

Taking a big leap

Mastek announced the acquisition of Evosys in a two step transaction, which involves cash payout of USD 65mn and dilution of 17.5% in Mastek Ltd. The deal is valued at EV/EBITDA of 9.2x and P/E of 11.2x based on FY19 financials and 70% economic interest. The deal is EPS accretive and will boost FY21/22E EPS by 11.8/14.1% respectively. Post the traction, Evosys promoters will hold 15% in Mastek Ltd and 30% CCPS in TAISTech, converted to equity based on targets over the next three years. This is a complex traction but involves value unlocking and diversification of revenue. Risk involves higher dependence on Oracle and multi geography footprint, which the company has not handled before. We increase our TP to Rs 595 based on 9x (~18% discount to 5Y average) FY22E EPS plus Rs 31/sh for residual 4.7% stake in Majesco US.

Details of the transaction

- The deal involves two separate transactions. First is all cash buyout of the Evosys middle-east business by Mastek UK for a cash consideration of USD 65mn. The second transaction is Demerger of Evosys US+UK+RoW business and merging it into TAISTech (100% subsidiary of Mastek Ltd). As a result promoters of Evosys will get 15% stake in Mastek Ltd resulting in a dilution of 17.5%.
- These are two separate transactions but we will have to view it as one deal and will value it based on the derived economic interest. The total revenue of Evosys is USD 60mn for FY19 with EBITDA margin of 22.9% and PAT margin of 18.8%.
- Mastek paid Rs 4.63bn (USD 65mn) in cash and Rs 1.62bn (15% stake value based on CMP) for the deal. The total consideration is Rs 6.25bn (USD 88mn) for an EBITDA/PAT of Rs 0.68/0.55bn based on 70% economic interest. The deal is valued at an EV/EBITDA and P/E of 9.2/11.2x based on FY19 financials.
- Mastek will fund the USD 65mn cash payout with a combination of debt and internal accruals. Mastek UK

will take a debt of USD 35mn (4% interest), USD 24mn from Majesco US stake sale and USD 6mn from internal accruals. The cash in the parent entity will remain at Rs 2.4bn and will not impact other income. The company will receive Rs 1.09bn from the residual Majesco US stake sale and Rs 0.40 bn from real estate monetisation. The net cash position post the transaction will reduce to Rs 1.60bn vs. Rs 4.30bn pre-transaction.

- Evosys, headquartered in Ahmedabad, was founded in 2006 by Umang Nahata and Rakesh Raman. Evosys is an Oracle platinum partner for implementation of ERP and HCM and SCM suites.
- Evosys has revenue is USD 70mn for FY20E with 1,300 employees and 300 customers. The revenue per employee is at 53.8K USD, which is healthy.
- Top-10 customers is 31% of revenue and has 100+ customers with revenue of more than USD 1bn. Evosys has 63% revenue from cloud and 55% of the revenue is repeat revenue. More than 25% of the clients have migrated to cloud and cloud revenue CAGR is 100% over FY16-19.
- Geographically the revenue is widely spread, Europe /Middle-East/US/APAC is 30/45/17/8% of revenue. Europe/US revenue has grown at a CAGR of 157/116% over FY17-19.

Financial Summary

YE March (Rs bn)	FY18	FY19	FY20E	FY21E	FY22E
Net Revenues	8.17	10.33	10.74	16.59	18.76
EBIT	0.82	1.16	1.29	2.13	2.48
APAT	0.70	1.01	1.15	1.49	1.78
Diluted EPS (Rs)	27.7	39.9	40.3	52.3	62.4
P/E (x)	16.4	11.3	11.2	8.7	7.2
EV / EBITDA (x)	10.0	7.5	8.9	5.1	4.0
RoE (%)	13.7	15.9	15.1	17.2	17.5

Source: Company, HDFC sec Inst Research # Consolidated

HDFC securities Institutional Research is also available on Bloomberg ERH HDF <GO>& Thomson Reuters

INDUSTRY	IT
CMP (as on 07 Feb 2020)	Rs 453
Target Price	Rs 595
Nifty	12,098
Sensex	41,142

