PINC RESEARCH

SECTOR REPORT

IT SERVICES

Pangs of Globalisation

Contents

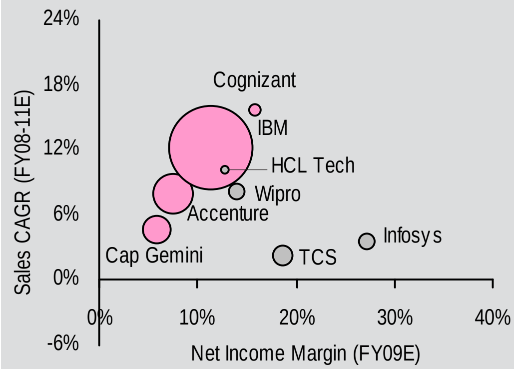
01 April 2009

Introduction

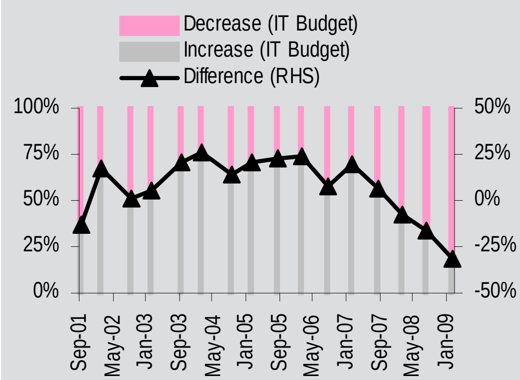
We initiate coverage on Indian IT services sector with a Negative view. We believe that the macro-economic factors will continue to impede Indian IT Services industry. The industry is experiencing multiple headwinds along with the slowdown that will play out in terms of reduced growth rates, pricing pressures, project cancellations, delays or no orders and return of economic nationalism resulting in sluggish top-line growth. We initiate coverage on Infosys (Sell), TCS (Sell), Wipro (Hold), and HCL (Hold) rating.

- **Global macro-economic headwinds: BFSI, Telecom and Retail the worst affected**: The current macro-economic outlook appears bleak in the near term. GDP of the US and Europe, which contributes about 85% of revenue for top 4 Indian IT comapanies, is expected to de-grow. BFSI, Telecom and Retail that contributes 65% of revenue for top 4, are suffering because of declining consumer confidence, write-offs and bankruptcies. M&A has further decreased the size of the pie.
- **Globalization of global delivery model:** Large global peers like IBM, HP-EDS, and Accenture have managed to grow at a faster pace in India than the top 4 Indian IT companies. Global players have steadily improved their margins over the last 3 years. Tier-1 Indian IT companies are also facing pricing pressure due to competition from the Tier 2 Indian IT companies.
- **Pyramid effect not geared for decelerated growth**: We believe that with little visibility of volume growth and gloomy macro-economic condition, and in declining attrition scenario, the ability to maintain the pyramid base would be difficult. Any decline in hiring would increase the average age and accelerated hiring would put pressure on utilization ratio and margins.
- **STPI benefit to end in FY10, slower volume growth could increase tax rate further in FY11:** End of tax holiday will have dampening effect on bottom-line of Indian IT companies. According to us, slower volume growth than expected could increase effective tax rate higher than anticipated in FY11. We are factoring in the number of new business moving to SEZ, but as the volume of new business dries up the companies' effective tax rate could be higher than anticipated.

Global peers eyeing stronger growth



CTO surveys forecast: Indicates sanguine demand



Shashi Bhusan
shashi.bhusan@pinc.co.in
Tel: +91-22-6618 6372

Karan Taurani
karan.taurani@pinc.co.in
Tel: +91-22-6618 6382

Jaikishan Kaurani
jaikishan.kaurani@pinc.co.in
Tel: +91-22-6618 6332

Sector Summary

KEY FINANCIALS

Company	CMP (Rs)	Mkt Cap (Rs bn)	Net sales (Rs mn)		EPS (Rs)		P/E (x)		TP (Rs)	Potential upside (%)
			FY10E	FY11E	FY10E	FY11E	FY10E	FY11E		
Infosys	1374.0	786.9	222,930	240,250	104.5	107.5	12.7	12.3	1050	(24%)
TCS	545.0	532.8	286,570	306,040	51.6	53.1	10.5	10.2	460	(15%)
Wipro	252.0	369.4	264,912	293,103	24.7	24.6	9.9	9.9	225	(10%)
HCL Tech	101.0	67.4	113,810	124,145	16.6	17.4	6.1	5.8	100	(1%)

INDUSTRY OVERVIEW

Initiate coverage on IT Services with a Negative view...

We initiate coverage on Indian IT Services sectpr with a Negative view. We believe that demand of IT services will remain under pressure due to unfolding of various macroeconomic events around the globe. The industry is exposed to multiple headwinds along with the slowdown that will play out in terms of reduced growth rates, pricing pressures, cancellations, delays or no contracts and return of economic nationalism resulting in gradual top-line growth. We expect currency depreciation to provide some relief but end of STPI in FY10, declining utilization ratio and shift in offshore-onshore mix will have negative impact on the both top-line and bottom-line of the companies. We initiate coverage on Infosys and TCS with a Sell rating and Wipro and HCL Tech with a Hold rating.

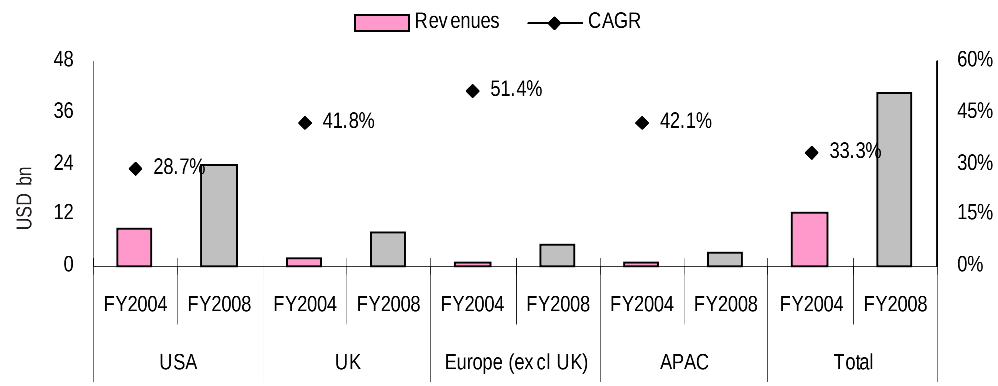
MACRO BLUES: PROTRACTED NEGATIVE IMPACT

GDP of G7 to contract in FY09, putting hold on IT spend...

Indian IT Services companies' biggest markets the US, the UK and Continental Europe are going through the worst financial turmoil. Economic growth for G7 nations, which had witnessed a surge in GDP growth post tech bubble bust, saw a sharp decline in 2008 and the situation is expected to worsen in 2009. According to IMF, recovery is not expected before CY2011. The economic downturn has put discretionary IT spending on hold.

A closer look at the customer profile of the Indian IT sector explains why the industry is in trouble. The U.S. accounts for 58% of the market and the UK another 19%. This is not too different from the respective values of 68.2% and 14.5% in financial year 2003-04. The growth for Indian IT companies has come from the US and Europe which grew at a CAGR of 29% and 46% respectively from FY04-08. But with the US and Europe in the grip of recession, we see the earning growth for the Indian IT companies at risk.

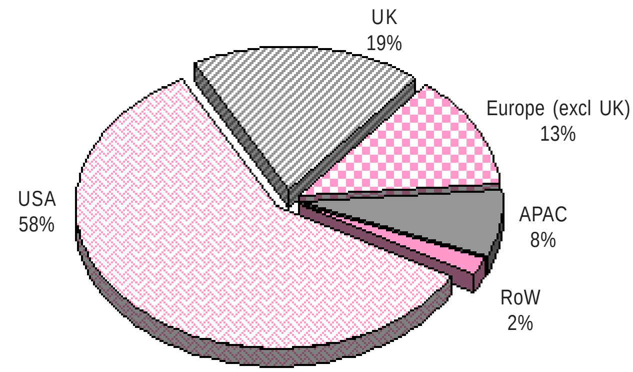
US continues to drive growth for Indian IT Services



Source: NASSCOM

Geographical breakup FY08

The US and the UK continue to dominate the pack...



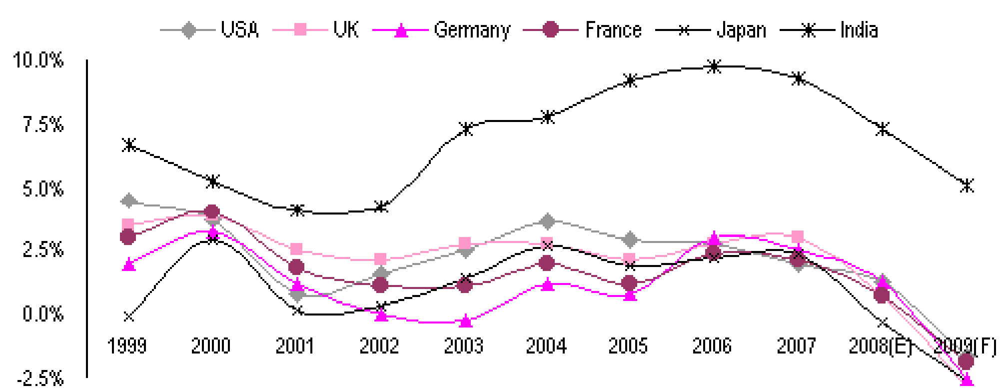
Source: NASSCOM

IMF forecasts global GDP to contract by 0.5% for the first time after WWII...

The deteriorating demand environment in the US and the UK economy will have a significant impact on the growth prospect of Indian IT services. According to IMF, GDP of the US and the UK will contract by 1.6% and 2.8% in 2009 whereas France and Germany will contract by 1.9% and 2.5% respectively. The US and the UK contribute about 2/3rd of revenue for the large four Indian IT services companies.

The aggregate figures don't tell the story of what is unraveling in individual countries. In the last quarter of 2008, U.S. GDP dropped by 6.2% at an annual rate, the U.K. by 5.9%, Germany by 8.2%, Japan by 12.7% and South Korea by 20.8%. The downturn could be much deeper than IMF forecast a month ago.

GDP growth rate: expected to be negative in CY09

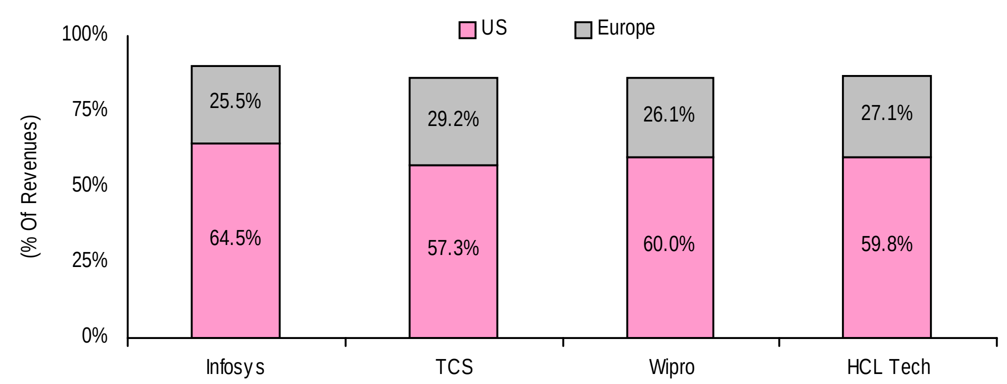


Source: IMF, PINC Research

Alarmingly high US and Europe exposure for Top 4 Indian IT companies...

Top 4 Indian IT companies derive a large chunk of revenues from US and Europe. Infosys is at the top of the list deriving 90% of revenue, TCS 87%, Wipro 86%, and HCL Tech 87% from US and Europe. IT spending of companies moves in-line with economic growth of a country. With the global economy contracting, we anticipate a decline in IT expenditure of the developed nations. IDC has already downgraded IT expenditure growth to 2.6% from earlier 5.9% in 2009, which could be further downgraded because of ever deteriorating demand environment in the global economy. In their worst case scenario analysis, they have forecasted a decline of 1-2% in IT spending in US and Europe. With a high dependence on US and Europe, we see protracted negative impact on earning of Indian IT companies.

Geographical Split: US and Europe contribute over 80% of revenues



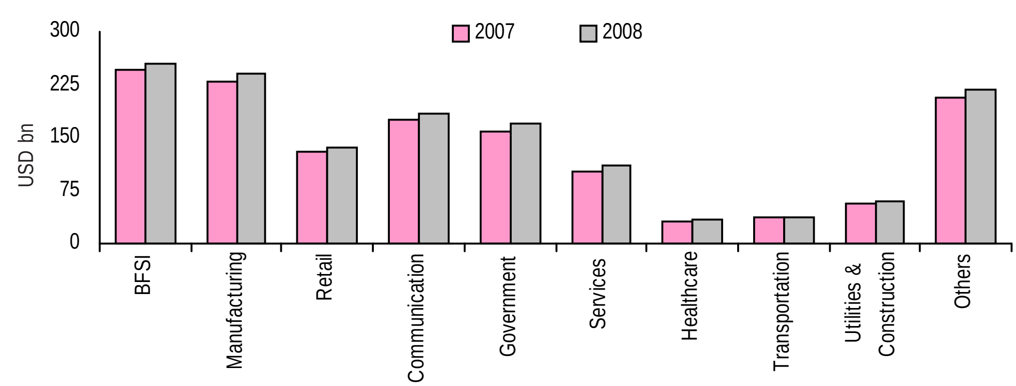
Source: PINC Research, Company reports (Q3FY09)

Macro-economic headwinds: Slowing IT spend by BFSI, Telecom, and Retail

BFSI, retail and telecom contribute about USD650bn of total IT Services revenue globally...

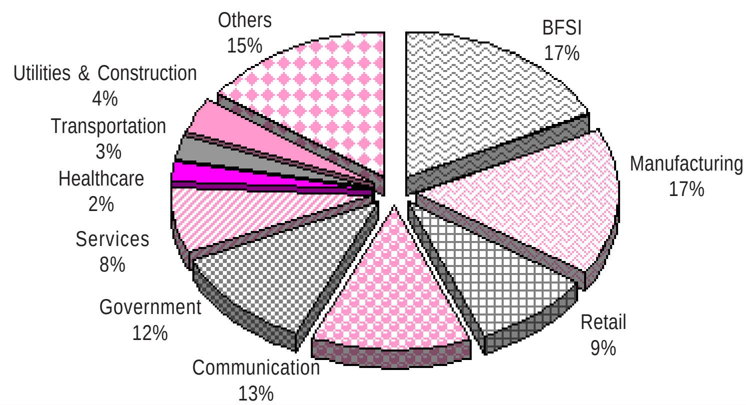
About 45-50% of the revenues for Indian IT outsourcing are tied to BFSI, retail and telecom. According to NASSCOM, BFSI, retail and telecommunication contributed about USD650bn of total IT Services revenue globally in 2008. These three verticals contributes high percentage of revenue for the Indian IT companies, retarding their growth due to a delay in IT budget decision and cancellation of IT projects in few cases.

BFSI, Retail and Telecom: major contributors for Indian IT Services



Source: NASSCOM, PINC Research

Vertical Split - FY08: BFSI, retail and telecom continue to reign



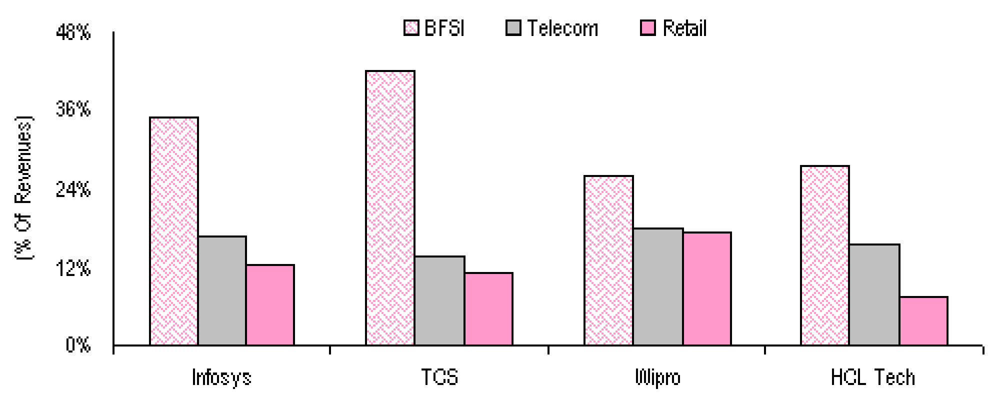
Source: NASSCOM

BFSI, retail and telecom contribute about 2/3rd of revenue for top 4 Indian IT players...

Under normal circumstances, growth from the other verticals would have sufficed to offset the revenue erosion by three verticals, which are the largest IT spender. But the problem is that other verticals are also impacted by the crisis, fading consumer demand and reduction in spend. Indian IT companies, which are largely dependent on these three verticals, are seeing budget ramp-down or deferment in IT projects in these verticals.

Top 4 Indian IT bellwethers derive higher revenue from BFSI, Telecom and Retail, with Infosys driving 64%, TCS 67%, Wipro 61% and HCL 51% from these verticals. The sudden decline in revenue from these three verticals has forced them to cocentrate on the other verticals.

Vertical Split : TCS has the highest and HCL has the lowest exposure



Source: Company Report (Q3FY09), PINC Research

Consumer confidence at its lowest ever...

US: Worst readings on record (1985=100)

Date	Reading
Feb-09	25.0
Jan-09	37.4
Dec-08	38.6
Oct-08	38.8
Dec-74	43.2
Feb-92	47.3
May-80	50.1
Jan-92	50.2
Jun-08	51.0
Jul-08	51.9
Dec-91	52.5
Nov-91	52.7
Oct-82	54.3

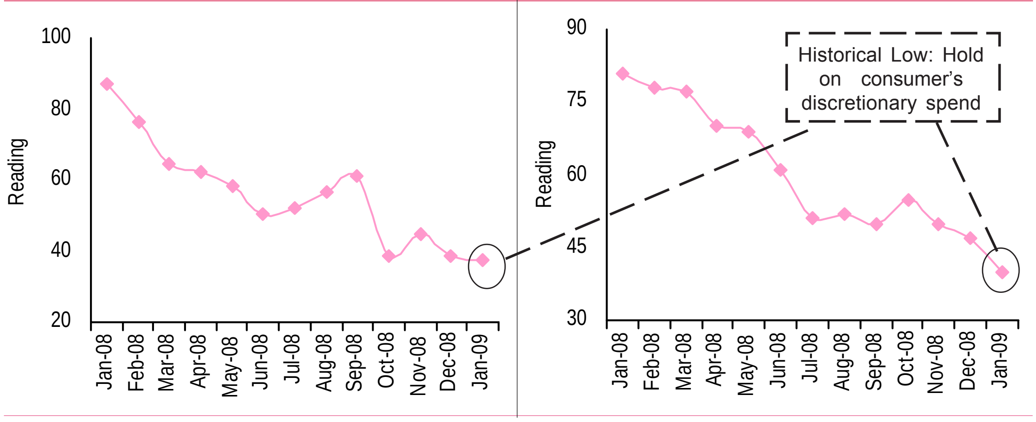
US: Biggest percentage drops

Date	Percentage
Oct-08	-38.1
Dec-73	-34.3
Oct-74	-29.5
Oct-90	-26.9
Apr-80	-25.1
Dec-74	-20.7
Feb-70	-19.3
Feb-03	-17.7
Oct-91	-17.6
May-80	-17.3

Our preliminary analysis of the financial health of companies from these verticals revealed that there is a deceleration in top line growth along with a significant erosion of their margins. The BFSI vertical has written down USD1293bn and raised USD1009bn out of which the US companies have written down USD812bn and raised USD571bn till Q1FY09, clearly indicating the magnitude of trouble they are going through.

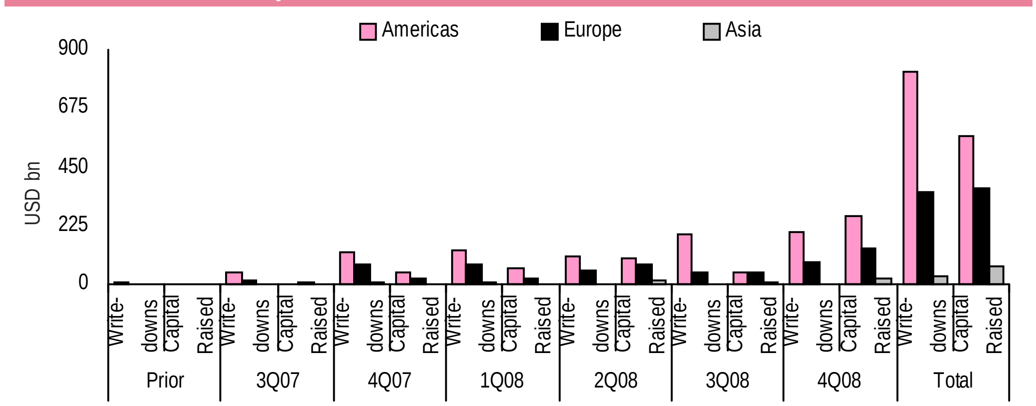
The demand in retail and telecom services vertical is driven by discretionary spend of the consumers. The surge in the number of jobless both in the US and the UK to a record high, has pushed the consumer confidence index to a new record low. The consumer confidence index is at 25, which is at all time low (index started in 1967). The short-term outlook of the consumers remains very pessimistic. The decline in the consumer confidence in October 2008 was the largest ever. According to us, the ability of retailers and telecom companies to spend in this deteriorating demand environment remains under doubt and it could further worsen if the confidence stays at this level for long or takes a further hit.

USA Consumer Confidence Index | **UK Consumer Confidence Index**



Source: The Conference Board Consumer Condfidence Survey, Nationwide Consumer Confidence Index

Writedowns vs Capital Raised: connote BFSI trouble



Source: Bloomberg, PINC Research

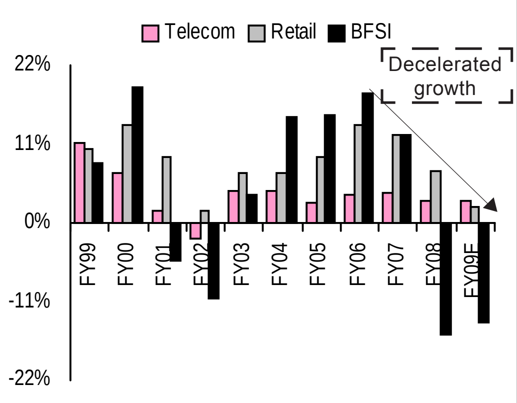
BFSI sector has written-down USD1.3trn and raised USD1.0trn...

S&P500: BFSI & retail revenues plunge and margins contract...

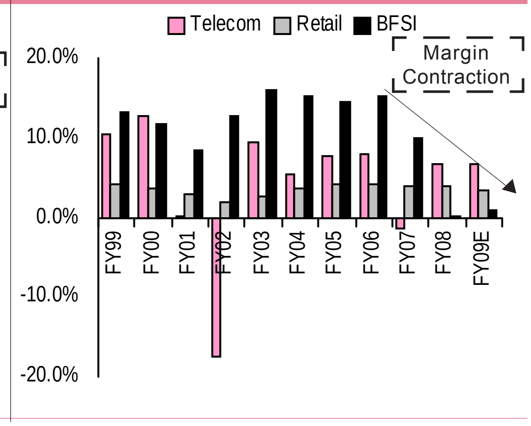
BFSI revenues have contracted by 15% in 2008 and are expected to contract by another 14% in 2009. Retail revenue growth has fallen from 13% in 2007 to 7% in 2008 and expected to further decline to 2.2% in 2009. Our analysis of S&P500 BFSI, Retail and Telecom led to the conclusion that the revenue growth has declined drastically in 2008 and according to Bloomberg 2009E estimates it is expected to be even worse.

