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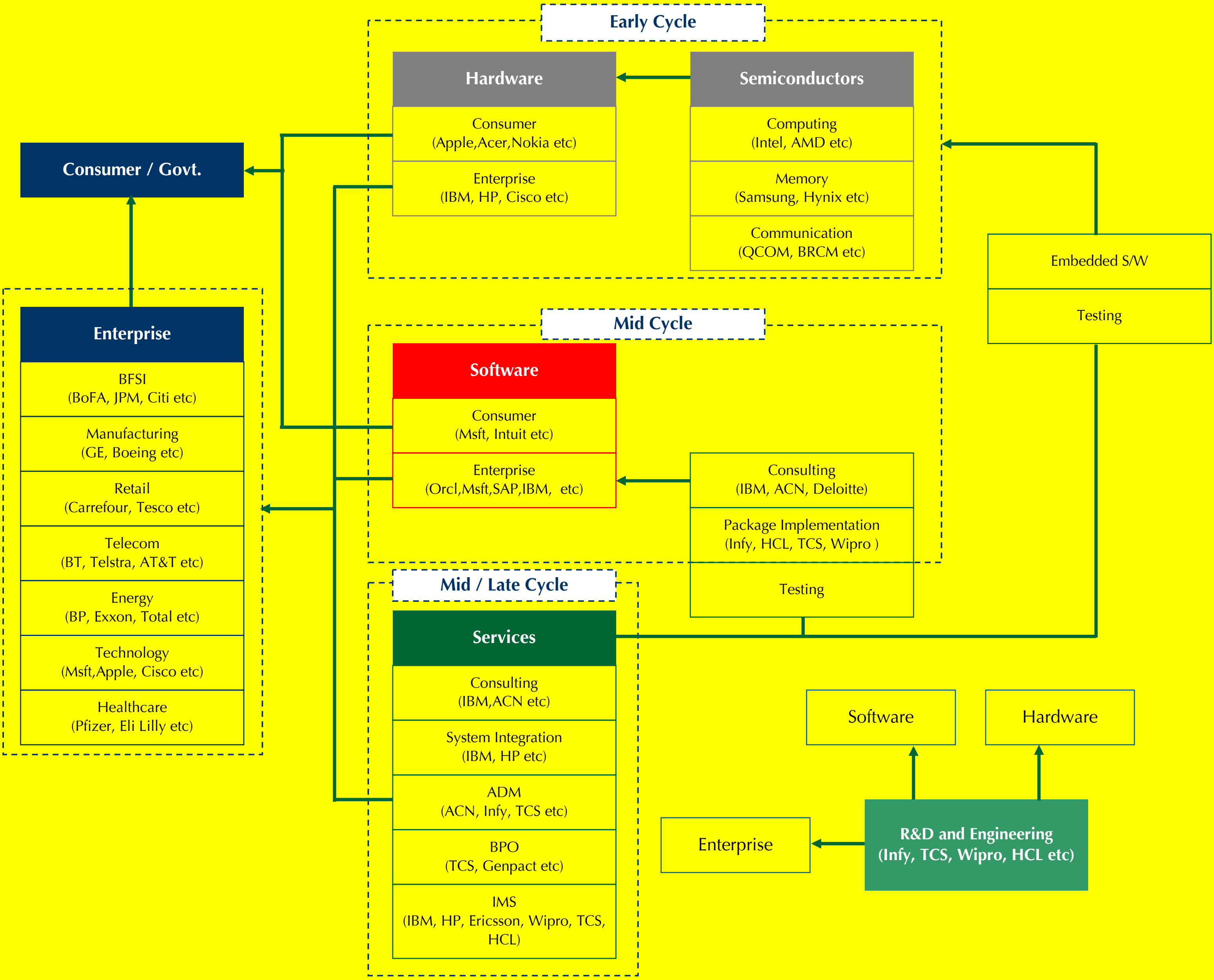
Information Technology

New Bytes...Indian Tech beginning to discount them



Why the note

- Are we entering a new tech cycle?
- Which sectors within tech are best positioned to outperform?
- How are key verticals of Indian IT positioned?
- How is Indian IT valued in light of Global tech valuations?

Key findings

- The right ingredients for a tech cycle are present
- Software is the best positioned to outperform
- Verticals w.r.t. Indian Tech – BFSI, Manuf., Retail to lead growth
- Value in Global tech; Indian IT beginning to discount a new tech cycle

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January 2011

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New Bytes...Indian Tech beginning to discount them

In this report, we look at the technology cycles across key segments over the last decade and examine leading indicators that could suggest the onset of a new cycle. Additionally, we ascertain the revenue and growth expectations for key clients and outsourcers spanning verticals relevant to Indian IT.

Our key findings are: (1) Tech spending should remain robust and improved US corporate health could usher in a new tech cycle, if aided by the US economic recovery. (2) CY10 saw a strong rebound in semiconductors and hardware driven by a hardware refresh across the enterprise segment; software and services could witness a pick-up in growth over the next two years. (3) The software segment (mid-cycle play) is best positioned given modest expectations and the likelihood of the highest earnings upgrades. (4) For Indian IT, the BFSI, manufacturing and retail verticals are likely to report strong growth in outsourcing in CY11, while companies with large telecom exposure could continue to lag peers.

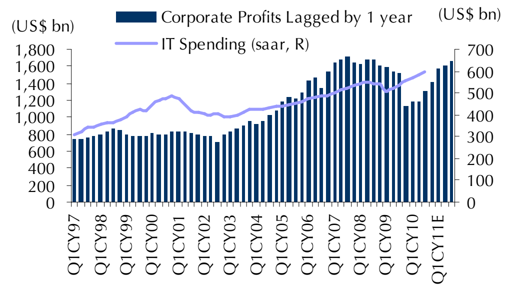
Overall, we believe technology investors globally would find more value in software/hardware names which have higher scope for earnings upgrades, superior operating leverage and greater comfort on valuations. The Indian technology space is now trading at a premium to global technology, and valuations are already beginning to discount the new cycle.

Technology spending likely to remain strong: US corporate profits are at the peak levels last seen in CY07; this should continue to drive technology spending. US tech investment is currently at 4.1% of GDP and has crossed its 8-year average of 3.7%. Further, there is an increased focus on operational efficiency among corporates, which in our view could attract continued investment in technology. We believe that drivers for tech spending must be supported by greater confidence in the US recovery. Though the outlook for spends remains stable, we are yet to see any sharp increase in IT budgets.

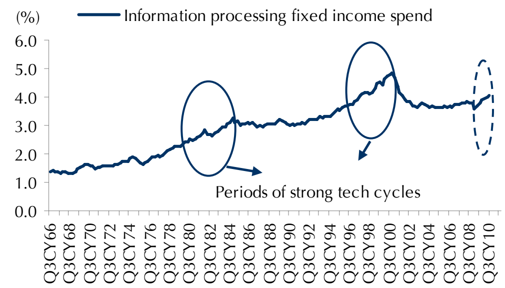
Software offers maximum leverage: From a cyclical perspective, hardware/ semiconductors tend to be an early play into the entire tech refresh cycle, while software and services tend to be mid/late-cycle plays. The recovery in software, though solid, has lagged behind the semi/hardware segment in CY10. In the present context, should the tech cycle continue, we believe that the strong rebound in semi/hardware in 2010 could prompt a rebound in the software segment. Further, analyst expectations in key software names indicate a modest 5–8% growth, far below the peaks of 2003–07, suggesting potential for upgrades. While we do expect services to benefit from the tech cycle, we believe valuations in software/ hardware remain reasonable given the current earnings CAGR and likely upgrades.

Global tech valuations undemanding: Valuations across global technology names remain reasonable, with most of them in line or below their 5-year average multiples. We recommend that global tech investors look at software names to play the tech cycle given possible earnings upgrades and higher comfort on valuations. While we do expect services to benefit from the upcycle, we believe that the valuation premium of the Indian IT services space has widened significantly (Infosys at 58% premium to Accenture). Further, following the recent round of earnings upgrades, Indian tech is now beginning to discount the new technology upcycle. We are positive on Oracle Financial Services Software (OFSS), which is the only large software play in India. As for large Indian IT services names, we would turn more positive post a 10% correction.

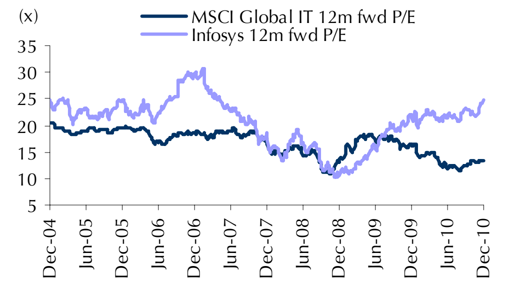
US corporate profits and IT spending



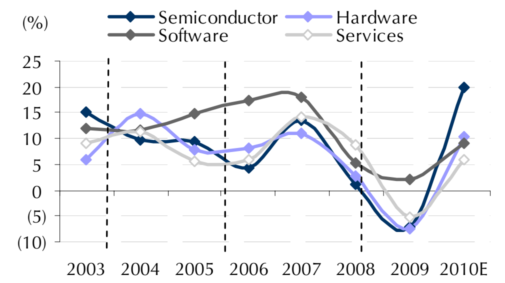
US fixed investment in IT as % of GDP



MSCI Global IT index v/s Infosys



Growth across tech chain



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Executive summary

Technology spending has seen a sharp rebound in 2010 with strong growth witnessed in the hardware segment. Given the improving macro environment in the US, robust corporate profits and high cash levels, US corporates are adequately positioned for investment in technology upgrades, after significant underinvestment over the past two years. Here, we conduct a study to determine how different segments in the tech supply chain are positioned for the cycle and the upsides one can expect, particularly with respect to Indian IT companies. We also examine the current outlook of other industry verticals in the context of IT Services to ascertain growth visibility for the latter over the next two years.

