



## Research



### RESEARCH:: COMPANY:: MPHASIS LTD.

22<sup>nd</sup> June' 2010

#### Long Term Buy

CMP	Rs 575
Target price	Rs 720
Projected PE	16-17
Investment period	6-12 months

#### Stock Info (TTM Basis)

Sector	IT
Market cap	Rs.120577 mn
Face value	Rs. 10
Book value	Rs. 96.56
EPS	Rs. 45.51
52 week H/L	796/332
Avg. Daily Vol (2wk)	1,01,000
Chairman	Andreas Mattes
Incorporation	1992
Listed At	BSE/NSE
Equity capital	Rs. 2097.3 mn
FII's/MF's (%)	16.78/5.25

Mphasis is a leading provider of Applications services, Remote management services and BPO services. The company delivers real improvements in business performance for clients through a blend of technology know-how, domain and process expertise. The current strength of over 37,000 employees enable Mphasis to service its clients in financial services, healthcare, transportation and communications, consumer & retail industries .

#### Key Highlights

- Mphasis launched its BPO centre in Raipur, Chhattisgarh which is expected to recruit over 500 employees. It will provide services to Telecom operator Idea Cellular from this centre.
- Mphasis prices were renegotiated with HP from cost-plus basis to rate-card basis. The lower pricing will decrease the operating profit margins but it would be off-set by larger business volumes from HP.
- Mphasis has acquired Fortify Infrastructure Services, a global provider of offshore based Remote IT Operations and Management (ROM) Services. This acquisition will facilitate Mphasis to provide outcome based services and grow with a CAGR of 30% in the following three years.

#### Future Outlook

At Current market price of Rs575, the stock is available at a P/E of 12.96x of its FY10E earnings, and 12.27x of its FY11E earnings. We recommend a BUY with target price of Rs720, given that company's future shows potential.

#### Why to Invest in Mphasis Ltd

.....Page8

#### CONTENTS

Key Highlights & Future Outlook.....	Page1
Company Profile.....	Page2

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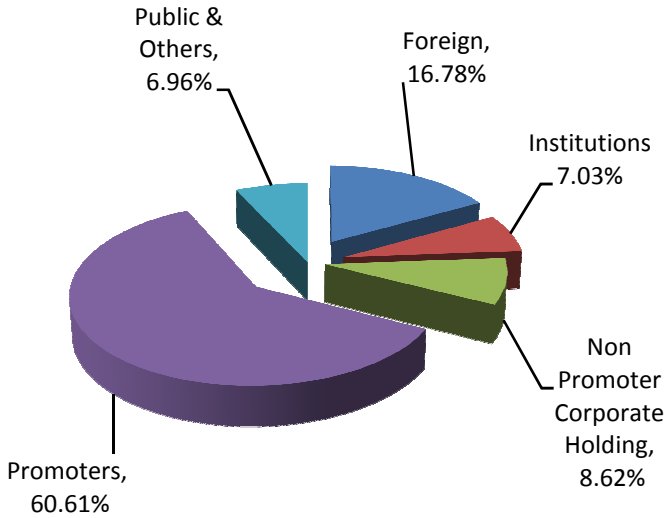
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(Consolidated Basis)

Particulars (Rs Millions)	FY09	FY10E*	FY11E*
Total Revenue	43200.9	49249	55158.9
Expenditure	31443.1	36739.8	41534.7
PBIDT	11757.8	12509.2	13624.3
Interest	8.1	12	20
Depreciation	2022.2	2044.2	2182.4
PBT	9727.5	10453	11421.9
Tax	640.7	1149.8	1599.1
PAT	9086.8	9303.2	9822.8
EPS	43.33	44.36	46.84
CEPS	52.97	54.10	57.24
OPM (%)	27.22	25.40	24.70
NPM (%)	21.03	18.89	17.81

Source: Company Reports, Fairwealth Research Estimate  
 \*Estimated

**SHAREHOLDING PATTERN**



**COMPANY PROFILE**

Mphasis is a premier global Application services and Business Process Outsourcing Services Company headquartered in Bangalore, India. It was formed in the year 2000 after the merger of Bangalore based BFL Software Limited and California, US, based Mphasis Corporation.