Contracting margin of these verticals is a double whammy for these IT companies. BFSI sector has completely wiped out its net income and expected to touch positive at 1% in FY09.

Revenue Growth (S&P500) (YoY)



Net Inc. Margin (S&P 500)



Source: Bloomberg

While BFSI, which is the worst affected sector in the current credit-crisis, remains the biggest sector with over 41% of total revenues for Indian IT-BPO, verticals like Hi-tech/ Telecom and Retail remain exposed to the discretionary spend of end consumer, whose confidence is at all time low. We believe that the current drop in the income growth and declining net income margin will act as double edged sword to cut IT spend of these companies.

Declining revenue growth and contracting margins force outsourcers to delay or cancel IT projects...

The global economic slowdown is forcing retailers to delay or cancel IT projects that aren't mission critical, offer tangible cost savings or rapid ROI. These cutbacks are affecting hardware, software and services vendors. For vendors with little exposure to the retail vertical, these cuts don't matter much, but for vendors such as TCS, Wipro and Infosys, with significant retail exposure, it creates a negative impact.

Although telecom earnings remained steady at this level, the recent bankruptcy filling by Nortel could be a leading indicator of the worsening demand environment in telecom. We believe that OEM is the first to bear the burnt due to decline in hardware spend by telecom service provider followed by IT services vendors.

IT BUDGET CUT: WARNING SIGN FOR INDIAN IT SECTOR

Outsourcing demand slowed down drastically in H2CY08...

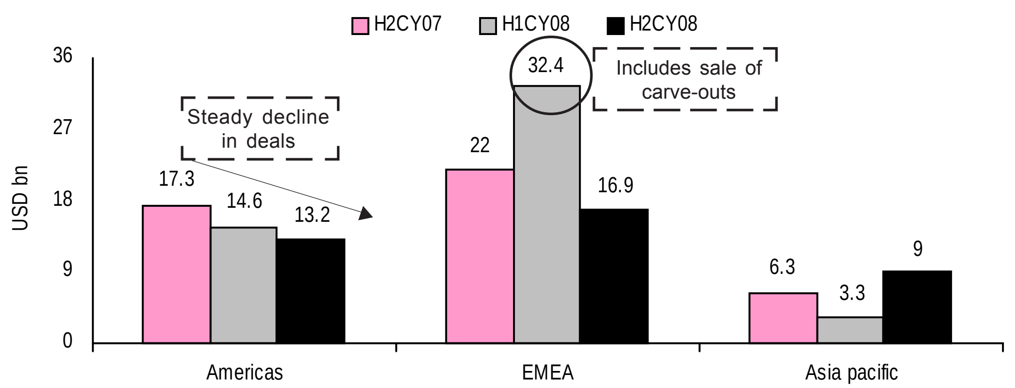
According to TPI, a sourcing advisory firm, outsourcing demand in H2CY08 slowed down drastically, although Q4CY08 saw slight improvement over Q3CY09. The weakness was primarily driven by a slowdown in mega deal activity. TPI expects that the continued economic weakness will certainly impact H1CY09 but it is still unclear if the TCV will decline sequentially.

The year 2009 is likely to see a number of smaller, more tactical contracts and associated multi-sourcing approach, with cost reduction being the primary driver. Further, TPI believes that a return to normal outsourcing activity and the resumption in mega-deals will signal that the economy is moving into growth mode.

Although 2008 was a strong year with global total contract value (TCV) growing by 5.6% YoY and global average contract value (ACV) growing by 9.5% YoY, the momentum slowed down drastically in the second half. In fact, the half over half drop in EMEA in H2CY08 was 48%, whereas US has seen steady decline over all contracts awarded in CY07, which declined by 31% from CY06. The US witnessed further decline in TCV in CY08 by 3% from CY07. Americas TCV has declined in last three half consistently.

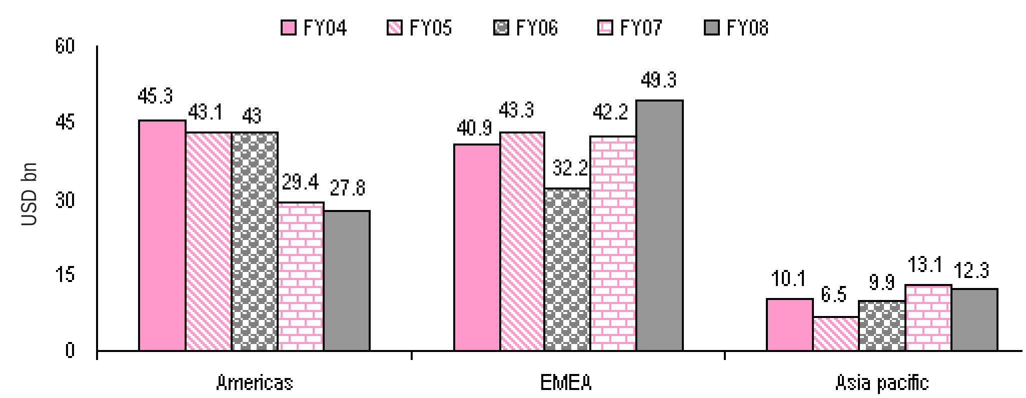
TCV from the US is declining steadily whereas EMEA witnessed a sudden drop in H2CY08...

Half-Year Comparison by TCV(USD bn): Europe witnessed a sharp dip



Source: TPI

Annual Comparison by TCV(USD bn): US declining steadily

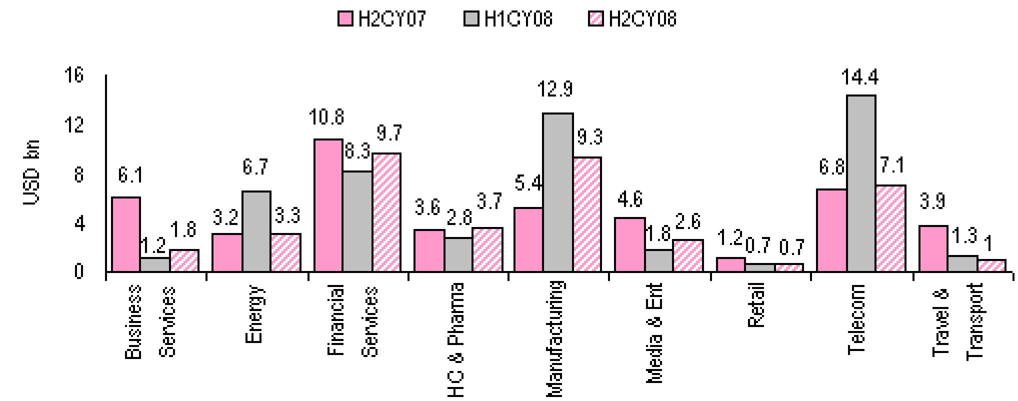


Source: TPI

Slowdown in BFSI is reflected in the TCV awarded...

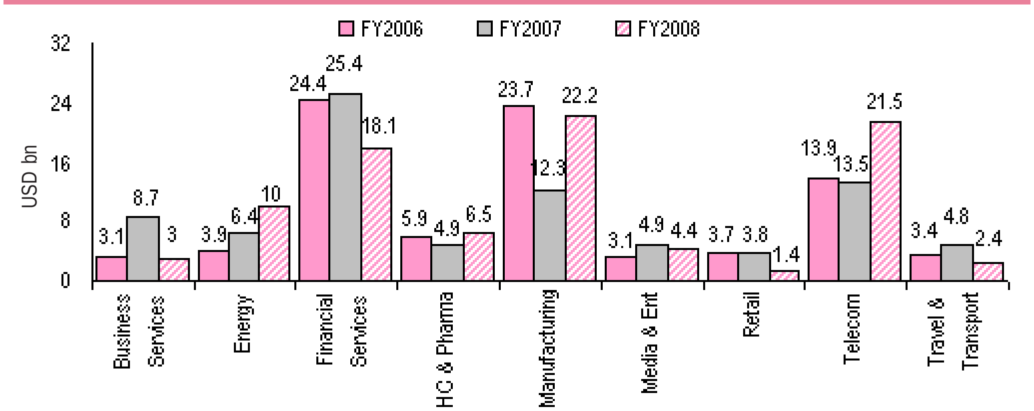
BFSI sector with a TCV of USD 18.1bn in 2008, witnessed a decline of 28.7% YoY, which happens to be its worst year since 2001. Interestingly, while global financial services TCV actually increased half over half in H2CY08, the divestiture of captive offshore operations accompanied by an outsourcing services agreement boosted financial services TCV, with EUR4.5bn in 2H TCV coming from divestitures of captives. TPI has signaled that a number of captive divestitures will take place in H1CY09. Telecom and Manufacturing TCV in H2CY08 declined by -50.7% and -27.9% respectively half over half.

TCV (USD bn) of Contracts Awarded Segment Comparison: 2H07-2H08



Source: *TPI*

TCV (USD bn) of Contracts Awarded Segment Comparison: Annually



Source: *TPI*

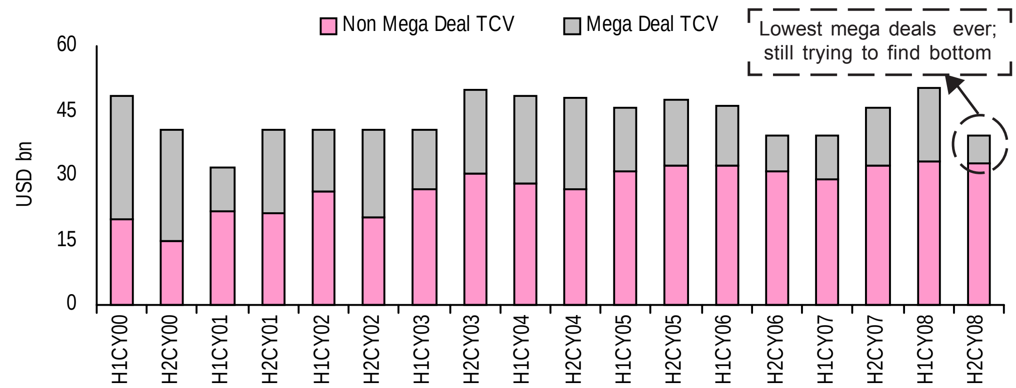
TCV witnessed 22% sequential drop in H2CY08, biggest fall in 10 years...

Global TCV in H2CY08 was USD 39.1bn, a sequential drop of 22%, the largest sequential fall in 10 years. It is worth pointing out that H1CY01 saw global TCV of just USD 31.9bn, a decline of 21% and similar to the current recession, the drop off was caused by slowdown in mega deal activity. Interestingly H1CY01 was preceded by an increase in TCV to USD 40.7bn in H2CY01 and followed by four steady halves of about USD40bn each in TCV. The global recession is still trying to find its bottom and a recovery like H2CY01 seems improbable.

According to TPI, these recession-associated low points represent a pause in strategic decision-making about outsourcing when companies take their time to assess the extent of the economic slowdown and prepare themselves for change.

Mega deals hit a new low, an indication of delay in strategic decision making...

H/H Comparison by TCV(USDbn) of Industrywide Contract Award Trends



Source: TPI

Contract size shrinks - A sign of lower spending: We believe that contract size has been reduced to USD 5-10mn this year, unlike the period of 2000-08 when the size of contracts were USD 15-100mn. The deals have been more tactical in nature. There are large deals, but they are moving slowly due to delay in decision making from clients. Over the past two quarters, customers have been in discussion with their service providers, asking them to help these companies cope with lower IT budgets.

Contract size is shrinking along with the decline in pricing, a sign of lower IT budgets and increase of tactical projects...

Forrester forecasted lower spend: According to Forrester, global purchases of IT goods and services by businesses and governments would decline by 3% in 2009 to USD 1.66 trillion. The 2009 drop measured in U.S. dollars is a distinct shift from 2008, when global IT purchases increased by 8%. The 2009 decline ends seven years of growth in global IT purchases; technology purchases fell by 6% in both 2001 and 2002. The forecast by Forrester is based on the assumption that the economic recession in the US and other major economies will start to end in the H2CY09. There is no growth market to offset the weak ones.

Pricing cut could affect the margin: Companies are willing to take a cut in billing rates in the short-term to preserve long-term relationships. First of all, clients want to spend less, which means many of the discretionary projects are expected to be discontinued. There is also pressure where clients would want to spend their money upfront and get the benefits later on, and clients expect IT companies to be doing some of that investment, along with them. *According to Gartner, prices of IT outsourcing services will shrink 5-20% through 2010 due to the uncertain economic climate, IT budget constraints and competition between vendors.*

Indian IT companies have the cushion to absorb ~5% pricing decline...

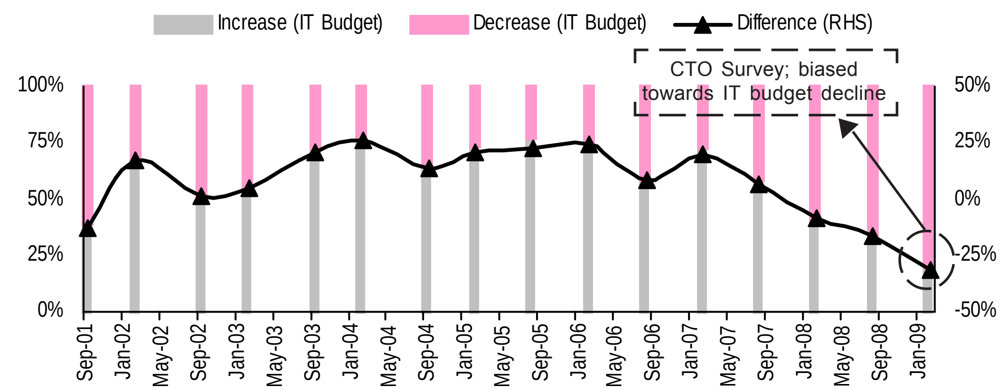
According to us, any pricing cut in the excess of 5% could affect the margin as they would stretch their cost control measure. The costs for clients can be brought down by higher off-shoring.

WEAK SENTIMENTS: IT BUDGET COULD HIT A NEW LOW

According to a survey conducted by ChangeWave for the expected IT spending in their organization, 41% of respondent said they are planning to decrease IT budgets or there will be no spending for the second quarter. Only 10% of respondents said that they are either increasing or keeping the IT budget same. The decline is the worst since 2001.

Negative sentiments to pull down IT spending...

CTO surveys forecast: indicates sanguine demand

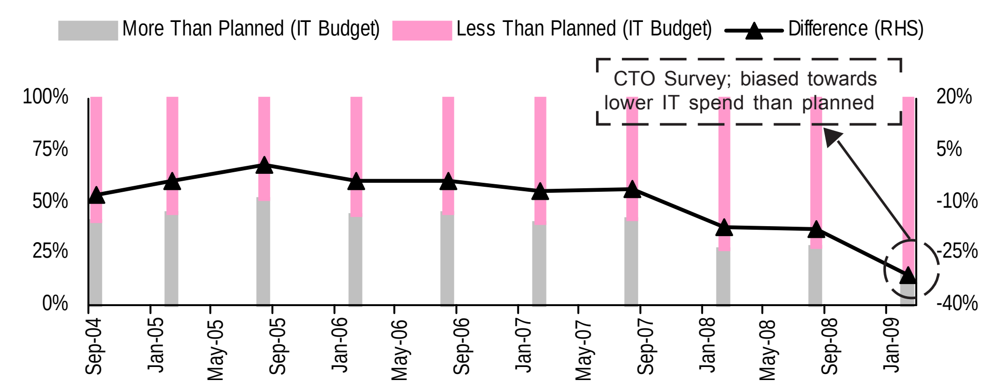


Source: Change Wave Research

In another survey by ChangeWave, they asked respondents if their IT spending was on track till the first quarter and the result was again very disappointing. About 38% of respondents spent less than planned and only 7% spend more than the planned expenditure.

Lower than budgeted spend expected to worsen the situation for IT service providers...

Survey signals judicious approach to IT spend



Source: Change Wave Research

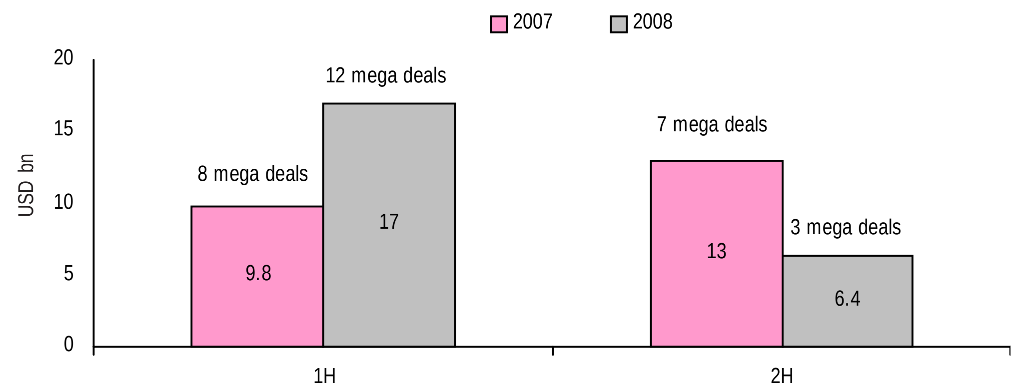
To summarize, there is not only significant decline in the IT budget but also companies are spending lower than budgeted IT expenditure. Both data points are the worst since 2001 when ChangeWave has started collecting data.

Slower momentum of mega deals: tapering the volume growth

Indian IT companies are seeing slowdown in getting new outsourcing contracts. Clients are very selective in the new projects. While the first half of H1CY08 saw 12 mega deals which include sales of carve outs, the H2CY08 was a complete wash-out for the mega deals and witnessed only 3 mega deals.

Slump in the mega deals is an indication of migration towards tactical projects...

Industrywide Contracts with TCV> USD 1bn

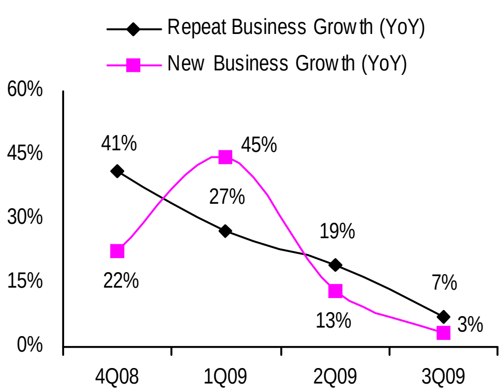


Source: TPI

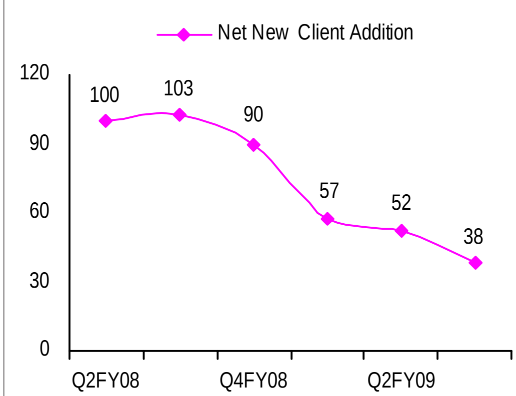
There are spates of projects cancellation in month of December-January. With new business not keeping in pace with the lost contracts, we believe that there is a likelihood of volume decline in projects. Repeat business and new business volume growth for top 4 IT companies has declined from peak of more than 40% to single digit.

New clients addition not in pace with ramp-down in projects...

Business Growth



Net New Client Addition



Source: PINC Research, Company Report (Infosys, TCS, Wipro and HCL Tech*), *June Year End

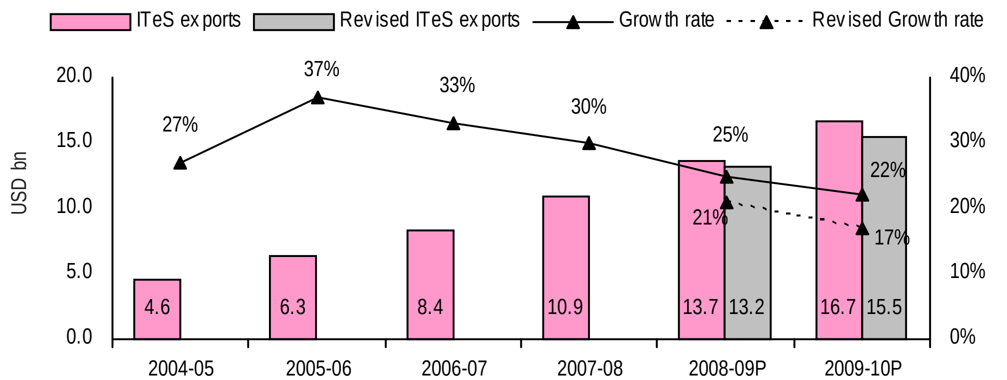
Top 4 IT companies are suffering from slowdown in IT budget or spate of projects cancellation from the existing clients. To add to the worsening situation, the new client addition has not been able to keep up the pace with slowdown in IT budget from the existing clients. Net new client addition for the top 4 IT companies in Q3FY09 has come down to 38 from 103 a year back in Q3FY08.

NASSCOM: Estimates look ambitious

In early February, NASSCOM lowered its projections for export revenues in India's IT and business process outsourcing (BPO) sector for the fiscal year ending March 2009. The target was originally set at USD50bn with a growth rate of 21-24%. Now, NASSCOM is projecting USD 47bn at a growth rate of 16-17%. According to us, the growth target still looks ambitious with the global demand environment still looking weak.

NASSCOM too optimist...

ITeS exports growth rate: not factoring the worst case



Source: NASSCOM

RETURN TO ECONOMIC NATIONALISM: A THREAT TO GLOBALIZATION

The deteriorating economic condition in the US and the UK could force the government to impose some stricter laws, if the condition does not improve from here. Economic nationalism-the urge to keep jobs and capital at home-is both turning the economic crisis into a political one and threatening the concept of free mobility of resources.

The current global financial problems began in the U.S., and it has been among the hardest hit countries so far. The BFSI industry has written down USD1.1trn and raised USD1.0trn. The pendulum is bound to swing back and partly because, having just given trillions of dollars to the banks, politicians will be under pressure to save jobs for locals.

"Tax payers money can not be used to outsource work"...

Bailouts: to extend pressure on outsourcing

The US		The UK	
Firm	**Total (USD bn)**	**Firm**	**Total (GBP bn)**
Citigroup	60.0	Royal Bank of Scotland	20.0
Bank of America Corp	45.0	HBOS Plc	11.5
AIG	40.0	LLYODS Banking Group	5.5
Wells Fargo & Co	25.0	Northern Rock PLC	3.4
JP Morgan Chase	25.0	**TOTAL**	**40.4**
Fannie Mae	15.2	**The Netherland**	
Freddie Mac	13.8	**Firm**	**Total (EUR bn)**
Morgan Stanely	10.0	ING Greop N.V	10.0
Goldman Sachs Group	10.0	Fortis	4.0
Others	47.1	Aegon NV	2.3
TOTAL	**291.1**	**TOTAL**	**16.3**

Source: Bloomberg

H1-B still in a fix: The new regulations on H-1B visas are still shrouded in a certain amount of confusion. The stimulus package that U.S. President Barack Obama signed into law on February 17 says that all companies, which receive federal funding under the Troubled Asset Relief Program will be considered "H-1B dependent" -- a category that so far included only businesses where more than 15% of the workforce were such visa holders. Companies within this category have to attest that they have made "good faith" attempts to recruit equivalent U.S. workers before hiring H-1B visa holders, haven't displaced any U.S. workers, and are paying the prevailing U.S. wages to any H-1B hires.

