Economy News

- A key group of ministers reached a consensus on allowing foreign airlines to buy up to 49% stake in Indian carriers. Foreign carriers are not currently allowed to directly or indirectly make any investment in Indian carriers. (BS)
- Gold and silver are set to cost more, with the government increasing the import and excise duties on these two precious metals. The new duty structure would be based on value, not a fixed rate. The new rates (on ad valorem basis) - 2% on 10 gm gold and 6% on one kg silver - mean that importers will have to pay double the duty. (BS)
- Standard & Poor's (S&P) cut its credit rating of the euro zone's European Financial Stability Facility (EFSF) rescue fund yesterday. S&P said in a statement the decision was all but inevitable following identical cuts three days earlier to the creditworthiness of France and Austria, two of the EFSF's guarantors. (BS)
- With a strong flow of portfolio investment in the capital market, the rupee closed at a two-month high of 50.71 against dollar. (BS)
- The Indian economy is likely to grow at 8% per annum between calendar years 2011 and 2013, said an United Nations report. The report, World Economic Situation and Prospects 2012, projected India's growth at 7.6 per cent in 2011, 7.7 per cent in 2012 and 7.9 per cent in 2013. (BS)
- China's economy expanded at its weakest pace in two-and-half-years in the latest quarter, with sagging real estate and export sectors heralding a sharper slowdown in coming months and fresh pro-growth measures from the government. (BS)

Corporate News

- In a major blow to **Essar Oil,** the Supreme Court rejected the company's 125% sales tax deferment benefit claim on its investment in the Vadinar refinery project. The company will now have to fork out at least Rs 63Bn in sales tax to the Gujarat government. (BS)
- **Maruti Suzuki India Ltd,** the country's top car maker, raised prices of all its models, sending its shares up as much as 11%, as investors rallied behind the company after months of falling sales appeared to have levelled in December. (BS)
- **Suzlon Energy Limited (SEL)** has signed an MoU with the Government of Andhra Pradesh for development of wind power generation capacity in the state totalling to 3,000 megawatt (Mw) between 2012 and 2016, creating potential investments of up to Rs 180Bn. (BS)
- **Reliance Communications (RCom)** has arranged loan for refinancing its $1.18-billion Foreign Currency Convertible Bonds (FCCBs) due on March 1, 2012 via Chinese lenders. The company, grappling with huge debt-redemption pressure has tied-up with the Chinese financiers to lower its refinancing costs. (BS)
- Buoyed by the influx of bookings for its newly-launched global sports utility vehicle (SUV) - XUV500 - **Mahindra & Mahindra (M&M)** is looking at scaling up the production capacity of the all-wheel drive vehicle at its Chakan plant near Pune to 3,000 units per month during the next fiscal. (BS)
- **Kingfisher Airlines** has told its creditors that the company is likely to receive support in form of equity infusion by end-March, said two bankers familiar with the matter. "They have said that they are looking at various possible options, and equity infusion is also not ruled out," said one of the bankers who attended a meeting of the beleaguered airline's lenders in Mumbai. (ET)
- **ONGC** is proposing to sign a Memorandum of Understanding (MOU) with ConocoPhillips for cooperation in exploration and development of shale gas and deepwater opportunities, a company official said. (BS)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange

Equity

	17 Jan 12	% Chg 1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	16,466	1.7	6.3	(1.7)
NIFTY Index	4,967	1.9	6.8	(1.4)
BANKEX Index	10,396	1.2	10.3	(5.2)
BSET Index	5,635	1.0	(1.4)	3.2
BSETCG INDEX	9,844	3.7	16.8	(7.9)
BSEOIL INDEX	7,903	2.8	3.0	(7.6)
CNXMcap Index	6,725	1.2	7.0	(5.8)
BSESMCAP INDEX	6,258	1.1	10.0	(8.7)
World Indices				
Dow Jones	12,482	0.5	5.2	7.8
Nasdaq	2,728	0.6	6.8	2.7
FTSE	5,694	0.6	5.7	5.2
NIKKEI	8,466	1.1	0.9	(3.0)
HANGSENG	19,628	3.2	7.1	8.3

Value traded (Rs cr)

	17 Jan 12	% Chg - Day
Cash BSE	2,651	28.5
Cash NSE	12,180	28.2
Derivatives	122,915	41.3

Net inflows (Rs cr)

	16 Jan 12	% Chg	MTD	YTD
FII	447	22.7	3,371	3,371
Mutual Fund	(102)	(774.8)	(659)	(659)

FII open interest (Rs cr)