Decoding the tech supply chain

More consensus upgrades for software over the next 2 years if tech cycle lifts; upgrades for services only from CY12

The tech supply chain can be broadly classified into four segments—semiconductors, hardware, software and services. Of these, hardware, software and services are to some extent directly exposed to the end demand for technology (corporate / consumer), while the semiconductor segment directly feeds into hardware. From a cyclical perspective, hardware/semiconductors tend to be an early play into the entire tech refresh cycle while software and services tend to be mid/late-cycle plays.

In the present context, 2010 saw a strong tech spending rebound, driven by increased hardware spends, which we believe could remain strong in CY11 as well. While this does bode well for the services segment, we note that services growth lagged behind other sectors for the first four years coming out of the tech bubble. As such, should the tech cycle pick up, software could see a higher share of consensus upgrades over the next two years, while the services sector could see meaningful upgrades only from CY12 onwards.

ADM likely to gain strength only mid-cycle, while PI and consulting could see strength during the early stages

Considering the new refresh cycle, it is important to know how services fit into the entire scheme of things. We note that the services segment is largely exposed to end demand through three primary linkages: (1) Directly in the form of corporate IT budgets for apps development/maintenance, business processes and handling of IT infrastructure; (2) Through software in the form of package implementation (PI) and testing services; and (3) Through hardware in the form of embedded software design and testing services. While ADM is largely independent of the hardware and software, it is likely to gain strength only towards the middle of the tech cycle, while PI and consulting could see strength during the early stages of the cycle as well. Our current estimates for top tier Indian IT companies point to 24%/18% growth in CY11/CY12.

Fig 1 - Mix of package implementation & consulting practice at Indian IT

(%)	FY06	FY07	FY08	FY09	FY10	2Q11
Infosys	19.7	21.1	23.8	24.9	24.4	25.8
TCS	22.5	15.7	16.5	15.1	12.4	12.4
Wipro	12.2	12.3	13.9	14.0	15.4	16.5
HCL Tech		12.8	11.2	18.3	22.0	21.7

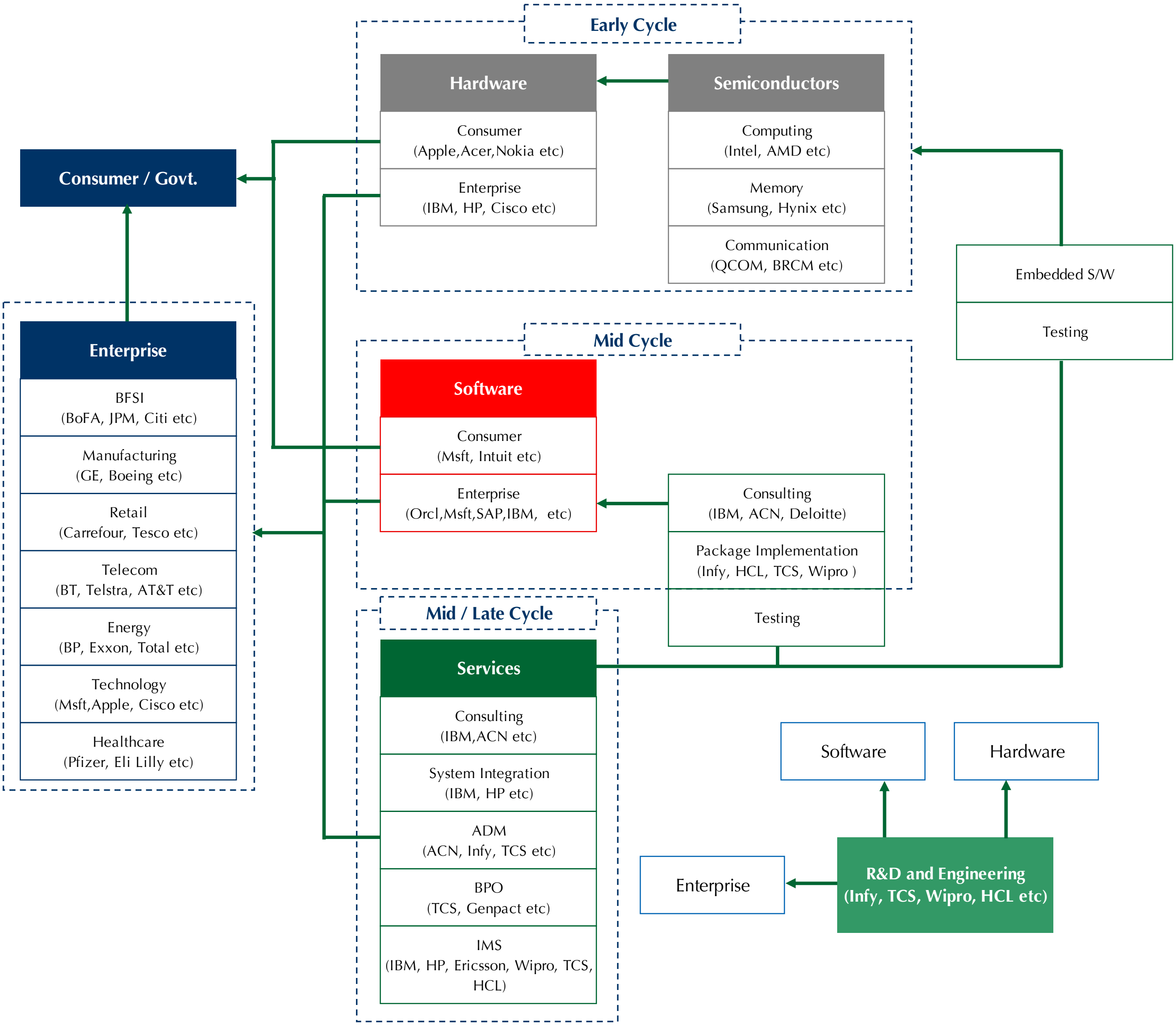
Source: Company

Valuations

Indian IT companies far more expensive than global tech counterparts

We also look at valuations across the tech space and find that Indian IT companies are significantly more expensive than global tech players. Even within the services space, Infosys' premium over Accenture has widened significantly over the past few months to 58%. We believe tech investors globally would find more value in software names which have higher scope for earnings upgrades, stronger operating leverage and better comfort on valuations.

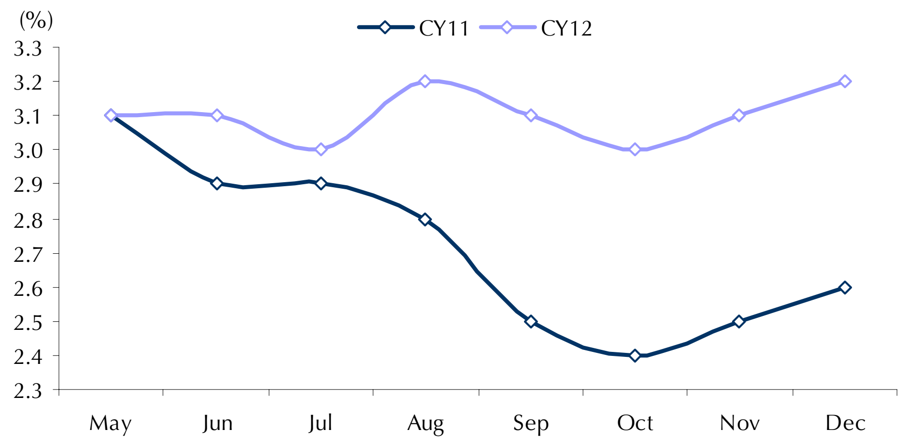
The tech engine



Right ingredients in place for a new tech cycle

In our view, US corporate health remains stable with expectations of a recovery in the US economy, healthy corporate profits and strong cash balances with companies. While there are initial indications of a new tech cycle, real triggers will emerge only once we see more clarity on any rise in IT budgets from leading companies and a revival in the US consumer sector, which has been a laggard so far.

Fig 2 - Consensus US real GDP growth estimates



Source: Bloomberg

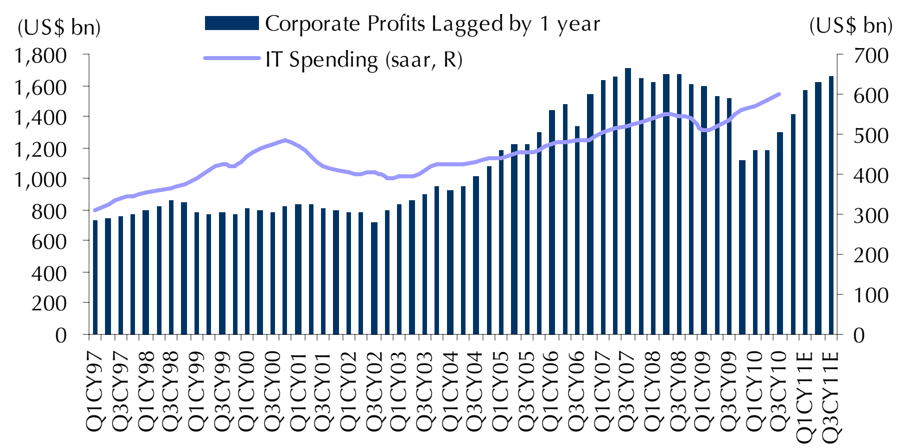
Corporate profits to support spending

While there are still concerns over the macro environment, US corporate profits have jumped sharply over the last 6–8 quarters, supporting investment in technology. US corporate profits grew 28% YoY in Q3CY10 to reach 2007 levels, suggesting a continued improvement in corporate health. US IT spending increased 12.2% YoY in the third quarter driven by strong hardware spending (up 23% YoY). Further, the sharp jump in corporate profits and underinvestment in 2008/09 are likely to result in record technology spends in 2010. In the services space, the offshoring trend remains intact with a sustained increase in market share for Indian IT in Q3CY10.

