

Tata Consultancy Services

Cost cutting measures being stepped up, Expect margin resilience in FY10, Remain fundamental positive but expect near-term weakness - ALERT

- **TCS is looking to reduce variable portion of employee salaries, has increased working hours of employees, and could defer joining dates of fresh graduates as per a news article in the *Business Standard*. These cost cutting measures are largely inline with our expectations and reinforce our view that top tier Indian IT companies would be able to defend margins in FY10E despite pricing pressure.**
- **However revenue growth remains the key variable of debate - we continue to believe that top tier players can deliver flat revenues in FY10E due to market share gains and Satyam issue. Given low investor expectations, flat revenue/EPS would be enough to drive share price outperformance in our view leading to our positive fundamental view on Infosys and TCS. However, 4QFY09 should be a tough quarter as companies absorb most of the impact of reduction in prices leading to our near-term cautious view.**
- **Variable salary reduction:** As per a newspaper report in the *Business Standard*, TCS is planning to review the variable component of employees' salaries. Variable pay accounts for 20-35% of TCS employees' gross salary, depending on their hierarchy. Further manpower cost accounts for 50%+ of revenues and hence reducing variable salaries can give as much as 500-800 bps of cushion on margins in our view. While TCS is not contemplating cutting fixed salaries at this stage, we believe that this remains an option if environment gets worse.
- **TCS is also increasing employee working hours** from 40 hours a week to 45 hours a week, with effect from April 1, 2009 as per Mr Ramadorai, company CEO. This would increase productivity per employee by 10%+, a significant advantage to margins.
- **Other steps:** TCS may also defer absorbing nearly 24,500 campus recruits, scheduled to join in June. Further, the company is looking to cut on capital expenditure plans and delay infrastructure building and new projects. Management is also looking to lay-off people delivering below-par performance.

Overweight

TCS.BO, TCS IN
Price: Rs480.60

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eBusiness/IT Services

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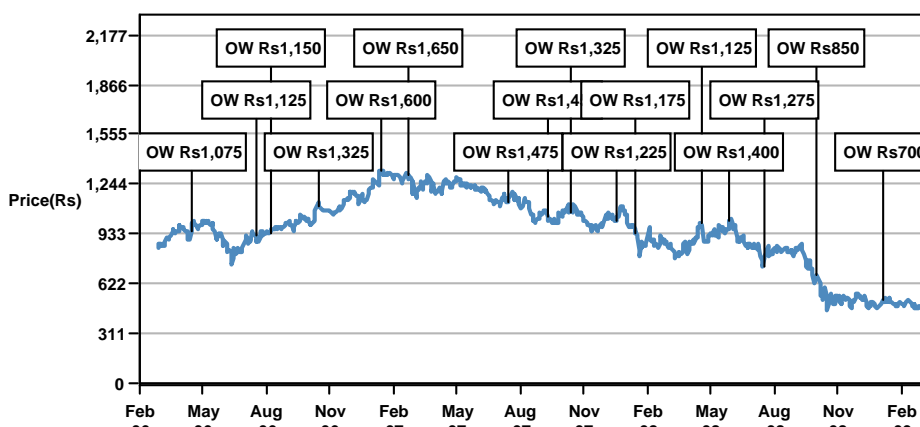
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Tata Consultancy Services (TCS.BO) Price Chart



Source: Reuters and J.P. Morgan; price data adjusted for stock splits and dividends.

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Date	Rating	Share Price (Rs)	Price Target (Rs)
17-Apr-06	OW	951.80	1075.00
19-Jul-06	OW	920.88	1125.00
08-Aug-06	OW	936.00	1150.00
16-Oct-06	OW	1104.75	1325.00
15-Jan-07	OW	1327.90	1600.00
21-Feb-07	OW	1297.20	1650.00
16-Jul-07	OW	1127.90	1475.00
10-Sep-07	OW	1046.95	1450.00
15-Oct-07	OW	1063.10	1325.00
20-Dec-07	OW	1021.35	1225.00
16-Jan-08	OW	938.25	1175.00
21-Apr-08	OW	1000.90	1125.00
29-May-08	OW	1009.70	1400.00
17-Jul-08	OW	727.35	1275.00
02-Oct-08	OW	671.00	850.00
06-Jan-09	OW	515.00	700.00

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