Mphasis added ITO (Infrastructure Technology outsourcing) services on 1 April 2006 with the acquisition of Electronic Data Systems (India) Private Ltd (EDS), a subsidiary of Electronic Data Systems (EDS) Corporation, USA. Since June 2006, the Group has become a subsidiary of Electronic Data Systems Corporation (EDS).

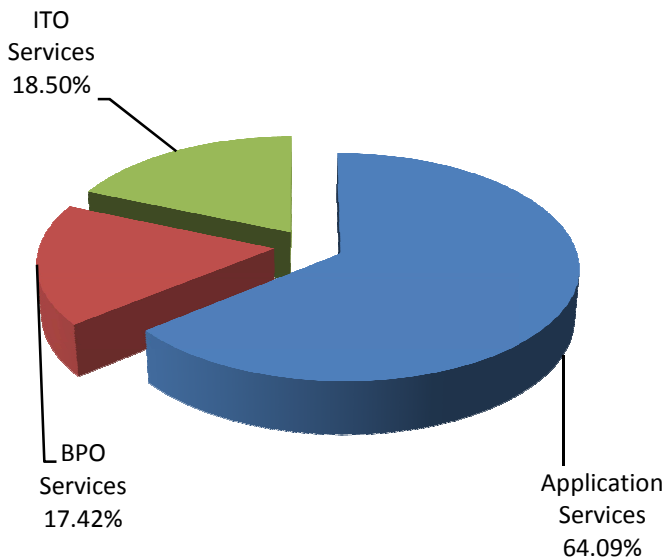
In 2008, HP acquired EDS and thus Mphasis came under the umbrella of HP.

Mphasis has strong offerings in the BFSI, Telecom and Healthcare verticals that account for 63% of the total company's revenues and gains strong traction on the back of its relationship with EDS and HP.

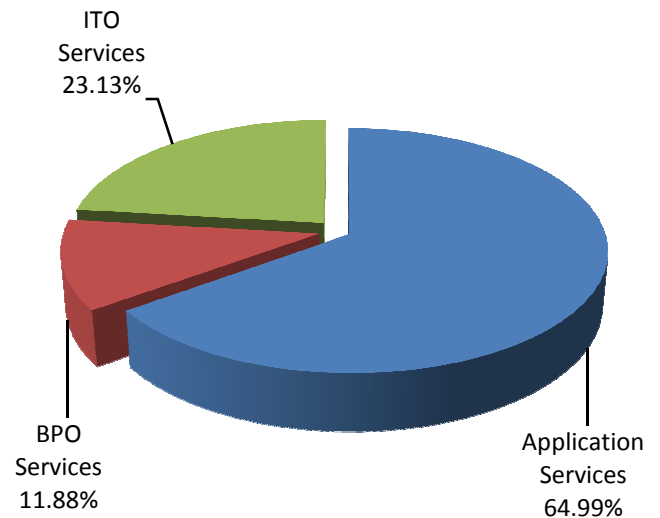
**BUSINESS SEGMENTS:**



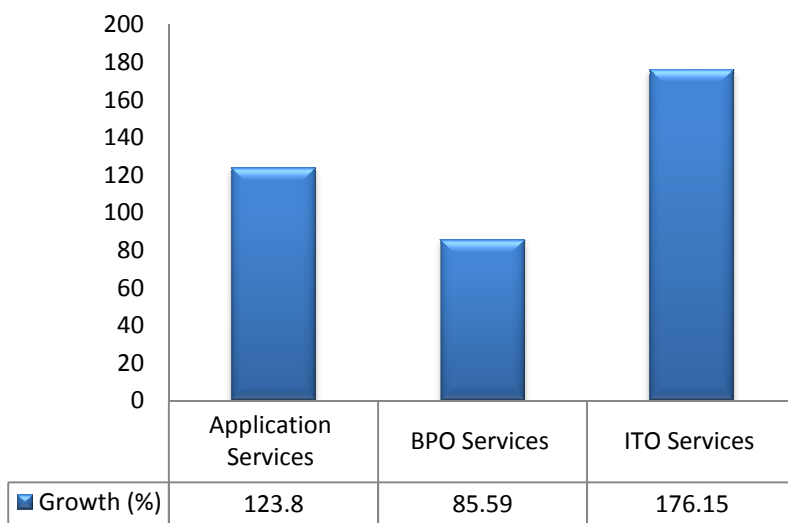
### REVENUE BREAKUP



### OPERATING PROFIT BREAKUP



### SEGMENTAL GROWTH (in %)



Application services cover consulting, application development, testing and application maintenance services. BPO services provide voice, transaction based services and knowledge based processes. ITO covers a range of infrastructure management services and service/ technical help desks.

