



## KEY DATA

Rating	BUY
Sector relative	Outperformer
Price (INR)	3,009
12 month price target (INR)	3,500
52 Week High/Low	3,081/2,068
Market cap (INR bn/USD bn)	569/6.8
Free float (%)	51.8
Avg. daily value traded (INR mn)	3,872.6

## SHAREHOLDING PATTERN

	June-24	Mar-24	Dec-23
Promoter	40.35%	55.45%	55.52%
FII	18.32%	14.84%	15.72%
DII	35.84%	24.63%	23.71%
Pledge	0%	0%	0%

## FINANCIALS

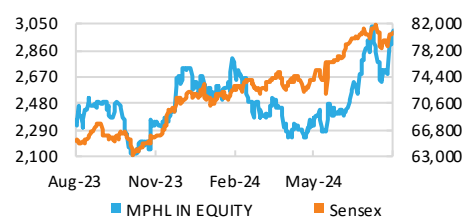
(INR mn)

Year to March	FY24A	FY25E	FY26E	FY27E
Revenue	1,32,785	1,42,876	1,59,200	1,79,926
EBITDA	24,220	26,677	30,131	33,881
Adjusted profit	15,549	17,454	20,433	23,665
Diluted EPS (INR)	81.8	91.8	107.4	124.4
EPS growth (%)	(6.0)	12.3	17.1	15.8
RoAE (%)	18.6	19.0	20.4	21.5
P/E (x)	36.7	32.7	27.9	24.1
EV/EBITDA (x)	21.9	19.6	17.1	15.0
Dividend yield (%)	2.2	2.3	2.3	2.3

## CHANGE IN ESTIMATES

Year to March	Revised estimates		% Revision	
	FY25E	FY26E	FY25E	FY26E
Rev (USD, mn)	1,703	1,894	0.5%	1.6%
EBIT	22,174	25,510	0.6%	2.1%
Adjusted profit	17,454	20,433	1.8%	3.7%
Diluted EPS (INR)	91.8	107.4	1.8%	3.7%

## PRICE PERFORMANCE



## All set to climb up the wall it fell from

We recently met with Mr Nitin Rakesh, CEO of Mphasis, who highlighted how Mphasis is taking giant strides to capture early-mover advantage in AI space. All along, its client-focused strategy has helped it to mine its clientele deeper along with diversifying the revenue base.

Mphasis has rallied 25% in the last three months, fuelled by expectations of interest rate cuts in US and early signs of a recovery in US-BFS. We see Mphasis at an inflection point – where the factors that led to its underperformance over the last two years – are now likely to reverse, leading to outperformance. We are upgrading FY25E/26E EPS by 2%/4% and target valuation to 30x Sep-26 PE (from 27x) – on better growth visibility; upgrade to 'BUY' with a target price of INR3,500.

## Growth to rebound sharply as macro turns favourable

Mphasis has had two lacklustre years – with 7.8% growth/-6.3% decline in top line in FY23/FY24. In FY25 too, it is likely to report mere mid single-digit growth. The high interest-rate regime has hurt its two businesses – BFS (47% of revenue) and mortgage (~6% of revenue). However, US macro is now showing signs of becoming favourable for the Indian IT industry. Mphasis's mortgage business has a perfect inverse correlation with interest rates, and should recover as sharply as it had fallen, once the Fed enters the interest rate cut territory.

Interest rate cuts are also likely to lead to a revival in tech spending by US corporates, which they had put on hold for almost two years now. The same is also corroborated by the commentary from various companies and clients – as they called out early signs of a recovery in US-BFS. Mphasis's top client too is a BFS corporate, and recently announced historically high tech spends for CY24. A reversal of these factors – interest rates and BFS spending – shall boost growth for Mphasis ahead of peers.

## Core business stays robust; trying to move early in Gen-AI domain

All along the last two years' underperformance, Mphasis' remaining businesses have continued to remain strong, and grown in line with peers. The company has backfilled the entire DXC channel with growth in other verticals/clients – and it now contributes only 3% to the top line (from 28% in FY19) – making it completely irrelevant. As Mphasis continues to execute its client-focused strategy, we reckon the revenue base shall further diversify over the next few years.

In our conversation with the CEO,, he highlighted how Mphasis is taking giant strides to capture the early-mover advantage in Gen-AI domain. He highlighted how Gen-AI shall change the way IT Services companies have been doing business, especially billing. Nitin is also highly excited about Mphasis's two platforms – NeoZeta™ and NeoCruz™ – that use Gen-AI to modernise legacy codes and improve SDLC.

## Upgrade to 'BUY' – perfect proxy for interest rate cycle

We view Mphasis as a perfect proxy for playing the interest rate cut cycle in the US along with the recovery in the BFS segment. We also forecast Mphasis shall be ahead of peers, in capturing Gen-AI driven opportunity; upgrade to 'BUY' (from 'HOLD').

## Financial Statements

### Income Statement (INR mn)

Year to March	FY24A	FY25E	FY26E	FY27E
Total operating income	1,32,785	1,42,876	1,59,200	1,79,926
Cost of revenues	78,413	94,049	1,06,781	1,20,316
Gross Profit	54,372	48,827	52,419	59,610
SG&A	30,152	22,150	22,288	25,729
EBITDA	24,220	26,677	30,131	33,881
Depreciation	4,106	4,503	4,620	4,640
EBIT	20,114	22,174	25,510	29,241
Add: Other income	2,178	3,122	3,459	3,989
Profit before tax	20,684	23,252	27,244	31,553
Prov for tax	5,135	5,798	6,811	7,888
Less: Other adj	0	0	0	0
Reported profit	15,549	17,454	20,433	23,665
Less: Excp.item (net)	0	0	0	0
Adjusted profit	15,549	17,454	20,433	23,665
Diluted shares o/s	190	190	190	190
Adjusted diluted EPS	81.8	91.8	107.4	124.4
DPS (INR)	67.0	70.0	70.0	70.0
Tax rate (%)	2,482.6	2,493.4	2,500.0	2,500.0

### Important Ratios (%)

Year to March	FY24A	FY25E	FY26E	FY27E
Employees cost	59.1	65.8	67.1	66.9
Other cost	22.7	15.5	14.0	14.3
Depreciation (% of rev)	3.1	3.2	2.9	2.6
EBIT margin (%)	15.1	15.5	16.0	16.3
Net profit margin (%)	11.7	12.2	12.8	13.2
Revenue growth (% YoY)	(3.8)	7.6	11.4	13.0
EBIT growth (% YoY)	(4.6)	10.2	15.0	14.6
Adj. profit growth (%)	(5.1)	12.3	17.1	15.8

### Assumptions (%)

Year to March	FY24A	FY25E	FY26E	FY27E
GDP (YoY %)	6.7	6.0	6.2	6.2
Repo rate (%)	6.5	6.0	5.0	5.0
USD/INR (average)	83.0	84.0	84.0	84.0
USD revenue (USD mn)	1,609.5	1,702.9	1,894.4	2,141.2
YoY growth (%)	(6.3)	5.8	11.2	13.0
CC YoY growth (%)	(6.5)	5.8	11.2	13.0
Tax rate as % of PBT	24.8	24.9	25.0	25.0
Capex (INR mn)	19,345.8	4,336.3	4,820.4	4,839.6

### Valuation Metrics

Year to March	FY24A	FY25E	FY26E	FY27E
Diluted P/E (x)	36.7	32.7	27.9	24.1
Price/BV (x)	6.5	6.0	5.5	4.9
EV/EBITDA (x)	21.9	19.6	17.1	15.0
Dividend yield (%)	2.2	2.3	2.3	2.3

Source: Company and Nuvama estimates

### Balance Sheet (INR mn)

Year to March	FY24A	FY25E	FY26E	FY27E
Share capital	1,890	1,891	1,891	1,891
Reserves	86,056	93,500	1,02,591	1,13,968
Shareholders funds	87,946	95,391	1,04,482	1,15,859
Minority interest	0	0	0	0
Borrowings	0	0	0	0
Trade payables	40,346	41,654	44,160	48,193
Other liabs & prov	0	0	0	0
Total liabilities	1,41,302	1,49,632	1,61,396	1,77,055
Net block	48,693	48,526	48,726	48,926
Intangible assets	0	0	0	0
Capital WIP	0	0	0	0
Total fixed assets	48,693	48,526	48,726	48,926
Non current inv	8,454	6,219	6,219	6,219
Cash/cash equivalent	34,071	41,551	48,187	56,335
Sundry debtors	24,256	26,501	29,449	33,823
Loans & advances	342	253	253	253
Other assets	7,655	7,887	8,549	9,531
Total assets	1,41,302	1,49,632	1,61,396	1,77,055

### Free Cash Flow (INR mn)

Year to March	FY24A	FY25E	FY26E	FY27E
Reported profit	15,549	17,454	20,433	23,665
Add: Depreciation	4,106	4,503	4,620	4,640
Interest (net of tax)	0	0	0	0
Others	0	0	0	0
Less: Changes in WC	19,056	(2,367)	(2,254)	(3,029)
Operating cash flow	38,711	19,590	22,799	25,275
Less: Capex	(19,346)	(4,336)	(4,820)	(4,840)
Free cash flow	19,365	15,253	17,979	20,435

### Key Ratios

Year to March	FY24A	FY25E	FY26E	FY27E
RoE (%)	18.6	19.0	20.4	21.5
RoCE (%)	20.0	20.7	21.7	22.6
Div Payout Ratio(%)	65.9	58.7	54.7	51.2
Working cap/Sales (%)	(6)	(5)	(4)	(3)
Receivable days	68	65	64	64
Asset Turnover Ratio	0.5	0.5	0.5	0.5
Current Ratio	1.6	1.8	2.0	2.1
Net debt/equity (x)	(0.4)	(0.4)	(0.5)	(0.5)

### Valuation Drivers

Year to March	FY24A	FY25E	FY26E	FY27E
EPS growth (%)	(6.0)	12.3	17.1	15.8
RoE (%)	18.6	19.0	20.4	21.5
EBITDA growth (%)	(0.5)	10.1	12.9	12.4
Payout ratio (%)	65.9	58.7	54.7	51.2

## Investment thesis – At inflection point

Mphasis has been on a rollercoaster ride over the last 36 months — from an unprecedented run-up in the stock price to a sector-wide sharp correction to a relative underperformance triggered by company-specific issues, followed by the recent run-up. The stock has traversed a journey of many years in a few quarters.

