

12 August 2011

MF Global Quarterly Report

# Tech Mahindra

| Revenues in line, margins disappoint

IT SERVICES

TECHM IN: **NEUTRAL**

RS 735

Tech Mahindra's 1QFY12 revenue growth was in line with our estimates, although margin decline of 180bp surprised us negatively. Revenues from BT (Buy; PT: GBP230\*) continued to be flat in GBP terms. Margin hit was mainly due to steep drop in utilization. The management indicated that BT is putting 'significant' contracts out for tender. The impact of this is difficult to quantify, however the re-bid could result in billing rate pressure. The company will be giving salary hikes in 2QFY12 which will have further margin pressure.

## Revenue growth in line, Margins decline 180bps

- » Tech Mahindra's US\$ revenues at \$290mn grew by 4.1% QoQ in line with our estimate of 3.5%. In constant currency, USD revenues grew by 2% QoQ, largely driven by growth in emerging markets.
- » In INR terms, Q1FY12 revenue at Rs12.9bn, grew 2.5% QoQ
- » BT revenues at US\$116mn grew by 1.5% QoQ. In GBP terms, BT was flat QoQ
- » EBITDA margins contracted by 180bps to 18.7% QoQ due to a 300bp drop in utilization during the quarter.
- » PAT excluding associates' profit at Rs1.8bn declined by 12.6% QoQ
- » PAT including Mahindra Satyam was at Rs2.8bn vs Rs925mn in 4QFY11.

**Valuation:** We value the stock at 9x FY13E earnings (excluding Satyam and restructuring charge) and assign a 25% holding company discount to Satyam's valuation. Maintain Neutral.

\* Covered by John Karidis, Telecom analyst, MF Global UK Ltd.

## VALUATION SUMMARY

Y/E MAR, RS MN	FY2009	FY2010	FY2011	FY2012E	FY2013E
NET SALES	44,647	46,254	51,402	54,185	58,181
GROWTH, %	18.5	3.6	11.1	5.4	7.4
EBIDTA	11,902	11,325	10,033	10,474	10,487
EBIDTA MARGINS, %	26.7	24.5	19.5	19.3	18.0
CORE EBIDTA	11,902	11,325	10,033	10,474	10,487
NET PROFIT (EXCL. SATYAM)	9,224	7,090	7,437	6,848	6,936
NET PROFIT MARGIN, %	20.7	15.3	14.5	12.6	11.9
EPS, RS	71.0	54.5	57.1	51.9	52.6
EPS GROWTH, %	19.8	(23.1)	4.7	(9.1)	1.3
PER, X	10.4	13.5	12.9	14.2	14.0
EV/EBIDTA, X	7.6	9.5	9.5	9.1	8.4
EV/NET SALES, X	2.0	2.3	1.8	1.8	1.5
PRICE/BOOK VALUE, X	4.9	3.3	2.2	1.8	1.5
ROIC, %	81.7	58.4	39.7	40.3	42.1
ROE, %	57.2	29.2	20.4	14.0	11.8
DIVIDEND YIELD %	0.5	0.4	0.3	0.4	0.4

Source: Company, MF Global India Research Estimates

## TARGET RS 720 (-2%)

### SECTOR RATING

OW	N	UW

### STOCK RATING

BUY	NEUTRAL	SELL
> 15%	-15% TO +15%	< -15%

## COMPANY DATA

O/S SHARES :	127MN
MARKET CAP (RS) :	93BN
MARKET CAP (USD) :	2.1BN
52 - WK HI/LO (RS) :	813 / 539
LIQUIDITY 3M (USD) :	3.8MN
FACE VALUE (RS) :	10

