

RESULTS

REVIEW

Wipro Ltd.

Strong volume growth a key highlight of the result

ACCUMULATE

Analyst

Pratik Gandhi

+91-22-4322 1367

pratik.gandhi@idbicapital.com

Nifty: 5,327; Sensex: 17,705

CMP	Rs366
Target Price	Rs390
Potential Upside/Downside	+7%

Key Stock Data

Sector	IT Services
Bloomberg / Reuters	WPRO IN /WIPR.BO
Shares o/s (mn)	2,457.5
Market cap. (Rs mn)	899,460
Market cap. (US\$ mn)	18,404
3-m daily average vol.	152,705

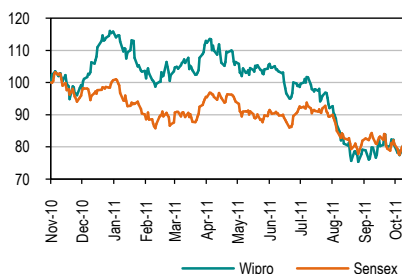
Price Performance

52-week high/low	Rs496/310		
	-1m	-3m	-12m
Absolute (%)	7	(6)	(14)
Rel to Sensex (%)	(0)	(3)	(1)

Shareholding Pattern (%)

Promoters	79.2
FII/IRIs/OCBs/GDR	7.7
MFs/Banks/FIs	4.2
Non Promoter Corporate	2.7
Public & Others	6.2

Relative to Sensex



Source: Capitaline

Summary

Wipro's constant currency (cc) growth rate of 5.5% in IT services came ahead of its peers TCS (5.2%) and Infosys (5%). This superior performance was due to strong QoQ volume growth of 6% (4.6% organic). The growth was largely broad-based across verticals barring 'Global Media & Telecom', down 0.6% in cc, Geographies and service lines (BPO - down 1% QoQ). Pricing has declined (offshore - down 4.1% QoQ and onsite - down 0.4% QoQ) for successive quarters, which has raised concerns whether the company has adopted disruptive strategy to bring back volume growth. However, the management attributed price decline as a quarterly aberration due to wind down of some fixed price projects. IT service EBIT margin declined 200bps to 20% largely on account of 12% offshore wage hike and integration of SAIC acquisition.

We estimate IT service's revenue growth (in US\$) at 15.1% and 15.4% for FY12E and FY13E. Though, current quarter top-line performance was ahead of expectations and its own guidance, we would like to wait for one or two quarters before turning positive on the stock. At CMP of Rs367, the stock is trading 16.3x and 14.1x FY12E and FY13E EPS respectively. However, 23% correction in stock price YTD enables a rating upgrade to ACCUMULATE from HOLD earlier with revised target price of Rs390 (425 earlier).

Result Highlights

- Revenue and net profit came in-line while operating profit missed street estimates

Consolidated revenue of Rs90.1 bn, up 6.1% QoQ, came in-line with street estimates (refer table 1), due to strong performance by IT services (up 6.6%), Consumer Care and Lighting (up 6.1%) and Others segment (up 14.8%). IT service revenue at US\$1,473 mn came ahead of its guidance US\$1,436 – US\$1,464 mn. 200bps and 90bps decline in EBIT margin for IT service and Consumer Care and Lighting segment, respectively led to operating profit (EBIT) of Rs14 bn, 6.8% lower than street estimate. Despite a miss on operating profit (EBIT), high forex gain (Rs875 mn v/s Rs711 mn in Q1) and lower tax rate due to write-back (18% v/s 18.9% in Q1) helped the company to meet street net profit expectation at Rs13 bn.

- Operating metric improved in current quarter

Positives: 1) 6% volume growth (4.6% organic, highest in past 4 quarters), 2) Strong growth in Financial services (up 6.9% in cc) and Energy & Utility (up 24% in cc) due to full quarter integration of SAIC, 3) Broad-based growth across geographies in cc – Europe (6.8%), India & ME (11.6%), Other emerging market (13.9%), 4) Impressive performance by top client (up 17.3% QoQ) and top-10 (up 7.9% QoQ), 5) Robust deal pipe-line (pursuing 25 large deals with avg size greater than US\$ 50mn), 6) **Highest net addition in past six quarters:** The company added 5,240 employees (~4k fresher) in Q2.