During the year ended 31 October 2009, Application services revenue grew by 123.8%, BPO services revenue appreciated 85.6% and ITO services revenue grew by 175.15% during the year. Application services contribute 64% to the revenues, while BPO and ITO services account for 17% and 19% of the revenues respectively.

**Revenues by Vertical/Industry**

**(Rs Millions)**

Vertical/Industry	FY09	%	FY08	%
<b>Banking &amp; Financial Services</b>	17,642	41%	12,244	41%
<b>Technology &amp; OEMs</b>	9,924	23%	6885	23%
<b>Telecom</b>	4704	11%	3637	12%
<b>Manufacturing &amp; Retail</b>	5442	13%	4124	14%
<b>Logistics, Airlines &amp; Transportation</b>	2294	5%	1773	6%
<b>Healthcare &amp; Pharma</b>	2827	7%	1111	4%
<b>Total</b>	42,833		29,774	

All verticals grew in FY09 with significant growth in healthcare & pharma (by 154%), banking & financial services (by 44%) and technology & OEM (by 44%). Banking & financial services vertical continued to be the largest segment, contributing 41% of the group's revenues

**Revenues by Service Type**

**(Rs Millions)**

Service Type	FY09	%	FY08	%
<b>Application Maintenance &amp; Other Services</b>	14,892	35%	10,271	35%
<b>Application Development</b>	12,536	29%	8,789	30%
<b>Infrastructure Management Services</b>	5,561	13%	2,160	7%
<b>Customer Service</b>	3,422	8%	3,062	10%
<b>Service / Technical Help Desk</b>	2,671	6%	2,446	8%
<b>Transaction Processing Service</b>	2,258	5%	1,860	6%
<b>Knowledge Processes</b>	1,400	4%	1,186	4%
<b>License Income</b>	93	0%	-	-
<b>Total</b>	42,833		29,774	

Application maintenance & application business revenues posted growths of 45% and 43% respectively during FY09 (contributing 64% to total revenues}.

Infrastructure management services business grew significantly during FY 09, registering a growth of 157% over FY08.

**Application Development** refers to customized software development services based on the requirements and specifications given by the customers and documented in Statement of Works.

**Application Maintenance** involves maintenance of existing customer software and they are mostly undertaken on annuity terms.

**Infrastructure Management Services** include end-to-end managed mobility solutions covering workplace management & other support services, hosting services which comprise mainframe or midrange, application & web hosting services and data center services focus on migration, automation & other software services.

**Customer services** include receivables collection support, product support, enrolment etc. provided to clients through BPO operations.

**Transaction Processing** includes claims and mortgage processing, account opening and maintenance, data processing and management etc.