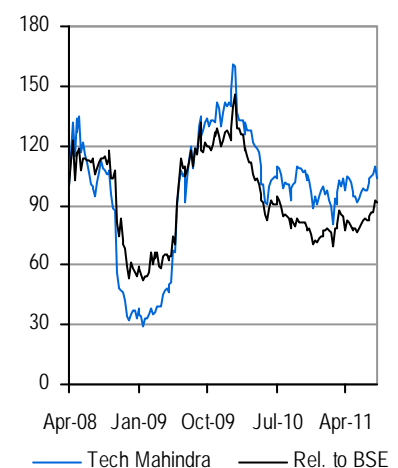
## SHARE HOLDING PATTERN, %

PROMOTERS :	71.1
FII / NRI :	4.3
FI / MF :	15.0
NON-PROMOTER CORP. HOLDINGS :	0.9
PUBLIC & OTHERS :	8.7

## PRICE PERFORMANCE, %

	1MTH	3MTH	1YR
ABS	-1.0	10.0	3.2
REL TO BSE	7.5	18.2	10.0

## PRICE VS. SENSEX



Source: Bloomberg, MF Global India Research

#### QUARTERLY RESULTS

RS MN	Q1FY12	Q4FY11	QOQ(%)	Q1FY11	YOY (%)
NET SALES	12,925	12,615	2.5%	11,337	14.0%
TOTAL INCOME	12,925	12,615		11,337	
OPERATING EXPENSES	10,507	10,025		9,210	
EBITDA	2,418	2,590	-6.7%	2,127	13.7%
MARGINS (%)	18.7%	20.5%		18.8%	
DEPRECIATION	334	387		354	
EBIT	2,084	2,203	-5.4%	1,773	17.5%
MARGINS (%)	16.1%	17.5%		15.6%	
PRE-TAX PROFIT	2,321	2,307	0.6%	1,762	31.7%
TAX PROVIDED	509	226		312	
PROFIT AFTER TAX	1,805	2,065	-12.6%	1,444	25.0%
MF NET PROFIT	1,805	2,065	-12.6%	1,444	25.0%
EPS, RS	13.7	15.9		11.1	

Source: Company, MF Global India Research;

Note: Excluding Satyam's earnings and not adjusted for restructuring fees

## FINANCIALS

### INCOME STATEMENT

Y/E MAR, RS MN	FY2009	FY2010	FY2011	FY2012E	FY2013E
<b>NET SALES</b>	<b>44,647</b>	<b>46,254</b>	<b>51,402</b>	<b>54,185</b>	<b>58,181</b>
GROWTH, %	19	4	11	5	7
OPERATING EXPENSES	-32,745	-34,929	-41,369	-43,711	-47,695
<b>EBITDA (CORE)</b>	<b>11,902</b>	<b>11,325</b>	<b>10,033</b>	<b>10,474</b>	<b>10,487</b>
GROWTH, %	44.2	(4.8)	(11.4)	4.4	0.1
MARGIN, %	26.7	24.5	19.5	19.3	18.0
DEPRECIATION	-1,097	-1,338	-1,435	-1,531	-1,629
<b>EBIT</b>	<b>10,805</b>	<b>9,987</b>	<b>8,598</b>	<b>8,943</b>	<b>8,858</b>
GROWTH, %	44.2	(4.8)	(11.4)	4.4	0.1
MARGIN, %	26.7	24.5	19.5	19.3	18.0
INTEREST PAID	-25	-2,184	-999	-771	-516
OTHER NON-OPERATING INCOME	-378	754	1,174	812	821
<b>PRE-TAX PROFIT</b>	<b>10,402</b>	<b>8,557</b>	<b>8,773</b>	<b>8,984</b>	<b>9,163</b>
TAX PROVIDED	-1,178	-1,440	-1,315	-2,108	-2,199
<b>MF NET PROFIT</b>	<b>9,224</b>	<b>7,090</b>	<b>7,437</b>	<b>6,848</b>	<b>6,936</b>
GROWTH, %	19.8	(23.1)	4.9	(7.9)	1.3
<b>NET PROFIT (ADJUSTED)</b>	<b>9,224</b>	<b>7,090</b>	<b>7,437</b>	<b>6,848</b>	<b>6,936</b>
EXTRAORDINARY ITEMS: GAINS/(LOSSES)	0	-85	0	0	0
UNADJ. SHARES (M)	130	130	130	132	132
WTD AVG SHARES (M)	130	130	130	132	132