Negatives: 1) Constant currency price decline for second quarter in-a-row (**offshore:** 3.5%), 2) Moderation in quarterly annualized rate 18.5%, however still high, 3) Weakness in BPO (down 1.0% QoQ), and Global Media and Telecom (down 2.2% QoQ) continues for successive quarters.

- Q3 guidance and commentary on CY12:

Wipro's Q3FY12 guidance of US\$1.5-1.53 bn implies sequential growth of 1.9%-3.9% which is lower than Infosys' guidance of 3.2% to 5.4%. The management expects high number of holidays to impact volume growth in Q3 whereas pricing to remain stable.

In terms of CY12, the interactions with clients in Financial service, Mfg, Media and E&U gives confidence of a normal year. On the other hand, in Retail segment decision making has started slowing down and for telecom struggle is likely to continue. We must admit that the current quarter performance was impressive and even the focused approach on client mining has started pay-off for the company.

Financial snapshot

(Rs mn)

Year	Revenue	EBITDA	EBITDA (%)	Adj. PAT	EPS (Rs)	P/E (x)	EV/EBITDA (x)	RoE (%)	RoCE (%)
FY10	271,957	60,059	22.1	45,935	18.8	19.5	15.0	26.5	22.0
FY11	310,542	65,437	21.1	52,977	21.6	17.0	13.8	24.3	20.2
FY12E	367,987	70,689	19.2	54,990	22.4	16.3	12.6	21.4	19.2
FY13E	422,271	85,496	20.2	63,910	26.0	14.1	10.1	21.4	21.4

Source: Company; IDBI Capital Research

Key Highlights

- Consolidated revenue and profit in-line while operating profit(EBIT) missed street estimate:** IT services revenue came at US\$1,473 mn, up 4.6% QoQ, and exceeded guidance of US\$1,436-1,464 mn. In constant currency, revenue was at US\$1,485 mn, up 5.5%, well above guidance of US\$1,423-1,451 mn. Consolidated revenue came at Rs90.1 bn, up 6.1% on sequential basis due to better-than-expected quarter for IT services (up 6.6% QoQ), Consumer Care and Lighting (up 6.1% QoQ) and Others segment (up 14.8% QoQ).

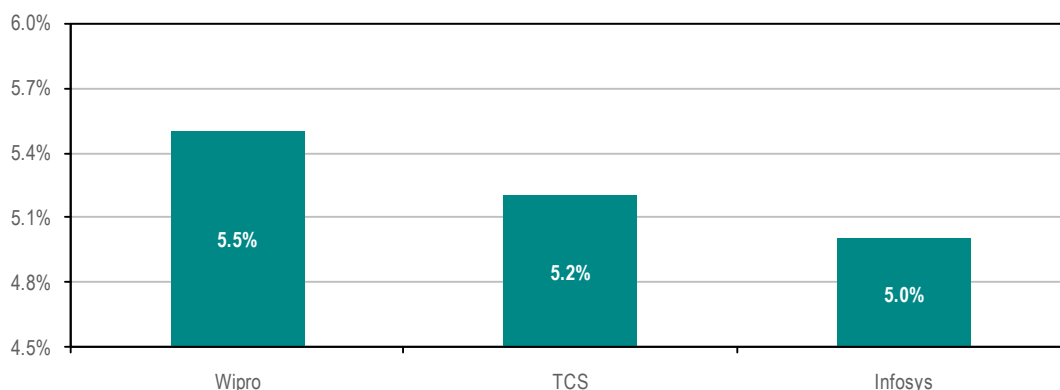
Table 1: Results in-line street estimates (Rs mn)

