

Indian IT Services

How to think about valuations as the digital disruption begins

Equities

India
Diversified Technology Services

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Industry is facing a model disruption, not just demand problems

India's IT services sector has provided the most cost-efficient IT services outsourcing model in the past decade, leading to significant market share gains. However, we believe the rise of digital technologies, such as social, mobile, analytics and cloud (SMAC), is ushering in mainstream adoption of new outsourcing models (mainly utility computing and autonomies) that are likely to be more efficient than offshore services. While tepid demand due to slower global GDP growth has impacted the sector's revenue growth, we believe the impact of the digital shift on market share gains could be much more disruptive.

Enough evidence to suggest the disruption has already begun

We believe two main data points support our view that the business model disruption has begun: 1) aggressive price competition among vendors, even when demand was steady in 2014-15; and 2) Indian IT exports have slowed in recent years despite stable growth in the global outsourcing market, implying market share loss for Indian vendors. Finally, UBS's offshore-centric Evidence Lab survey reveals Indian service providers are less preferred than specialists and consulting-led global vendors for digital services.

We expect a multi-year valuation de-rating cycle; precedents exist in the sector

Valuations for Indian IT stocks have corrected in the past 18 months, and the stocks may appear more reasonably valued now, in our view. However, we caution against ascribing historical PE multiples in an environment where the sector's business model is at risk of disruption. Valuations for global vendors like IBM and Accenture corrected for three to four years when Indian offshore vendors disrupted their onsite-centric business models. We expect Indian IT services companies to experience a similar multi-year valuation correction as the digital disruption takes hold.

We remain cautious; no Buy ratings

We stay cautious on the sector, with no Buy ratings. We have Neutral ratings on Tata Consultancy Services (TCS), Cognizant, HCL Technologies (HCL Tech) and Tech Mahindra. We maintain our Sell ratings on Infosys and Wipro. Infosys performed better than expected in 9M FY16; we update our FY17/FY18 EPS forecasts by 6% and cut our target PE discount for Infosys relative to TCS from 30% to 10%. We reduce Tech Mahindra's EPS estimates for FY17/FY18 by 5% and increase the valuation discount to TCS from 10% to 25% to factor in likely lower medium-term earnings growth.

Valuations

Company	Share price	Mkt cap (US\$bn)	Rating	Price Target		Upside (%)	PE (x) FY17E	EV/EBITDA (x) FY17E	EPS CAGR FY15-18E (%)
				Old	New				
TCS	Rs2,278.00	65.0	Neutral	Rs2,550	Rs2,550	11.9%	16.8	13.2	13.8
Cognizant	US\$55.01	33.6	Neutral	US\$63	US\$63	14.5%	16.6	10.1	11.9
Infosys	Rs1,095.45	36.1	Sell	Rs810	Rs1,070	-2.3%	16.9	11.2	8.6
Wipro	Rs525.00	18.9	Sell	Rs520	Rs520	-1.0%	13.4	9.7	5.6
HCL Technologies	Rs824.60	16.9	Neutral	Rs950	Rs950	15.2%	13.9	10.7	8.6
Tech Mahindra	Rs430.15	6.0	Neutral	Rs600	Rs475	10.4%	13.0	7.9	11.9

Above data as at 17 February 2016. Year-end for Cognizant is December.

Source: Company data, UBS estimates

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Indian IT Services

UBS Research THESIS MAP MOST FAVORED

LEAST FAVORED

Cognizant, Tata Consultancy Services

Infosys, Wipro

PIVOTAL QUESTIONS

Q: Will digital technologies impact the revenue growth of India's offshoring model?

Yes. We expect a business model disruption as IT services outsourcing shifts away from headcount-driven delivery to: 1) utility computing; and 2) autonomies. These new models are much less reliant on headcount and provide more cost benefits to IT users than the existing offshore model. We expect the industry's revenue growth to slow from low double digits to high single digits over 2014-18, while consensus forecasts low double-digit growth. Our lower estimates are based on: 1) increasing pressure on legacy services (85-90% of total revenue); and 2) shrinking contract sizes (due to new outsourcing models) that may weaken incremental revenue growth.

[more →](#)

Q: Can currency depreciation prevent market share loss for India's offshore services vendors?

No, but we believe it could help delay the shift to new outsourcing models if vendors aggressively pass on the benefits to clients. Over the past few years, the correlation between Indian vendors' market share and currency movements has increased, but it has not stopped India's IT revenue from slowing relative to the global outsourcing market.

[more →](#)

Q: Are operating margins at risk due to the shift to digital technologies?

No. We expect the shift to digital technologies to be margin-accretive in the medium term. Digital models have better operating leverage, due to much less reliance on headcount and greater automation benefits. However, we still expect lower earnings growth in the medium term, as the potential margin expansion is unlikely to be enough to compensate for the revenue shrinkage due to the shift to digital outsourcing models.

[more →](#)

WHAT'S PRICED IN?

We believe the market has priced in a cyclical slowdown, due to recent revenue disappointments and macroeconomic concerns, as was evident in the PE de-rating of many large vendors in 2015. However, we think a business model disruption is not priced in, which could imply a multi-year de-rating. As the revenue disruption of digital technologies becomes more visible, we expect a multi-year PE de-rating for Indian vendors, similar to the trend in IBM and Accenture in 2003-07.

[more →](#)

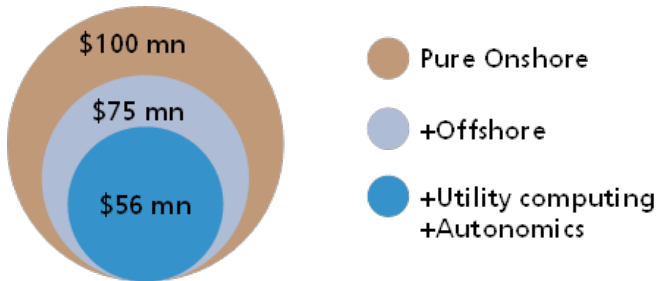
UBS VIEW

We maintain our anti-consensus cautious view on Indian IT and expect industry revenue growth to be at high-single digits over 2014-18, compared to low double-digit consensus estimates. We are below consensus on medium-term earnings and see risks to valuations, which are above five-year averages for most vendors.

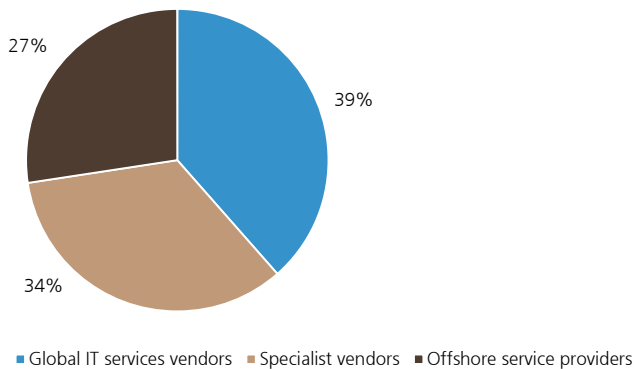
EVIDENCE

UBS Evidence Lab; slower revenue growth in 2014-15, despite steady demand: Indian IT vendors saw revenue deceleration in 2014 and 2015, despite a revival in demand in 2014 and stable IT services spending in 2015, suggesting incremental market share loss. Competitive pricing pressure has increased significantly in the past 12 months. UBS's offshore-vendor-centric Evidence Lab survey showed that IT users preferred consulting-led vendors like IBM and Accenture over Indian vendors for digital services.

OUR THESIS IN PICTURES

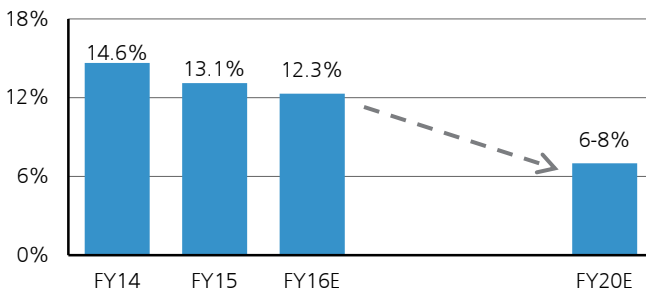
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We expect contract sizes to shrink by 20-30%, due to the rise of digital outsourcing models



UBS Evidence Lab survey showed Indian vendors are less preferred for digital services outsourcing

Indian IT services revenue (YoY)



Indian IT revenue is likely to slow to high-single-digit growth by FY20E, compared to 12-13% at present

Mkt cap weighted 1-year fwd PE (x) - Top



Sector valuations have corrected in the past 12-months; we expect the trend to continue

Sources for exhibits above: Company data, UBS estimates

PIVOTAL QUESTIONS

[return](#) ↑**Q: Will digital technologies impact the revenue growth of India's offshoring model?****UBS VIEW**

Yes. We maintain our views that the increasing adoption of digital services may impact the revenue growth and competitiveness of Indian IT services providers (see our earlier notes [Digital services: not only a technology shift, but a change in the business model as well](#) and [Q-Series: Will digital diminish the offshore advantage?](#)). We expect contract sizes to shrink as a result of the move to outsourcing models driven by utility computing and autonomies, leading to revenue cannibalisation for incumbent Indian vendors.