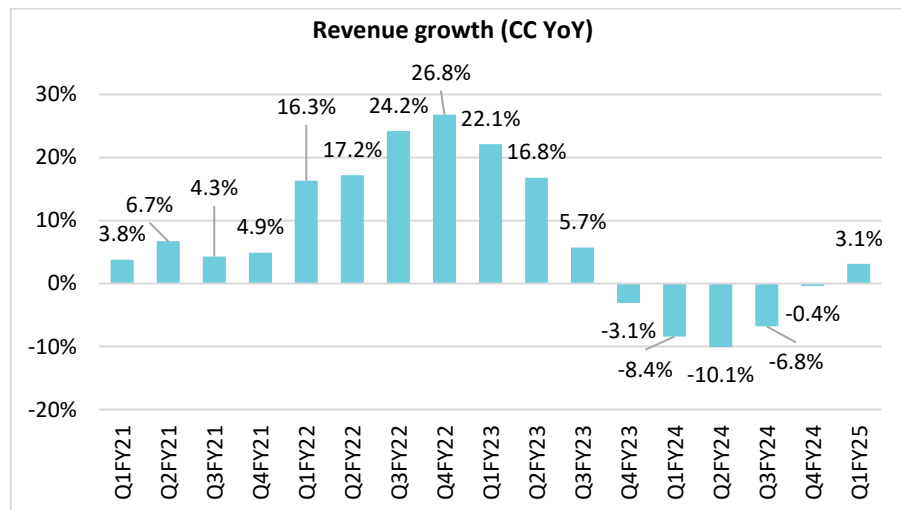
**Exhibit 1: Mphasis stock has rallied sharply in last three months**

Stock returns	Mphasis	LTIM	Coforge	Persistent	Nifty IT
Last 3 months	26.6%	19.8%	27.3%	39.9%	18.0%
Last 6 months	13.1%	4.6%	-6.8%	15.4%	11.0%
Last 12 months	29.6%	10.1%	22.0%	96.2%	34.2%
Last 24 months	25.4%	15.9%	55.4%	30.6%	38.3%

Source: Company, Nuvama Research

Over the last few quarters, the stock has run up sharply (3m, +25%) – despite the company reporting underwhelming results (especially compared with peers). This, we believe is driven by expectations of the growth bottoming out – as we get close to the US Fed cutting interest rates. Mphasis has high exposure to the BFS segment (47% of revenue) – and it should benefit disproportionately from any recovery in the segment (as indicated by multiple players in their recent commentary) – just like it was affected disproportionately over the last two years. Moreover, given its mortgage business has a near-perfect inverse correlation with mortgage rates (in turn dependent on interest rates) – we expect Mphasis’s growth to rebound sharply.

**Exhibit 2: Mphasis’ headwind appears to have bottomed out**



Source: Company, Nuvama Research

We double-click on the following factors, which we believe should lead to a turnaround in fortunes for the company:

- Mortgage business recovery to drive growth
- Core business has remained strong
- BFS recovery, top client to boost growth
- Making early inroads in Gen-AI space
- Strong deal flow to sustain growth; margins to remain stable
- Coveted clientele and diversification

Driven by the above factors, we anticipate growth to pick up sharply for Mphasis in FY26 and beyond. That accompanied by stable margins, should lead to robust earnings growth for the company.

### Exhibit 3: Mphasis growth to pick up sharply in next two years

USD growth	FY23	FY24	FY25E	FY26E	FY27E
<b>USD revenue</b>	<b>1,718</b>	<b>1,609</b>	<b>1,703</b>	<b>1,894</b>	<b>2,141</b>
<b>Overall growth</b>	<b>7.8</b>	<b>-6.3</b>	<b>5.8</b>	<b>11.2</b>	<b>13.0</b>
Organic overall growth	7.8	-8.2	3.0	11.2	13.0
Direct core growth	10.3	-4.9	6.6	11.6	13.4
Direct core organic growth	10.3	-7.0	3.6	11.6	13.4
<b>EBIT margins</b>	<b>15.3</b>	<b>15.1</b>	<b>15.5</b>	<b>16.0</b>	<b>16.3</b>
<b>EPS</b>	<b>86.9</b>	<b>81.8</b>	<b>91.8</b>	<b>107.4</b>	<b>124.4</b>
EPS growth	14.1	-6.0	12.3	17.1	15.8

Source: Company, Nuvama Research

We see Mphasis at an inflection point, where the multiple factors (internal as well as external), which caused its underperformance over the last two years – are all set to reverse over the next 12–18 months. We view Mphasis as a perfect proxy for playing the interest rate cut cycle in the US along with the recovery in the BFS segment. We also reckon Mphasis shall be ahead of peers, in capturing Gen-AI driven opportunity.

We turn positive on Mphasis and are upgrading FY25E/26E EPS by 2%/4%. We are upgrading target valuation too to 30x Sep-26 PE (earlier 27x) on better growth visibility; upgrade to 'BUY' (from 'HOLD') with a target price of INR3,500 (earlier INR3,030).

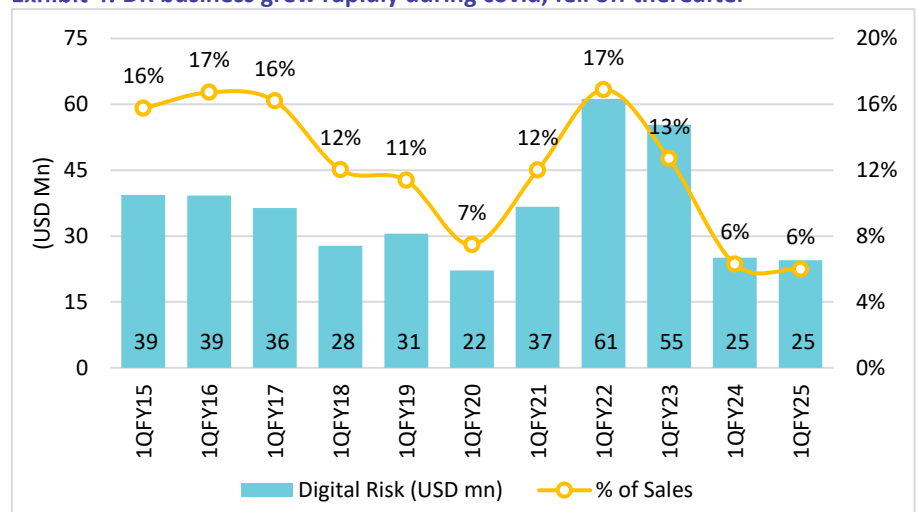
## Mortgage business recovery to drive growth

The primary source of Mphasis’s pain over the last two years has been its mortgage or the ‘Digital risk’ business. The business benefitted immensely from the interest rate cuts over FY21–22 but was impacted adversely by interest rate hikes over FY23–24. US mortgage rates are currently at ~6.5%—not far from their historical peak. The rates have come down by almost 120bp over the last nine months – primarily on expectations of interest rate cuts by the Fed. As the Fed embarks upon interest rate cuts (likely to start by Sep-24) – it is likely to reverse the interest rate cycle leading mortgage rates to come down too.

As mortgage rates come down, we forecast Mphasis’s DR business shall recover – possibly not as sharply as it fell, but with a good velocity. This shall provide a big boost to Mphasis’s revenue and earnings growth. While part of this is already baked into consensus estimates – we believe the recovery would be much sharper, leading to an incremental earnings upgrade.

Mphasis had acquired the mortgage business in Dec-12 as an entity named ‘Digital Risk’ (DR) – which had annual revenue of USD127mn (2012). The business reported healthy growth over FY13–17, hitting a quarterly run rate of USD42mn in FY16. Thereafter, the business was hurt by overall lower mortgage volumes—declining to a quarterly run rate of USD20mn in FY19. Then came covid, and with it, the lower mortgage rates as the US government (and others across the world) lowered interest rates to boost economic growth. The DR business never had it better, and reached a peak quarterly run rate of USD70mn in FY22.

