

RESULTS REVIEW
Tech Mahindra Limited
Hold
Share Data

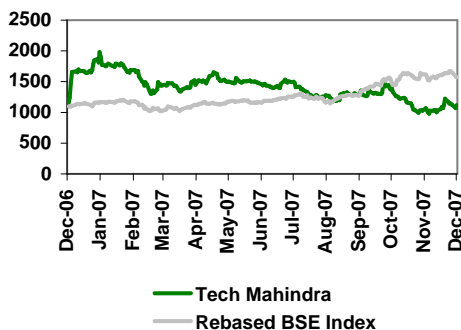
Market Cap	Rs. 135.88 bn
Price	Rs. 1,120.30
BSE Sensex	19,079.64
Reuters	TEML.BO
Bloomberg	TECHM IN
Avg. Volume (52 Week)	0.3 mn
52-Week High/Low	Rs. 2,049.8 / 974
Shares Outstanding	121.29 mn

Valuation Ratios (Consolidated)

Year to 31 March	2008E	2009E
EPS (Rs.)	59.3	78.9
+/- (%)	26.3%	32.9%
PER (x)	18.9x	14.2x
EV/ Sales (x)	3.4x	2.5x
EV/ EBITDA (x)	14.9x	11.1x

Shareholding Pattern (%)

Promoters	84
FII's	1
Institutions	3
Public & Others	12

Relative Performance

Topline growth remains sluggish

In Q2'08, Tech Mahindra (TEML) registered yet another quarter of sluggish revenue growth. Topline grew by 2.4% qoq, as two of the Company's key clients BT and AT&T witnessed restructuring and consolidation, respectively. EBITDA went up by 2.0% qoq, while the EBITDA margin fell by 9 bps due to a dip in the utilization rate. However, on account of a lower effective tax rate, PAT increased by 6.9% qoq to Rs. 1.8 bn.

Further restructuring and consolidation in BT and AT&T, respectively has affected TEML's revenue growth. Going forward, topline growth seems hazy due to the slower than expected ramp up of the BTGS deal. As in the previous quarter, improving the utilization rate remains a cause of concern for the Company. We believe that it will be difficult for TEML to enhance the billing rate, with the consolidation going on in the telecommunication market. However, the Company is gaining traction in the non-telecom service provider space.

We have revised our sales estimates downward by 10% for FY08E and 11% for FY09E, due to uncertainty in the timely completion of the ramp up of the BTGS project. The earnings estimates have also been reduced by 10% for FY08E and by 8% for FY09E. The stock is currently trading at a P/E of 23.8x and at a forward P/E of 18.9x for FY08E. Maintain Hold.

Result Highlights

Revenue for Q2'08 went up by just 2.4% qoq to Rs. 9.0 bn. This sluggish revenue growth is attributable to the restructuring taking place in BT

Key Figures (Consolidated)

Quarterly Data	Q2'07	Q1'08	Q2'08	YoY%	QoQ%	H1'07	H1'08	YoY%
(Figures in Rs mn, except per share data)								
Net Sales	6,976	8,763	8,976	28.7%	2.4%	12,847	17,739	38.1%
EBITDA	1,769	1,933	1,972	11.5%	2.0%	3,076	3,905	27.0%
Net Profit	1,769	1,701	1,818	2.8%	6.9%	2,835	3,519	24.1%

Margins(%)

EBITDA	25.4%	22.1%	22.0%	23.9%	22.0%
NPM	25.4%	19.4%	20.3%	22.1%	19.8%

Per Share Data (Rs.)

EPS	13.8	12.9	13.9	0.8%	7.3%	22.1	26.9	21.7%
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(top client) and consolidation in AT&T (a key client). Management expects revenue growth from BT to gain momentum from Q3'08 onwards, as was expected earlier. However, the ramp up on the BTGS deal has been slower than expected.

BPO segment witnessed robust growth

Amongst the business segments, revenue from the Telecom Service Provider grew by 2.2% qoq to stand at Rs. 7.9 bn. The Telecom Equipment Manufacturer segment witnessed a decline of 27.9% qoq to Rs. 220 mn. The BPO segment revenue recorded an upsurge of 73.2% qoq to Rs. 265 mn, as the Company gained traction from BT on the BPO front. In order to meet the growing demand for BPO services, TEML ramped up the employee base from 2,019 in Q1'08 to 3,191 in Q2'08.

EBITDA grew by 2.0% qoq to Rs. 2.0 bn. However, the EBITDA margin went down by 9 bps on account of decline in the utilization rate (for IT employees including trainees) from 67% in the prior quarter to 63% in Q2'08.

Bottomline growth was a bit better when compared with revenue growth. Net profit, at Rs. 1.8 bn, went up by 6.9% due to a lower effective tax rate, which declined by 44 bps qoq. The net profit margin also increased by 84 bps qoq to stand at 20.3%.

In Q2'08 TEML captured two clients in the WiMAX space for the first time

The Company won 9 new clients in Q2'08 and had a total of 96 clients at the end of the quarter. Two of the Company's new clients are cable companies in the WiMAX space. The number of clients providing revenues of USD +5 mn increased from 9 in Q1'08 to 12 in Q2'08. TEML's employee base stood at 23,100, as the Company made 1,954 new recruitments during the quarter. Management has indicated that it will make 5,000 campus offers in 2008.

Key Events

- TEML announced that it will set up three software centres in Chandigarh, Jaipur and Noida, with an estimated investment of USD 254.7 mn. On completion, these centres will have approximately 15,000 employees.

Key Risks

Key concerns to our rating include any delay in the completion of the restructuring in BT; slower than expected completion of the ramp up of the BTGS project and more than anticipated decline in the utilization rate.

Outlook

Further restructuring in BT and consolidation in AT&T continues to hit TEMPL's topline growth. Future revenue growth seems hazy due to slower than expected ramp up of the BTGS deal. In the last quarter, we had mentioned the challenges that were being confronted by the Company, which included, among others, improving the utilization rate and increasing the billing rate. TEMPL continues to grapple with these problems. Dip in the utilization rate negatively impacted the operating margin of the Company in Q2'08. Going forward, it will be difficult to improve the utilization rate as TEMPL will make 5,000 campus offers in 2008. We believe that with the consolidation going on in the telecommunication market, it will be difficult for the Company to exercise a hike in the billing rate. However, the Company is gaining traction in the non-telecom service provider space.

On account of uncertainty over the timely completion of the ramp up of the BTGS project, we have revised our sales estimates downward by 10% for FY08E and 11% for FY09E. The earnings estimates have also been reduced by 10% for FY08E and by 8% for FY09E. The stock is currently trading at a P/E of 23.8x and at a forward P/E of 18.9x for FY08E. Maintain Hold.

Key Figures (Consolidated)

Year to March	FY05	FY06	FY07	FY08E	FY09E	CAGR (%)
(Figures in Rs mn, except per share data) (FY07-09E)						
Net Sales	9,456	12,427	29,290	39,445	54,356	36.2%
EBITDA	1,353	2,683	7,369	9,072	12,230	28.8%
Net Profit	1,026	2,359	6,128	7,792	10,354	30.0%
Margins(%)						
EBITDA	14.3%	21.6%	25.2%	23.0%	22.5%	
NPM	10.9%	19.0%	20.9%	19.8%	19.0%	
Per Share Data (Rs.)						
EPS	9.0	18.8	47.0	59.3	78.9	29.6%
PER (x)	124.6x	59.7x	23.8x	18.9x	14.2x	

Quick ramp up of the BTGS project will benefit the Company to a great extent

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