

May 23, 2011

Reco	Previous Reco
Hold	Reduce
CMP	Target Price
Rs. 74	Rs 76
EPS change FY12E/13E (%)	14/10
Target Price change (%)	17
Nifty	5,387
Sensex	17,993

Price Performance

(%)	1M	3M	6M	12M
Absolute	(2)	(24)	(23)	(34)
Rel. to Nifty	2	(16)	(23)	(42)

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	IT Services
Bloomberg	SCS@IN
Equity Capital (Rs mn)	2353
Face Value(Rs)	2
No of shares o/s (mn)	1177
52 Week H/L	114/54
Market Cap (Rs bn/USD mn)	87/1,922
Daily Avg Volume (No of sh)	3472112
Daily Avg Turnover (US\$mn)	5.4

Shareholding Pattern (%)

	Mar-11	Dec-10	Sep-10
Promoters	42.7	42.7	42.7
FII/NRI	20.2	18.4	22.5
Institutions	3.4	3.1	3.3
Private Corp	7.1	9.1	8.4
Public	26.7	26.7	23.2

Source: Capitaline

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- Mahindra Satyam reported revenues at US\$ 304 mn(+7.2% QoQ) ahead of Emkay est, with margins expanding by ~660 bps to 13% (V/s Emkay expectations of ~8.6%)
- Profits (ex exceptional items) at Rs 2,445 mn (+118% QoQ) helped by better than expected operating show, higher other income and tax write backs
- Opmetrics mixed with rev from US/ROW up by 4.7/42% QoQ while European rev down by ~11% QoQ. We believe that MahSat faces higher supply-side pressures(refer section)
- Raise FY12/13E earnings by 14.4/10.3% to Rs 5/6.4 as we assume higher mgns at 12.7/13.7 % (11.1/12.5% earlier). Raise rating to HOLD TP Rs 76 (V/s REDUCE,TP Rs 65 earlier)

Good operating show, however op metrics performance remains mixed

Mahindra Satyam reported revenues at US\$ 304 mn (+7.2% QoQ), ahead of estimates aided by volume growth of 3.5% QoQ, ~160 bps cross currency gains and efficiency related QoQ increase of ~210 bps. However we are positively surprised by co's operating margin show with EBITDA margins at 13% (up by ~660 bps QoQ significantly ahead of Emkay expectations of ~220 bps improvement). **We note that co's personal costs have largely remained flat over the past 3 quarters despite adding ~1500 people over the period.** Profits (ex exceptional losses of Rs 5,715 mn) at Rs 2,455 mn (+118% QoQ) were higher than Emkay expectations of Rs 984 mn driven by higher than expected operational performance, higher than expected other income and tax reversals of Rs. 115 mn (V/s expectations of ~21% effective tax rate).

Metrics show mixed; still believe that Mahindra Satyam faces strong margin headwinds

Op metrics performance was mixed with revenue growth during the quarter was led by US(+4.7% QoQ) and ROW (+42% QoQ) while European revenues declined by ~11% QoQ (after a 21% QoQ growth in Dec'10 quarter). While March'11 margins caught us by a surprise we believe that Mahindra Satyam has limited room to improve margins further given that (1) Mahindra Satyam's non manpower expenses are already in line with Tier 1 peers Infosys and TCS, (2) co has already leveraged non manpower expenses meaningfully over FY11(refer table below). We build in EBITDA margins at 12.7%/13.7% (V/s 11.1%/12.5% earlier and 13% in March'11 quarter) for FY12/13.

Raise FY12/13E by ~14%/10% to Rs 5/6.4, Upgrade to HOLD

We raise our FY12/13E earnings by ~14.4%/10.3% to Rs 5/6.4 (V/s Rs 4.4/5.8 earlier) driven primarily by higher margin assumptions to 12.7%/13.7% (V/s 11.1%/12.5% earlier). We upgrade our rating to HOLD(V/s REDUCE earlier) with a revised TP of Rs 76(V/s Rs 65 earlier) however believe that a good March'11 quarter remains priced in and believe that further upsides in the stock hinge on consistent performance ahead

Financials

Rs mn

Y/E	Net	EBITDA	EBITDA	PAT	EPS	ROE	P/E(x)	EV/	P/B
March	Sales		%		(Rs)	%	(x)	EBITDA	(x)
FY10	54,810	4,569	8.3	3,917	2.5	58.4	29.7	14.3	4.6
FY11	51,450	4,551	8.8	4,318	4.2	27.4	17.6	13.1	5.0
FY12E	61,854	7,868	12.7	5,921	5.1	29.6	14.5	7.7	3.8
FY13E	73,022	9,994	13.7	7,534	6.4	28.3	11.4	5.5	2.8