	16 Jan 12	% Chg
FII Index Futures	13,608	10.3
FII Index Options	37,167	8.2
FII Stock Futures	27,826	2.1
FII Stock Options	1,541	7.2

Advances / Declines (BSE)

17 Jan 12	A	B	S	Total	% total
Advances	158	1,465	283	1,906	64
Declines	45	760	168	973	33
Unchanged	1	73	29	103	3

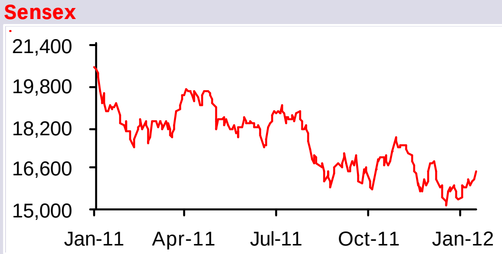
Commodity

	17 Jan 12	% Chg 1 Day	1 Mth	3 Mths
Crude (NYMEX) (US$/BBL)	101.2	0.5	8.2	14.5
Gold (US$/OZ)	1,656.5	0.8	3.4	(0.4)
Silver (US$/OZ)	30.1	0.5	1.7	(6.1)

Debt / forex market

	17 Jan 12	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	NA	NA	NA	NA
Re/US$	50.7	51.4	52.9	48.9

Sensex



HCL Technologies Ltd (HCLT)

Result Update

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Price: Rs.425 **Recommendation: BUY**
Target Price: Rs.499 **FY12E P/E: 13.1x**

HCLT's operating results were marginally above expectations. The 4.9% (5.1% in 1Q) volume growth in Software Services was above expectations. HCLT has achieved consistency in revenues, especially in Software Services, over the past few quarters. The 140bps improvement in margins was slightly higher than estimates. Average realizations were stable on a CC basis.

Management has indicated continuing headwinds for the industry in the form of an uncertain macro which is affecting decision making. On the other hand, it expects to continue to participate and win large deals in the next few quarters as the churn ratio in re-bidding of large IT outsourcing deals is very high (30% v/s 5% earlier). The company won orders with total contract value (TCV) of more than $1bn in 2Q. It added 57 new clients, which is also encouraging.

About $47bn worth of deals are expected to come up for restructuring in CY12. This should likely support the revenue growth for HCLT in future quarters. However, margins may remain range-bound as the company focuses on revenue growth, we believe (ex-rupee impact).

We have tweaked our earnings estimates for FY12. Rupee is expected to average 50 / USD in the remaining part of FY12 (v/s Rs.48 assumed earlier). This is expected to keep margins higher on a YoY basis, despite salary increments. EPS is expected to be Rs.32.3 (Rs.30.8 earlier) post ESOP-related charges. We have tweaked our PT to Rs.499 (Rs.496) as the increase in EPS estimates is largely led by the rupee depreciation. We continue to accord a valuation discount v/s larger peers due to the relatively lower margins. We maintain BUY, based on the near 17% upside potential. A sharp appreciation in the rupee against various currencies and a delay in recovery in major user economies remain the key concerns.

Summary table

(Rs mn)	FY10	FY11	FY12E
Sales	125,650	160,381	209,332
Growth (%)	18.2	27.6	30.5
EBITDA	25,728	27,491	37,668
EBITDA margin (%)	20.5	17.1	18.0
PBT	15,417	21,952	31,649
Net profit	12,152	16,197	22,819
EPS (Rs)	17.6	22.9	32.3
Growth (%)	0.9	30.7	40.9
CEPS (Rs)	24.8	30.0	40.4
BV (Rs/share)	101.7	119.5	147.7
Dividend / share (Rs)	4.0	4.0	4.0
ROE (%)	12.3	13.6	15.6
ROCE (%)	11.0	14.2	17.8
Net cash (debt)	(2,213)	2,769	6,953
NW Capital (Days)	63.9	57.0	63.4
P/E (x)	24.2	18.5	13.1
P/BV (x)	4.2	3.6	2.9
EV/Sales (x)	2.4	1.9	1.4
EV/EBITDA (x)	11.7	10.8	7.8