KEY STOCK DATA	
Bloomberg	MAST IN
No. of Shares (mn)	24
MCap (Rs bn) / (\$ mn)	11/153
6m avg traded value (Rs mn)	26

STOCK PERFORMANCE (%)			
52 Week high / low	Rs 509/294		
	3M	6M	12M
Absolute (%)	36.4	27.2	14.5
Relative (%)	35.2	15.1	3.2

SHAREHOLDING PATTERN (%)		
	Dec-19	Dec-19*
Promoters	45.43	38.45
FIs & Local MFs	12.38	10.54
FPIs	6.52	5.55
Public & Others	35.67	45.46
Pledged Shares	25.89	22.04

Source : BSE

*post dilution SHP

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Evosys revenue is evenly spread with strong presence in Middle-East and Europe

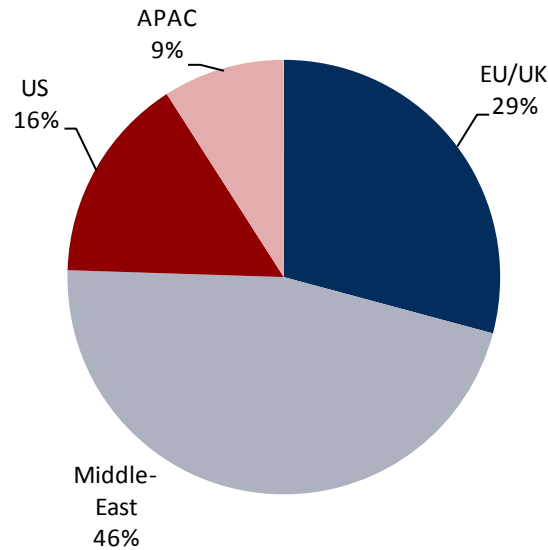
Europe presence is across Denmark and Netherlands

RoW include Australia, Singapore and India

Evosys revenue from cloud implementation has increased to 63% of revenue, which was just 20% in FY16

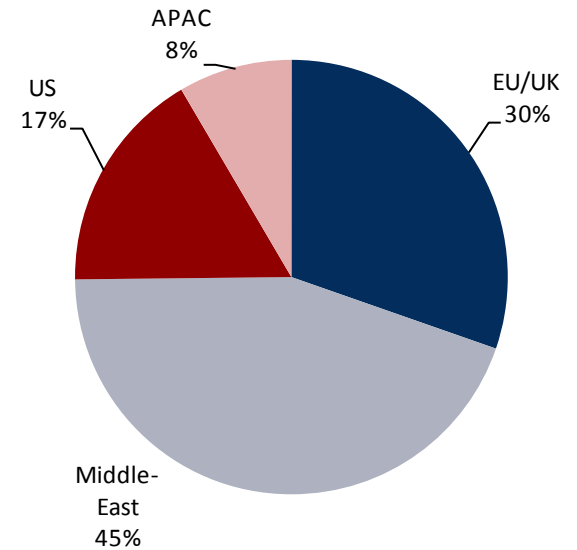
Annuity revenue stream is 32% while repeat revenue is 55% of revenue, which includes subscription and maintenance revenue

Evosys Geographical Mix (FY19)



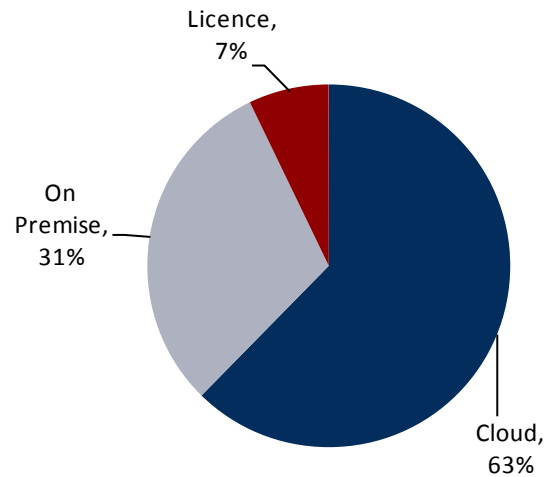
Source: Company, HDFC sec Inst Research,

