	-	-	24.0	-
Minority share in Profit / Loss	84	102	127	51.2	24.5	52	144.2
PAT (Reported)	10,474	9,593	11,239	7.3	17.2	8,866	26.8
Exceptional Item (Adj-post Tax)	(133)	(78)	3	-	-	(150)	-
PAT (Adjusted)	10,341	9,515	11,242	8.7	18.2	8,716	29.0
NPM (%)	12.0	11.0	12.4	-	-	9.8	-

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 1: Key financials

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Revenues	307,730	347,421	382,913	410,364	431,021
YoY (%)	5.6	12.9	10.2	7.2	5.0
Gross Profit	92,431	113,831	115,098	122,987	125,964
% of sales	30.0	32.8	30.1	30.0	29.2
EBIT	36,321	52,076	53,866	60,124	62,511
% of sales	11.8	15.0	14.1	14.7	14.5
PAT	38,001	42,735	46,434	49,733	53,430
YoY (%)	35.1	12.5	8.7	7.1	7.4
FDEPS	42.8	48.1	52.3	56.0	60.2
RoE (%)	21.5	21.9	21.5	20.4	19.3
RoCE (%)	17.2	22.8	21.9	21.8	20.3
RoIC (%)	25.8	37.9	36.4	36.8	38.4
P/E (x)	17.9	15.9	14.6	13.7	12.7
P/BV (x)	3.6	3.3	3.0	2.6	2.3

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Change in our estimates

Change in estimates	New			Old			% Change		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
INR/USD	71.8	74.6	76.4	71.8	74.6	76.4	-	-	-
USD Revenue (USD mn)	5,327	5,505	5,642	5,285	5,461	5,597	0.8	0.8	0.8
Revenue (Rsmn)	382,913	410,364	431,021	379,702	407,129	427,623	0.8	0.8	0.8
EBIT (Rsmn)	53,866	60,124	62,511	51,175	55,989	58,971	5.3	7.4	6.0
EBIT Margin (%)	14.1	14.7	14.5	13.5	13.8	13.8	-	-	-
PAT (Rsmn)	46,020	49,373	53,070	43,337	47,831	52,278	6.2	3.2	1.5
EPS (Rs)	52.3	56.0	60.2	49.2	54.4	59.4	6.4	3.0	1.3

Source: Company, Nirmal Bang Institutional Equities Research

View on Indian IT services sector: We went back to being cautious on the Indian IT sector in late December 2018 (see report: [Street Is Not Factoring Even A Soft Landing; We Downgrade](#)) after being 'Tactically bullish' on it through most of 2018. This is based on: (1) Consensus not factoring in significantly softer growth in FY21 as the best demand environment since 2008-09 is largely behind us with corporate capex in both the US and Europe likely to have peaked in 2018. (2) Global BFSI customers could witness pressure on margins from a flattened/inverted yield curve and negative yields across a large part of European bonds (see our recent note [Global BFSI malaise](#)) and could therefore curtail IT spending (3) Pressure on cost structure because of tariffs levied on imports from China impacting US manufacturers. (4) Front-office capabilities in digital still largely eluding Indian IT services players, leading to inability to tap into the marketing budgets of customers in a material way. The focus has been on the technology-intensive back-end of digital where we believe the field is relatively more crowded. (5) 'Automation at scale' in legacy services constricting the opportunity being addressed by the Indian Industry. This is driven by explosive growth in both intelligent and robotic process automation software industry. (6) Capital return to shareholders not being as potent a stock driver as it was earlier as the cash hoard is shrinking after two to three rounds of buyback over the past four years. Besides, recent taxation introduced on buybacks could be a dampener (7) Talent pressure in the US in new age services because of a tighter H1-B visa regime. We reiterate our no-industry-growth-in-FY21 call initiated in March 2018. We base this scenario on an explicit expectation of a soft landing in the US (0%-1.5% real GDP growth) in 2020. We believe consensus is expecting mid-high single-digit revenue growth in FY21 for the industry, implicitly assuming continued robust growth in the US (2%-2.5%). It is our belief that the street will converge with our no-growth expectations over time. Until the market prices in this scenario, we believe technical factors are not likely to hold the sector up. A hard landing (recession) - not our current base case - could lead to single-digit negative growth for the sector. Just as outperformance of the sector in 2018 was driven largely by P/E multiple expansion in the belief that growth is going to accelerate, we believe the downside in 2019 will be driven by P/E multiple deflation as investors begin to re-calibrate growth expectations on FY20-FY22. We prefer large-caps over mid-caps. The faster growth shown by select mid-caps is a case of 'rising tide lifting all boats', a smaller base and lower exposure to legacy services. But as digital demand shifts from the front to back, we believe that traditional large Indian companies will be in a better position to capture the market. We would advise investors to focus on sustainability and not overpay for a riskier business model - some companies have seen client concentration rising over the past two years.

Exhibit 3: Vertical-based USD QoQ and YoY revenue growth in 2QFY20

Verticals	Contribution to Revenue (%)	Growth-QoQ (%)	Growth-YoY (%)
Communication (Telecom)	41.1	1.0	4.6
Manufacturing	18.0	(4.2)	(5.4)
Technology, media & entertainment	8.1	10.0	17.2
Banking, financial services & insurance	13.0	4.8	1.8
Retail, transport & logistics	7.0	16.5	13.8
Others	12.8	11.0	20.8
Total	100.0	3.2	5.7

Source: Nirmal Bang Institutional Equities Research

Exhibit 4: Geography- based USD QoQ and YoY revenue growth in 2QFY20

Geography	Contribution to Revenue	Growth-QoQ (%)	Growth-YoY (%)
North America	48.5	5.2	9.0
Europe	26.7	(0.2)	(4.7)
Rest of World	24.9	3.6	12.4
Total	100.1	3.2	5.7