Note: Excluding Satyam's earnings and not adjusted for restructuring fees

### CASH FLOW

Y/E MAR, RS MN	FY2009	FY2010	FY2011	FY2012E	FY2013E
PRE-TAX PROFIT	10,402	8,557	8,773	8,984	9,163
DEPRECIATION	1,097	1,338	1,435	1,531	1,629
CHG IN WORKING CAPITAL	2,944	-5,777	-3,536	7,053	-2,492
TOTAL TAX PAID	-1,259	6,040	-3,442	-7,864	-2,110
OTHER OPERATING ACTIVITIES	-1,824	2,702	7,876	3,236	3,809
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>	<b>11,360</b>	<b>12,861</b>	<b>11,106</b>	<b>12,940</b>	<b>9,999</b>
CAPITAL EXPENDITURE	-1,621	-4,069	542	-3,300	-2,100
CHG IN INVESTMENTS	-3,714	-25,798	1,064	-8,615	0
<b>CASH FLOW FROM INVESTING ACTIVITIES</b>	<b>-5,335</b>	<b>-29,867</b>	<b>1,606</b>	<b>-11,915</b>	<b>-2,100</b>
FREE CASH FLOW	6,025	-17,006	12,711	1,025	7,899
EQUITY RAISED/(REPAID)	30	50	37	-43	0
DEBT RAISED/(REPAID)	-300	13,672	-1,445	-5,176	-2,952
DIVIDEND (INCL. TAX)	-1,352	91	-501	-377	-457
<b>CASH FLOW FROM FINANCING ACTIVITIES</b>	<b>-1,619</b>	<b>13,811</b>	<b>-1,910</b>	<b>-5,620</b>	<b>-3,432</b>
NET CHG IN CASH	4,406	-3,195	10,802	-4,594	4,467

## BALANCE SHEET

AS AT 31ST MAR, RS MN	FY2009	FY2010	FY2011	FY2012E	FY2013E
CASH & BANK	5,382	2,187	12,989	8,395	12,861
DEBTORS	9,022	10,420	12,468	12,697	14,254
INVENTORY	13	14	0	5	10
LOANS & ADVANCES	1,271	6,724	8,321	1,543	1,656
OTHER CURRENT ASSETS	1,682	0	0	2,487	2,829
<b>TOTAL CURRENT ASSETS</b>	<b>17,370</b>	<b>19,345</b>	<b>33,778</b>	<b>25,126</b>	<b>31,611</b>
INVESTMENTS	4,346	30,144	29,081	37,695	37,695
NET FIXED ASSETS	6,520	9,251	7,274	9,043	9,514
<b>TOTAL ASSETS</b>	<b>28,432</b>	<b>59,016</b>	<b>70,770</b>	<b>72,502</b>	<b>79,458</b>
<b>CURRENT LIABILITIES</b>	<b>6,738</b>	<b>5,895</b>	<b>5,631</b>	<b>8,437</b>	<b>7,756</b>
PROVISIONS	2,150	2,770	3,080	3,430	3,676
<b>TOTAL CURRENT LIABILITIES</b>	<b>8,888</b>	<b>8,665</b>	<b>8,711</b>	<b>11,867</b>	<b>11,432</b>
NON-CURRENT LIABILITIES	0	21,349	18,064	7,051	4,098
<b>TOTAL LIABILITIES</b>	<b>8,888</b>	<b>30,014</b>	<b>26,775</b>	<b>18,917</b>	<b>15,530</b>
PAID-UP CAPITAL	1,217	1,223	1,260	1,217	1,217
RESERVES & SURPLUS	18,214	27,640	42,576	52,203	62,542
SHAREHOLDERS' EQUITY	19,544	29,002	43,995	53,585	63,928
<b>TOTAL EQUITY &amp; LIABILITIES</b>	<b>28,432</b>	<b>59,016</b>	<b>70,770</b>	<b>72,502</b>	<b>79,458</b>

## PER-SHARE DATA

	FY2009	FY2010	FY2011	FY2012E	FY2013E
MF EPS (INR)	71.0	54.5	57.1	51.9	52.6
GROWTH, %	19.8	(23.1)	4.7	(9.1)	1.3
BOOK NAV/SHARE (INR)	150.3	223.1	337.8	406.0	484.4
FDEPS (INR)	71.0	54.5	57.1	51.9	52.6
CEPS (INR)	79.4	64.8	68.1	63.5	64.9
CFPS (INR)	104.3	72.3	15.8	67.4	40.7
DPS (INR)	3.8	2.7	2.5	3.0	2.6

## FINANCIAL STRUCTURE

	FY2009	FY2010	FY2011	FY2012E	FY2013E
TOTAL DEBT/EQUITY (%)	-	47.1	27.8	13.2	6.4
NET DEBT/EQUITY (%)	(27.5)	39.6	(1.7)	(2.5)	(13.7)