EVIDENCE

The Indian IT sector's revenue growth slowed in 2014-15, despite a steady demand environment, with many vendors missing consensus forecasts and their own initial guidance. We believe pricing pressure has intensified, as competition for market share has increased due to the compression of legacy revenue. Finally, our Evidence lab survey of offshore IT users revealed low preference for Indian vendors in digital services outsourcing, despite heavy usage of these companies for legacy services.

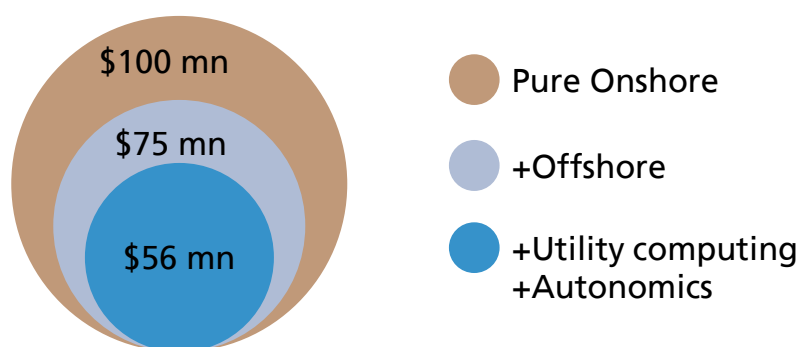
WHAT'S PRICED IN?

We believe the market views the shift to digital technologies as an incremental revenue opportunity that could offset shrinking legacy revenue but ignores the likely impact of the ongoing budgetary pressure at the time of such a major technology shift. We note that previous technology shifts typically occurred in times of budgetary expansion.

Contract size shrinkage to be similar in magnitude to offshore shift

IT deal sizes shrank by 20-25% in the early 2000s, when the business model shifted from pure onshore to onshore+offshore. We expect the shift to digital technologies to lead to similar size shrinkage, as outsourcing models move to utility computing and autonomies (see our [2016—Digital shift to keep revenue under pressure: slow valuation de-rating likely](#) in January 2016). The new models are much less reliant on headcount and provide more cost benefits to IT users than the existing offshore model.

Figure 1: Deal sizes to shrink due to digital adoption (US\$ m)



Source: UBS estimates

Consulting-led global vendors preferred for digital services

An UBS Evidence Lab survey in 2015 showed that global vendors were most preferred across all digital technologies. We believe this is due to the significant investments made by these firms in the past few years to build and acquire digital solutions, and their exposure to consulting, which allows them to remain ahead of their offshore peers in the transition to digital technologies. We expect the shift to digital to result in slower revenue growth for Indian offshore vendors in the next three to five years.

Figure 2: Preferred IT services providers by digital segment

Cloud Services		Big Data		Social		Mobility	
IBM	56%	IBM	54%	IBM	51%	IBM	50%
Accenture	24%	Accenture	27%	Accenture	32%	Accenture	31%
Atos	19%	Atos	21%	Atos	21%	Atos	21%
Capgemini	16%	Capgemini	16%	Capgemini	19%	Capgemini	21%
Luxoft	13%	Wipro	13%	Infosys	13%	Infosys	13%
Wipro	13%	Luxoft	13%	Luxoft	13%	Luxoft	13%
Cognizant	13%	Infosys	11%	Wipro	12%	Cognizant	11%
Infosys	10%	Cognizant	10%	TCS	8%	Wipro	10%
TCS	7%	TCS	9%	Cognizant	8%	TCS	9%
HP	7%	HP	5%	EPAM	4%	EPAM	3%
Tech Mahindra	4%	EPAM	4%	HCL Technologies	2%	Tech Mahindra	2%
EPAM	4%	HCL Technologies	2%	HP	2%	HP	2%
Fujitsu	1%	Dell	2%	Fujitsu	1%	Fujitsu	1%
HCL Technologies	1%	Fujitsu	1%	Tech Mahindra	1%	HCL Technologies	1%
Dell	1%	Tech Mahindra	1%	Dell	1%	Dell	1%
In-house	4%	In-house	4%	In-house	5%	In-house	4%
Others	5%	Others	5%	Others	6%	Others	5%

Consulting-led global vendors
 Indian IT Services vendors
 European IT Services vendors
 Others

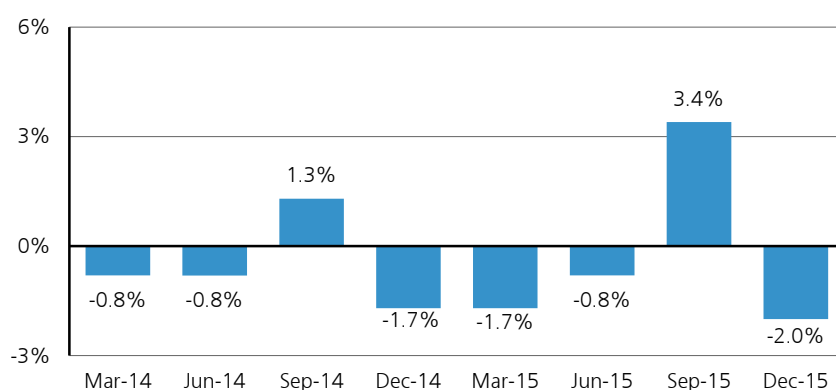
Source: UBS Evidence Lab

Increasing competitive pressure on legacy revenue

The legacy offshoring business, which contributes 85-90% of Indian IT vendors' total revenue, has been under pricing pressure over the past few quarters. Using Infosys' constant-currency QoQ per-capita productivity changes as the proxy for the industry, since most Indian IT services companies do not disclose their pricing details, it is evident that the pricing environment has been quite negative. Vendor commentary suggests that the pricing pressure is due to increasing competitive intensity rather than client demand for rate reductions.

Figure 3: Pricing has declined in majority of recent periods

Infosys: QoQ change in per-capita productivity



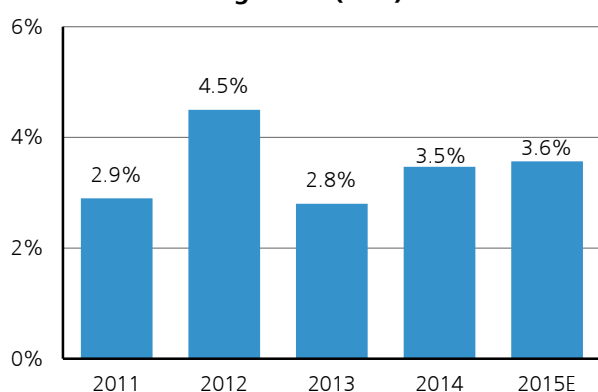
Source: Company data

Indian IT has slowed, despite growing global demand

Indian IT vendors have witnessed revenue deceleration over the past few years, despite stable global demand for IT services outsourcing, suggesting incremental market share loss. We believe this is early indication that the adoption of new digital technologies is causing revenue growth disruptions for Indian IT firms.