	Consensus	Actual	Variance (%)
Revenues	88,809.4	90,070.0	1.4
EBITDA	16,950.4	16,522.0	(2.5)
EBITDA margin (%)	19.1	18.3	
EBIT	15,025.0	14,003.0	(6.8)
EBIT margin (%)	16.9	15.5	
Net Profit	13,041.1	13,009.0	(0.2)
Net margin (%)	14.7	14.4	
EPS (Rs)	5.4	5.3	

Source: Company; IDBI Capital Research

- Operating profit (EBIT) for the quarter stood at Rs14.0 bn, down 1.7% QoQ and 3.1% YoY.** EBIT margin declined 122bps QoQ to 16.5%, due to 200bps margin decline in IT service and 90bps in Consumer Care and Lighting segments.
- Higher forex gains and lower tax rate boosted net profit:** Wipro's net profit of Rs13 bn came in-line with street estimates despite 7% below estimate operating profit, thanks to high forex gain (Rs875 mn versus Rs711 mn in Q1) and lower tax rate (18% compared to 18.9% in Q1). Net margin declined by around 130bps to 14.4%.
- Segmental analysis**
 - IT services business: Strong volume growth but pricing decline continues for second quarter in-a-row**
 - IT services revenue stood at Rs68.3 bn (US\$1,473 mn), representing sequential growth of 6.6% in Rs and 4.6% in US\$. On constant currency basis, revenue was at US\$1,485 mn, up 5.5% sequentially.
 - Overall volume 6.0% was better than Infosys (4.5%) and lower than TCS (6.2%). However, organic volume growth of 4.6% was in-line with peers. This organic volume growth was highest in past four quarters.

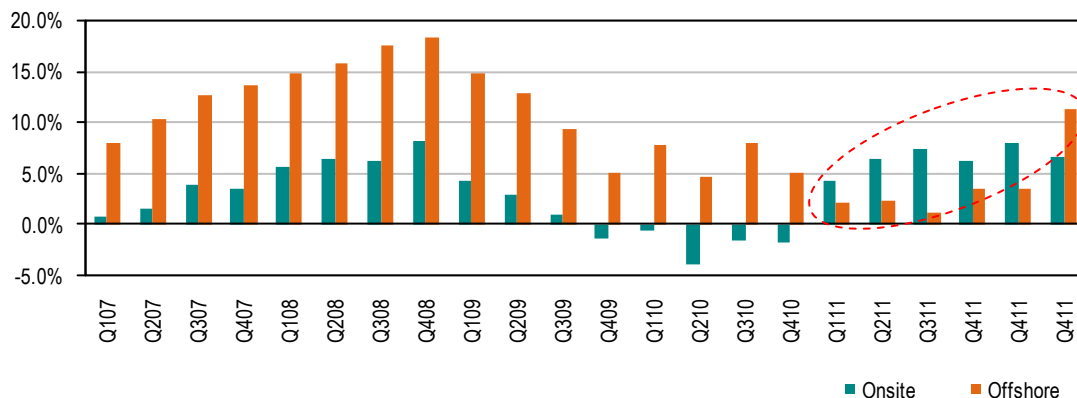
Figure 1: Wipro's growth rate in constant currency terms exceeded than its peers



Source: Company; IDBI Capital Research

Pricing decline raises concern: The constant currency price decline of 3.5% for offshore segment raises concerns whether the company is adapting disruptive pricing strategy to re-gain market share. However, the management indicated that current quarter price decline was due to termination of few fixed price projects, which should be normalized in coming quarters.

Figure 2: Infosys' pricing premium over Wipro has increased significantly in past 6 quarters



Source: Company; IDBI Capital Research

- 200bps EBIT margin dip in Q2FY12:** Operating profit (EBIT) at Rs13.6 bn declined 3.0% QoQ largely on account of wage hike (12% for offshore) and integration of SAIC (low margin business). EBIT margin declined 200bps sequentially to 20.0%. However, with impact of salary hike, promotions and pricing now behind, one should expect margin trajectory to go up in coming quarters.
- Q3FY12 guidance of 1.9% to 3.9%:** Wipro's guidance of 1.9% to 3.9% sequential growth is lower compared to Infosys guidance of 3.2% to 5.4%. However, this lower guidance is on account of seasonality which most IT companies expect to kick-in during Q3, unlike Infosys.
- Broad-based growth across service line:** Barring BPO (down 1%), every service reported growth in the current quarter. Analytics and Information Management (up 7.9%), Technology Infrastructure Services (up 6.5%), Product Engineering & Mobility (up 5.9%), Business Application Services (up 5.0%), and ADM (up 2.8%) led growth during the quarter.

