Student Electronic Assignment Cover Sheet

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1. Report Objective

Objective of this report is to review financial performance of Wipro Ltd, analyze it with its competitor Infosys Technologies Ltd by estimating its worth of 10% market capital and prepare recommendation for Board of Directors whether to invest in buying 10% of competitor’s shares.

2. Wipro Ltd

2.1. Introducing Wipro

Azim Premji founded Wipro in 1945 in India as from Western India Vegetable Product Ltd. In 1981, Wipro entered into technical domain by producing and selling computer hardware in India. Some notable achievements in company’s history-

- Joint venture with GE in 1989
- Achieved CMM Level 5 in 1998
- Listed on NY Stock Exchange in 2000
- In 2002, made entry in BPO business

Today Wipro is known as one of top 5 IT companies in India by revenue as well as headcount. In fiscal year 2014-15, IT services revenue of the company was $6.6 billion. Pot of this total revenue, 49.8% was from America, 29.4% was from Europe, Asia-pacific & other countries was 12.2 while remaining 8.6% came from Middle-East & Indian market. Employee strength of the company is around 160,000 employees.

Company provides IT and IT-enabled services as well as products. These services include system integration, software development and maintenance, project consulting, mobility and analytics services etc. Company has many development centers spread across the globe e.g. USA, Europe, Australia, China etc. Apart from this, company also has offshore development centers in major cities in India like Bangalore, Chennai, Hyderabad, Pune etc.

Wipro’s market capital as on 2015 is $30.19 billion. It has average outstanding shares - 2,462,579,161.

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1 [Wipro.com - About]
2 [InfotechLead, 2014]
3 [Reuters.com, 2015 – Wipro Profile]
2.2. Financial Performance

2.2.1. How Wipro performed in last 5 years

Wipro’s 51% IT services revenues come from US market so currency exchange rate between US Dollar and Indian Rupees has major impact on its revenues. 4

In last 5 years, there have been ups and downs in Wipro’s revenue. Revenue in Rupees has always shown upward trend in last 5 years while Dollar revenue had gone up in 2012 but went down substantially in 2013.

Since foreign currency exchange rates are always fluctuating, revenues in US$ have followed different pattern compared to revenue in Rupees which is evident in the graph below. Graph indicates revenue of $6.96 billion in financial year 2011. It grew by 4.88% to $7.3 billion and then slipped to worst figure $6.88 billion. It again rebounded to $7.51 billion in current year.

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5 (ComputerWeekly.com, 2015)
6 Revenue figures from (Revenue - Wikinvest.com, 2015)
7 Source - for key statistics and ratios, pls refer attached spreadsheet
8 Profit figures from (Net Income - Wikinvest.com, 2015)
3. Ratio Analysis

3.1. Profitability Ratios

Profitability ratios of a company are indicator of its capacity to generate profits by using assets or capital. It forms important part of company performance review by analysing it over few years. There are two major profitability ratios – gross profit and operating profit.

- **Gross Profit and Operating Profit Margin %**

![WIPRO Profit Margins for Last 5 Years](image)

In 2015, surprisingly gross profit ratio has gone down. Even though revenue has been up by 3.4%, cost of sales has been up 3.7% also due to increase in employee compensations in 2015 compared to 2014. Cost of sales has increased due to rise in sales & marketing and administrative expenses. Reasons for this rise are Rupee currency depreciation against US dollar, salary increments of employees after annual review. Apart from these factors, company’s overall profitability has also affected due to additional employees recruited, increase travel expenses etc.  

There are another set of profitability ratios. They help investors to understand how much profit company is generating as percentage of assets, sales and equity.

- **Return on Sales, Return on Assets and Return on Equity**

<table>
<thead>
<tr>
<th>Year</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Return on Sales</td>
<td>17.1</td>
<td>15</td>
<td>16.4</td>
<td>18</td>
<td>18.3</td>
</tr>
<tr>
<td>Return on Assets</td>
<td>14.29</td>
<td>12.91</td>
<td>13.58</td>
<td>15.78</td>
<td>15.33</td>
</tr>
<tr>
<td>Return on Equity</td>
<td>22.16</td>
<td>19.87</td>
<td>20.89</td>
<td>23.72</td>
<td>22.51</td>
</tr>
</tbody>
</table>