Source: Nirmal Bang Institutional Equities Research

2QFY20 analyst call highlights

- Key operating performance:** Revenue in 2QFY20 in USD terms increased 3.2% QoQ basis and grew by 5.7% YoY. All geographies increased QoQ, except Europe (de-grew by 0.2%) with US and RoW growing by 5.2%/3.6%, respectively. There was strong YoY revenue growth from RoW (12.4% YoY in USD terms). Among verticals, the growth in Communication stood at 4.6% YoY in USD terms. Technology, Media and Entertainment (TME) grew by 17.2% YoY. Retail, Transport and Logistics, BFSI and Others verticals grew by YoY by 13.8%/1.8%/20.5%, respectively, in USD terms. The growth in retail was on the back of series of small engagements where TechM is not in direct competition with the other Tier-I players. Except the 'Manufacturing' vertical (which declined by 5.4% YoY in USD terms), all verticals grew on a YoY basis. Management said that the decline in Manufacturing was due to softness from the Auto sub segment and in particular due to slowdown in Europe. TML believes that Manufacturing vertical has bottomed out. Also, management said that the BFSI deal pipeline is healthy too.
- Enterprise bounce back:** Enterprise was soft since last 2 quarters, owing to slowdown in Automobile and BFSI industries. Healthcare and BFSI have made a comeback and Hi-Tech has also gained good momentum in the Enterprise segment. There is momentum from synergy in the portfolio companies too. The recovery in Enterprise has come on the back of Infrastructure and cloud migration deals. There have been deal wins in platforms as well.
- Digital:** It formed 39% of revenue, up 11.8% QoQ which is an industry leading figure. But the management indicated that the EBITDA margins in Digital deals is only marginally better than the rest of the business due to ongoing investments, which explains the lower overall margins despite a high growth in digital.
- BPO growth:** BPO revenue grew by ~4.9% QoQ and 27.8% YoY in 2QFY20 vs 2.7% QoQ and 25.9% YoY in USD terms, in 1QFY20. Most of TML's BPS work is centered around enhancing customer experience through RPA, Chat-bots and Social Media Tools. TML says that competition is less in BPO as TCS, Wipro, etc are largely playing on platforms. Contrary to IT services, there has been headcount addition in BPO in 2QFY20 by ~7200. This is partially due to increased sub-contracting on-site and partially, due to an increased focus on digital growth which grew by 11.8% QoQ.
- QoQ Margin improvement:** After last quarter's margin decline of 150 bps YoY and 390 bps QoQ, the seven-quarter margin recovery journey stopped. But 2QFY20 saw some margin recovery with 130 bps QoQ margin uptick, 100bps above our estimate of 11.8%, standing at 12.8%. The margin improved because of factors like: (1) operational efficiency-100bps. (2) lack of visa costs (3) synergy benefits from the portfolio companies offset by salary hike of a part of workforce- 30bps. The YoY decline in margins was mainly due to currency acting as a tailwind in 2QFY19 vs a headwind in 2QFY20. The management has indicated that the margin will decline by 150-200bps going forward in 2HFY20 (YoY). Management

indicated that it has levers to pull up margins from the current low levels but that will be dependent on conversion of deals. It hinted at EBIT margin number of 15% for FY21 without indicating a specific revenue number for that year. TML said it will leverage utilization, pyramid optimization, synergy of the portfolio companies and automation to push up margins from 2QFY20 levels. Countervailing forces will include investments in Digital and transition costs on large deals. In FY19, the big positive in TML was the strong margin expansion.

- **Commentary on Communication vertical:** The revenue from this vertical accounted for ~41% of total. It increased 4.6% YoY and 1% QoQ in USD terms. The large deal win from AT&T will propel the growth in this vertical in the next two quarters. The management is confident of the pipeline in this vertical. The deal wins in Communication vertical mostly centered on digital transformation and increasing operational efficiency of telecom companies. Management indicated that M&A among its clients will lead to more work for TML. Work is going to be mainly around migration, integration, business process rationalisation, farming of network assets and providing inventory management support.
- **Highest ever TCV:** The TCV increased QoQ from US\$475mn in 1QFY20 to ~US\$1490mn in 2QFY20 with ~US\$1bn from the Telecom side and US\$0.49bn coming from the communication side. The high TCV has come on the back of AT&T deal (likely ~US\$800mn in size). TCV has grown by ~1.7x YoY and broken free from the earlier range of US\$275mn-US\$350mn. The deal wins are broad-based across geographies and verticals. AT&T deal is for a duration of 6.5 years and hence the annualized revenue run rate will be lower.
- **Nature of deal wins:** Management stated that deal wins are highly transformational in nature. The offerings are built on pillars such as: (1) Transformation of network infrastructure (2) Transformation of underlying software architecture (3) Offerings across enterprise and consumer markets (4) Transforming and increasing operational efficiency of telecom players and (5) Humungous increase in data consumption. Also, management stated that deal wins were coming from all geographies and hence it was broad-based growth. Among verticals, Healthcare, Banking, and Retail have a lot of focus on the analytics related to retail customer experience.
- **DSO shoots up:** DSOs further (including unbilled revenue) increased sharply to 114 days in 2QFY20 from 110 in 1QFY20. This is high as per industry trend. Typically, these have been in the range of 75-90 for its peers. High DSOs were explained by longer credit cycles of telecom clients, the geography mix (RoW being higher) and currency problems to some extent. DSOs have shot up due to large unbilled revenues which the company has tried to reduce to an extent by converting some unbilled revenues to billed revenues and the company is trying to bring it down further. The FCF for the quarter was at 50% of the net profit which is fairly poor number.
- **Mad*Pow acquisition:** TML acquired a Digital boutique company in US called “Mad*Pow” with a capability in customer experience, human centered design and understanding of behavioral science, which will give Tech Mahindra edge in digital transformation projects. TML has acquired 65% stake in the company which will have a FY20 revenue of US\$17.5mn and have margins in mid-teens. The balance 35% will be acquired over the next three years. We understand that it has paid US\$17.5mn for its 65% stake. Mad*Pow has a 70-member team and is focused on the verticals of Financial Services, Healthcare and Media. The acquisition was completed in this quarter.
- **Other conference-call highlights:**
 - HCI – TML’s aim is long term multiyear contract from providers. HCI has begun to show traction from synergy with the Healthcare vertical at Tech Mahindra. The revenue streams from HCI have also stabilized now due to the synergies and the impact of seasonality is going to be lower.
 - Attrition rate in 2QFY20 stood at 21%, flat vis-à-vis 21% in 1QFY20. Management stated that attrition in top talent is much lower than the overall average. TML is giving wage hikes that are higher than before. It had also introduced a career transformation program to control attrition.
 - In 2QFY20, the company’s employee utilization (including trainees) level increased vis-à-vis 80% in 1QFY20 and stood at 82%.
 - Management stated that a large part of sub-contractor expenses came from hiring onsite. Sub-contractor expenses are currently at a higher than industry level of ~15.1% versus 14.1% in 1QFY20. The increase in sub-contracting costs is due to demand of special skills for the TME vertical for a short duration.

- One client was added to >US\$50mn bucket and the >US\$20mn bucket remained flat, QoQ. One Client dropped out of the >US\$10mn bucket. The share of Top 5 accounts increased from 21.4% in 1QFY20 to 21.6% in 2QFY20.
- TML in 2QFY20 had tax rate of ~17%. Going forward the normalized tax rate will be 25%-26%.
- Cash and cash equivalents was slightly north of US\$1 billion during the quarter versus US\$1.2 billion as of 30th June, as TechM paid out a dividend of about US\$229 million and also paid out money for the 'Mad*pow' acquisition.