Table 2: Constant currency growth in verticals and geographies

Parameters	Q2FY12
Verticals (%)	
Global Media & Telecom	(0.6)
Finance Solutions	6.9
Manufacturing & Hitech	1.2
Healthcare, Life Sciences & Services	1.8
Retail & Transportation	3.8
Energy & Utilities	24.0
Geography (%)	
America	2.2
Europe	6.8
Japan	16.2
India & Middle East business	11.6
Other emerging markets	13.9

Source: Company; IDBI Capital Research

- **Strong client addition continues for Wipro:** Client addition has been strong (44 new clients versus 49 in Q1) during the quarter taking active client count to 930 versus 937 in Q1FY12. However, client attrition also remains high as the company lost 51 clients in the current quarter, highest in past nine quarters.
- **Impressive performance by Top accounts:** In Q2FY12, top/top-5 and top-10 clients grew by 17.3%/11.3% and 7.9% QoQ respectively.
- **Over 5,000 net addition, highest in past six quarters:** Net addition of 5,240 in the current quarter (highest in past six quarters) takes the total employee count to 131,730. Of the total additions, 4,000 employees were in fresher category.
- **Moderation in attrition rate:** Voluntary attrition (qtrly annualized) in IT services (18.5% v/s 23.2% in Q1) and BPO (14.1% v/s 15.3% in Q1) has moderated in current quarter largely on account of wage hike and promotions in last quarter.
- **Utilisation:** Gross utilisation for IT services stood at 69.3% compared to 69.7% in Q1FY12. Utilisation (excluding trainees) stood at 80.7%, down 30bps over Q1FY12. The management expects utilization rate to stay at current levels as the company is preparing bench for future growth.
- **IT products business:** IT product segment revenue was marginally down 0.5% QoQ to Rs10 bn, largely due to lumpy nature of the business. EBIT stands at Rs451 mn, up 6.6% QoQ. EBIT margin improved marginally by 30bps QoQ to 4.5%.
- **Consumer Care and Lighting business:** Revenue for this segment grew 6.1% QoQ to Rs8 bn. EBIT declined 1.5% QoQ to Rs882 mn. Operating margins stood at 11.0%, down 90bps QoQ largely on account of higher input cost.

Table: Financial snapshot

(Rs mn)

