

**BUY****Rs 1,906.5****Sensex: 11,540, Nifty: 3,425****Stock data**

Bloomberg	TCS IN
Reuters	TCS.BO/TCS.NS
Shares outg (mn)	489
Market cap (Rs bn)	932
Market cap (US\$ bn)	21
3-m dly avg vol	526,106

**Share price performance**

52-week high/low (Rs)	2005/1091		
	-1m	-3m	-12m
Abs (%)	2.4	17.7	44.6
Rel* (%)	(3.5)	(4.2)	(33.1)

\*to Nifty

**Financial snapshot**

Rs mn

YE March	FY06	FY07E	FY08E
Net sales	132,550	178,284	229,918
(%) chg	36.3	34.5	29.0
Net Income*	28,968	38,116	47,976
(%) chg	41.2	31.6	25.9
EPS (Rs.)	59.2	77.9	98.1
(%) chg	38.5	31.6	25.9
P/E (x)	32.2	24.5	19.4
ROE (%)	64.8	52.5	43.6
ROCE (%)	75.8	62.1	51.3

\* After extraordinary items

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**Tata Consultancy Services****April 18, 2006****Results in line, bonus issue would boost stock sentiment**

Tata Consultancy Services (TCS) reported revenues and net profit of Rs7.3bn and Rs 8.1bn in Q4FY06, a sequential increase of 8.1% and 7.9%, respectively. As TCS merged Tata Infotech with itself from Q4FY06, it declared the consolidated numbers for Q4FY06 and Q3FY06, without the standalone numbers for Q4FY06.

We are increasing our FY07E and FY08E estimates to factor in a) merger of Tata Infotech and b) increased visibility, going forward, as the company expects to add 23,000 net employees in FY07E as against 20,766 in FY06.

We expect TCS to post revenues of Rs178.3bn and Rs229.9bn in FY07E and FY08E, respectively, an increase of 8.4% and 10.6% from our previous estimates. This translates into an EPS of Rs77.9 and Rs98.1 in FY07E and FY08E indicating growth of 31.6% and 25.9%, respectively.

TCS also announced a 1:1 bonus issue that we believe is likely to boost the stock sentiment. At the current PER of 24.5X FY07E earnings, we maintain our Buy on the stock.

**The key highlights of the Q4FY06 results were:**

- ◆ **Volume growth drives revenue growth:** The consolidated entity (TCS + Tata Infotech) posted a sequential revenue growth of 8.1%, driven wholly by an 8.2% volume growth. A 0.9% appreciation in rupee impacted revenues but higher onsite contribution negated it. With the Pearl group deal beginning to contribute from Q1FY07, we believe that future growth too would be volume driven.
- ◆ **Rupee appreciation and higher onsite component impacts margins:** The EBITDA margins reduced by 110 bps on account of a) higher onsite revenues and b) 0.9% rupee appreciation. Though it is difficult to calculate the impact of the merger of Tata Infotech on the margins of TCS in Q4FY06 due to lack of data, the EBITDA margins in Q3FY06 reduced by 80 bps due to the merger. Going forward, we believe that there could a 90 bps drop in EBITDA margins in FY07E on account of a) 15% offshore and 3% onsite salary hikes and b) some of the large deals won by the company in the last few months are expected to start from FY07E onwards. These deals have lower margins for two-three quarters which is expected to impact the EBITDA margin of TCS.
- ◆ **Higher other income and lower taxes boost net income:** The company posted an other income of Rs16mn in Q4FY06 as against a loss of Rs154mn in Q3FY06. Further, the company wrote back assets to the tune of Rs310 mn in Q4FY06 that reduced the effective tax rate from 14.9% in Q3FY06 to 9.6% in Q4FY06. Due to the higher other income and lower tax, the company posted a 10.9% sequential increase in net income (before one-off items) to Rs8.3bn. However, the company wrote off Rs232mn in

Q4FY06 as Tata Infotech gave shares and cash to some of its employees before the merger. This led to net income reducing to Rs8.09bn –a sequential increase of 7.9%.

- ◆ **Guidance:** Though TCS does not give revenue and profit guidance, it indicated an addition of 23,000 net employees in FY07E as against 20,766 employees in FY06. The increased hiring shows that the company has good visibility, going forward.
- ◆ **Forecast:** We have increased our FY07E and FY08E estimates to factor in the Tata Infotech merger. We estimate the company to post revenues of Rs178.3bn and profit of Rs38.1bn in FY07E, a growth of 34.5% and 31.6%, respectively. We expect the company to post an EPS of Rs77.9 and Rs98.1 in FY07E and FY08E, an increase of 2.9% and 5.1% from our previous estimates.
- ◆ **Valuations:** At the current PER of 24.5X FY07E and 19.4X FY08E earnings, we believe that there are still some upsides for investors. Hence, we maintain a Buy for TCS with a price target of Rs2,100 at 27X FY07E earnings.

Quarterly result table

Rs mn

	Q4 FY06	Q3FY06	QoQ (%)	Q4FY05*	YoY (%)
Revenues	37,328	34,527	8.1	25,846	44.4
Cost of revenues	19,850	18,064	9.9	13,324	49.0
Gross profit	17,479	16,462	6.2	12,522	39.6
GPM	46.8	47.7		48.4	
Operating expenses	7,341	6,696	9.6	5,203	41.1
Operating profit	10,137	9,767	3.8	7,318	38.5
OPM	27.2	28.3		28.3	
Depreciation	861	738	16.7	509	69.1
EBIT	9,276	9,029	2.7	6,809	36.2
EBIT (%)	24.9	26.2		26.3	
Other income	16	-154		-414	
PBT	9,293	8,875	4.7	6,396	45.3
Tax	896	1,319	-32.1	834	7.4
PAT before exceptional items & minority interest	8,397	7,556	11.1	5,561	51.0
Minority interests	-103	-48		115	
Equity in net earnings of affiliates	33	-3		1	
One-off items	-232	-3		979	
PAT after exceptional items and minority int.	8,094	7,502	7.9	4,698	72.3

\* excl Tata Infotech

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