Source: Company, Kotak Securities - Private Client Research

2QFY12 results

(Rs.mn)	2QFY12	1QFY12	QoQ (%)	2QFY11	YoY (%)
Turnover	**52,452**	**46,513**	**12.8**	**38,884**	**34.9**
Expenditure	42,750	38,564		32,538	
Operating Profit	**9,702**	**7,949**	**22.1**	**6,346**	**52.9**
Depreciation	1,394	1,309		1,238	
Gross Profit	**8,308**	**6,640**		**5,108**	**62.6**
Interest	0	0		0	
Other Income	-670	59		-80	
PBT	**7,638**	**6,699**	**14.0**	**5,028**	**51.9**
Tax	1,911	1,728		1,031	
PAT	**5,727**	**4,971**	**15.2**	**3,997**	**43.3**
Share of income	0	0		0	
ESOP charge	199	171		252	
Minority interest	0	3		0	
Adj. PAT	**5,528**	**4,797**	**15.2**	**3,745**	**47.6**
Shares (mns)	706	706		706	
EPS (Rs) *	**7.8**	**6.8**		**5.3**	
OPM (%)	18.5	17.1		16.3	
GPM (%)	15.8	14.3		13.1	
NPM (%)	10.9	10.7		10.3	

Source : Company

Volume revenue growth of 5%

- Revenues grew by 13% sequentially in INR terms and by 2% in USD terms. In CC terms, revenues grew by 3.7% QoQ. Thus, the impact of cross currency movements was to the tune of about 1.7%.
- We understand that, the India revenues were also impacted, when converted in USD, because of the sharp rupee depreciation v/s USD. IMS business derives a sizeable part of revenues from India
- The 3.7% CC revenue growth was led by volumes, which grew by about 5% QoQ. This was better than our expectations and reflects the benefits of focus on value / innovation.
- Volume growth in Software services was 4.9%, which is encouraging. HCLT had also invested in demand generating initiatives over the past few quarters.
- Average realizations were stable on a CC basis in the Software Services business.
- The overall client profile has improved for HCLT. HCLT earned more than $100mn (annualized) revenues from 3 clients in 2Q as compared to 1 in 1Q.
- All the Top 10 clients of the company are in the Fortune 500 / Global 500 list.
- HCLT has also been penetrating deeper into its clients by offering diverse services. According to a data provided by the company, these clients use 3.4% of the 5 services offered by the company, which is encouraging.

Software services

- The CC revenue growth was at 5.3% QoQ.
- Volume growth at 4.9% was better than our expectations and was also higher than the 4% reported in the previous quarter. Average realisations were marginally higher, we understand.
- We opine that, this volume growth is the result of scale up in large deals won in the past few quarters, apart from the initiation of new accounts.
- In fact, the company won 18 deals during the quarter (12 transformational deals in 1Q) with TCV of more than $1bn. Some customers with whom the company signed the engagements include AstraZeneca, CEVA, etc. These deals spanned across all service lines.
- Within services, Enterprise Application Services and custom application services reported strong CC growth of 6.5% and 5.4%, respectively.
- The growth in engineering is encouraging and indicates higher outsourcing traction in this area. The management expects to grow this business significantly in future quarters on the back of additional outsourcing.
- Growth in custom applications also reflects that discretionary "Grow the business" spends are continuing in a cautious macro scenario. According to the management, discretionary spends remain high in emerging economies.
- Within geographies, US reported a 7.3% growth in CC terms. Europe pitched in with a 6.3% growth. The growth in Europe comes on the back of high growth rates in the past five quarters. This likely indicates improvement in demand scenario and increased spending by clients in that region.
- The management has indicated that, companies in the Financials Services space in Europe have initiated the vendor consolidation process and are opening up to appointing new vendors.
- HCLT has benefitted from this exercise and four out of the 18 new deals in 2Q are from these customers in Europe.
- Within verticals, Financial Services, Hitech / manufacturing and Retail / CPG reported strong traction. However, Telecom continued to remain impacted with a negative growth in CC terms.

Infrastructure services de-grew - CC at play

- Infrastructure services revenues de-grew marginally during the quarter.
- However, this was due to the sharp depreciation in INR. The sharp depreciation impacted the viability of a few projects, which were stopped and are being re-negotiated.
- Excluding these, the revenues grew at a decent pace of 4% QoQ.
- The IMS business already has more than 17000 employees who service more than 100 accounts. Some of the major accounts serviced are Nokia, Xerox, RDA, SGB, etc. HCLT currently manages more than 1mn devices for its clients.
- HCLT is now looking at penetrating the service deeper. It has carved out three new services with a view to give them increased focus - SI, managed MF services and telecom. The company is already providing significant services around these micro - businesses.
- This horizontalisation of existing services is expected to allow deeper penetration into existing clients while inviting new accounts also.

BPO revenues grew marginally

- After several quarters, BPO revenues stabilized and grew by 1.6% QoQ in CC terms. The company is shedding the non-strategic accounts and this has impacted growth rates.
- The drag is also coming in from the insurance business services. HCLT has acquired a platform and is investing in upgrading the same.
- The other continuing voice and non-voice business is growing at a steady pace.
- The company has been increasingly focusing on increasing the contribution from the platform-based services. The target is to reach 60% non-voice and 40% voice revenues in the next 3 - 4 quarters. The ratio is the reverse currently.
- The management had indicated that, the BPO stream would start contributing to profits in CY12.
- We have assumed the business to break even at EBIDTA level in 4QFY12.