**Exhibit 4: DR business grew rapidly during covid, fell off thereafter**

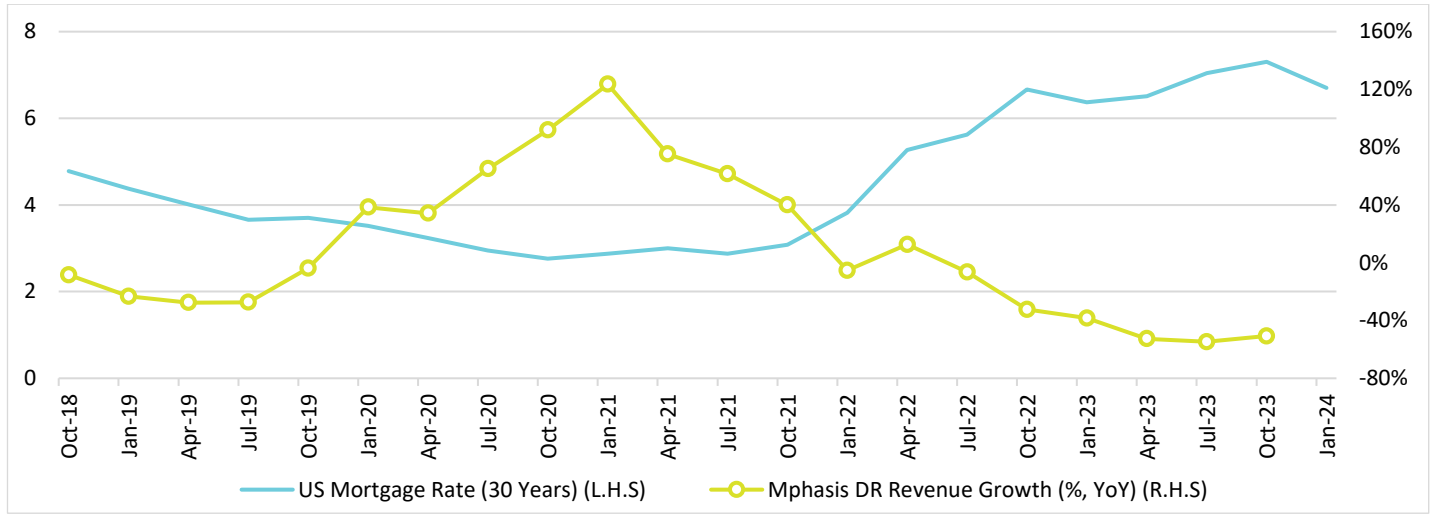


Source: Company, Nuvama Research

With the advent of 2022, the US Fed started hiking interest rates to rein in the runaway inflation. This spurred a sharp spike in mortgage rates, leading to a plunge in mortgage volumes. According to our estimates (*the company stopped reporting DR business separately from 2021*), the DR business fell over 30% in FY23. From a quarterly peak of USD70mn, the business fell to USD24mn in Q2FY24 – and has remained stable since. This affected Mphasis’s overall growth as it grew only +7.8% YoY in FY23 and declined by -6.3% YoY in FY24, whereas the Direct Core business (excluding mortgage and DXC) reported growth of 19.6% in FY23 and declined by -0.3% YoY in FY24.

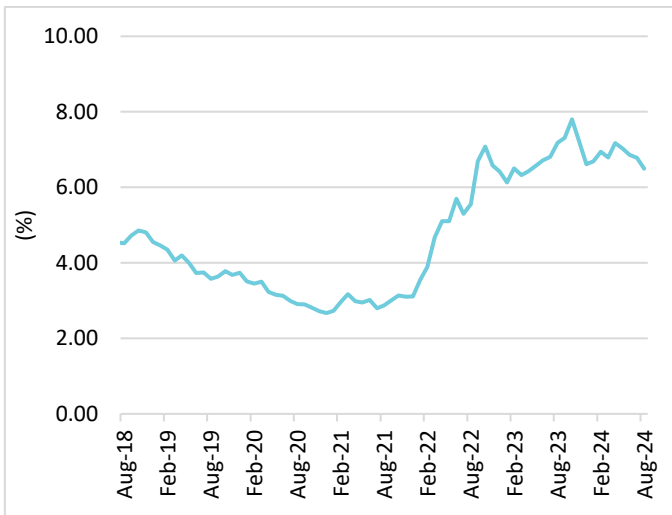
The DR business, by its very nature, has a completely inverse correlation with mortgage rates. The last five years’ history shows a remarkable inverse correlation.

**Exhibit 5: DR business has perfect inverse correlation with US mortgage rates**



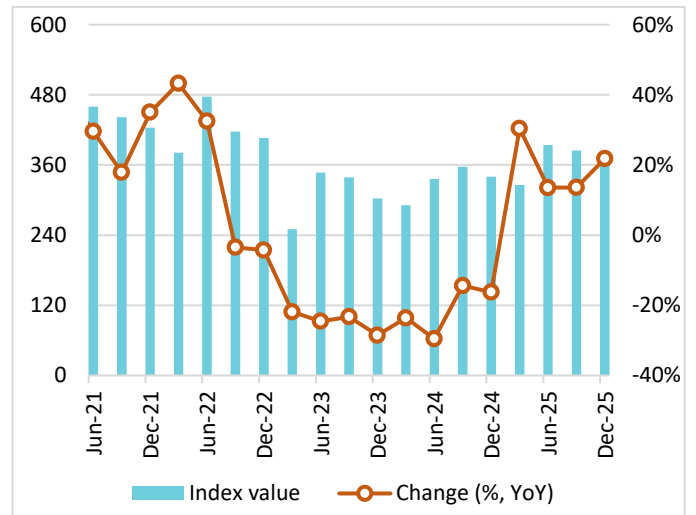
Source: Company, Nuvama Research, Bloomberg

**Exhibit 6: Mortgage rates (30-year) are gradually receding**



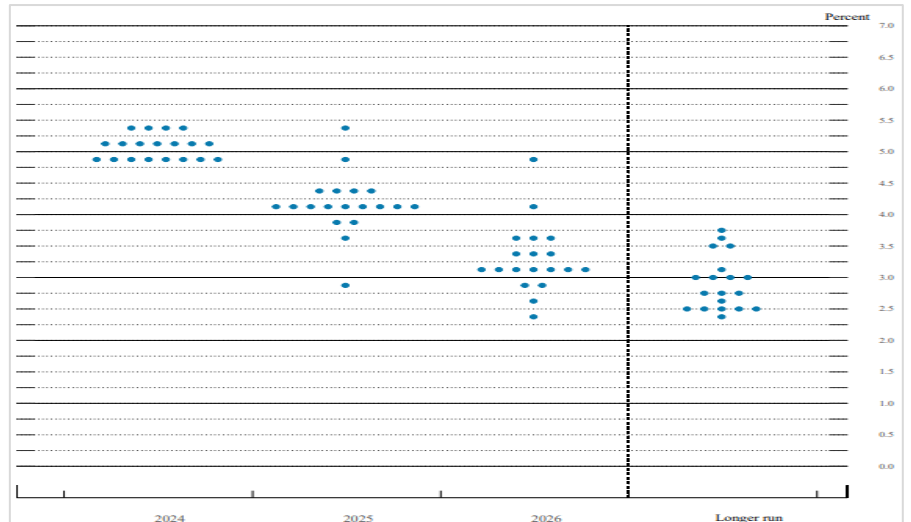
Source: FRED.

**Exhibit 7: Mortgage volumes have shown signs of pickup**



Source: Mortgage Banker Association.

**Exhibit 8: Interest rate expectations by year by FOMC members (Dot plot)**

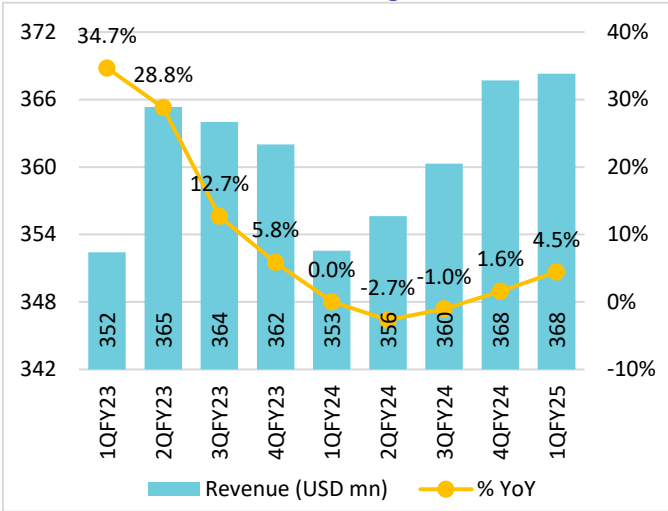


Source: FOMC (September review), Nuvama Research. Please note, above chart is from Fed Economic Projections after June-24 meeting.

