

Company Flash

12 March 2008 | 5 pages

Tata Consultancy Services (TCS.BO)

Citi India Conference 2008: Day 2 Takeaways

- Conference takeaways** — TCS spoke with investors at the Citi India Investor Conference 2008. Here are some of the highlights of that presentation.
- Cautious in near term** — TCS indicated that a couple of large clients have cut IT budgets and delayed further projects. With the business environment remaining uncertain, TCS remains cautious in the near term.
- Pipeline solid** — However, pipeline remains very strong and is up 2.5x yoy – implying continued momentum in offshoring.
- Wage hikes to moderate** — Wage hikes are expected to moderate to ~10-12% yoy from the 12-15% levels in the last few years. All the Tier I companies presenting in our conference till now have supported the view that wage hikes are likely to moderate this year after high increase over the last few years.
- Pricing remains stable** — TCS has not witnessed any pricing pressure till now and is looking at price hikes from select customers going forward.

Buy/Medium Risk	1M
Price (12 Mar 08)	Rs832.70
Target price	Rs1,165.00
Expected share price return	39.9%
Expected dividend yield	1.7%
Expected total return	41.6%
Market Cap	Rs814,889M
	US\$20,191M

Price Performance (RIC: TCS.BO, BB: TCS IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2006A	29,074	29.71	39.1	28.0	14.0	64.3	0.8
2007A	40,608	41.50	39.7	20.1	9.2	55.1	1.4
2008E	50,817	51.93	25.1	16.0	6.5	47.2	1.7
2009E	57,077	58.33	12.3	14.3	4.9	38.9	1.9
2010E	63,031	64.41	10.4	12.9	3.8	33.1	2.2

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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Tata Consultancy Services

Company description

TCS is India's largest and among the oldest IT companies. It is part of the diversified Tata Group, one of the largest corporate groups in Asia. It has more than 100,000 employees, including its subsidiaries, with marketing presence across 32 countries and development presence in 10 countries besides India. It provides a comprehensive range of IT services to industries such as banking and financial services, insurance, manufacturing, telecommunications, retail and transportation. It had more than 800 active clients, including six of the Fortune Top 10 companies in the US. The company started with data processing work in 1968, and was the first to provide offshore services in 1974. Over the last three decades, the company has come a long way with deep technical and project management expertise in handling complex client projects and strong offshore processes.

Investment strategy

We rate TCS as Buy/Medium Risk (1M) based on a fundamental 12-month view. As India's largest and most experienced IT services firm, TCS looks well positioned to benefit from the growing demand for offshore IT services. It is a well-regarded stock among investors familiar with India and the IT-services sector. We believe TCS' margins in its international IT services business (around 95% of EBIT) are likely to trend down over the next few years. However, we expect this decline to be relatively modest, as we expect positive leverage from a better onsite-offshore mix, more hiring of fresh graduates, and improved utilization with a strong demand outlook to offset margin pressures from wage inflation. We expect revenue CAGR of 21.8% and an EPS CAGR of 16.9% in FY07-10E.

Valuation

Our target price of Rs1,165 is based on 19x average of FY09-10E EPS, derived from a small discount to our target 21x for Infosys, TCS's closest peer on business model. We expect TCS to continue to trade at slightly lower multiples than Infosys due to investors' greater comfort and familiarity with Infosys and the periodic supply of additional stock by Tata Sons. Our target price assumes a one-year forward P/E of 15-20% above the average BSE Sensex multiple, which we think is justified given TCS' superior FCF, RoIC and growth rates than the overall market, and it actually implies a slightly lower premium than that for Infosys. We believe P/E remains the most appropriate valuation measure given TCS' profitable track record and strong earnings visibility.

Risks

Although our quantitative risk-rating system suggests Low Risk for TCS, we rate TCS as Medium Risk given the similar risk ratings for other similar-sized IT peer-group companies in our coverage universe. The key downside risks that could impede the stock from reaching our target price include: (1) any significant appreciation of the rupee against the US Dollar/Euro/GBP; (2) a sharp slowdown in the US economy; (3) H1B visa quotas; (4) large exposure to fixed-price contracts; (5) higher onsite revenue contribution (~53% of total); and (6) acquisition-related risks, including M&A with other Tata-group IT firms

Appendix A-1

Analyst Certification

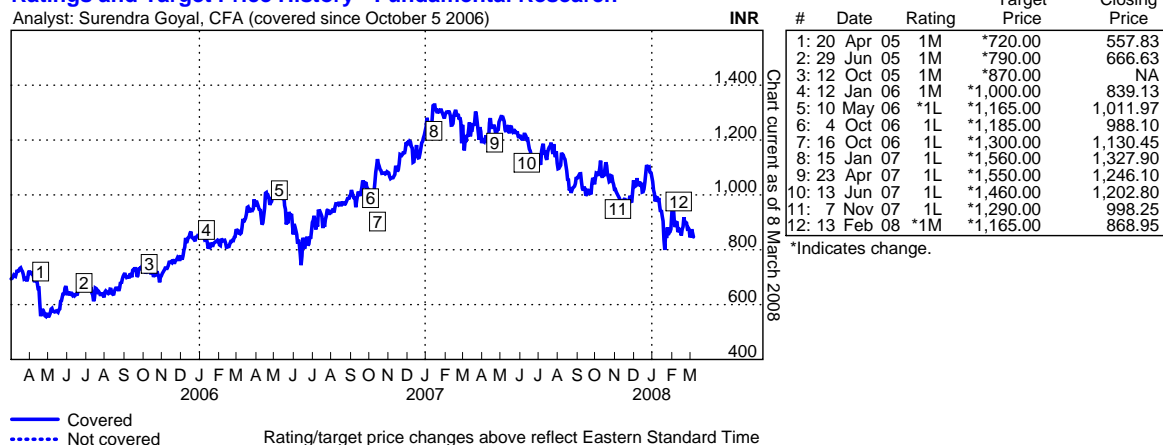
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Tata Consultancy Services (TCS.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Surendra Goyal, CFA (covered since October 5 2006)



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