

Mastek

Q2FY10 Earnings Review

Recommendation	:	Marketperformer
CMP	:	Rs 407
Target	:	Rs 462
Upside Potential	:	13.51%

Sector	:	IT
Sensex	:	17641
Bloomberg code	:	MAST IN
Reuters Code	:	MAST BO

AT A GLANCE

Issued Equity Capital (Cr. Shrs)	:	2.69
Mkt. Cap (Rs. in Crs)	:	1095
Major Shareholders		
Promoters (%)	:	42.91%
Free Float (%)	:	57.09%
Avg. Daily Vol. ('000)	:	267.43

Background: Incorporated in 1982, Mastek is a leading IT player with global operations providing enterprise solutions to businesses and governments worldwide. Mastek is having its operations in the U.S, Europe, Canada, Middle East and Asia Pacific with employee strength of over 3700 people. The company has crystallized its focus on two verticals – Insurance and Government – in which it has substantial experience and intellectual property. The company derives majority of its revenue from the government vertical (35.7%) followed by insurance (29.4%) while the rest comes from banking & financial services (BFSI). In Insurance vertical company is acknowledged for its enterprise solution offering called Flixir.

ANALYST

Sheetal Aggarwal +91 44 3000 7365
sheetala@dbschola.murugappa.com

Quarterly numbers below guidance...

The company reported 0.8% sequential dip in operating revenues at Rs 193.23crore for Q1FY10 against a guidance of Rs 195 – 205 crore. The net profit for the quarter was down by 10.9% sequentially at 23.54crore, against a guidance of Rs. 27 -29 crore. The decline was majorly on account of delay in revenue generation from Capita deal on which the investments were made during the quarter. Also, rupee appreciation impacted the earnings with forex loss of Rs 1.47 crore for the quarter. Consequentially, EBIDTA margin declined for the quarter by 320bps at 12.2% against 15.5% in Q1FY10.

Order book reported a big jump...

The order book at the quarter ending December 2010, jumped 22% to Rs 296 crore against Rs 242 crore at the end of sequential quarter. During the quarter, Mastek has entered into an agreement with Capita for a contract value of GBP 24 mn over a period of 24 months. A part of this deal is reflected in the current order book. Capita would see the migration of Zurich Life to Elixir and more clients are expected to add starting FY2011.

Rupee mutes the guidance for Q3FY10...

Mastek's management has guided for a total income of Rs 188 – 195 crore for Q3FY10. The guidance is flat largely on account of the anticipation of rupee appreciation going forward. The net profit is guided at Rs 21 – 23 crore while the operating margins are likely to be restored at 15.5-16% benefiting on ramp ups and cost cutting initiatives taken up by the Company.

Valuations

Mastek reported Q2FY10 numbers on a weak note largely on account of delay in one of the big deals. However, the company's depleting order book reported a sequential jump of 22% during the quarter. The increased order book is likely to translate in better growth going forward. We maintain our estimates for FY10 and FY11, though we do not rule out the impact of appreciating rupee. We also introduce our FY12 earnings estimates. At the current market price the stock is quoting at 8.5x and 7.0x its FY11E and FY12E estimates. We recommend a Marketperformer rating on the stock with a 12-18 months target price of 462.

FY June (Rs Crore)	Turnover	EBITDA	Pre-tax Profit	Net Profit	EPS (Rs)	BVPS (Rs)	PE (X)	DPS	P/BV (X)	ROE (%)
2010E	834.2	145.99	125.44	109.76	40.80	225.9	10.0	10	1.80	18.06%
2011E	934.3	168.17	147.13	128.74	47.85	268.5	8.5	10	1.52	17.82%
2012E	1083.8	195.50	178.60	155.40	57.76	318.8	7.0	10	1.28	18.12%

Operational highlights

Mastek materialized its first win for Elixir in the distribution & management area in the US. In Asia, the company won its first deal for Elixir Asia Individual Life and Group Life Projects for an insurer based in Thailand. The Company is witnessing a revival in UK geography and would be working on adding new partnerships and direct clients there. The US operations revenues for the quarter were up 1% sequentially at Rs 80.04 crore. UK operations contributed 52.2% against 51.8% in sequential quarter up by 2% at Rs 99.68 crore. In the industry verticals, Insurance dipped 0.1% contributing 32.1%, Government revenues dipped 3.8% sequentially contributing 28.8%, Other Financial Services grew 11.4% contributing 22% and IT & others dipped 2.1% contributing 17.1% of the operating revenues. In the service offerings, revenues from Development increased 13.2% sequentially at Rs 117.37 crore, Maintenance dipped 14.8% at Rs 69.89 crore and BPO decreased 1.9% at Rs 3.63 crore.

