

# New IT CEO – Rebuild process ahead, Cut to Neutral

## New CEO for IT business; Current CEOs step down

In a surprising development the joint-CEOs of the IT business, Girish Paranjpe & Suresh Vaswani have stepped down and will be with the company until March 31. Mr. T.K.Kurien, who has been heading the eco-energy business for the last 9 months, takes over as the new CEO from Feb1. We have high regard for Mr. Kurien, who helped restructure BPO in 2005 but are concerned at the departure of the present joint-CEOs, long time Wipro stalwarts. While the IT spending environment remains strong and we have a positive view on the sector, we believe Wipro could lag peers as the new CEO relooks at strategy and given possible churn in BU heads. 3Q was weak, as expected and we see risk to 4Q guidance being achieved. Also believe stock could de-rate on second top management change in 18 months. Cut to Neutral.

## Risk to our estimates

While Wipro was making progress in solving the fulfillment (attrition related) issue and client relationship building, we think the process could be hit in the next few quarters, as the new CEO reviews strategy and rebuilds company. We would watch for possible churn in BU heads to be behind, attrition levels to continue to decline and for anecdotal evidence of uptick in discretionary IT related project wins before turning more positive.

## 4Q guidance: Risk of being missed

Wipro has guided for 4Q IT services USD terms revenue growth at 3-5% qoq in constant currency terms. While this sounds reasonably strong, it will likely be a stretch, in our view, like in 3Q, given muted hiring growth (16% of base over LTM vs 25-30% for peers). In 3Q, Wipro could only achieve the midpoint of their constant currency rev growth guidance at 4.1% qoq vs the upper end of guidance at 5.5%. Infy has guided 1-2% qoq USD rev growth for 4Q, but street would likely be at 5-6% rev growth for Infy/TCS/HCL, which have been performing better.

## 3Q weaker than peers, as expected

As in our preview, Wipro reported a weaker 3Q than peers at 5.6% qoq growth in IT services revenue USD terms vs the 6 -7.5% reported by their peers. Volumes grew a mere 1.5% qoq, cross-currency helped 1.5% and constant currency pricing moved up 2.6% likely helped by productivity gains in fixed price. Poor volume growth was led by lower exposure to banking vertical (27% of revs vs 35 to 45% for Infy and TCS), and weakness in the technology vertical and healthcare verticals (8% each of revs) which saw ~3.5% qoq decline each. Secondly, as we had anticipated, fulfillment issues could have restricted participation in some discretionary IT spending related projects.

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## Stock Data

|                          |                         |
|--------------------------|-------------------------|
| Price (Common / ADR)     | Rs477.50 / US\$14.98    |
| Price Objective          | Rs570.00 / US\$18.00    |
| Date Established         | 4-Jan-2011 / 4-Jan-2011 |
| Investment Opinion       | C-2-7 / C-2-7           |
| Volatility Risk          | HIGH / HIGH             |
| BofAML Ticker / Exchange | WIPRF / BSE             |
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| Bloomberg / Reuters      | WPRO IN / WIPR.BO       |