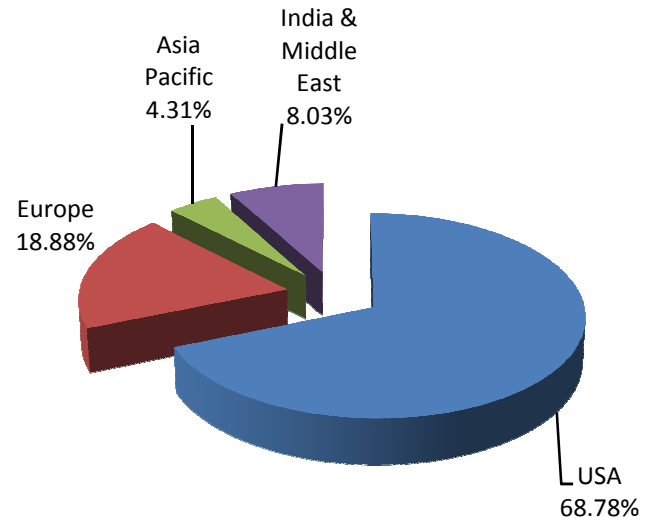
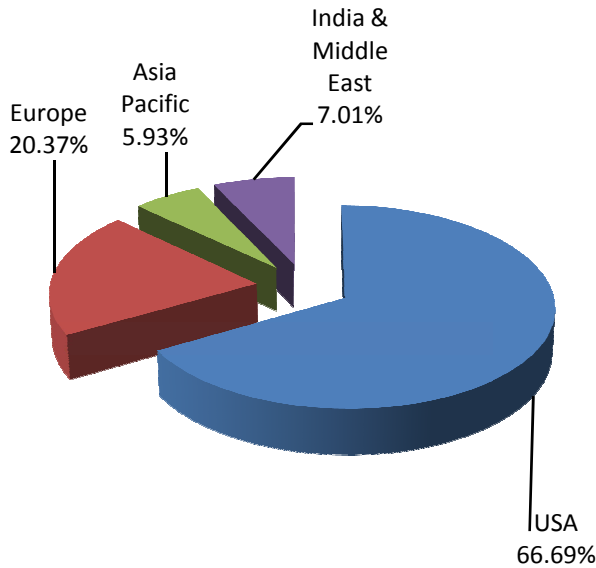
**Service/Technical Help Desk** comprises inbound and outbound customer interaction programs including technical product support, customer care and allied services.

**License Income** pertains to the income from license sale in the health care space of the Group's product Javelina developed by its foreign subsidiary that was acquired in 2005.