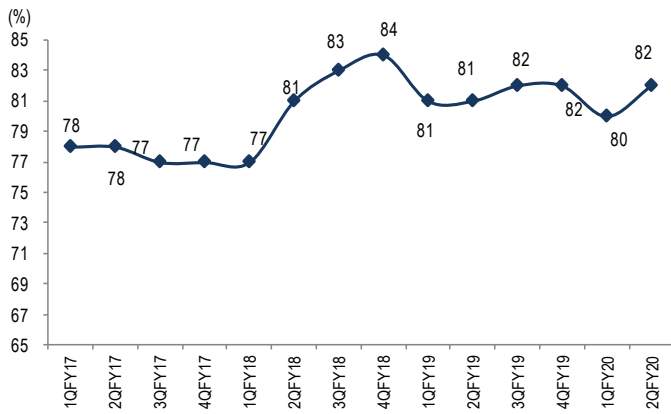
BORN Acquisition:

- Tech Mahindra has acquired BORN Group, a New York-based digital content and production agency, for US\$95 million in an all-cash deal. According to TML, Born Group is the largest independent, integrated agency for strategy, creative content and commerce offerings with strong technology capabilities. The acquisition is expected to enhance Tech Mahindra's Transformation consulting capabilities through addition of creative and design skills, technology and analytics platforms and commerce expertise
- BORN's services include consulting, content creation, maintenance and hosting services, digital and social marketing, among others. It has clients such as Google, Tata, Red Bull and TAG Heuer. It is expected to give further traction to the Digital Retail-CPG revenues. BORN has offices in New York City, London, Hong Kong, Singapore and India and employs over 1,100 people. BORN recorded a revenue of US\$50 million in 2018, up from US\$39 million and US\$36 million in the preceding two years. Tech M will buy BORN's India unit, while Tech Mahindra Pte, the IT firm's Singapore arm, will takeover other entities. The deal is expected to close by 15 November 2019. While the enterprise value of BORN has been pegged at US\$95 million, the deal includes a future payout of US\$25 million linked to achievement of financial targets for the year to December, 2019.

AT&T Deal

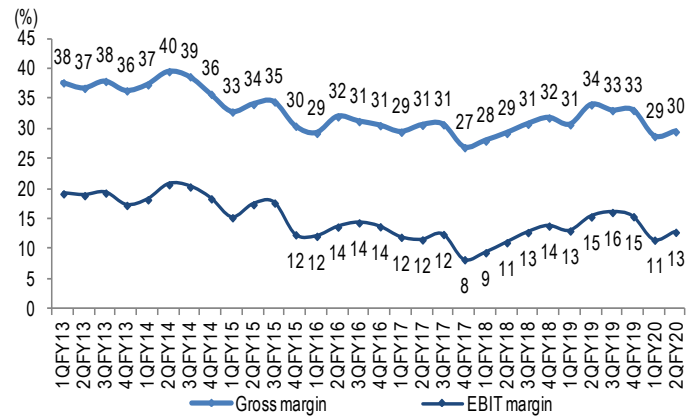
- **The deal details:** TML will assume management of many of the applications which support AT&T's network and shared systems. This would help AT&T to focus on building an advanced software defined 5G network, and migrate the majority of its non-network workloads to the public cloud by 2024. Based on comments by management in the media and other sources, we believe the deal size will likely be US\$800mn-US\$1bn spread over 6.5 years. With this deal, we believe AT&T, which is likely TML's second largest customer in Communications vertical (behind BT), will become the largest by 3QFY20 when we believe revenue from the deal would start kicking in. We believe this deal would involve rebranding of AT&T employees and subcontractors. TML has indicated that the deal would be margin dilutive for 2-3 quarters and would deliver corporate level margins over the life of the contract.
- **AT&T's relationship with TML:** This started in 2004 with the outsourcing from AT&T rising strongly over the years. The agreement that got signed at that time gave AT&T call options to acquire 8% of the company in 2010 at a predetermined exercise price. This was linked to the quantum of outsourcing done by AT&T to TML. The options were exercised by AT&T in 2010 only for the shares to be divested by AT&T almost immediately. Just as the share of BT in the revenue mix continued to dip over the years the share of AT&T continued to rise. But, we believe it remained the second largest communication services customer behind BT.
- **AT&T has struck multiple deals in recent months:** These have been with IBM, Microsoft and Dell. Applications which are part of the AT&T Business – division that caters to enterprise customers of AT&T – will be shifted to IBM cloud. This deal also likely revolves around the capability of handling multi-cloud and hybrid clouds acquired through the Red-Hat acquisition. AT&T seems to have also hedged its bets by a tie-up with Microsoft to use its Azure platform. It seems to be working with Dell with help connected with the edge part of its likely 5G network. On 5G itself, AT&T seems to have spread its risks by involving three partners on the equipment side – Ericsson, Nokia and Samsung. Indian companies can aspire to strike subcontracting relationships with these players as the 5G networks get rolled out globally over the next 5 years.

Exhibit 5: Employee utilisation (including trainees) increases in 2QFY20



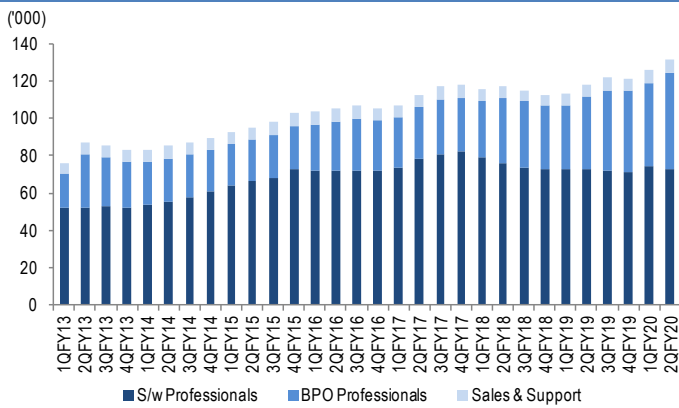
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 6: EBIT margin increases in 2QFY20 owing to decline in SGA