Figure 4: Global IT revenue growth has been stable

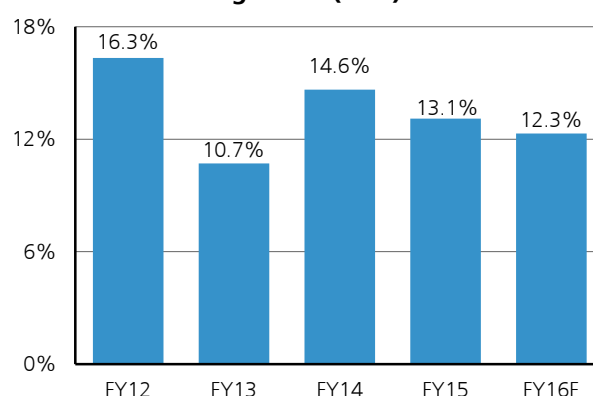
Global IT services growth (YoY)



Note: Constant currency growth.
Source: Gartner

Figure 5: Indian IT revenue growth has slowed

Indian IT services growth (YoY)

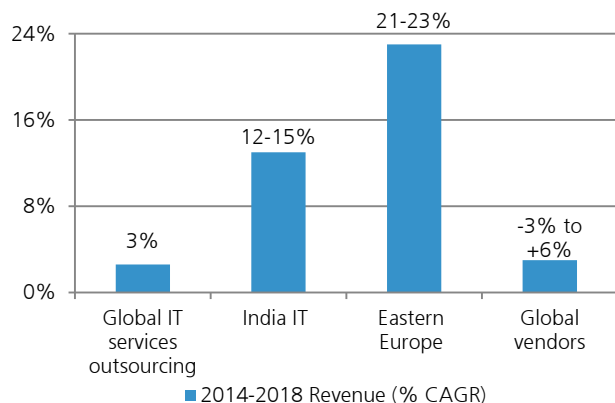


Note: Constant currency growth. March financial year-end.
Source: NASSCOM

We expect Indian IT revenue to slow further

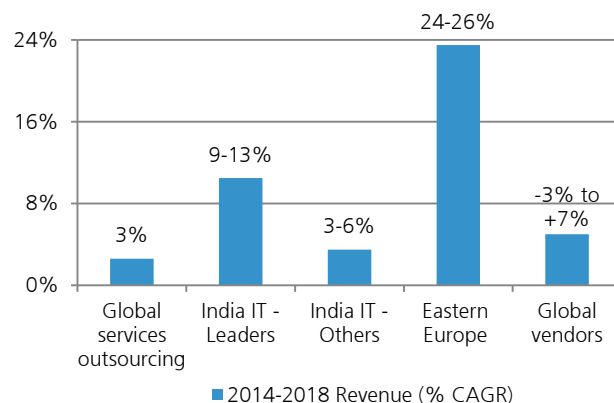
Driven by the business model shift, we expect revenue growth of Indian IT services companies to slow further from low double digits to high single digits over 2014-18, with a wider dispersion in growth among vendors. We forecast vendors that successfully adapt to the digital model to increase revenue by 3-4x the pace of the global outsourcing market, and 1-2x for other vendors. We believe consensus estimates have not factored in the potential disruptions to the offshoring model and face downside risks.

Figure 6: Consensus industry revenue forecasts



Source: Bloomberg, NASSCOM

Figure 7: UBS industry revenue estimates



Source: UBS estimates

PIVOTAL QUESTIONS

[return](#) ↑**Q: Can currency depreciation prevent market share loss for India's offshore services vendors?****UBS VIEW**

No, but we believe it could help delay the shift to new outsourcing models, if vendors aggressively pass on the benefits of currency-related gains to clients, which would help the clients realise better cost-savings in the current model. However, we think this is a difficult strategy to execute, as currency moves tend to be volatile and tough to predict.

EVIDENCE

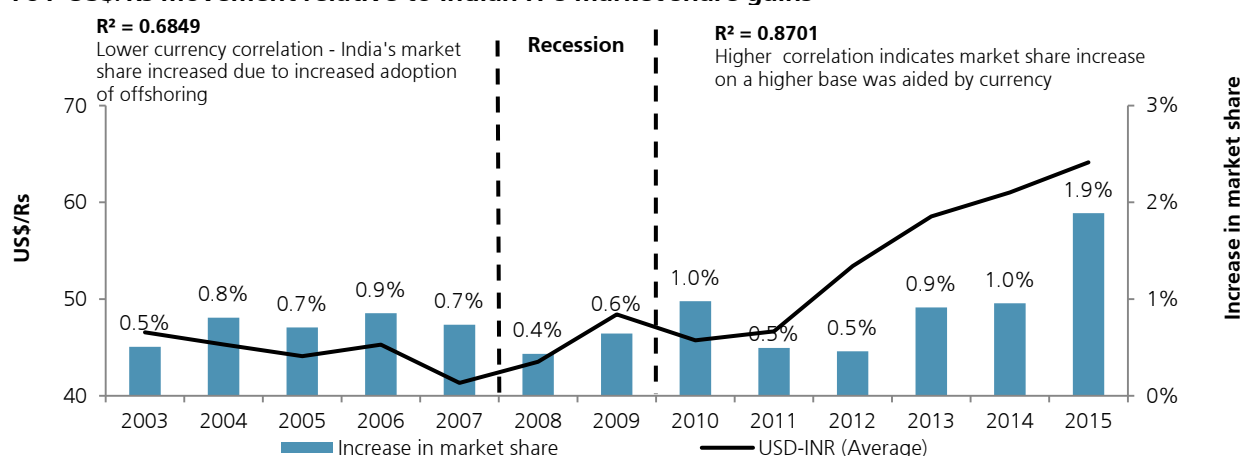
Over 2013-15, the correlation between market share gains for the Indian IT sector and currency moves increased, in step with the sharp depreciation of the rupee against the US dollar. Vendor commentary and our channel checks suggest that currency gains have been passed on to customers to help keep the labour arbitrage wide and encourage more offshoring.

WHAT'S PRICED IN?

We believe current valuations suggest that the market expects currency gains to be passed on to customers, as the pressure on legacy revenue forces vendors to do so to sustain market share gains.

Rupee depreciation has aided Indian IT's market share gains

Over the past few years, weakening of the Indian rupee against major currencies, mainly the US dollar has helped Indian IT services providers gain market share. The currency tailwind has also helped them absorb the pricing pressure on legacy revenue. We believe Indian vendors could delay the digital shift in the near term by passing on the currency benefits to their clients, but ultimately the shift is likely to be inevitable.

Figure 8: A weak rupee has aided Indian IT's market share gains**YoY US\$/Rs movement relative to Indian IT's market share gains**

Source: Bloomberg, NASSCOM, Gartner, UBS estimates

PIVOTAL QUESTIONS

[return](#) ↑**Q: Are operating margins at risk due to the shift to digital technologies?****UBS VIEW**

No. We expect the shift to digital technologies to be margin-accretive in the medium term. Digital models have better operating leverage, due to much less reliance on headcount and greater automation benefits. Although the adoption of digital technologies is likely to be margin-accretive, we expect lower earnings growth for Indian IT in the medium term, as the potential margin expansion is unlikely to be enough to compensate for the revenue shrinkage due to the shift to digital outsourcing models.

EVIDENCE

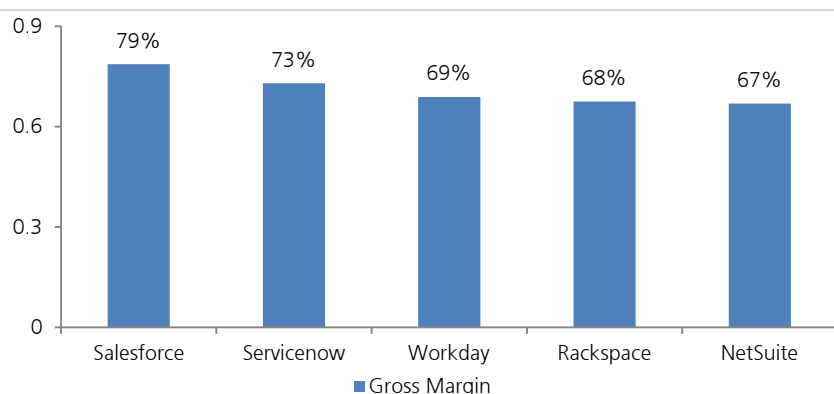
An examination of the financial statements of listed digital services vendors (which are all global companies) shows gross margins are in the range of 65-80% in the most recent reported financial year, compared to 30-45% for Indian vendors. Our interactions with autonomics companies indicate that their gross margins could be even higher, as digital workers (ie, intelligent software) are much cheaper than full-time employees in India.

WHAT'S PRICED IN?

We believe current valuations suggest that the market expects legacy margins to remain under pressure on a constant-currency basis, in line with the trends of the past three to five years. With the dollar appreciating against the rupee almost consistently over the past two to three years, most investors likely expect reported margins to remain flat in the medium term.

Increased non-linearity to lead to improved profitability

With the rise of digital models, we expect the adoption of pricing models based on business outcomes and consumption (pay-per-use) to increase. As the new pricing models have higher revenue non-linearity, due to the delinking of headcount from revenue, we anticipate Indian IT vendors' profitability to improve. This view is also in line with the high gross margins of digital service companies.