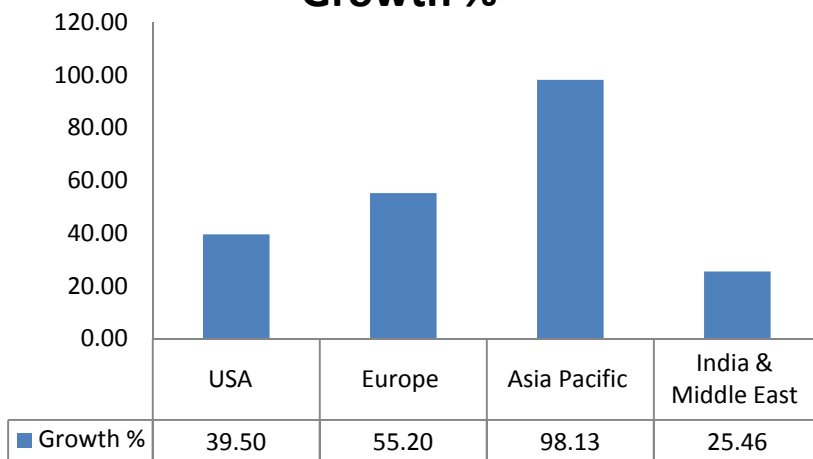
**Revenue Breakup (Geographically)**

IN FY09

IN FY08



**Growth %**

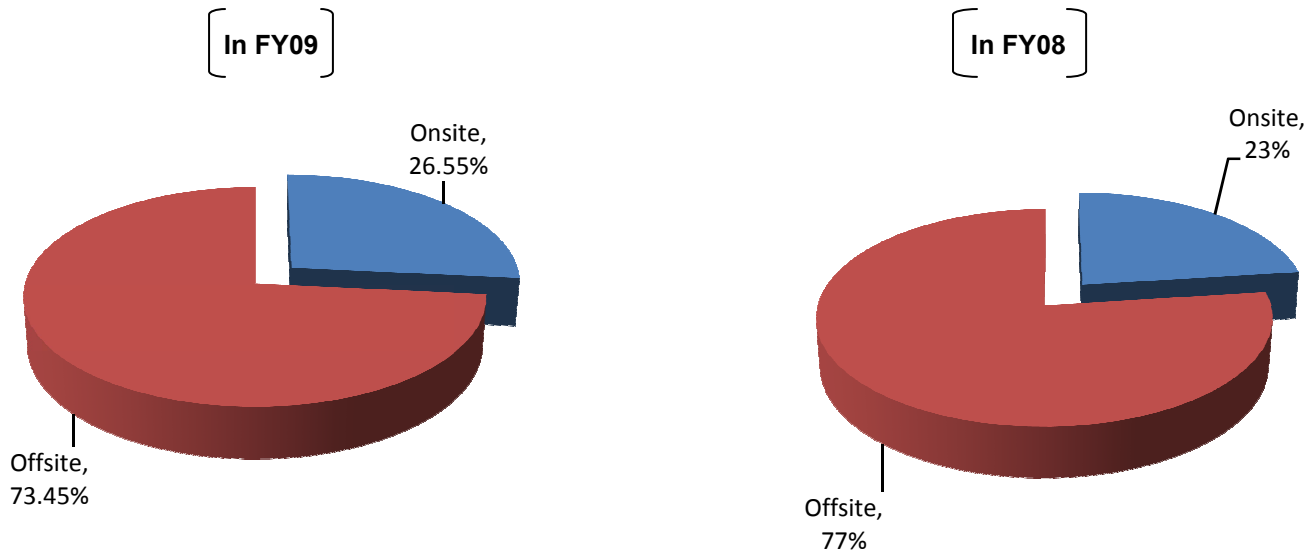


In FY09, company derived 87% of its revenues from USA & EUROPE.

Asia pacific revenues grew a significant 98% in FY09 over FY08; revenues from Europe grew by 55% over FY08 whereas revenues from the US expanded by 39.5% as compared to FY08.

This depicts an increasing geographical presence of the company with healthy growth in revenues and client base.

**REVENUES BY DELIVERY LOCATION**



The Group charges higher billing rates and incurs higher compensation expenses for work performed by the onsite teams at a customer's premises as compared to work performed at its offshore centres. Services performed onsite typically generate higher revenues per capita than the same amount of services performed at its offshore centres in India. Share of onsite revenues have increased substantially in FY09 compared to FY08 due to new transformation and transition engagements involving higher onsite efforts in their execution.

Revenues from onsite grew 63.5% contributing 26.55% to total revenues in FY09 and offsite revenues grew 37.8% contributing 73.45% to total revenues.

**QUARTERLY ANALYSIS**

Particulars (Rs Millions)	201004	200904	%Var	201001	%Var
<b>Net Sales</b>	12205	10484.7	16.41	11915.6	2.43
<b>Other Income</b>	273.3	143.8	90.06	80.9	237.82
<b>Total Income</b>	12478.3	10628.5	17.40	11996.5	4.02
<b>Expenditure</b>	9054.7	7666.6	18.11	8780.1	3.13
<b>PBIDT</b>	3423.6	2961.9	15.59	3216.4	6.44
<b>Interest</b>	-1.3	-9.4	-86.17	-248.8	-99.48
<b>PBDT</b>	3424.9	2971.3	15.27	3465.2	-1.16
<b>Depreciation</b>	402.1	552.3	-27.20	457.7	-12.15
<b>Tax</b>	350	174.5	100.57	324.8	7.76
<b>Profit After Tax</b>	2672.8	2244.5	19.08	2682.7	-0.37
<b>Equity</b>	2097.3	2089.7	0.36	2096.6	0.03
<b>Face Value</b>	10	10	0.00	10	0.00
<b>EPS</b>	12.73	10.74	18.53	12.8	-0.55