Evosys Geographical Mix (LTM May 19)



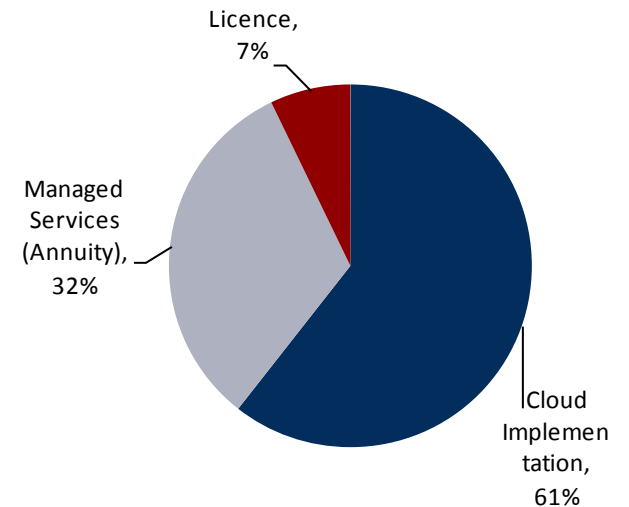
Source: Company, HDFC sec Inst Research

Evosys Revenue Mix By Platform (LTM May 19)



Source: Company, HDFC sec Inst Research

Evosys Revenue Mix By Services (LTM May 19)



Source: Company, HDFC sec Inst Research

Based on our proforma calculation the revenue/EBIT/PAT increases by 50/79/35% for FY20E

EPS increase is 15% due to dilution impact

These numbers are not comparable with actual FY20E financials as the revenue will be split between FY20E and FY21E. We have assumed two months impact in FY20E and full year impact in FY21E

The net cash position post the transaction remains at Rs 1.60bn including Rs 1.09bn from Majesco US stake sale and Rs 0.40bn from real estate monetisation

Pre and Post Acquisition Proforma Financials

Year ending March	FY20 (Pre)	EVOSYS (FY20)	FY20E (Post)	Change %
Net Revenues (USD mn)	139.7	70	209.6	50%
Net Revenues	9,873	4,983	14,856	50%
EBITDA	1,337	997	2,334	
EBITDA Margin %	14%	20%	16%	
Depreciation	225	114	339	
EBIT	1,112	883	1,994	79%
EBIT Margin (%)	11.3%	17.7%	13.4%	
Other Income (Including EO Items)	204		204	
Interest	33		144	
PBT	1,282	883	2,054	60%
Tax (Incl Deferred)	276	225	501	
Minority Interest	-		197	
RPAT	1,006	658	1,356	35%
PAT Margin %	10.2%	13.2%	9.1%	
Adjusted EPS (Rs)	41.5		47.6	15%
No of Shares	24.3		28.5	17%

Source: Company, HDFC sec Inst Research

Cash/Debt position (Rs mn)	FY20 (Pre)	FY20E (Post)
India Entity	2,400	2,400
Real Estate Monetisation	-	400
Residual Majesco stake	-	1,092
Mastek UK (Including Majesco stake sale)	2,600	900
Total Cash	5,000	4,792
Debt (TAIS Tech)	704	704
Debt(Mastek UK)		2,492
Net Cash	4,296	1,596

Source: HDFC sec Inst Research

Split of Cash Payment to Evosys (USD mn)	
Debt Funded	35
Majesco stake Sale	24
Internal Accruals	6
Total	65

Source: Company, HDFC sec Inst Research

We increase FY20/21/22 revenue by 8.7/50.4/49.4% factoring in Evosys acquisition. FY20E includes two month impact and FY21E has full contribution from Evosys

EBIT margin for Evosys is at 20.7% which is higher than company average of 11%. The EBIT increase is 66.2/68.7% for FY21/22E

EPS improves by 11.8/14.1% for FY21/22E due to minority interest and dilution of equity by 17%