Macro scene - headwinds persist; churn ratio in re-bidding is high, though

- In line with other companies, HCLT management has indicated that, the headwinds against the sector persist in the form of uncertain global economic scene, which is creating uncertainties in client spends.
- Moreover, with the supply scene getting more competitive, the management assigns low probability to billing rate increases. Average realisations were flat in 2Q.
- However, it has indicated that, the churn ratio in project re-bidding is unusually high and this provides an opportunity to HCLT to win larger projects.
- According to the management, when projects come for re-bidding, normally about 5% of those are given to new vendors with the remaining staying with existing vendors.
- However, the churn ratio has been at a high 30% this year as clients look for better value.
- According to the management, about $47bn worth of projects are coming up for restructuring in the current calendar and HCLT is looking at bagging a few of these deals.
- In 2QFY12, HCLT won about 18 deals of total TCV of $1bn.

Margins higher than estimated

- Margins rose by about 140bps on a QoQ basis. This was largely on the back of the rupee depreciation, which added 260bps to the profitability.
- However, the company gave the balance salary increments during the quarter and also paid some one-time bonuses (about $5mn, we believe).
- These factors impacted margins by about 100bps, after accounting for cost efficiencies gained during the quarter.
- Margins were better than our estimates. We understand that, margins may remain in a narrow band as the company goes after market share. The expected depreciation in rupee may help restrict the impact to some extent.
- Low margins have been a cause of concern for us and the company will have to strive hard to improve the same sustainably while increasing the growth rates also, we opine.

Other income

- The company incurred a forex loss of Rs.760mn. The company has significantly increased the hedges to $1.2bn ($980mn of cash-flow hedges and balance are balance-sheet hedges).
- Out of these $980mn, hedges worth $545mn are for maturity of less than 1 year and the balance are for maturity of more than 1 year.
- As at the previous quarter end, the company had total hedges of $713mn.

Future prospects

- We have suitably modified our earnings estimates for FY12E.
- Revenues are expected to rise by 31% in FY12E. HCLT plans to once again focus on increasing volumes and improving market share.
- Margins are expected to be marginally higher. While salary increments will likely rein in margins, rupee depreciation, mix change in favour of IT services and Infrastructure services, better utilization as well as improved efficiencies are expected to set-off that impact. We have assumed the rupee at Rs.50 / USD in the remaining two quarters of FY12.
- We expect the company to report an EPS of Rs.32.3 (Rs.30.8) in FY12E. This is after assuming a further equity dilution due to ESOPs.

Valuations

- We largely maintain our target price at Rs.499 (Rs.496 earlier) for HCL Tech based on a suitable discount to larger peers on FY12E earnings.

We recommend BUY on HCL Technologies with a price target of Rs.499

- We believe the discount is justified because of the differences in margins. Improvement in margins on a sustainable basis may lead us to accord higher valuations to HCLT.
- We have maintained the price target despite the increase in earnings estimates because the increase in earnings is largely on the back of rupee depreciation.
- With a near 17% upside, we maintain **BUY.**

Concerns

- A delayed recovery in major user economies may impact our projections.
- A sharp acceleration in the rupee from our assumed levels may impact our earnings estimates for the company.

RESULT UPDATE

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TATA CONSULTANCY SERVICES LTD (TCS)

PRICE: RS.1104 **RECOMMENDATION: BUY**
TARGET PRICE: RS.1241 **FY13E P/E: 16.9X**

TCS' 3Q operating results were in line with our expectations. Volume growth at 3.2% (6.25% in 2Q) was impacted by seasonality. Improvement in EBIT margins was along expected lines. More importantly, the growth was broad - based with most verticals, geographies and services growing QoQ. Pricing was higher QoQ due to mix change. We view this as a positive. The company is cautious about pricing and sees low probability of like-to-like improvement.

On the macro side, TCS also conceded that, the uncertainty is likely to persist. Client budgets have been largely finalized with mixed trends. About 1/3rd of the sample clients (120) will have lower budgets in CY12. We also understand that, decisions on discretionary budgets are being delayed. This may have an impact on the growth in 4Q. For FY13, TCS does not see any cause of undue concern, as of now. Clients have already adjusted to the changing macro and are navigating spends accordingly. TCS has not seen any project cancellations.