Mastek added 5 new clients against 3 in the sequential quarter, taking the total active clients to 90 from 88 clients in the sequential quarter. The top 5 clients' contribution was down to 54% from 58% in sequential quarter and Top 10 clients' contribute was down to 69% from 71% in sequential quarter. The company reduced net 230 employees with the headcount at 3363 employees at the end of the quarter. Fixed Price contracts contributed 48.9% up from 45.3% in the sequential quarter, Time & Material contributed 49.2% down from 52.8% in sequential quarter and BPO contributed 1.9%. The management expects T&M share of revenues to increase going forward.

REVENUE BY REGIONS	Q2FY10	Q1FY09	Q2FY09
North America	42%	42%	34%
Europe	52%	52%	61%
Others	6%	6%	5%
Total	100%	100%	100%
REVENUE BY OFFERINGS	Q2FY10	Q1FY09	Q2FY09
Development	61%	55%	65%
Maintenance	37%	43%	34%
Processing (BPO / PAAS)	2%	2%	1%
Total	100%	100%	100%
PROJECTS REVENUE BY TYPE	Q2FY10	Q1FY09	Q2FY09
Fixed Price	49%	45%	52%
Time & Material	49%	53%	47%
Processing (BPO / PAAS)/Transaction based Revenues	2%	2%	1%
Total	100%	100%	100%
REVENUE BY INDUSTRY	Q2FY10	Q1FY09	Q2FY09
Insurance	32%	32%	27%
Government	29%	30%	39%
Other Financial Services	22%	20%	16%
IT & Other services	17%	18%	18%
Total	100%	100%	100%

Result summary and comments Q2FY10 (Consolidated)

in Rs crore	Q2 FY10	Q2FY09	Gr yoy (%)	Q1 FY10	Gr qoq (%)	Comments
Revenue	190.90	251.08	-24.0%	189.42	0.8%	Delay in ramp ups
Other Income	2.33	5.12	-54.5%	2.02	15.3%	
Total Income	193.23	256.20	-24.6%	191.44	0.9%	
Staff Costs	119.53	148.18	-19.3%	115.90	3.1%	
<i>As a % of sales</i>	62.6%	59.0%		61.2%		
Travelling & conveyance	10.30	11.51	-10.5%	9.20	12.0%	
Exchange Loss / (gain)	1.47	11.73	-87.5%	0.14	950.0%	
Other Expenses	36.38	41.54	-12.4%	34.90	4.2%	
Total Expenditure	167.68	212.96	-21.3%	160.14	4.7%	
EBIDTA	25.55	43.24	-40.9%	31.30	-18.4%	
Interest	0.85	1.29	-34.1%	0.99	-14.1%	
Gross Profit after Interest	24.70	41.95	-41.1%	30.31	-18.5%	
Depreciation and amortisation	6.64	7.74	-14.2%	7.05	-5.8%	
Profit Before Tax	18.06	34.21	-47.2%	23.26	-22.4%	
Provision for taxation - Current Tax	3.68	9.71		3.94		
- Deferred Tax	(0.78)	(2.36)		(6.00)		
- Previous period	(8.38)	(4.57)		(1.09)		
- Net	(5.48)	2.88		(3.15)		
Net profit after Tax	23.54	31.33	-24.9%	26.41	-10.9%	
EBIDTA Margin %	12.2%	15.2%		15.5%		
PBT Margin %	9.3%	13.4%		12.3%		
PAT Margin %	12.3%	12.5%		13.9%		

DBS Cholamandalam Securites Limited

Member: BSE, NSE, MSE

Regd. Office: Dare House, 2 (Old # 234) N.S.C. Bose Road, Chennai – 600 001.

