

Mahindra Satyam

Performance highlights

Y/E March (₹ cr)	4QFY11	3QFY11	% chg (qoq)	Consensus est.	% Var.
Net sales	1,375	1,279	7.5	1,336	2.9
EBITDA margin (%)	13.0	6.4	656bp	7.8	516bp
Recurring PAT*	245	112	118	104.0	135.1

Source: Company, Angel Research; Note: * excluding exceptional items

Quarterly results highlights: Mahindra Satyam (Satyam) reported its 4QFY2011 numbers. The company outperformed street's expectations on the revenue as well as operational front, but its net profit got knocked off due to exceptional items. Dollar revenue grew by whopping 7.0% qoq (surpassing all Indian tier-1 IT players) to US\$304mn from US\$284mn in 3QFY2011 on the back of 3.5% qoq volume growth, 1.6% qoq gain due to favourable cross-currency movement and ~2% on the back of efficiency gained from fixed price bids. Pricing remained stable on a qoq basis for the company. In rupee terms, revenue came in at ₹1,375cr compared to ₹1,279cr in 3QFY2011, up 7.5% qoq.

The company recorded significant improvement of 531bp qoq in gross margin to 34.3% from 29.0% in 3QFY2011. EBITDA margin almost doubled qoq to 13.0% from 6.4% in 3QFY2011, registering an increase of 656bp. Margin enhancement came on the back of slightly lower employee costs, improved efficiency due to optimisation of resources (which led to lower SG&A) and steady utilisation level qoq at 73.5%.

Satyam's bottom line during the quarter was negatively affected due to exceptional items worth ₹571cr (including ₹569cr as consideration of class action settlement and rest ₹2cr due to expenses related to forensic investigation and litigation support), which led to net loss of ₹327cr for the company. However, excluding exceptional items, PAT came in at ₹245cr, up 118% qoq, aided by tax reversal of ₹12cr and higher other income of ₹102cr (including ₹17cr of forex gain) vs. ₹87cr in 3QFY2011.

Operating metric highlights

- The media and entertainment service industry emerged as the company's primary growth driver during the quarter. Satyam is also witnessing strong traction in service industries, such as banking and financial services, manufacturing (aerospace, defense and technology) and healthcare.
- Geography wise, US and Rest of the World led the company's growth, registering combined growth of 4.2% qoq and contributing 42% to the company's revenue, while Europe declined by 11% qoq.
- Among service lines, enterprise solutions (~45% to revenue), engineering services and infrastructure management services showed good strength.
- During the quarter, Satyam added 434 employees, taking its total headcount to 29,266 (78% offshore and 22% onsite).
- Attrition rate fell to 22% (quarterly annualised basis) from 25% in 3QFY2011.
- The company's client pyramid saw qualitative improvement, with clients contributing less than US\$10mn to revenue increasing to 34 from 31 in 3QFY2011. Also, in the US\$10mn–20mn bracket, the company added two new clients, taking its client base to 12.
- Total active client base stood at 229 (active clients are clients who contribute more than US\$100,000 per year to revenue).

NOT RATED

CMP	₹74
Target Price	-

Stock Info

Sector	IT
Market Cap (₹ cr)	8,653
Beta	0.8
52 Week High / Low	114/54
Avg. Daily Volume	2,965,567
Face Value (₹)	2
BSE Sensex	17,993
Nifty	5,387
Reuters Code	SATY.BO
Bloomberg Code	SCS@IN

Shareholding Pattern (%)

Promoters	42.7
MF / Banks / Indian Fls	3.7
FII / NRIs / OCBs	8.9
Indian Public / Others	44.7

Abs. (%)	3m	1yr	3yr
Sensex	(1.0)	9.4	9.4
Mahindra Satyam	18.2	(9.6)	(84.7)