TCS won 10 large deals (10 in 2Q) during the quarter. Management has seen continued revival in cost efficiency initiatives, which is encouraging. Significant hiring during the quarter also indicates good visibility for FY13. TCS added 11981 employees on a net basis.

We make changes to our earnings estimates. FY12E earnings now stand at Rs.55.8 (Rs.54.7 earlier). FY13 earnings are expected to be Rs.65.4 per share (Rs.62.2 earlier). We tweak our price target to Rs.1241 based on FY13 estimates (Rs.1240 earlier). We have accorded valuations which are almost similar to those of Infosys. TCS' revenue growth in the past few quarters has been better than Infosys and it has been able to restrict impact on margins. We maintain a BUY. A sharp appreciation in the rupee against various currencies and a delay in recovery in major user economies remain the key risks to our call.

Summary table

(Rs mn)	FY11	FY12E*	FY13E*
Sales	373,246	492,672	580,993
Growth (%)	24.3	32.0	17.9
EBITDA	111,893	147,421	168,692
EBITDA margin (%)	30.0	29.9	29.0
PBT	109,147	143,396	169,542
Net profit	86,828	109,128	128,052
EPS (Rs)	44.4	55.8	65.4
Growth (%)	26.3	25.7	17.3
CEPS	49.0	61.0	71.3
BV (Rs / Share)	128.9	174.2	228.3
Dividend / Share (Rs)	9.5	10.0	10.0
ROE (%)	37.6	43.1	43.0
ROCE (%)	45.1	54.1	54.8
Net cash (debt)	52,823	66,353	136,878
NW capital (Days)	80.2	77.0	75.0
P/E (x)	24.9	19.8	16.9
P/BV (x)	8.6	6.3	4.8
EV/Sales (x)	5.6	4.3	3.5
EV/EBITDA (x)	18.8	14.2	12.0

*Source: Company, Kotak Securities - Private Client Research; * - based on IFRS*

3QFY12 results - above estimates

(Rs mn)	3QFY12	2QFY12	QoQ (%)	3QFY11	YoY (%)
Turnover	**132,040**	**116,335**	**13.5**	**96,634**	**36.6**
Expenditure	91,119	82,506		67,459	
EBIDTA	**40,921**	**33,829**	**21.0**	**29,175**	**40.3**
Depreciation	2,303	2,286		1,856	
EBIT	**38,618**	**31,543**		**27,319**	
Interest	0	0		0	
Other Income	-920	997		1,822	
PBT	**37,698**	**32,540**	**15.8**	**29,141**	**29.4**
Tax	8,538	7,913		5,491	
PAT	**29,160**	**24,627**	**18.4**	**23,650**	**23.3**
Minority interest	294	237		189	
Share of profit	0	0		0	
Adjusted PAT	28,866	24,390	18.3	23,461	23.0
EO items	0	0		0	
Shares (mns)	1,957	1,957		1,957	
EPS (Rs)	**14.7**	**12.5**		**12.0**	
EBIDTA (%)	31.0	29.1		30.2	
Net Profit (%)	22.1	21.2		24.5	``

Source : Company

Volumes grew by 3.2% - seasonality at play; realisations were higher

- Volumes grew by 3.2% on a sequential basis, which was in line with estimates. We understand that, the growth was relatively lower because of the seasonality associated with the quarter. The growth follows a string of high volume growth rates in past few quarters.
- TCS has been reporting relatively high growth rates in the past few quarters (6.25% in 2Q, 7.4% in 1Q, 2.9% in 4QFY11, 5.7% in 3QFY11, 11.2% in 2QFY11, 8.1% in 1QFY11, 4% in 4QFY10, 6.5% in 3QFY10 and 5% in 2QFY10).
- The high volume growth reflects the company's ability to mine deeper into existing accounts as well as win new large deals.
- The company won 10 large deals (> 100mn deals) including transformational deals, during the quarter. The company also got a higher share of wallet, as reflected in the number of $1mn - $100mn accounts.

Growth in revenues from top clients

(Rs mn)	3QFY12	2QFY12	QoQ (%)	3QFY11	YoY (%)
Top client	9,111	8,027	13.5	7,441	22.4
Top 5 clients	25,880	23,267	11.2	21,163	22.3
Top 10 clients	36,575	32,923	11.1	29,087	25.7

Source : Company

- Infosys reported a 3% volume growth and HCLT reported a 4.9% growth for the quarter.
- In our opinion, TCS continued its significant focus on its large accounts. Consistently good execution also helped in improving the run rates.
- Pricing was higher by about 198bps QoQ on a CC basis, we understand. The company has indicated that, this is largely due to mix change and the like-to-like pricing was stable.
- Nevertheless, this improvement is encouraging as the company had been facing pressure on realisations over the past couple of quarters. (-95bps in 2Q).
- The management has indicated that, price increases may be difficult to come by though no reductions are expected.