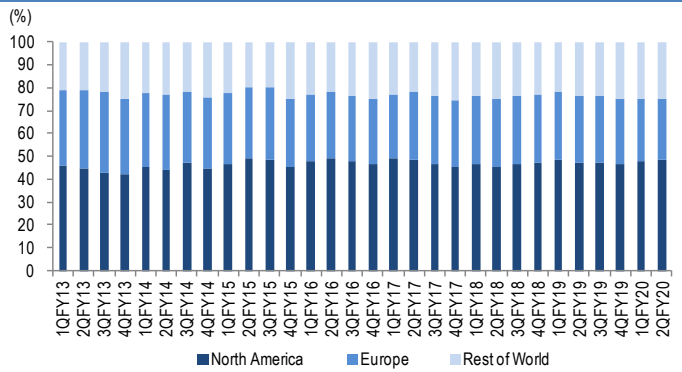
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: BPO headcount increases



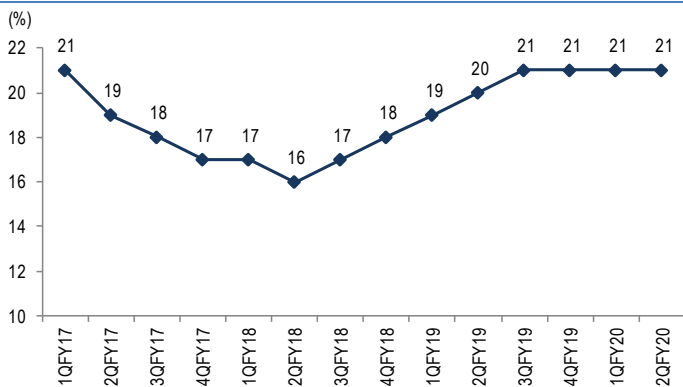
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Revenue contribution in terms of geographies



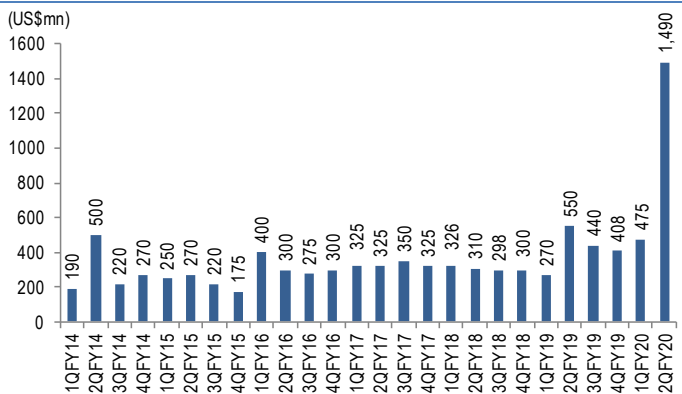
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: Attrition rate remains high



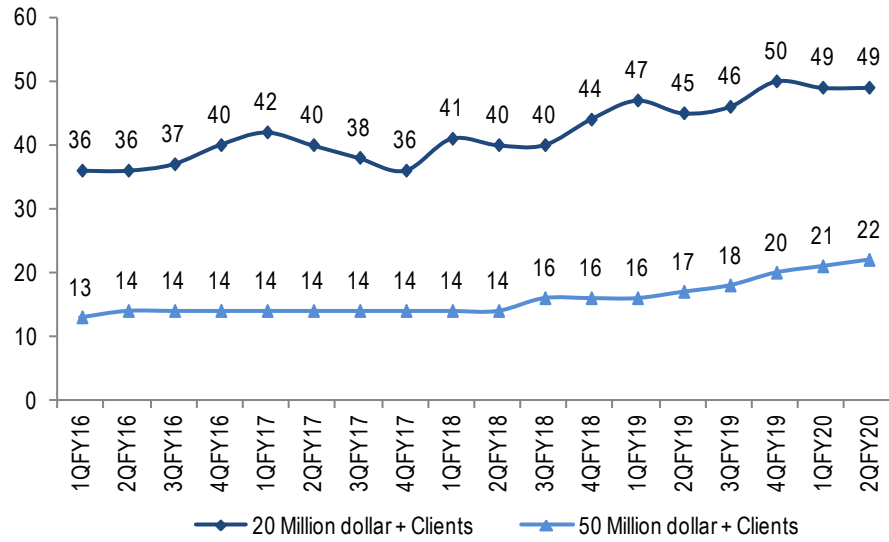
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 10: TCV of large deals increases QoQ



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 11: >US\$50mn bucket witnessed addition of clients; >US\$20mn bucket remains flat



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 12: Quarterly snapshot

Year to 31 March (Rsmn)	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
INR/USD	66.47	64.44	64.45	64.35	64.64	67.51	70.68	71.11	70.32	69.42	70.3
USD Revenue (USD mn)	1131	1138	1179	1209	1244	1224	1218	1261	1268	1247	1287
INR Revenue	74,950	73,361	76,064	77,760	80,545	82,763	86,298	89,437	88,923	86,530	90,699
Gross Margin	20,165	20,543	22,275	23,953	25,660	25,423	29,375	29,592	29,441	24,888	26,806
SGA	11,178	11,196	11,218	11,306	11,541	11,854	13,189	12,366	13,054	11,747	11,797
EBITDA	8,987	9,347	11,057	12,647	14,119	13,569	16,186	17,226	16,387	13,141	15,009
Depreciation	2,835	2,468	2,653	2,742	2,986	2,808	2,944	2,836	2,704	3,213	3,415
EBIT	6,152	6,879	8,404	9,905	11,133	10,761	13,242	14,390	13,683	9,928	11,594
Other income (net)	2,379	4,106	3,223	2,251	4,513	1,114	1,751	806	1,671	3,413	2,163
PBT	8,213	10,615	11,241	11,815	15,119	11,570	14,472	14,706	14,801	12,809	13,377
Tax	2,552	2,698	2,847	2,570	2,810	2,457	3,914	2,638	3,535	3,318	2,265
Minority Share in profit/Loss	31	(68)	31	(187)	88	16	84	(39)	59	102	127
Exceptional Item	-	-	-	-	0	(118)	(133)	(132)	(272)	(78)	3
PAT Adjusted for exceptional items	5,630	7,985	8,363	9,432	12,221	9,072	10,438	12,083	11,142	9,369	11,240
YOY Growth (%)											
USD Revenue	10.6	10.3	10.0	8.3	10.0	7.6	3.3	4.3	1.9	1.9	5.7
INR Revenue	8.9	6.0	6.1	2.9	7.5	12.8	13.5	15.0	10.4	4.6	5.1
Gross Profit	(4.2)	0.7	1.4	3.1	27.3	23.8	31.9	23.5	14.7	(2.1)	(8.7)
EBITDA	(22.6)	(9.2)	3.3	6.6	57.1	45.2	46.4	36.2	16.1	(3.2)	(7.3)
EBIT	(34.8)	(16.8)	1.8	5.5	81.0	56.4	57.6	45.3	22.9	(7.7)	(12.4)
Net Profit	(37.2)	6.6	29.7	10.3	117.1	12.4	23.7	27.0	(10.5)	3.7	8.7
QoQ Growth (%)											
USD Revenue	1.4	0.6	3.6	2.5	2.9	-1.6	-0.48	3.5	0.5	(1.6)	3.2
INR Revenue	(0.8)	(2.1)	3.7	2.2	3.6	2.8	4.3	3.6	(0.6)	(2.7)	4.8
EBITDA	(24.3)	4.0	18.3	14.4	11.6	(3.9)	19.3	6.4	(4.9)	(19.8)	14.2
EBIT	(34.4)	11.8	22.2	17.9	12.4	(3.3)	23.1	8.7	(4.9)	(27.4)	16.8
Net Profit	(34.2)	41.8	4.7	12.8	29.6	(26.5)	15.2	15.8	(8.7)	(14.9)	20.7
Margins (%)											
Gross Margin	26.9	28.0	29.3	30.8	31.9	30.7	34.0	33.1	33.1	28.8	29.6
EBITDA	12.0	12.7	14.5	16.3	17.5	16.4	18.8	19.3	18.4	15.2	16.5
EBIT	8.2	9.4	11.0	12.7	13.8	13.0	15.3	16.1	15.4	11.5	12.8
PAT	7.5	10.9	11.0	12.1	15.2	10.8	12.0	13.4	12.3	10.8	12.4
SGA	14.9	15.3	14.7	14.5	14.3	14.3	15.3	13.8	14.7	13.6	13.0