9 Source - for key statistics and ratios, pls refer attached spreadsheet
10 [Wipro Annual Report 2014-15 Page 31, 35]
Return on sales ratio in 2015 has gone up slightly due to rise in revenue and net profit. In local currency, the rise in revenue seems merely 8% over last year. But in US$ it is 14% due to fluctuations in exchange rate. Conversion from Rupee to US$ in 2015 has been done using exchange rate of $1 = ₹ 62.31 \textsuperscript{11} while 2014 calculations have been done using exchange rate $1 = ₹ 60 \textsuperscript{12}

Return on Assets ratio indicates efficiency of generating revenue using its assets. ROA ratio of the company had gone down significantly in 2012. In next two years it went up but again slipped in 2015 by 2%. Even though this is a minor decline, it indicates that company needs to improve its strategies of asset management to improve this ratio. Also this ratio is less than industry average of 17.62 \textsuperscript{13}

Company’s Return on Equity ratio has dropped in 2015 which indicates that company is not able to generate more profit using shareholder’s equities efficiently. This is because company’s equity has gone by 18% but net profit is up by 11% only. To improve this ratio, company can take following steps-
- Improve profit margin by generating more revenue
- Lower equities by giving more dividend
- Invest in research projects
- Buy shares back from owners which brings down shareholder’s equity
- Control cost of sale to improve profitability \textsuperscript{14}

3.2. Liquidity Ratios \textsuperscript{15}

Liquidity ratios indicate company’s ability to take care of short-term liabilities by using assets. Current ratio of a company is calculated by dividing total current assets by total current liabilities. Ideally this ratio should be a higher number since company can manage its short-term obligations.

\textsuperscript{11} [Wipro Annual Report 2014-15 Page 218]  
\textsuperscript{12} [Wipro Annual Report 2013-14 Page 190]  
\textsuperscript{13} [Reuters.com, 2015 – Wipro Financials]  
\textsuperscript{14} [Kokemuller, 2015]  
\textsuperscript{15} Source - for key statistics and ratios, pls refer attached spreadsheet
• Current and Quick Ratio

Both Current and Quick ratios have shown considerable decline in 2013 compared to 2012. It is due to increase in company’s current liabilities thus affecting its ability to take care of short-term obligations. This increase is primarily attributed to almost 72% increase in loans and borrowings and bank overdraft. In 2014, company was able to improve current liabilities slightly due to reduced loans & borrowings as well as increase in current assets. In 2015 current assets went up by 23% but at the same time current liabilities also rose by 20% causing current ratio improving marginally.

• Current Liability and Operating Cash Flow Ratio

Current liability coverage ratio for Wipro has been consistently low during last 5 years which indicates that company doesn’t have enough cash to fulfil its short term obligations. This is because of big increase in its current liabilities which has resulted due to jump in short term debts like loans & borrowings. Ideally this ratio should be greater than 1 means enough cash available to pay off entire current liabilities. To improve this ratio, company has to take measures to generate more cash using its assets efficiently and reduce short term debts.

16 [Wipro Annual Report 2012-13 Page 184]
17 [Wipro Annual Report 2013-14 Page 183]
18 [Wipro Annual Report 2014-15 Page 211]
19 [Wipro Annual Report 2014-15 Page 211]
3.3. Efficiency Ratios

- **Account Receivable and Payable Days**

Receivable days indicate efficiency of company in terms of average days needed to receive payments from customers. This ratio has gone up in 2015 indicating that company is not doing well in recovering money from customers. It is primarily due to increase in accounts receivables compared to 2014. To reduce this ratio, company can follow these steps –

- improve its collection policy
- change credit policy to reduce outstanding amounts
- offer discounts to customers to encourage timely payments
- disciplined follow-up in case late payments

On the other hand, payable days have been reduced in 2015 due to decrease in account payable and increase in cost of sales, indicating company’s ability to repay outstanding to creditors. The days also seem to be under 30, usually average period given by creditors.

