

## Company

6 September 2010 | 7 pages

# Tata Consultancy Services (TCS.BO)

 Equity 

## Takeaways from India Investor Conference, Sept 6-7

- Takeaways from India Conference** – Tata Consultancy Services (TCS) presented at Citi's India Conference on September 6-7. Below are key takeaways.
- Demand robust** - TCS indicated that demand continued to be strong. US continues to do well. Within Europe, UK is doing well, while rest of Europe is still relatively slow. BFSI continues to lead growth - demand is well spread rather than being M&A driven.
- Supply side manageable** - TCS does not expect further wage hikes this year. Variable component of wages could be higher - function of performance. Q2 could see some impact of promotions - could impact margins by ~70 bps. Offshore wage hike could effectively be ~13% for the year including promotions. TCS remains confident of delivering margins of ~27% for FY11.
- Other key points** - (a) Utilization at close to peak levels - comfort zone is 77-79% ex trainees; (b) Telecom segment underperformance is due to client specific issues - has bottomed out. (c) Diligenta progressing well (recently announced a deal) - expect breakeven in the course of the year. (d) Visa costs - the increase in visa cost will not impact margins meaningfully. (e) Cloud computing an area of focus - TCS highlighted its initiatives in this space.
- Commentary from both TCS/Infosys largely similar** - (a) FY11 visibility high - no let-up in demand as of now; (b) US leading growth; UK doing well; rest of Europe a little slow; (c) Supply side manageable; visa costs to have minimal impact on margins; (d) IT budgets for CY11 the key - clients communicate their budgets early next year (assuming normal budgeting cycle).

<b>Hold/Low Risk</b>	<b>2L</b>
Price (06 Sep 10)	Rs853.10
Target price	Rs930.00
Expected share price return	9.0%
Expected dividend yield	1.3%
<b>Expected total return</b>	<b>10.3%</b>
Market Cap	Rs1,669,705M US\$35,919M

### 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)	(%)	(%)
2009A	51,721	26.42	3.0	32.3	10.7	37.0	0.8
2010A	68,729	35.11	32.9	24.3	8.0	37.6	2.3
2011E	80,009	40.87	16.4	20.9	6.3	33.7	1.3
2012E	89,104	45.52	11.4	18.7	5.0	29.7	1.3
2013E	99,239	50.70	11.4	16.8	4.1	26.6	1.3

Source: Powered by dataCentral

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Fiscal year end 31-Mar	2009	2010	2011E	2012E	2013E
<b>Valuation Ratios</b>					
P/E adjusted (x)	32.3	24.3	20.9	18.7	16.8
EV/EBITDA adjusted (x)	22.9	18.9	15.6	13.3	11.4
P/BV (x)	10.7	8.0	6.3	5.0	4.1
Dividend yield (%)	0.8	2.3	1.3	1.3	1.3
<b>Per Share Data (Rs)</b>					
EPS adjusted	26.42	35.11	40.87	45.52	50.70
EPS reported	26.42	35.11	40.87	45.52	50.70
BVPS	79.97	107.03	135.89	170.41	210.11
DPS	7.00	20.00	11.00	11.00	11.00
<b>Profit &amp; Loss (RsM)</b>					
Net sales	278,129	300,289	356,280	417,168	481,265
Operating expenses	-212,114	-220,698	-261,706	-310,119	-360,749
<b>EBIT</b>	<b>66,015</b>	<b>79,591</b>	<b>94,574</b>	<b>107,049</b>	<b>120,516</b>
Net interest expense	-4,673	2,255	3,373	8,520	12,322
Non-operating/exceptionals	-6	-10	0	0	0
<b>Pre-tax profit</b>	<b>61,336</b>	<b>81,836</b>	<b>97,947</b>	<b>115,569</b>	<b>132,838</b>
Tax	-9,011	-12,089	-16,850	-25,377	-32,511
Extraord./Min.Int./Pref.div.	-604	-1,018	-1,088	-1,088	-1,088
<b>Reported net income</b>	<b>51,721</b>	<b>68,729</b>	<b>80,009</b>	<b>89,104</b>	<b>99,239</b>
Adjusted earnings	51,721	68,729	80,009	89,104	99,239
Adjusted EBITDA	71,781	86,800	102,659	116,226	130,863
<b>Growth Rates (%)</b>					
Sales	21.7	8.0	18.6	17.1	15.4
EBIT adjusted	23.0	20.6	18.8	13.2	12.6
EBITDA adjusted	20.9	20.9	18.3	13.2	12.6
EPS adjusted	3.0	32.9	16.4	11.4	11.4
<b>Cash Flow (RsM)</b>					
<b>Operating cash flow</b>	<b>71,458</b>	<b>30,303</b>	<b>102,463</b>	<b>80,194</b>	<b>87,135</b>
Depreciation/amortization	5,766	7,209	8,085	9,178	10,347
Net working capital	8,694	-44,398	16,654	-10,655	-11,217
<b>Investing cash flow</b>	<b>-12,673</b>	<b>-53,876</b>	<b>-37,906</b>	<b>-20,108</b>	<b>-14,955</b>
Capital expenditure	-7,495	-11,421	-22,798	-18,575	-19,799
Acquisitions/disposals	11,907	-16,382	3,845	8,520	12,322
<b>Financing cash flow</b>	<b>-18,995</b>	<b>-14,183</b>	<b>-23,512</b>	<b>-21,533</b>	<b>-21,533</b>
Borrowings	-1,788	621	0	0	0
Dividends paid	-13,703	-39,151	-21,533	-21,533	-21,533
<b>Change in cash</b>	<b>39,791</b>	<b>-37,756</b>	<b>41,045</b>	<b>38,553</b>	<b>50,648</b>
<b>Balance Sheet (RsM)</b>					
<b>Total assets</b>	<b>226,858</b>	<b>274,546</b>	<b>347,869</b>	<b>427,009</b>	<b>516,893</b>
Cash & cash equivalent	13,440	10,249	68,687	116,206	173,243
Accounts receivable	60,463	58,098	81,944	95,949	110,691
Net fixed assets	37,494	41,706	56,419	65,816	75,268
<b>Total liabilities</b>	<b>67,215</b>	<b>60,978</b>	<b>77,803</b>	<b>89,372</b>	<b>101,550</b>
Accounts payable	0	0	0	0	0
Total Debt	7,913	3,417	3,383	3,383	3,383
<b>Shareholders' funds</b>	<b>159,643</b>	<b>213,568</b>	<b>270,065</b>	<b>337,637</b>	<b>415,343</b>
<b>Profitability/Solvency Ratios (%)</b>					
EBITDA margin adjusted	25.8	28.9	28.8	27.9	27.2
ROE adjusted	37.0	37.6	33.7	29.7	26.6
ROIC adjusted	49.1	42.8	44.5	44.5	43.1
Net debt to equity	-3.5	-3.2	-24.2	-33.4	-40.9
Total debt to capital	4.7	1.6	1.2	1.0	0.8