## Core business remains strong

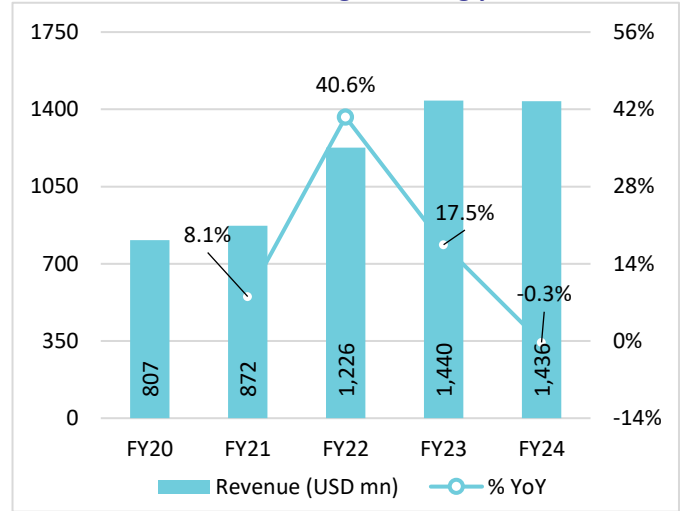
Mphasis's Direct Core business (excluding DXC and mortgage) has continued to report robust growth and deal-wins. In FY23, the business grew 17.5% YoY — among the highest in the industry. While FY24 growth was hurt by weakness in the overall industry (especially BFSI), Mphasis clocked strong deal-wins during the year – which should translate into decent growth in FY25.

**Exhibit 9: Direct Core ex-DR turning around**



Source: Company, Nuvama Research

**Exhibit 10: Direct Core ex-DR grew strongly in FY22–23**



Source: Company, Nuvama Research

Interestingly, while Mphasis's growth was severely affected by softness in DXC and the mortgage (DR) business, its growth excluding DXC was largely in line with peers. This strong growth was driven by Mphasis's robust performance across verticals – BFSI, Logistics and Hi-tech. The company's BFSI performance – despite the headwinds of a declining mortgage business – has been commendable, and is testament to its strength in this domain (more on this later).

**Exhibit 11: Direct ex-DR growth comparable to peers; overall growth weak**

USD rev growth (% YoY)	FY21	FY22	FY23	FY24
LTIMindtree	5.1	27.5	17.2	4.4
Coforge	5.8	38.0	15.6	11.7
Persistent	12.8	35.2	35.3	14.5
Mphasis				
Overall growth	5.6	21.7	7.8	-6.3
Direct growth	17.9	34.9	10.3	-4.9
<b>Direct ex DR growth</b>	<b>8.1</b>	<b>40.6</b>	<b>17.5</b>	<b>-0.3</b>

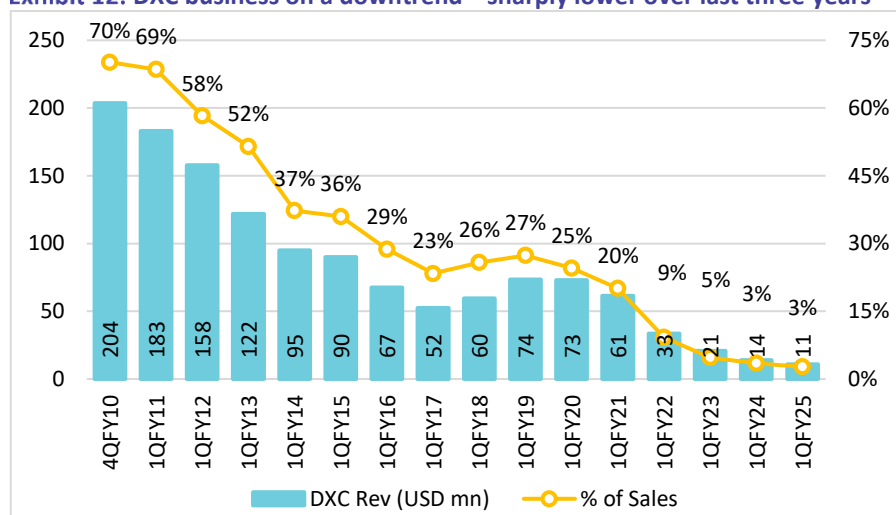
Source: Company, Nuvama Research (\*incl acquisitions)

## DXC business – Losing relevance in the overall scheme of things

The DXC business is part of the Mphasis business that has, probably, absorbed a disproportionate share of management bandwidth and drawn investor concern over the last few years. DXC has been part of Mphasis’s business since its inception – and the relationship was further cemented by an 11 years’ Master Service agreement (MSA) signed at the time Blackstone acquired Mphasis from HPE in 2016.

Under this MSA, HPE committed a minimum revenue of USD990mn over the next five years. Through this, DXC became a client of Mphasis – as part of its DXC/HP channel – which also includes revenue from HPE, HP Inc and Micro Focus. Over FY17–19, the DXC business expanded at a CAGR of 22%. In May-19, DXC appointed Mika Salvinio as the CEO, who focused on optimising the operation model for DXC. This led DXC to cut down on its subcontracting business, also driven by its acquisition of Luxoft in Jan-19. Since then, DXC has been going downhill for Mphasis with DXC channel revenue falling from USD83mn in Q4FY19 to a meagre USD11mn in Q1FY25.

**Exhibit 12: DXC business on a downtrend—sharply lower over last three years**



Source: Company, Nuvama Research

It is interesting to note that Mphasis has done remarkably well, over the last five years, in its Direct Core business (ex-DXC). Its performance, ex-DXC, has been very much in line with peers such as Coforge, Persistent, LTI and Mindtree. The company has managed to fill the void created by declining DXC revenue, by diversifying into other segments (more on this later).

Overall, DXC has now become completely irrelevant to Mphasis’s overall growth profile; management expects to achieve revenue stability in DXC at current levels. It is not a segment in which it intends to invest further.



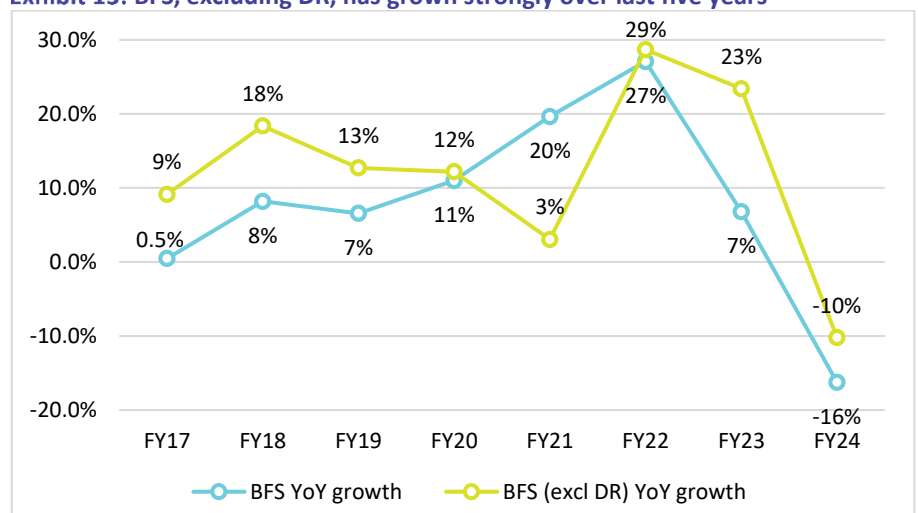
## BFS recovery and top client to boost growth

BFS is Mphasis’s largest vertical (47% of revenue) and is fairly diversified within micro verticals such as Consumer Banking, Corporate Banking, Investment Banking, Mortgage and Wealth Management. The company enjoys a long-tenured preferred relationship with marquee customers.

- Mphasis works with ten of the top-ten US banks.
- It also works with five of the top-ten European banks.
- On the employee front, 70%-plus of Mphasis’s domain specialists are financial services experts.

The BFS vertical, ex-mortgage, has recorded robust growth over the last many years. Before FY24, FY21 was the only year in which the segment reported single-digit growth – was compensated by exceptional growth in the mortgage business. FY24 anyway saw curtailed spending in the BFS segment across the board, leading to a decline in revenue for the segment. For long, Mphasis has maintained its “right to win” on this vertical, with a set of marquee clients up its sleeve. Its top client too, is from the same segment, and has been continuously growing for the company.

**Exhibit 13: BFS, excluding DR, has grown strongly over last five years**



Source: Company, Nuvama Research

Multiple indicators are alluding to early signs of a recovery in US-BFS. From the commentary of larger peers such as Accenture, TCS and Infosys to large US banks (such as JP Morgan, and Citi) talking about incremental tech spends – all pointers are indicating a period of sustained technology spends by BFS clients.

Mphasis derives 47% of its revenue from the BFS vertical – by far the highest among peers (large caps and mid caps). While this impacted its growth adversely in FY24, as the large US banks curtailed their tech spends – it should now translate into a commensurate tailwind, as the same banks are likely to revive their spends, following interest rate cuts by the US Fed.

We reckon Mphasis’s growth over the next two years shall be largely driven by a revival in spending in the BFS segment – even if we were to exclude the boost from the mortgage business.

**Exhibit 14: Mphasis has highest revenue contribution from BFSI**

Company	BFSI rev share
TCS	32.0%
Infosys	27.5%
Wipro	33.4%
HCL Tech	22.1%
Tech Mahindra	15.4%
LTIMindtree	36.2%
Coforge	56.5%
Persistent	31.8%
<b>Mphasis</b>	<b>58.5%</b>
Birlasoft	20.9%
Zensar	37.7%

Source: Company, Nuvama Research

### Top client continues to increase tech spends

Mphasis's top client has been on a tech-spending spree. In its analyst day earlier this year, the company declared it would be spending USD17bn on technology – digital banking, modernising its back office, and of course, AI adoption. The client's tech spend of USD17bn is likely to be higher than that of the other eight largest banks in the US, put together.