Figure 9: Digital services companies generate high gross margins

Note: Year-end for Salesforce, Workday: Jan 2015; Rackspace: Dec 2014; Servicenow, NetSuite: Dec 2015.
Source: Company data

Cost-savings through autonomics to also boost margins

Intelligent automation (autonomics) vendors—both technology specialists and system integrators—are coming up with solutions that have the value proposition of reducing reliance on human mediation and offer significant cost-savings when compared to offshoring. With the rise of such value propositions in the market, traditional vendors have also started launching autonomics solutions. We believe autonomics-driven deals could be operating-margin-accretive, as the per-capita cost of digital worker (ie, software) is 60-90% lower than that of offshore headcount. We expect vendors to retain some of the cost-savings achieved through automation, leading to higher margins.

Figure 10: Upcoming automation vendors and key value propositions

Company	Product/service offering	Value proposition/cost-savings
Arago	AutoPilot	AutoPilot reduces overall IT operating cost by 30-50% in an average corporate environment.
Blue Prism	Robotic Process Automation software platform	Robotic full-time equivalent (FTE) is one-third the cost of offshored FTE. 50% reduction in headcount in the back office.
Deskover	UiPath	UiPath robot is one-third the cost of an FTE with a potential cost-savings of 80%.
Genfour	Robotics-as-a-Service	An onshore FTE costing US\$80,000 can be replaced by an offshore FTE for US\$30,000, whereas Genfour robot performs the same function for US\$15,000.
Innovise	Cortex	Cortex reduces costs with 6x faster deployment utilising 4x fewer people.
IPsoft	Amelia, IPcenter	IPcenter, the autonomic IT management service, provides 35% IT savings compared to traditional infrastructure management.
ParadigmRPA	Automation BPO software	ParadigmRPA's RPS Enterprise licence provides 720 hours of human labour per month for US\$2,500, which implies one robot is equivalent to three to five FTE at less than 50% of the offshore FTE cost.
Thoughtonomy	Thoughtonomy Virtual Workforce	One virtual resource of Thoughtonomy Virtual Workforce (which costs similar to an offshore resource) is equivalent to six to 20 offshore FTEs.

Source: Company data

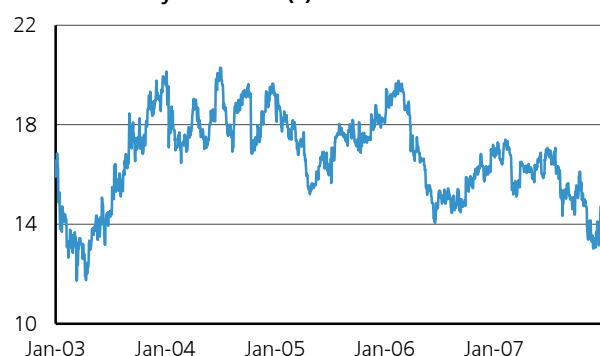
WHAT'S PRICED IN?

[return](#) ↑

We believe the market has priced in a cyclical slowdown, due to recent revenue disappointments and macroeconomic concerns, as was evident in the PE de-rating of many large vendors in 2015. However, we think a business model disruption is not priced in, which could imply a multi-year de-rating.

Incumbents witnessed multi-year de-rating during disruptions

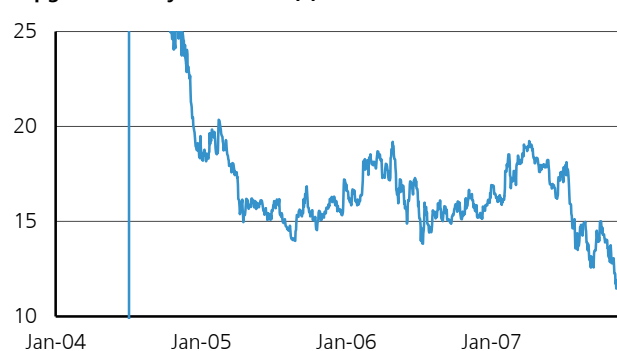
History shows that whenever there is a business model disruption in technology services, the valuations of incumbents tend to get re-rated. This was evident during the model shift to offshoring in the early 2000s, when global IT players such as IBM and Accenture experienced a multi-year PE de-rating. Their multiples corrected in 2003-07, before vendors that adopted offshoring successfully (such as Accenture and Capgemini) eventually retraced some losses. For others, like CSC, valuations have stayed muted, as they were unable to transition to the offshore business model as well as IBM and Accenture.

Figure 11: Accenture witnessed PE de-rating in 2003-07...**Accenture one-year fwd PE (x)**

Source: Company data, Bloomberg, UBS

Figure 12: ...as did IBM**IBM one-year fwd PE (x)**

Source: Company data, Bloomberg, UBS

Figure 13: Capgemini also witnessed a similar trend...**Capgemini one-year fwd PE (x)**

Source: Company data, Bloomberg, UBS

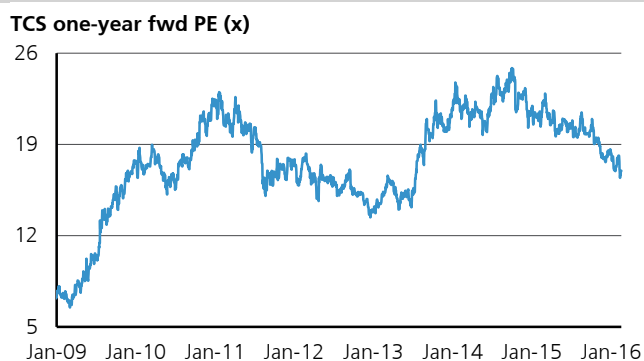
Figure 14: ...so did CSC**CSC one-year fwd PE (x)**

Source: Company data, Bloomberg, UBS

We expect Indian IT vendors' de-rating to continue

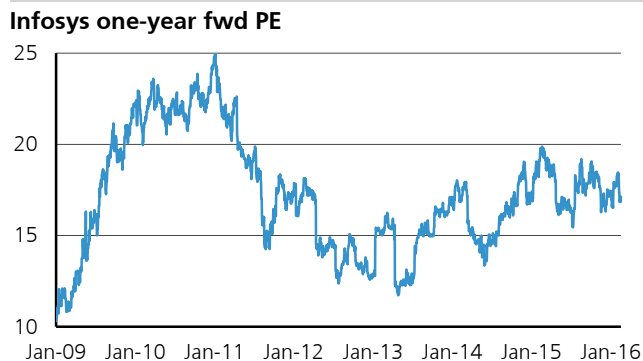
We believe the market has priced in a cyclical slowdown, due to recent revenue disappointments and macroeconomic concerns, as was evident in the PE de-rating of many large vendors in 2015. However, we think a business model disruption is not priced in, which could imply a multi-year de-rating. As the revenue disruption of digital technologies becomes more visible, we expect a multi-year PE de-rating for Indian vendors, similar to the trend in IBM and Accenture in 2003-07.

Figure 15: TCS has de-rated in the past 18 months



Source: Company data, Bloomberg, UBS estimates

Figure 16: Infosys's PE has re-rated recently



Source: Company data, Bloomberg, UBS estimates

Figure 17: Wipro's valuations have been trending down



Source: Company data, Bloomberg, UBS estimates

Figure 18: HCL Tech's PE has also de-rated



Source: Company data, Bloomberg, UBS estimates

Changes to our estimates and price targets in this report

Infosys: The company beat our initial estimates for 9M FY16, and we revise our earnings forecasts for FY17/FY18 by 6%/7% to factor in better-than-expected revenue growth. The company is likely to close the revenue growth gap with TCS in FY16E, though we remain cautious on its FY17-18 revenue relative to TCS. Our revised price target implies a PE discount of 10% (30% earlier) to our target multiple for TCS. We maintain a valuation discount to TCS, due to several concerns: 1) Infosys is not as dominant as TCS in its key industry segments, which could impact medium-term revenue growth; 2) separation of Infosys' delivery business from its industry-facing units could hamper development of its digital solutions; and 3) any gains from an aggressive pricing strategy are likely to be short-lived.

Tech Mahindra: We cut our FY17/FY18 earnings forecasts by 4%/5% to factor in slower 9M FY16 earnings compared to our initial expectations. Our revised estimates take into account likely weaker revenue growth in the company's telecom segment and a slower margin recovery, due to reduced operating leverage. Our revised price target values Tech Mahindra at 12.5x FY18E PE, in line with our target multiple for Wipro.