- **Assets Turnover and Inventory Turnover Ratio**

<table>
<thead>
<tr>
<th>Year</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assets Turnover</td>
<td>0.84</td>
<td>0.86</td>
<td>0.83</td>
<td>0.88</td>
<td>0.83</td>
</tr>
<tr>
<td>Inventory Turnover</td>
<td>21.06</td>
<td>23.28</td>
<td>34.13</td>
<td>96.64</td>
<td>85.15</td>
</tr>
</tbody>
</table>

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20 Source - for key statistics and ratios, pls refer attached spreadsheet
21 [Wipro Annual Report 2014-15 Page 211]
22 [Myers, 2015]
In 2015, asset turnover ratio has gone down from 0.88 to 0.83 indicating that company is not able to increase revenue using its assets compared to 2014. Both revenue and total assets have gone up in 2015 but assets have increased by 14% while growth in revenue was merely 3.4% that resulted reducing this ratio. In order to improve this ratio, company’s revenue growth has to be similar or more than growth in assets. Similarly company can sell obsolete or unused assets to bring down assets value and make efficient use of available assets.

### 3.4. Gearing Ratios

- **Debt to Equity and Total Liabilities to Total Assets**

<table>
<thead>
<tr>
<th>Year</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt to Equity</td>
<td>0.55</td>
<td>0.53</td>
<td>0.54</td>
<td>0.46</td>
<td>0.47</td>
</tr>
<tr>
<td>Total Liabilities to Total Assets</td>
<td>0.35</td>
<td>0.34</td>
<td>0.35</td>
<td>0.31</td>
<td>0.32</td>
</tr>
</tbody>
</table>

Both Debt to Equity and Assets to Liabilities ratios in last two years have not changed much but there is slight increase in 2015 compared to 2014. D/E ratio has increased because the liabilities have risen by 16% while equity has gone up by 13%. In case of other ratio, assets have gone up by 14%. Since the ratio is quite low, company may likely have low risk factors which will help it to gain confidence of lenders. But despite this, company has to take appropriate steps to control its liabilities in future.

### 3.5. Investment Ratios

- **Earnings per Share**

<table>
<thead>
<tr>
<th>Year</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>EPS</td>
<td>0.49</td>
<td>0.44</td>
<td>0.5</td>
<td>0.53</td>
<td>0.56</td>
</tr>
<tr>
<td>P/E</td>
<td>24.9</td>
<td>18.5</td>
<td>28.5</td>
<td>21.0</td>
<td>22.2</td>
</tr>
</tbody>
</table>
EPS (Earning per Share) denotes company’s capacity to generate income that would be available for shareholders. A higher EPS amount means company has substantial income per share because then shareholder will get increased dividend. So this is always favoured by investors. Price Earnings ratio is comparison between market share price and EPS. This ratio helps investors to estimate how much they need to pay for buying stock compared to earnings.

In case of Wipro, EPS had gone downward in 2012 as like many Indian IT companies. But EPS in 2015 has risen marginally compared to 2014 in terms of US dollar due to exchange rate fluctuations. But company has generated more income in order to improve EPS in future. Similarly P/E ratio has also gone up this year due to rise in share price. This ratio is close to industry average value of 23.19

3.6. Trends

Graph below shows fluctuations in Wipro’s share price over last 5 years. It is evident that due to heavy dependency on IT industry in US market and unpredictable Dollar-to-Rupee exchange rate, stock prices have been up & down. Also balance sheet points out that company must control growth in total liabilities in order to increase net profit.

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23 [AmigoBulls, WIT 2015]
4. Have a look at the competitor – Infosys

4.1. About Infosys

Infosys is one of well-known IT and outsourcing companies in India similar to Wipro. It was founded by Narayan Murthy in 1981. It has around 180,000 employees with about 100 development centres spread across globe. It provides various IT services like strategic consulting, outsourcing, software development, cloud computing etc. to its clients.\(^{24}\)

Its market capital as of year 2015 is US$ 41.5 Billion. Its revenue is US$ 8.71 Billion and share price is US$18.16 as of on 1\(^\text{st}\) November 2015.\(^{25}\) Most of its revenues are from US markets which accounted for almost 60% while European market contributed quarter of total revenue.\(^{26}\)

4.2. Comparison with Wipro

After analysing revenue and net profit graphs below, it can be seen that initially Infosys revenue was less than Wipro during 2011 & 2012 and then took over Wipro in revenue next year. As far as net profit is concerned, Infosys has been consistently making more profit than Wipro. It indicates that Infosys has been successful in controlling its cost of sales & expenses to generate profit more than Wipro even with less revenue.