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 13: Key metrics

Key Metrics	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
P and L (Rsmn)													
Revenue	71,674	75,575	74,950	73,361	76,064	77,760	80,545	82,763	86,298	89,437	88,923	86,530	90,699
EBITDA	10,701	11,865	8,987	9,347	11,057	12,647	14,119	13,569	16,186	17,226	16,387	13,141	15,009
PAT	6,447	8,550	5,630	7,985	8,363	9,432	12,221	8,979	10,341	11,975	10,935	9,311	11,242
Vertical Mix (%)													
Communication (Telecom)	48.4	47.3	46.3	45.2	43.7	42.8	41.6	39.6	41.5	41.1	42.7	42.0	41.1
Manufacturing	19.2	18.4	19.2	19.3	19.0	19.1	19.3	20.1	20.1	20.5	20.2	19.4	18.0
Technology, media & entertainment	7.2	6.4	6.2	6.0	5.9	6.5	7.3	7.2	7.3	7.0	7.5	7.6	8.1
Banking, financial services & insurance	11.5	13.1	14.1	14.4	14.1	13.3	13.0	13.6	13.5	13.4	13.1	12.8	13.0
Retail, transport & logistics	6.8	7.6	6.5	6.8	7.2	7.1	6.2	6.1	6.5	6.7	6.4	6.2	7.0
Others	6.8	7.1	7.7	8.3	9.9	11.3	12.6	13.4	11.2	11.3	10.2	11.9	12.8
Geographical Mix (%)													
North America	48.3	46.7	45.1	46.8	45.3	46.9	47.4	48.2	47.0	47.4	46.4	47.6	48.5
Europe	29.7	29.4	29.6	29.8	30.0	29.8	29.6	30.0	29.6	28.9	28.6	27.6	26.7
Rest of World	22.0	23.9	25.3	23.4	24.7	23.3	23.0	21.9	23.4	23.7	24.9	24.8	24.9
Delivery (%)													
Onsite	63.5	63.9	64.3	63.7	64.1	65.8	67.0	66.6	64.5	65.5	65.2	65.3	65.4
Offshore	36.5	36.1	35.7	36.3	35.9	34.2	33.0	33.4	35.5	34.5	34.8	34.7	34.6
Utilization (%) (including trainees)													
	78	77	77	77	81	83	84	81	81	82	82	80	82
Clients Concentration (%)													
Top 5 Clients	28.5	27.8	26.6	25.9	24.8	23.2	23.2	21.9	23.3	22.6	22.8	21.4	21.6
Top 10 Clients	39.9	38.4	37.6	36.3	35.1	33.2	32.7	32.5	32.7	31.6	32.0	30.7	31.5
Top 20 Clients	51.7	50.5	49.0	48.5	46.2	45.0	45.7	46.2	45.6	44.0	45.1	43.6	43.6
Number of Client													
1 USD mn +	341	356	354	377	390	389	392	396	407	416	425	429	437
5 USD mn +	120	128	134	139	147	154	156	154	157	157	156	160	155
10 USD mn +	66	65	71	74	81	83	85	86	86	88	83	81	80
20 USD mn +	40	38	36	41	40	40	44	47	45	46	50	49	49
50 USD mn +	14	14	14	14	14	16	16	16	17	18	20	21	22
Employees	112,886	117,095	117,693	115,980	117,225	115,241	112,807	113,552	118,391	121,842	121,082	125,773	131,522
Attrition (%)	19	18	17	17	16	17	18	19	20	21	21	21	21
Financial Metrics (USD mn)													
Revenue	1,072	1,116	1,131	1,138	1,179	1,209	1,244	1,224	1,218	1,261	1,268	1,247	1,287
EBITDA	160	175	137	145	171	197	217	200	227	245	235	190	212
EBIT	124	138	94	107	130	154	171	158	185	205	196	144	163
PAT	96	125	89	123	130	144	189	134	150	174	165	138	157
Per Capita (Annualised) - USD													
Revenue	37,999	38,126	38,446	39,252	40,237	41,968	44,121	43,120	41,159	41,391	41,872	39,662	39,148
EBITDA	5,680	5,978	4,646	4,994	5,835	6,838	7,702	7,031	7,663	8,033	7,757	6,039	6,442
EBIT	4,383	4,728	3,191	3,673	4,433	5,356	6,067	5,569	6,257	6,727	6,485	4,567	4,966
PAT	3,412	4,260	3,038	4,235	4,422	5,002	6,716	4,713	5,068	5,699	5,457	4,402	4,772

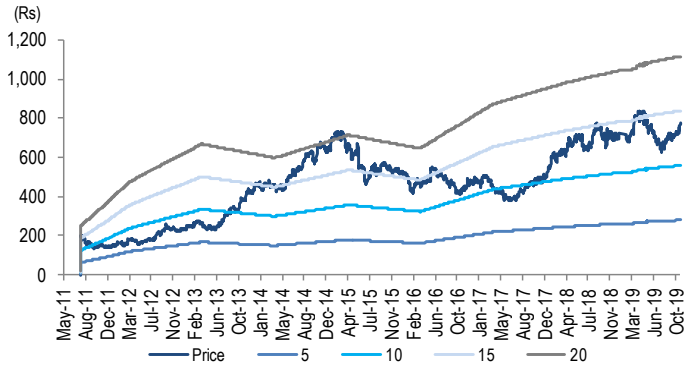
Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 14: YoY and QoQ growth of various parameters