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## Tata Consultancy Services

### Company description

TCS is the largest and among the oldest IT companies in India. It is a part of the diversified Tata Group, one of the largest corporate groups in Asia, with more than 160,000 employees (including subsidiaries). It provides a comprehensive range of IT services to industries such as Banking & Financial Services, Insurance, Manufacturing, Telecom, Retail and Transportation. It has more than 900 active clients. The company started with data processing work in 1968, and was the first to provide offshore services in 1974. Over the past three decades, it 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 Hold/Low Risk (2L). The company has benefitted significantly from the return of spends in the BFSI segment and we are worried that this might taper off. We may see good growth in FY11 due to pent up demand, however, we are concerned that expectations are running ahead of reality. Its earlier valuation discount vis-à-vis Infosys has virtually ceased to exist.

### Valuation

Our target price of Rs930 is based on 21x Dec'11E EPS. Given that businesses are bottoming and we estimate TCS' earnings will grow at an ~13% CAGR over FY10-13E, we believe the stock should trade closer to the higher end of its historical three-year trading range of 7-27x 12-month forward earnings. We believe PE remains the most appropriate valuation measure given TCS' past profitability and future earnings visibility.

### Risks

We rate TCS Low Risk which is inline with our quantitative risk-rating system, which tracks 260-day historical share price volatility. Key downside risks that could cause the shares to be lower than our target price are: (1) any significant appreciation of the rupee against the USD/EUR/GBP; (2) a prolonged recession in the US; and (3) any margin-dilutive acquisition. Key upside risks that could cause the shares to be higher than our target price are: (1) any significant depreciation of the rupee against the USD/EUR/GBP; (2) aggressive pent up demand from corporates in the US; and (3) any margin accretive acquisition.

# Appendix A-1

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Analyst: Surendra Goyal, CFA



Chart current as of 4 September 2010

Date	Rating	Target Price	Closing Price
1 7-Nov-07	1L	*645.00	499.13
2 13-Feb-08	*1M	*582.50	434.48
3 26-Jun-08	1M	*587.50	438.43
4 23-Jul-08	*2M	*462.50	429.25
5 23-Oct-08	2M	*312.50	273.73

Date	Rating	Target Price	Closing Price
6 20-Nov-08	*2H	*280.00	234.75
7 28-Apr-09	*3M	*307.50	299.30
8 10-Jun-09	*1L	*465.00	390.88
9 17-Jul-09	1L	*525.00	433.60
10 26-Aug-09	1L	*630.00	548.30

Date	Rating	Target Price	Closing Price
11 19-Oct-09	1L	*695.00	599.00
12 7-Jan-10	1L	*855.00	714.65
13 22-Apr-10	*2L	855.00	785.30
14 24-Aug-10	2L	*930.00	868.90

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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