HCL Tech: We adjust our earnings estimates to reflect the change in HCL Tech's fiscal year-end from 30 June to 31 March, effective FY16 (ending 31 March 2016). We also incorporate the potential financial impact of the Volvo IT acquisition. This impacts our FY16/FY17/FY18 earnings estimates by -23%/+4%/+7%.

Figure 19: Our price target and EPS changes

Company	Rating		Price target (Rs)		FY16E EPS (Rs)		FY17E EPS (Rs)		FY18E EPS (Rs)	
	New	Old	New	Old	New	Old	New	Old	New	Old
Infosys	Sell	Sell	1,070	810	59.06	57.74	64.79	60.98	69.09	64.78
HCL Technologies	Neutral	Neutral	950	950	40.06	51.78	59.13	56.91	65.78	61.44
Tech Mahindra	Neutral	Neutral	475	600	29.26	29.40	33.09	34.50	37.07	38.85

Source: UBS estimates

Tata Consultancy Services Ltd.

Strong digital portfolio to help sustain leadership

Early digital investments to help keep revenue growth strong

TCS is one of the early investors in digital services among Indian IT vendors. We estimate this has helped the company increase revenue from this segment at over 30% YoY over the past year, to 13.5% (company data) of consolidated revenue at present. In an UBS Evidence Lab survey last year, TCS ranked below global vendors like IBM and Accenture in future digital outsourcing vendor preferences, in line with other Indian IT services providers. However, TCS has high market share in some digital segments, such as big data. We believe the company's strong digital capabilities could help it stay ahead of its Indian peers in terms of revenue growth in the medium term.

Core markets remain relatively robust; no evidence of market share erosion

Following the revenue disappointments in the past few quarters, there have been concerns that TCS is losing market share due to competitors' aggressive pricing. Our analysis shows the company's core markets—the US and Europe—remained relatively robust in 9M FY16, with the revenue woes coming mainly from Japan, Latin America and Diligenta, TCS' UK subsidiary. TCS has few Indian competitors in these three markets, and we find no evidence that it is losing market share to competition due to the pricing pressure just yet.

Near-term negatives likely priced in, but we see limited upside catalysts

We expect the revenue drag from TCS' underperforming segments to ease from Q1 FY17, adding a revenue tailwind of around 2% YoY. While the market is extrapolating Q4 FY16's leap year-driven seasonality to strong revenue in H1 FY17 for Infosys, revenue growth expectations for TCS are relatively muted. We see minimal risks to consensus forecasts for TCS from current levels; we are +0.3%/-1.9% away from consensus on FY17/FY18 earnings estimates, compared to -3%/-5% before Q3 FY16.

Valuation: maintain Neutral rating

At 10% below its five-year average one-year forward PE, TCS is the only stock other than Cognizant that is trading at such a discount. We expect limited valuation downside at current levels but see no upside catalysts amid potential revenue disruption. Our price target is based on 17.2x FY18E PE.

Equities

India
Diversified Technology Services

12-month rating **Neutral**

12m price target **Rs2,550.00**

Price **Rs2,278.00**

RIC: TCS.BO BBG: TCS IB

Trading data and key metrics

52-wk range	Rs2,774.70-2,196.05
Market cap.	Rs4,462bn/US\$65.3bn
Shares o/s	1,959m (ORD)
Free float	30%
Avg. daily volume ('000)	1,036
Avg. daily value (m)	Rs2,432.8
Common s/h equity (03/16E)	Rs703bn
P/BV (03/16E)	6.3x
Net debt / EBITDA (03/16E)	NM

EPS (UBS, diluted) (Rs)

	UBS	Cons.
03/16E	123.11	121.95
03/17E	135.38	133.19
03/18E	147.84	150.65

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Highlights (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenues	629,895	818,094	946,484	1,083,227	1,202,087	1,318,862	1,439,239	1,567,039
EBIT (UBS)	170,080	238,079	227,964	289,231	317,187	341,391	368,133	398,305
Net earnings (UBS)	139,060	191,168	196,484	241,130	265,180	289,583	314,161	342,208
EPS (UBS, diluted) (Rs)	71.05	97.60	100.31	123.11	135.38	147.84	160.39	174.71
DPS (Rs)	22.00	32.00	79.00	49.24	54.15	59.14	64.16	69.88
Net (debt) / cash	15,109	11,720	15,045	38,191	65,597	76,308	85,966	100,701
Profitability/valuation	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
EBIT margin %	27.0	29.1	24.1	26.7	26.4	25.9	25.6	25.4
ROIC (EBIT) %	48.7	53.2	42.8	47.9	44.8	41.2	38.1	35.7
EV/EBITDA (core) x	14.0	14.7	19.6	14.4	13.1	12.1	11.1	10.2
P/E (UBS, diluted) x	18.3	19.3	24.6	18.5	16.8	15.4	14.2	13.0
Equity FCF (UBS) yield %	3.8	3.5	3.8	4.2	5.0	5.5	6.1	6.6
Net dividend yield %	1.7	1.7	3.2	2.2	2.4	2.6	2.8	3.1

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of Rs2,278.00 on 17 Feb 2016 20:26 HKT

Investment Thesis

Tata Consultancy Services Ltd.

Investment case

TCS remains a strong market leader in the offshore IT services space, with a well-diversified services portfolio and geographic spread. We believe the company's leadership in large sectors, such as banking and manufacturing, and strong R&D capabilities could support a smooth transition to digital outsourcing models, which should help sustain its market share gains in the medium term.

Upside scenario

In our upside scenario, we assume 11% YoY revenue growth in reported dollar terms, as a pick-up in global GDP growth drives better demand for IT services, which in turn should ease the pricing pressure on the legacy business. We also assume the rupee continues to weaken to 69 as the US dollar strengthens against emerging market currencies. We expect EBIT margin to improve to 27% in FY16. Our upside valuation of Rs2,998.00 is based on 21x PE, close to one standard deviation above its five-year average multiple.

Downside scenario

In this scenario, we assume global GDP slows more than anticipated, exerting pressure on demand for IT services. We also assume the rupee strengthens to 65 in a relatively stable Indian economy. Revenue growth in this scenario slows to 6.5% YoY in FY16E, with the EBIT margin falling to 25.8%. We expect TCS to correct to 15x PE, around one standard deviation below its five-year average. This implies a valuation of Rs1,920.00 per share.

Upcoming catalysts

TCS will report its next quarterly earnings in April 2016. A softer-than-expected result in a seasonally strong quarter would be a negative catalyst.

12-month rating

Neutral

12m price target

Rs2,550.00

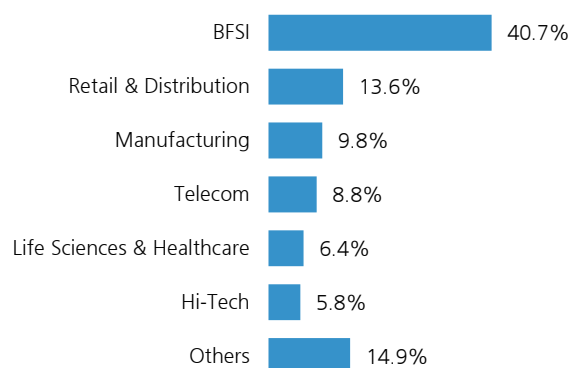
Business description

Incorporated in 1968, Tata Consultancy Services (TCS) is the largest Indian IT-services company. It generated US\$15.5bn revenue and had 319,656 employees in FY15. TCS provides services in application development and maintenance, enterprise solutions, IT infrastructure management, consulting, and business process outsourcing. Its customers are from the banking, financial services and insurance, manufacturing, telecom, retail and distribution, energy and utilities, and life sciences verticals. Its key markets are North America (52% of FY15 revenue) and Europe (28%).

Industry outlook

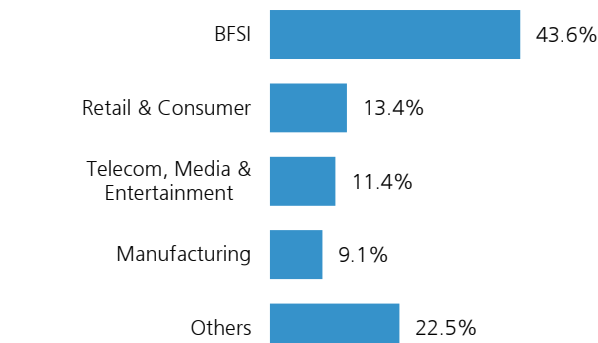
We believe the Indian IT services sector is facing a structural disruption, with large IT users beginning to adopt new outsourcing models for incremental cost efficiencies. Despite stable demand and growth in the global IT outsourcing market, many large Indian offshore vendors missed consensus revenue expectations in FY15, with soft revenue growth across key markets and service lines. Price competition has intensified in the past 12 months, indicating increased pressure on revenue from the legacy business, which contributes 85-90% of the industry's revenue.