QoQ Growth (%)	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20
By Geography (%)																	
North America	4.8	(1.9)	(1.3)	5.6	2.5	0.6	(2.1)	4.4	0.3	6.2	4.0	0.0	(3.0)	4.4	(1.6)	0.9	5.2
Europe	1.9	(1.0)	(0.6)	0.2	9.1	3.0	2.0	1.3	4.3	1.9	2.2	(0.3)	(1.8)	1.0	(0.5)	(5.0)	(0.2)
Rest of World	(2.2)	6.3	7.3	(6.9)	0.3	13.1	7.3	(6.9)	9.4	(3.3)	1.6	(6.3)	6.3	4.8	5.6	(2.0)	3.6
By Industry (%)																	
Communication (Telecom)	2.6	(2.7)	(0.0)	(2.5)	2.3	1.7	(0.8)	(1.8)	0.2	0.4	0.0	(6.4)	4.3	2.5	4.4	(3.2)	1.0
Manufacturing	(0.2)	2.8	0.8	6.8	10.3	(0.3)	5.8	1.1	2.0	3.1	4.0	2.5	(0.5)	5.6	(0.9)	(5.5)	(4.2)
Technology, media & entertainment	14.8	(9.4)	2.1	0.9	(0.2)	(7.5)	(1.8)	(2.6)	1.9	13.0	15.6	(3.0)	0.9	(0.8)	7.7	(0.3)	10.0
Banking, financial services & insurance	(1.9)	2.5	9.0	7.5	5.8	18.6	9.1	2.8	1.5	(3.3)	0.6	2.9	(1.2)	2.7	(1.7)	(3.9)	4.8
Retail, transport & logistics	(5.6)	13.7	(8.1)	5.8	8.8	16.3	(13.3)	5.3	9.7	1.1	(10.1)	(3.2)	6.0	6.7	(4.0)	(4.7)	16.5
Others	3.8	15.6	2.1	(3.1)	(4.5)	8.7	9.9	8.4	23.6	17.0	14.8	4.6	(16.8)	4.4	(9.3)	14.8	11.0
By Client classification (%)																	
Top 5 Clients	(0.9)	(12.2)	0.4	4.1	2.9	1.5	(3.0)	(2.0)	(0.8)	(4.1)	2.9	(7.1)	5.9	0.4	1.4	(7.7)	4.2
Top 10 Clients	(0.1)	(6.6)	(1.7)	3.5	3.7	0.2	(0.8)	(2.9)	0.2	(3.0)	1.4	(2.2)	0.1	0.0	1.8	(5.6)	5.9
Top 20 Clients	0.4	(6.8)	0.6	2.2	2.2	1.7	(1.7)	(0.4)	(1.3)	(0.1)	4.5	(0.5)	(1.8)	(0.1)	3.0	(4.9)	3.2
YoY Growth (%)																	
By Geography (%)																	
North America	11.9	7.5	7.1	7.1	4.8	7.5	6.6	5.4	3.1	8.8	15.6	10.8	7.2	5.4	(0.3)	0.6	9.0
Europe	5.5	1.0	(0.6)	0.4	7.5	11.9	14.9	16.2	11.1	9.8	10.0	8.3	1.9	1.1	(1.6)	(6.3)	(4.7)
Rest of World	24.3	28.6	3.5	3.8	6.6	13.3	13.3	13.2	23.5	5.6	(0.0)	0.7	(2.1)	6.1	10.3	15.4	12.4
By Industry (%)																	
Communication (Telecom)	14.3	10.6	(4.4)	(2.6)	(3.0)	1.4	0.6	1.4	(0.7)	(2.0)	(1.2)	(5.8)	(1.9)	0.1	4.6	8.1	4.6
Manufacturing	6.0	(4.7)	7.7	10.4	22.0	18.4	24.2	17.6	8.8	12.5	10.6	12.0	9.3	11.9	6.6	(1.7)	(5.4)
Technology, media & entertainment	11.0	11.3	11.3	7.1	(6.9)	(4.9)	(8.6)	(11.7)	(9.9)	10.0	29.5	29.1	27.8	12.3	4.7	7.5	17.2
Banking, financial services & insurance	11.2	9.8	21.0	17.8	27.1	47.0	47.1	40.6	34.8	10.0	1.4	1.6	(1.1)	5.1	2.6	(4.1)	1.8
Retail, transport & logistics	8.7	16.6	3.9	4.3	20.2	22.9	16.0	15.4	16.4	1.2	4.9	(3.5)	(6.7)	(1.6)	5.2	3.5	13.8
Others	21.6	39.1	33.4	18.7	9.3	2.8	10.6	23.8	60.1	72.4	80.0	73.6	16.9	4.3	(17.5)	(9.5)	20.8
By Client classification (%)																	
Top 5 Clients	(10.1)	(16.9)	(12.1)	(9.0)	(5.5)	9.2	5.5	(0.8)	(4.3)	(9.6)	(4.1)	(9.1)	(2.9)	1.6	0.1	(0.4)	(2.0)
Top 10 Clients	(5.3)	(10.4)	(9.9)	(5.2)	(1.6)	5.6	6.6	0.1	(3.3)	(6.3)	(4.3)	(3.7)	(3.8)	(0.7)	(0.3)	(3.8)	1.8
Top 20 Clients	(0.1)	(6.4)	(5.4)	(3.8)	(2.1)	6.8	4.4	1.7	(1.7)	(3.5)	2.6	2.5	2.0	2.0	0.5	(3.9)	1.0

