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Tata Consultancy Services (TCS)**(Rs 1155, FY09E - P/E 23x FY09E, BUY with a target price of Rs. 1518)****Quarter Ended: Under US GAAP**

(Rs Mn)	Q1FY07 (A)	Q4FY07 (A)	Q1FY08 (A)	QoQ Var%	YoY Var%	Q1FY08 (P)	Deviation from our estim.
Revenues (Rs Mn)	41,443.0	51,463.7	52,028.2	1.1	25.5	52,144.0	(0.2)
EBIT %	22.4	25.6	23.1	(253.3)	70.7	23.5	43.7
EBIT	9,265.0	13,172.7	11,999.3	(8.9)	29.5	12,253.8	(2.1)
Net Profit Before EO	8,625.7	11,149.9	11,855.0	6.3	37.4	11,153.1	6.3
Net Profit After EO	8,625.7	11,727.9	11,602.0	(1.1)	34.5	11,153.1	4.0

Source: Company and Emkay Private Client Research

EO: Extraordinary Items includes Rs 578 mn for Q4FY07 (sale of 40% stake in Sitel JV) and Rs 253 mn for Q1FY08 (Tax reversal)

Q1FY08 Result: Better than expectations

After a lackluster performance in Q4FY07, TCS has tactically combat the rising rupee environment, and reported a better than expected numbers for Q1FY08. On a consolidated basis, revenues grew by 1% QoQ in rupee terms, which was quite inline with the expectations, however in \$ term its reported a sequential growth of 8% QoQ.

On the other hand, despite facing odds from rising rupee environment coupled with wages hikes and visa cost, TCS has managed to negate margin decline to certain extent with better utilization, SG&A leverage and productivity improvement. For Q1FY08. EBIT margin sequentially declined by around 253bps to 23.1, which was quite inline with our expectations.

For Q1FY08, other income was significantly higher by 374% to Rs 1516 mn, which was primarily on account of Rs1070 mn gain from hedging. Thus, net profit before EO was up by 6.3% QoQ and 37.4% YoY to Rs 11855 mn, which was higher than our expectations. After considering EO (40% stake sale in Sitel JV) in Q4FY07, and tax write back of Rs 253 mn, net profit for the quarter under review was marginally down by 1% QoQ and up by 34.5 YoY.

Operational and Financial Highlights:**Revenue: Inline with expectations**

- ❑ In \$ term revenues grew by 8% for Q1FY08. For Q1FY08, volume grew by around 7.6%, as compared to 6.4% in Q4FY07, blended pricing improvement at 0.6% QoQ.
- ❑ Revenue growth was negatively impacted by 660 bps on account of rupee appreciation.
- ❑ Top 5 and Top 10 clients grew by 10.8% and 11.3% respectively.
- ❑ Among the industry vertical, Life Science and Healthcare with 40% QoQ growth, followed by BFSI and Energy and Utilities growth remains 12.5% QoQ.

Net profit before EO up by 6% QoQ

Revenues in \$ term grew by 8% QoQ

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- Healthy clients ramps up seen across the clients accounts, clients in the \$1 mn run rate increases by 25 to 322 as compared to 297 in Q4FY07, Clients in \$20 mn and \$10 mn run rate increases by 6 and 10 respectively to 45 and 85 at the end of Q1FY08. For the quarter under review, clients in \$100 mn brackets increases to 6 from 3 in Q4FY07.

EBIT Margin: Declined by 250 bps QoQ, inline with expectation

EBIT margin for the quarter under review declined by 250bps to 23.1%, which was inline with our expectations.

- ❖ During the quarter under review, margin was negatively impacted by rupee appreciation to the extent of 258 bps; wages hikes impacted margins by around 208 bps and increase in the SG&A expenses. Nevertheless, with improvement in the employee productivity coupled with scale benefits has restricted the margins fall to 250 bps at 23.1% for Q1FY8.

Operational efficiency restrict margin fall to 250bps QoQ

Other key Metrics:

- ❖ Total number of active clients stood at 771, added 54 new clients during Q1FY08.
- ❖ Repeat business gone up to 99.2% for Q1FY8 as compared to 94.9% in Q4FY07.
- ❖ Offshore revenues contribution stood at 41.1% as compared to 41.3% in Q4FY07. Revenues contribution from GDC was stood at 4.6% as compared to 4.1% in Q4FY07.
- ❖ Utilization rates including trainees improved to 76% as compared to 74.7% in Q4FY07. Utilization rates excluding trainees marginally declined to 79.1% as compared to 79.6% in Q4FY07.
- ❖ TCS has added 8706 gross employees for Q1FY08, total employees strength stood 94902 at the end of Q1FY08.
- ❖ Attrition rate stood at 11.5%, attrition rate in IT services stood at 11% and BPO at 16.7% on LTM basis.
- ❖ Total forex hedge stood at \$2.5 bn for next two years, and \$1.75 bn for fiscal 08.
- ❖ Pursuing 20 deals worth \$50 mn and some more than \$100mn.

Forex cover stood at \$2.5 bn

Business Outlook and Valuation: Aggressive hedging mechanism

TCS with its mammoth scale and global delivery capability is better off among the Indian IT companies to combat the rising rupee environment, which was Clearly depicted in the performance of quarter gone by.

Going forward, deals pipelines are getting stronger and we don't witness any kind of concern from the management comment on secular demand environment, further robust growth in the industry and services verticals coupled with healthy clients transformation and 3-4% pricing increases in contracts renewals, assures strong business traction for TCS.