This higher tech spend by its top client, augurs well for Mphasis. For long, Mphasis has enjoyed a strong relationship with its top client – its revenue growing at a CAGR of 12% over last 10 years – double the company's overall CAGR of 6% over the same period.

**Exhibit 15: Top client has performed really well for Mphasis over last 10 years – growing much faster than company growth**

Mphasis	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24	CAGR
Total revenue	944.0	924.6	893.6	989.0	1,118.7	1,239.3	1,309.0	1,592.8	1,717.6	1,609.5	6.1%
% YoY	-7.9%	-2.1%	-3.4%	10.7%	13.1%	10.8%	5.6%	21.7%	7.8%	-6.3%	
<b>Top client</b>	<b>83</b>	<b>90</b>	<b>101</b>	<b>121</b>	<b>154</b>	<b>167</b>	<b>147</b>	<b>175</b>	<b>206</b>	<b>233</b>	<b>12.2%</b>
% YoY		8.7%	11.6%	20.0%	27.6%	8.6%	-12.1%	19.3%	17.5%	13.3%	
% share of rev	8.8%	9.7%	11.3%	12.2%	13.8%	13.5%	11.2%	11.0%	12.0%	14.5%	

Source: Nuvama Research, Company

## Making early inroads into Gen-AI space

Mphasis appears to have moved early, in a rigorous manner, to make inroads into the latest technology on the horizon – Gen-AI. Gen-AI is likely to completely transform the customer experience and lead to efficiencies across enterprise customers, employees and partners. While still in early stages, its potential is being realised as IT services companies move from concept to application across multiple domains within an enterprise.

Mphasis started as early as 2018, with its machine learning and AI labs at Next Labs. It has since been working with customers to build a point of view, help them think through their AI journeys on productivity, customer experience and modernisation. The company believes it is now entering a phase where platforms are getting adopted at scale and AI is beginning to seep into almost every solution.

Mphasis has recently launched two path-breaking platforms in the Gen-AI space:



**NeoZeta™:** An industry-first modernisation platform, for transforming legacy applications, written in languages like COBOL, Natural or legacy Java, using Gen-AI LLMs and LAMs to reduce relearning time by over 50%. This is particularly big for applications that are too complex and expensive for modernisation. Mphasis has already gone live with this solution and some early beta plan engagements.

**NeoCruX™:** An industry-leading platform designed to improve software engineering productivity by streamlining the software development life cycle (SDLC) processes and integrating Gen-AI functionalities. Management claims it is the first such platform in the marketplace available as an integrated development environment (IDE) extension and is already in production at two live clients.

Some client engagements as highlighted by management are:



- KYC and Know Your Businesses (KYB) modernisation for a large European bank
- Gen-AI enabled Intelligent Document Processing (IDP), for insurance clients servicing FSA and HSA claims as well as IDP solutions for mortgage clients
- Live Call Analytics for a large global bank to provide sentiment analysis, and compliance check
- AI-led developer efficiency for a large banking platform company

Some partner projects as highlighted by management:

- AWS and Mphasis have partnered in providing architecture review, solution support and guidance in ensuring faster completion of POCs and accelerating Gen-AI adoption
- Mphasis is partnering with Microsoft to improve adoption of the Microsoft Copilot stack, ensuring data governance and security, employee productivity and extending functionality with third-party and custom integration.

## Coveted clientele and diversification

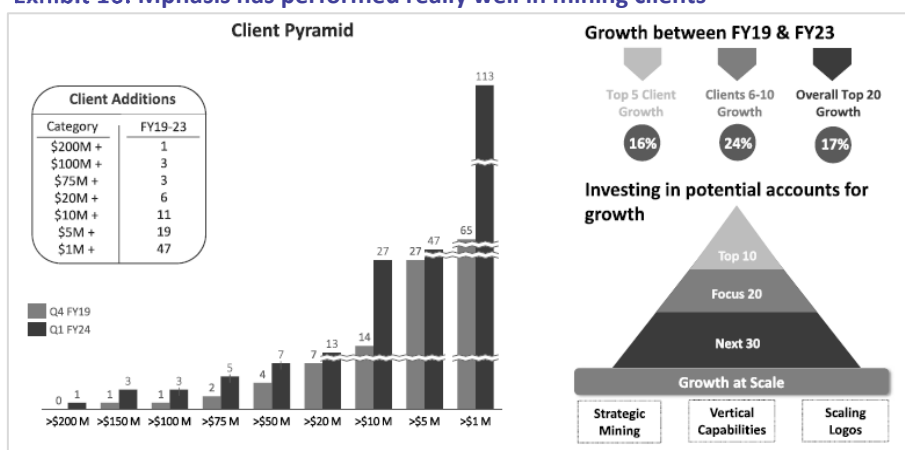
Mphasis has a coveted clientele across its verticals. It works with 20 of the Fortune 100 and 37 of the Fortune-500 companies across the four non-BFS verticals. As much as 47% of its revenue comes from the BFS segment (59% from BFSI), and it boasts the who's who of BFS as its clientele. The company:

- works with 10 of the top-ten US banks
- is chosen as a top-two vendor partner in its top-5 accounts

Over the last four years, Mphasis has particularly done well in adding clients as well as mining existing ones. While client addition had always been its strong suit, it had failed to scale up accounts over FY16–19. However, over the last five years (FY19–24), the company managed to achieve both driven by its Tribes and Squads model and focused on account-centric strategies. As a result, over FY19–24, Mphasis:

- more than doubled its total clients (>USD1mn) from 65 in FY19 to 135 in FY24
- almost doubled its clients (>USD20mn) from six in FY19 to ten in FY24
- added one/three/three clients in the USD200mn/150mn/100mn buckets— from zero in all these buckets in FY19.

**Exhibit 16: Mphasis has performed really well in mining clients**



Source: Company, Nuvama Research

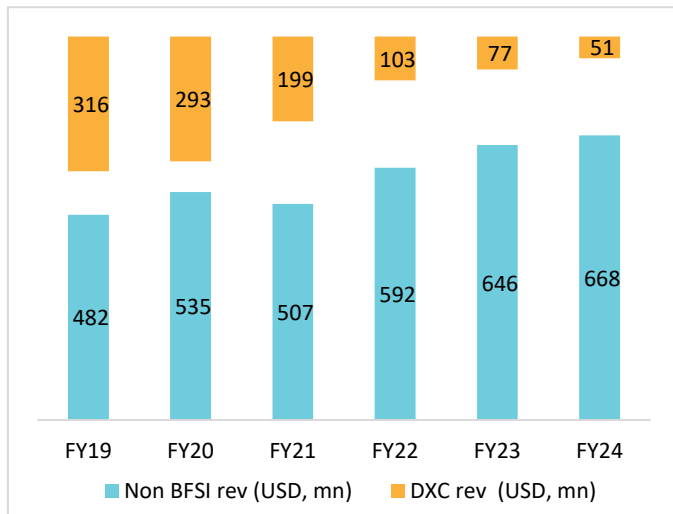
### Client diversification – a less understood story

Mphasis is often associated with high client and verticals concentration. For long, BFSI has remained ~60% of its revenue with all other verticals put together forming the remaining 40%. Top client still forms 14% of its overall revenue, and its contribution has actually increased over the last two years. The top-five client bucket too contributes 44% to Mphasis's revenue— one of the highest in the industry.

What this data does not capture however is how Mphasis has diversified its revenue, vertical and client base – while compensating for the fall in DXC revenue. Over the last eight years, DXC revenue has fallen from 24% of revenue to 3% in FY24. On an annual run rate, this translates into a fall from USD215mn in FY17 to USD51mn in FY24. Mphasis has compensated for all this lost revenue, by growing in non-BFS verticals (along with BFSI too) adding more third party clients.

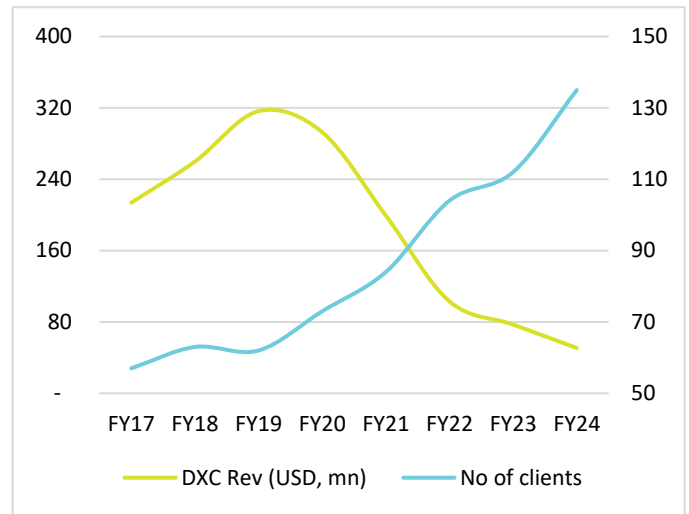
Consider this: Over FY17–24, Mphasis' total revenue grew at 8.8% CAGR. Over the same period, the BFSI revenue for Mphasis grew at 7.3% CAGR while that for non-BFSI verticals grew at 11.1% CAGR. The same is visible in the total number of USD1mn-plus clients – that more than doubled from 57 in FY17 to 135 in FY24.