H1-B politics: could rejig onshore-offhsore mix...

NASSCOM fighting the crisis: NASSCOM is lobbying hard to work with Sen. Grassley to ensure that there is no fraudulent use of H1-B visas and legitimate business does not get affected. Indian IT companies constitute about 11% of total H1-B visa pool issued by the US government. Any protectionist measure by the US government will rejig onsite-offshore mix and hence could dent the earning of Indian IT companies. Any decline in the current level could affect their onshore capabilities.

No of H1-B visa petitions approved

	FY06	FY07	FY08
Infosys Technologies Ltd	4908	4559	4559
Wipro Ltd	4002	2567	2678
Tata Consultancy Services Ltd	3046	797	1539
HCL Ltd	910	218	103

Source: US CIS

THE GLOBALIZATION OF GLOBAL DELIVERY MODEL

Large global competitors have replicated the global delivery model and managed to grow their Indian employee base faster than the Indian peers thereby giving tough competition to Indian IT Services giants. EDS, Capgemini, Cognizant, Accenture and IBM have increased their employee count in India at a CAGR of 37% in last three years faster than Indian peers, which grew touch slower at a CAGR of 33%. Global peers pose significant competition to the Indian peers at both the international and the home-turf.

Global peers grew at a faster pace in India when compared to top 4 Indian IT companies...

Global peers: growing employee base at a CAGR of 37%

Companies	2006	2007	2008	CAGR
EDS*				
Worldwide	120,000	139,500	143,000	9%
India	32,000	41,000	47,190	21%
Capgemini				
Worldwide	67,889	83,508	91,621	16%
India	6,979	17,000	23,000	82%
IBM				
Worldwide	355,766	386,558	398,455	6%
India	51,800	74,000	80,000	24%
Cognizant Tech				
Worldwide	24,300	38,800	61,700	59%
India	17,010	29,100	49,360	70%
Accenture				
Worldwide	146,000	170,000	186,000	13%
India	23,000	38,000	45,000	40%
Total				
Worldwide	713,955	818,366	880,776	11%
India	130,789	199,100	244,550	37%

*Source: Company Report, Bloomberg, * Includes Mphasis*

Indian top 4: growing at a slower pace than the global peers

Companies	2006	2007	2008	CAGR
Infosys	52,715	72,241	91,187	32%
TCS	66,480	89,419	111,407	29%
Wipro	37,655	67,818	82,122	48%
HCL	32,626	42,017	50,741	25%
Total	**189,476**	**271,495**	**335,457**	**33%**

Source: Company Report, PINC Research

Global peers like IBM have managed to capture a big pie of the Indian IT market...

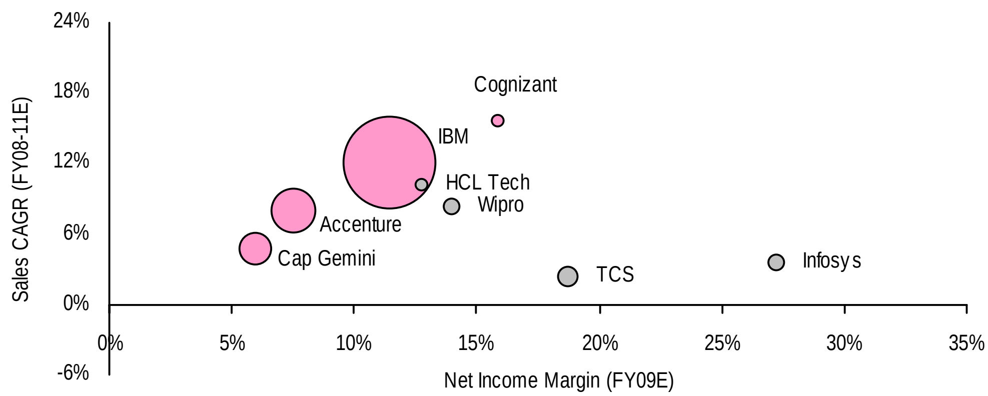
The big four global IT companies have not only managed to replicate the model of Indian IT companies by hiring employees in India but has also taken the competition to their home turf. The margin conscious Indian companies have focused on the US and European market. Faced with slowing volumes from existing customers in the US and Europe, Indian vendors in recent quarters have increased their focus on the Indian market. IT budgets in India are expected to grow at 5.5% in 2009, down from 13% in 2008, according to Gartner CIO poll. IBM is the leading IT vendor in India.

Global peers are growing faster in India than Top 4 Indian players...

Growth vs Margin: Global peers of Indian IT companies are expected to grow faster according to Bloomberg analyst estimates. In CY08, global peers managed a better growth when compared to the growth of Indian IT companies. Acquisition by Wipro and HCL would help them achieve inorganic growth. Infosys abstained from making any acquisitions but still command the highest margin among its peers. In the given demand environment, when multiple headwinds are acting against the margins, we believe that Infosys has to use multiple cost cutting measures to maintain the same margins. *We believe that due to replication of GDM by global competitors they are giving strong competition to large Indian IT companies for smaller contracts that were earlier a low hanging fruits for Indian players.*

Indian IT companies are high on margins but low on volumes...

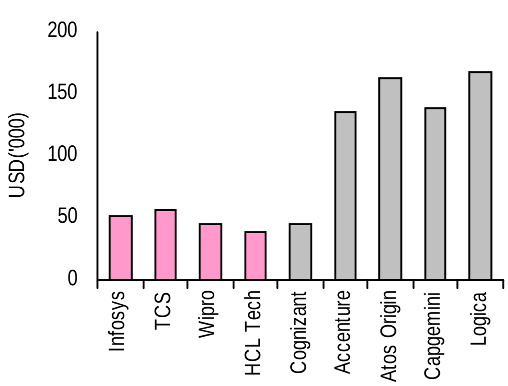
Global peers eyeing stronger growth



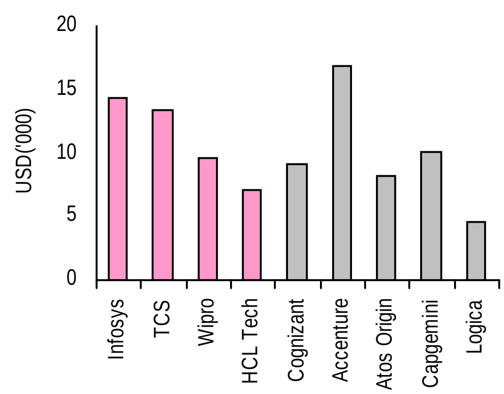
Source: PINC Research, Bloomberg Estimates

Indian top 4 IT players scores in profitability per employee...

Revenue per employee (FY08)



EBIT per employee (FY08)

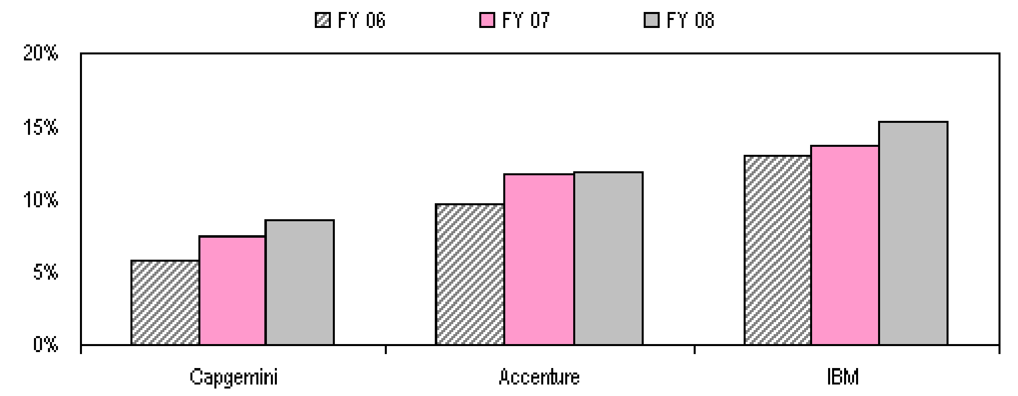


Source: PINC Research

Global peers like Capgemini, Accenture and IBM have managed to steadily increase their EBITDA margins over last 3 years by hiring more professionals than Top 4 Indian players in India. Capgemini improved margins by 274bps, Accenture by 244bps and IBM by 233bps over the last three years, whereas Indian players were either steady or declined over the same period with Infosys & TCS managed to maintain the margins while Wipro & HCL Tech witnessed a decline. There is still scope for global peers to grow and scale their business in India. Global peers could improve their operational efficiency and under-cut Indian peers for the same projects in pricing. Indian IT bellwethers have already exploited the system to the fullest.

EBIDTA Margin - global players steady on the path of improvement

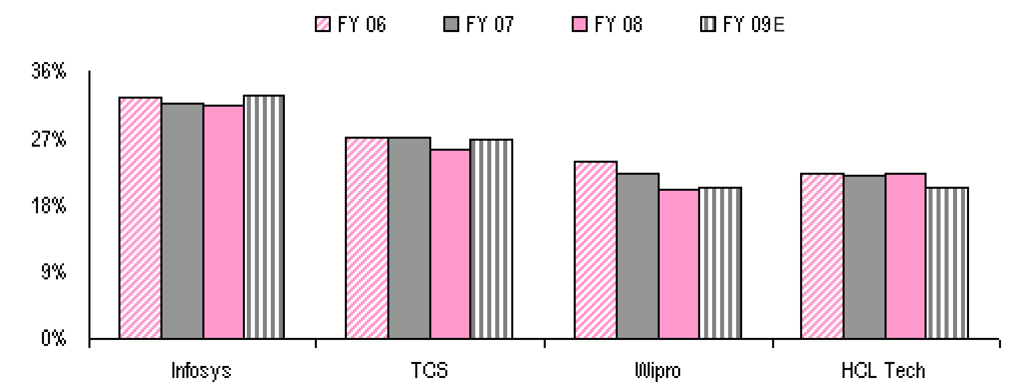
Global players replicating margin levers of Indian players...



Source: PINC Research, Company report

EBIDTA margin - Indian players have little room for improvement

Indian players have already exploited the low-cost benefit to the fullest possible extent...

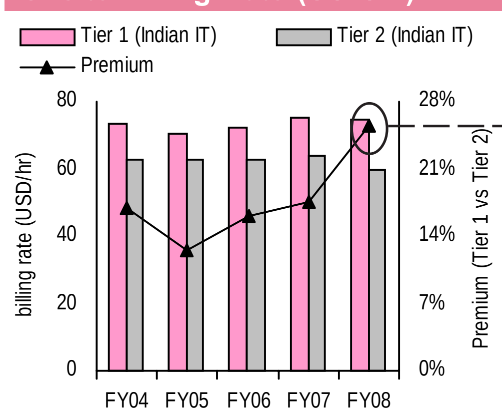


Source: PINC Research, Company report

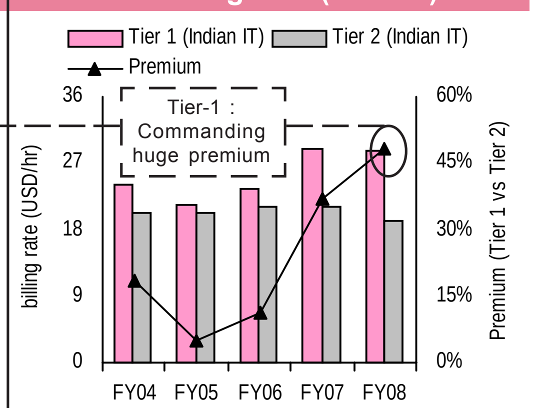
Indian IT companies are facing tough competition from the Tier 2 IT companies. Although Tier 1 players managed to command higher price over Tier 2, we believe that the gap will narrow down as Tier 2 players scale up. The premium of the billing rate of Tier 1 IT companies over Tier 2 IT companies has increased 25.5% for onsite and 48% for offshore. We believe that the billing rate would converge for the service offering bringing the premium down. The huge premium of billing rate of Tier 1 players over Tier 2 players will put pricing pressure on Tier 1.

Tier-2 Indian IT players giving tough competition to Tier-1 players by cutting their price aggressively...

Onsite Billing Rate (USD/hr)



Offshore billing rate (USD/hr)



Source: Crisil Research

IGNORED DOMESTIC MARKET: GLOBAL PEERS GIVING TOUGH COMPETITION

IBM scoring high on Indian turf, which is largely ignored by Indian players...

Although domestic market presents a significant opportunity as IT spending in India is growing at a faster pace than any other country in the Asia-Pacific region, Indian IT companies largely ignored the opportunity due to lower operating margin, giving global giant like IBM to strengthen its foothold.

The demand in the local market is driven more by skilled labor rather than cost arbitrage giving little incentive to Indian IT vendors to bid for domestic projects. Domestic IT-BPO revenues are expected to grow at almost 20% to Rs1,113bn in FY09, driven by increased IT-BPO adoption.

INDIAN IT OUTSOURCING CONTRACTS: IBM STANDS TALL

Service Provider	Client	Amount	Details
2008			
HCL Tech	RBI	Rs100cr	Setting up of 2 centres and their maintainence for 7 years
HP-led consortium	United India Insurance	Rs100cr	7 yr contract to implement core insurance solution
IBM	India s Central Board Of Direct Taxes	USD45 mn	Integrated Infrastructure solutions for its data centres
IBM	BSNL	Rs70 cr	To provide end to end network solutions
2009			
Convergys	BSNL	na	Support and maintainence contract for providing infinys rating and billing solution
HCL Tech	National Insurance Co LTD	USD79.5mn	Deployment of core insurance solutions at NICL's offices
HP India	Godrej	na	Providing IT outsourcing services
IBM	Idea Cellular	USD700mn	To provide support in end to end transformational
IBM Daksh	MakeMy Trip	na	Augmentation of back office capabilities
IBM Daksh	Bharti Airtel	na	To provide services in the voice and back office areas
Infosys Tech	Bharti Airtel	na	Providing a comprehensive product portfolio including devices & application servers
TCS	Min. Of Ext. Affairs, Govt Of India	Rs1000 cr	Implementation of the passport serva project which will roll out countrywide within 6 years
Wipro	ESIC	Rs1182cr	To streamline registration filings and payouts at its centres

Source: NASSCOM

PYRAMID EFFECT NOT GEARED FOR DECELERATED GROWTH

Indian IT companies managed to maintain employee cost steady at 53-57% of total revenue despite a salary hike of 10-15% for offshore employee and 2-4% for onsite employees. The companies managed to do so by hiring more number of employees at the bottom of pyramid (broadening the base of the pyramid). The hiring done at the bottom was at an accelerated pace at the bottom of pyramid.

The pyramid structure did give them distinct edge to manage margins. Low to mid-teens attrition rate acted as sweetener to the proposed strategy. The average age of Indian IT companies remained steady at 26-28 years.

We believe that with little visibility of volume growth, gloomy macro-economic condition, and in declining attrition scenario, the ability to maintain the pyramid base would be difficult.

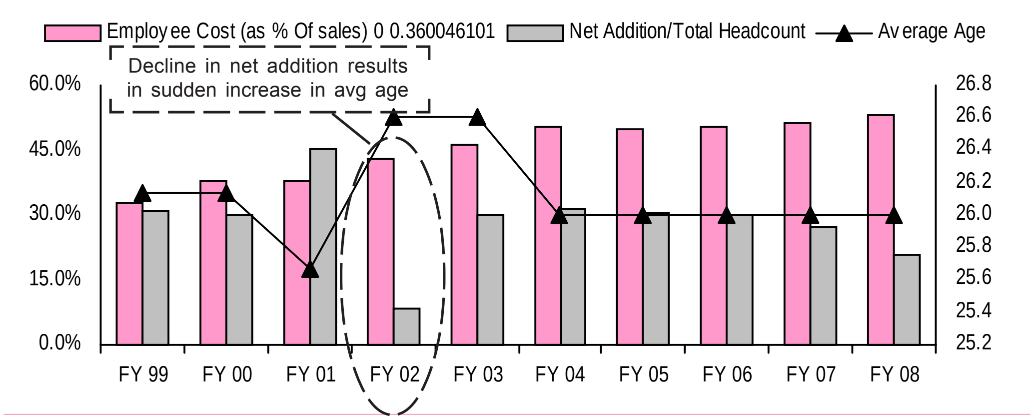
According to our estimate, freezing the hiring process for one year could increase the average age of employee by one year and given the same level of wage hike it could erode margin by 300-400bps. Although each company has variable pay structure built into their pay which could provide some cushion for the margin pressure in a declining volume scenario.

Low growth visibility and declining attrition exerts pressure on pyramid..

Our calculation shows that for an attrition rate of 15%, Infosys should have net addition of 17% (to total employees) as fresh graduates (assuming average age of fresh graduate is 21 years and rest all hires have an average age of 26). For each percentage point decline in the attrition the net addition should increase by 20bps. So we believe that if Infosys has to grow in volume at a CAGR of 17% with an attrition of 15%, it should have 100% hires as fresh graduates. So, any decline in attrition and growth rate would deteriorate the pyramid structure.

Any deceleration in hiring plans would disrupt pyramid structure...

Pyramid: geared for an accelerated growth



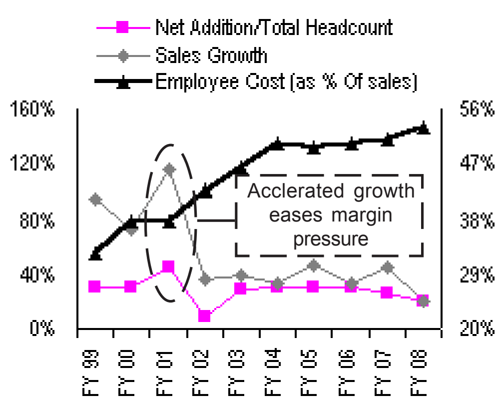
Source: PINC Research

The pyramid structure is geared towards an accelerated top-line growth, which has very little visibility in the current environment. Historically, the average age of employees for Infosys went up to 26.6 years in FY02, when Infosys put a freeze on hiring in FY02 and hired only 907 employees, the lowest in last 9 years. Employee cost (as a % of sales) for Infosys has been growing steadily despite addition at the bottom of pyramid. We believe that any deceleration in the growth of Infosys could not only increase the average age but also accelerate the employee cost putting pressure on margin.

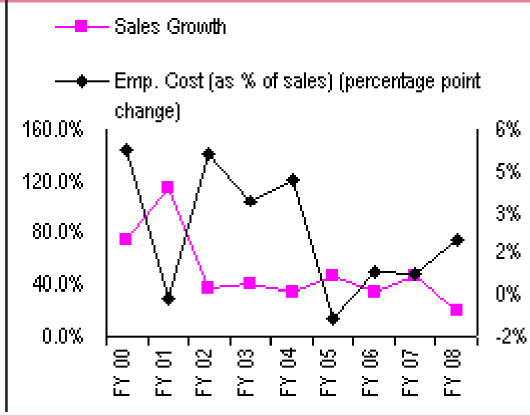
Employee cost in FY05 saw a slight dip because of higher sales growth with stable employee addition. In FY01, when the revenue grew by 115%, there was a drop in the employee cost (as a % of sales) by 15bps and acceleration in sales in FY05 has seen similar behavior in Employee cost as a percentage of sales. We believe that with high single digit pricing decline and low single digit volume growth, the companies have to freeze hiring in order to contain the cost which will disrupt the pyramid structure.

Strong sales growth could help containing employee cost structure...

Employee cost: steadily increasing



Growth stalls emp. cost

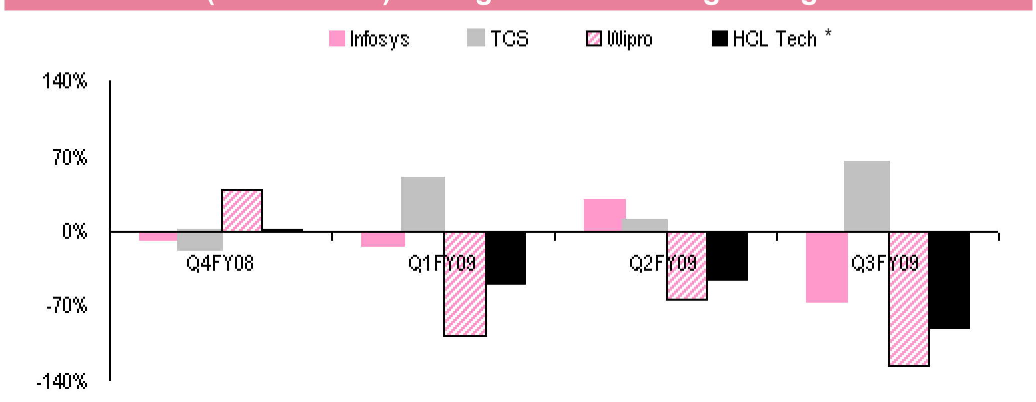


Source: PINC Research

Indian IT companies have proactively acted to withstand the slowing revenue growth. Wipro and HCL Tech were the most proactive with net head count addition and freezed hiring in Q1FY09 and doing just in time hiring, hence net employee addition has shown decline steadily in last 3 quarters. Any decceleration in the hiring plan would put pressure on the pyramid structure of the employee. Net employee addition for top 4 Indian IT companies has witnessed YoY decline over the last three quarters except for TCS.

Hiring freeze could help cut cost but would disrupt pyramid structure...

Net Addition (YoY Growth): hiring freeze resulting in negative addition



*Source: PINC Research, *June Year End*

PINC RESEARCH

New Joinees: pressure on margins

Infosys, TCS, Wipro and HCL Tech have made offers to students passing out in the middle of this year, expecting to win projects. Due to the ever worsening demand environment, volume growth is expected to be in low single digit together with a decline in pricing. Infosys has made offers to 20,000 students, TCS to 24,000 and Wipro to 16,000. These freshers are expected to join in FY10. Companies' utilization rate would fall and there could be pressure on margin if the volume growth does not move in tandem.

New joinees could negatively impact the margins...

Utilization rate: could decline further due to new joinees addition

	FY05	FY06	FY07	FY08	Q1FY09	Q2FY09	Q3FY09
Infosys							
Utilisation Rate (incl trainees)	72.9%	71.40%	69.50%	70.90%	68.9%	69.4%	68.5%
Net addition	11,116	15,892	19,526	18,946	3,192	5,927	2,772
TCS							
Utilisation Rate (incl trainees)	76.9%	75.8%	79.6%	75.8%	74.6%	74.7%	71.8%
Net addition	10,871	21,140	22,750	22,116	4,895	5,328	8,692
Wipro							
Global IT - Excl IFOX - Gross	67%	65%	64%	67.10%	67.90%	70.30%	69.8%
Net addition	13,355	11,885	14,076	14,304	13,553	1,877	(587)
HCL Tech							
Utilisation Rate (incl trainees)	70.5%	71.8%	71.1%	73.9%	73.90%	74.40%	74.50%
Net addition	7,732	8,479	9,391	8,724	939	1,973	243

Source: PINC Research

Utilization rate is at an all time low for most of the Indian IT companies...