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## Q3FY11 Result Summary

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| INR Million                                | Q3 11  | Q2 11  | QoQ     | Q310   | YoY    | BofAMLe | Variation |
|--------------------------------------------|--------|--------|---------|--------|--------|---------|-----------|
| Net Sales                                  | 78,202 | 77,719 | 0.6%    | 69,380 | 12.7%  | 79,276  | -1.4%     |
| Expenditure                                |        |        |         |        |        |         |           |
| Cost of Goods sold                         | 53530  | 53270  | 0.5%    | 47766  | 12.1%  | 54173   | -1.2%     |
| S&M                                        | 5485   | 5751   | -4.6%   | 4817   | 13.9%  | 6093    | -10.0%    |
| G&A                                        | 4921   | 4251   | 15.8%   | 3655   | 35%    | 4711    | 4.5%      |
| Forex                                      | 91     | -414   | -122.0% | 394    | -76.9% | 0       | nm        |
| Total expenses                             | 61767  | 61718  | 0.1%    | 53861  | 14.7%  | 62939   | -1.9%     |
| EBITDA                                     | 16,435 | 16,001 | 2.7%    | 15,519 | 5.9%   | 16,337  | 0.6%      |
| Depreciation                               | 2078   | 1968   | 5.6%    | 1983   | 4.8%   | 2038    | 2.0%      |
| EBIT                                       | 14,357 | 14,033 | 2.3%    | 13,536 | 6.1%   | 14,299  | 0.4%      |
| Other Income                               | 1751   | 1422   | 23.1%   | 721    | 142.9% | 1500    | 16.7%     |
| Interest & Finance charges                 | 427    | 467    | -8.6%   | 0      | NA     | 450     | -5.1%     |
| PBT                                        | 15,681 | 14,988 | 4.6%    | 14,257 | 10.0%  | 15,349  | 2.2%      |
| Tax                                        | 2582   | 2183   | 18.3%   | 2321   | 11.2%  | 2840    | -9.1%     |
| PAT before extraords                       | 13,099 | 12,805 | 2.3%    | 11,936 | 9.7%   | 12,510  | 4.7%      |
| Minority interest                          | -71    | -148   | -52.0%  | -31    | 129.0% | -63     | nm        |
| Equity in earnings/ (losses) of affiliates | 160    | 192    | -16.7%  | 128    | 25.0%  | 202     | -20.6%    |
| PAT                                        | 13,188 | 12,849 | 2.6%    | 12,033 | 9.6%   | 12,649  | 4.3%      |
| Margin Summary                             | Q311   | Q2 11  | (bps)   | Q310   | (bps)  | BofAMLe | (bps)     |
| EBITDA                                     | 21.0%  | 20.6%  | 43      | 22.4%  | -135   | 20.6%   | 41        |
| EBIT                                       | 18.4%  | 18.1%  | 30      | 19.5%  | -115   | 18.0%   | 32        |
| PAT                                        | 16.9%  | 16.5%  | 33      | 17.3%  | -44    | 16.0%   | 91        |
| Tax Rate                                   | 16.5%  | 14.6%  | 190     | 16.3%  | 19     | 18.5%   | -203      |

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## Price objective basis & risk

### Wipro (WIPRF / WIT)

Our Price Objective of Rs570 is set at a target FY12 EV/EBITDA to 2yr EBITDA growth of 0.77x, at a 10% discount to Infosys. This implies a target FY13e PE of 18x, at about 15% discount to Infosys, in line with its 3-yr average discount. Downside risks to estimates stem from delays in recovery of IT spending by technology and telecom verticals and success in client mining efforts, apart from macro risks relating to IT spending and Rupee.

## Link to Definitions

### Industrials

Click [here](#) for definitions of commonly used terms.

### Technology

Click [here](#) for definitions of commonly used terms.