US IT spending increased 12% YoY in Q3CY10 on the back of improving corporate profits

Sustained improvement in corporate profits indicates that the IT spending recovery will continue

Fig 3 - US corporate profits and IT spending



Source: US BEA, RCML Research

Fig 4 - S&P operating EPS by sector

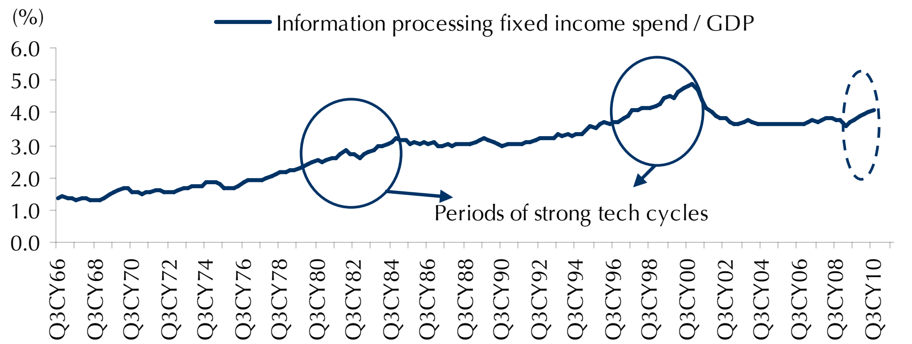
	2004	2005	2006	2007	2008	2009	2010E	2011E
S&P 500	**67.7**	**76.4**	**87.7**	**82.5**	**49.5**	**56.9**	**83.7**	**94.8**
S&P 500 Consumer Discretionary	13.6	13.2	15.8	13.3	5.3	11.0	17.9	19.7
S&P 500 Consumer Staples	12.8	13.5	14.2	15.6	17.2	18.4	19.3	21.3
S&P 500 Energy	24.3	35.0	43.6	46.3	50.9	17.3	35.2	40.2
S&P 500 Financials	30.9	32.0	37.6	22.8	-21.2	4.4	15.5	18.1
S&P 500 Health Care	17.2	18.7	20.1	23.3	24.5	26.4	29.0	33.0
S&P 500 Industrials	13.1	16.4	19.0	21.3	21.2	14.2	17.7	20.0
S&P 500 Information Technology	12.6	14.9	15.1	17.4	16.1	17.5	25.7	29.1
S&P 500 Materials	10.1	12.0	15.2	16.0	8.1	7.1	12.6	16.1
S&P 500 Telecommunication Services	6.9	7.2	8.0	8.3	8.2	7.2	7.7	8.3
S&P 500 Utilities	8.6	9.7	11.5	11.7	12.2	11.5	12.6	13.2

Source: S&P

Previously, tech has seen strong investment cycles in the late 70s-early 80s and then in mid/late90s

Given weak investments over the past decade, should macro conditions continue to improve, one could witness increased investment in IT

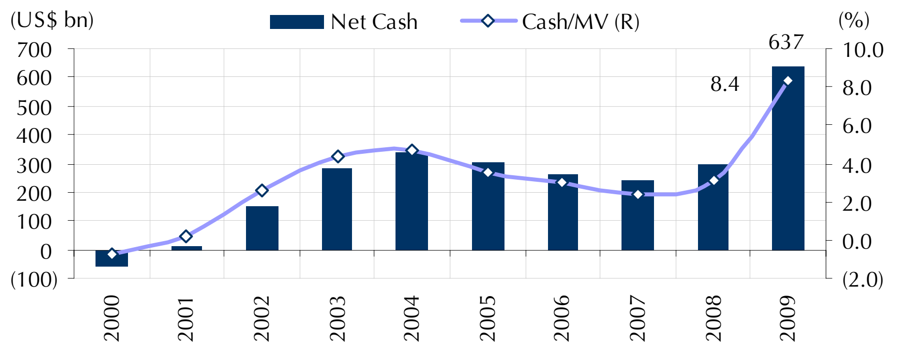
Fig 5 - US fixed investment in IT as % of GDP



Source: US BEA

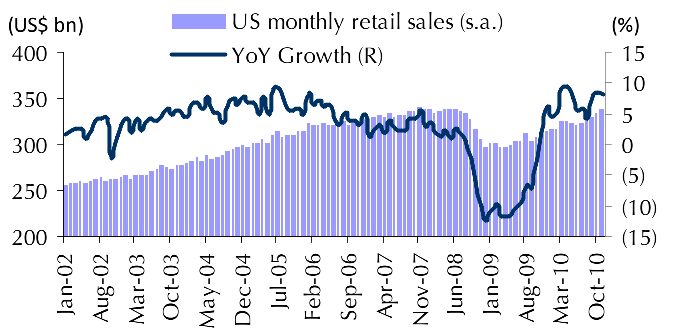
S&P 500 companies (excluding financials) are sitting on record net cash balances at the end of 2009

Fig 6 - US corporate (ex-financials) net cash balance



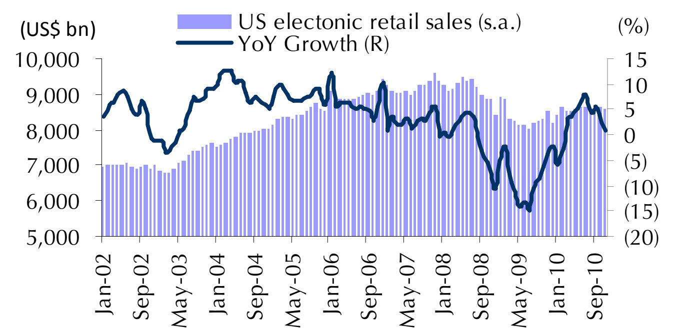
Source: Datastream

Fig 7 - US monthly retail sales



Source: US BEA

Fig 8 - US monthly electronic retail sales



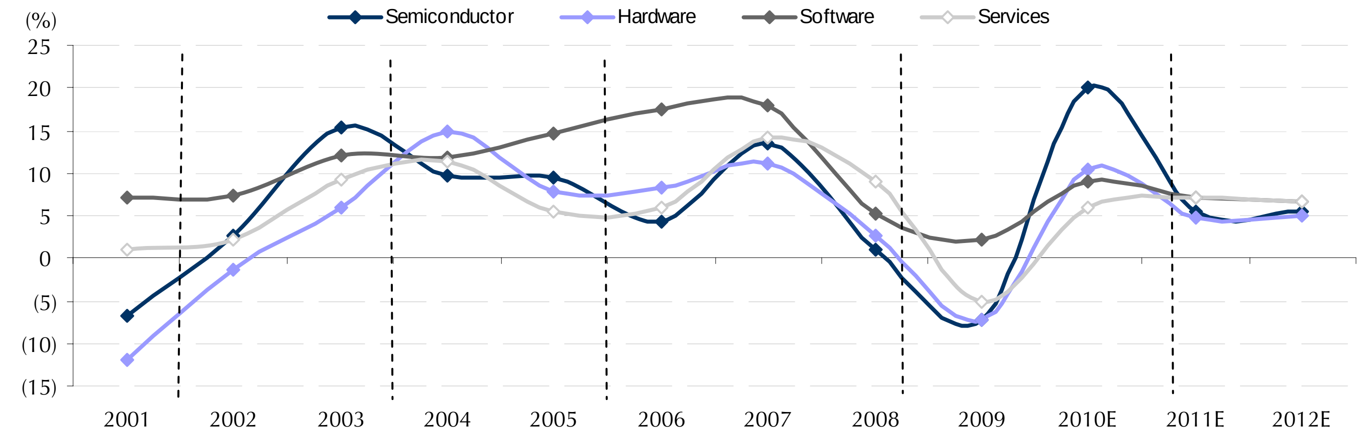
Source: US BEA

Growth across tech supply chain

2010 – A year of strong rebound

Technology spending has recovered sharply coming out of the recession, with US tech spending expected to have grown more than 10% in 2010 after a 3% decline in 2009. The growth was largely driven by increased spending in the enterprise segment where a refresh cycle is kicking in. As seen from the chart below, the rebound in 2010 was led by a sharp recovery in semiconductors followed by hardware, on the back of inventory restocking and a pick-up in end demand. While services growth has been muted, we highlight that Indian IT services players have seen 20%+ growth through the year, driven by strong demand in the BFSI vertical (M&A and regulatory compliance–related work) and a continued push towards offshoring as customers look to cut costs.

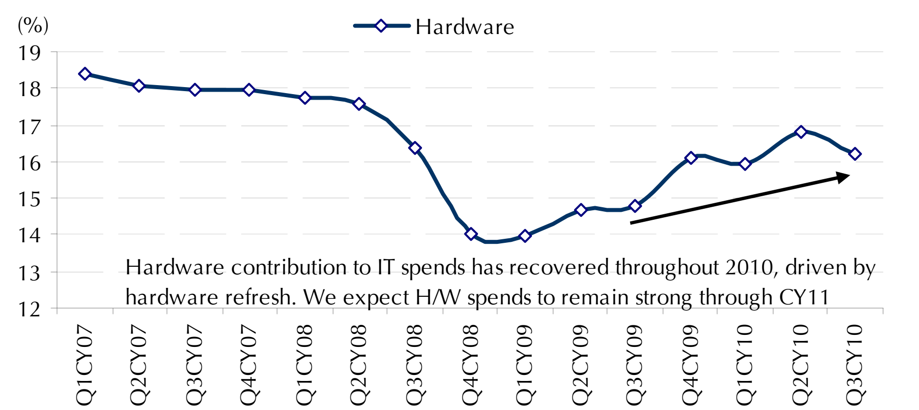
Fig 9 - Growth across Tech chain over CY01-CY12



Source: RCML Research, Companies, Bloomberg estimates, IBES estimates Note: This is on a RCML sample set of companies for each segment. Estimates are IBES consensus estimates.

