

Company

23 July 2010 | 9 pages

Wipro (WIPR.BO)

Equity

Good Quarter; Strong Guidance

- Good 1Q; 2Q guidance strong** — IT Services revenues in 1Q11 were up ~4% QoQ in constant currency and ~3% in US\$-terms (CIRA est.: ~4%). Volume growth was healthy at ~5%, with onsite volumes picking up ~16%, indicating material project starts. Profits at ~Rs13b were up ~9% QoQ (CIRA est.: -1%). Guidance for 2Q is for a strong ~4-6% QoQ revenue growth, slightly ahead of Infosys (~4-5% QoQ).
- Margins improve yet again** — EBIT margins in IT Services improved ~30bps QoQ despite the headwinds of wage hikes (one month of additional impact) and cross currency. The tailwinds were better realizations from forex covers and other operational efficiencies. Wipro has improved margins by ~400bps over the last six quarters – despite wage hikes and forex volatility.
- How does it compare with peers?** — TCS came up with the best performance of the quarter. In terms of guidance, Wipro is a little ahead of Infosys. In terms of margins, Infosys disappointed vis-à-vis high expectation while Wipro continued on its improvement trajectory. Despite absorbing wage hikes in the last two quarters, Wipro's margins have gone up by ~100bps in the last two quarters.
- Other highlights** — (1) Strong ~4,900 employee net add; (2) Realized pricing was down ~5% QoQ onsite and ~1% offshore; (3) Attrition spiked by more than 500bps; (4) Among verticals, CMSP (~7% QoQ), BFSI (~6%), and Manufacturing & Healthcare (~5%) were the growth drivers, while Energy & Utilities (~-4%) and Technology/Telecom (each ~-2%) dragged. (5) Among the services, package implementation (~10%) and ADM (~4%) stood out, while BPO (~-4%), Testing and Infra (each ~1%) were sluggish; (6) Among geographies, India/Middle East (~6%) and North America (~4%) were strong while Europe (flattish) was slow.
- Maintain Buy** — Among the top three Indian vendors, Wipro carries the least investor expectation in terms of growth/margins etc. and it continues to deliver. The margin improvement story continues to play out and valuations appear reasonable, thus we continue to prefer Wipro on a sector relative basis.

Buy/Low Risk	1L
Price (22 Jul 10)	Rs415.60
Target price	Rs486.00
Expected share price return	16.9%
Expected dividend yield	1.2%
Expected total return	18.1%
Market Cap	Rs1,017,892M
	US\$21,600M

Price Performance (RIC: WIPR.BO, BB: WPRO IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2009A	38,763	15.92	19.9	26.1	6.8	28.0	0.6
2010A	45,937	18.77	17.9	22.1	5.1	26.8	0.9
2011E	53,128	21.69	15.5	19.2	4.3	24.5	1.2
2012E	60,350	24.64	13.6	16.9	3.5	23.1	1.3
2013E	71,344	29.12	18.2	14.3	2.9	22.7	1.3

Source: Powered by dataCentral

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Other Segments

- Consumer business revenues at Rs6.4b were up ~23% YoY with EBITDA margins at ~15% (down ~200bps YoY).
- 'Others' segment had revenues of Rs2.3b (up ~56% YoY) with EBITDA losses at Rs70m (significantly down YoY).

Result Tables

Figure 1. Wipro Ltd – Key Financials

RsM	1Q10	4Q10	1Q11	QoQ	YoY
Revenue (US\$M)	1,366	1,547	1,574	1.8%	15.2%
Revenue	63,868	69,772	71,906	3.1%	12.6%
Cost of revenue	43,247	47,764	48,647	1.8%	12.5%
Gross profit	20,621	22,008	23,259	5.7%	12.8%
Gross margin	32.3%	31.5%	32.3%	80bp	6bp
Operating expenses	7,791	8,701	9,225	6.0%	18.4%
Forex gains/(losses)	-1,406	57	458	703.5%	-132.6%
EBIT	11,424	13,364	14,492	8.4%	26.9%
EBIT margin	17.9%	19.2%	20.2%	100bp	227bp
Dep & Amort.	2,157	2,100	2,118	0.9%	-1.8%
EBITDA	13,581	15,464	16,610	7.4%	22.3%
EBITDA margin	21.3%	22.2%	23.1%	94bp	184bp
Other income	355	1,612	948	-41.2%	167.0%
Profit before tax	11,779	14,976	15,440	3.1%	31.1%
Income tax expense	1,740	3,015	2,345	-22.2%	34.8%
Income from operations	10,039	11,961	13,095	9.5%	30.4%
Affiliates/Minority	65	130	90	-30.8%	38.5%
Net profit	10,104	12,091	13,185	9.0%	30.5%
EPS - basic	4.16	4.97	5.42	9.0%	30.1%
EPS - fully diluted	4.14	4.94	5.42	9.7%	31.0%