Nevertheless, rising rupee is still a cause for concern for entire Indian IT sector and TCS is no exception. Going forward, we expect EBIT margins to remain under pressure in the short to medium term, however improvement in pricing coupled with continual productivity improvement will offset margin contraction to certain extent.

On the other hand, with TCS aggressive hedging mechanism and hedge cover of \$2.5bn will provide some cushions to maintain the net margin in rising rupee scenario.

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We have marginally revised our estimates for FY08E and FY09E. We expect TCS revenue and net profit to grow at a CAGR of 27% and 24% respectively over FY07A-09E.

Financial Estimates -

Year Ended	Old Estimates			Revised Estimates		Implied Change (%)	
	FY07A	FY08E	FY09E	FY08E	FY09E		
Net Sales (Rs Mn)	186332.1	246717.5	311610.3	233620.1	300612.3	(5.3)	(3.5)
EBIT Mn)	46444.4	59705.6	74786.5	56068.8	71150.4	(6.1)	(4.9)
EBIT%)	24.9	24.2	24.0	24.0	23.7	(20.0)	(33.1)
PAT (Rs Mn)	41315.3	53085.7	66200.2	50383.2	63899.8	(5.1)	(3.5)
EPS (Rs)#	42.2	54.2	67.6	51.1	64.9	(5.7)	(4.1)
P/E (x) @ Rs 1155	27.5	21.4	17.2	22.7	17.9		

Maintain BUY with a target price of Rs 1518

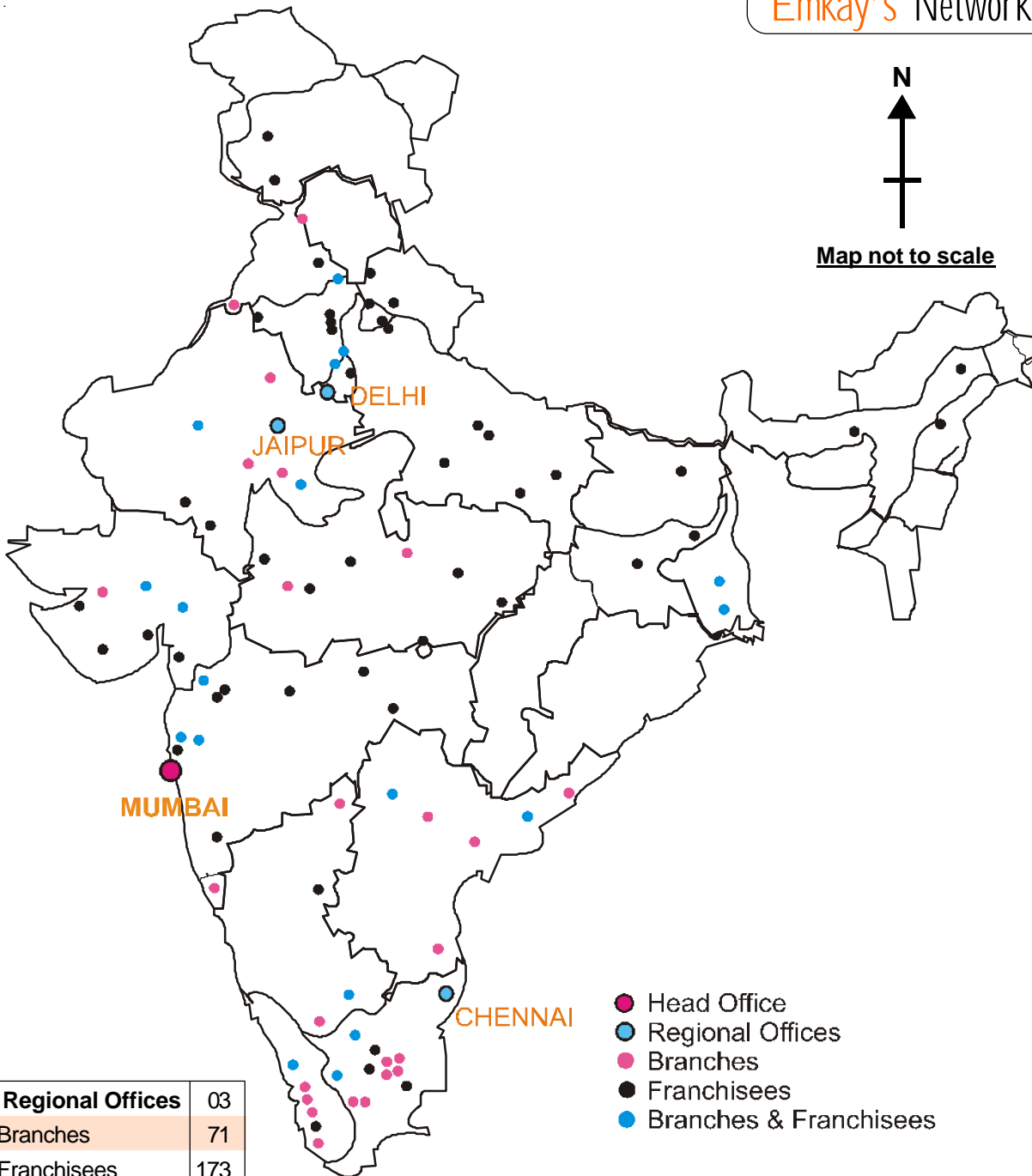
Source: Emkay Private Client Research

TCS stock trades at a P/E of 23x FY08E and 18x FY09E, we continue to maintain a BUY on TCS with target price of Rs 1518, at our target price the stock will be valued at 30x for FY08E earning and 23x FY09E.

Emkay's Network



Map not to scale



Total Regional Offices	03
Total Branches	71
Total Franchisees	173

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