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Key concall takeaways

- Satyam plans to hire 5,000 freshers in FY2011. Management indicated that of the total hiring to be done in FY2012, 40% would be freshers. Thus, the total gross addition for Satyam in FY2012 comes at 12,500. If we assume the joining ratio to be around 50%, the employee base will increase by ~21% yoy in FY2012, which is positive for the company.
- Currently, 18–20% of Satyam’s employees have less than three years of work experience, which makes the company’s employee pyramid bulging; this can be restructured going ahead to improve margins.
- The company will be giving wage hikes in 2QFY2012, which will negatively affect its margins.
- Management is focusing on improving utilisation level by couple of percentage points, which will aid its operating margins going forward.
- Management is also looking to re-engage in large deals of US\$30mn–100mn as well as deals greater than US\$100mn.
- Tax rate for FY2012 is expected to be at 25–28%.
- Management specified that almost all the major liabilities are settled, except the issue with the Income Tax Department. Hence, management does not foresee occurrence of any exceptional item going forward.
- Capex plan related to setting up campuses in SEZ of Hyderabad and Chennai is at around ₹325cr for FY2012.
- Currently, the company has got hedges worth US\$349mn spanning across the next 18 months.
- On the merger of Satyam with Tech Mahindra, management has indicated that it will trigger the process post October 2011.
- Overall, results were decent vis-à-vis tier-I companies, which sported revenue growth of 3–5% qoq in 4QFY2011. At the CMP of ₹74, the stock is trading at a trailing PE of 17.5x FY2011 recurring EPS of ₹4.2.

Exhibit 1: Profit and loss statement (Consolidated)

(₹ cr)	4QFY2011	3QFY2011	% chg (qoq)	FY2011	FY2010
Income from operations	1375	1279	7.5	5,145	5,481
Employee cost	904	909	(0.5)	3,594	3,981
as % to sales	65.7	71.0		69.9	72.6
Gross profit	471	370	27.2	1,551	1,500
% margin	34.3	29.0	531bp	30.1	27.4
Oper. and admin exp.	293	289	1.5	1,096	1,043
as % to sales	21.3	22.6		21.3	19.0
EBITDA	178	82	117.7	455	457
% margin	13.0	6.4	656bp	8.8	8.3
Depreciation	44	38	16.3	185	214
EBIT	134	44	205.9	270	243
% margin	9.7	3.4	632bp	5.3	4.4
Interest charges	2	2	4.3	10	33
Other income	102	87	17.3	294	106
PBT	234	129	81.7	555	315
Exceptional item	572	53	-	641	417
PBT (after exceptions)	(338)	76	-	(86)	(102)
Tax	(12)	16	(172.3)	58	22
PAT (excl. exceptions)	246	113	117.4	497	293
PAT (incl. exceptions)	(326)	60	-	(144)	(124)
Minority interest	1	1	42.9	3	1
Final PAT	(327)	59	-	(147)	(125)
Adj. PAT	245	112	117.9	494	292
Recurring EPS (₹)	2.1	1.0	117.9	4.2	2.5

Source: Company, Angel Research

Exhibit 2: Balance sheet (Consolidated)

(₹ cr)	FY2011	FY2010	FY2009
Liabilities			
Share capital	235	235	135
Share application money pending allotment	-	0.1	-
Reserves and surplus	4,386	4,395	1,610
Total shareholders' funds	4,621	4,630	1,745
Minority interest	23	20	20
Loan funds	32	42	814
Deferred tax liability	7	4	5
Sub-total	4,683	4,696	2,583
Amount pending investigation suspense account (net)	1,230	1,230	1,230
Total capital employed	5,913	5,927	3,813
Assets			
Fixed assets	950	987	1,239
Investments	435	627	
Deferred tax asset	8	7	7
Current assets, loans and advances			
Inventories	59	-	1
Sundry debtors	1,159	923	1,552
Cash and bank balances	2,754	2,177	501
Other current assets	379	496	291
Loans and advances	378	385	466
Less: Current liabilities and provisions			
Liabilities	1,546	882	1,389
Provisions	1,558	1,540	1,478
Profit and loss account	2,896	2,749	2,625
Sub-total	5,913	5,927	3,813
Unexplained differences suspense account (net)	-	-	-
Total capital deployed	5,913	5,927	3,813

Source: Company, Angel Research

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Disclosure of Interest Statement	Mahindra Satyam
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors

Ratings (Returns):	Buy (> 15%) Reduce (-5% to 15%)	Accumulate (5% to 15%) Sell (< -15%)	Neutral (-5 to 5%)
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