Revenue by industry (FY15)



Source: Company data

EBIT by segment (FY15)



Source: Company data

Tata Consultancy Services Ltd. (TCS.BO)

	03/13	03/14	03/15	03/16E	% ch	03/17E	% ch	03/18E	03/19E	03/20E
Income statement (Rsm)										
Revenues	629,895	818,094	946,484	1,083,227	14.4	1,202,087	11.0	1,318,862	1,439,239	1,567,039
Gross profit	297,395	396,029	414,210	491,499	18.7	538,321	9.5	581,369	624,605	677,172
EBITDA (UBS)	180,872	251,322	246,662	307,999	24.9	335,099	8.8	361,043	389,578	421,655
Depreciation & amortisation	(10,792)	(13,243)	(18,698)	(18,768)	0.4	(17,912)	-4.6	(19,652)	(21,446)	(23,350)
EBIT (UBS)	170,080	238,079	227,964	289,231	26.9	317,187	9.7	341,391	368,133	398,305
Associates & investment income	0	0	0	0	-	0	-	0	0	0
Other non-operating income	130	260	13,085	5,882	-55.0	8,750	48.8	12,000	12,000	12,000
Net interest	10,689	15,631	18,311	21,572	17.8	23,947	11.0	28,810	34,660	41,698
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Profit before tax	180,899	253,970	259,360	316,685	22.1	349,884	10.5	382,200	414,793	452,003
Tax	(40,346)	(60,712)	(60,828)	(74,220)	-22.0	(83,972)	-13.1	(91,728)	(99,550)	(108,481)
Profit after tax	140,553	193,258	198,532	242,465	22.1	265,912	9.7	290,472	315,242	343,522
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	(1,493)	(2,090)	(2,048)	(1,335)	34.8	(732)	45.2	(890)	(1,081)	(1,314)
Extraordinary items	0	0	0	0	-	0	-	0	0	0
Net earnings (local GAAP)	139,060	191,168	196,484	241,130	22.7	265,180	10.0	289,583	314,161	342,208
Net earnings (UBS)	139,060	191,168	196,484	241,130	22.7	265,180	10.0	289,583	314,161	342,208
Tax rate (%)	22.3	23.9	23.5	23.4	-0.1	24.0	2.4	24.0	24.0	24.0
Per share (Rs)										
EPS (UBS, diluted)	71.05	97.60	100.31	123.11	22.7	135.38	10.0	147.84	160.39	174.71
EPS (local GAAP, diluted)	71.05	97.60	100.31	123.11	22.7	135.38	10.0	147.84	160.39	174.71
EPS (UBS, basic)	71.05	97.60	100.31	123.11	22.7	135.38	10.0	147.84	160.39	174.71
Net DPS (Rs)	22.00	32.00	79.00	49.24	-37.7	54.15	10.0	59.14	64.16	69.88
Cash EPS (UBS, diluted)*	76.56	104.36	109.86	132.69	20.8	144.53	8.9	157.88	171.34	186.63
Book value per share	209.22	282.51	293.44	358.93	22.3	430.96	20.1	509.61	594.94	687.88
Average shares (diluted)	1,957.22	1,958.73	1,958.73	1,958.73	0.0	1,958.73	0.0	1,958.73	1,958.73	1,958.73
Balance sheet (Rsm)										
Cash and equivalents	18,432	14,688	18,622	41,525	123.0	68,711	65.5	79,226	88,706	103,281
Other current assets	309,953	418,199	460,381	492,995	7.1	524,968	6.5	558,301	592,870	630,695
Total current assets	328,384	432,887	479,003	534,520	11.6	593,679	11.1	637,527	681,576	733,977
Net tangible fixed assets	81,944	103,644	115,716	128,948	11.4	143,036	10.9	158,384	171,938	186,589
Net intangible fixed assets	35,063	41,568	39,308	39,767	1.2	39,767	0.0	39,767	39,767	39,767
Investments / other assets	74,154	111,026	115,511	185,843	60.9	262,110	41.0	365,507	485,274	611,868
Total assets	519,545	689,125	749,537	889,078	18.6	1,038,592	16.8	1,201,185	1,378,556	1,572,200
Trade payables & other ST liabilities	85,716	109,056	144,281	154,450	7.0	162,376	5.1	170,218	179,551	189,986
Short term debt	1,013	1,696	2,434	2,191	-10.00	1,972	-10.00	1,775	1,597	1,437
Total current liabilities	86,729	110,752	146,715	156,641	6.8	164,347	4.9	171,993	181,148	191,423
Long term debt	2,310	1,273	1,143	1,143	0.0	1,143	0.0	1,143	1,143	1,143
Other long term liabilities	14,465	16,845	17,776	17,776	0.0	17,776	0.0	17,776	17,776	17,776
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	103,503	128,869	165,634	175,559	6.0	183,266	4.4	190,912	200,067	210,342
Common s/h equity	409,481	553,352	574,768	703,048	22.3	844,124	20.1	998,182	1,165,316	1,347,371
Minority interests	6,561	6,905	9,136	10,470	14.6	11,202	7.0	12,092	13,173	14,487
Total liabilities & equity	519,545	689,125	749,537	889,078	18.6	1,038,592	16.8	1,201,185	1,378,556	1,572,200
Cash flow (Rsm)										
Net income (before pref divs)	139,060	191,168	196,484	241,130	22.7	265,180	10.0	289,583	314,161	342,208
Depreciation & amortisation	10,792	13,243	18,698	18,768	0.4	17,912	-4.6	19,652	21,446	23,350
Net change in working capital	(20,239)	(39,813)	11,181	(25,225)	-	(24,910)	1.2	(26,331)	(26,084)	(28,357)
Other operating	(6,390)	(5,382)	(14,308)	(17,459)	-22.0	(4,072)	76.7	(4,108)	(4,201)	(4,031)
Operating cash flow	123,222	159,217	212,055	217,215	2.4	254,110	17.0	278,796	305,322	333,169
Tangible capital expenditure	(25,788)	(30,605)	(28,786)	(32,000)	-11.2	(32,000)	0.0	(35,000)	(35,000)	(38,000)
Intangible capital expenditure	(149)	(75)	(18)	0	-	0	-	0	0	0
Net (acquisitions) / disposals	0	0	0	0	-	0	-	0	0	0
Other investing	(42,614)	(78,049)	(6,974)	(49,220)	-	(70,600)	-	(97,559)	(113,638)	(120,281)
Investing cash flow	(68,552)	(108,729)	(35,778)	(81,220)	-127.0	(102,600)	-26.3	(132,559)	(148,638)	(158,281)
Equity dividends paid	(57,021)	(54,930)	(170,285)	(112,849)	33.7	(124,104)	-10.0	(135,525)	(147,027)	(160,153)
Share issues / (buybacks)	0	(1,000)	(745)	0	-	0	-	0	0	0
Other financing	0	0	0	0	-	0	-	0	0	0
Change in debt & pref shares	365	(454)	(255)	(243)	4.54	(219)	10.00	(197)	(177)	(160)
Financing cash flow	(56,656)	(56,384)	(171,285)	(113,092)	34.0	(124,323)	-9.9	(135,722)	(147,205)	(160,313)
Cash flow inc/(dec) in cash	(1,985)	(5,897)	4,992	22,903	358.8	27,187	18.7	10,515	9,480	14,575
FX / non cash items	(14,303)	2,154	(1,058)	0	100.0	0	-	0	0	0
Balance sheet inc/(dec) in cash	(16,288)	(3,743)	3,934	22,903	NM	27,187	18.7	10,515	9,480	14,575

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.*Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

Tata Consultancy Services Ltd. (TCS.BO)

