

Tech Mahindra - Hold

Investment overview

- Tech Mahindra is India's fifth largest software exporter, owned by diversified group Mahindra & Mahindra.
- In the Telecom sector which contributes 48 percent of its revenues, Tech Mahindra has a niche and proven domain expertise.
- The company is likely to see benefits of the currency's fall in the next two quarters.
- The company is witnessing good growth led by manufacturing, which is its second largest vertical after telecom and has been able to reduce its debts considerably.

Business Overview

Tech Mahindra, a part of the Mahindra Group is a leading provider of solutions and services to the telecommunications industry. Tech Mahindra serves telecom service providers, equipment manufacturers, software vendors and systems integrators worldwide and their proven delivery models, distinctive IT skills and decades of domain expertise enable clients to maximize returns on their IT investment.

Tech Mahindra's Development centers are ISO 9001:2008, ISO 27001:2005, ISO 20001:2005, BS 25999-2: 2007 certified. Tech Mahindra has principal offices in the UK, United States, Germany, UAE, Egypt, Singapore, India, Thailand, Taiwan, Malaysia, Philippines, Canada and Australia.

Tech Mahindra has successfully implemented more than 18 Greenfield Operations globally and has over 151 active customer engagements mostly in the Telecom sector. The company has been involved in about 9 transformation programs of incumbent telecom operators.

In the Telecom sector, Tech Mahindra has a niche and proven domain expertise, distinctive IT skills, research and development, innovative delivery models and approach to offshoring. Company's solutions enable clients to maximize returns on IT investment by achieving faster time to market, reduced total cost of ownership resulting into high levels of customer satisfaction. Tech Mahindra's achievements have been recognized by various industry analysts, forums and clients - winning several prestigious awards and accolades. Tech Mahindra has a global footprint through operations in more than 31 countries with 17 sales offices and 15 delivery centers.

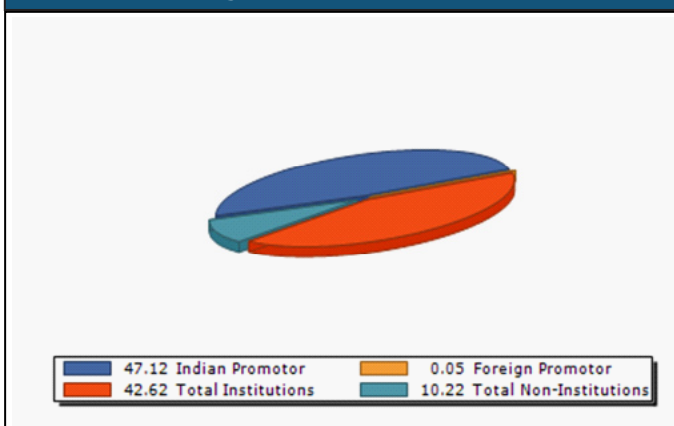
Financial Health

Tech Mahindra reported over three and a half fold jump in its net profit after tax at Rs 598.87 crore for the first quarter ended June 30, 2013 as compared to Rs 167.50 crore for the same quarter in the previous year. Total income from operation of the company increased by 137.65% at Rs 3552.88 crore for quarter under review as compared to Rs 1495.00 crore for the quarter ended June 30, 2012.

On the consolidated basis the company reported a rise of 27% in its PAT to Rs 686 crore compared to Rs 540.5 crore in the same quarter last year, while the operating profit was up by 16.9% to Rs 864 crore, while the Revenue increased by 21.4% to Rs 4103 crore for the quarter ended June 30, 2013.

Stock Data	15/10/2013
Current Mkt Price (Rs)	1583.15
52 Week High	1594.00
52 Week Low	865.25
Mkt Cap (Rs. in Cr)	36796.30
Return in last one Month (%)	23.08

Share Holding



Performance in last one year



Y-o-Y Performance (Consolidated)

Particulars	(Rs. in Cr.)		
	Mar 2013	Mar 2012	Change(%)
Net Sales	6873.10	5489.70	25.20
Other Income	46.20	111.40	-58.53
Total Expenditure	5569.80	4584.70	21.49
Operating Profit	1349.50	1016.40	32.77
Interest	103.00	102.60	0.39
Profits After Tax	811.00	542.10	49.60
Reserve & Surplus	5205.40	3875.30	34.32
Reported EPS(Rs)	100.53	85.92	17.00
Core EBITDA Margin (%)	18.96	16.49	15.02

Company's industry wise revenue witnessed a good surge in Telecom for the first quarter to 48% from 44% in same quarter last year, while Technology, media & entertainment declined to 12% from 13%, banking, financial services and insurance declined to 9% from 11%. On the other hand manufacturing and Retail, transport & logistics remained the same at 12% and 6% respectively.