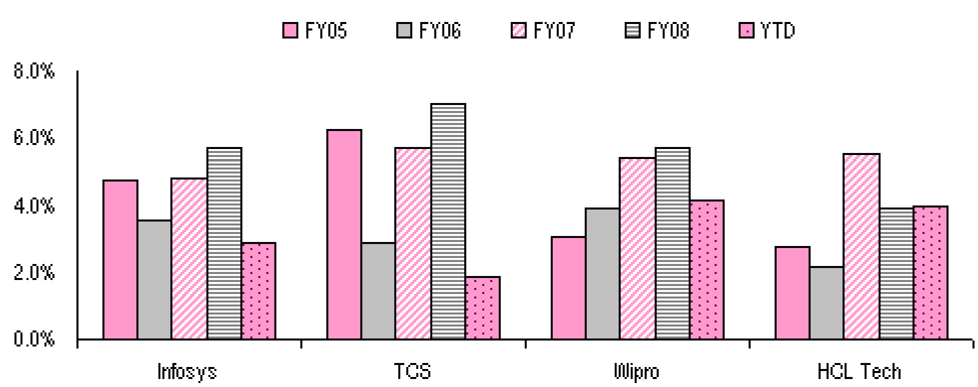
We expect utilization rate to fall by another 75-100bps for all the four Indian IT companies putting further pressure on the margins. We believe that utilization rate at the current run rate of our forecasted volume growth could fall to the lowest level in last 8 years (Infosys' lowest utilization 67.5% (Q2FY07), TCS 71.8% (Q3FY09), Wipro 67.0% (Q3FY07), HCL 67.0% (Q1FY06)).

According to the company data, for each percentage point decline in utilization the headwind against margin is about 50bps.

We believe that they have already stretched their bench strength. Given the little visibility for volume growth unlike FY07, Indian IT bellwethers cannot afford benches anymore. They would need to redeploy and retrain existing bench and also put a freeze on lateral hiring.

Infosys and TCS have hired the highest number of employees despite lower growth visibility...

△ Sales (USD mn))/ Net Employee Addition: TCS is the worst placed



Source: PINC Research

According to the NASSCOM, India's IT services companies and BPOs are expected to hire about 200,000 people by next March, lower compared to earlier projection of 276,000. The revised figure represents a 20% decrease from the 250,000 new hires recorded for the previous fiscal year.

IT companies are using innovative techniques to utilize the bench strength...

Steps taken by companies to utilize the bench strength without any respite to margins pressure

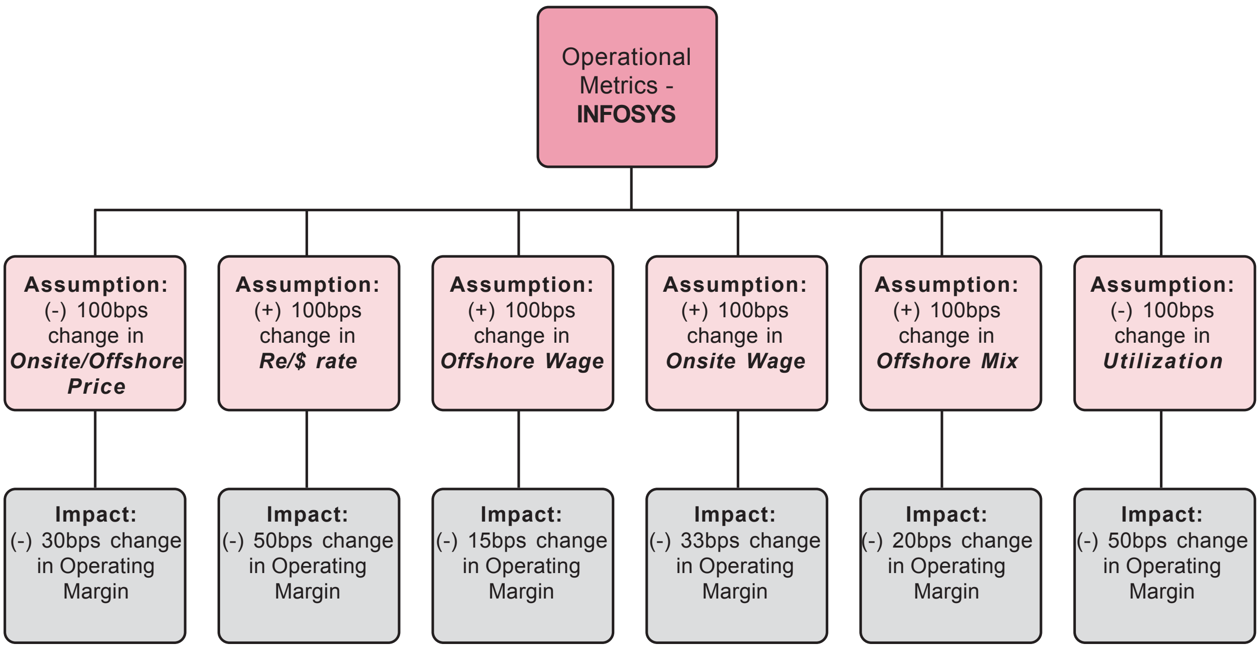
- *Increase the training period*: Companies are increasing the training period for the new joinees. Infosys has increased the training period from 3 months to 6 months. TCS has put its benched employee at high end training and has also invited to write white papers on different technologies.
- *Internal IT projects*: IT companies are using their bench staff for internal IT projects for example Infosys has revealed that it will put 10% of its workforce to work on developing internal systems, such as human resources and invoicing systems, in order to keep them busy despite slowing demand.
- Leave-without-pay: Companies are offering leave-without-pay to their employees. This will help companies to contain the cost. Infosys has offered their employees to work for non-profit organization at 50% of their salary. Wipro under a special programme has given an option given to employees, who have been on the bench for over six months, that allows them to come to work for 10 days a month, at half their salary.

MULTIPLE HEADWINDS: A DETAILED ANALYSIS

Unlike past, IT companies are facing mulitple headwinds in 2009...

Indian IT companies are feeling the pain because of multiple headwinds. Although we are evaluating operating metrics of Infosys, we firmly believe that the data for TCS, Wipro and HCL Tech would not vary hugely. Top 4 Indian IT companies are struggling with falling prices. Clients have asked for a price cut of 5-20%. If we assume a price cut of 5%, the margin of companies could get affected in the order of 150bps. All the companies have levers like lowering SG&A cost, avoiding travel, moving people from onsite to offshore and variable employee salary. According to the company, they have already adopted cost control measure to absorb a price cut of 5%, but a price cut beyond that could impact the margins.

Headwind analysis: multiple levers in play

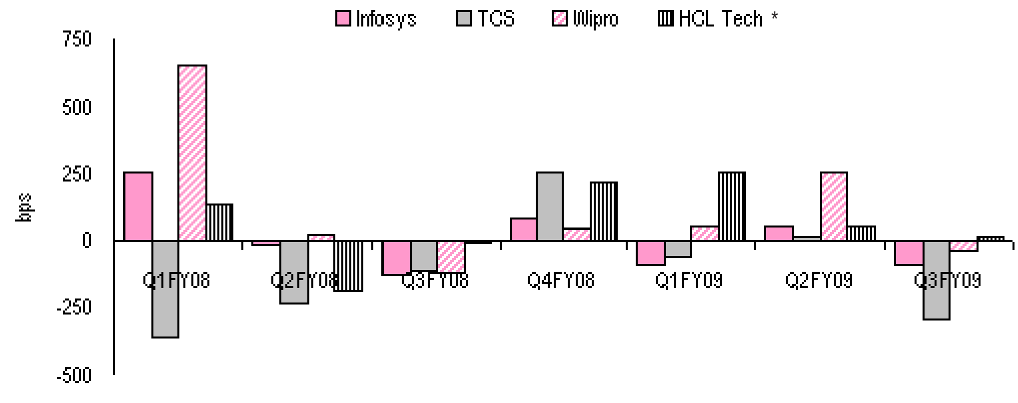


Source: PINC Research

Due to recruitments by companies in FY08 and falling volumes there is a secular decline in the utilization rate. We are forecasting low single digit volume growth for all the four players and with campus recruits which are expected to join in FY10, we expect utilization rate to fall further. In last 3 quarters, utilization rate for Infosys has fallen by 130bps, for TCS 338bps, but for Wipro and HCL Tech utilization rate increased by 270bps and 320bps respectively. A decline by 100bps in utilization rate could erode margin by 50bps.

Utilization rates have fallen to the lowest level...

Change in Utilization Rate (QoQ Growth): Infosys & TCS shows decline (YTD)

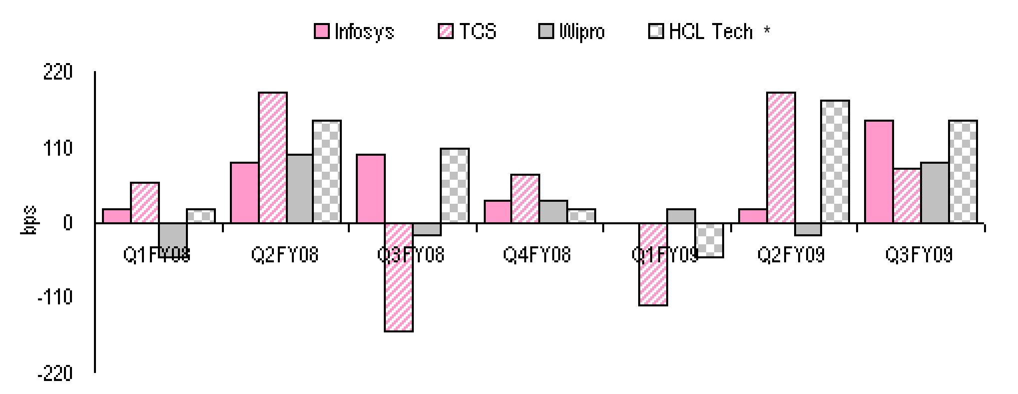


Source: PINC Research, *June Year End

As clients renegotiate their contracts at lower prices, the companies have to work hard to maintain margins by moving more work to offshore. Offshoring has surged to 170bps, 150bps, 90bps and 280bps for Infosys, TCS, Wipro and HCL Tech respectively. The increasing offshore could negatively impact margins provided all the other criteria for the project remains the same. According to our estimates for each percent point shift in offshoring, the margin would get diluted by 20bps.

Increased offshore mix is helping to contain cost but affecting the margins...

Change in Offshore Mix (QoQ Growth): move towards offshoring

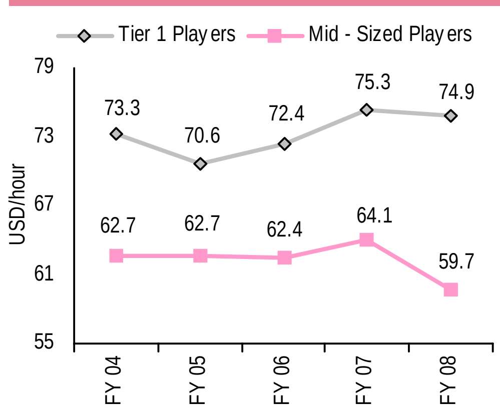


Source: PINC Research, *June Year End

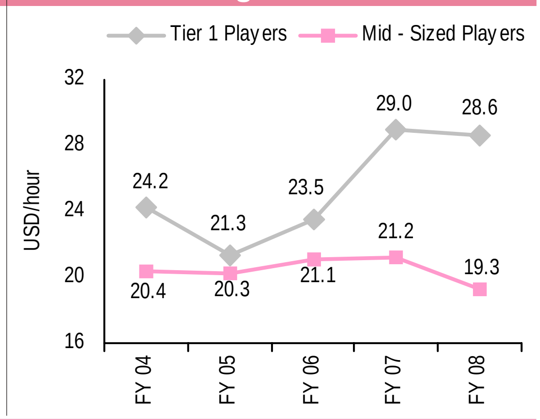
The offshore billing rate declined by 1.4% YoY in FY08 when compared to 0.5% decline in onsite billing rate. The drop in the offshore billing rate was higher than higher than onsite and shift of more offshore work is a double whammy for margins of top IT companies.

Offshore billing rate has declined more compared to onsite billing rate...

Onsite Billing Rate



Offshore Billing Rate



Source: PINC Research, CRISIL Research

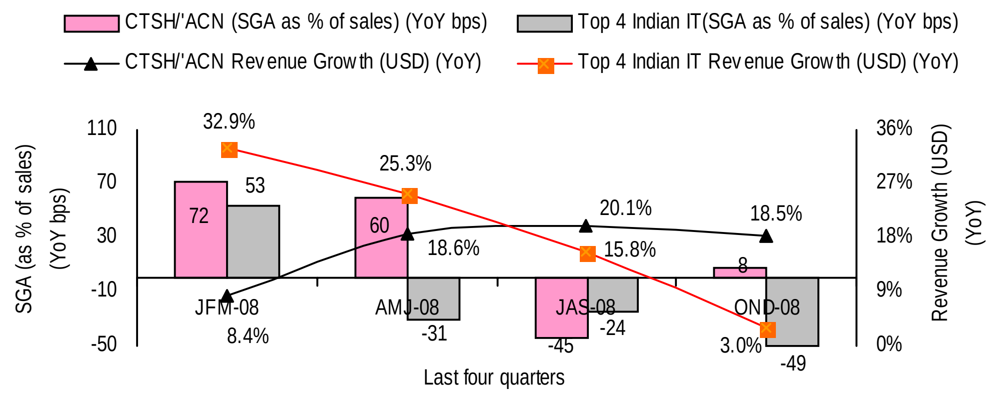
Cost lever: Double edged sword, should be played cautiously

Unlike 2000-01, when the Indian IT companies didn't cut their Sales and Marketing expense, the Indian IT bellwethers are cutting down on their S&M cost to maintain margins. S&M cost of top 4 Indian IT companies when compared to Cognizant and Accenture has seen steady decline in the last four quarters with a decline of 49bps YoY in the most recent quarters. The cut in sales and marketing expense has affected their revenue growth, which has reduced to low single digit in the quarter ended December with a growth of 3% YoY.

Cutting on S&M cost could get translated into lower sales growth...

In a downturn like this one, Indian IT bellwether are cutting down on their marketing budget in line with customers, who themselves are cutting budgets, opting instead to save more than spend. With an eye on margin, a cut in sales and marketing expense could get reflected in revenue growth when the economy recovers.

SGA levers: Clamp-down of SGA tapering the growth of Indian IT



Source: PINC Research, Company Reports

STPI AND FOREX: HITTING BELOW THE LINE, RETARDING BOTTOM LINE

Forex, a double edged sword for the earning of Indian IT companies, played havoc to the top line and margin in FY08. The increased forwards taken by Indian IT companies have affected their bottom line when currency started depreciating. The advantage of STPI, which Indian IT companies reaped for long, is getting over in FY10. The effective tax rate would surge in FY11. The slower than expected growth rate could increase effective tax rate.

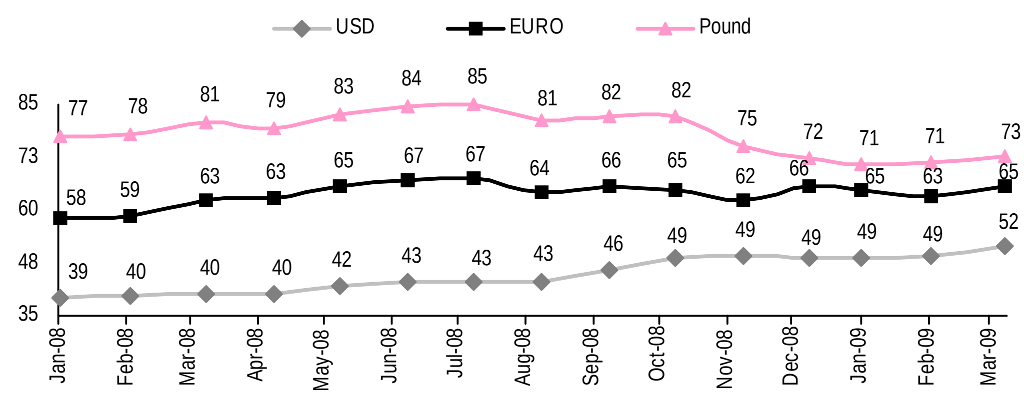
Help from rupee depreciation: Base effect in Q3FY10

Unable to reap the benefit of depreciating currency because of cross currency exposure ...

Top four Indian IT companies still have over USD 1bn as forex hedge position except for Infosys that has USD576mn as forex hedge position. The declining volume and pricing pressure has got some respite from the depreciating currency. But we believe that currency depreciation is soon catching up with the base effect and Q3FY09 scenario is less likely to happen when revenue in rupee term has got breather. We don't have house-view on currency and thus we are forecasting a stable currency of Rs50/USD for all the forward quarters.

Rupee finally depreciated from the level of Rs39/USD in Jan-08 to Rs51/USD in Mar-09. However, the rupee's movement from Rs49/USD to Rs51/USD assisted the revenue in rupee term for Q4FY09, but the companies are facing the wrath of hedging losses.

Forex movements: base effect could dampen growth in Q3FY10



Source: RBI

Indian IT services companies managed mid teens growth in FY09 despite tailwind from rupee depreciation by about 28% in FY09. In USD terms, revenue of top four Indian IT companies has increased by 16% YTD (including acquisitions by Wipro and TCS) in FY09. With tough FY10 ahead, we expect volume growth to be in low-single digit. We forecast a stable currency going forward giving no tailwind to revenue.

Infosys has the lowest hedge whereas HCL Tech has the highest ...

Company specific: Infosys has least amount of hedges with USD576mn of hedges at the end of the fourth quarter. The policy is to hedge for two quarters. The company mark to market all the hedges and nothing flows through the cash-flow.

TCS has close to USD1.25bn in hedges. The post hedge realization rate was Rs46.75/USD after Q3FY09. Since it follows the cash flow method, hence OCI from the balance sheet would also come into P&L, which gets recognized for this quarter going forward.

Wipro has USD1.8bn of hedges at the end of the fourth quarter. The hedge is spread over 3-4 years. About 15% (of revenue) are flowing in every quarter are flowing as hedge position. The range of average rate is Rs39-49/USD

HCL Tech has the highest forex hedges among its peers with total hedge position of USD1.6bn lowered significantly from US$2bn in Jun-08.

Hedge Position: Infosys in the driver's seat

		FY2009	
$ mn	**Q1FY09**	**Q2FY09**	**Q3FY09**
Infosys	811	932	576
TCS	1680	1019	1250
Wipro	2600	2100	1800
HCL Tech	2000	1900	1580

Source: Company Report, PINC Research

HCL Tech to be the worst affected in Q4FY09 ...

Forex loss: TCS and HCL Tech would be the worst affected in Q4FY09

Forex Gain/Loss		FY2009		
Rs mn	**Q1FY09**	**Q2FY09**	**Q3FY09**	**Q4FY09E**
Infosys(Indian GAAP)	(800)	(1,260)	(2,180)	(407)
TCS(Indian GAAP)	(753)	(2,608)	(2,506)	(1,207)
Wipro(US GAAP)	(689)	(1,000)	(371)	(370)
HCL Tech(US GAAP)	(2,999)	(974)	(1,419)	(1,113)
Currency movement (Avg USD rate)		**FY2009**		
Infosys	42.0	44.6	49.4	51.0
TCS	42.0	44.3	49.1	51.0
Wipro	41.2	42.7	46.0	47.5
HCL Tech	42.0	44.5	49.4	51.0
Currency movement (Avg USD rate)		**FY2009**		
Infosys	5.7%	6.0%	10.9%	3.2%
TCS	1.3%	5.4%	10.8%	3.9%
Wipro	3.3%	3.6%	7.7%	3.3%
HCL Tech	5.4%	5.9%	11.1%	3.2%

Source: Company report, PINC Research

China posing threat to appreciating dollar ...

China forex reserve: a threat to USD: China is concerned about holding huge amount of the US dollar in its forex reserves. Governor of People's Bank of China has asked for new currency as reserve from IMF that could be more stable and economically viable. China holds about USD2trn as foreign exchange reserve of which more than 50% is in US treasuries and USD denominated bond. According to our estimates the USD reserves with China is about 7-8% of the US GDP. China suggested that the dollar's reserve status should be transferred to the SDR (Special Drawing Rights), a synthetic currency created by the IMF, whose value is determined as a weighted average of the dollar, euro, yen and pound. The SDR was created in 1969, during the Bretton Woods fixed exchange-rate system, because of concerns that there was insufficient liquidity to support global economic activity. Russia has also made similar proposal some time back. Any change in the reserve currency by China could devalue US dollar. *We believe that a step towards change in reserve currency could significantly impact the USD movement against Indian rupee and depreciation of USD against Indian currency could make the situation worse for the Indian IT companies.*

PINC RESEARCH

STPI to end, negative impact on PAT

Currently, units operating under the STPI or EoU schemes can avail income-tax deductions under section 10A/10B of the Income-tax Act, 1961 ("the Act") in respect of export profits. However, this deduction is available only until March 31, 2010, and there is uncertainty regarding the further extension of these provisions. The STPI and EoU schemes also provide various indirect tax benefits (i.e. exemption from excise, customs etc) which would continue to be available even beyond 2010.

Given the fact that STPI was extended just only for one year by the current government, we believe that it might not get extended in current form if baton does not exchange hands at centre.

The Government has also introduced the SEZ scheme which seeks to provide benefits similar to sections 10A and 10B. The Company also has operations in Special Economic Zones (SEZ). Income from SEZ are eligible for 100% deduction for the first 5 years, 50% deduction for the next 5 years and 50% deduction for another 5 years subject to fulfilling of certain conditions.

Slower than forecasted volume growth could increase the effective tax rate for FY11 more than anticipated ...

SEZ clarification: Under the older law, the tax exemption for SEZ export unit (section 10 AA) will be calculated in conjunction with the total revenue of the company. So if the company's total export is x% of the total turnover, then x% of the profit from SEZ will be exempted from the tax. This was against the companies having multiple units and IT companies were planning to set-up subsidiaries to reap the complete benefit from SEZ.

Slower volume increase could result in higher than expected tax rate: *According to us, slower volume growth than anticipated could raise the effective tax rate more than anticipated in FY11. We are factoring in the number for new business moving to SEZ, but as the volume of new business dries up the companies' effective tax rate could go higher than anticipated.*

TCS has the highest contribution from SEZ ...

SEZ and STPI centres	STPI	SEZ
Infosys	15	4
TCS	36	10
Wipro	na	10
HCL Tech	na	4

Revenue contribution	STPI	SEZ
TCS	67%	23%
Infosys	90%	6%
HCL	90%	7%

Source: Company data, PINC Research

FY 11 (EPS Sensitivity)

Tax Rate	16%	18%	20%	22%	24%
Infosys	118.2	115.4	112.6	109.8	107.0
TCS	58.4	57.0	55.6	54.2	52.8
Wipro	26.2	25.6	24.9	24.3	23.7
HCL Tech	18.2	17.7	17.3	16.9	16.4

Source: PINC Research

LEASING IP VS LEVARGING IQ: LINEAR VS NON-LINEAR

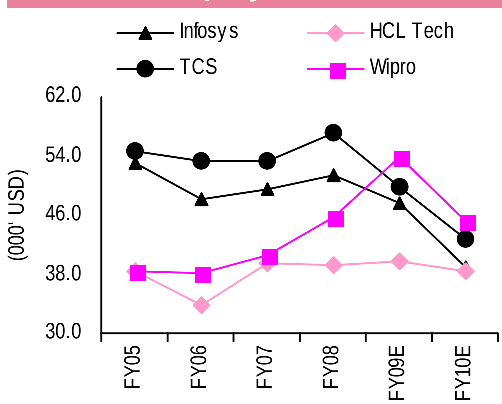
Indian IT companies have pegged their growth to the linear model, where the revenue increase is linked to the volume growth, which is linked to headcount. There is still scope of growth opportunity left in the system where they can grow at the same pace. Nevertheless, building non-linearity in the model like developing products and consulting business would not only help maintaining margins but also build cushion for the margins.

Indian IT companies pegged their growth to employee addition...