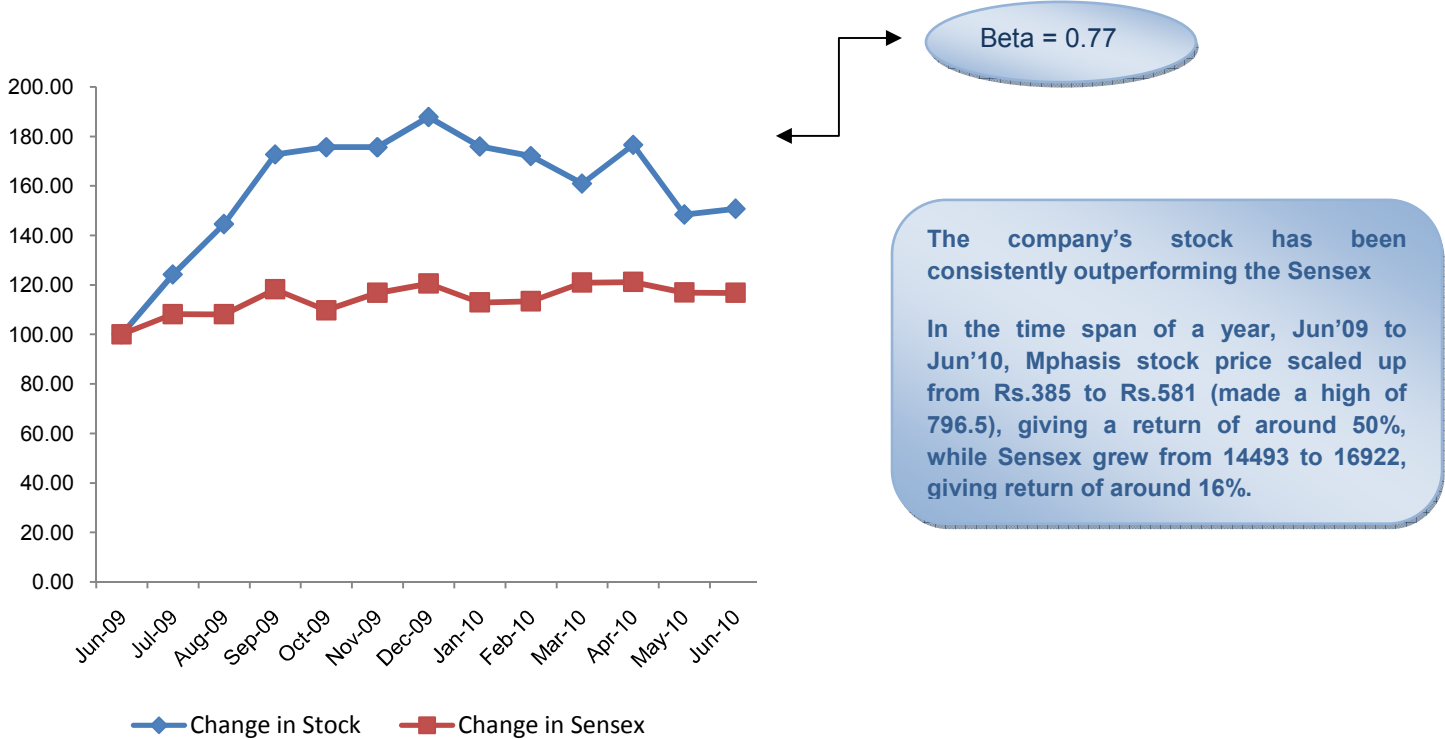
Company's consolidated revenues in Q2'10 stood at Rs 12205 mn as compared to Rs 10484.7 mn in the same quarter last year clocking a growth of 16.4%. During the same period, net profit increased 19% from Rs 2244.5 mn to Rs 2672.8 mn. Operating Profit during the quarter ended 30 April, 2010 was Rs 3423.6 mn, a growth of 15.59% over the same quarter last year. EPS for the quarter was Rs 12.73, an increase of 18.5% over the same period last year. Operating and net margins for the quarter ended 30 April, 2010 were 22.5% and 21.9% respectively.

Consolidated revenues for the quarter ended 30 April, 2010 are estimated at Rs 12205 mn, an increase of 2.4% compared to Rs 11915.6 mn in the previous quarter. Operating profit recorded a growth of 6.44% sequentially and operating margin was maintained at 22.5%.

During the quarter ended 30 April, 2010, the Group added 22 new clients, including 14 through the HP Channel. These include a large pharmaceutical company and a company engaged in manufacturing for the aircraft industry. Additionally, during this quarter, TD AMERITRADE, a provider of securities brokerage services and technology-based financial services, selected Mphasis to support some of its non-client facing services. The Group added net headcount of 1,429 during the quarter which totals to 37,119 as of 30 April, 2010.

This quarter, Mphasis acquired Fortify Infrastructure Services, a global provider of offshore based Remote IT Operations and Management (ROM) Services expanding their presence in the ROM services market. Effective date of acquisition is 1 May, 2010. The combined entity will help the Group gain a bigger share of the ROM market. Through this acquisition, the Group will provide outcome based services which go beyond technical SLAs.

### Stock Performance



## ANALYSIS & REPORT

### Why to invest in shares of Mphasis Ltd.?

#### SECTOR:

Earlier Application Development and Maintenance (ADM) and Business Process Offshoring (BPO) industries have dominated offshoring business. Now, Infrastructure Management Services (IMS) that manage an enterprise's core IT systems (hardware, software, connectivity and people) have become equally important.