Broad - based growth across verticals, services, geographies

- The growth during the quarter has been broad based and in our opinion, this makes it more sustainable.
- While the growth drivers are different, the underlying aims of clients have been to reduce costs and improve the growth rates.
- The management has indicated that, it has not witnessed any cancellations of projects from any client across geographies.
- All the verticals except Telecom and Energy / Utilities grew at a healthy pace (in USD terms), indicating all round improvement in spending patterns.
- Revenues from Energy & Utilities vertical fell after growing by 22% QoQ in 2Q. The telecom vertical witnessed de-growth and has also been pretty volatile.
- However, the company has won large deals in this vertical, which are strategic and long term assignments. This should help the vertical achieve some stability in growth rates, going ahead.
- The management expects the vertical to report growth in FY12, albeit lower-than-average growth.

Vertical - wise growth

Rs mns	3QFY12	2QFY12	QoQ (%)	3QFY11	YoY (%)
Insurance, Banking and Financial services	57,173	50,606	13.0	43,099	32.7
Manufacturing	10,299	9,074	13.5	6,958	48.0
Telecom	13,204	12,448	6.1	11,499	14.8
Life Sciences & Healthcare	6,998	6,166	13.5	5,025	39.3
Retail	16,241	14,077	15.4	10,533	54.2
Hi-tech	7,790	6,864	13.5	4,832	61.2
Travel / Hospitality	5,018	4,421	13.5	3,286	52.7
Energy&Utilities	5,414	5,002	8.2	4,252	27.3
Media Entertainment	2,905	2,443	18.9	2,223	30.7
Others	6,998	5,235	33.7	4,928	42.0

Source : Company

- In terms of service lines also, Consulting and Enterprise Solutions reported high growth.
- However, we will closely watch the future performance of these services in light of the delays experienced by TCS in closure of discretionary spend deals. Infrastructure Management Services reported high growth during the quarter.

Services growth

(Rs mn)	3QFY12	2QFY12	QoQ (%)	3QFY11	YoY (%)
ADM	58,098	52,002	11.7	43,485	33.6
BI	5,810	5,468	6.3	5,122	13.4
Engg & Industrial	6,074	5,584	8.8	4,638	30.9
Infrastructure	13,996	11,168	25.3	10,147	37.9
Enterprise Soln	15,053	12,913	16.6	9,277	62.3
Consulting	3,697	3,025	22.2	2,223	66.3
Asset Leveraged Soln	5,018	4,653	7.8	3,865	29.8
Assurance Services	10,035	8,841	13.5	6,861	46.3
BPO	14,260	12,681	12.5	11,016	29.4

Source : Company

- Geographically, US and Continental Europe reported high growth rates, indicating continued demand traction, as clients looked out for cost efficiencies and growth.
- Growth in Continental Europe belies concerns relating to the geography. We understand that, clients in this geography are increasing off-shoring as they focus on reducing costs and improving efficiencies.
- We understand that, the company has not witnessed any slowdown in the Government projects in UK and in fact, a large UK project had gone live in 2Q.

Growth in geographies

(Rs mn)	3QFY12	2QFY12	QoQ (%)	3QFY11	YoY (%)
North America	70,377	62,123	13.3	51,699	36.1
Europe	13,864	11,750	18.0	8,987	54.3
UK	19,806	18,032	9.8	15,461	28.1
India	11,091	9,656	14.9	8,890	24.8
A-PAC	10,035	8,725	15.0	6,668	50.5
Latin America	4,093	3,490	17.3	2,996	36.6
MEA	2,773	2,559	8.3	1,933	43.5

Source : Company

Cautious on macro and on discretionary spends

- TCS has indicated that, the macro scene remains uncertain.
- TCS has surveyed about 120 clients (out of about 1000 clients) out of which 96 clients have frozen their budgets for CY12.
- While 2/3rds of the clients will see flat - to - higher budgets, the balance are expected to see a fall YoY. There are no specific trends in terms of verticals or geographies, which may see a cut.
- Moreover, in a survey of 130 clients, the company has concluded that, about half of them have delayed discretionary projects. This is on account of the deeper due diligence, which the clients want to make.
- A few of them have started in 4Q and the others may start in 4Q or later.
- The company is not seeing any of its large accounts getting impacted by the budget delays or discretionary spend cuts.
- TCS management is optimistic on client spending trends over the medium term, except in case of global economic turmoil.