Year-end: March	Q2FY12	Q1FY12	Growth (%)	Q2FY11	Growth (%)	FY10	FY11	FY12E	FY13E
IT Services	68,294	64,046	6.6	57,471	18.8	202,491	234,850	302,034	345,385
IT Products	10,008	10,058	(0.5)	10,693	(6.4)	38,205	36,910	65,828	73,752
Consumer care & lighting	8,002	7,545	6.1	6,651	20.3	22,584	27,259	32,816	37,544
Others	3,766	3,280	14.8	2,904	29.7	8,677	11,523	17,377	21,686
Revenues	90,070	84,929	6.1	77,719	15.9	271,957	310,542	367,987	422,271
IT Services	47,125	42,559	10.7	37,659	25.1	142,967	166,065	202,522	229,283
IT Products	8,934	9,007	(0.8)	9,586	(6.8)	43,465	43,694	51,513	57,442
Consumer care & lighting	4,671	4,257	9.7	3,659	27.7	11,805	15,141	18,987	21,588
Others	4,249	4,198	1.2	2,366	79.6	8,193	11,378	18,778	21,252
Total direct cost	64,979	60,021	8.3	53,270	22.0	186,299	212,850	261,873	296,026
Gross profit	25,091	24,908	0.7	24,449	2.6	85,658	97,692	106,114	126,246
SG&A	11,088	10,667	3.9	10,002	10.9	33,430	40,466	45,685	52,362
EBITDA	16,522	16,579	(0.3)	16,415	0.7	60,059	65,437	70,689	85,496
Depreciation	2,519	2,338	7.7	1,968	28.0	7,831	8,211	10,261	11,612
EBIT	14,003	14,241	(1.7)	14,447	(3.1)	52,228	57,226	60,429	73,884
Other income	863	1,432	(39.7)	955	(9.6)	3,369	4,718	4,407	5,629
Foreign exc. gain / (loss)	875	711	23.1	(414)	(311.4)	(715)	444	2,586	-
Profit before tax & minority int.	15,741	16,384	(3.9)	14,988	5.0	54,882	62,388	67,422	79,512
Tax	2,841	3,096	(8.2)	2,183	30.1	9,293	9,714	12,820	15,902
Adj. net income	12,900	13,288	(2.9)	12,805	0.7	45,589	52,674	54,602	63,610
Minority interest	10	(49)	(120.4)	(148)	(106.8)	(184)	(345)	(19)	(50)
Equity in earnings of affi.	99	110	(10.0)	192	(48.4)	530	648	407	350
Reported net income	13,009	13,349	(2.5)	12,849	1.2	45,935	52,977	54,990	63,910
Diluted EPS (Rs)	5.3	5.4	(2.5)	5.3	1.0	18.8	21.6	22.4	26.0
% of revenue									
Gross profit	27.9	29.3		31.5		31.5	31.5	28.8	29.9
SG&A	12.3	12.6		12.9		12.3	13.0	12.4	12.4
EBITDA	18.3	19.5		21.1		22.1	21.1	19.2	20.2
EBIT	15.5	16.8		18.6		19.2	18.4	16.4	17.5
Reported net profit	14.4	15.7		16.5		16.9	17.1	14.9	15.1
Tax rate	18.0	18.9		14.6		16.9	15.6	19.0	20.0

Source: Company; IDBI Capital Research

Financial Summary

Profit & Loss Account

(Rs mn)

Year-end: March	FY10	FY11	FY12E	FY13E
Net sales	271,957	310,542	367,987	422,271
Growth (%)	5.9	14.2	18.5	14.8
Operating expenses	(211,898)	(245,105)	(297,297)	(336,775)
EBITDA	60,059	65,437	70,689	85,496
Growth (%)	15.6	9.0	8.0	20.9
Depreciation	(7,831)	(8,211)	(10,261)	(11,612)
EBIT	52,228	57,226	60,429	73,884
Interest paid	-	(1,933)	(4,425)	(3,591)
Other income	2,654	7,095	11,418	9,219
Pre-tax profit	54,882	62,388	67,422	79,512
Tax	(9,293)	(9,714)	(12,820)	(15,902)
Effective tax rate (%)	16.9	15.6	19.0	20.0
Net profit	45,589	52,674	54,602	63,610
Adjusted net profit	45,935	52,977	54,990	63,910
Growth (%)	18.4	15.3	3.8	16.2
Shares o/s (mn nos)	2,447	2,451	2,452	2,454

Balance Sheet

(Rs mn)

Year-end: March	FY10	FY11	FY12E	FY13E
Net fixed assets	111,270	113,463	113,371	112,108
Investments	32,765	52,275	57,802	66,652
Other non-curr assets	11,366	6,121	6,121	6,121
Current assets	174,146	199,283	220,156	257,919
Inventories	7,926	9,707	12,548	14,808
Sundry Debtors	50,928	61,627	75,614	84,454
Cash and Bank	64,878	61,141	61,028	78,738
Loans and advances	33,706	42,659	47,778	54,467
Total assets	329,547	371,142	397,450	442,800
Shareholders' funds	196,548	240,371	274,117	324,222
Share capital	2,936	4,908	4,883	4,887
Reserves & surplus	193,175	234,772	268,524	318,575
Total Debt	67,066	63,196	50,557	40,030
Curr Liab & prov	65,933	67,575	72,776	78,548
Total liabilities	132,999	130,771	123,333	118,578
Total equity & liabilities	329,547	371,142	397,450	442,800
Book Value (Rs)	80	98	112	132