**Exhibit 17: Mphasis has backfilled DXC with Non-BFSI growth**



Source: Company, Nuvama Research

**Exhibit 18: As DXC revenue fell, Mphasis grew its client base**



Source: Company, Nuvama Research

### Concentration still remains high, especially relative to peers

However, client and vertical diversification is still a work-in-progress for Mphasis. The company still has one of the more concentrated revenue profiles in the sector. Its share of top client, top-five clients and top-ten clients in the revenue – is by far, the highest in the industry. This client concentration does imply a higher business risk to the company’s operations. While we note that Mphasis’s top client is one the largest global banks, any unforeseen external event, which might impact the top/top-five clients, could have a disproportionately larger knock-on effect on Mphasis’s business than peers.

**Exhibit 19: Client concentration still among highest**

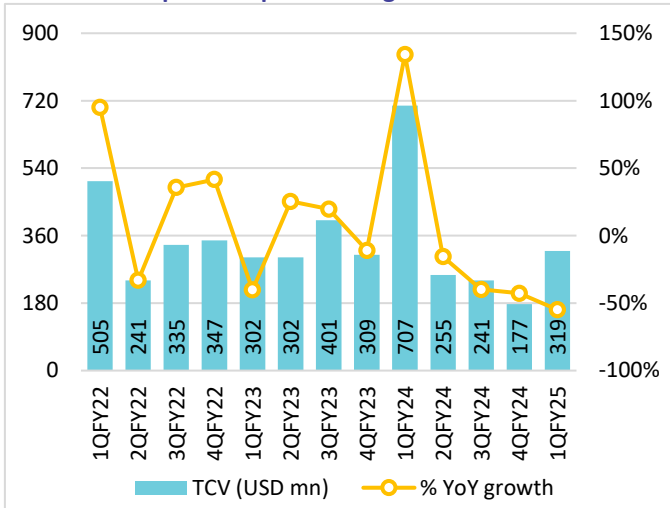
Companies	Top-5	Top-10
	FY24	FY24
Infosys	13.4%	20.2%
Wipro	12.6%	20.9%
HCLT	10.0%	17.7%
TechM	16.5%	26.5%
LTIMindtree	27.3%	34.8%
<b>Mphasis</b>	<b>45.0%</b>	<b>56.3%</b>
Persistent	28.4%	39.6%
Coforge	23.6%	35.4%

Source: Company, Nuvama Research

## Strong deal flow to sustain growth

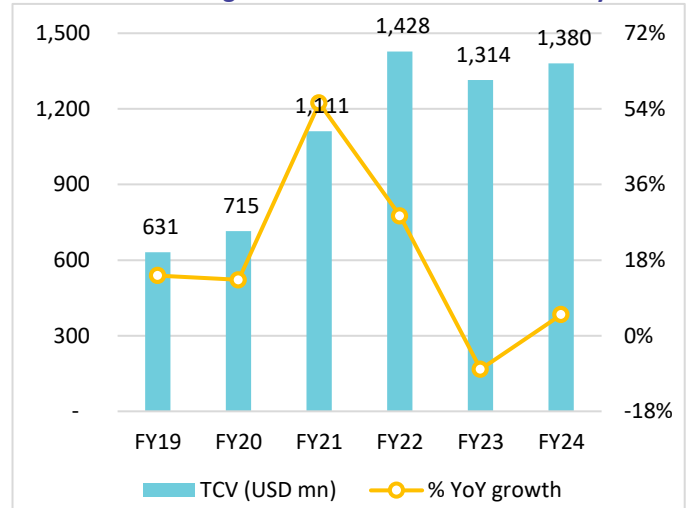
Direct Core (including DR) has reported strong deal flows for the last three years. The average quarterly deal flow for the company pre-covid stood at USD150–200mn. Mphasis, buoyed by the strong demand for transformation deals, took it well past USD300mn in FY22 (USD1.4bn annual) and has been building on it ever since. Deal-wins have been broad-based across strategic accounts and new clients. Average deal size has also increased ~2x over the past two years.

**Exhibit 20: Mphasis reports strong TC**



Source: Company, Nuvama Research

**Exhibit 21: TCV range now well over USD1bn annually**

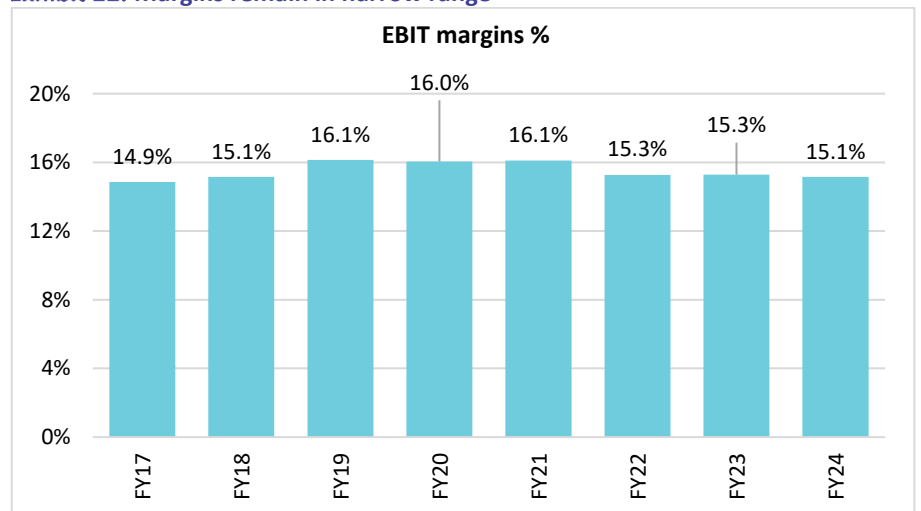


Source: Company, Nuvama Research

## Margins to remain stable

Mphasis’s margins have been highly resilient—all through pre-covid, during-covid and post-covid periods. Management takes great efforts to maintain this profile, and invest any incremental benefits, back into the business, to secure future growth. This, we believe, provides high visibility on the margin range – leading to high earnings predictability. Management has guided for a margin band of 14.5%–16% for FY25. We anticipate this band to be achieved easily.

**Exhibit 22: Margins remain in narrow range**

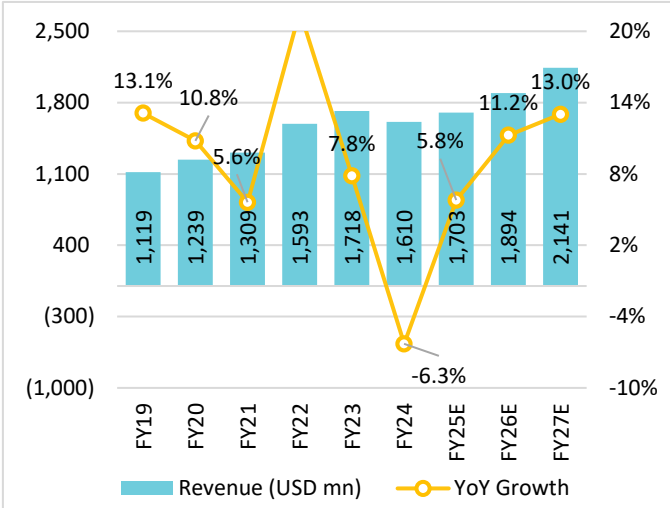


Source: Company, Nuvama Research

## Financial Outlook

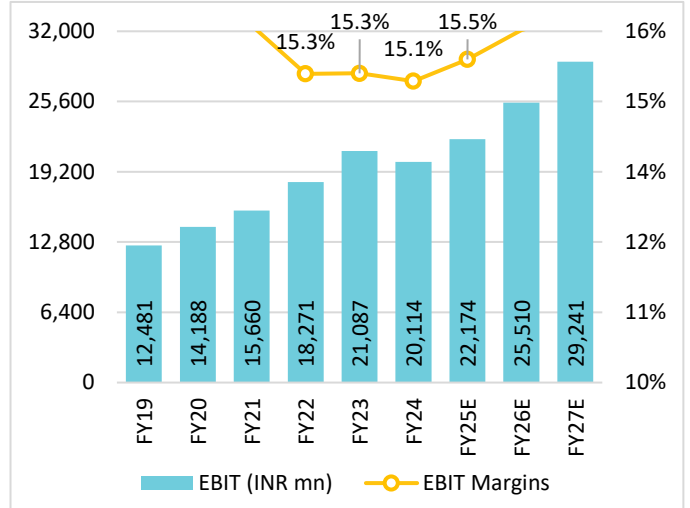
Mphasis is likely to report strong growth over the next three years—primarily driven by the BFS vertical. Its recent acquisition of Silverline is expected to boost growth by 2.9% in FY25E. All along, margins are anticipated to remain in the stable range of 15.5% (+/- 50bp).