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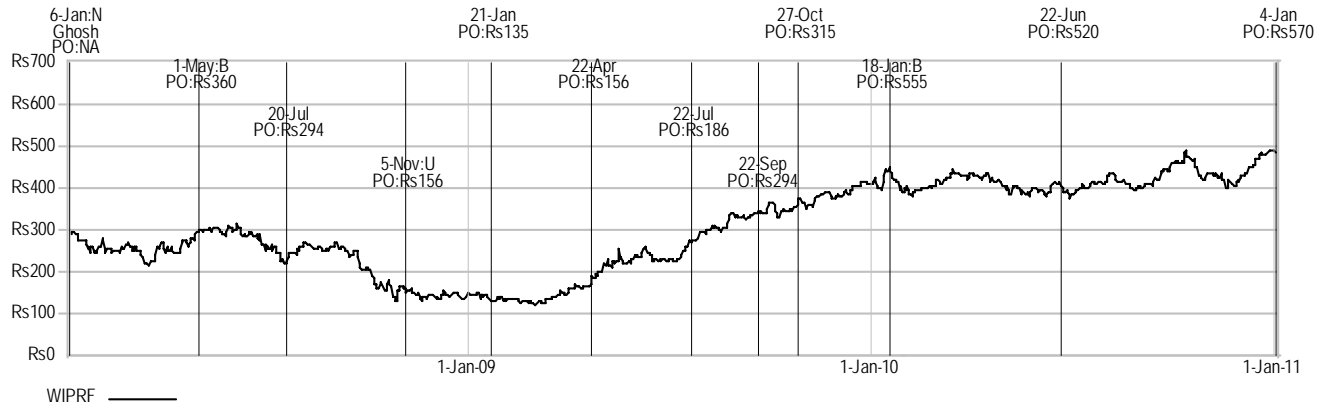
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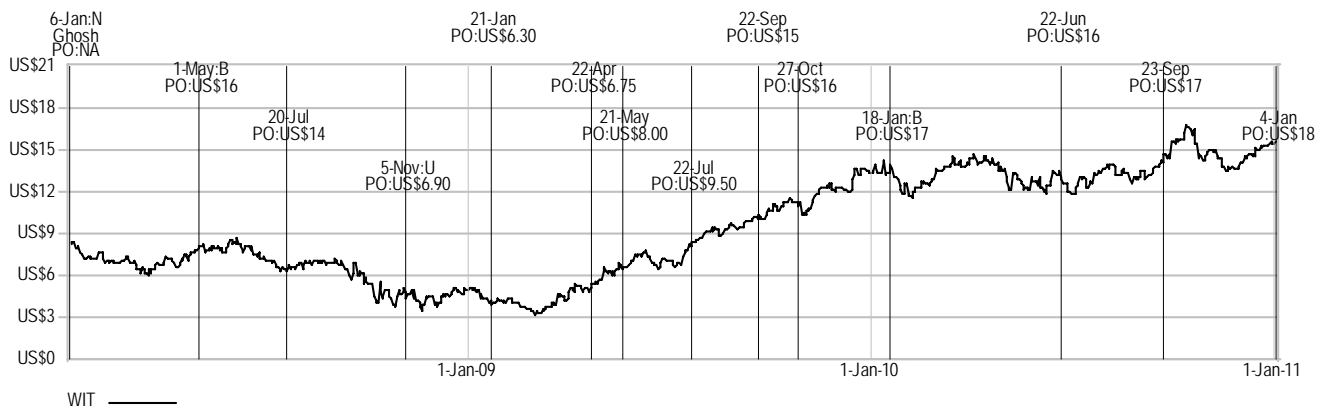
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B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid, NR: No Rating

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### WIT Price Chart



B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid, NR: No Rating

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| Coverage Universe | Count | Percent | Inv. Banking Relationships* | Count | Percent |
|-------------------|-------|---------|-----------------------------|-------|---------|
| Buy               | 47    | 58.75%  | Buy                         | 24    | 58.54%  |
| Neutral           | 20    | 25.00%  | Neutral                     | 9     | 52.94%  |
| Sell              | 13    | 16.25%  | Sell                        | 4     | 36.36%  |

### Investment Rating Distribution: Technology Group (as of 01 Jan 2011)

| Coverage Universe | Count | Percent | Inv. Banking Relationships* | Count | Percent |
|-------------------|-------|---------|-----------------------------|-------|---------|
| Buy               | 128   | 54.01%  | Buy                         | 53    | 46.49%  |
| Neutral           | 48    | 20.25%  | Neutral                     | 21    | 46.67%  |
| Sell              | 61    | 25.74%  | Sell                        | 16    | 27.59%  |

### Investment Rating Distribution: Global Group (as of 01 Jan 2011)

| Coverage Universe | Count | Percent | Inv. Banking Relationships* | Count | Percent |
|-------------------|-------|---------|-----------------------------|-------|---------|
| Buy               | 2011  | 53.86%  | Buy                         | 874   | 48.31%  |
| Neutral           | 925   | 24.77%  | Neutral                     | 444   | 52.30%  |
| Sell              | 798   | 21.37%  | Sell                        | 276   | 36.75%  |

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|-------------------|-----------------------------------------------------------------------------|-----------------------------------------------------|
| Buy               | ≥ 10%                                                                       | ≤ 70%                                               |
| Neutral           | ≥ 0%                                                                        | ≤ 30%                                               |
| Underperform      | N/A                                                                         | ≥ 20%                                               |

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