Quarterly performance

Rs mn	Q1 FY11	Q2FY11	Q3FY11	Q4FY11	QoQ (%)	FY 11	FY10	YoY %
Revenue	12,480	12,424	12,793	13,753	7.5	51,450	54,810	(6.1)
Operating Expenditure	11,266	11,689	11,974	11,970	(0.0)	46,899	50,241	(6.7)
Cost of revenues	8,677	9,136	9,089	9,041	(0.5)	35,943	39,811	(9.7)
as % of sales	69.5	73.5	71.0	65.7		69.9	72.6	
SG&A expenses	2,589.0	2,553.0	2,885.0	2,929.0	1.5	10,956	10,430	5.0
as % of sales	20.7	20.5	22.6	21.3		21.3	19.0	
EBITDA	1,214	735	819	1,783	117.7	4,551	4,569	(0.4)
Depreciation	594	429	381	443	16.3	1,847	2,144	(13.9)
EBIT	620	306	438	1,340	205.9	2,704	2,425	11.5
Other Income	707	909	850	1,000	17.6	3,466	727	376.8
PBT	1,327	1,215	1,288	2,340	81.7	6,170	3,152	95.7
Total Tax	264	270	159	(115)	(172.3)	578	222	160.4
Adjusted PAT	1,063	945	1,129	2,455	117.4	5,592	2,930	90.9
(Profit)/loss from JV's/Ass/MI	9.0	7.0	7.0	10.0		33	7	
APAT after MI	1,054	938	1,122	2,445	117.9	5,559	2,923	90.2
Extra ordinary items	-79	-84	-533	-5715		-6,411	4,169	
Reported PAT	975	854	589	(3,270)	(655.2)	(852)	7,092	(112.0)
Reported EPS	0.8	0.7	0.5	(2.8)	(655.2)	-0.7	2.5	(129.1)

Margins (%)	(bps)				(bps)			
EBIDTA	9.7	5.9	6.4	13.0	656	8.8	8.3	(51)
EBIT	5.0	2.5	3.4	9.7	632	5.3	4.4	(83)
EBT	10.6	9.8	10.1	17.0	695	12.0	5.8	(624)
PAT	7.8	6.9	4.6	(23.8)	(2,838)	10.8	5.3	(547)
Effective Tax rate	19.9	22.2	12.3	(4.9)	(1,725.9)	9.4	7.0	(232.5)

Source: Company, Emkay Research

Mahindra Satyam has leverage non manpower expenses meaningfully through FY11

Cost per employee (in Rs mn)	June'10	Sep'10	Dec'10	March'11
Infosys	1.18	1.24	1.23	1.22
TCS	1.14	1.20	1.15	1.14
Mahindra Satyam	1.28	1.34	1.29	1.27

Non manpower expenses, as % of revenues

Infosys	9.4	14.4	13.0	13.7
TCS	13.9	13.6	14.2	14.1
Mahindra Satyam	18.0	16.7	18.0	14.9

Source: Companies, Emkay Research

Raise FY12/13E earnings by ~14.4%/10.3% to Rs 5/6.4 driven primarily by higher op margin assumptions

(All fig in Rs mn except EPS)	FY12E			FY13E		
	Old	New	% change	Old	New	% change
Revenues(US\$ mn)	1,348	1,375	2.0	1,611	1,623	0.7
Revenues	60,650	61,854	2.0	72,495	73,022	0.7
EBITDA	6,725	7,868	17.0	9,061	9,994	10.3
Net profits	5,150	5,893	14.4	6,832	7,506	9.9
EPS	4.4	5.0	14.4	5.8	6.4	10.3

Source: Emkay Research

Financials

Income Statement

Y/E, Mar (Rs. m)	FY10	FY11E	FY12E	FY13E
Net Sales	54,810	51,450	61,854	73,022
Growth (%)		(6)	20	18
Total Expenditure	(50,241)	(46,899)	(53,986)	(63,028)
Growth (%)		(7)	15	17
EBIDTA	4,569	4,551	7,868	9,994
Growth (%)		(0)	73	27
EBIDTA %	8.3	8.8	12.7	13.7
Other Income	2,043	2,289	1,955	2,080
Depreciation	(2,144)	(1,847)	(1,836)	(1,936)
EBIT	4,468	4,993	7,987	10,138
Interest	(329)	(97)	(92)	(92)
EBT	4,139	4,896	7,895	10,046
Tax	(222)	(578)	(1,974)	(2,511)
EAT	3,917	4,318	5,921	7,534
Growth (%)		10	37	27
EAT (%)	7.1	8.4	9.6	10.3