Source: Nirmal Bang Institutional Equities Research

Exhibit 15: P/E charts

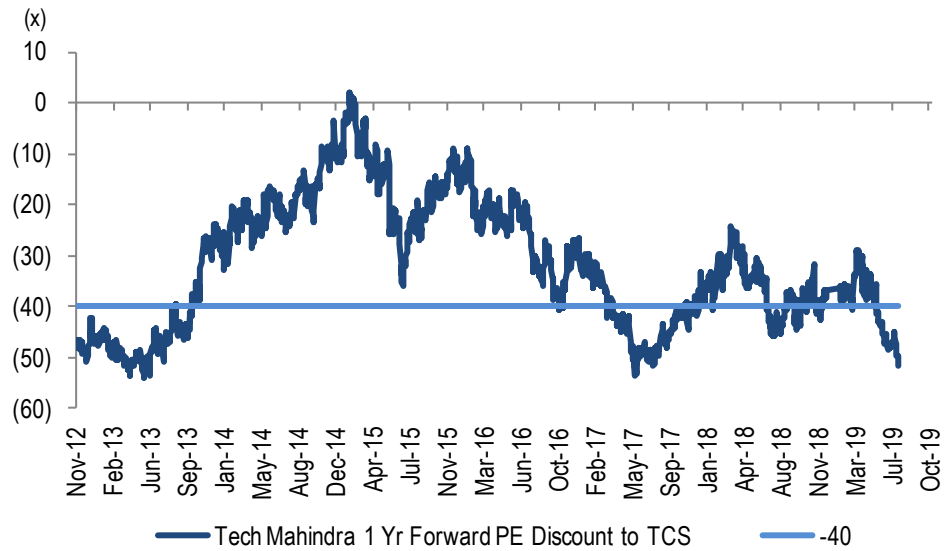


Source: Company, Nirmal Bang Institutional Equities Research



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 16: P/E premium/ (discount) to TCS



Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 17: Comparative valuation

Year Ending	TCS	Infosys	Wipro	HCL Tech	TechMahindra	Mindtree	Persistent
	March	March	March	March	March	March	March
Prices as on 5-Nov-19	2,202	696	259	1,159	773	710	599
Currency	INR	INR	INR	INR	INR	INR	INR
Market Value (Rs Bn)	8,430	3,026	1,276	1,572	682	118	48
(US\$m)	117,083	42,023	17,729	21,827	9,469	1,632	665
September 2021 Target Price	1,593	625	221	1,153	575	532	525
Upside/(downside)	-27.7%	-10.2%	-14.5%	-0.4%	-25.6%	-25.1%	-12.4%
Recommendation	Sell	Sell	Sell	Accumulate	Sell	Sell	Sell
FDEPS (Rs)							
FY18	67.0	32.5	16.8	62.9	42.8	34.6	40.4
FY19	83.1	36.0	18.6	73.5	48.1	45.8	44.1
FY20E	89.5	39.9	17.4	79.2	52.3	38.3	49.9
FY21E	93.0	41.5	18.7	84.2	56.0	50.3	51.8
FY22E	100.1	42.8	19.6	90.6	60.2	57.1	54.2
PE (x)							
FY18	32.9	21.4	15.4	18.4	18.1	20.5	14.8
FY19	26.5	19.3	13.9	15.8	16.1	15.5	13.6
FY20E	24.6	17.4	14.8	14.6	14.8	18.5	12.0
FY21E	23.7	16.8	13.8	13.8	13.8	14.1	11.6
FY22E	22.0	16.3	13.2	12.8	12.8	12.4	11.1
EV/EBITDA (x)							
FY18	23.5	16.5	12.7	12.2	13.2	15.1	9.9
FY19	18.9	15.0	10.1	10.2	9.3	10.5	7.2
FY20E	18.5	13.8	9.6	9.2	8.8	10.2	6.5
FY21E	17.5	13.0	8.8	8.3	7.4	7.7	5.7
FY22E	16.2	12.6	8.2	7.7	6.7	6.8	5.0
EV/Sales (x)							
FY18	6.2	4.5	2.4	2.8	2.0	2.1	1.5
FY19	5.2	3.8	2.0	2.4	1.7	1.6	1.2
FY20E	4.8	3.4	1.9	2.1	1.6	1.5	1.0
FY21E	4.6	3.2	1.8	1.9	1.4	1.3	0.9
FY22E	4.3	3.1	1.6	1.8	1.2	1.2	0.8
Pre Tax ROIC (%)							
FY18	57.3	44.9	24.5	38.9	25.8	32.9	29.7
FY19	61.8	47.5	30.4	36.3	37.9	46.4	44.2
FY20E	55.3	47.5	34.7	31.1	36.4	33.1	44.7
FY21E	55.0	46.8	35.1	28.2	36.8	39.7	50.1
FY22E	57.6	38.6	36.0	29.7	38.4	44.9	58.8

Source: Bloomberg, Nirmal Bang Institutional Equities Research

Financials

Exhibit 18: Income statement

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Average INR/USD	64.5	69.9	71.8	74.6	76.4
Net Sales (US\$m)	4,771	4,971	5,327	5,505	5,642
-Growth (%)	9.6	4.2	7.2	3.3	2.5
Net Sales	307,730	347,421	382,913	410,364	431,021
-Growth (%)	5.6	12.9	10.2	7.2	5.0
Cost of Sales & Services	215,299	233,590	267,815	287,377	305,057
Gross Profit	92,431	113,831	115,098	122,987	125,964
% of sales	30.0	32.8	30.1	30.0	29.2
SG&A	45,261	50,463	47,610	47,891	47,169
% of sales	14.7	14.5	12.4	11.7	10.9
EBITDA	47,170	63,368	67,488	75,096	78,795
% of sales	15.3	18.2	17.6	18.3	18.3
Depreciation	10,849	11,292	13,622	14,972	16,284
% of sales	3.5	3.3	3.6	3.6	3.8
EBIT	36,321	52,076	53,866	60,124	62,511
% of sales	11.8	15.0	14.1	14.7	14.5
Interest expenses	1,624	1,332	1,554	1,201	1,096
Other income (net)	14,093	5,342	8,803	8,225	10,662
PBT	48,790	56,086	61,114	67,148	72,077
-PBT margin (%)	15.9	16.1	16.0	16.4	16.7
Provision for tax	10,925	12,544	14,296	16,787	18,019
Effective tax rate (%)	22.4	22.4	23.4	25.0	25.0
Minority Interest	(136)	120	483	508	508
Net profit	38,001	42,767	46,020	49,373	53,070
-Growth (%)	35.1	12.5	7.6	7.3	7.5
-Net profit margin (%)	12.3	12.3	12.0	12.0	12.3