Source: Company; IDBI Capital Research

Cash Flow Statement

(Rs mn)

Year-end: March	FY10	FY11	FY12E	FY13E
Pre-tax profit	54,882	62,388	67,422	79,512
Depreciation	10,838	6,214	10,261	11,612
Tax paid	(20,874)	(4,469)	(12,820)	(15,902)
Chg in working capital	(16,225)	(27,232)	(15,786)	(14,280)
Other operating activities	22,376	3,536	(1,672)	(1,729)
Cash flow from operations (a)	50,997	40,437	47,405	59,213
Capital expenditure	(5,140)	(8,407)	(10,169)	(10,350)
Chg in investments	(14,577)	(19,510)	(5,527)	(8,850)
Other investing activities	(14,098)	10,678	599	718
Cash flow from investing (b)	(33,815)	(17,239)	(15,097)	(18,482)
Equity raised/(repaid)	169	2,908	(6,844)	1,098
Debt raised/(repaid)	6,315	(3,870)	(12,639)	(10,527)
Dividend (incl. tax)	(10,305)	(14,308)	(15,659)	(15,672)
Chg in minorities	548	557	407	350
Other financing activities	1,414	(11,142)	1,672	1,729
Cash flow from financing (c)	(1,859)	(25,855)	(33,063)	(23,022)
Net chg in cash (a+b+c)	15,323	(2,657)	(755)	17,710

Financial Ratios

Year-end: March	FY10	FY11	FY12E	FY13E
Adj. EPS (Rs)	18.8	21.6	22.4	26.0
Adj. EPS growth (%)	17.7	15.1	3.8	16.1
EBITDA margin (%)	22.1	21.1	19.2	20.2
Pre-tax margin (%)	20.2	20.1	18.3	18.8
ROE (%)	26.5	24.3	21.4	21.4
ROCE (%)	22.0	20.2	19.2	21.4
Turnover & Leverage ratios (x)				
Asset turnover (x)	0.9	0.9	1.0	1.0
Leverage factor (x)	1.8	1.6	1.5	1.4
Net margin (%)	16.9	17.1	14.9	15.1
Working Capital & Liquidity ratio				
Inventory days	11	11	12	13
Receivable days	68	72	75	73
Payable days	75	66	62	62

Valuation

Year-end: March	FY10	FY11	FY12E	FY13E
P/E (x)	19.5	17.0	16.3	14.1
Price / Book value (x)	4.6	3.7	3.3	2.8
PCE (x)	16.7	14.7	13.8	11.9
EV / Net sales (x)	3.3	2.9	2.4	2.0
EV / EBITDA (x)	15.0	13.8	12.6	10.1
Dividend Yield (%)	1.0	1.4	1.5	1.5



Notes

Vikrant Oak – Head Institutional Equities	(91-22) 4322 1385	vikrant.oak@idbicapital.com
Sonam H. Udasi – Head Research	(91-22) 4322 1375	sonam.udasi@idbicapital.com
Dealing	(91-22) 6637 1150	dealing@idbicapital.com

Key to Ratings

Stocks:

BUY: Absolute return of 15% and above; **ACCUMULATE:** 5% to 15%; **HOLD:** Upto $\pm 5\%$; **REDUCE:** -5% to -15%; **SELL:** -15% and below.

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Equity Research Desk

3rd Floor, Mafatlal Centre, Nariman Point, Mumbai – 400 021. Phones: (91-22) 4322 1212; Fax: (91-22) 2285 0785; Email: info@idbicapital.com

SEBI Registration: NSE CM – INB230706631, NSE F&O – INF230706631, BSE CM – INB010706639, BSE F&O – INF010706639, NSDL – IN-DP-NSDL-12-96

Compliance Officer: Christina Fernandes; Email: compliance@idbicapital.com; Telephone: (91-22) 4322 1212

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