**PROFITABILITY, PRODUCTIVITY, LIQUIDITY AND VALUATION RATIOS**

	FY2009	FY2010	FY2011	FY2012E	FY2013E
RETURN ON ASSETS (%)	36.5	19.5	12.5	10.3	9.6
RETURN ON EQUITY (%)	57.2	29.2	20.4	14.0	11.8
RETURN ON INVESTED CAPITAL (%)	81.7	58.4	39.7	40.3	42.1
ROIC/COST OF CAPITAL (X)	10.3	6.7	4.7	4.9	5.2
ROIC - COST OF CAPITAL (%)	73.8	49.6	31.2	32.1	34.1
RETURN ON CAPITAL EMPLOYED (%)	52.8	23.4	14.0	11.6	11.0
COST OF CAPITAL (%)	7.9	8.7	8.5	8.2	8.1
ROCE - COST OF CAPITAL (%)	44.9	14.7	5.5	3.4	2.9
ASSET TURNOVER (X)	3.5	2.9	2.4	2.7	3.1
SALES/TOTAL ASSETS (X)	1.8	1.1	0.8	0.8	0.8
SALES/NET FA (X)	7.1	5.9	6.2	6.6	6.3
WORKING CAPITAL/SALES (X)	0.1	0.2	0.3	0.1	0.2
FIXED CAPITAL/SALES (X)	-	-	-	-	-
RECEIVABLE DAYS	73.8	82.2	88.5	85.5	89.4
INVENTORY DAYS	0.1	0.1	-	0.0	0.1
PAYABLE DAYS	75.1	61.6	49.7	87.2	90.0
CURRENT RATIO (X)	2.3	2.7	5.0	2.6	3.5
QUICK RATIO (X)	2.3	2.7	5.0	2.6	3.5
INTEREST COVER (X)	435.7	4.6	8.6	11.6	17.2
DIVIDEND COVER (X)	18.9	20.2	23.1	17.5	20.0
PER (X)	10.4	13.5	12.9	14.2	14.0
PEG (X) - Y-O-Y GROWTH	0.5	(0.6)	2.7	(1.6)	11.0
PRICE/BOOK (X)	4.9	3.3	2.2	1.8	1.5
YIELD (%)	0.5	0.4	0.3	0.4	0.4
EV/NET SALES (X)	2.0	2.3	1.8	1.8	1.5
EV/EBITDA (X)	7.6	9.5	9.5	9.1	8.4
EV/EBIT (X)	7.6	9.5	9.5	9.1	8.4
EV/NOPLAT (X)	8.4	10.8	10.9	11.4	10.6
EV/CE	4.3	2.1	1.5	1.5	1.3
EV/IC (X)	7.0	6.6	4.4	4.8	4.7

Source: Company, MF Global India Research Estimates

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**RECOMMENDATION HISTORY**

RECOMMENDATION	TARGET, RS	CMP, RS	DATE
NEUTRAL	720	659	26 MAY 2011
NEUTRAL	700	689	24-JANUARY 2011
NEUTRAL	729	786	27-OCTOBER 2010
NEUTRAL	782	756	9-JULY-2010

VINEET BHATNAGAR	MANAGING DIRECTOR	91-22-2300 2999	VBHATNAGAR@MFGLOBAL.COM
SAJID KHALID	HEAD – INSTITUTIONAL EQUITIES	91-22-6667 9972	SAKHALID@MFGLOBAL.COM
JIGNESH SHAH	HEAD – EQUITY DERIVATIVES	91-22-6667 9735	JSHAH@MFGLOBAL.COM