Source: Company Reports

Figure 2. Wipro Tech – Key Financials

RsM	1Q10	4Q10	1Q11	QoQ	YoY
Revenue (US\$M)	1,220	1,362	1,376	1.0%	12.8%
Revenue	57,009	61,439	62,864	2.3%	10.3%
Cost of revenue	38,804	41,943	42,607	1.6%	9.8%
Gross profit	18,205	19,496	20,257	3.9%	11.3%
Gross margin	31.9%	31.7%	32.2%	49bp	29bp
Operating expenses	6,166	6,843	7,086	3.6%	14.9%
Forex gains/(losses)	-1,406	57	458	703.5%	-132.6%
EBIT	12,039	12,653	13,171	4.1%	9.4%
EBIT margin	21.1%	20.6%	21.0%	36bp	-17bp
Dep & Amort.	1,963	1,891	1,916	1.3%	-2.4%
EBITDA	14,002	14,544	15,087	3.7%	7.7%
EBITDA margin	24.6%	23.7%	24.0%	33bp	-56bp

Source: Company Reports

Figure 3. Key Client Metrics

	1Q10	2Q10	3Q10	4Q10	1Q11
Client relationship					
Total active clients	830	840	822	845	858
New clients	26	37	31	27	22
Relationship size					
\$1M+	413	403	398	406	434
\$1M-\$3M	194	187	165	180	196
\$3M-\$5M	63	64	77	60	73
\$5M-\$10M	59	53	61	70	65
\$10M-\$20M	44	48	42	40	42
\$20M+	36	35	37	40	41
Client concentration					
Top customer	2.6%	2.7%	2.6%	2.5%	2.9%
Top 5	11.4%	11.3%	10.8%	10.5%	10.9%
Top 10	20.6%	19.7%	19.5%	19.3%	19.8%

Source: Company Reports

Figure 4. Revenue Mix

	1Q10	2Q10	3Q10	4Q10	1Q11
Service Mix					
Technology Infra Services	20.9%	20.6%	21.3%	21.6%	21.1%
Testing	12.1%	12.0%	11.5%	11.7%	11.4%
Package Implementation	13.4%	13.3%	12.8%	12.7%	13.5%
Product Engineering	4.6%	3.9%	4.1%	4.1%	4.7%
BPO	10.1%	10.5%	10.6%	10.9%	10.1%
ADM	38.9%	39.7%	39.7%	39.0%	39.2%
Vertical Mix					
Technology	9.4%	8.7%	8.4%	8.6%	8.5%
Telecom	8.4%	8.1%	7.9%	8.2%	8.1%
CMSP	8.9%	9.6%	9.8%	8.8%	9.1%
Technology Business	26.7%	26.4%	26.1%	25.6%	25.7%
Financial Services	26.3%	25.7%	25.8%	26.1%	26.9%
Mfg & Healthcare	15.5%	15.6%	15.1%	14.8%	15.1%
Retail & Transportation	15.2%	15.2%	14.8%	14.7%	14.9%
Energy & Utilities	8.3%	9.0%	9.5%	9.6%	8.9%
Enterprise Business	73.3%	73.6%	73.9%	74.4%	74.3%
Geographic Mix					
North America	59.7%	58.4%	57.1%	56.7%	57.3%
Europe	25.5%	26.5%	26.3%	26.3%	25.4%
Japan	1.8%	1.6%	1.6%	1.5%	1.5%
India & ME	7.9%	8.1%	8.9%	8.8%	9.0%
Other EM	5.1%	5.4%	6.1%	6.7%	6.8%

Source: Company Reports

Figure 5. Key Execution Metrics

	1Q10	2Q10	3Q10	4Q10	1Q11
Closing Headcount	98,521	97,891	102,746	108,071	112,925
Realization - Global IT (Inc. APAC IT Exc. BPO & IFOX)					
Onsite	11,787	12,340	12,299	12,254	11,647
Offshore	4,302	4,450	4,345	4,352	4,293
Volume - Global IT (Inc. APAC IT Exc. BPO & IFOX)					
Available person-month					
- Onsite	34,607	34,070	35,505	36,206	42,117
- Offshore	126,628	122,581	123,428	132,063	135,970
- Support	16,390	16,216	16,309	16,863	17,729
Billed person-month					
- Onsite	32,876	32,367	33,730	34,396	40,011
- Offshore	91,454	90,093	94,487	99,067	99,698
Utilization					
Global IT - Gross (ex IFOX)	70%	71%	73%	72%	71%
Global IT - Net (ex IFOX)	77%	78%	81%	79%	78%
Global IT - Net ex trainees (ex IFOX)	78%	81%	85%	83%	82%
Attrition					
Global IT services	16%	23%	17%	19%	24%
BPO - quarterly	14%	17%	15%	17%	16%
BPO - during training	7%	7%	6%	8%	7%
BPO - post training	7%	10%	9%	9%	9%