We have taken the residual value of 4.7% stake in Majesco US valued at Rs 1.09bn which is 38/sh

Change In Estimates

Particulars	Earlier estimates	Revised estimates	% change
FY20E			
Revenue (USD mn)	139.7	151.8	8.7
Revenue (Rs mn)	9.9	10.7	8.8
EBIT (Rs bn)	1.1	1.3	15.8
EBIT margin (%)	11.3	12.0	72 bps
EPS (Rs)	42.0	40.3	-4.1
FY21E			
Revenue (USD mn)	154.2	232.0	50.4
Revenue (Rs mn)	11.0	16.6	50.4
EBIT (Rs bn)	1.3	2.1	66.2
EBIT margin (%)	11.6	12.8	122 bps
EPS (Rs)	46.8	52.3	11.8
FY22E			
Revenue (USD mn)	172.0	257.0	49.4
Revenue (Rs mn)	12.6	18.8	49.4
EBIT (Rs bn)	1.5	2.5	68.7
EBIT margin (%)	11.7	13.2	151 bps
EPS (Rs)	54.7	62.4	14.1

Source: HDFC sec Inst Research

Valuation

Particulars	Per Share (Rs)
EPS FY22	62
Target P/E (x)	9
Value of Core Business (Rs)	565
Stake in Majesco US (Rs)	38
Discount (20%)	8
Value of Stake in Majesco US (Rs)	31
Target Price (Rs)	595
Upside (%)	32%

Source: Company, HDFC Sec Inst Research

INSTITUTIONAL RESEARCH

Peer Set Comparison

Company	MCap (Rs bn)	CMP (Rs)	TP (Rs)	RECO	EPS (Rs)				P/E (x)				RoE (%)			
					FY19	FY20E	FY21E	FY22E	FY19	FY20E	FY21E	FY22E	FY19	FY20E	FY21E	FY22E
TCS	8,017	2,137	2,025	NEU	83.9	86.5	93.6	104.7	25.5	24.7	22.8	20.4	36.1	35.7	37.2	39.7
Infosys	3,300	777	850	BUY	37.1	38.2	43.5	48.1	20.9	20.4	17.9	16.2	24.3	25.4	28.2	28.3
Wipro	1,391	244	235	NEU	15.8	17.4	18.3	20.0	15.5	14.0	13.3	12.2	17.3	17.7	17.3	16.2
HCL Tech	1,648	608	665	BUY	37.3	39.0	41.7	48.2	16.3	15.6	14.6	12.6	26.0	23.2	21.0	20.7
TechM	796	825	910	BUY	48.9	49.7	54.3	62.7	16.9	16.6	15.2	13.2	22.0	21.1	21.0	21.2
Tier-1 IT Median									16.9	16.6	15.2	13.2	24.3	23.2	21.0	21.2
LTI	338	1,945	2,090	BUY	87.1	85.6	101.6	120.7	22.3	22.7	19.1	16.1	34.6	28.0	28.4	28.7
Mphasis	175	937	1,165	BUY	57.6	58.3	65.5	75.0	16.3	16.1	14.3	12.5	20.0	19.7	19.9	20.2
L&T Tech	176	1,688	1,790	BUY	67.8	76.0	86.6	103.7	24.9	22.2	19.5	16.3	32.0	29.4	28.4	28.5
Mindtree	152	922	830	NEU	44.1	38.5	48.0	63.3	20.9	23.9	19.2	14.6	24.9	18.3	22.7	26.0
Hexaware *	113	377	450	BUY	19.6	21.6	24.5	28.3	19.3	17.5	15.4	13.3	26.5	24.7	24.1	24.0
Cyient	55	487	490	NEU	43.6	36.3	40.9	46.0	11.2	13.4	11.9	10.6	19.5	15.3	15.9	16.2
Zensar	37	161	177	NEU	14.2	10.8	12.9	17.1	11.4	15.0	12.5	9.4	17.6	11.9	12.9	15.3
Persistent	54	710	745	BUY	47.8	47.1	50.0	59.6	14.8	15.1	14.2	11.9	15.7	14.4	15.2	16.2
Tata Elxsi	64	1,031	NA	NR	46.6	39.5	50.7	58.9	22.1	26.1	20.3	17.5	34.5	24.3	26.6	26.1
Sonata	36	345	422	BUY	23.7	28.5	31.6	36.3	14.5	12.1	10.9	9.5	35.1	36.1	35.3	35.7
Intellect	22	165	255	BUY	7.7	2.6	7.3	11.2	21.6	64.4	22.6	14.7	11.1	3.3	8.7	12.1
eClerx	23	634	NA	NR	61.7	52.0	53.7	57.0	10.3	12.2	11.8	11.1	17.6	14.0	14.7	14.6
Majesco	11	407	655	BUY	18.3	19.9	30.0	36.7	22.2	20.5	13.6	11.1	8.4	7.9	11.0	12.2
HGS	15	715	NA	NR	84.6	100.3	110.9	129.5	8.5	7.1	6.4	5.5	8.5	13.1	13.3	13.7
Mastek	11	453	595	BUY	39.9	40.3	52.3	62.4	11.3	11.2	8.7	7.2	15.9	15.1	17.2	17.5
Tier-2 IT Median									16.3	16.1	14.2	11.9	19.5	15.3	17.2	17.5