Balance Sheet

Y/E, Mar (Rs. m)	FY10	FY11P	FY12E	FY13E
Equity share capital	2,352	2,353	2,353	2,353
Reserves & surplus	43,947	43,860	49,753	57,260
Networth	46,299	46,213	52,106	59,613
Minority Interest	201	234	234	234
Secured Loans	422	315	315	-
Unsecured Loans	-	-	-	-
Loan Funds	422	315	315	-
Total Liabilities	46,923	46,762	52,655	59,847
Goodwill				
Gross Block	25,635	30,847	33,847	37,847
Less: Depreciation	(19,501)	(21,348)	(23,184)	(25,119)
Net block	6,134	9,499	10,663	12,728
Capital WIP	3,731	-	-	-
Investment	6,268	4,348	4,348	4,348
Current Assets	39,799	47,286	49,780	60,108
Inventories	-	592	-	-
Sundry debtors	9,230	11,588	13,557	16,005
Cash & bank balance	21,768	27,538	26,055	32,100
Loans & advances	3,845	3,782	5,084	6,002
Other current assets	4,956	3,786	5,084	6,002
Current Liab & Prov	24,222	31,044	28,809	34,010
Current liabilities	8,818	15,463	13,557	16,005
Provisions	15,404	15,581	15,252	18,005
Net current assets	15,577	16,242	20,971	26,098
Misc exps	15,187	16,660	16,660	16,660
Deferred Tax	26	13	13	13
Total Assets	46,923	46,762	52,656	59,847

Cash Flow

Y/E, Mar (Rs. m)	FY10	FY11E	FY12E	FY13E
Net Profit after Tax	(1,246)	(1,473)	5,985	7,598
Add : Depreciation	2,144	1,847	1,836	1,936
Add : Misc exp w/off				
Net changes in WC	(990)	5,484	(5,883)	(1,836)
Operational Cash Flows	914	5,525	1,637	10,480
Capital expenditure	379	(1,481)	(3,000)	(4,000)
Investments	(5,994)	-	-	-
Investing Cash Flows	(5,615)	(1,481)	(3,000)	(4,000)
Borrowings	(7,720)	(107)	-	(315)
dividend paid	-	-	-	-
Issue of shares	29,180	-	(92)	(92)
Share Premium			-	-
Financing Cash Flows	21,460	(107)	(92)	(407)
changes in cash	16,759	3,937	(1,455)	6,073
Opening balance	5,009	21,768	27,538	26,055
Closing balance	21,768	27,538	26,055	32,100

Key Ratios

Y/E, Mar	FY10	FY11E	FY12E	FY13E
EPS (Rs)	2.5	4.2	5.1	6.4
CEPS (Rs)	4.3	5.8	6.6	8.1
Book Value Per Share (Rs)	15.9	14.6	19.6	26.0
Dividend Per Share (Rs)	-	-	-	-
Valuations Ratios (x)				
PER	29.7	17.6	14.5	11.4
P/CEPS	17.2	12.9	11.2	9.2
P/BV	4.6	5.0	3.8	2.8
EV/EBIDTA	14.3	13.1	7.7	5.5
EV/Sales	1.2	1.2	1.0	0.7
M-Cap/sales	1.8	2.0	1.6	1.4
Profitability Ratios (%)				
RoCE	25.5	14.5	29.2	29.6
RoNW	58.4	27.4	29.6	28.3
EBITDA Margin	8.3	8.8	12.7	13.7
EBIT Margins	4.4	5.3	9.8	11.0
Net Profit Margin	7.1	8.4	9.6	10.3

Recommendation History: Mahindra Satyam – SCS IN

Date	Reports	Reco	CMP	Target
14/02/2011	Mahindra Satyam Q3FY11 Result Update	Reduce	65	65
16/11/2010	Mahindra Satyam Q2FY11 Result Update	Reduce	85	70
11/10/2010	Mahindra Satyam Re-initiating Coverage	Reduce	86	81

Recent Research Reports

Date	Reports	Reco	CMP	Target
18/05/2011	eClerx Services Q4FY11 Result Update	Accumulate	737	840
10/05/2011	Infinite Computer Q4FY11 Result Update	Buy	164	250
28/04/2011	Hexaware Q1CY11 Result Update	Accumulate	70	80
27/04/2011	Patni Computer Q1CY11 Result Update	Not Rated	459	NA

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