We remain optimistic on the medium term

- While the findings of surveys are of concern, we believe that, they are based on a small sample size (less than 10% of all clients) and also do not reflect the trends with the large clients of TCS.
- Moreover, revenues from discretionary spend of clients, form only about 20% of TCS' revenues of which, a part may be impacted.
- The non-discretionary spends including the large transformational deals are not seeing any slowdown, according to the management.
- In addition to this, we believe that, over 4QFY12, more clarity will emerge on the macro, which may lead to release of budgets in FY13.
- Thus, which the scenario is less optimistic in the short term, it is confined to a small part of revenues.
- The large number of employee addition also reinforces our optimism on FY13.
- Nevertheless, there may be some moderation of revenue growth in 4Q due to slower discretionary spends.

Average realizations higher

- TCS reported a 198bps improvement in average realizations, which was due to mix change, we understand.
- The change in service mix and also higher proportion of revenues from global delivery centres contracts helped overall realizations.
- The management has indicated that, this improvement is not a trend. It has indicated that, the probability of pricing increases is low in the near term.

Margins almost in line with estimates

- EBIDTA margins were about 190bps higher on a QoQ basis, on the back of the rupee depreciation.
- The high employee intake and the consequent fall in utilization rates set off some of the gains from currency depreciation.
- The margins improved despite the high employee intake and the consequent fall in utilization rates.
- Utilisation rates including trainees were down by almost 200bps QoQ. The management has indicated that, it is comfortable operating at utilization rates of 82% - 84%, excluding trainees.
- We understand that, the company is comfortable with the absolute number of people on bench, which has increased with the base.

High employee additions

- TCS added 11981 (12,580 in 2Q) employees on a net basis, which was much higher than our estimates.
- The company has indicated that, it will likely add close to 65000 employees on a gross basis v/s its earlier target of 60000. We are encouraged by these additions as it indicates adequate revenue visibility over the medium term.
- Attrition was also lower at 12.8% on a LTM basis, including BPO services. (13.7% in 2Q).

Other income

- The company has a negative other income of Rs.920mn. This was largely due to a forex loss of Rs.3bn for the quarter.
- The forex loss was much larger than our expectations.
- The company has hedges of $2.8bn of which, $1.7bn are cash-flow hedges ($1.3bn for 4Q) and $1.1bn are balance sheet hedges (against receivables).
- The tax rate was at 22.6%. For FY12E, we expect the tax rate to be about 23%, moving up to about 24% in FY13E.

Future prospects

- We have made changes to our FY12 and FY13 earnings estimates.
- We expect revenues to grow by about 32% in FY12E and 18% in FY13E on the back of higher volumes.
- The rupee is expected to be at 50 per USD in 4QFY12 and 49 / USD in FY13. Realisations are expected to be stable over 3QFY12 levels.
- Margins are expected to be lower YoY in FY13 because of the expected salary increments and employee additions.
- With tax expected to be at around 24%, PAT is expected to rise by 17% to Rs.128bn. EPS works out to Rs.65.4.

Valuations

We maintain BUY rating on TCS with a price target of Rs.1241

- We have valued TCS at valuations which are similar to those of Infosys. TCS' recent revenue growth has been better than Infosys and it has been able to restrict impact on margins.
- This leads us to a price target of Rs.1241 based on FY13E earnings. (Rs.1240 earlier).
- At our target price, our FY13E earnings will be discounted by about 19x. We maintain our **BUY** rating on the stock.

Concerns

- A delay in recovery of major user economies may impact our projections.
- A sharp appreciation of rupee beyond our assumed levels may impact our earnings estimates for the company.

