

Mahindra Satyam (SATCOM)

₹ 84

We met the management of Mahindra Satyam to understand demand trends and execution strategy, going forward. Incorporated in 1987 by the two Raju brothers, Satyam Computers was the fourth largest Indian IT company till Q2FY09 with ~53,000 employees and revenues in excess of \$2 billion, providing services to global 2000 companies. The company's historical focus has been manufacturing and package implementation services, thanks to its relationship with SAP. Mahindra group acquired Satyam in April 2009 after the erstwhile founders reported financial irregularities in January 2009. The key takeaways are highlighted below.

Revenue growth, EBIT margin pressures get alleviated

In Q4FY11, Mahindra Satyam's revenues grew 7.5% QoQ to ₹ 1,375 crore while EBIT margins before exceptional items stood at 9.7% vs. 2.5% in Q2FY11. For the full year FY11, the company reported EBIT margins of 5.3%. The demand pick-up in the fourth quarter is notable considering that the company would not have likely participated in >\$50 million total contract value (TCV) deals in the first half of FY11. Finally, with the client roster stabilising at ~230, we believe the new management has laid the foundation, of rebuilding the company, in the first two years of its three-year resurrection strategy.

Improvement in employee pyramid may yield EBIT margins expansion

Analysing the current employee pyramid at Mahindra Satyam suggests that the company has 20% of its workforce in the 0-3 year band, 34% in 3-6 years, 25% in 6-10 years and the remaining 21% in >10 years. As a rule of thumb, freshers (0-3 year experience) constitute 40-50% of the workforce and employee costs accounts for ~55-65% of revenues, depending on the operating model. The anomaly at Mahindra Satyam can largely be attributed to minimal fresher hiring during the two year rebuilding process. However, hiring of ~17,000 freshers in the next three years could flatten the employee pyramid leading to cost rationalisation, yielding meaningful improvements in EBIT margins.

View

Mahindra Satyam is currently trading at 1.9x on the Mcap/FY11 sales metric vs. 4-6x for Tier-1 Indian IT companies. With a majority of class action lawsuits settled and the organisation rebuilding process almost complete, we believe, management focus should shift to achieving industry comparable revenue and earnings growth, resulting in a re-rating of the stock.

Exhibit 1: Financial summary

(₹ Crore)	FY08	FY09	FY10	FY11
Net Sales (₹ crore)	8473.5	8812.6	5481.0	5145.0
EBITDA margin (%)	21.7	-2.3	4.7	8.8
Depreciation	163.6	839.4	227.6	184.7
Interest	20.2	62.1	32.9	9.7
Other Income	267.2	63.1	105.6	294.2
Related PAT	1687.9	-8015.6	-101.7	-86.2
EPS	25.2	-121.5	-1.1	-1.3

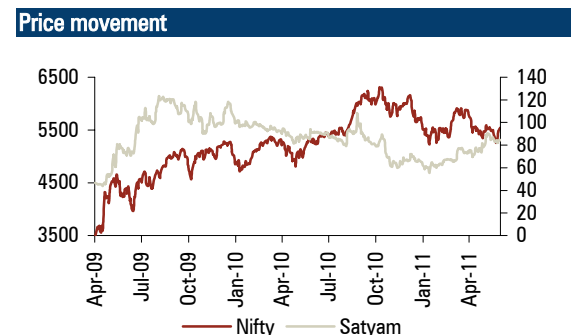
Source: Company, ICICIdirect.com Research

Rating matrix	
Rating	: Unrated
Target	: N/A
Target Period	: N/A
Potential Upside	: N/A

Key Financials				
(₹ Crore)	FY08	FY09	FY10	FY11
Net Sales	8473.5	8812.6	5481.0	5145.0
EBITDA	1834.9	-200.6	256.7	455.1
Net Profit	-123.9	-8176.6	-124.6	-147.3

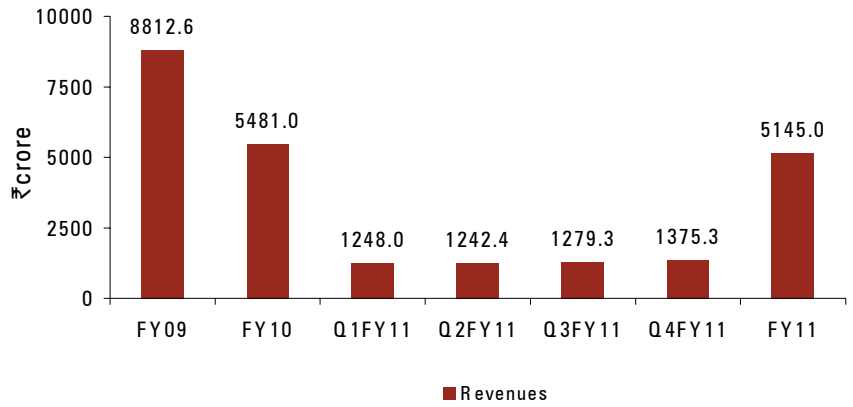
Valuation Summary				
	FY08	FY09	FY10	FY11
PE (x)	NM	NM	NM	NM
EV to EBITDA(x)	NM	NM	NM	NM
Price to book (x)	NM	3.3	2.2	3.4
RONW (%)	NM	NM	NM	NM
ROCE (%)	NM	11.8	9.8	2.6