Source: HDFC sec Inst Research

Income Statement (Consolidated)

Year ending March	FY18	FY19	FY20E	FY21E	FY22E
Net Revenues (USD mn)	126.8	147.8	151.8	232.0	257.0
Growth (%)	51.8%	16.5%	2.7%	52.8%	10.8%
Net Revenues	8.17	10.33	10.74	16.59	18.76
Growth (%)	45.9%	26.4%	3.9%	54.5%	13.1%
Employee Expenses	4.81	5.87	5.93	9.21	10.14
Other Operating Expenses	2.36	3.12	3.28	4.78	5.63
EBITDA	1.00	1.34	1.53	2.59	3.00
Depreciation	0.19	0.17	0.25	0.47	0.51
EBIT	0.82	1.16	1.29	2.13	2.48
EBIT Margin (%)	10.0%	11.3%	12.0%	12.8%	13.2%
EBIT Growth (%)	126.7%	42.5%	10.6%	65.2%	16.8%
Other Income (Including EO Items)	0.20	0.23	0.19	0.24	0.30
Interest	0.06	0.06	0.05	0.14	0.16
PBT	0.96	1.33	1.42	2.22	2.63
Tax (Incl Deferred)	0.26	0.32	0.31	0.51	0.60
Minority Interest	-	-	0.03	0.22	0.24
RPAT	0.70	1.01	1.08	1.49	1.78
EO (Loss) / Profit (Net Of Tax)	-	0.01	(0.07)	-	-
APAT	0.70	1.01	1.15	1.49	1.78
APAT Growth (%)	95.5%	44.3%	13.75%	29.8%	19.4%
Adjusted EPS (Rs)	27.7	39.9	40.3	52.3	62.4
EPS Growth (%)	95.5%	44.3%	0.9%	29.8%	19.4%

Source: Company, HDFC sec Inst Research

Balance Sheet (Consolidated)