**Exhibit 23: Revenue growth to rebound**



Source: Company, Nuvama Research

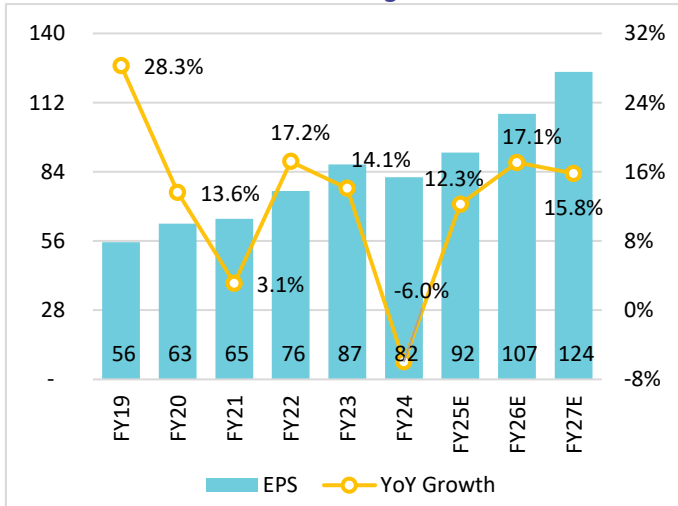
**Exhibit 24: Margins to remain stable with positive bias**



Source: Company, Nuvama Research

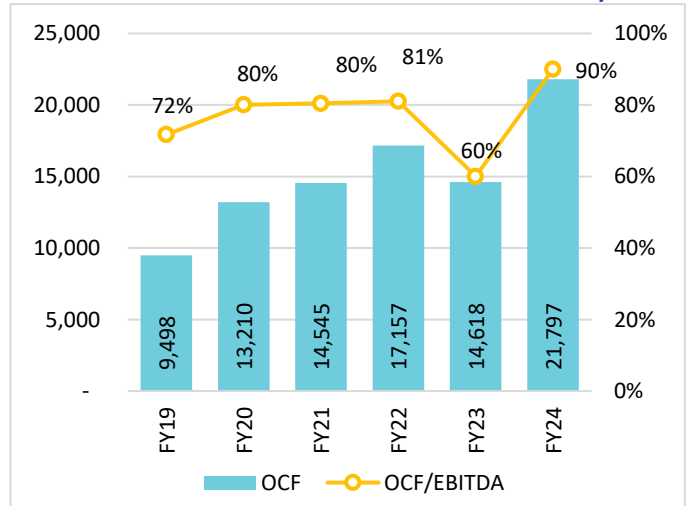
Mphasis’s earnings growth is also likely to be strong through FY27—owing to strong revenue growth and small margin expansion. While the company generates healthy cash (OCF close to 80% of EBITDA) – FY23 saw the same dropping to 60%, due to weakness in the BFSI (especially mortgage) segment – which recovered smartly in FY24. We expect cash flow conversion to remain healthy.

**Exhibit 25: EPS CAGR of 15% during FY24–27**



Source: Company, Nuvama Research

**Exhibit 26: OCF to EBITDA conversion remains healthy**



Source: Company, Nuvama Research

## Valuation

Over the last few months, Mphasis has run up (3m, +25%), outperforming most peers. It is now trading at 28x FY26E PE—broadly in line with LTIMindtree (26x) and Coforge (29x). While the earnings growth over the next three years for LTIMindtree (+17%) and Coforge (+25%) might appear higher than Mphasis (15%), we note that Mphasis is yet to recover from the weak BFS and mortgage business in FY25. This means that the earnings growth in FY26–27 shall be sharply higher. We see an upside risk to the earnings estimate for Mphasis, if there is a sharper recovery in the BFS vertical and/or the US Fed decides to cut interest rates more sharply than anticipated.

Also, while Mphasis might appear expensive on a PE basis, we note that on PEG basis, it compares well with peers and is in fact, trading at discount to most largecap peers. Even on a historical basis, its PEG compares well with its historical average, and is in line with that during the covid period – which saw strong growth in mortgage and BFSI segments – which we expect to be repeated over the next two years.

**Exhibit 27: Mphasis' PEG close to industry average**

	Pre Covid			During Covid			Current		
	PE	EPS growth	PEG	PE	EPS growth	PEG	FY26 PE	EPS growth	PEG
	Mar 2017-20	FY18-21		Mar 2020-23	FY20-23		FY24-27		
TCS	21.4	7.6%	2.8	29.1	10.2%	2.9	27.2	13.4%	2.0
Infosys	16.3	10.3%	1.6	25.2	13.6%	1.9	24.6	11.1%	2.2
Wipro	14.0	10.4%	1.3	21.2	7.5%	2.8	21.1	9.3%	2.3
HCL Tech	13.1	13.8%	0.9	19.0	10.4%	1.8	23.8	11.0%	2.2
TechM*	13.5	5.2%	2.6	18.0	7.5%	2.4	26.1	34.1%	0.8
LTIMindtree	16.3	20.9%	0.8	30.9	27.1%	1.1	26.5	17.3%	1.5
Coforge*	15.8	17.6%	0.9	29.6	16.8%	1.8	29.1	25.3%	1.1
Persistent	14.7	11.7%	1.2	28.2	39.5%	0.7	42.4	27.1%	1.6
<b>Mphasis</b>	<b>15.9</b>	<b>15.1%</b>	<b>1.0</b>	<b>24.0</b>	<b>11.3%</b>	<b>2.1</b>	<b>28.3</b>	<b>15.0%</b>	<b>1.9</b>

Source: Company, Nuvama Research (\*EPS growth high due to low margin base of FY24)

We are valuing Mphasis at 30x average of FY26–27E PE— in line with target valuation for LTIMindtree and Coforge. We upgrade to 'BUY' (from 'HOLD') with a target price of INR3,500.

**Exhibit 28: Our target valuation for Mphasis much lower than tier-2 peers**

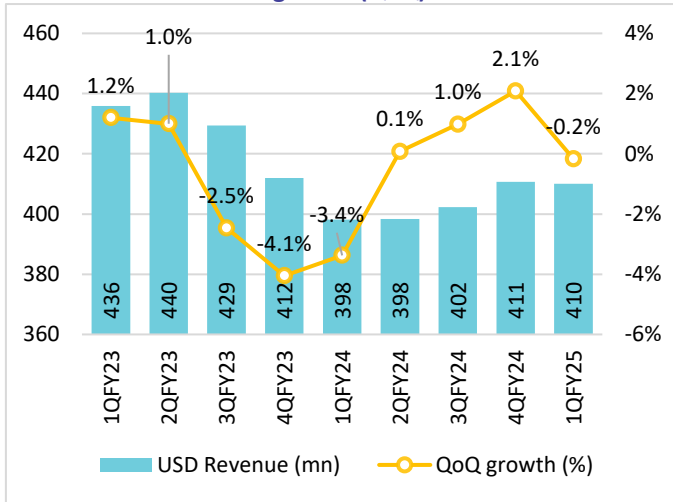
Companies	Current PE (FY26)	Target PE	Average PE		
			Last 3 years	Last 5 years	Last 10 years
Coforge	29.5	30x	30.4	27.9	20.5
Persistent	42.6	40x	36.8	30.4	23.0
<b>Mphasis</b>	<b>27.9</b>	<b>30x</b>	<b>26.3</b>	<b>23.2</b>	<b>18.8</b>
LTIM	26.4	30x	30.4	28.1	23.8