Website : www.choladbsdirect.com

E-mail id - customercare@dbschola.murugappa.com

To open Trading Account **SMS CDWM TA** to 55050



LOCATION	BEM	PHONE NUMBERS	E-MAIL ID
AHMEDABAD	Mr.Mehul M Min	079 - 64500318/19	mehulmm@dbschola.murugappa.com
BANGALORE	Mr. Sajesh M	080- 41503340/41	sajeshm@dbschola.murugappa.com
CHANDIGARH	Mr. Krishna Kumar R M		krishnakumarm@dbschola.murugappa.com
CHENNAI	Mr. Vishal Arora	0172 - 26248051	vishalarora@dbschola.murugappa.com
CHENNAI	Mr. Baskaran S	044 - 26198919/16	baskarans@dbschola.murugappa.com
CHENNAI	Mr. M Sundaresan	044- 25307306	sundaresanm@dbschola.murugappa.com
COCHIN	Mr. Preethi Damiyan	0484- 3073859	preethid@dbschola.murugappa.com
COIMBATORE	Mr. Mohan V N	0422- 4292041	mohanvni@dbschola.murugappa.com
DELHI	Mr. Kunal Kaushish	011- 66134224/25	kunalkaushish@dbschola.murugappa.com
HYDERABAD	Mr. Anupum Periwal	040- 64550572/77	anupamp@dbschola.murugappa.com
HYDERABAD	Mr. Srinivasa Reddy D V	040- 23316567/68	srinivasardv@dbschola.murugappa.com
JAMSHEDPUR	Mr. Amit Kumar Mahto	0657 - 2320098/177	amitkumarm@dbschola.murugappa.com
KOLKATA	Mr. Kumar Gaurav	033- 44103638/3639	kumargaurav@dbschola.murugappa.com
KOLKATA	Mr.Subhrodeep Chatterjee		subhrodeepc@dbschola.murugappa.com
MUMBAI	Mr. Navneet Kedia	022- 66156591	navneetk@dbschola.murugappa.com
MUMBAI	Ms Shweta Shantaram Padhey	022- 66574000	shwetasp@dbschola.murugappa.com
MUMBAI	Ms. Sheetal Bheda	022 -22153610	sheetalbhedaa@dbschola.murugappa.com
PATNA	Mr.Sanjay Kumar	0612 - 2500008	sanjaykumarr@dbschola.murugappa.com
PUNE	Mr. Sujit Arvind Gaidhani	020 - 30264811/12	sujitag@dbschola.murugappa.com
RANCHI	Mr. Sanjiv Kumar	0651 - 6453496	sanjivkumar@dbschola.murugappa.com
REGIONAL EQUITY MANAGER			
CHENNAI	Mr. Lakshmanan T S P	9840019701	lakshmanantsp@dbschola.murugappa.com
EAST & WEST	Mr. Ananthanarayan	9930103070	anathanarayanj@dbschola.murugappa.com
NORTH	Mr. Ajay Kumar Minocha	9838074353	ajaykm@dbschola.murugappa.com
SOUTH	Mr. Shankar P V	9840494132	shankarpv@dbschola.murugappa.com
RESEARCH			
Mr. Sandip Raichura	Head of Equities	044-25307216	raichuraS@dbschola.murugappa.com
Mr. Radhakrishnan.R	Manager Research / Technicals	044-25307353	radhakrishnanR@dbschola.murugappa.com
Mr. Alagappan A	Financial Services	044-25307363	alagappana@choladbs.murugappa.com
Mr. Balajee Tirupati	Infrastructure	044-25307364	balajee@dbschola.murugappa.com
Mr. Kumar Rahul Chauhan	Sugar, Capital Goods	044-25307364	kumarrc@dbschola.murugappa.com
Mr. Rohith Thomas Mathew	Metals, Mining, Cement	044-25307363	rohithm@dbschola.murugappa.com
Mr. Ramasubramaniam P	Telecom, Capital Goods	044-25307360	ramasubramaniamP@dbschola.murugappa.com
Ms. Sheetal Aggarwal	Information Technology	044-25307365	sheetala@dbschola.murugappa.com
Mr. Sathyajith N	Mutal Fund Analyst	044-25307225	sathyajithn@dbschola.murugappa.com
COMPLIANCE			
Mr Guruswamy Raj	Manager-Compliance		guruswamyrg@dbschola.murugappa.com

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STOCK RATING: Outperformer: > 20% upside over the next 12 months; Marketperformer: trade within a +/-20% range over the next 12 months; Underperformer: > 20% downside over the next 12 months.