As at March (Rs bn)	FY18	FY19	FY20E	FY21E	FY22E
SOURCES OF FUNDS					
Share Capital - Equity	0.12	0.12	0.14	0.14	0.14
Reserves	5.37	7.04	7.87	9.21	10.79
Total Shareholders' Funds	5.49	7.16	8.01	9.35	10.93
Long Term Debt	0.50	0.69	3.18	3.19	3.19
Short Term Debt	0.20	0.01	0.01	0.01	0.01
Total Debt	0.70	0.70	3.19	3.20	3.20
Net Deferred Taxes	(0.34)	(0.16)	(0.16)	(0.16)	(0.16)
Other Non-current Liabilities & Provns	0.33	0.12	0.12	0.12	0.12
TOTAL SOURCES OF FUNDS	6.18	7.83	11.17	12.51	14.09
APPLICATION OF FUNDS					
Net Block	0.71	0.70	5.18	5.08	5.00
CWIP	0.02	0.01	0.01	0.01	0.01
Goodwill	1.08	0.98	0.98	0.98	0.98
Investments	1.66	2.82	1.11	1.11	1.11
Other Non-current Assets	0.11	0.15	0.15	0.15	0.15
Total Non-current Assets	3.59	4.66	7.43	7.33	7.24
Cash & Equivalents	2.06	2.07	2.40	2.78	4.01
Debtors	1.74	2.08	2.24	3.45	3.91
Other Current Assets	0.49	0.69	0.79	1.10	1.27
Total Current Assets	2.23	2.77	3.02	4.56	5.18
Creditors	0.19	0.09	0.10	0.16	0.18
Other Current Liabilities & Provns	1.50	1.58	1.59	1.99	2.16
Total Current Liabilities	1.69	1.68	1.69	2.15	2.34
Net Current Assets	0.54	1.09	1.34	2.40	2.84
TOTAL APPLICATION OF FUNDS	6.18	7.83	11.17	12.51	14.09

Source: Company, HDFC sec Inst Research

Cash Flow (Consolidated)

Year ending March (Rs bn)	FY18	FY19	FY20E	FY21E	FY22E
Reported PBT	0.96	1.33	1.42	2.22	2.63
Non-operating & EO Items	(0.03)	(0.03)	(0.19)	(0.24)	(0.30)
Interest Expenses	0.06	0.06	0.05	0.14	0.16
Depreciation	0.19	0.17	0.25	0.47	0.51
Working Capital Change	(0.45)	(0.51)	(0.24)	(1.07)	(0.44)
Tax Paid	(0.09)	(0.31)	(0.31)	(0.51)	(0.60)
OPERATING CASH FLOW (a)	0.64	0.73	0.98	1.01	1.96
Capex	(0.21)	(0.32)	(4.73)	(0.36)	(0.43)
<i>Free Cash Flow (FCF)</i>	<i>0.43</i>	<i>0.41</i>	<i>(3.74)</i>	<i>0.65</i>	<i>1.52</i>
Non-operating Income	0.04	0.02	1.90	0.24	0.30
INVESTING CASH FLOW (b)	(0.17)	(0.30)	(2.83)	(0.13)	(0.13)
Debt Issuance/(Repaid)	0.04	0.01	2.49	0.01	0.01
Interest Expenses	(0.03)	(0.02)	(0.05)	(0.14)	(0.16)
<i>FCFE</i>	<i>0.45</i>	<i>0.39</i>	<i>(1.30)</i>	<i>0.51</i>	<i>1.37</i>
Share Capital Issuance	0.02	0.03	0.02	-	-
Dividend	(0.11)	(0.18)	(0.29)	(0.37)	(0.44)
FINANCING CASH FLOW (c)	(0.07)	(0.16)	2.17	(0.51)	(0.60)
NET CASH FLOW (a+b+c)	0.40	0.27	0.33	0.37	1.23
EO Items, Others	(0.13)	0.25	-	-	-
Closing Cash & Equivalents	2.06	2.07	2.40	2.78	4.01