Source: Company, Nuvama Research



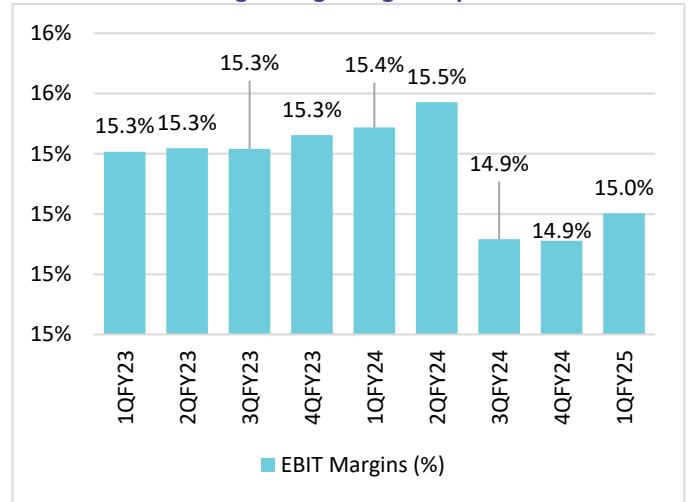
## Key charts

**Exhibit 29: USD revenue growth (QoQ)**



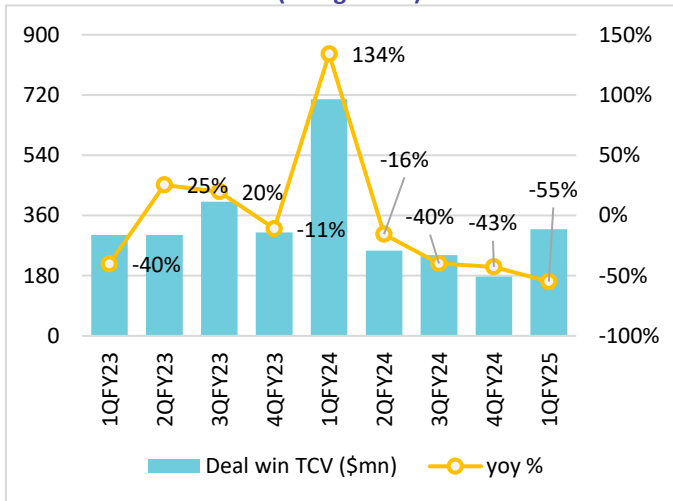
Source: Company, Nuvama Research

**Exhibit 30: EBIT margins beginning to expand**



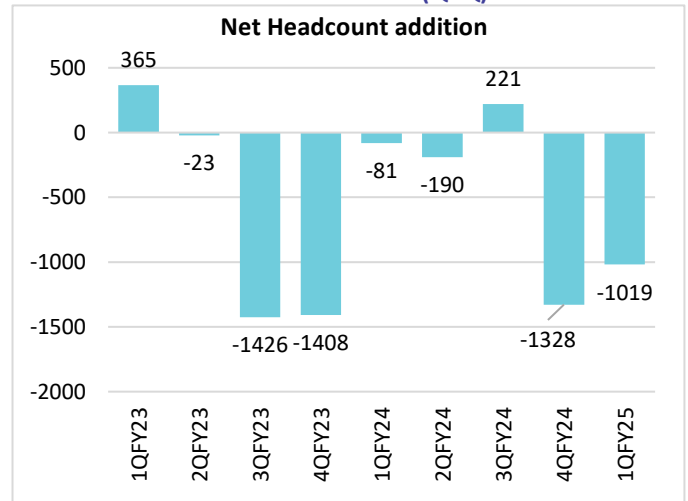
Source: Company, Nuvama Research

**Exhibit 31: Deal-win TCV (YoY growth)**



Source: Company, Nuvama Research

**Exhibit 32: Net headcount reduction (QoQ)**



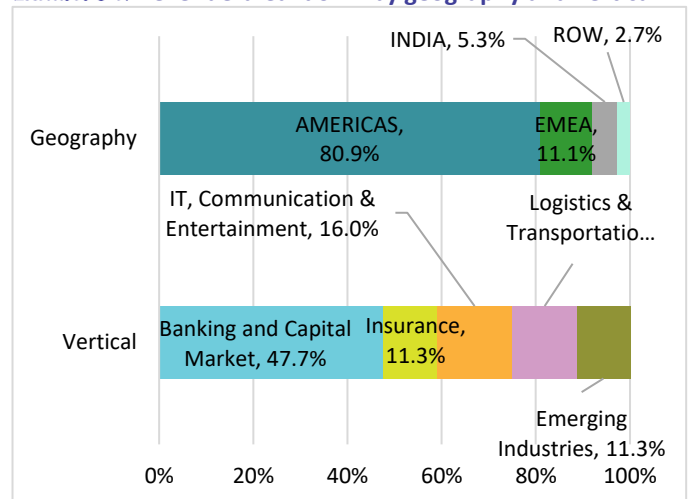
Source: Company, Nuvama Research

**Exhibit 33: Revenue contribution by clients**



Source: Company, Nuvama Research

**Exhibit 34: Revenue breakdown by geography and vertical**



Source: Company, Nuvama Research

## Company Description

Mphasis was formed in June 2000 following the merger of the US-based IT consulting company Mphasis Corporation (founded in 1998) and Indian IT services company BFL Software Limited (founded in 1992).

In June 2006, Electronics Data Systems Corporation (EDS) acquired a majority holding in Mphasis' equity capital. In August 2008, EDS itself was acquired by Hewlett-Packard (HP). In September 2016, Blackstone Group, through its fund "Marble II PTE", acquired HP's stake in Mphasis - thereby making it a Blackstone group company. Mphasis derives ~95% of revenue from the Direct International segment. By geography, Mphasis operates in the Americas, EMEA and India, and has the highest presence in the Americas (79%) in terms of revenue.

The company focuses on five key industry verticals: Banking and capital market, Insurance, IT & Communication, Logistics & Transportation and Emerging verticals (Healthcare). BFSI continues to be its biggest source of revenue (58%).

## Investment theme

Mphasis derives ~95% of revenue from the Direct International segment. By geography, Mphasis operates in the Americas, EMEA and India, and has the highest presence in the Americas (79%) in terms of revenue.

The company focuses on five key industry verticals: Banking and capital market, Insurance, IT & Communication, Logistics & Transportation and Emerging verticals (Healthcare). BFSI continues to be its biggest source of revenue (58%). The other verticals - Logistics (and transportation) and Technology, Media & Telecom (TMT) contributes ~13% each. Within others (11% of revenue), the company has manufacturing and healthcare/pharma clients. It works with 20 of the Fortune 100 and 37 of the Fortune-500 companies across the four verticals.

Given the low base of FY24, revival in non-mortgage-BFS and other verticals – we believe Mphasis can achieve double-digit growth in FY26. The growth will largely be driven by the interest rate cycle – which should benefit Mphasis disproportionately, when it reverses.

## Key Risks

- **Client concentration:** Top client, top-five clients and top-ten clients contribute 14%, 44% and 54% to revenue, respectively, in Q4FY24. Any loss of key clients can hamper Mphasis's growth momentum.
- **Geographical concentration:** Americas and EMEA collectively contribute 92% to total revenue.
- **Vertical concentration:** BFSI forms 58% of the revenue for Mphasis – leading to significant risk from any macro event impacting the banking industry.
- **Generic currency risk:** The exchange rate volatility in USD and EUR vis-à-vis INR can result in significant volatility in the Mphasis's operating results.

## Additional Data

### Management

CMO	Veda Iyer
CEO	Nitin Rakesh
CFO	Aravind Viswanathan

### Holdings – Top 10\*

	% Holding	% Holding	
BCP Topco IX Pt	40.35	ICICI Prudentia	2.03
LIC of India	6.62	Vanguard Group	1.76
Kotak Mahindra	5.41	Blackrock Inc	1.70
HDFC AMC	2.94	Government Pens	1.66
Mirae Asset Glo	2.06	HDFC Life Insur	1.25

\*Latest public data

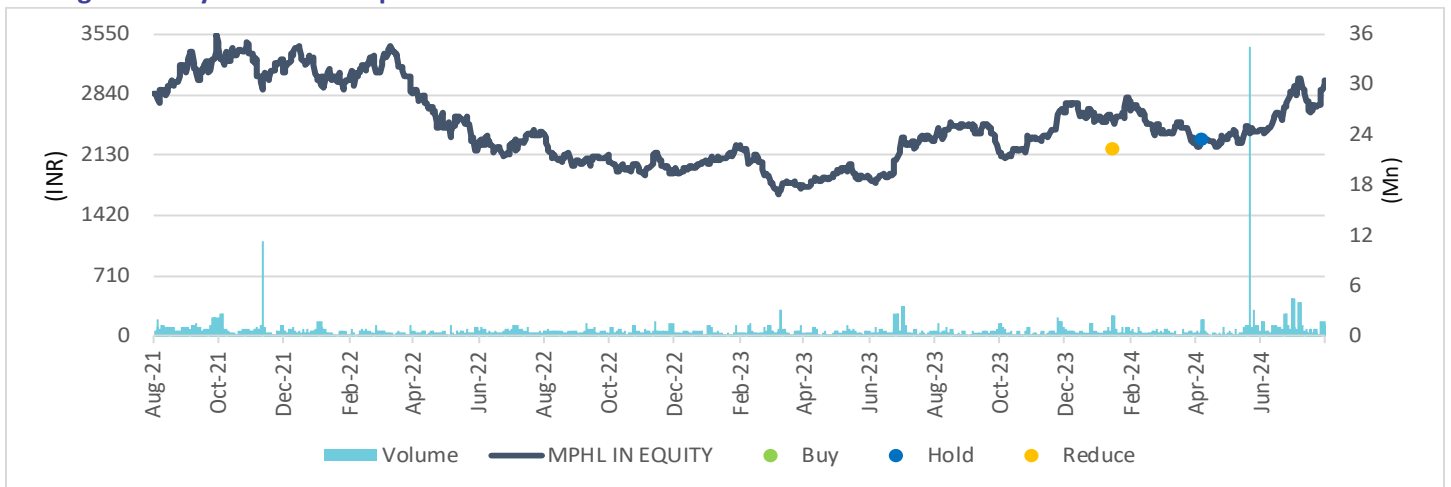
### Recent Company Research

Date	Title	Price	Reco
26-Jul-24	Modest results; outlook sanguine; <i>Result Update</i>	2,845	Hold
26-Apr-24	Decent results; gradual recovery in play; <i>Result Update</i>	2,298	Hold
02-Feb-24	Numbers weak; outlook remains bleak; <i>Result Update</i>	2,555	Reduce

### Recent Sector Research

Date	Name of Co./Sector	Title
14-Aug-24	eClerx Services	In-line results; margins to remain soft; <i>Result Update</i>
10-Aug-24	TCS	All set to ride the next tech cycle; <i>Nuvama Flash</i>
02-Aug-24	IT	Amazon: AWS continues to accelerate; <i>Sector Update</i>

### Rating and Daily Volume Interpretation



Source: Bloomberg, Nuvama research

### Rating Rationale & Distribution: Nuvama Research

Rating	Expected absolute returns over 12 months	Rating Distribution
Buy	15%	218
Hold	<15% and >-5%	60
Reduce	<-5%	27

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