\(^{24}\) [Infosys.com, 2015 - About]  
\(^{25}\) [Morningstar.com, 2015 – Share Price]  
\(^{26}\) [Infosys.com, 2015 - Metrics]
5. Big question – to invest in Infosys or not

5.1. Quick Analysis
There are many strong points in case of Infosys as a company.
- It has now established a trusted brand in India
- Its leadership & management is much transparent
- It caters wide range of services

But one weak point about Infosys is that it relies too much on US markets. It’s also not a good player in domestic market in India. So it can view it as an opportunity. It also has huge cash reserves which it can utilize in new acquisitions. Due to its dependence on US market, it becomes vulnerable during any economic crisis there.  

Graph below explains general trends followed by shares of both companies during last 5 years. Year 2012 was particularly bad for both companies.

5.2. What’s the cost of 10% stake in Infosys?

To calculate stake in a company, use company’s current market capital amount. It can computed using formula - total outstanding shares * share price. As of financial year 2015, Infosys’s market capital is US$ 41.5 Billion. (Outstanding shares = 2.29 Billion)

- Total Book value of Wipro = $6.52 Billion
- Retained earnings of Wipro as of 2015 = $5.95 Billion
- 10% stake value of Infosys = $4.15 Billion
- Total Book value of Infosys = $8.74 Billion
- Total Shares outstanding = 2.29 Billion
- Book value per share of Infosys = $3.83
- Infosys market value of share as of 7th Nov 2015 = $17.90
- Infosys Price/Book ratio : 17.90/3.83 = 4.67

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27 [Kumar, 2014]
28 [Wikinvest.com, 2015 - Infosys]
29 [Wikinvest.com, 2015 - Infosys]
30 [Finance.yahoo.com, 2015 - Statistics]
If we look at current investment ratios of Infosys compared to industry average then they look favourable and sometimes are better or at par with industry ratio values.

- P/E ratio of IT Service industry in 2015 is 23.4 and that of Infosys is 20.5%.
- Dividend pay-out ratio of Infosys is 48% compared to 28% industry average.
- Profitability as well as efficiency ratios are also good during this year.
- Quick ratio of 3.72 is better compared to 2.80.
- Company’s average profit margin for last 5 years is better than attractive than industry average of 19.87.
- Last 5 years average ROI is 25.17 compared to 25.52.\(^{31}\)

But one thing to point about Infosys is its reduction of expenditure on R&D activities which is essential for an IT company. In 2015, the expenditure has reduced from 2% of total revenue in 2014 to 1.3%.\(^{32}\)

\(^{31}\) [Reuters.com, 2015 – Infosys Financials]
\(^{32}\) [Infosys.com, 2015 – Annual Report Page 54]
6. Recommendation

Infosys has been able to keep share prices going up unlike Wipro whose share price had dropped in 2014. Ideally price/book of a company whose stakes are to be purchase, should be one or less than one. As of now, price/book ratio of Infosys is 4.74 but IT companies usually do have higher P/B ratio due to majority of intangible assets. So at this value also, it might look as an attractive option to buy 10% stake in Infosys.

Apart from this, analysts are also predicting a good forecast for this company. According to industry experts, company is expected to perform well in coming years which will see growth in terms of revenue as well as stock price. They are also suggesting buying company shares although some are suggesting holding transaction for some time.

But investment decisions should be made carefully taking into account all other aspects of buying company as well. Even though Wipro has enough retained earnings for this deal, it will be left with barely $1.8 billion to sustain after spending almost 70% of total amount. Most of the companies need retained earnings for various reasons like funding new research projects, investing in new companies, expand company operations, construct new buildings/plants, purchase new assets, reduce liabilities etc. Similarly it takes time for any investment to produce results for buyer so Wipro also has to wait for few months or even years to get results from this deal.

Since Wipro’s liabilities have gone up by 16% in 2015, it would be risky to spend 70% of its earnings on single deal to buy 10% stakes. Its short term debt has been going up consistently since last few quarters and as of now, it is more than $1 billion. So it needs liquidity to meet its obligations that are due in less than a year. Also investors would like Wipro to use earnings to invest in assets that would generate more income. So best policy at this moment is – wait and watch for next few years.

Alternatively Wipro can look out for some different company that is making good profit and whose 10% stake won’t be too much compared to earnings. In case, Wipro needs to build immediate additional funds then it can opt for these techniques like borrowing from lenders, getting loan from banks, floating new shares in the market to generate capital from shareholders etc.

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33 [Chauhan, 2014]
34 [Wikinvest.com, 2015 – Wipro Short Term Debt]
7. Bibliography