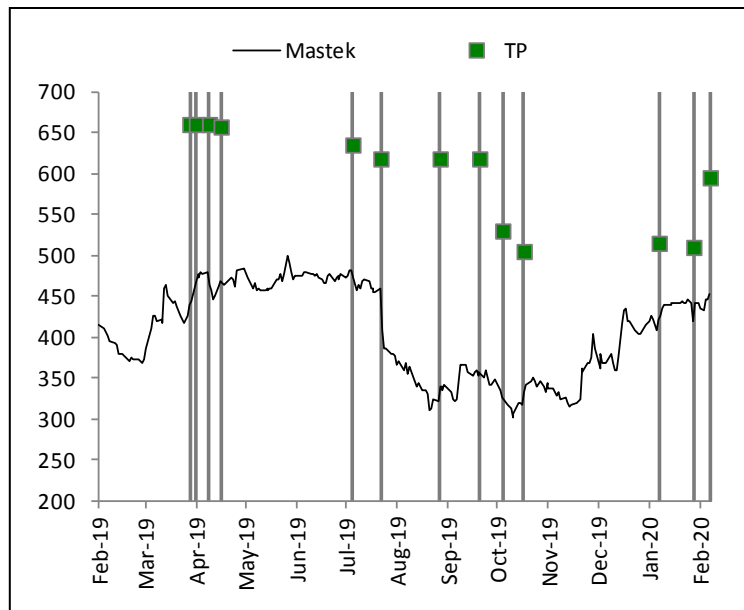
Source: Company, HDFC sec Inst Research

Key Ratios (Consolidated)

	FY18	FY19	FY20E	FY21E	FY22E
PROFITABILITY (%)					
EBITDA Margin	12.3	12.9	14.3	15.6	16.0
APAT Margin	8.6	9.8	10.7	9.0	9.5
RoE	13.7	15.9	15.1	17.2	17.5
RoIC (or Core RoCE)	23.9	32.8	19.0	20.1	21.7
RoCE	12.5	15.1	12.5	13.5	14.3
EFFICIENCY					
Tax Rate (%)	27.1	23.9	21.7	23.0	23.0
Fixed Asset Turnover (x)	11.5	14.8	2.1	3.3	3.8
<i>Debtors (days)</i>	<i>78</i>	<i>74</i>	<i>76</i>	<i>76</i>	<i>76</i>
<i>Other Current Assets (days)</i>	<i>22</i>	<i>24</i>	<i>27</i>	<i>24</i>	<i>25</i>
<i>Payables (days)</i>	<i>8</i>	<i>3</i>	<i>4</i>	<i>4</i>	<i>4</i>
<i>Other Current Liab & Provns (days)</i>	<i>67</i>	<i>56</i>	<i>54</i>	<i>44</i>	<i>42</i>
<i>Cash Conversion Cycle (days)</i>	<i>24</i>	<i>39</i>	<i>45</i>	<i>53</i>	<i>55</i>
Debt/EBITDA (x)	0.7	0.5	2.1	1.2	1.1
Net D/E (x)	-0.2	-0.2	0.1	0.0	-0.1
Interest Coverage (x)	13.9	19.0	26.0	14.8	15.5
PER SHARE DATA (Rs)					
EPS	27.7	39.9	40.3	52.3	62.4
CEPS	35.1	46.8	48.9	68.7	80.5
Dividend	6.0	8.5	9.9	12.8	15.3
Book Value	217	283	281	328	384
VALUATION					
P/E (x)	16.4	11.3	11.2	8.7	7.2
P/BV (x)	2.1	1.6	1.6	1.4	1.2
EV/EBITDA (x)	10.0	7.5	8.9	5.1	4.0
EV/Revenues (x)	1.2	1.0	1.3	0.8	0.6
OCF/EV (%)	6.4	7.2	7.2	7.6	16.2
FCF/EV (%)	4.3	4.0	-27.4	4.9	12.6
FCFE/Mkt Cap (%)	3.9	3.4	-10.1	4.0	10.6
Dividend Yield (%)	1.3	1.9	2.2	2.8	3.4

Source: Company, HDFC sec Inst Research

RECOMMENDATION HISTORY



Date	CMP	Reco	Target
29-Mar-19	439	BUY	660
1-Apr-19	443	BUY	660
9-Apr-19	480	BUY	660
17-Apr-19	463	BUY	657
5-Jul-19	472	BUY	635
23-Jul-19	460	BUY	618
27-Aug-19	322	BUY	618
22-Sep-19	357	BUY	618
4-Oct-19	334	BUY	530
18-Oct-19	332	BUY	505
7-Jan-20	409	BUY	515
29-Jan-20	420	BUY	510
10-Feb-20	453	BUY	595

Rating Definitions

- BUY : Where the stock is expected to deliver more than 10% returns over the next 12 month period
- NEUTRAL : Where the stock is expected to deliver (-)10% to 10% returns over the next 12 month period
- SELL : Where the stock is expected to deliver less than (-)10% returns over the next 12 month period

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