Industry Scenario

The Indian IT industry is broadly divided into IT (software and hardware) and BPO services. India has laid firm foot and has emerged as a strong player in the global market. India accounts for 55% of global IT-BPO services. The Indian companies' ability to provide quality IT-BPO services at low-cost attracts consumers across the globe. India is now one of the biggest IT capitals in the modern world.

The past few years have witnessed a noticeable shift in the Indian software product business ecosystem which has helped in creating an enabling environment for the growth of Indian software products. These include acceleration in software product business activity in the country, improvements in the knowhow and support ecosystem and innovations in software product technology, delivery/business models, and changes in the Indian economy, helping catalyze the development of the domestic market for software products. Increasing IT adoption in India has also helped in creating a sizeable product business market opportunity locally.

Over the years, Indian IT service offerings have evolved from application development and maintenance, to emerge as full service players providing testing services, infrastructure services, consulting and system integration. The coming of a new decade heralds a strategic shift for IT services organisations, from a 'one factory, one customer' model to a 'one factory, all customers' model. Central to this strategy is the growing customer acceptance of Cloud-based solutions which offer best in class services at reduced capital expenditure levels.

IT-BPO sector has become one of the most significant growth catalysts for the Indian economy. In addition to fuelling India's economy, this industry is also positively influencing the lives of its people. IT industry has seen growth by around 16% in the current fiscal; however, issues hovering around the global and domestic economy are posing a hindrance in its further upmove. Indian IT firms could be looking at Europe as the next frontier for expanding business but proposed changes in the European data protection rules could make it tougher for them to expand as fast as they would want. On the positive side, the global enterprise mobility (EM) market opportunity is expected to be \$140 billion by the year 2020, growing at a compounded annual growth rate of 15%. The existing spend by enterprises on mobility is also expected to grow to 10-12% of the total IT spend by 2020, compared to less than 5% at present.

Investment Rationale

- Tech Mahindra's consolidated net profit increased by 27 percent, while the revenue was up 22 percent in the first quarter. The company's debt declined by Rs 413 crore during the quarter to Rs 747 crore. Though, the numbers of this quarter represent the combined entity of

Q-o-Q Performance (Consolidated)

(Rs. in Cr.)			
Particulars	Jun 2013	Jun 2012	Change(%)
Net Sales	4103.23	1543.42	165.85
Expenditure	3247.85	1241.91	161.52
Other Income	207.3	6.86	2921.87
EBITDA	1062.68	308.37	244.61
Interest	13.20	19.50	-32.31
Net Profit	699.27	188.27	271.42
EBITDA Margin (%)	25.90	19.98	29.62
NPM (%)	17.04	12.20	39.71
EPS	53.30	26.54	100.83

Profit & Loss (Consolidated)

(Rs. in Cr.)			
Particulars	Mar 2013	Mar 2012	Change(%)
Net Sales	6873.10	5489.70	25.20
Total Income	6919.30	5601.10	23.53
Total Expenditure	5569.80	4584.70	21.49
Operating Profit	1349.50	1016.40	32.77
Profits After Tax	811.00	542.10	49.60

Balance Sheet (Consolidated)

(Rs. in Cr.)			
Particulars	Mar 2013	Mar 2012	Change(%)
Share Capital	128.10	127.50	0.47
Reserve & Surplus	5205.40	3875.30	34.32
Total Liabilities	8833.20	6835.50	29.23
Investments	4098.70	3587.60	14.25
Current Liabilities	672.15	233.55	187.80
Net Current Assets	373.10	554.10	-32.67
Total Assests	8833.20	6835.50	29.23

Key Ratios (Consolidated)

Particulars	Mar 2013	Mar 2012
Reported EPS (Rs)	100.53	85.92
Core EBITDA Margin (%)	18.96	16.49
EBIT Margin (%)	16.72	14.34
ROA (%)	10.35	8.45
ROE (%)	17.37	14.76
ROCE (%)	19.18	16.15
Price/Book (x)	2.54	2.29
Net Sales Growth (%)	25.20	6.80
EBIT Growth (%)	46.02	-20.38
PAT Growth (%)	49.60	-27.31
Total Debt/Mcap (%)	0.10	0.12

Peer group comparison (Rs. crore) (Standalone)

*latest based on last traded price

Company	Year End	Net Sales	PBDIT	PAT	PATM%	EPS	P/E*
Tech Mahindra	201303	6001.90	1047.20	652.50	10.87	50.94	33.90
TCS	201303	48426.14	14306.27	12786.34	26.40	65.23	32.80
Infosys	201303	36765.00	11016.00	9116.00	24.80	158.82	21.00
Wipro	201303	33226.50	6933.50	5650.20	17.01	22.94	21.00