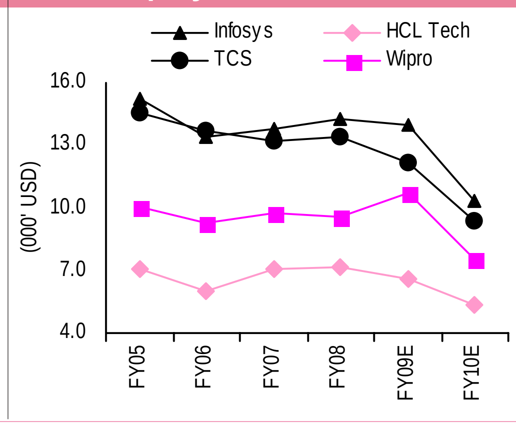
We believe that managing resource by top four IT companies will become key constraint for the growth of these companies. In a decelerating revenue growth environment, the top 4 companies have to put strict control on the cost with a proactive freeze on hiring and salary hikes. We believe that, Wipro due to its proactive hiring freeze would be able to maintain its per employee revenue for FY09, but for Infosys revenue and EBIT per employee would show maximum decline due to 20k campus hires.

Tapering growth putting pressure on profitability per employee...

Revenue/Employee



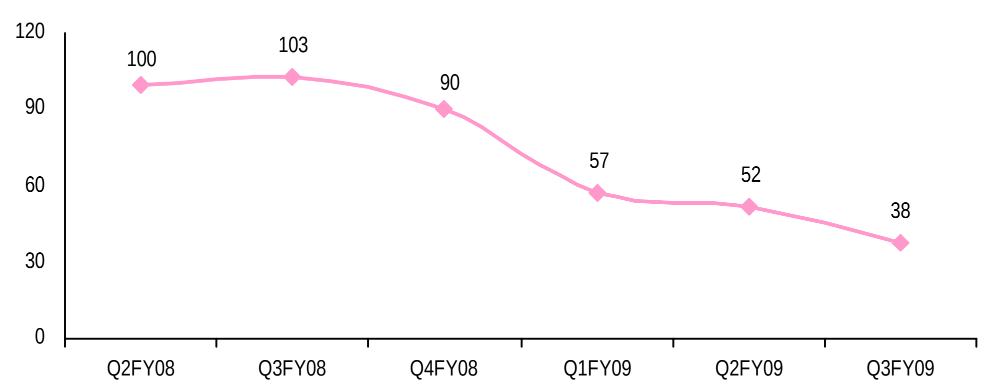
EBIT/Employee



Source: PINC Research

Net new client additions: declining trend (Top 4 Indian IT companies)

Net new client additions are not keeping pace with project ramp-downs ...



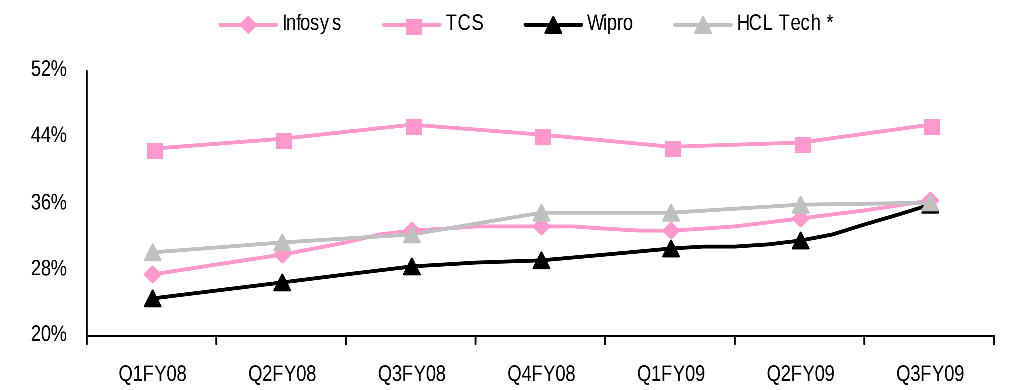
Source: PINC Research

Some of the key strategic initiatives taken by companies to build non-linearity model has helped them maintain the margin and gave some non-linearity to the model.

Fixed price model could give limited non-linearity to the revenue ...

- *Outcome based pricing*: Indian IT companies are trying to move more towards Fixed Price contract in order to give boost to their margins. We are now witnessing fixed price contracts, which were earlier restricted mostly to application development projects, followed in ordinary maintenance projects also. IT companies are incorporating outcome based pricing in their BPO model by negotiating for success-fee or profit-sharing model.

Fixed Price Contracts (as a % of sales): using an efficiency parameter



Source: PINC Research

Consulting and product contribution is still in mid single digit ...

- *Consulting and Product portfolio*: Indian IT companies have made conscious effort to move up the value chain by moving into IT consulting. HCL Axon acquisition has helped them build IT consulting capability inorganically. But despite all the efforts by Indian IT companies, the consulting remains very small part Infosys' Finacle & ShoppingTrip360, TCS' Bancs, HCL acquisition of Axon are some of the key non-linearity built by these companies. Despite all the efforts to move up the value chain, they derive sub 10% of revenues from product and consulting domain.

- *Managed Service*: Wipro's acquisition of Infocrossing has put it in the forefront of Managed Service. Wipro compete with likes of IBM, CSC and EDS in division of managed services. Managed Services helps selling IT infrastructure (both hardware and software) as a service. Besides Wipro, the presence of Indian IT companies in this domain remains miniscule.

Result and expectation

We expect Infosys to give revenue guidance of low single digit decline in USD terms for FY10...

- Accenture result: Accenture expects net revenues for the third quarter of fiscal 2009 to be in the range of $5.1 billion to $5.3 billion (-1.2% decline QoQ). This range assumes a foreign-exchange impact of negative 12% compared with the Q3FY08. For the FY09, Accenture now expects net revenue growth to be in the range of 0-4% in local currency. The company's previous range was 6-10% in local currency.

Expectation from Q4FY09

1) For Q4FY09: We believe top four IT companies would report a decline of low single digit organic revenue on QoQ basis in USD terms.

2) We expect Infosys to provide revenue guidance of low single digit decline in USD terms for FY10.

M&A: CAUTIOUS APPROACH TO INORGANIC GROWTH

Indian IT bellwethers have taken cautious approach on acquisition despite their abilities to generate good cash from the business and robust balance sheet, and remained wary of inorganic growth.

Infosys is the most conservative and Wipro is the most acquisitive..

Indian IT companies have been averse to acquisition. Among top 4, Infosys has been least active at M&A front, whereas TCS has successfully acquired carve-outs to grow inorganically. Wipro tops the table of acquisitions and managed to build some keen capabilities. Recent acquisition of Infocrossing is an excellent example. Wipro and HCL are the most aggressive in factoring the inorganic growth whereas Infosys remains the most conservative in acquisition.

Infosys has the most robust balance sheet to reap the benefit of current market environment...

Now is the time: Due to expected weakness in the demand, we expect Top 4 Indian IT companies to look for an acquisition. The valuation and value proposition which the target companies can provide at this time could be really attractive. We believe that, Infosys is at the most comfortable position with cash of USD1.8bn. We believe that high cash position, low volume growth visibility in FY10 and attractive valuations of target companies could force Infosys to take an inorganic root. We expect Infosys to make acquisition in Europe to diversify its geographical presence.

Cash Reserve (Rs mn) : Infosys leading the pack

	Q1FY09	Q2FY09	Q3FY09
Infosys	62,980	78,210	86,610
TCS	44,012	41,454	21,610
Wipro	64,854	60,401	58,954
HCL Tech	24,619	26,088	20,265

Source: Company Report, PINC Research

Mid-caps and small-caps need to consolidate for survival...

Considering consolidation: There was near unanimity that the big players would thrive. Hence, there is a scope of industry consolidation. The boutique firms (specializing in niche technology areas) would also cope with the downturn. But the mid-tier companies would have to redefine themselves. In any mature industry, a spate of mergers & acquisitions (M&A) would have happened by now. But IT is a first-generation sector; most of the original company founders are still at the helm, and are not about to let go easily.

BearingPoint bankruptcy: The recent bankruptcy filing of BearingPoint US is one of the most visible examples of how the deepening recession is dragging on the global IT consulting market. Some customers clearly are cutting back, postponing or forgoing discretionary consulting projects, which is affecting revenues for global consulting and systems integration (SI) firms. This however provides opportunity for Indian IT companies to get some high quality assets (clients) at stressed valuation. To our surprise, no Indian IT companies have showed inclination towards it.

Wipro and HCL Tech lead the acquisition pack

Date	Target	Target Revenue	Amount Paid	Amnt paid / target's rev.	No of people in target company	Advantage
Infosys						
Jan-04	Expert Info. Services	AUD 46.7m	AUD 31m	0.7	330	To get a foothold and accquire clients in Australia
TCS						
Oct-08	Citigroup GSL	USD278mn	USD505m	1.8	12000	Platform base BPO
Nov-06	TCS Management	AUD $5.5m	AUD 16.7m	3.0	35	Australian clients and high-end consultancy
Nov-06	TKS-Teknosoft	INR 2600m	INR 3620 mn	1.4	115	
Nov-05	Comicrom S.A., Chile	USD 35.5m	USD 23m	0.6	1257	Footprint in BFSI BPO market in Latam
Oct-05	FNS	USD 22m	USD 26m	1.2	190	
Oct-05	Pearl group BPO	INR 4278	INR 4261	1.0	950	Insurance BPO clients - life and pension business
May-05	SITAR	ND	INR 215.3m	NA	NA	To blue-chip european customers
May-04	Phoenix Soln	ND	INR 394.3m	NA	ND	Insurance sector expertise
May-03	AFS				400	Airline sector expertise
Oct-01	CMC Ltd	INR 6570m	51% for INR 1.5bn		3100	Business capabilities in India, Government sector
Wipro						
Dec-08	Citi Tech Svc	USD 80m	USD 127m	1.6	1650	TIS and domain led ADM services to all Citi business segments
Jul-08	Gallagher Fin Sys	N.A	USD 6m	N.A	150	Platform based BPO services for BFSI (mortgage)
Sep-07	Infocrossing	USD 232.4m	USD 600m	2.6	926	Data center and maintenance for RIM
Aug-07	Unza Hold.	USD 169m	USD 246m	1.5	4000	Personal care products in S.E. Asia
Oct-06	3D Networks-India	USD 36m	USD 23m + EO	0.6	270	Expertise in convergence solutions
Sep-06	Hydrauto	USD 112.2m	USD 30.6m	0.3	612	Expertise in hydraulic cylinders, solution for excavators, dumpers etc
Jun-06	Enabler	USD 37.7m	USD 51m + EO	1.4	300	Retek and package integration and entry into latam
Jun-06	Saraware	USD 16.8m	USD 40.4m	2.4	180	Expertise in 3G and mobile security
May-06	Quantech Global Svc	USD 12.7m	Not disclosed	NA	445	Engineering services capabilities in automotive vertical
Feb-06	cMango	USD 13m	USD 20m + EO	1.5	120	Business service management solutions from BMC
Dec-05	mPower and MPACT	USD 18m	USD 28m	1.6	300	Expertise in payment space
Dec-05	New Logic Tech	USD 17m	USD 56m	3.3	125	Wireless IP and RF space
Apr-03	NerveWire	USD 20m	USD 18.7m	0.9	90	Consulting of security services, private client, BFSI
Nov-02	American Mngmt Sys	NA	USD 26m	NA	NA	Expertise in energy vertical
Sep-02	Ericsson India (R&D)	NA	USD 5.73m	NA	NA	R&D capabilities in telecom domain
Jul-02	GE Med System's IT	NA	INR 281m	NA	NA	Expertise in healthcare vertical
Oct-01	Spectramind	NA	USD 93m	NA	NA	Entry into BPO space
HCL Tech						
Sep-08	Axon (US)	£ 204.5m	£ 440m	2.2	2500	Business Transformation consultancy for SAP
Aug-08	ControlPoint Solution	$28m (FY09E)	$20.8m (EV)	NA	211	Multi-service delivery platforms for customers with CPS' TEM expertise complementing RIM
Jul-08	Liberata Finan.Solutions	$60m in year 1	Undisclosed	NA	500	BPO service for administrative and customer services for the Life and Pensions industry.
Feb-08	CapitalStream	NA	USD40m	NA	NA	End-to-end lending and straightthrough processing solutions to BFSI in NA
Feb-05	AnswerCall Direct	NA	£ 3.9m	NA	190	To gain expertise in media and transportation verticals
Oct-04	Shipara Tech Ltd	NA	NA	NA	NA	Competency in avaiation vertical
Jul-02	Aquila	INR 30.4 m	Initial 35.5% for INR 55.5m	NA	51	To acquire engineering software & services expertise
Jun-02	Gulf Computers	NA	USD 8m	NA	NA	Business process automation and development management
Dec-01	Apollo Contact Centre	NA	USD 12.7m	NA	400	Business from BT and Entry into Europe to service other clients

CONTRACTION IN CAPITAL MARKET INVESTMENT: NOT A LESSER DEVIL

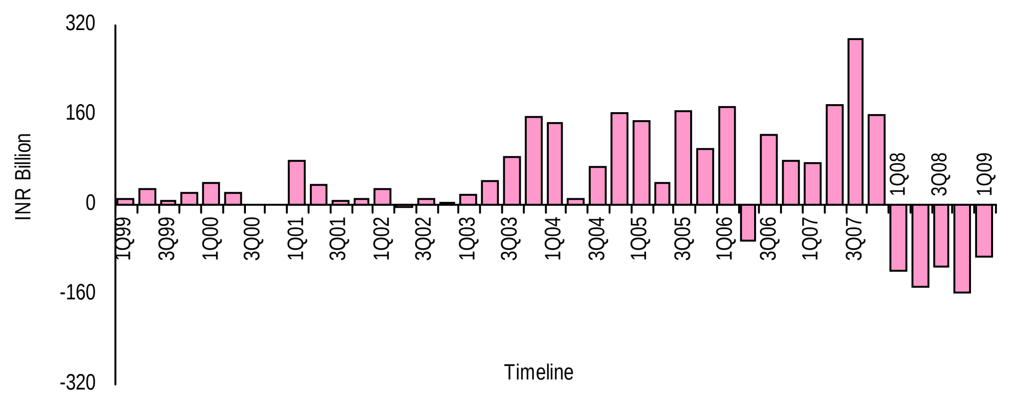
Net inflow of private capital to Emerging Markets will slow down drastically...

We believe that the situation is the worst in emerging markets. Projections from the Institute of International Finance (IIF), an industry group, show that net inflow of private capital will slow to USD165bn this year, down from a peak of USD929bn in 2007. Much of that retreat is happening in the capital markets, but the banks are fleeing fastest.

Last 5 quarters have seen steady decline in FII investment in the Indian capital market. FII has withdrawn USD13bn from the market in the last 5 quarters. Our analysis on NIFTY 50 stocks revealed that although FIIs interest have declined steadily in the last 5 quarters for non-IT companies but IT companies still remain favorite of FIIs and the interest is ever increasing. We believe that a systemic withdrawal of money by FII due to uncertainties like outcome of upcoming election, further trouble in the capital market, redemption pressure for funds etc. could affect IT stocks more as it is over-owned by FII.

FII pulling out from the Indian market...

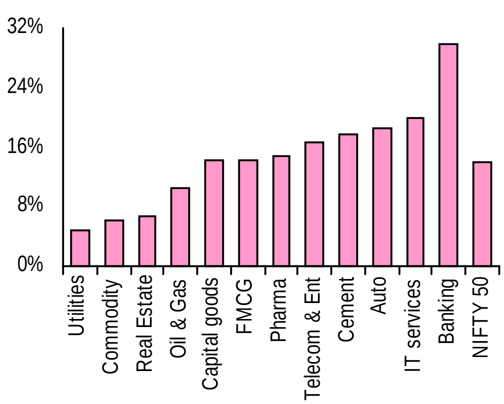
FII Inflows in the Indian capital market: negative in the last 5 quarters



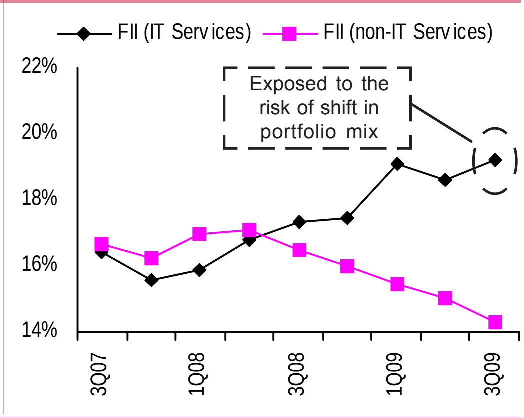
Source: PINC Research

...however have shown hightened interest in top 4 Indian IT companies over the last 7 quarters ...

% FII Holding (Nifty 50)



FII Holding Nifty vs Top 4 IT players



Source: PINC Research, SEBI

Tapering growth indicates end of long spell of riding high

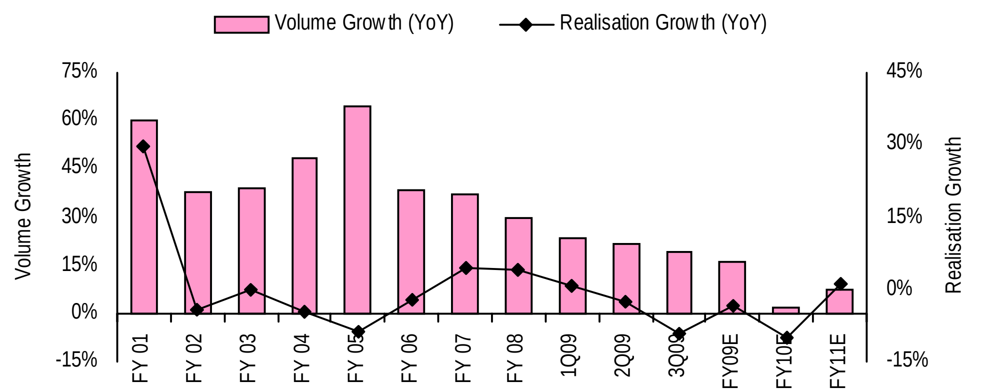
We believe that the nickel and dime (TCV < USD25mn) approach has given top 4 IT companies a strong volume growth from FY01-05 for example Infosys grew with a CAGR of 52% from FY01-05 and at a CAGR of 33% from FY05-08.

Infosys grew at a CAGR of 52% and 33% from FY01-05 and FY05-08 respectively. ...

The cost advantage of India has attracted global competitors to India providing tough competition for Indian IT companies. Global competitors like IBM, HP-EDS, Accenture and Cognizant managed to replicate the global delivery model and are giving tough competition for the low hanging fruits. We believe that due to significant decline in large transformational deal, recessionary global economy, with companies cutting down their IT budgets and significantly stiff competition from the global peers the spell of riding high growth is over.

The volume has decelerated over last 4 quarters for Indian IT companies. With multi-million dollars business transformational deals drying up and considering the multiple headwinds acting against, we expect Infosys revenue to grow at a CAGR of 12% over FY08-12E with pressure on margins.

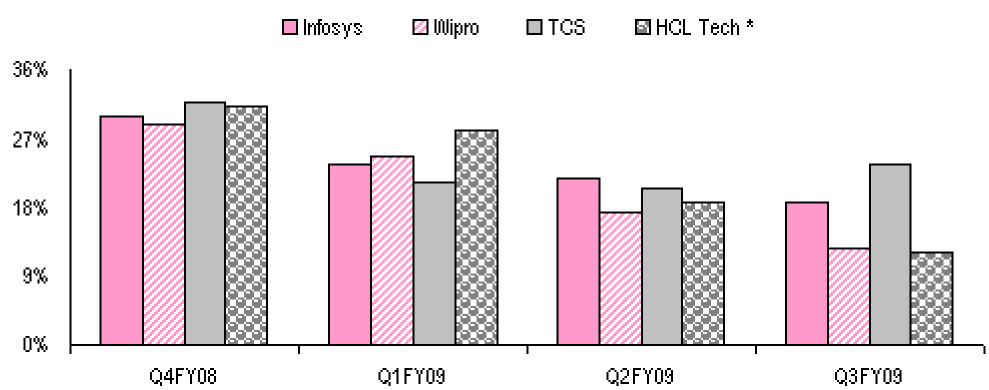
Infosys: decelerating volume growth with pressure on pricing



Source: PINC Research

Volume Growth: declining steadily over last 4 quarters

Top 4 Indian IT companies witnessed slump in volume growth ...



*Source: PINC Research, *June Year End*

FINANCIALS & GROWTH OUTLOOK: LOW VOLUME GROWTH & PRICING PRESSURE

We forecast low single digit organic growth for our coverage universe for FY10 ...

For FY10, we forecast a price decline of 5-8% for top 4 IT companies. The clients are asking for a pricing cut in the range of 5-20%. While consensus still forecast a volume growth of mid single digit, we forecast a low single digit organic growth for top 4 IT companies. We believe that Infosys could be the worst affected in terms of pricing cut. Meanwhile TCS volume growth will deteriorate following its highest exposure to BFSI exposure. We see a tough demand environment with very tight pricing scheduling by clients.

We also believe that consensus has factored in the pricing decline but has not accounted for decline in organic volume growth, which could be a possibility.

Although we do believe that vendor consolidation could benefit top 4 but very selectively. While our forecast factors in most of the bad news in its estimates but we don't rule out any major event which could provide further downside to our estimates. In case of any major jolts like Lehman collapse in October, we don't rule out further decline in volume.

Financial Valuations

	Sales (Rs mn)					CAGR (%)	EPS (Rs)					CAGR (%)
	2008	2009E	2010E	2011E	2012E	2008-12E	2008	2009E	2010E	2011E	2012E	2008-12E
Infosys	166,920.0	216,986.5	222,930.0	240,250.0	262,065.0	11.9	81.3	103.5	104.5	107.5	114.4	8.9
TCS	228,614.0	280,046.7	286,570.0	306,040.0	333,830.0	9.9	51.3	53.6	51.6	53.1	56.4	2.4
Wipro	197,428.0	258,493.0	264,912.4	293,103.0	324,418.4	13.2	22.2	24.9	24.7	24.6	26.6	4.7
HCL Tech	76,394.0	103,212.9	113,810.0	124,145.0	137,925.0	15.9	16.5	18.8	16.6	17.4	18.4	2.8

Source: PINC Research

IT companies have traded at historical PEG of less than 1.0

Historically, top 4 Indian IT companies have traded at a PEG lower than 1. Our analysis for the PEG of Infosys for both the period 2000-04 and 2004-08 has revealed PEG (calculated using 1 year rolling forward PE and rolling forward with EPS CAGR of 4 years) of 0.62 and 0.57 respectively. Infosys sales grew at a CAGR of 60.4% and 36.2% (in INR term) in the interval of 2000-04 and 2004-08 respectively. The average PE at which Infosys traded in the interval was 41.1 and 22.5 in the period of 2000-04 and 2004-08 respectively.

We forecast sales CAGR of 12.2% for period of FY08-12E and PEG of 0.82 (as it excludes bubble period). We give PE of 10x for FY10 earning for Infosys.

We are factoring a PEG of 0.9 for our target price ...

