

## 4Q: Concerns on HP channel drag continue

# First Look

Breaking news, market events and company announcements

### Results below expectations; maintain Reduce

4QFY11 results were below expectations on US\$ revenue growth, EBIT margins and PAT. The drag on HP channel continues (62% of revenue) with US\$ revenues declining by 3.6% q-q and 18% y-y. We will be revisiting our numbers post the conference call tomorrow and incorporating 4Q results and particularly the lag in HP channel revenues. We maintain our Reduce rating and expect the stock to react negatively to results. Our current EPS estimates are INR33.9/INR35.5 in FY12/13F.

### 4QFY11 results highlights

- Mphasis revenues were US\$274mn (flat sequentially) using average exchange rates reported by the company (vs est. of 6% q-q increase).
- EBITDA margins improved by 280bp to 17.9%, primarily due to the 7.5% depreciation of the rupee against USD (vs est. of 380bp rise).
- PAT at INR1.83bn (vs est. of INR1.89bn).
- HP channel US\$ revenues declined by 3.6% q-q and 18% y-y and is now 62% of Mphasis revenues.
- Direct channel US\$ revenues increased by 10.6% q-q and were 38% of revenues. 4Q included ~USD4mn inorganic contribution from the Wyde acquisition, organic growth in direct channel was 6.3% q-q.
- Headcount declined by 838 people (2% q-q decline) to 40,426, on the back of a 1.1% q-q decrease in 3Q, with declines across Apps, ITO and BPO.
- Pricing saw a decline in apps, onsite from US\$70 to US\$69 per hour, while remaining flat at other divisions.
- Cash and cash equivalents were USD317mn or Rs79/share. This is after excluding the INR4.2bn in an escrow account for payout towards the Wyde acquisition.

Note: All of our calculations exclude the impact of one-off prior period revenues of INR665mn in 3Q.

Fig. 1: Mphasis 4QFY11 Actual vs. Expected

Key parameters	4QFY11		3QFY11	q-q (%)	4QFY10	y-y (%)
	Actual	Est.				
Revenues (US\$ mn)	274	292	275	-0.4%	296	-7.5%
Revenues (Rs mn)	13,138	12,999	12,271	7.1%	13,454	-2.3%
EBITDA (Rs mn)	2,347	2,462	1,851	26.8%	3,204	-26.7%
EBITDA (%)	17.9	18.9	15.1	280bp	23.8	-600bp
Adj. PAT (Rs mn)	1,830	1,898	1,430	28.0%	2,840	-35.6%

Note: 3QFY11 revenues, EBITDA and PAT exclude impact of Rs665mn of one-off prior year revenues

Source: Company data, Nomura estimates

November 30, 2011

<b>Rating</b> Remains	<b>Reduce</b>
<b>Target price</b> Remains	INR 335
<b>Closing price</b> November 29, 2011	INR 322

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# Appendix A-1

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### Mentioned companies

Issuer name	Ticker	Price	Price date	Stock rating	Sector rating	Disclosures
Mphasis	MPLH IN	INR 322	29-Nov-2011	Reduce	Not rated	

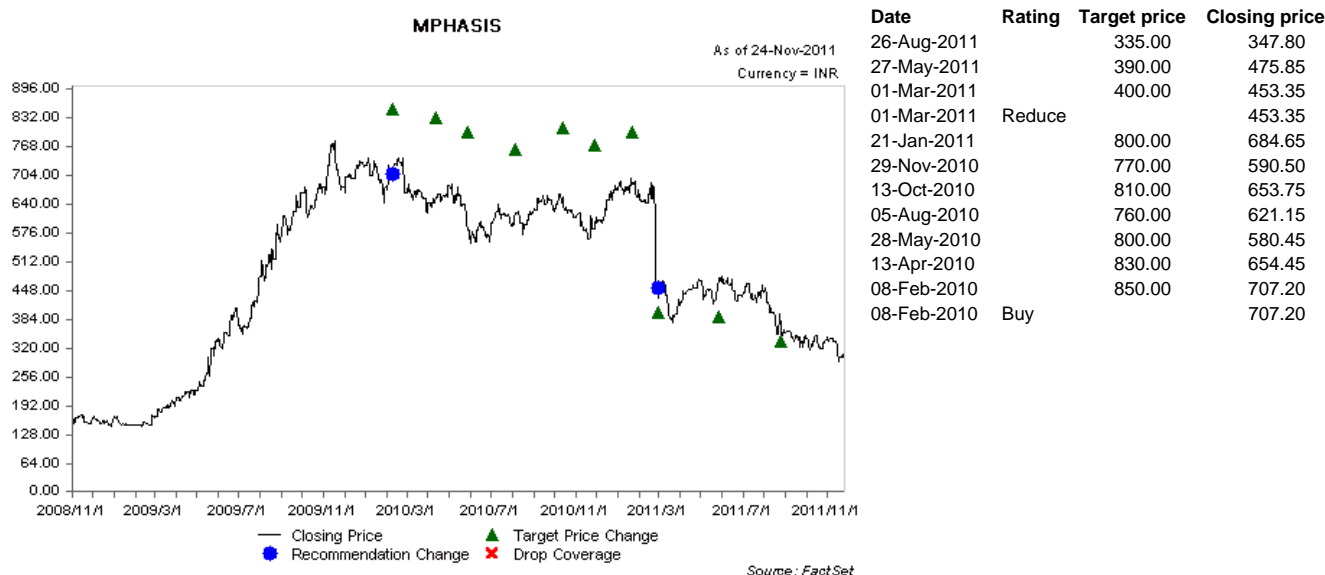
## Previous Rating

Issuer name	Previous Rating	Date of change
Mphasis	Buy	01-Mar-2011

### Mphasis (MPLH IN)

INR 322 (29-Nov-2011) Reduce (Sector rating: Not rated)

Rating and target price chart (three year history)



For explanation of ratings refer to the stock rating keys located after chart(s)

**Valuation Methodology** Our target price of INR335 is based on 9.5x one-year rolling forward earnings (INR35.5), a discount of ~50% to the target multiple at which we value Infosys. We consider the discount justified based on deterioration in the HP channel outlook.

**Risks that may impede the achievement of the target price** Inorganic triggers on usage of cash of USD450mn+, favourable rethink on HP's offshoring strategy towards Mphasis and delisting by the promoter remain upside risks.

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### Explanation of Nomura's equity research rating system for Asian companies under coverage ex Japan published from 30 October 2008 and in Japan from 6 January 2009

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