Growing contribution of hardware in tech spends driven by enterprise refresh cycles

Fig 10 - Contribution of hardware in US IT spends



Source: US BEA

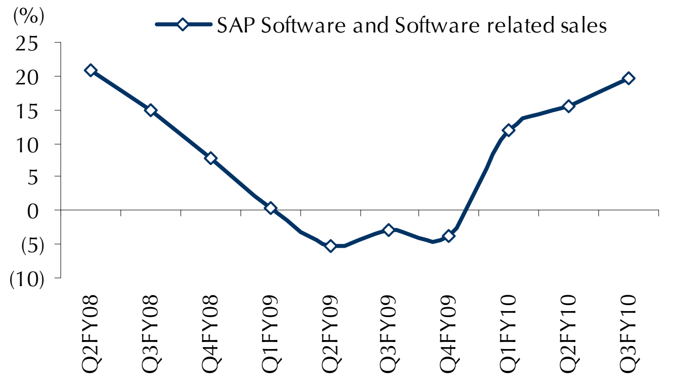
Technology trends for 2011

We believe that the tech spending environment is likely to remain sturdy in 2011 on the back of improved corporate health, provided the macro environment remains stable. We have broken down tech spends into four key areas: (1) Semiconductors, (2) Hardware, (3) Software, and (4) Services. Thereafter, we have compiled 10-year historical growth data and analyst expectations for the next two years for our selected sample set of key companies. Based on consensus estimates, overall growth rates for CY11/CY12 would likely be modest and with a pick-up in tech spending, there could be scope for possible upgrades across the supply chain.

2010 saw a recovery in early-cycle semiconductor/hardware plays; software to take the baton now

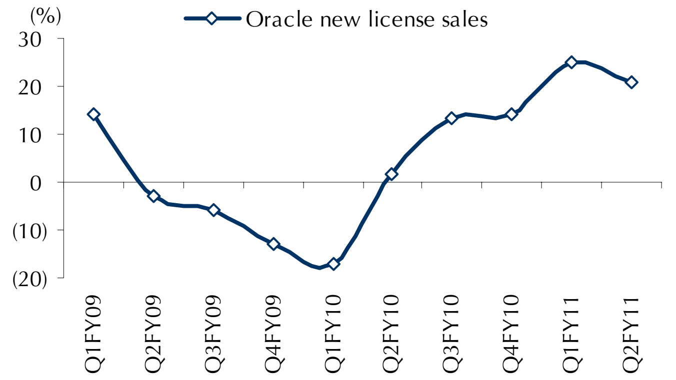
Our data reveals that 2010 saw a recovery in early-cycle plays, especially in the semiconductor and hardware segment. While 2010 was clearly a year of strong hardware refresh, we believe that if the tech cycle gains strength, software companies stand to see the highest earnings upgrades in CY11/CY12. Both Oracle and SAP have also seen a recovery in growth of new software sales throughout CY10. Growth acceleration at the software stage should also directly help in the PI practice of Indian IT players, besides being a precursor to further software and maintenance demand later in the cycle.

Fig 11 - SAP SSRS sales (YoY growth)



Source: Company

Fig 12 - Oracle new licence sales (YoY growth)

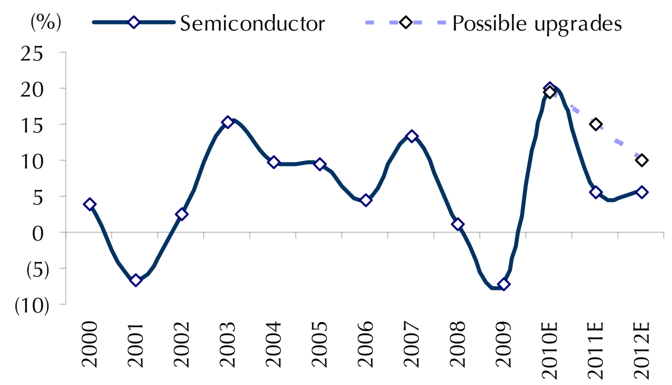


Source: Company

Services growth to pick up later in the tech cycle

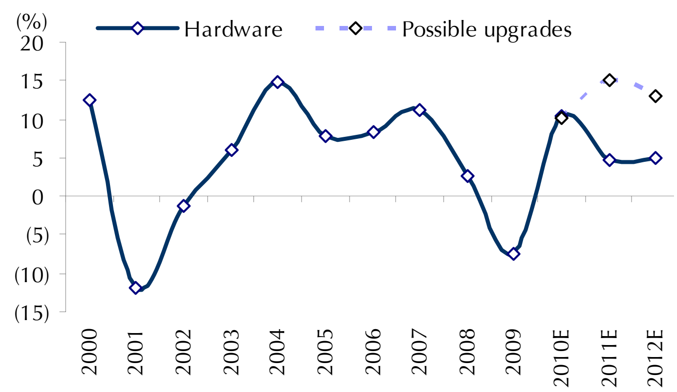
In our view, services should also benefit from the coming tech cycle; however being a later-cycle play, growth should pick up from CY12/CY13 onwards. Hence, even with a heightened tech cycle, significant earnings upgrades here are likely to come in only from CY12 onwards. Looking back at the recovery post the tech bubble, we note that while services growth did rebound in 2003/04 off a low base, the segment had underperformed the rest of the tech space for four years till 2007. From an Indian IT standpoint, our current estimates for FY12/FY13 already stand at 24%/18%. As such, should the tech cycle gain strength, there could be some upside to our estimates for FY13.

Fig 13 - Semiconductor revenue growth



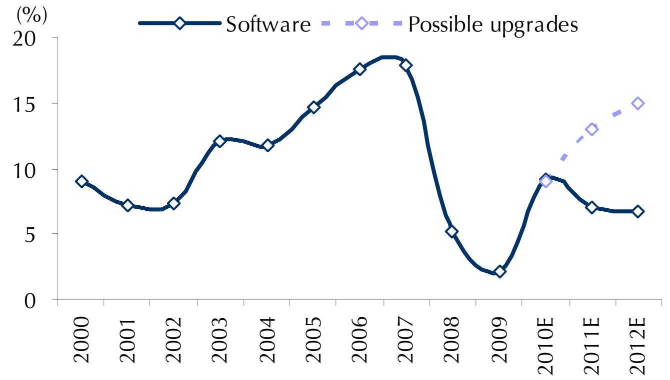
Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 14 - Hardware revenue growth



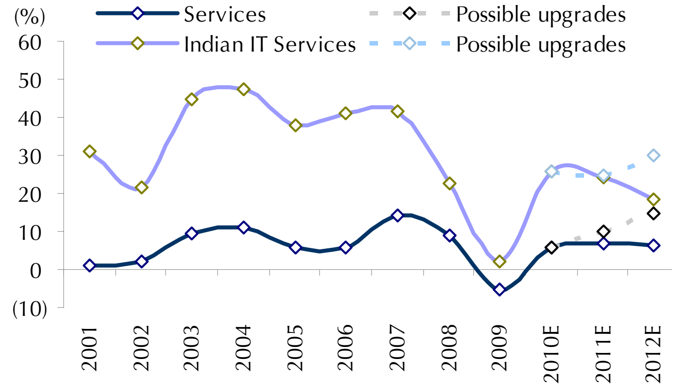
Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 15 - Software revenue growth



Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 16 - Services revenue growth



Source: Company data, Bloomberg, IBES estimates, RCML Research

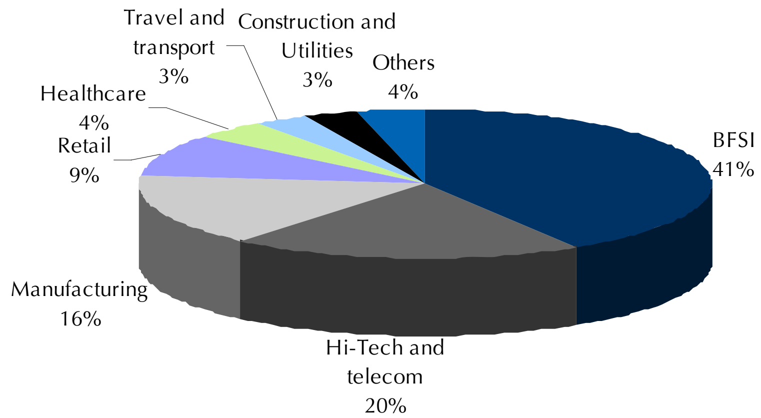
Growth expectations across key verticals for Indian IT

We look at the revenue and growth expectations for key clients and outsourcers across verticals in the context of Indian IT. Among the top-tier Indian companies, BFSI has been the key driver of spends in 2010 and contributes ~40% of revenues. This is followed by manufacturing which contributes 16% and telecom ~14–15%.

Strong outsourcing outlook for BFSI, manufacturing, retail and healthcare in CY11E, but not telecom

We note that coming out of the downturn, offshore players with higher exposure to the BFSI, retail and healthcare segments have seen stronger growth than companies with high telecom and manufacturing segments. Our analysis on the current outlook for these sectors indicates that the BFSI, manufacturing, retail and healthcare segments should see strong growth in outsourcing in CY11 as well, while companies with large telecom exposure could continue to trail behind peers.