The Infrastructure Management Services (IMS) industry is moving towards a remote delivery model where services are increasingly delivered by vendors from low-cost locations. This phenomenon is a by-product of three factors – the continuous effort by enterprises to enhance service and performance levels and reduce costs, advancements in technologies that have improved infrastructure efficiency and management, and evolution in offshore capabilities. The addressable market for RIMS is estimated to be worth US\$96 billion to US\$104 billion. Remarkably, this emerging segment is comparable to the offshore ADM opportunity of US\$77 billion to US\$93 billion and offshore BPO opportunity of US\$120 billion to US\$150 billion. It is expected that the majority of growth will come from off-shoring midrange services, which is likely to account for approximately 70 percent of the overall opportunity by 2013. So far, India accounts for US\$3 billion to US\$4 billion of the total US\$6 billion to US\$7 billion worth of services off-shored. RIMS, as an independent industry, could unleash the next largest wave of opportunity in off-shoring. This provides a considerably large opportunity for Indian players to grab a larger part of the global market share.

#### COMPANY:

- It has been ranked No. 23 in Bloomberg Business Week's Tech 100 list; a ranking of the world's best performing tech companies of 2009 and is ranked third best in the world in terms of total shareholder return. This is the first time Mphasis made it to the Business week's Top 100 list of technology companies.
- Dataquest recognize the company as one of the Top 20 IT companies in the country with the highest growth percentage. National Association of Software and Services Company India (NASSCOM) ranks it as #7 among the top software exporters.
- It is certified with ISO 9001:2008, ISO/IEC 27001:2005 (formerly known as ISO 17799) and is assessed at CMMI v 1.2 Level 5. It also provides SEI CMMI, ISO and Six Sigma related services support.

#### FUNDAMENTALS:

- It acquired AIG Systems Solutions Private Limited (AIGSS), an Indian subsidiary of American International Group Inc (AIG), USA. Based in Chennai and Kolkata, AIGSS has over 700 employees and provides IT services to AIG and its member companies. It was then renamed as Mphasis Fin Solutions Private Limited. This acquisition will help the Company to augment its capabilities for the insurance industry.
- 72% of total revenues of Mphasis came from HP and it added a total of 16 new clients, of which 13 were added through HP channel. Mphasis' association with HP has not only enabled strong new client wins but has also improved the average deal size. The alignment with HP has significantly reduced the competition risk and company is leveraging HP's technology and service offerings to broaden its client base. It depicts the strong parent backing by HP leading to the future growth of the company.
- Company has set up the off-shore delivery centre in Sri Lanka which would get operational by mid 2010 and will join the company's network of Global Delivery Centres, by providing an array of IT and ITES services to clients, world-wide. This new global delivery centre would set up new milestones in the journey of company.



- Company launched its Global Command and Control Centre (GCCC) in Pune. This would further expand its Infrastructure Outsourcing capability and will extend services to customers in India and global markets including the U.S., Europe, and Asia Pacific - Japan.

### **KEY CONCERNS:**

#### **Global Economic crisis**

The Group derives 87% of its revenues for the year from the USA and Europe. Its growth has been sustained with augmentation of work from new clients and new service streams there. Thus, weak economic condition may affect its total revenues.

#### **Client / Business concentration risk**

During the year the Group derived 13% of its total revenues from a single client and about 70% of the total revenue through HP and such dependencies can impact the Group's operations in case of any adversity. From the business concentration perspective 41% of the revenue is from Banking and Financial Services segment based clients.

#### **Competition risk**

New competitors may enter the markets the company operates in or current competitors could decide to focus more on these markets, and thereby intensify the highly competitive conditions that already exist. This could result in lower margins in future for the company and could also result in increased pricing pressures.

#### **Service delivery risks**

Due to expansion in volume of operations and new client / geography / service offerings there could be service delivery related risks, transition phase risks, intellectual property rights related risks and change in proportion of offshore–on–site mix with risk of consequential skill mismatches.

#### **Foreign exchange fluctuation risk**

About 93% of the Group's billings for the year is in foreign currency and hence exposed to volatility against the Indian rupee and cross currency movements. Changes in the exchange value of the Rupee with other currencies would affect the earnings and carrying value of net assets located overseas.

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