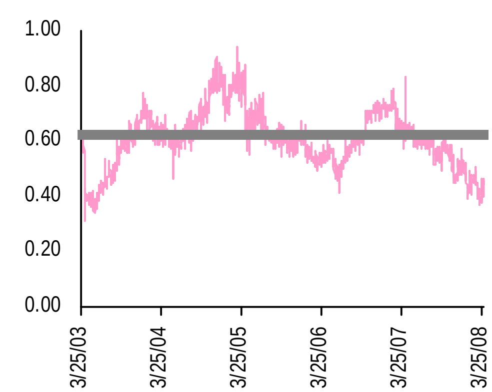
PEG Analysis: traded at PEG less than 1.0

	Avg. PEG (rolling)	Standard Deviation (ó)	PEG+1ó	PEG+2ó	PEG-1ó	PEG-2ó
2000-04	0.57	0.19	0.76	**0.95**	0.37	0.18
2004-08	0.62	0.10	0.72	**0.82**	0.52	0.43
2000-08	0.59	0.16	0.75	**0.91**	0.43	0.27

Source: PINC Research

PEG 2000-04: average PEG 0.57

PEG 2004-08: average PEG 0.62



Source: PINC Research

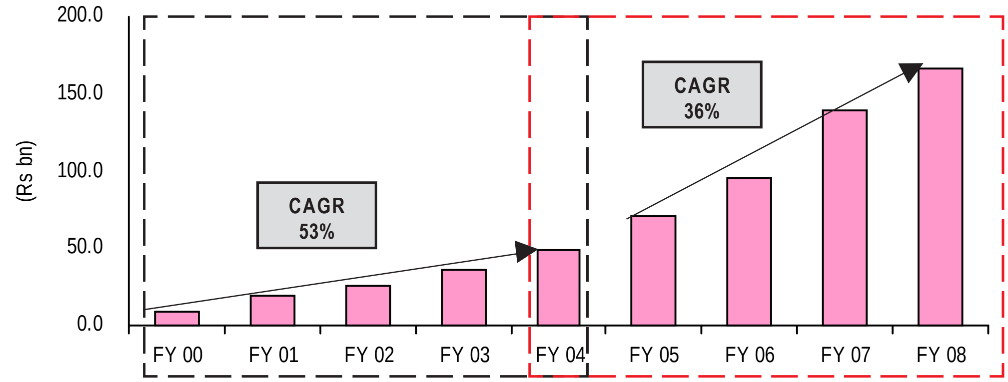
PEG 2000-08: average PEG 0.57

Source: PINC Research

PINC RESEARCH

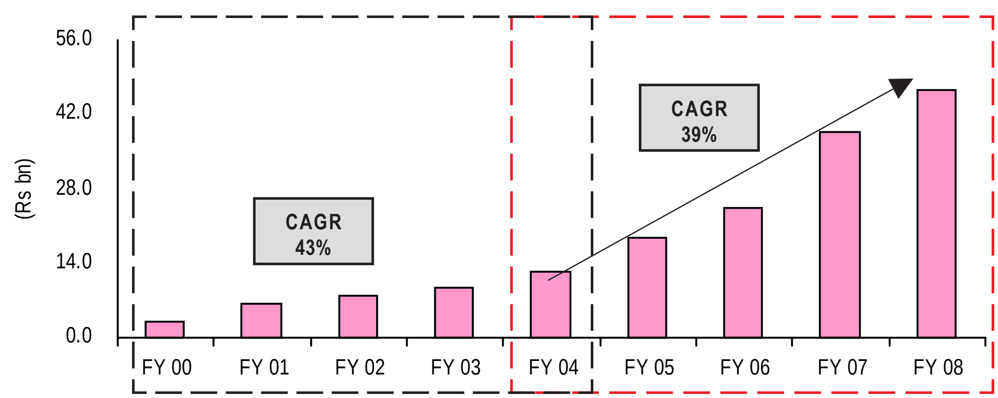
Tapering growth profile of Infosys...

Infosys - Revenue



Source: PINC Research

Infosys - PAT

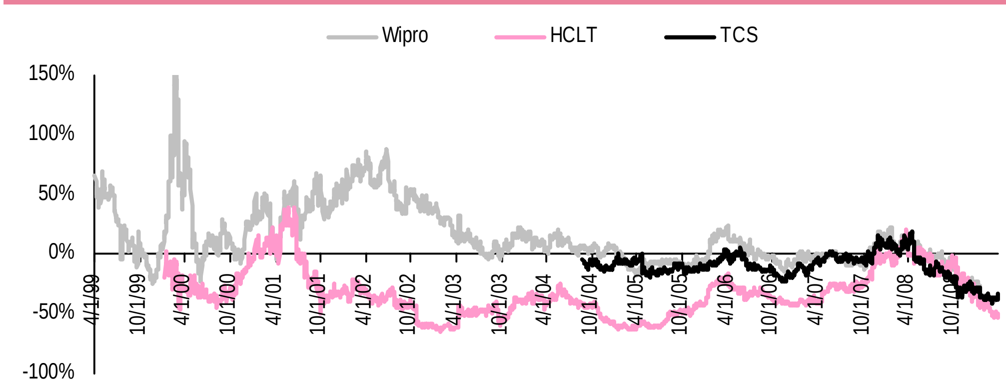


Source: PINC Research

Our analysis shows TCS, Wipro and HCL Tech is trading at discount to Infosys. We are using 10% discount for TCS and Wipro and 30% discount for HCL Tech...

TCS, Wipro and HCL have traded at discount to Infosys in last four years. According to our analysis, TCS traded at a discount of 10% whereas HCL Tech traded at a discount of 35%. We are giving a one year forward PE multiple of 9 for TCS and Wipro and HCL tech at a multiple of 6.5.

P/E Discount to Infosys



Source: PINC Research

PINC RESEARCH

Initiating Coverage

INFOSYS TECHNOLOGIES LTD.

SELL

CMP : Rs1374 TP : Rs1050 **BSE Sensex : 9,901**

We initiate coverage on Infosys with Sell rating and a target price of Rs1050, a downside of 24% from the current level. We believe that demand environment will continue to worsen during H1CY09 before it might see some respite. High BFSI and the US exposure and pricing pressure would result in flat volume growth with pressure on pricing in FY10. We have strong faith in the management's ability to sail across the tough time, but they would face short-term pressure on volume and margins.

BFSI and US exposure retards volume growth

Infosys' exposure to the US and BFSI continues to be high despite the company's effort to diversify its exposure. We are now forecasting tapering growth trajectory for the company with a volume CAGR of 7% for FY09-12E when compared to 30% for FY05-09E. We see no immediate catalyst for the earning momentum of the company. The demand environment continues to look weak.

Pricing pressure continues to mount

We believe that as contracts are renewed clients will continue to mount pressure to cut prices as they are fighting their own sets of problem of declining revenue growth and margins. We expect realization to decline by about -10% on an average, with various clients asking for 5-15% of pricing cut.

Strict focus on margin

Infosys continues to play its card with a strict vigil on margins. The company remained cautious in making acquisition. The Indian IT bellwether stands in danger of being under-cut by competitor on pricing as the days of fast growth and high profit margins disappear. The company is geared for accelerated growth; hence a decline in the sales momentum puts pressure on margin.

RISKS

- Depreciating rupee, improvement in global macro-economic outlook, Large business transformational deals and a strategic acquisition at good valuation could give impetus to earnings.

VALUATIONS

Infosys is currently trading at 13x FY10E earnings and a 3% EPS CAGR and 7% sales CAGR over FY09-12E. We initiate coverage with a Sell rating and a target price of Rs1050 with a downside of 24%.

KEY FINANCIALS Rs mn

	FY07	FY08	FY09E	FY10E	FY11E
Net Sales	138,930	166,920	216,987	222,930	240,250
YoY Gr. (%)	*45.9*	*20.1*	*30.0*	*2.7*	*7.8*
Op. Profits	43,910	52,380	71,234	70,080	73,090
OPM (%)	*31.6*	*31.4*	*32.8*	*31.4*	*30.4*
Adjusted Net Profit	38,560	46,590	59,314	59,903	61,606
YoY Gr. (%)	*56.7*	*20.8*	*27.3*	*1.0*	*2.8*
KEY RATIOS					
Dil. EPS (Rs)	67.3	81.3	103.5	104.5	107.5
ROCE (%)	34.2	33.8	31.1	26.5	23.5
RoE (%)	34.3	33.8	31.1	26.5	23.5
PER (x)	19.3	16.2	12.8	12.7	12.3
EV/Net sales (x)	5.0	4.1	3.0	2.9	2.5
EV/EBDITA (x)	15.9	13.1	9.3	9.1	8.4

01 April 2009

Shashi Bhusan
shashi.bhusan@pinc.co.in
Tel: +91-22-6618 6372

Karan Taurani
karan.taurani@pinc.co.in
Tel: +91-22-6618 6382

Jaikishan Kaurani
jaikishan.kaurani@pinc.co.in
Tel: +91-22-6618 6332

STOCK DATA

Market Cap	Rs786.9bn
Book Value per share	Rs236
Eq Shares O/S (FV Rs5)	572.8mn
Free Float	82.0%
Avg Traded Value (6 mnths)	Rs4,155mn
52 week High/Low	Rs2,017/1,040
Bloomberg Code	INFO IN
Reuters Code	INFY.BO

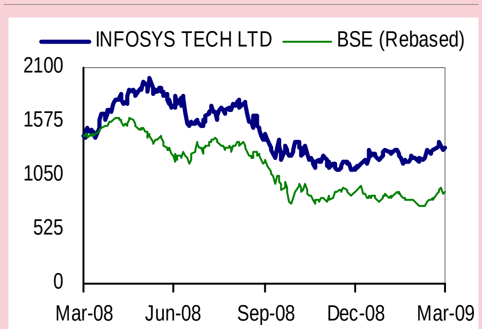
TOP SHAREHOLDERS

Name	% holding
Life Insurance Corporation of India	4.3
Oppenheimer Funds Inc	1.8
Government of Singapore	1.5
Abu Dhabi Investment Authority	1.1
ICICI Prudential	1.1
Fidelity Mgmt & Research Company	1.0

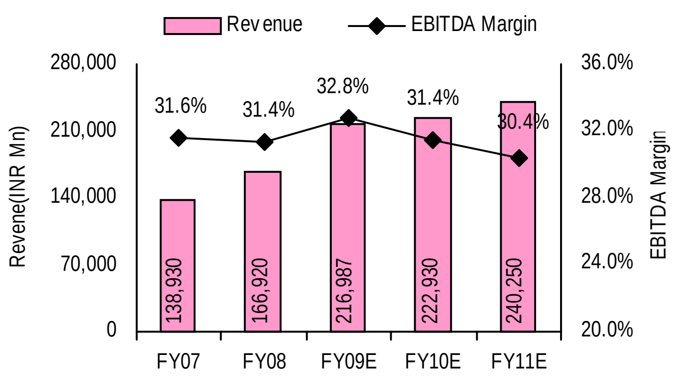
PERFORMANCE (%)

	1M	3M	12M
Absolute	12.7	19.6	(3.5)
Relative	(2.0)	19.7	52.3

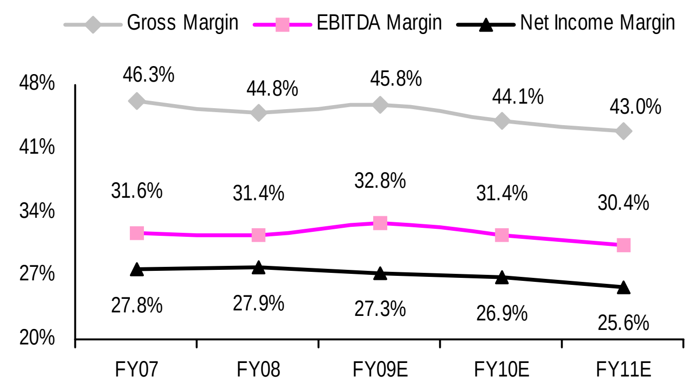
RELATIVE PERFORMANCE



Revenue / EBIDTA

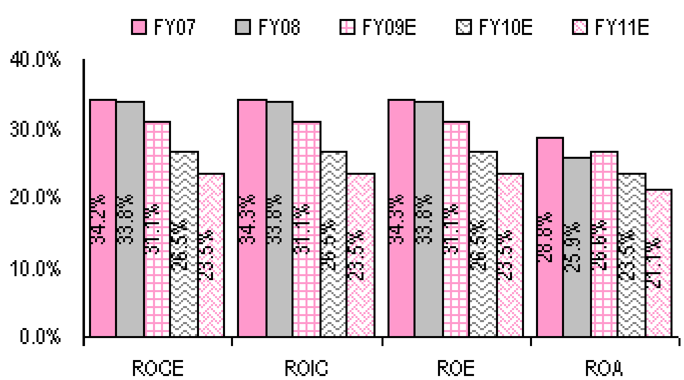


Margins

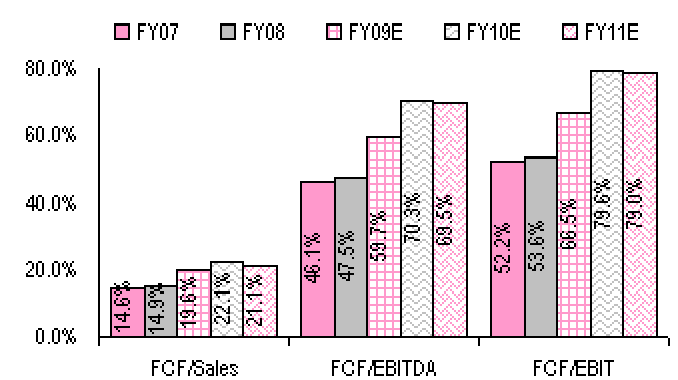


Source: PINC Research, Company Report

Return on Capital Ratios



Other Ratios

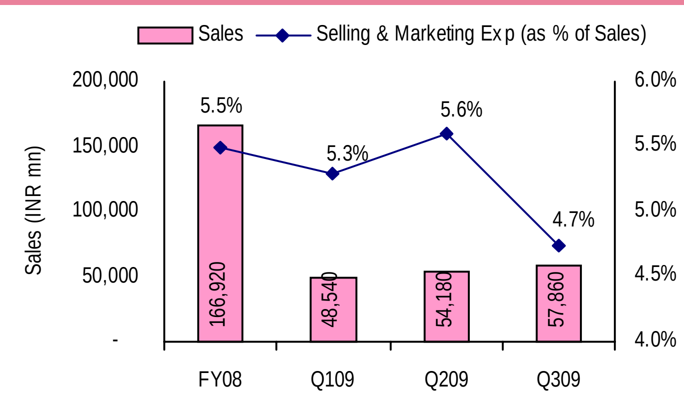


Source: PINC Research, Company Report

EPS Sensitivity

Realization Growth	Volume Growth			
	-5%	**0**	**5%**	**10%**
-10%	69.31	71.37	73.43	75.48
-5%	81.36	84.03	86.70	89.37
0%	93.42	96.70	99.98	103.26
5%	105.47	109.37	113.26	117.15

Clamp-down on S&M cost



Source: PINC Research, Company Reports

Year Ended March (Figures in Rs mn)

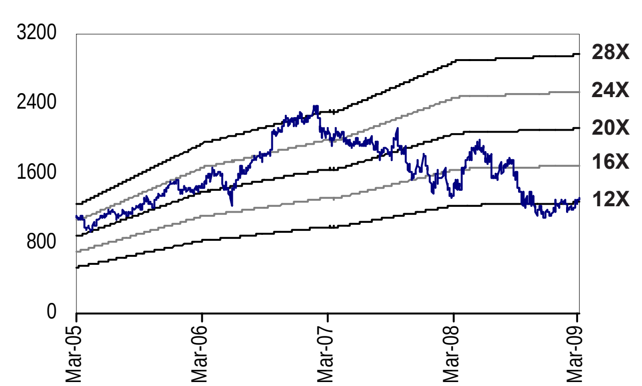
Income Statement	FY07	FY08	FY09E	FY10E	FY11E
Net sales	**1,38,930**	**1,66,920**	**2,16,987**	**2,22,930**	**2,40,250**
Growth (%)	*45.9*	*20.1*	*30.0*	*2.7*	*7.8*
Gross profit	**64,350**	**74,850**	**99,275**	**98,215**	**103,373**
Other operating charges	20,440	22,470	28,041	28,135	30,283
EBITDA	**43,910**	**52,380**	**71,234**	**70,080**	**73,090**
Growth (%)	*42.0*	*19.3*	*36.0*	*(1.6)*	*4.3*
Depreciation	5,140	5,980	7,262	8,187	8,801
Other income	3,700	7,040	4,010	8,581	14,693
EBIT	**42,470**	**53,440**	**67,982**	**70,475**	**78,982**
Interest paid	-	-	-	-	-
PBT (before E/o items)	**42,470**	**53,440**	**67,982**	**70,475**	**78,982**
Tax Provision	3,860	7,070	8,838	10,571	17,376
E/o loss / (Income)	50	-	-	-	-
Net profit	**38,610**	**46,590**	**59,314**	**59,903**	**61,606**
Adjusted net profit	**38,560**	**46,590**	**59,314**	**59,903**	**61,606**
Growth (%)	*56.7*	*20.8*	*27.3*	*1.0*	*2.8*
Diluted EPS (Rs)	**67**	**81.3**	**103.5**	**104.5**	**107.5**
Diluted EPS Growth (%)	53.7	20.7	27.3	1.0	2.8

Cash Flow Statement	FY07	FY08	FY09E	FY10E	FY11E
Pre-tax profit	42,470	53,440	67,982	70,475	78,982
Depreciation	5,140	5,980	7,262	8,187	8,801
Total tax paid	(4,460)	(5,490)	(8,838)	(10,571)	(17,376)
Chg in working capital	(4,770)	(6,100)	(5,418)	(8,390)	(8,215)
Other operating activities	(3,170)	(7,000)	(5,420)	-	-
Cash flow from operat. (a)	**35,210**	**40,830**	**55,568**	**59,700**	**62,191**
Capital expenditure	(14,960)	(15,950)	(13,019)	(10,433)	(11,412)
Chg in investments	800	(710)	(1,210)	-	-
Other investing activities	2,950	5,460	7,830	-	-
Cash flow from inv. (b)	**(11,210)**	**(11,200)**	**(6,399)**	**(10,433)**	**(11,412)**
Free cash flow (a+b)	24,000	29,630	49,169	49,267	50,780
Equity raised/(repaid)	12,160	580	480	-	-
Debt raised/(repaid)	-	-	-	-	-
Change in Minorities Interest	-	-	-	-	-
Dividend (incl. tax)	(15,320)	(8,350)	(24,930)	(24,913)	(24,913)
Other financing activities	-	(11,110)	2,600	-	-
Cash flow from finan. (c)	**(3,160)**	**(18,880)**	**(21,850)**	**(24,913)**	**(24,913)**
Net chg in cash (a+b+c)	**20,840**	**10,750**	**27,319**	**24,355**	**25,867**

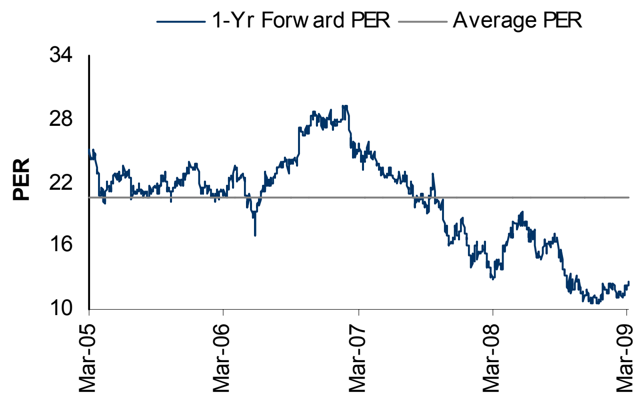
Balance Sheet	FY07	FY08	FY09E	FY10E	FY11E
Equity Share Capital	2,860	2,860	2,860	2,860	2,860
Reserves & surplus	109,690	135,090	187,864	222,855	259,548
Shareholders' funds	112,550	137,950	190,724	225,715	262,408
Minorities interests	40	-	-	-	-
Total Debt	-	-	-	-	-
Capital Employed	1,12,590	1,37,950	1,90,724	2,25,715	2,62,408
Net fixed assets	37,710	47,770	55,156	59,929	63,579
Cash & Cash Eq.	58,340	69,500	96,539	1,20,894	1,46,760
Net Other Current Assets	15,370	18,770	35,669	41,532	48,708
Investments	250	720	1,980	1,980	1,980
Net Deferred Tax Assets	920	1,190	1,380	1,380	1,380
Total assets	1,12,590	1,37,950	1,90,724	2,25,715	2,62,408

Key Ratios	FY07	FY08	FY09E	FY10E	FY11E
OPM (%)	32%	31%	33%	31%	30%
Net margin (%)	28%	28%	27%	27%	26%
Yield (%)	2%	1%	3%	3%	3%
Net debt/Equity (x)	-	-	-	-	-
Net Working Capital (days)	66	70	78	90	96
Asset turnover (x)	1.0	0.9	1.0	0.9	0.8
ROCE (%)	34%	34%	31%	27%	23%
RoE (%)	34%	34%	31%	27%	23%
EV/Net sales (x)	5.1	4.1	3.1	2.9	2.6
EV/EBITDA (x)	16.0	13.1	9.3	9.1	8.4
PER (x)	19.3	16.2	12.8	12.7	12.4
Price/Book (x)	7	5	4	3	3

P/E Band



Average PE



PINC RESEARCH

Initiating Coverage

TCS LTD.

SELL

CMP : Rs545 TP : Rs460

BSE Sensex : 9,901

We initiate coverage on TCS with Sell rating with a target price of INR460 a downside of 15% from the current level. We believe that high exposure to BFSI and the US would put pressure on pricing with flat volume growth. We believe that TCS' management would drive the company out of the troubled time but in near term we expect pressure on pricing and volume growth.

Worrying growth outlook for FY10

TCS has got the highest exposure to BFSI sector among the top 4 IT players, exposing them to the risk of deepening Banking crisis. BFSI continues to contribute 42% and the US contributes 52% of total revenue. Both of these are under severe strain in the current market environment. The project cancellation which happened in Q3FY09 will see its full blown impact in Q4FY09 and FY10.

Margin levers should be played cautiously

TCS is trying to contain cost by boosting efficiency and increasing working hours of employee by 10%. TCS is also looking at tweaking variable pay up to 35% of an employee's salary. With TCS cutting down incentive based salary, it could possibly become difficult to retain talent putting them in vicious cycle of declining growth and cost containment.

Lowest cash to market capitalization and high on receivables

TCS has about 4% of cash to market capitalization lowest among peers, Infosys has 11.5% and Wipro has 16% Although TCS has strong ability to generate the free cash flow from operation with FCF/EBITDA of 48%, but a prolonged weakness in the demand environment could put strain on the business. TCS has got highest DSO of about 77 days when compared Infosys (55) and Wipro (66). Also, receivables as a percentage of total assets are the highest for TCS at 29% whereas Infosys and Wipro have 17%. The uncertainty of the business environment today makes these high receivables numbers looks like earning at risk.

RISKS

- Depreciating rupee, improvement in global macro-economic outlook, Large business transformational deals and a strategic acquisition at good valuation could give impetus to earnings.

VALUATIONS

TCS is currently trading at 11x FY10E earnings and a 2% EPS CAGR and 6% sales CAGR over FY09-12E. We initiate coverage with a Sell rating and a target price of Rs460 with a downside of 15%.