Fig 17 - Vertical split of Indian IT exports (FY10)



Source: NASSCOM

BFSI mix for Indian IT companies

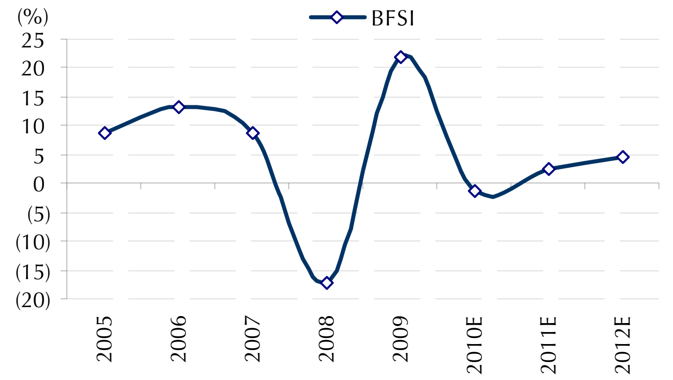
(%)	4Q10	1Q11	2Q11
TCS	45.6	44.7	44.0
Infosys	34.8	36.1	35.4
Wipro	26.1	26.9	26.9
HCL Tech	25.5	24.9	25.2

Source: Company

BFSI

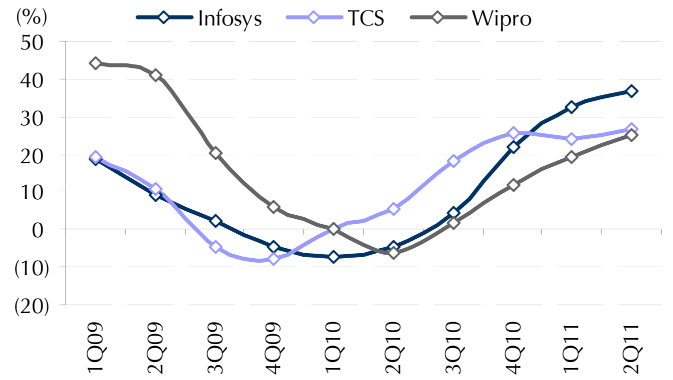
Indian IT companies have seen strong growth in the BFSI vertical in CY10 with all the leading players recording 25%+ YoY growth in the last quarter. Consensus estimates for our sample set of 14 leading global BFSI companies indicate that they are likely to grow by 2%/5% in CY11/CY12 after a flat CY10.

Fig 18 - BFSI companies: Revenue growth



Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 19 - BFSI practice at Indian IT companies (YoY growth)



Source: Company data, RCML Research

Telecom mix for Indian IT companies

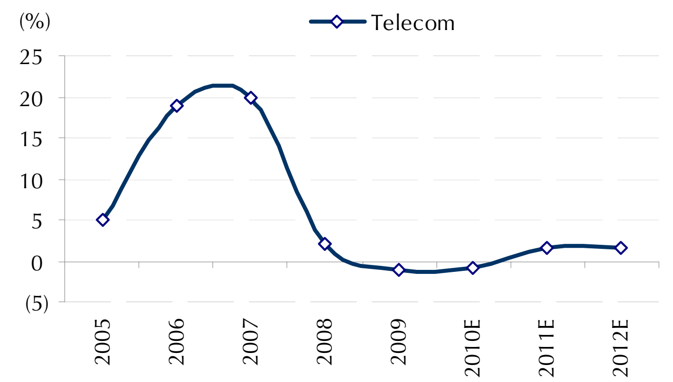
(%)	4Q10	1Q11	2Q11
Wipro	25.6	25.7	25.0
HCL Tech	19.5	18.3	17.9
TCS	14.0	14.6	14.8
Infosys	15.3	14.1	13.3

Source: Company. Note: Wipro mix is Tech and Telecom.

Telecom

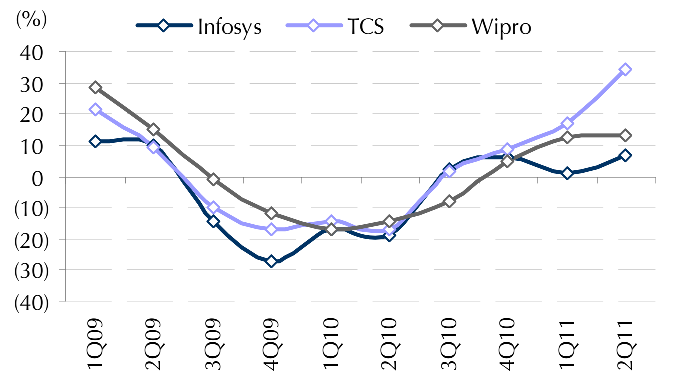
The telecom vertical has witnessed a weaker rebound coming out of the recession and companies with a larger telecom exposure have seen growth lagging their larger peers. Our sample of 13 global telecom players indicates that telecom revenues have stagnated over the past 2–3 years and consensus estimates for the same do not indicate any major improvement in growth rates in CY11/CY12.

Fig 20 - Telecom companies: Revenue growth



Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 21 - Telecom practice at Indian IT companies (YoY growth)



Source: Company data, RCML Research

Mfg mix for Indian IT companies

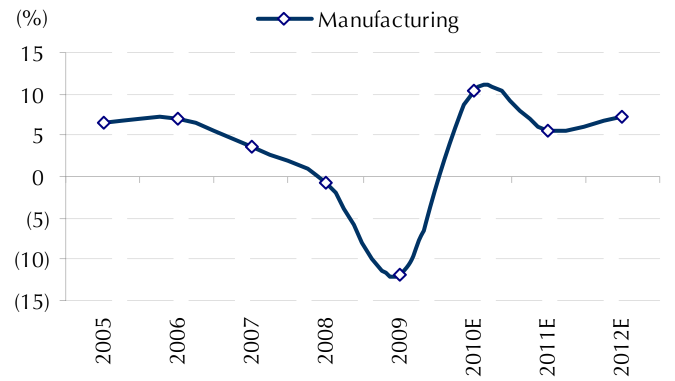
(%)	4Q10	1Q11	2Q11
HCL Tech	26.7	27.3	27.2
Infosys	20.2	19.5	18.9
Wipro	14.8	15.1	14.8
TCS	7.8	7.4	7.4

Source: Company

Manufacturing

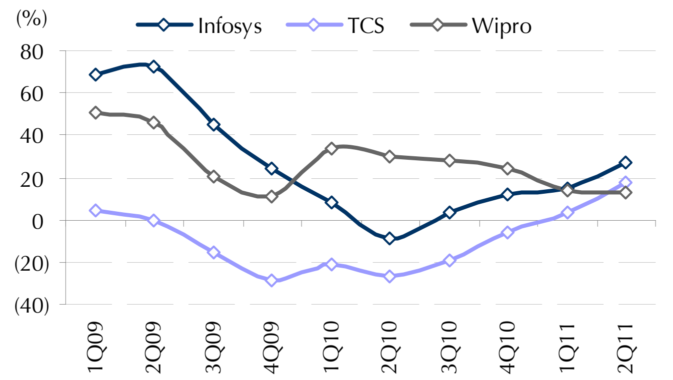
Although our sample set of 13 manufacturing companies indicates that manufacturing revenues are expected to grow by 10% in CY10 post a decline of 12% in CY09, the manufacturing vertical for IT services has only recently started to gather pace. Both Infosys and TCS have seen YoY growth improve in the September quarter. Consensus estimates indicate that manufacturing companies should post a growth of 6%/7% in CY11/CY12; we believe growth should return to the vertical over the next two years.

Fig 22 - Manufacturing companies: Revenue growth



Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 23 - Manufacturing practice of Indian IT (YoY growth)



Source: Company data, RCML Research

Retail mix of top Indian IT companies

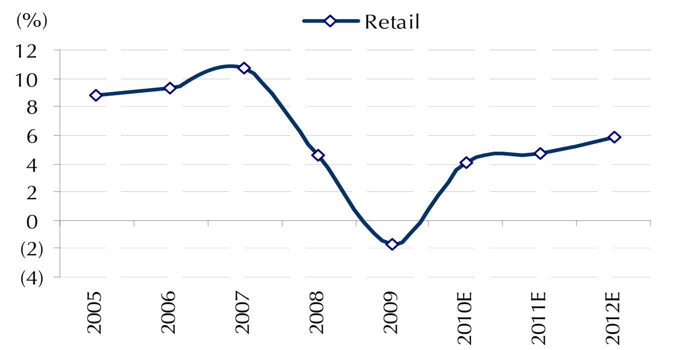
(%)	4Q10	1Q11	2Q11
Wipro	14.7	14.9	15.5
Infosys	13.0	13.2	14.4
TCS	10.9	11.0	10.9
HCL Tech	7.5	8.2	8.5

Source: Company

Retail

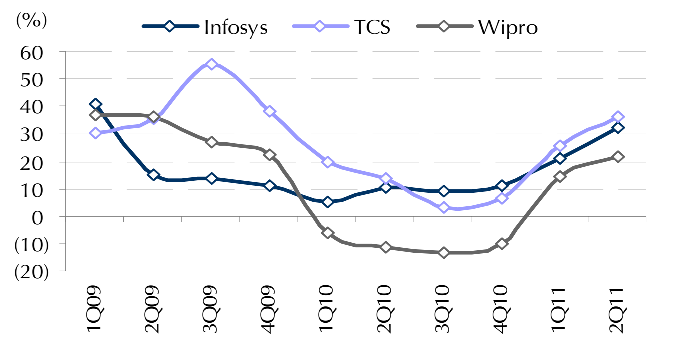
Our sample of 18 retail companies is expected to show 5% growth in revenues in CY10 following a 2% decline in CY09. Retail has been one of the fastest growing verticals for Indian IT players, as global companies continue to increase outsourcing in order to improve operational efficiencies. Consensus estimates indicate that growth rates in the segment would remain at 5%/6% levels for CY11/CY12.