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 20: Balance sheet

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
Equity capital	4,417	4,437	4,353	4,353	4,353
Reserves & surplus	184,011	198,407	221,153	253,479	288,209
Net worth	188,428	202,844	225,506	257,832	292,562
Minority Interest	5,091	4,777	5,190	5,190	5,190
Other liabilities	18,246	18,441	18,988	18,988	18,988
Total loans	13,440	5,095	10,801	8,444	8,444
Total liabilities	225,205	231,157	260,485	290,454	325,184
Goodwill	27,727	28,163	29,238	29,238	29,238
Net block (incl. CWIP)	50,896	45,212	43,226	40,430	36,322
Investments	15,116	12,050	5,525	5,525	5,525
Right of Use Asset	-	-	9,951	9,951	9,951
Deferred tax asset - net	5,766	6,091	6,285	6,285	6,285
Other non-current assets	23,797	26,934	33,298	32,164	35,919
Other current assets	19,623	26,770	31,236	30,172	33,695
Debtors	64,979	69,586	83,297	80,458	89,853
Loans & Advances	30,917	29,425	39,566	38,218	42,680
Cash & bank balance	64,892	89,486	88,848	124,238	154,388
Inventory	659	752	383	383	383
Total current assets	181,070	216,019	243,330	273,468	320,998
Total current liabilities	79,167	103,312	110,368	106,607	119,055
Net current assets	101,903	112,707	132,961	166,862	201,944
Total assets	225,205	231,157	260,485	290,454	325,184

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 19: Cash flow

Y/E March (Rsmn)	FY18	FY19	FY20E	FY21E	FY22E
EBIT	36,321	52,076	53,866	60,124	62,511
(Inc./dec. in working capital)	8,227	13,790	(20,893)	1,490	(4,932)
Cash flow from operations	44,548	65,866	32,973	61,614	57,579
Other income	14,093	5,342	8,803	8,225	10,662
Depreciation & amortisation	10,849	11,292	13,622	14,972	16,284
Financial expenses	(1,624)	(1,332)	(1,554)	(1,201)	(1,096)
Tax paid	(10,925)	(12,544)	(14,296)	(16,787)	(18,019)
Dividends paid	(14,835)	(14,900)	(19,502)	(20,888)	(22,441)
Net cash from operations	42,106	53,724	20,045	45,936	42,969
Capital expenditure	(21,142)	(5,608)	(11,636)	(12,176)	(12,176)
Net cash after capex	20,964	48,116	8,409	33,760	30,793
Inc./(dec.) in debt	3,963	(8,150)	6,253	(2,357)	-
(Inc./dec. in investments)	(15,609)	(396)	(33)	1,135	(3,756)
Equity issue/(buyback)	29	(19,560)	(84)	-	-
Cash from financial activities	(11,617)	(28,106)	6,136	(1,222)	(3,756)
Others	1,447	4,584	(15,183)	2,853	3,112
Opening cash	54,098	64,892	89,486	88,848	124,238
Closing cash	64,892	89,486	88,847	124,238	154,388
Change in cash	10,794	24,594	(639)	35,390	30,150

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 21: Key ratios

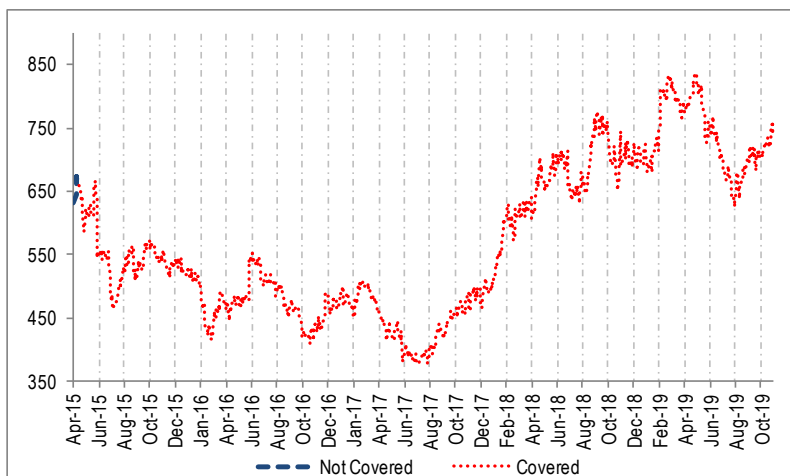
Y/E March	FY18	FY19	FY20E	FY21E	FY22E
Per Share (Rs)					
FDEPS	42.8	48.1	52.3	56.0	60.2
Dividend Per Share	14.2	17.1	18.6	19.9	21.4
Dividend Yield (%)	1.8	2.2	2.4	2.6	2.8
Book Value	216	232	258	295	335
Dividend Payout Ratio (% Incl DDT)	39.0	34.8	42.4	42.3	42.3
Return ratios (%)					
RoE	21.5	21.9	21.5	20.4	19.3
RoCE	17.2	22.8	21.9	21.8	20.3
RoIC	25.8	37.9	36.4	36.8	38.4
Turnover Ratios					
Asset Turnover	1.0	1.0	1.0	1.0	1.0
Debtor Days	77	73	79	72	76
Working Capital Cycle Days	44	24	42	38	40
Valuation ratios (x)					
P/E	17.9	15.9	14.6	13.7	12.7
P/BV	3.6	3.3	3.0	2.6	2.3
EV/EBITDA	13.2	9.3	8.8	7.4	6.7
EV/Sales	2.0	1.7	1.6	1.4	1.2
M-cap/Sales	2.2	1.9	1.8	1.6	1.6

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
13 April 2015	Sell	660	593
28 May 2015	Sell	549	511
19 June 2015	Sell	541	470
28 July 2015	Sell	520	470
28 September 2015	Sell	567	474
4 November 2015	Sell	557	472
15 December 2015	Sell	543	471
8 January 2016	Under Review	522	-
2 February 2016	Under Review	497	-
14 March 2016	Sell	459	395
25 May 2016	Sell	480	409
21 June 2016	Sell	544	421
3 August 2016	Sell	499	400
28 October 2016	Sell	414	385
10 January 2017	Sell	473	368
31 January 2017	Sell	472	383
14 February 2017	Sell	500	388
7 March 2017	Sell	501	408
29 May 2017	Sell	429	403
21 June 2017	Sell	395	367
1 August 2017	Sell	385	360
28 September 2017	Sell	447	358
2 November 2017	Sell	478	387
11 December 2017	Sell	496	426
26 December 2017	Under Review	493	-
30 January 2018	Under Review	605	-
17 March 2018	Accumulate	635	608
28 May 2018	Accumulate	703	721
3 July 2018	Accumulate	655	716
31 July 2018	Accumulate	658	718
5 October 2018	Buy	696	845
31 October 2018	Accumulate	685	731
27 November 2018	Accumulate	695	731
27 December 2018	Sell	695	590
7 January 2019	Sell	681	525
6 February 2019	Sell	751	561
19 March 2019	Sell	789	587
6 June 2019	Sell	750	562
31 July 2019	Sell	641	535
9 September 2019	Sell	684	544
23 September 2019	Sell	688	563
5 November 2019	Sell	775	575

Rating track graph



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Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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