Source: Company Reports

Wipro

Company description

Wipro is a leading Indian company with business interests in IT and BPO services exports, domestic hardware, consumer lighting and consumer care. It has one of the widest ranges of services, including systems integration, IT-enabled services, package implementation, software application development & maintenance and R&D services. Wipro is the first P-CMM Level 5 and SEI-CMM Level 5 certified IT services company in the world. It has ~850 clients spanning the BFSI, Manufacturing, Retail, Utilities and Telecom verticals. Its IT services exports team has ~70,000 employees and BPO operation has more than 24,000 employees.

Investment strategy

We rate Wipro shares as Buy/Low Risk (1L). As one of the top three Indian IT services firms, Wipro looks well positioned to benefit from growing demand for offshore IT services. Apart from economies of scale in offshore delivery, one of Wipro's key strengths is its full-service model. This includes a strong position in the infrastructure/R&D services business, which offers significant long-term growth potential. It has strong exposure to the BPO segment, which should offer above-average growth in the long term. Wipro's management has actively pursued acquisitions to strengthen its service portfolio. We expect ~17% revenue and ~16% EPS CAGR over FY10-13E.

Valuation

Our target price of Rs486 is based on 21x the average of FY11-12E EPS. Our target multiple is derived from a PE-band analysis of Wipro's historical trading pattern and peer group valuations. Wipro has traded at 8-31x over the past 3 years. Given that revenue visibility is improving with business environment stabilizing, we believe Wipro should trade higher than the mid-point of the band. We think Wipro will continue to trade at a marginal discount to Infosys. PE is the most appropriate valuation measure, in our view, given Wipro's profitability and earnings visibility.

Risks

We rate Wipro Low Risk despite our quantitative risk-rating system suggesting High Risk as the company has significant scale, enjoys a good brand name and continues to generate significant FCF. Key downside risks that could cause shares to fall below our target price include: (1) an extended slowdown in the US economy; and (2) any significant appreciation of the rupee against the USD/EUR/GBP.

Appendix A-1

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Wipro (WIPR.BO)

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Analyst: Surendra Goyal, CFA

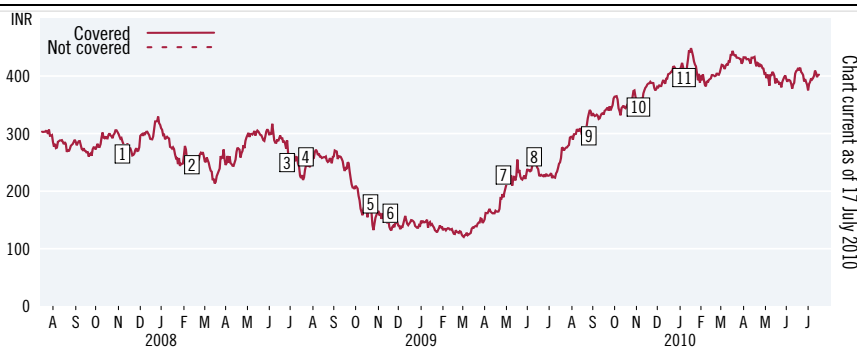


Chart current as of 17 July 2010

	Date	Rating	Target Price	Closing Price
1	7-Nov-07	1L	*339.00	286.41
2	13-Feb-08	*1M	*321.00	245.97
3	26-Jun-08	1M	*330.00	287.97
4	23-Jul-08	*2M	*264.00	244.65

* Indicates change

	Date	Rating	Target Price	Closing Price
5	22-Oct-08	2M	*195.00	167.55
6	19-Nov-08	*2H	*159.00	133.53
7	28-Apr-09	*2M	*216.00	189.24
8	10-Jun-09	*2L	*270.00	259.62

	Date	Rating	Target Price	Closing Price
9	26-Aug-09	*1L	*372.00	334.35
10	4-Nov-09	1L	*408.00	357.48
11	7-Jan-10	1L	*486.00	406.53

Rating/target price changes above reflect Eastern Standard Time

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