Valuation (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
P/E (local GAAP, diluted)	18.3	19.3	24.6	18.5	16.8	15.4	14.2	13.0
P/E (UBS, diluted)	18.3	19.3	24.6	18.5	16.8	15.4	14.2	13.0
P/CEPS	17.0	18.1	22.4	17.2	15.8	14.4	13.3	12.2
Equity FCF (UBS) yield %	3.8	3.5	3.8	4.2	5.0	5.5	6.1	6.6
Net dividend yield (%)	1.7	1.7	3.2	2.2	2.4	2.6	2.8	3.1
P/BV x	6.2	6.7	8.4	6.3	5.3	4.5	3.8	3.3
EV/revenues (core)	4.0	4.5	5.1	4.1	3.7	3.3	3.0	2.8
EV/EBITDA (core)	14.0	14.7	19.6	14.4	13.1	12.1	11.1	10.2
EV/EBIT (core)	14.9	15.5	21.2	15.3	13.8	12.8	11.8	10.8
EV/OpFCF (core)	17.0	18.6	20.2	16.8	15.0	13.9	12.7	11.7
EV/op. invested capital	7.3	8.2	9.1	7.3	6.2	5.3	4.5	3.9
Enterprise value (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Market cap.	2,547,274	3,689,283	4,828,667	4,461,982	4,461,982	4,461,982	4,461,982	4,461,982
Net debt (cash)	(13,813)	(13,414)	(13,382)	(26,618)	(51,894)	(51,894)	(81,137)	(93,334)
Buy out of minorities	6,561	6,905	9,136	10,470	11,202	12,092	13,173	14,487
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	2,540,021	3,682,773	4,824,420	4,445,835	4,421,291	4,422,180	4,394,018	4,383,136
Non core assets	0	0	0	(19,297)	(28,946)	(39,077)	(52,754)	(71,218)
Core enterprise value	2,540,021	3,682,773	4,824,420	4,426,537	4,392,345	4,383,103	4,341,264	4,311,918
Growth (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenue	28.8	29.9	15.7	14.4	11.0	9.7	9.1	8.9
EBITDA (UBS)	25.4	39.0	-1.9	24.9	8.8	7.7	7.9	8.2
EBIT (UBS)	25.8	40.0	-4.2	26.9	9.7	7.6	7.8	8.2
EPS (UBS, diluted)	30.1	37.4	2.8	22.7	10.0	9.2	8.5	8.9
Net DPS	-12.0	45.4	146.9	-37.7	10.0	9.2	8.5	8.9
Margins & Profitability (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Gross profit margin	47.2	48.4	43.8	45.4	44.8	44.1	43.4	43.2
EBITDA margin	28.7	30.7	26.1	28.4	27.9	27.4	27.1	26.9
EBIT margin	27.0	29.1	24.1	26.7	26.4	25.9	25.6	25.4
Net earnings (UBS) margin	22.1	23.4	20.8	22.3	22.1	22.0	21.8	21.8
ROIC (EBIT)	48.7	53.2	42.8	47.9	44.8	41.2	38.1	35.7
ROIC post tax	37.8	40.5	32.8	36.7	34.0	31.3	28.9	27.2
ROE (UBS)	37.8	39.7	34.8	37.7	34.3	31.4	29.0	27.2
Capital structure & Coverage (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Net debt / EBITDA	(0.1)	(.0)	(0.1)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
Net debt / total equity %	(3.6)	(2.1)	(2.6)	(5.4)	(7.7)	(7.6)	(7.3)	(7.4)
Net debt / (net debt + total equity) %	(3.8)	(2.1)	(2.6)	(5.7)	(8.3)	(8.2)	(7.9)	(8.0)
Net debt/EV %	(0.6)	(0.3)	(0.3)	(0.9)	(1.5)	(1.7)	(2.0)	(2.3)
Capex / depreciation %	NM	NM	154.0	170.5	178.7	178.1	163.2	162.7
Capex / revenue %	4.1	3.7	3.0	3.0	2.7	2.7	2.4	2.4
EBIT / net interest	NM	NM	NM	NM	NM	NM	NM	NM
Dividend cover (UBS)	3.2	3.1	1.3	2.5	2.5	2.5	2.5	2.5
Div. payout ratio (UBS) %	31.0	32.8	78.8	40.0	40.0	40.0	40.0	40.0
Revenues by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	629,895	818,094	946,484	1,083,227	1,202,087	1,318,862	1,439,239	1,567,039
Total	629,895	818,094	946,484	1,083,227	1,202,087	1,318,862	1,439,239	1,567,039
EBIT (UBS) by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	170,080	238,079	227,964	289,231	317,187	341,391	368,133	398,305
Total	170,080	238,079	227,964	289,231	317,187	341,391	368,133	398,305

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Cognizant Technology Solutions

Industry focus to help smooth the digital transition

Focus on few large sectors to help speed up development of digital capabilities

Unlike many services vendors, Cognizant remains focused on a few large industries. It derives more than two-thirds of its revenue from the banking, financial services & insurance (BFSI) and healthcare & life sciences sectors, where it maintains market-leading revenue growth. The company also continues to build its front-end consulting business in these segments. We believe Cognizant's strong industry focus is an advantage, as IT users are likely to require digital solutions tailored to their industries. Like TCS, Cognizant also ranked below global vendors in digital vendor preferences in the UBS Evidence Lab survey last year. However, it scored well in cloud services—a large digital segment, suggesting Cognizant is ahead of its Indian peers in this space.

Ability to make large acquisitions (such as TriZetto) is an advantage

While history shows Cognizant has been more open to M&A than its Indian peers, until recently the company had stuck to small deals. The US\$2.7bn acquisition of TriZetto in late 2014, while a departure from its standard M&A policy of tuck-in acquisitions, was a bold move to bring utility computing capabilities in-house, in our view. We believe Cognizant's ability to engage in large transactions could support a faster transition to digital services than its Indian peers.

Valuations appear reasonable relative to medium-term earnings potential

Cognizant trades at a slight PE premium to TCS, which we think is due to its stronger revenue growth visibility in 2016. We believe valuations are reasonable relative to its earnings growth potential in the medium term and that its softer-than-expected 2016 guidance has been priced in. However, we see no upside catalyst in the face of likely industry-wide disruptions.

Valuation: maintain Neutral rating

We maintain our Neutral rating. Like TCS, Cognizant is trading at a 10% discount to its five-year average one-year forward PE. We expect limited valuation downside at current levels but see no upside catalysts amid potential revenue disruption. Our price target is based on 17.9x 2017E PE, which is at a 5% premium to our FY18 target multiple for TCS, to account for better revenue visibility in 2016.

Equities

Americas
Diversified Technology Services

12-month rating **Neutral**

12m price target **US\$63.00**

Price **US\$55.01**

RIC: CTSH.O BBG: CTSH US

Trading data and key metrics

52-wk range	US\$69.76-52.11
Market cap.	US\$33.6bn
Shares o/s	610m (COM)
Free float	100%
Avg. daily volume ('000)	4,595
Avg. daily value (m)	US\$273.5
Common s/h equity (12/16E)	US\$11.1bn
P/BV (12/16E)	3.0x
Net debt / EBITDA (12/16E)	NM

EPS (UBS, diluted) (US\$)

	12/16E	
	UBS	Cons.
Q1E	0.76	0.79
Q2E	0.84	0.84
Q3E	0.84	0.87
Q4E	0.87	0.89
12/16E	3.31	3.39
12/17E	3.66	3.86
12/18E	4.00	4.34

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Highlights (US\$m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenues	8,843	10,263	12,416	13,894	15,423	16,965	18,492	20,156
EBIT (UBS)	1,821	2,068	2,450	2,665	2,936	3,217	3,526	3,859
Net earnings (UBS)	1,333	1,598	1,877	2,017	2,216	2,426	2,635	2,878
EPS (UBS, diluted) (US\$)	2.19	2.61	3.06	3.31	3.66	4.00	4.35	4.75
DPS (US\$)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Net (debt) / cash	3,747	2,137	3,662	5,600	7,384	9,636	12,111	14,921
Profitability/valuation	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
EBIT margin %	20.6	20.2	19.7	19.2	19.0	19.0	19.1	19.1
ROIC (EBIT) %	83.2	51.8	43.7	48.0	53.2	57.4	63.0	70.1
EV/EBITDA (core) x	10.5	12.1	12.7	9.6	8.1	6.9	5.7	4.6
P/E (UBS, diluted) x	17.7	18.8	20.4	16.6	15.0	13.7	12.7	11.6
Equity FCF (UBS) yield %	5.4	4.8	5.3	6.4	7.2	7.6	8.6	8.8
Net dividend yield %	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of US\$55.01 on 17 Feb 2016 07:41 EST

Investment Thesis

Cognizant Technology Solutions

Investment case

Cognizant has become a tier-1 global services player by moving up the value stack to build on its labour arbitrage capabilities. We believe SMAC technologies (Horizon 3), vertical BPO (Horizon 2), remote infrastructure management, and expansion into Europe could double its available markets and help it maintain mid-teen revenue growth. Although we are positive on the company's revenue growth prospects in the long term, we think the risk-reward is balanced for now, as it will take time for the company to integrate its largest acquisition yet and achieve synergies.