#### EQUITY RESEARCH

MANISH AGARWALLA	VP - BANKING	91-22-6667 9962	MAGARWALLA@MFGLOBAL.COM
AARTHISUNDARI JAYAKUMAR	PHARMACEUTICALS	91-22-6667 9950	AJAYAKUMAR@MFGLOBAL.COM
ABHISHEK RANGANATHAN, CFA	RETAIL, REAL ESTATE	91-22-6667 9952	ABHISHEKR@MFGLOBAL.COM
ANJALI VERMA	ECONOMIST	91-22-6667 9969	ANVERMA@MFGLOBAL.COM
ANKUR SHARMA	ENGINEERING, CAPITAL GOODS	91-22-6667 9759	ASHARMA@MFGLOBAL.COM
DEEPAK JAIN	AUTOMOBILES & AUTO ANCILLARIES	91-22-6667 9758	DJAIN@MFGLOBAL.COM
DHAWAL DOSHI	METALS, POWER	91-22-6667 9769	DDOSHI@MFGLOBAL.COM
DIPEESH SOHANI	REAL ESTATE, MIDCAP	91-22-6667 9756	DSOHANI@MFGLOBAL.COM
ENNETTE FERNANDES	FMCG	91-22-6667 9764	EFERNANDES@MFGLOBAL.COM
GAURI ANAND	OIL & GAS, FERTILISER	91-22-6667 9943	GANAND@MFGLOBAL.COM
KAPIL BAGARIA	MIDCAP, SUGAR	91-22-6667 9965	KBAGARIA@MFGLOBAL.COM
NAVEEN KULKARNI, CFA, FRM	TELECOM, FMCG, MEDIA	91-22-6667 9947	NKULKARNI@MFGLOBAL.COM
SACHIT MOTWANI	BANKING	91-22-6667 9953	SMOTWANI@MFGLOBAL.COM
VAIBHAV AGARWAL	CEMENT	91-22-6667 9967	VAGARWAL@MFGLOBAL.COM
VIBHOR SINGHAL	INFRASTRUCTURE	91-22-6667 9949	VSINGHAL@MFGLOBAL.COM
VIHANG NAIK, CFA	IT SERVICES, MIDCAP	91-22-6667 9768	VNAIK@MFGLOBAL.COM
VIVEKANAND SUBBARAMAN	TELECOM, MEDIA	91-22-6667 9766	VSUBBARAMAN@MFGLOBAL.COM
DHARMESH SHAH	RESEARCH ASSOCIATE	91-22-6667 9974	DHSHAH@MFGLOBAL.COM
JISHAR THOOMBATH	RESEARCH ASSOCIATE	91-22-6667 9986	JTHOOMBATH@MFGLOBAL.COM
NEHA GARG	RESEARCH ASSOCIATE	91-22-6667 9996	NGARG@MFGLOBAL.COM
SAURABH RATHI	RESEARCH ASSOCIATE	91-22-6667 9951	SRATHI@MFGLOBAL.COM
VARUN VIJAYAN	RESEARCH ASSOCIATE	91-22-6667 9992	VVIJAYAN@MFGLOBAL.COM
GANESH DEORUKHKAR	PRODUCTION	91-22-6667 9966	GDEORUKHKAR@MFGLOBAL.COM
ROSHNI KALLOOR	RESEARCH COMPLIANCE OFFICER	91-22-6667 9762	RKALLOOR@MFGLOBAL.COM

#### TECHNICAL & QUANT RESEARCH

NEPPOLIAN PILLAI	CHIEF TECHNICAL STRATEGIST	91-22-6667 9989	PNEPPOLIAN@MFGLOBAL.COM
SHIKHA KHURANA	QUANT ANALYST	91-22-6667 9948	SKHURANA@MFGLOBAL.COM

#### INSTITUTIONAL CASH EQUITY SALES

SUDHIR PADIYAR	VP - EQUITY SALES (ASIAPAC)	91-22-6667 9991	SPADIYAR@MFGLOBAL.COM
KINSHUK TIWARI	EQUITY SALES	91-22-6667 9946	KTIWARI@MFGLOBAL.COM
PAWAN KAKUMANU	EQUITY SALES	91-22-6667 9934	PKAKUMANU@MFGLOBAL.COM
SHIV CHANANI	EQUITY SALES	91-22-6667 9944	SCHANANI@MFGLOBAL.COM
SHUBHANGI AGRAWAL	EQUITY SALES	91-22-6667 9964	SAGRAWAL@MFGLOBAL.COM
ROSIE FERNS	SR. EXEC. – EQUITIES SALES SUPPORT	91-22-6667 9971	RFERNS@MFGLOBAL.COM

#### INSTITUTIONAL CASH EQUITY SALES TRADING

SUNIL KAMATH	VP - SALES TRADER	91-22-6667 9747	SKAMATH@MFGLOBAL.COM
CHETAN SAVLA	SALES TRADER	91-22-6667 9749	CSAVLA@MFGLOBAL.COM
RAJESH ASHAR	SALES TRADER	91-22-6667 9746	RASHAR@MFGLOBAL.COM

#### INSTITUTIONAL CASH EQUITY DEALING

MAYUR SHAH	DEALER	91-22-6677 9945	MASHAH@MFGLOBAL.COM
GURUDATT UCHIL	DEALER	91-22-6667 9750	GUCHIL@MFGLOBAL.COM

#### Rating Rationale

BUY and SELL recommendations are used to draw attention to stocks, which we believe are under-priced or over-priced by circa 15%, that is, price differential of +/- 15% between our price target and the market price. Stocks which do not achieve this price differential are NEUTRAL. Price targets are established in the context of a flat market.

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MF Global Sify Securities India Pvt. Limited, 2nd Floor, C-Block, Modern Centre, Mahalaxmi, Mumbai-400 011

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India Pvt. Limited**  
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Mahalaxmi, Mumbai  
400 011

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