Bulk deals

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
17-Jan	Action Fin	Shrish L Keniya	S	100,000	24.8
17-Jan	Emporis	Dipak Kalyanji Tanna	B	142,000	38.7
17-Jan	Emporis	Accurate Finstock Pvt Ltd	S	142,000	38.7
17-Jan	Essen Supp	Anil R Chokhani (Huf)	S	32,000	57.1
17-Jan	Gangotri Iron	R B K Securities Private Limited	B	150,000	30.1
17-Jan	Gk Consultants	Mamta Singhal	S	40,000	14.9
17-Jan	Gujarat Intrux-$	Omprakash Siremalji Kanungo	S	50,000	35.0
17-Jan	Gujarat Medi	Mahak Bhargava	B	24,000	18.1
17-Jan	Gujarat Medi	Rakesh Hasmukhlal Shah	S	50,000	19.5
17-Jan	Icra	Templeton Mutual Fund A/C Franklin India Prima Plus	B	95,445	830.0
17-Jan	Icra	Sbi Mutual Fund A/C Sbi Tax Advantage Fund Series I	S	162,127	830.0
17-Jan	Il&Fs Trans	Il & Fs Financial Services Limited	B	2,440,534	166.0
17-Jan	Il&Fs Trans	Standard Chartered Il&Fs Asia InfraGrowth Fund Co Pte L	S	2,440,534	166.0
17-Jan	Infotech Enter	Reliance Mf Ac Equity Opportunities	B	1,216,000	120.0
17-Jan	Infotech Enter	Capital World Gth & Income Fund Inc	S	1,925,493	120.0
17-Jan	Kanchan Intl	Chandrakanta Satish Mandowara	B	19,361	62.8
17-Jan	Kanchan Intl	Jeetendra M Fagania Huf	S	20,000	62.7
17-Jan	Kanchan Intl	Surendrakumar Moolchand Fagania	S	50,000	63.0
17-Jan	Karma Ind	Kersy Darabshaw Chindhy	S	211,623	47.9
17-Jan	Karma Ind	Amy Kersy Chindhy	S	200,344	47.9
17-Jan	Ken Fin Serv	Chandak Housing Private Limited	B	20,000	93.5
17-Jan	Ken Fin Serv	Rakesh Maneklal Jain	B	16,950	87.8
17-Jan	Ken Fin Serv	Vimalkumar Sureshchandra Raval	B	33,000	88.0
17-Jan	Ken Fin Serv	Amit Sampathraj Shah	S	19,800	93.5
17-Jan	Ken Fin Serv	Kamal Kumar Chaudhary Huf	S	50,000	87.9
17-Jan	Ncl Research	Ellisbridge Trading Private Limited	B	25,920	158.8
17-Jan	Nouveau Global	Asha Krishan Khadaria	B	3,085,809	3.7
17-Jan	Nouveau Global	Rajat Commercial Enterprises	S	3,085,809	3.7
17-Jan	Prraneta Inds	Multiplier Share & Stock Advisors	S	1,472,851	0.4
17-Jan	Prraneta Inds	Vora Financial Services	S	2,500,000	0.4
17-Jan	Ram Informatics	Srinivasaraju Raju Penmatcha	B	77,000	3.6
17-Jan	Ram Informatics	Deendayal Singh	S	77,107	3.6
17-Jan	Raymed Labs	Rakesh Kumar Sharma	B	30,000	30.7
17-Jan	Raymed Labs	Fastcon Infrastructure	B	30,000	30.8
17-Jan	Raymed Labs	Monica Agarwal	S	30,000	30.2
17-Jan	Sambhaav Media	Kiranbhai Bhupatbhai Vadodaria	B	1,289,300	1.0
17-Jan	Spectacle	Rajesh Jayantilal Khandhar	B	400,000	4.8
17-Jan	Spectacle	Jigar Praful Ghoghari	S	350,000	4.8
17-Jan	Synergy Cos	Meherdad Minocher Kermani	S	67,745	1.0
17-Jan	Vaishnavi	Sharmila Parvataneni	B	79,401	7.6
17-Jan	Vaishnavi	Ashwani Kumar Agarwal	S	91,834	7.5

Source: BSE

Forthcoming events

Company/Market

Date	Event
18-Jan	Agro Tech Foods, Asian Flora, Assambrook, Bajaj Finserv, Infotech Ent, Jindal Steel, Manali Petro, Mindtree, NIIT Tech, Raymond, Riddhi Siddhi, TCI Ind earnings expected
19-Jan	Bajaj Auto, Bajaj Holdings, Balaji Tele, Dish TV India, HDFC Bank, Hero MotoCorp, IFCI, Mastek earnings expected
20-Jan	Axis Bank, Bank of Maharashtra, Exide Ind, Hindustan Const, Hindustan Zinc, ITC, Praj Ind, RIL, Syndicate Bank, United Spirits, Wipro, Wire & Wireless earnings expected
21-Jan	Asian Paints, Godrej Cons, JSW Energy, Karnataka Bank, M&M Finance, Patel Engineering, Sobha Dev, Torrent Power, Ultratech Cem, Zee entertainment earnings expected

Source: BSE

Gainers & Losers

Nifty Gainers & Losers

	Price (Rs)	chg (%)	Index points	Volume (mn)
Gainers				
Reliance Ind	742	4.1	16.2	5.2
L&T	1,267	5.5	11.6	3.0
HDFC Bank	468	1.7	4.7	1.8
Losers				
ICICI Bank	786	(0.8)	(2.3)	4.3
ITC	208	(0.3)	(1.2)	6.8
TCS	1,104	(0.5)	(0.9)	1.9

Source: Bloomberg

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