Stock Data	
Market cap (₹ crore)	9894.4
Debt (Mar-11)	814.2
Cash (Mar-11)	1633.4
EV	9075.2
52 week H/L (₹)	114 / 54
Equity capital	235.30
Face value	2.00
DII Holding (%)	3.7
FII Holding (%)	8.9



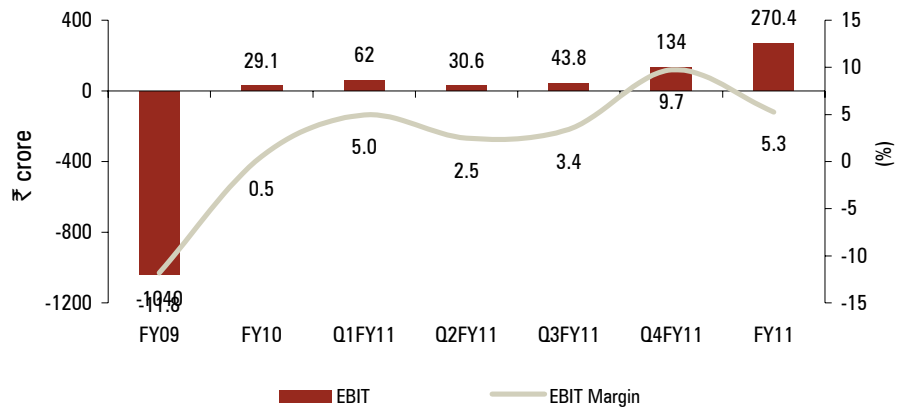
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Exhibit 2: Revenue trajectory



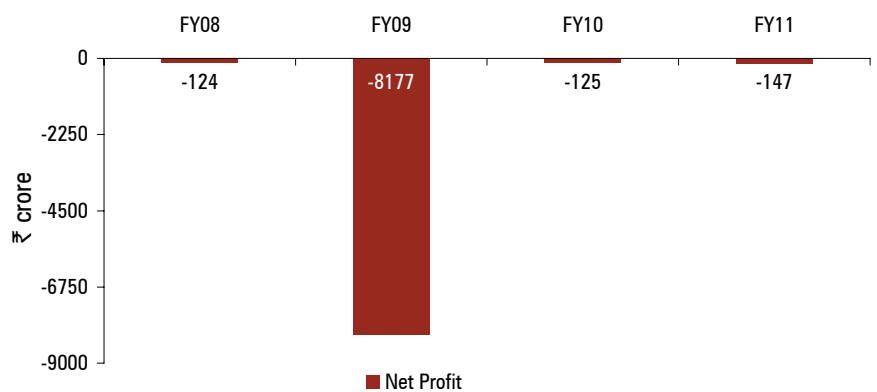
Source: Company, ICICIdirect.com Research

Exhibit 3: EBIT margin profile trend



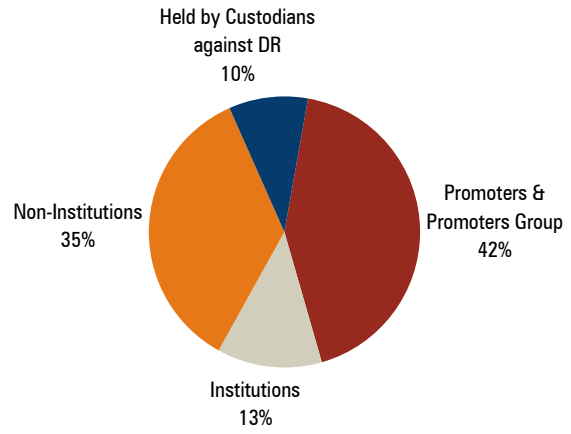
Source: Company, ICICIdirect.com Research

Exhibit 4: Profit after tax profile



Source: Company, ICICIdirect.com Research

Exhibit 5: Shareholding pattern



Source: As on March 31, 2011, Company, BSE, ICICIdirect.com Research

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Buy: Between 10% and 15%/20% for large caps / midcaps, respectively;
Hold: Up to +/-10%;
Sell: -10% or more;

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