KEY FINANCIALS (Rs mn)

	FY07	FY08	FY09E	FY10E	FY11E
Net Sales	186,332	228,614	280,047	286,570	306,040
YoY Gr. (%)	*40.7*	*22.7*	*22.5*	*2.3*	*6.8*
Op. Profits	46,445	53,651	68,260	60,453	63,268
OPM (%)	*24.9*	*23.5*	*24.4*	*21.1*	*20.7*
Adjusted Net Profit	41,315	50,191	52,418	50,460	52,002
YoY Gr. (%)	*43.3*	*21.5*	*4.4*	*(3.7)*	*3.1*
KEY RATIOS					
Dil. EPS (Rs)	42.2	51.3	53.6	51.6	53.1
ROCE (%)	47.1	40.2	40.9	30.0	26.6
RoE (%)	46.4	40.4	32.6	25.8	22.4
PER (x)	12.8	10.5	10.1	10.5	10.2
EV/Net sales (x)	2.9	2.3	1.9	1.7	1.5
EV/EBDITA (x)	10.5	9.1	7.0	7.3	6.4

01 April 2009

Shashi Bhusan
shashi.bhusan@pinc.co.in
Tel: +91-22-6618 6372

Karan Taurani
karan.taurani@pinc.co.in
Tel: +91-22-6618 6382

Jaikishan Kaurani
jaikishan.kaurani@pinc.co.in
Tel: +91-22-6618 6332

STOCK DATA

Market Cap	Rs532.8bn
Book Value per share	Rs111.4
Eq Shares O/S (FV Rs1)	978.6mn
Free Float	24%
Avg Traded Value (6 mnths)	Rs1,615mn
52 week High/Low	Rs1,054/418
Bloomberg Code	TCS IN
Reuters Code	TCS.BO

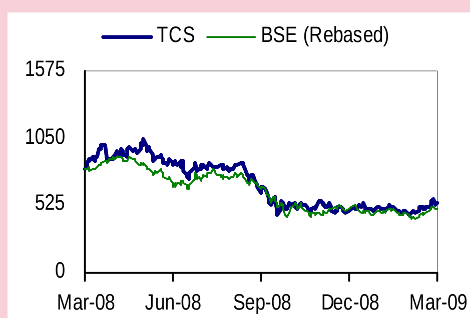
TOP SHAREHOLDERS

Name	% holding
Life Insurance Corporation of India	2.3
HSBC Global Investment Funds	1.1

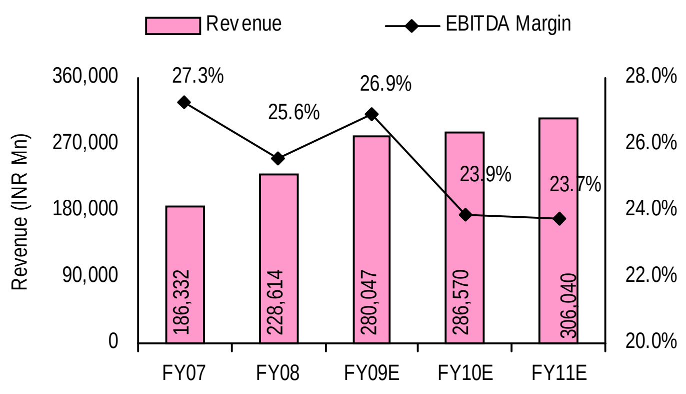
PERFORMANCE (%)

	1M	3M	12M
Absolute	18.4	9.6	(34.6)
Relative	2.9	9.6	3.2

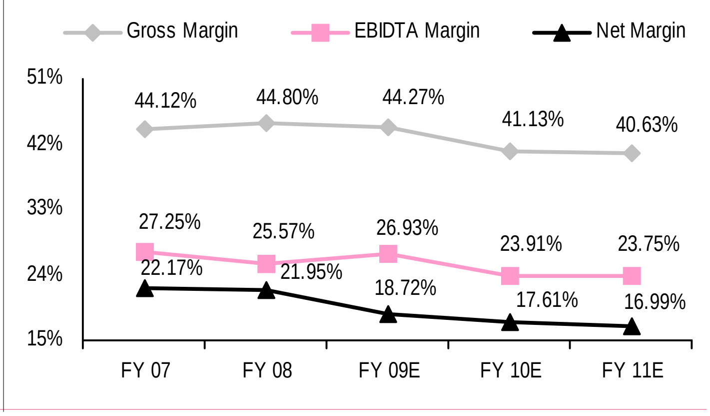
RELATIVE PERFORMANCE



Revenue / EBIDTA

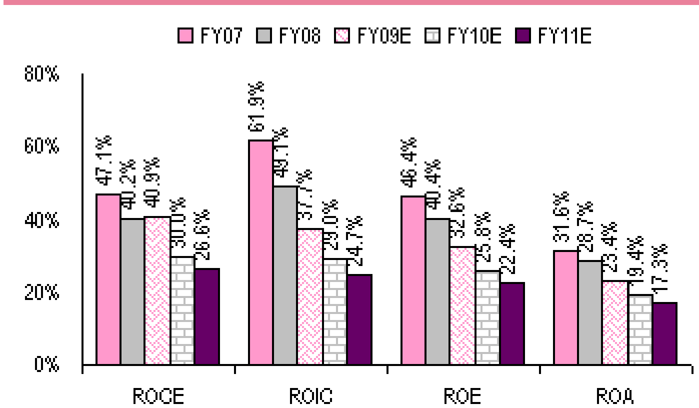


Margins

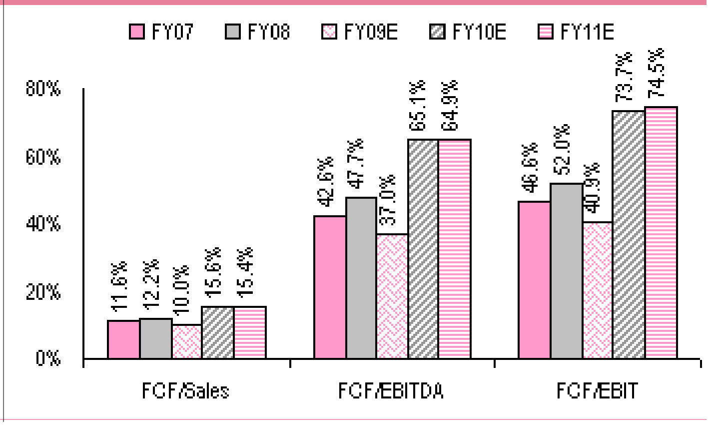


Source: PINC Research

Return on Capital Ratios



Other Ratios



Source: PINC Research

EPS Sensitivity

Realization Growth	Volume Growth			
	-5%	0	5%	10%
-10%	31.69	33.89	36.10	38.30
-5%	42.23	44.99	47.75	50.52
0%	52.76	52.38	55.70	59.02
5%	55.82	59.71	63.59	67.47

Lowest cash to market cap

	Cash (a)	Market Capitalizat. (b)	a/b (%)	DSO	Recievables/ Total Assets
Infosys	86,610	770,399.0	11.2%	55.4	17.1%
TCS	21,610	562,554.5	3.8%	77.4	28.6%
Wipro	58,954	370,443.9	15.9%	65.6	17.4%
HCLT	20,265	70,258.0	28.8%	97.3	21.1%

Source: Company Reports, PINC Research

Year Ended March (Figures in Rs mn)

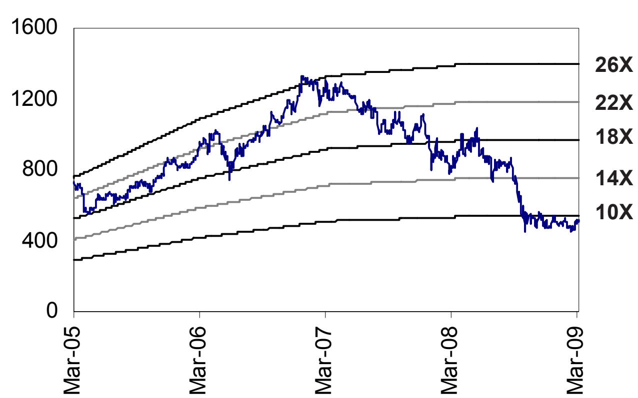
Income Statement	FY07	FY08	FY09E	FY10E	FY11E
Net sales	**186,332**	**228,614**	**280,047**	**286,570**	**306,040**
Growth (%)	*41*	*23*	*22*	*2*	*7*
Gross profit	**82,206**	**102,420**	**123,974**	**117,859**	**124,350**
Other operating charges	31,426	43,958	48,553	49,351	51,668
EBITDA	**50,780**	**58,462**	**75,421**	**68,508**	**72,682**
Growth (%)	*42*	*15*	*29*	*(9)*	*6*
Depreciation	4,335	4,811	7,160	8,055	9,414
Other income	2,181	4,902	(5,079)	1,632	3,161
EBIT	**48,389**	**58,101**	**62,815**	**62,085**	**66,429**
Interest paid	237	452	366	-	-
PBT (before E/o items)	**48,389**	**58,101**	**62,815**	**62,085**	**66,429**
Tax provision	6,700	7,494	9,956	11,175	13,950
E/o Income / (loss)	373	416	441	450	477
Net profit	**41,688**	**50,607**	**52,859**	**50,910**	**52,479**
Adjusted net profit	**41,315**	**50,191**	**52,418**	**50,460**	**52,002**
Growth (%)	*43*	*21*	*4*	*(4)*	*3*
Diluted EPS (Rs)	**42.2**	**51.3**	**53.6**	**51.6**	**53.1**
Diluted EPS Growth (%)	43	21	4	(4)	3

Cash Flow Statement	FY07	FY08	FY09E	FY10E	FY11E
Pre-tax profit	-	-	-	-	-
Depreciation	-	-	-	-	-
Total tax paid	-	-	-	-	-
Chg in working capital	-	-	-	-	-
Other operating activities	-	-	-	-	-
Cash flow from oper. (a)	**33,976**	**40,312**	**39,385**	**57,462**	**59,392**
Capital expenditure	(12,324)	(12,430)	(11,482)	(12,896)	(12,242)
Chg in investments	(157,807)	(287,263)	(281,298)	-	-
Other investing activities	151,629	272,294	269,727	-	-
Cash flow from inv. (b)	**(18,501)**	**(27,399)**	**(23,053)**	**(12,896)**	**(12,242)**
Free cash flow (a+b)	15,474	12,913	16,332	44,567	47,150
Equity raised/(repaid)	211	33	26	-	-
Debt raised/(repaid)	3,949	718	(347)	-	-
Chg in Minorities int.	-	-	-	-	-
Dividend (incl. tax)	(10,921)	(14,953)	(16,125)	(16,147)	(16,147)
Other financing activities	-	-	-	-	1
Cash flow from fin. (c)	**(6,761)**	**(14,202)**	**(16,446)**	**(16,147)**	**(16,146)**
Net chg in cash (a+b+c)	**8,714**	**(1,289)**	**(114)**	**28,420**	**31,004**

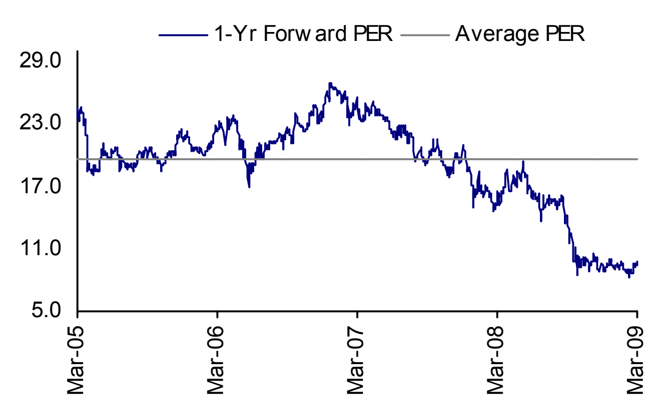
Balance Sheet	FY07	FY08	FY09E	FY10E	FY11E
Equity Share Capital	25,351	26,351	26,351	26,351	26,351
Reserves & surplus	64,310	98,469	130,946	165,709	202,041
Shareholders' funds	**89,661**	**124,819**	**157,296**	**192,059**	**228,391**
Minorities interests	2,121	2,300	2,892	2,892	2,892
Total Debt	6,906	6,483	6,896	6,896	6,896
Capital Employed	**98,688**	**133,602**	**167,083**	**201,847**	**238,179**
Net fixed assets	43,084	55,351	97,888	102,729	105,557
Cash & Cash Eq.	12,291	10,352	14,797	43,216	74,219
Net other Current Assets	30,601	41,397	47,646	49,149	51,649
Investments	12,711	26,503	6,752	6,752	6,752
Net Deferred Tax Assets	-	-	-	-	-
Total assets	**98,688**	**133,602**	**167,083**	**201,847**	**238,179**

Key Ratios	FY07	FY08	FY09E	FY10E	FY11E
OPM (%)	24.9	23.5	24.4	21.1	20.7
Net margin (%)	22.2	22.0	18.7	17.6	17.0
Dividend yield (%)	2.1	2.9	3.2	3.2	3.2
Net debt/Equity (x)	0.1	0.0	0.0	0.0	0.0
Net Working Capital (days)	60	66	62	63	62
Asset turnover (x)	1.4	1.3	1.3	1.1	1.0
ROCE (%)	47.1	40.2	40.9	30.0	26.6
RoE (%)	46.4	40.4	32.6	25.8	22.4
EV/Net sales (x)	2.8	2.2	1.8	1.7	1.5
EV/EBITDA (x)	10.5	9.1	7.0	7.3	6.4
PER (x)	12.8	10.5	10.1	10.5	10.2
Price/Book (x)	5.8	4.2	3.3	2.7	2.3

P/E Band



Average P/E



Initiating Coverage

WIPRO LTD.

HOLD

CMP : Rs252 TP : Rs225 **BSE Sensex : 9,901**

We initiate coverage on Wipro with Hold rating with a target price of Rs225. We believe that string of pearls acquisition strategy has helped Wipro build some of the key capabilities. Also a proactive cost control measures helped them maintaining margin.

Strategic string of pearls acquisitions could play trick

Wipro has made the highest number of acquisitions among top 4 Indian IT companies. USD600mn acquisition of Infocrossing in 2007 has helped Wipro to leverage its remote infrastructure management expertise against Infocrossing's offering. According to the Everest Research Institute, the RIM outsourcing market to touch $5.9 billion in 2009 and $8.6 billion in 2010.

Proactive cost control and strong EM focus

Wipro was the first to put freeze on hiring process in Q1FY09. Wipro has the lowest net addition of -1,500 employees on YTD basis when compared to Infosys (12,000) and TCS (19,000). We believe a proactive approach has helped Wipro in containing the cost. Wipro has got highest 14% of revenue from APac, the highest among its peers. Wipro has got highest share of 8.1% of Indian IT outsourcing space, a close second to IBM that has 10% market share.

Limited near term catalyst

Wipro earning is exposed to the same macro to which other Indian IT services are exposed but we believe that Technology Infrastructure Services, which contributes about 19% of revenue, are sticky in nature. Also, Wipro has got the highest contribution Application Development and Package implementation (55% of total revenue) when compared to its top 3 Indian peers that is high margin business. We do believe that in the near term we can't envisage any earning catalyst, but we do believe in the up-cycle Wipro has got high margin levers to play with.

RISKS

- Depreciating rupee, improvement in global macro-economic outlook, and large business transformational deals.

VALUATIONS

Wipro is currently trading at 10x FY10E earnings with sales CAGR of 8% over FY09-12E. We initiate coverage with a Hold rating and a target price of Rs225.

KEY FINANCIALS Rs mn

	FY07	FY08	FY09E	FY10E	FY11E
Net Sales	149,433	197,428	258,493	264,912	293,103
YoY Gr. (%)	*40.8*	*32.1*	*30.9*	*2.5*	*10.6*
Op. Profits	30,153	33,565	44,460	39,434	40,713
OPM (%)	*20.2*	*17.0*	*17.2*	*14.9*	*13.9*
Adjusted Net Profit	29,170	32,241	36,194	35,987	35,822
YoY Gr. (%)	*43.9*	*10.5*	*12.3*	*(0.6)*	*(0.5)*
KEY RATIOS					
Dil. EPS (Rs)	20.2	22.2	24.9	24.7	24.6
ROCE (%)	29.2	22.9	25.1	18.9	17.9
RoE (%)	28.8	24.7	22.4	18.8	16.9
PER (x)	12.0	11.0	9.8	9.9	9.9
EV/Net sales (x)	2.3	1.7	1.3	1.2	1.0
EV/EBDITA (x)	10.1	8.4	6.3	6.1	5.8

01 April 2009

Shashi Bhusan
shashi.bhusan@pinc.co.in
Tel: +91-22-6618 6372

Karan Taurani
karan.taurani@pinc.co.in
Tel: +91-22-6618 6382

Jaikishan Kaurani
jaikishan.kaurani@pinc.co.in
Tel: +91-22-6618 6332

STOCK DATA

Market Cap	Rs369.4bn
Book Value per share	Rs78.9
Eq Shares O/S (FV Rs5)	1463.9mn
Free Float	25.9%
Avg Traded Value (6 mnths)	Rs770mn
52 week High/Low	Rs538/182
Bloomberg Code	WPRO IN
Reuters Code	WIPR.BO

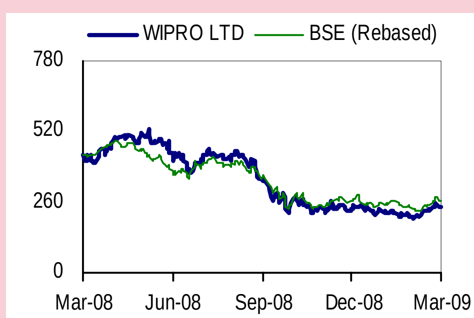
TOP SHAREHOLDERS

Name	% holding
HSBC Global Investment Funds	1.8
Life Insurance Corporation of India	1.3

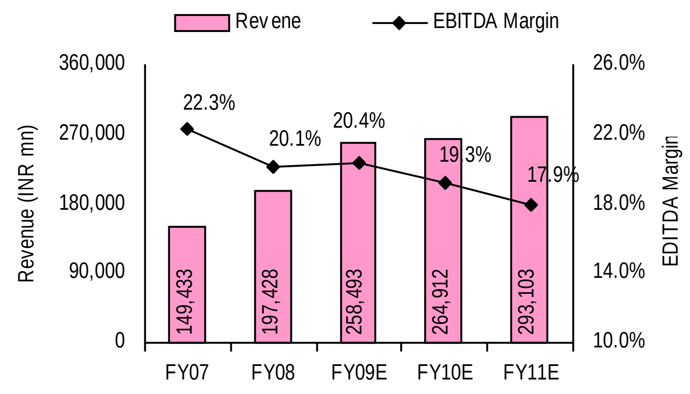
PERFORMANCE (%)

	1M	3M	12M
Absolute	24.1	1.7	(38.3)
Relative	7.9	1.7	(2.7)

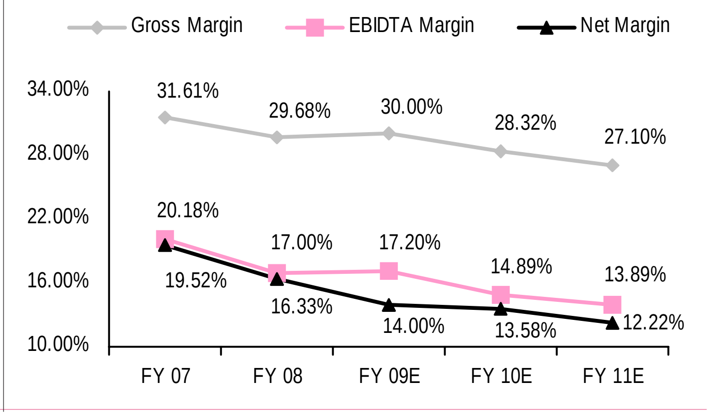
RELATIVE PERFORMANCE



Revenue / EBIDTA

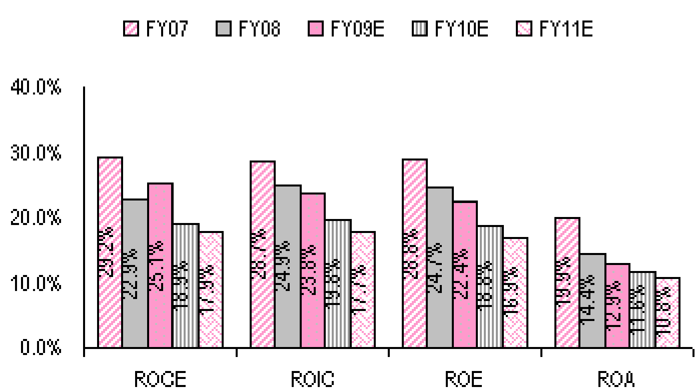


Margins

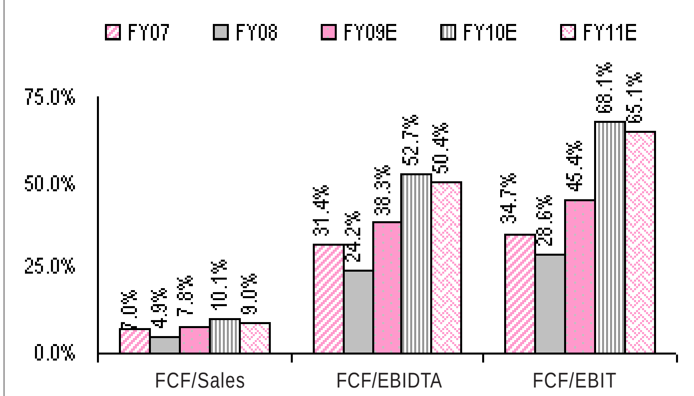


Source: Company Report

Return on Capital Ratios

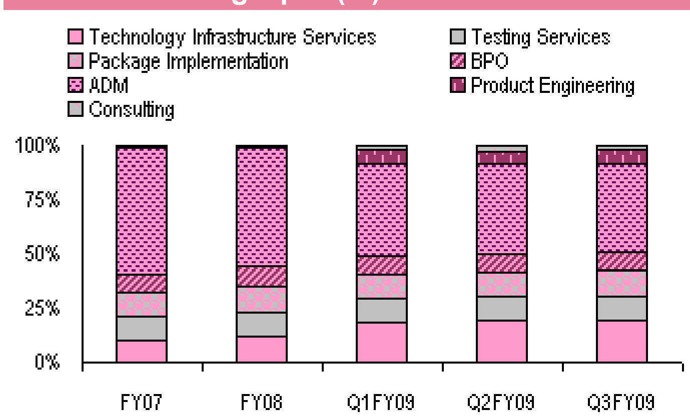


Other Ratios

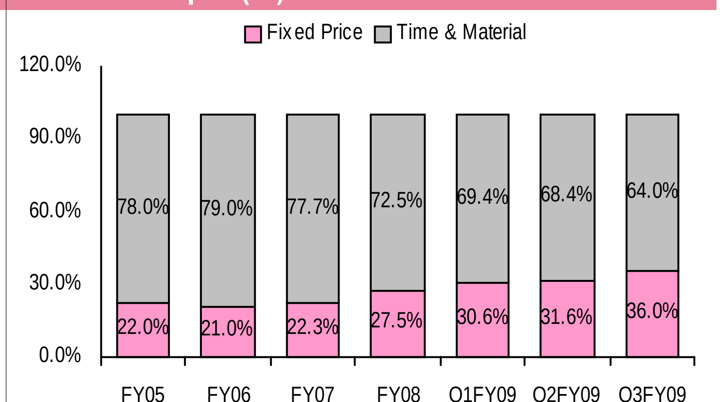


Source: Company Report

Service Offering Split (%)



Contract Split (%)



Source: Company Report

Wipro Ltd.