Fig 24 - Retail companies: Revenue growth



Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 25 - Retail practice at Indian IT companies (YoY growth)

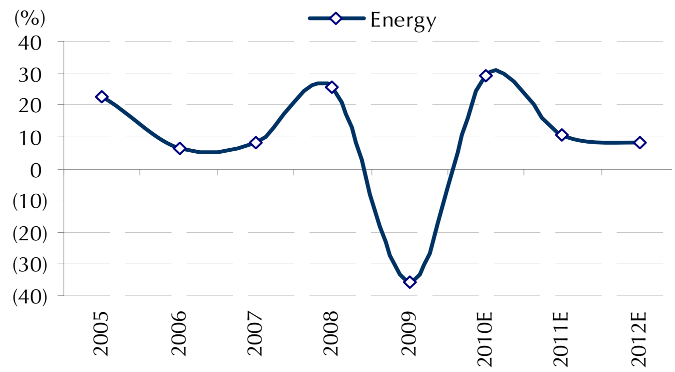


Source: Company data, RCML Research

Other verticals

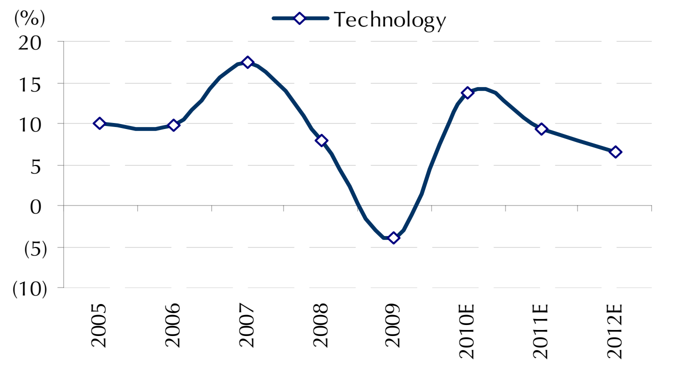
Among other verticals, healthcare is a fast growing segment for Indian IT companies largely driven by regulation changes in the US healthcare space. The hi-tech vertical will be another fast growing segment as technology companies benefit from improving tech spends and higher testing outsourcing. Although healthcare companies are expected to see a decent 8% revenue growth in CY10, growth rate expectations fall over the next two years, possibly due to industry-specific issues such as key product patent expiries.

Fig 26 - Energy companies: Revenue growth



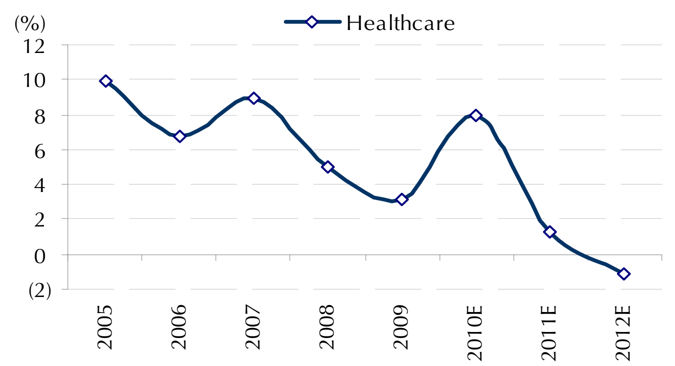
Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 27 - Tech companies: Revenue growth



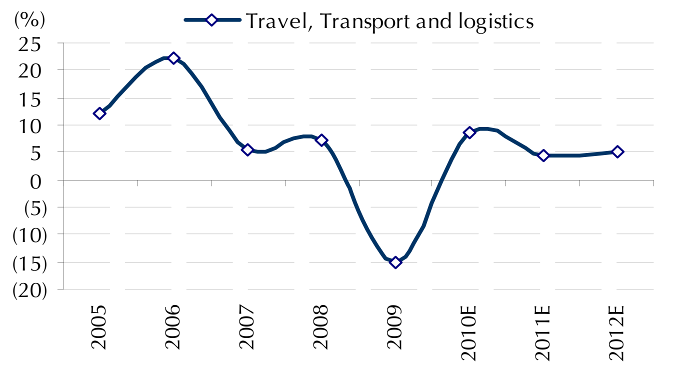
Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 28 - Healthcare companies: Revenue growth



Source: Company data, Bloomberg, IBES estimates, RCML Research

Fig 29 - Travel and Logistics companies: Revenue growth



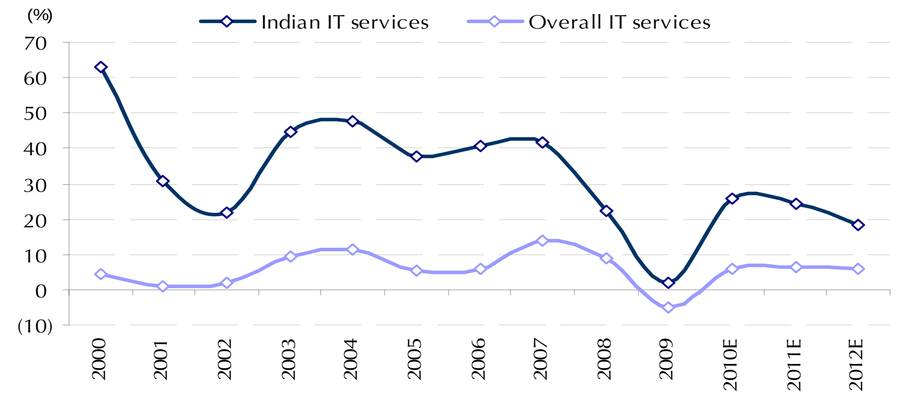
Source: Company data, Bloomberg, IBES estimates, RCML Research

Offshoring continues to gain market share in services

Indian IT companies likely to grow at 24%/18% in CY11/CY12 vs. 6.5%/6% for global players (incl India)

Despite protectionist vibes in the US, Indian IT services continued to gain market share through CY10, at the expense of global incumbents, as the trend towards offshoring continued among US corporates. Based on consensus estimates for our sample of 15 large global IT service providers (except for the 4 Indian companies where we have used our own estimates), we expect overall IT services revenue to grow 6.5%/6% in CY11/CY12 compared to 24%/18% for Indian IT companies. We maintain our view that Indian companies will continue to gain market share—consensus estimates indicate that larger players would capture 13% market share by CY12, up from 8% in CY09.

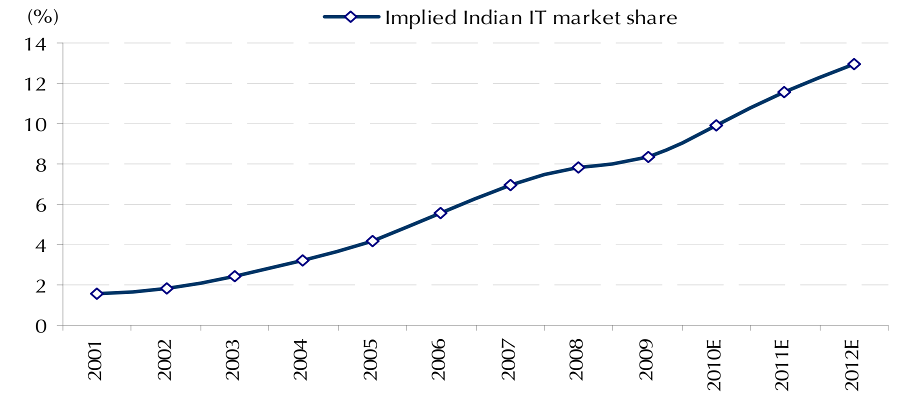
Fig 30 - Performance of Indian IT services and overall IT services (YoY growth)



Source: Companies, Bloomberg, IBES estimates, RCML Research. Indian IT companies comprises the top 4 Indian companies and overall services comprises of our sample of 15 large global IT companies.

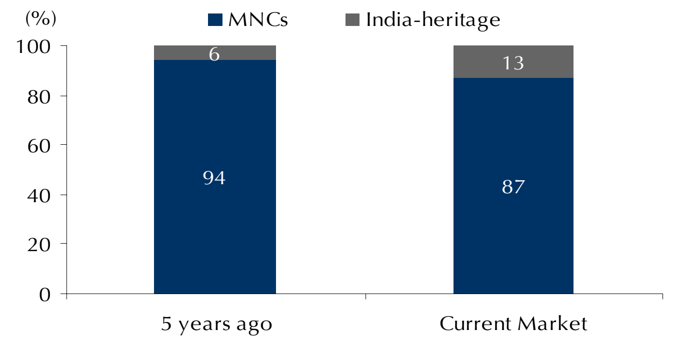
As per consensus, large Indian player market share would increase 5ppt to 13% over CY09-CY12

Fig 31 - Implied market share of Indian IT in the sample



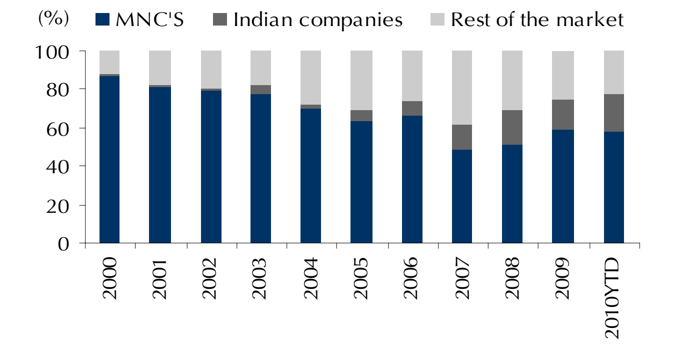
Source: Companies, Bloomberg, IBES estimates, RCML Research