Tech Mahindra and Mahindra Satyam. In June 2013, Tech Mahindra had announced the completion of the merger of Mahindra Satyam to create the country's fifth largest IT company. The company witnessed good growth led by manufacturing, which is its second largest vertical after telecom, at 5.7% growth quarter-on-quarter. Media and entertainment too reported good growth of 8.7%, while retail grew over 6%. Telecom, despite of the accounts not growing significantly, saw q-o-q growth of 2.5%. During the quarter, the company launched a new branch in Istanbul, Turkey and was having 567 active clients at the end of the quarter.

- Tech Mahindra is witnessing strong demand for IT & Engineering solutions in China, driven by local enterprises upgrading productivity through technology and international retail brands seeking solutions to tap the fast-growing domestic consumer market. The company is helping Chinese automakers in designing smarter, more connected future cars, which include electronic power steering, human machine interface and infotainment, while helping the car makers attain quality certification. Not only this, the company is witnessing significantly higher demand from international retail brands seeking to penetrate or enlarge their market presence in China. Tech Mahindra's business activity in China in the financial year ended March 2013 grew approximately 50% year-on-year, more than twice the rate of global growth rate for the Company. Of the total, engineering sector accounts for 65% of Tech Mahindra's revenue in China. Keeping all these development in view, the company has been adding 70 associates every quarter for its China operations and is on track to triple the total headcount to 1,500 by 2015.
- Tech Mahindra has inked an outsourcing contract for Application Maintenance and Development with Volvo Cars. The company has been chosen as a strategic partner for the purpose by the Volvo Car Corporation (Volvo Cars). This partnership will provide Volvo Cars with a service to maintain and develop a wide range of applications across the business and to develop and implement new applications as part of its drive to increase efficiency and reduce costs. The contract which commences from September 2013 will provide Volvo Cars with Application maintenance and development across multiple domains, including Manufacturing, Product Development, Marketing, Sales and Reporting.

The company has also set up its first European testing laboratory in Sweden to provide solutions to device manufacturers. The deal which is estimated about \$40 million will help Tech Mahindra increase its contribution to Volvo Cars and further develop its business in the region.

- Tech Mahindra, a specialist provider of connected solutions to the connected world, is reportedly planning to invest around Rs 1,000 crore over the next 3 years to expand its infrastructure capacity and increase its delivery capabilities. This expansion plan is not only for big cities like Mumbai and Chennai but also for tier 2 and tier 3 cities. Further, the company has entered into a global partnership with ThingWorx. This partnership will enable Tech Mahindra to deliver innovative Machine-to-Machine (M2M) solutions at minimized cost, risk, and time to market for its customers worldwide by utilizing the ThingWorx Platform. The development advantage offered by ThingWorx will enable the company to deliver innovative applications that are much richer in functionality, in a fraction of the time required with alternate approaches.
- At the CMP of Rs 1,583.15, Tech Mahindra is trading at the consolidated TTM P/E of 22.50x and EV/EBIDTA of 18.00x, we would recommend a 'HOLD' in the scrip and buying at dips with a price target of Rs 1650.00. The stock has been on a gaining spree, supported by favourable environment of rupee depreciation and the rise in FII limit to 35 percent. Tech Mahindra is aiming to become the top three IT companies of the country by 2021 from its present fifth position. The inorganic growth strategy of the company has now started paying reward and Mahindra Satyam's business has been growing well with improvement in profit margins. Over the last few years, the company has been successful in scaling up its Non-BT revenues. This has not only helped it offset the decline in BT revenues but also post an overall growth for the company. The company is expected to perform well not only in the Q2, which is traditionally a strong quarter for the IT sector but quarters to come of the fiscal, as there has been better than expected recovery in US and Europe, while the company is hoping to do well in video services, mobility, cloud and security segment on huge uptick in demand. While the company will also see benefits of the currency's fall in the next two quarters.

Disclaimer : This document has been prepared by FRR GROUP and Accord Fintech Pvt. Ltd. and is being distributed in India by FRR GROUP, a registered broker dealer. This information in the document has been compiled by the research department. Due care has been taken in preparing the above document. However, this document is not, and should not be construed, as an offer to sell or solicitation to buy any securities. Any act of buying, selling or otherwise dealing in any securities referred to in this document shall be at investor's sole risk and responsibility. This document may not be reproduced, distributed or published, in whole or in part, without prior permission from the company.

© Copyright - 2013 - Accord Fintech Pvt. Ltd. and FRR GROUP