Year Ended March (Figures in Rs mn)

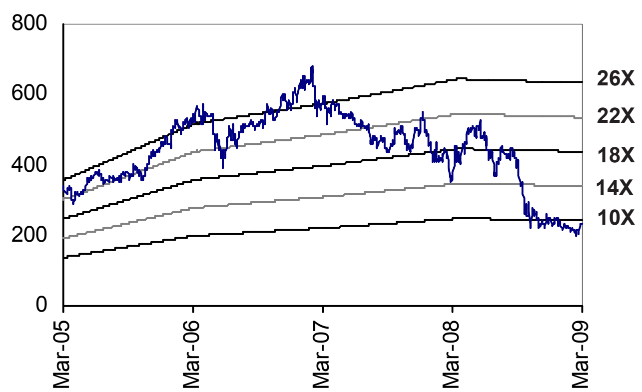
Income Statement	FY07	FY08	FY09E	FY10E	FY11E
Net sales	**149,433**	**197,428**	**258,493**	**264,912**	**293,103**
Growth (%)	*41*	*32*	*31*	*2*	*11*
Gross profit	**47,233**	**58,597**	**77,560**	**75,017**	**79,417**
Other operating charges	13,910	18,966	24,888	24,007	26,879
EBITDA	**33,323**	**39,631**	**52,672**	**51,010**	**52,538**
Growth (%)	*31*	*19*	*33*	*(3)*	*3*
Depreciation	3,170	6,066	8,212	11,577	11,825
Other income	2,667	2,167	(91)	6,379	7,218
EBIT	**32,536**	**35,881**	**40,731**	**42,044**	**45,028**
Interest paid	-	-	-	-	-
PBT (before E/o items)	**32,536**	**35,881**	**40,731**	**42,044**	**45,028**
Tax provision	3,723	3,873	4,888	6,307	9,456
E/o Income / (loss)	357	233	350	250	250
Net profit	**28,813**	**32,008**	**35,844**	**35,737**	**35,572**
Adjusted net profit	**29,170**	**32,241**	**36,194**	**35,987**	**35,822**
Growth (%)	*44*	*11*	*12*	*(1)*	-
Diluted EPS (Rs)	**20.2**	**22.2**	**24.9**	**24.7**	**24.6**
Diluted EPS Growth (%)	42	10	12	(1)	-

Cash Flow Statement	FY07	FY08	FY09E	FY10E	FY11E
Profit After Tax	20,555	32,241	36,194	37,089	35,822
Depreciation	3,170	6,066	8,212	11,577	11,825
Total tax paid	-	-	-	-	-
Chg in working capital	(5,541)	(13,256)	(4,757)	(6,076)	(5,852)
Other operating activities	515	(783)	(2,676)	2,820	2,296
Cash flow from oper. (a)	**18,699**	**24,268**	**36,973**	**45,410**	**44,091**
Capital expenditure	(8,228)	(14,673)	(16,802)	(18,544)	(17,586)
Chg in investments	(84,092)	(231,684)	(268,762)	-	-
Other investing activities	69,488	217,975	262,867	-	-
Cash flow from inv. (b)	**(22,832)**	**(28,382)**	**(22,697)**	**(18,544)**	**(17,586)**
Free cash flow (a+b)	(4,133)	(4,114)	14,276	26,866	26,505
Equity raised/(repaid)	3,905	749	343	-	-
Debt raised/(repaid)	1,429	35,589	(4,265)	-	-
Chg in Minorities int.	-	-	-	-	-
Dividend (incl. tax)	(8,123)	(5,404)	(6,828)	(6,834)	(15,994)
Other financing activities	17,746	(7,170)	18	-	-
Cash flow from fin. (c)	**14,957**	**23,764**	**(10,732)**	**(6,834)**	**(15,994)**
Net chg in cash (a+b+c)	**10,824**	**19,650**	**3,544**	**20,032**	**10,511**

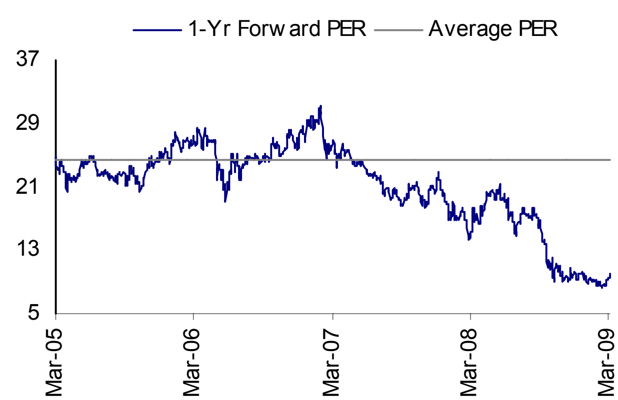
Balance Sheet	FY07	FY08	FY09E	FY10E	FY11E
Equity Share Capital	27,426	29,364	30,968	30,968	30,968
Reserves & surplus	74,042	100,003	120,794	151,048	170,876
Shareholders' funds	**101,468**	**129,367**	**151,762**	**182,016**	**201,844**
Minorities interests	-	114	192	192	192
Total Debt	1,794	17,281	25,003	25,948	25,948
Capital Employed	**103,262**	**146,762**	**176,957**	**208,156**	**227,984**
Net fixed assets	43,918	93,260	115,289	120,381	123,846
Cash & Cash Eq.	19,650	39,270	43,301	63,333	73,844
Net other Current Assets	38,095	12,534	16,346	22,422	28,274
Investments	1,599	1,698	1,965	1,965	1,965
Net Deferred Tax Assets	-	-	56	56	56
Total assets	**103,262**	**146,762**	**176,957**	**208,156**	**227,984**

Key Ratios	FY07	FY08	FY09E	FY10E	FY11E
OPM (%)	20.2	17.0	17.2	14.9	13.9
Net margin (%)	19.5	16.3	14.0	13.6	12.2
Dividend yield (%)	2.3	1.5	1.9	1.9	4.5
Net debt/Equity (x)	0.0	0.1	0.1	0.1	0.1
Net Working Capital (days)	93	23	23	31	35
Asset turnover (x)	1.0	0.9	0.9	0.9	0.9
ROCE (%)	29.2	22.9	25.1	18.9	17.9
RoE (%)	28.8	24.7	22.4	18.8	16.9
EV/Net sales (x)	2.3	1.7	1.3	1.2	1.0
EV/EBITDA (x)	13.7	10.1	8.4	6.3	6.1
PER (x)	12.0	11.0	9.8	9.9	9.9
Price/Book (x)	3.5	2.8	2.3	2.0	1.8

P/E Band



Average P/E



Initiating Coverage

HCL TECHNOLOGIES LTD.

HOLD

CMP : Rs101 TP : Rs100 **BSE Sensex : 9,901**

We initiate coverage on HCL Tech with Hold rating with a target price of Rs100. We believe that lower exposure to BFSI, telecom and retail would shield the earning from any downside risk. Also the acquisition of Axon would provide some cross-selling opportunity. The stock has corrected by 60% since the news of acquisition and is currently trading at 50% discount to Infosys.

Low BFSI, telecom and retail exposure shield earning risk

Among the top 4 Indian IT services company, HCL Tech has lowest exposure to BFSI, telecom and retail exposure, which shield its earning volatility risk. HCL Tech drives 27% from BFSI vertical, 16% from telecom and 8% from retail, lowest among its peers, providing stablity in its earning environment.

Acquisition provides cross selling and downstream opportunity

We believe that acquisition of Axon would not only build ADM capability but also strengthen consulting business. It provides strong opportunity of cross selling and downstream revenues. Axon strong presence in Europe and government contracts provides some immunity from current recessionary evnironment and diversifies risk. In Q3FY09 Axon would contribute US$93mn to the top-line. We believe that in this tough environment Axon would help HCL Tech win some clients.

Financial risk in the price

HCL Tech raised USD 585mn bridge loan facility for the acquisition of Axon. HCL tech is paying 300bps plus 3 months Libor (4.25%) on the deb . The bridge loan facility is valid till December 2009. The company has got strong operational leverage and generated FCF/EBITDA of about 49% in FY08. We believe that company's ability to generate cash would help them raise the debt as credit market eases. The company has got the highest dividend yield among its peer of 8% when compared to 3% for Infosys and TCS and 2% for Wipro.

RISKS

- Depreciating rupee, improvement in global macro-economic outlook, and large business transformational deals. Further tightening of the credit market could make situation worse.

VALUATIONS

We initiate coverage on HCL Tech with Hold rating and a target price of Rs100. HCL Tech is currently trading at 6x FY10E earnings with sales CAGR of 10% over FY09-12E.

KEY FINANCIALS Rs mn

	FY07	FY08	FY09E	FY10E	FY11E
Net Sales	60,337	76,394	103,213	113,810	124,145
YoY Gr. (%)	*37.1*	*26.6*	*35.1*	*10.3*	*9.1*
Op. Profits	13,371	16,939	21,199	20,418	21,388
OPM (%)	*22.2*	*22.2*	*20.5*	*17.9*	*17.2*
Adjusted Net Profit	13,549	11,245	12,605	11,128	11,694
YoY Gr. (%)	*74.9*	*(17.0)*	*12.1*	*(11.7)*	*5.1*
KEY RATIOS					
Dil. EPS (Rs)	19.8	16.5	18.8	16.6	17.4
ROCE (%)	25.9	29.0	22.6	20.6	20.4
RoE (%)	27.0	21.6	23.3	18.8	18.1
PER (x)	4.9	6.0	5.4	6.1	5.8
EV/Net sales (x)	1.1	0.9	0.4	0.3	0.3
EV/EBDITA (x)	4.2	3.4	1.5	1.5	1.4

01 April 2009

Shashi Bhusan
shashi.bhusan@pinc.co.in
Tel: +91-22-6618 6372

Karan Taurani
karan.taurani@pinc.co.in
Tel: +91-22-6618 6382

Jaikishan Kaurani
jaikishan.kaurani@pinc.co.in
Tel: +91-22-6618 6332

STOCK DATA

Market Cap	Rs67.4bn
Book Value per share	Rs76.4
Eq Shares O/S (FV Rs5)	669.7mn
Free Float	28.5%
Avg Traded Value (6 mnths)	Rs275mn
52 week High/Low	Rs325/89
Bloomberg Code	HCLT IN
Reuters Code	HCLT.BO

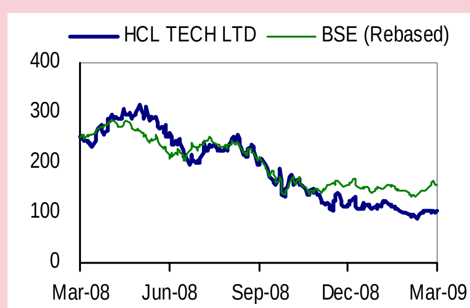
TOP SHAREHOLDERS

Name	% holding
HSBC Global Investment Funds	7.1
Life Insurance Corporation of India	2.7
Warhol Ltd	2.6
Master Trust Bank of Japan Ltd	1.7
Dali Ltd	1.3
Deutsche Bank	1.2

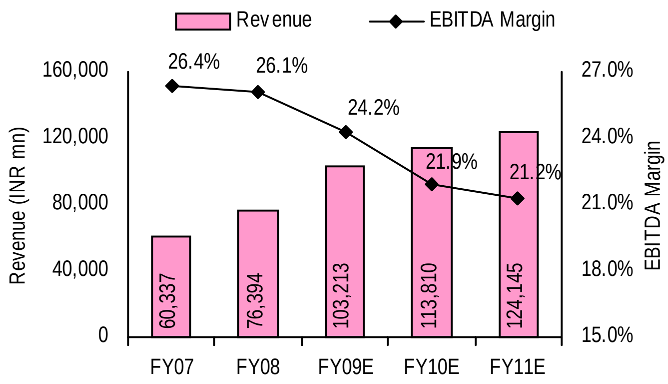
PERFORMANCE (%)

	1M	3M	12M
Absolute	6.7	(18.0)	(59.1)
Relative	(7.2)	(17.9)	(35.4)

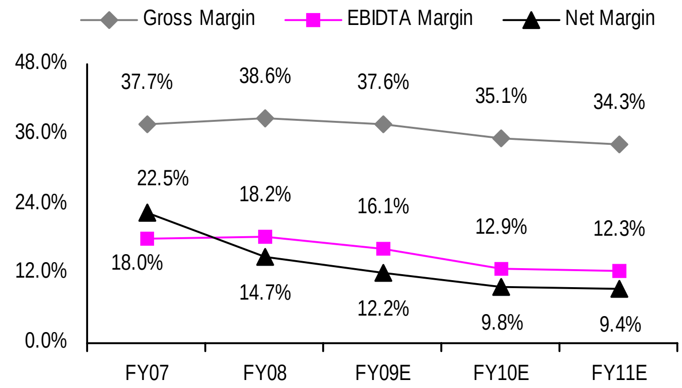
RELATIVE PERFORMANCE



Revenue / EBIDTA

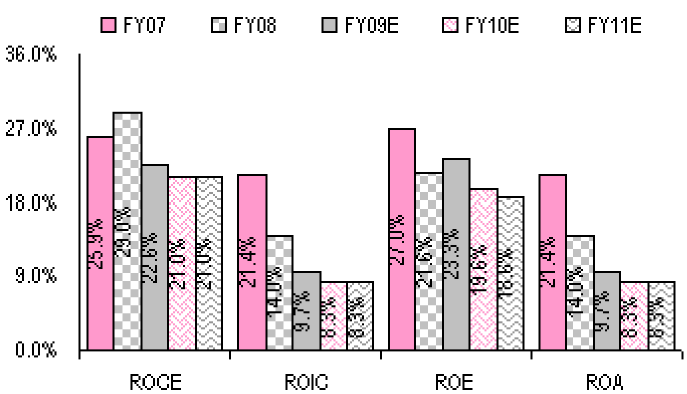


Margins

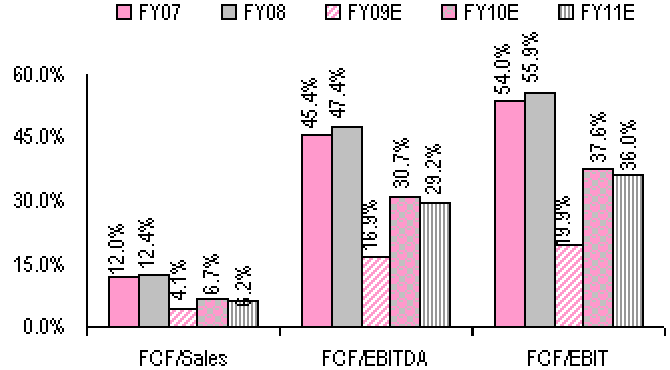


Source: Company Report

Return on Capital Ratios



Other Ratios

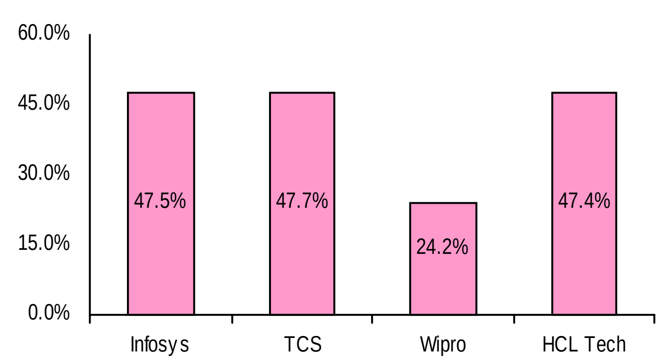


Source: Company Report

Return on Capital Ratios

Realization Growth	Volume Growth			
	-5%	0	5%	10%
-10%	5.80	6.56	7.31	8.06
-5%	10.66	11.67	12.68	13.69
0%	15.52	16.78	18.05	19.31
5%	20.37	21.89	23.41	24.94

FCF/EBITDA (FY08)



Source: Company Report, PINC Research

Year Ended June (Figures in Rs mn)

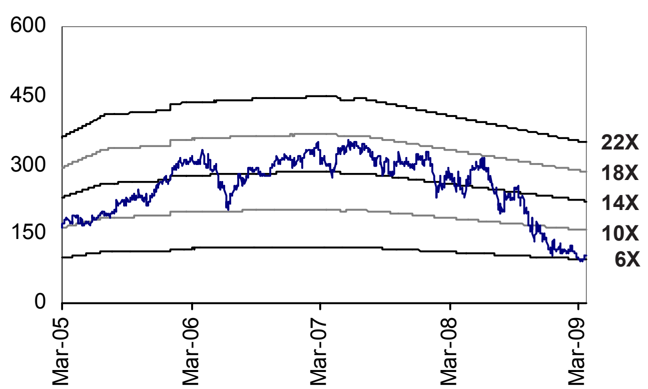
Income Statement	FY07	FY08	FY09E	FY10E	FY11E
Net sales	**60,337**	**76,394**	**103,213**	**113,810**	**124,145**
Growth (%)	*37*	*27*	*35*	*10*	*9*
Gross profit	**22,745**	**29,518**	**38,854**	**39,957**	**42,597**
Other operating charges	9,374	12,579	17,655	19,540	21,209
EBITDA	**13,371**	**16,939**	**21,199**	**20,418**	**21,388**
Growth (%)	*36*	*27*	*25*	*(4)*	*5*
Depreciation	2,532	3,033	4,544	5,729	6,119
Other income	4,259	(1,370)	(2,014)	(1,281)	(276)
EBIT	**10,839**	**12,536**	**14,641**	**13,407**	**14,993**
Interest paid	-	-	-	-	-
PBT (before E/o items)	**15,098**	**12,536**	**14,641**	**13,407**	**14,993**
Tax provision	1,485	1,272	2,050	2,279	3,298
E/o Income / (loss)	(64)	(19)	14	-	-
Net profit	**13,613**	**11,264**	**12,591**	**11,128**	**11,694**
Adjusted net profit	**13,549**	**11,245**	**12,605**	**11,128**	**11,694**
Growth (%)	*75*	*15*	*12*	*(12)*	*5*
Diluted EPS (Rs)	**19.8**	**16.5**	**18.8**	**16.6**	**17.4**
Diluted EPS Growth (%)	81	(17)	14	(12)	5

Cash Flow Statement	FY07	FY08	FY09E	FY10E	FY11E
Profit After Tax	13,093	12,510	11,538	11,128	11,694
Depreciation	2,601	3,333	3,669	4,552	4,966
Total tax paid	-	-	-	-	-
Chg in working capital	(4,291)	1,885	(4,269)	(2,351)	(3,038)
Other operating activities	(241)	(2,149)	(1,041)	1,177	1,153
Cash flow from oper. (a)	**11,161**	**15,580**	**9,897**	**14,506**	**14,776**
Capital expenditure	(3,944)	(6,117)	(5,677)	(6,829)	(7,076)
Chg in investments	(2,106)	(36)	7,555	-	-
Other investing activities	4	(1,814)	(28,225)	-	-
Cash flow from inv. (b)	**(6,045)**	**(7,966)**	**(26,346)**	**(6,829)**	**(7,076)**
Free cash flow (a+b)	5,117	7,613	(16,449)	7,677	7,699
Equity raised/(repaid)	2,329	416	172	-	-
Debt raised/(repaid)	-	-	26,134	-	-
Chg in Minorities int.	-	-	-	-	-
Dividend (incl. tax)	(6,013)	(7,006)	(6,092)	(6,023)	(6,023)
Other financing activities	(510)	(225)	873	-	-
Cash flow from fin. (c)	**(4,195)**	**(6,815)**	**21,086**	**(6,023)**	**(6,023)**
Net chg in cash (a+b+c)	**922**	**798**	**4,637**	**1,654**	**1,677**

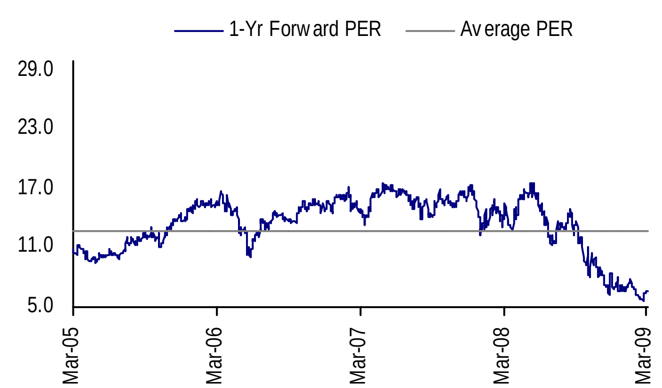
Balance Sheet	FY07	FY08	FY09E	FY10E	FY11E
Equity Share Capital	**50,150**	**52,177**	**53,995**	**59,100**	**64,771**
Reserves & surplus	-	-	-	-	-
Shareholders' funds	**50,150**	**52,177**	**53,995**	**59,100**	**64,771**
Minorities interests	145	57	23	23	23
Total Debt	1,292	6,234	39,931	39,931	39,931
Capital Employed	**51,587**	**58,468**	**93,949**	**99,054**	**104,725**
Net fixed assets	20,905	27,965	66,455	67,554	68,511
Cash & Cash Eq.	3,587	3,840	7,465	9,119	10,796
Net other Current Assets	26,999	26,562	19,865	22,216	25,254
Investments	96	101	164	164	164
Net Deferred Tax Assets	-	-	-	-	-
Total assets	**51,587**	**58,468**	**93,949**	**99,054**	**104,725**

Key Ratios	FY07	FY08	FY09E	FY10E	FY11E
OPM (%)	22.2	22.2	20.5	17.9	17.2
Net margin (%)	22.5	14.7	12.2	9.8	9.4
Dividend yield (%)	9.0	10.4	9.9	8.9	8.9
Net debt/Equity (x)	0.0	0.0	0.6	0.5	0.5
Net Working Capital (days)	163	127	70	71	74
Asset turnover (x)	1.0	1.0	0.8	0.8	0.9
ROCE (%)	25.9	29.0	22.6	20.6	20.4
RoE (%)	27.0	21.6	23.3	18.8	18.1
EV/Net sales (x)	1.1	0.9	0.4	0.3	0.3
EV/EBITDA (x)	4.2	3.4	1.5	1.5	1.4
PER (x)	4.9	6.0	5.4	6.1	5.8
Price/Book (x)	1.3	1.3	1.3	1.1	1.0

P/E Band



Average P/E



T E A M

EQUITY DESK

Gealgeo V. Alankara	Head - Institutional Sales	*alankara@pinc.co.in*	*91-22-6618 6466*
Sailav Kaji	Head Derivatives & Strategist	*sailavk@pinc.co.in*	*91-22-6618 6344*

SALES

Anil Chaurasia	*anil.chaurasia@pinc.co.in*	*91-22-6618 6483*
Alok Doshi	*adoshi@pinc.co.in*	*91-22-6618 6484*
Sundeep Bhat	*sundeepb@pinc.co.in*	*91-22-6618 6486*
Gagan Borana	*gagan.borana@pinc.co.in*	*91-22-6618 6485*

DEALING

Amar Margaje	*amar.margaje@pinc.co.in*	*91-22-6618 6327*
Ashok Savla	*ashok.savla@pinc.co.in*	*91-22-6618 6400*
Raju Bhavsar	*rajub@pinc.co.in*	*91-22-6618 6301*
Manoj Parmar	*manojp@pinc.co.in*	*91-22-6618 6326*
Hasmukh D. Prajapati	*hasmukhp@pinc.co.in*	*91-22-6618 6325*
Pratiksha Shah	*pratikshas@pinc.co.in*	*91-22-6618 6329*

DIRECTORS

Gaurang Gandhi	*gaurangg@pinc.co.in*	*91-22-6618 6400*
Hemang Gandhi	*hemangg@pinc.co.in*	*91-22-6618 6400*
Ketan Gandhi	*ketang@pinc.co.in*	*91-22-6618 6400*

COMPLIANCE

Rakesh Bhatia	Head Compliance	*rakeshb@pinc.co.in*	*91-22-6618 6400*

PINC bright thinking

Infinity.com

Financial Securities Ltd

SMALL WORLD, INFINITE OPPORTUNITIES

Member : Bombay Stock Exchange & National Stock Exchange of India Ltd. : Sebi Reg No: INB 010989331. Clearing No : 211
1216, Maker Chambers V, Nariman Point, Mumbai - 400 021; Tel.: 91-22-66186633/6400 Fax : 91-22-22049195