Fig 32 - Services revenue share: Top 10 MNCs vs. Indian cos



Source: TPI Report, RCML Research

Fig 33 - Industry TCV contract awards above $25mn breakup



Source: TPI Report, RCML Research

Valuations across the technology space

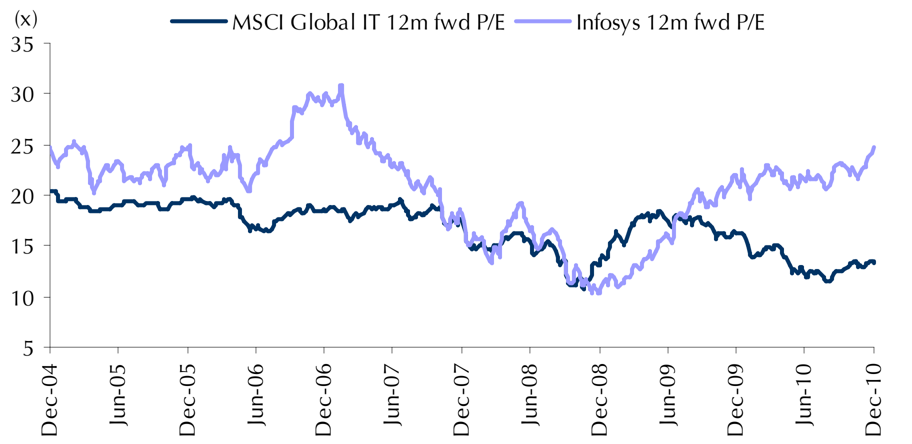
Indian IT stocks are trading at a significant premium to global tech companies

Looking at Indian IT valuations in the context of the global technology space, we find that Indian tech is already trading at a significant premium. Our conclusion is based on the following: (1) Global tech (MSCI Global IT) is currently trading at 13x twelve-month forward P/E compared to 25x for Infosys; (2) On P/B versus ROE, Indian IT companies are far more expensive (Fig 36); and (3) Even within the services space, the premium of Infosys to Accenture has widened to 58% versus the historical average of 40%.

For global tech investors, upside in software names is likely to be higher due to higher possibility of earnings upgrades as tech cycle rolls on

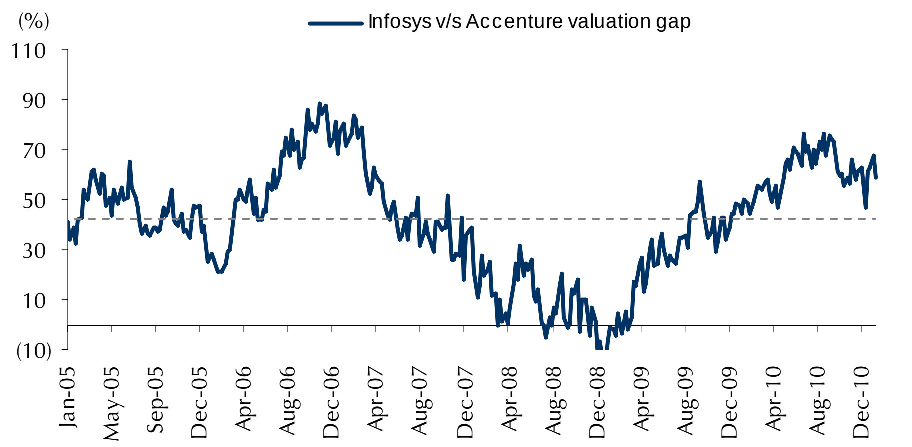
We would advise global investors to play the tech cycle largely through software/hardware in the early years of the cycle. We believe global tech stocks make for better investments than Indian IT at present due to (1) the higher possibility of consensus upgrades; (2) higher operating leverage in hardware and software companies, leading to faster EPS growth; and (3) more comfort on valuations. For investors looking to play the tech cycle in India, we would advise good quality second tier companies, such as HCL Tech and strong product players like OFSS where valuations are cheaper. As for large Indian IT services names, we would turn more positive post a 10% correction.

Fig 34 - MSCI World IT 12m fwd P/E v/s Infosys 12m fwd P/E



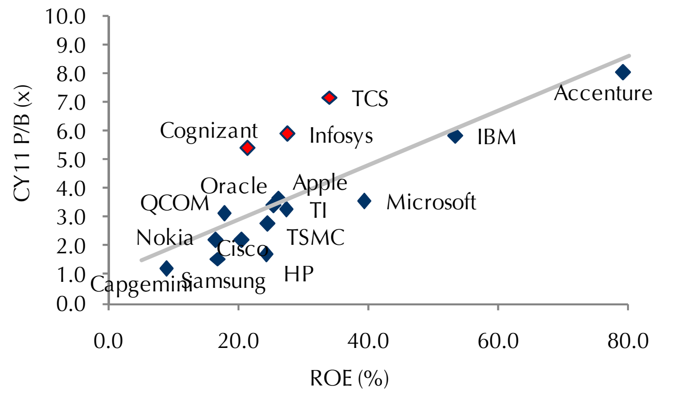
Source: IBES, RCML Research

Fig 35 - Infosys premium to Accenture



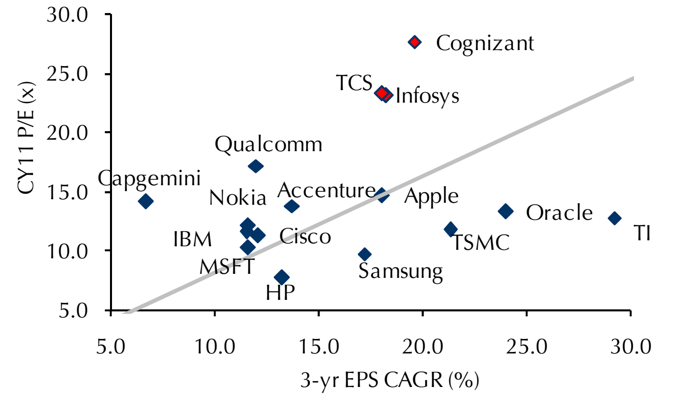
Source: Company, Bloomberg, RCML Research

Fig 36 - P/B v/s ROE



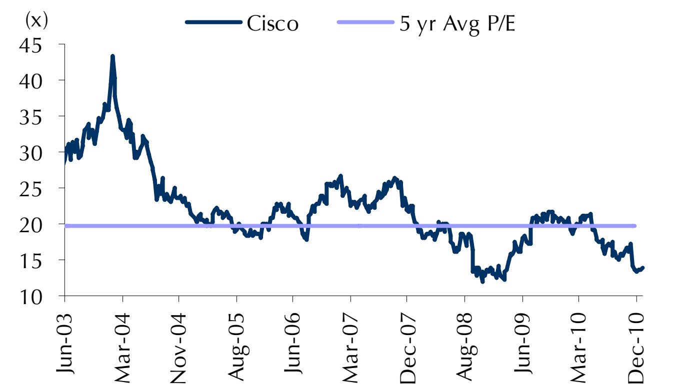
Source: Bloomberg, RCML Research

Fig 37 - Fwd P/E v/s EPS CAGR



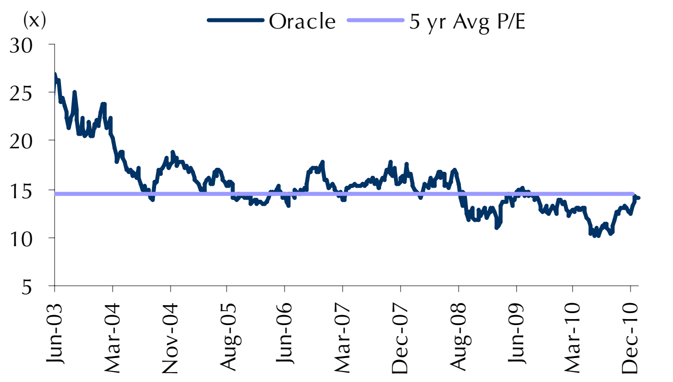
Source: Bloomberg, RCML Research

Fig 38 - Cisco P/E



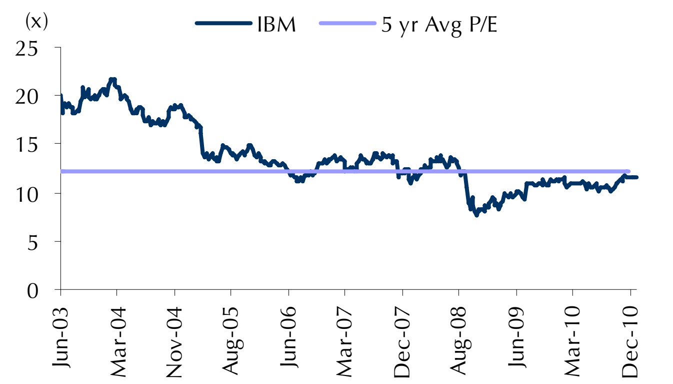
Source: Bloomberg; RCML Research

Fig 39 - Oracle P/E



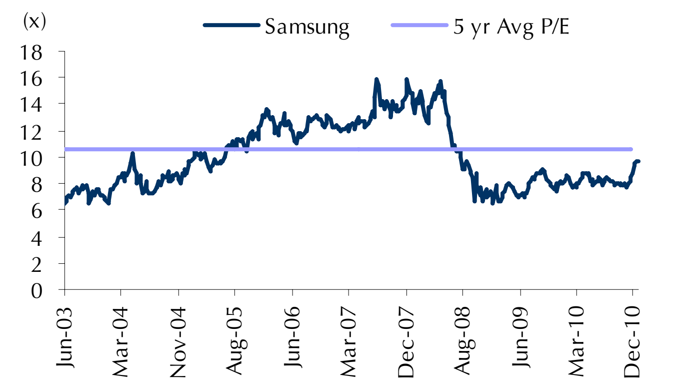
Source: Bloomberg; RCML Research

Fig 40 - IBM P/E



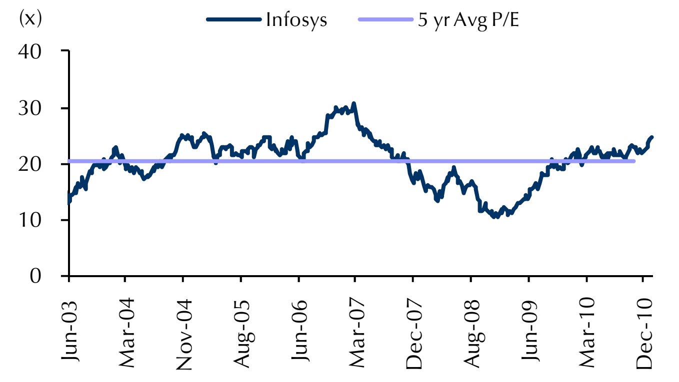
Source: Bloomberg; RCML Research

Fig 41 - Samsung P/E



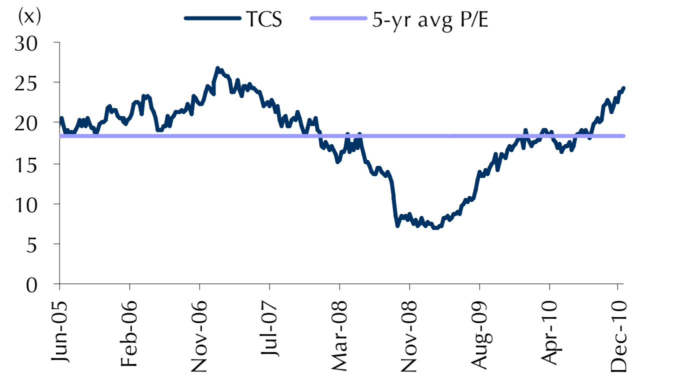
Source: Bloomberg; RCML Research

Fig 42 - Infosys P/E



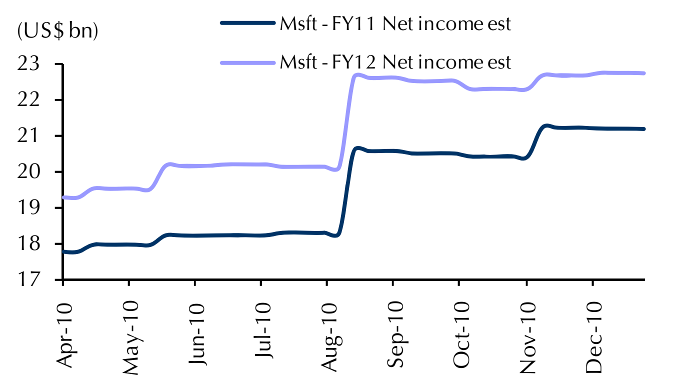
Source: Bloomberg; RCML Research

Fig 43 - TCS P/E



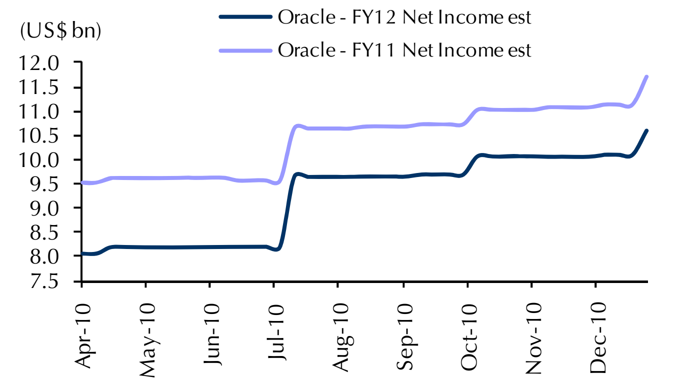
Source: Bloomberg; RCML Research

Fig 44 - Consensus net income forecasts for Microsoft



Source: IBES estimates

Fig 45 - Consensus net income forecasts for Oracle



Source: IBES estimates

Fig 46 - Global tech valuations

	Year End	Price	Market Cap	EPS			EPS CAGR	P/E			P/B	ROE
			US$ mn	CY10	CY11	CY12	(CY09-12)	CY10	CY11	CY12	CY11	CY11
				FY11	FY12	FY13		FY11	FY12	FY13	FY12	FY12
Semis												
Intel	Dec	20.69	115,409	2.0	2.0	2.1	27%	10.5	10.7	10.1	2.1	21.0
Qualcomm	Sep	51.69	83,620	2.8	3.0	3.1	17%	18.8	17.1	16.7	2.9	17.9
TI	Dec	33.38	39,193	2.5	2.6	2.7	43%	13.1	12.8	12.2	3.3	27.4
TSMC	Dec	74.5	66,184	6.1	6.0	6.2	32%	11.7	11.8	12.0	2.9	24.4
Hardware												
Cisco	Jul	20.79	115,234	1.6	1.8	1.9	16%	13.0	11.3	10.8	2.2	20.4
Dell	Jan	14.011	27,045	1.4	1.5	1.6	20%	9.2	8.8	8.8	2.7	24.7
Nokia	Dec	8.025	38,874	0.5	0.7	0.6	25%	14.9	12.1	13.4	2.2	16.6
Apple	Sep	342.455	315,416	19.5	22.7	25.1	22%	17.2	14.8	13.7	3.9	26.1
Software												
Microsoft	Jun	28.22	241,437	2.5	2.7	2.9	13%	11.4	10.4	9.6	3.6	39.4
Oracle	May	31.04	156,827	2.1	2.3	2.6	30%	14.8	13.4	11.9	3.4	25.4
SAP	Dec	37.72	59,858	2.1	2.5	2.7	24%	18.1	15.3	14.0	3.7	24.7
Services												
Accenture	Aug	48.11	34,230	3.1	3.5	3.9	15%	15.4	13.8	12.2	8.2	79.2
Capgemini	Dec	34.255	6,902	2.0	2.5	2.8	4%	17.8	14.2	12.2	1.2	8.9
Infosys	Mar	3331.95	42,271	121.2	145.1	168.2	15%	27.4	22.9	19.8	5.4	26.3
TCS	Mar	1108	48,002	43.2	49.7	58.1	19%	25.5	22.1	18.9	6.6	33.7
Cognizant	Dec	75.335	22,863	2.4	2.8	3.3	21%	31.2	27.7	23.0	5.3	21.5
Integrated												
IBM	Dec	147.64	183,422	11.4	12.6	13.9	12%	12.9	11.6	10.6	5.9	53.4
Samsung	Dec	913000	119,691	97,708	95,672	105,945	21%	9.5	9.7	8.6	1.3	16.2
HP	Oct	44.86	98,262	5.2	5.7	6.0	18%	8.5	7.8	7.5	1.8	24.7

Source: Bloomberg, RCML Research

Key risks to a tech cycle

Sluggishness in US economic recovery

While US corporate health has clearly been improving over the past year, concerns linger over the revival in the consumer space. Retail sales have picked up, but they are still below pre-recession levels. Unemployment rates remain high and could limit consumer electronic spending. This in turn could hamper the tech cycle, in our view.

Corporate IT budgets remaining flat

In order to enable the start of a new tech cycle, we believe corporates would have to raise their IT budgets in order to meet the higher spending requirements for hardware and software refreshes. If IT budgets remain at current levels, we would at best see a weaker-than-expected tech cycle.

Appendix

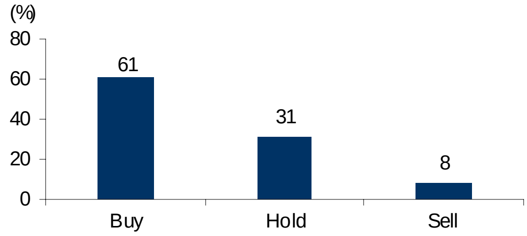
Constituents of our study

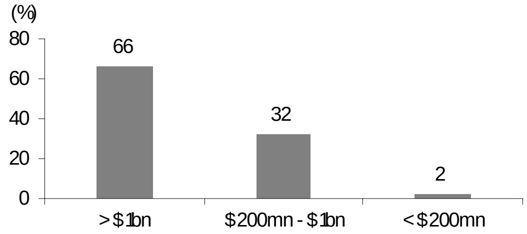
Tech segments	Sample set
Semiconductors	10 leading IDMs and fabless companies
Hardware	20 leading hardware companies from fields including PC/servers, communications, consumer electronics and storage We have excluded Apple in this field as it distorts the picture due to its high growth and innovation in creating new consumer segments
Software	16 software companies in both consumer and enterprise segments
Services	15 services companies across service domains and geographies. The list also includes 4 top Indian IT players—Infosys, TCS, Wipro and Cognizant.
Customer segments	
BFSI	14 leading BFSI companies and top outsourcers in the vertical
Manufacturing	13 manufacturing companies and top outsourcers in the vertical Sample included autos, industrials and manufacturing companies
Telecom	13 telecom service providers
Retail	18 companies including general retailers, electronic retailers and consumer goods players
Technology	9 large IT outsourcing technology companies including Microsoft, Cisco and Apple
Healthcare	11 healthcare companies in the US and Europe including pharmaceutical & healthcare players and life insurance providers
Energy and Travel & Logistics	Energy: 9 large oil & gas exploration and drilling service providers Travel & Logistics: 5 companies that are large IT outsourcers

In our compilation, we have retrospectively adjusted for any major acquisitions and have split the revenues of large integrated players into respective areas. For example, we have adjusted IBM revenues across hardware, software and services segments and adjusted HP revenues for the EDS acquisition, etc.

Coverage Profile

By recommendation	By market cap (US$)





Recommendation interpretation

Recommendation	Expected absolute returns (%) over 12 months
Buy	More than 15%
Hold	Between 15% and –5%
Sell	Less than –5%

Recommendation structure changed with effect from March 1, 2009

Expected absolute returns are based on share price at market close unless otherwise stated. Stock recommendations are based on absolute upside (downside) and have a 12-month horizon. Our target price represents the fair value of the stock based upon the analyst's discretion. We note that future price fluctuations could lead to a temporary mismatch between upside/downside for a stock and our recommendation.

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