Upside scenario

In this scenario, we assume organic growth accelerates to 15%, driven by improved demand for IT services due to a better US macro environment. Operating margins should touch the higher end of the company's target 19-20% band. The market values Cognizant on PE, in line with global trends. We expect Cognizant to trade 21x PE, close to one standard deviation above its five-year average, implying a fair value of US\$73.50.

Downside scenario

In this scenario, we assume organic growth slows to 10% as a result of GDP slowdown in the US and delays in contract flows, due to widely reported M&As among US healthcare companies, some of which make up Cognizant's large clients. EBIT margin in this scenario falls to 19% in 2016E, the lower end of the company's 19-20% target range. We expect the stock to correct to 15x PE, around one standard deviation below its five-year average. We derive a valuation of US\$45.00 in this case.

Upcoming catalysts

Cognizant will report its Q116 earnings in May 2016. The company needs to deliver at the higher end of its quarterly revenue guidance to meet consensus expectations.

12-month rating

Neutral

12m price target

US\$63.00

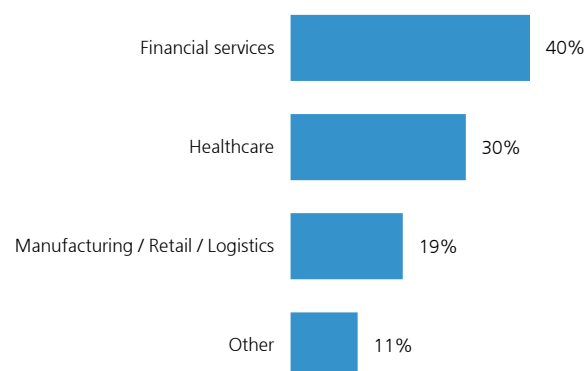
Business description

Cognizant is a leading provider of offshore IT services to US and European companies. It provides application development and management solutions under an on-site/offshore business model with its India-based development centres. The company is focused on delivering full life-cycle e-business and application service solutions across several key verticals, including financial services, healthcare, retail, manufacturing and logistics. More than two-thirds of Cognizant's revenue comes from its clients in North America.

Industry outlook

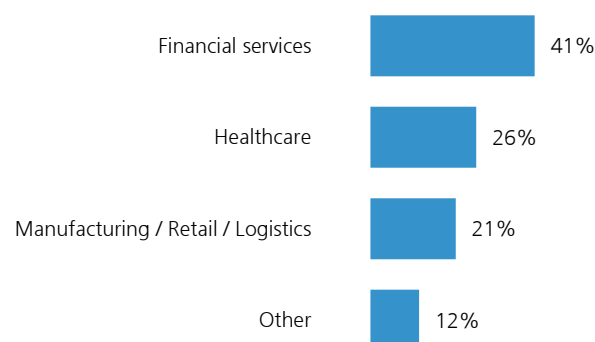
We believe the Indian IT services sector is facing a structural disruption, with large IT users beginning to adopt new outsourcing models for incremental cost efficiencies. Despite stable demand and growth in the global IT outsourcing market, many large Indian offshore vendors missed consensus revenue expectations in FY15, with soft revenue growth across key markets and service lines. Price competition has intensified in the past 12 months, indicating increased pressure on revenue from the legacy business, which contributes 85-90% of the industry's revenue.

Revenue by segment (2014)



Source: Company data

Operating profit by segment (2014)



Source: Company data

Cognizant Technology Solutions (CTSH.O)

	12/13	12/14	12/15	12/16E	% ch	12/17E	% ch	12/18E	12/19E	12/20E
Income statement (US\$m)										
Revenues	8,843	10,263	12,416	13,894	11.9	15,423	11.0	16,965	18,492	20,156
Gross profit	3,578	4,122	4,976	5,549	11.5	6,214	12.0	6,840	7,510	8,238
EBITDA (UBS)	1,993	2,268	2,775	3,015	8.7	3,324	10.2	3,644	3,992	4,367
Depreciation & amortisation	(172)	(200)	(325)	(350)	7.7	(389)	11.0	(428)	(466)	(508)
EBIT (UBS)	1,821	2,068	2,450	2,665	8.8	2,936	10.1	3,217	3,526	3,859
Associates & investment income	0	0	0	0	-	0	-	0	0	0
Other non-operating income	(39)	(21)	(49)	(44)	10.1	(48)	-9.0	(52)	(60)	(68)
Net interest	49	60	71	105	48.8	128	21.9	136	144	152
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Profit before tax	1,831	2,107	2,471	2,726	10.3	3,015	10.6	3,300	3,610	3,943
Tax	(498)	(509)	(594)	(709)	-19.3	(799)	-12.7	(875)	(975)	(1,065)
Profit after tax	1,333	1,598	1,877	2,017	7.5	2,216	9.9	2,426	2,635	2,878
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	0	0	0	0	-	0	-	0	0	0
Extraordinary items	0	0	0	0	-	0	-	0	0	0
Net earnings (local GAAP)	1,333	1,598	1,877	2,017	7.5	2,216	9.9	2,426	2,635	2,878
Net earnings (UBS)	1,333	1,598	1,877	2,017	7.5	2,216	9.9	2,426	2,635	2,878
Tax rate (%)	27.2	24.2	24.1	26.0	8.1	26.5	1.9	26.5	27.0	27.0
Per share (US\$)										
EPS (UBS, diluted)	2.19	2.61	3.06	3.31	8.1	3.66	10.6	4.00	4.35	4.75
EPS (local GAAP, diluted)	2.19	2.61	3.06	3.31	8.1	3.66	10.6	4.00	4.35	4.75
EPS (UBS, basic)	2.19	2.61	3.06	3.31	8.1	3.66	10.6	4.00	4.35	4.75
Net DPS (US\$)	0.00	0.00	0.00	0.00	-	0.00	-	0.00	0.00	0.00
Cash EPS (UBS, diluted) ¹	2.47	2.93	3.59	3.88	8.1	4.30	10.7	4.71	5.12	5.59
Book value per share	10.17	12.73	15.21	18.23	19.8	21.35	17.1	25.25	29.12	33.65
Average shares (diluted)	609.66	612.50	613.28	609.95	-0.5	606.00	-0.6	606.00	606.00	606.00
Balance sheet (US\$m)										
Cash and equivalents	3,747	3,775	4,950	6,848	38.4	8,592	25.5	10,804	12,992	15,802
Other current assets	2,400	2,976	2,959	3,301	11.6	3,671	11.2	4,041	4,384	4,750
Total current assets	6,148	6,750	7,909	10,149	28.3	12,263	20.8	14,845	17,376	20,552
Net tangible fixed assets	1,081	1,247	1,271	1,360	7.0	1,485	9.2	1,618	1,636	1,791
Net intangible fixed assets	576	3,367	3,269	3,109	-4.9	3,229	3.9	3,269	3,309	3,349
Investments / other assets	404	354	616	700	13.6	777	11.0	855	932	1,016
Total assets	8,209	11,719	13,065	15,319	17.2	17,754	15.9	20,587	23,253	26,708
Trade payables & other ST liabilities	1,775	1,892	2,307	2,615	13.3	3,153	20.6	3,594	4,136	4,782
Short term debt	0	700	406	366	-9.84	326	-10.92	286	0	0
Total current liabilities	1,775	2,592	2,714	2,981	9.8	3,479	16.7	3,880	4,136	4,782
Long term debt	0	938	881	881	0.0	881	0.0	881	881	881
Other long term liabilities	299	449	192	375	94.8	457	22.1	525	590	655
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	2,073	3,979	3,787	4,237	11.9	4,818	13.7	5,286	5,607	6,318
Common s/h equity	6,136	7,740	9,278	11,082	19.4	12,936	16.7	15,300	17,645	20,390
Minority interests	0	0	0	0	-	0	-	0	0	0
Total liabilities & equity	8,209	11,719	13,065	15,319	17.2	17,754	15.9	20,586	23,252	26,708
Cash flow (US\$m)										
Net income (before pref divs)	1,333	1,598	1,877	2,017	7.5	2,216	9.9	2,426	2,635	2,878
Depreciation & amortisation	172	200	325	350	7.7	389	11.0	428	466	508
Net change in working capital	(41)	(140)	74	95	28.1	176	85.7	78	206	11
Other operating	56	64	75	96	27.6	117	21.2	138	159	181
Operating cash flow	1,520	1,722	2,351	2,558	8.8	2,897	13.3	3,069	3,466	3,578
Tangible capital expenditure	(262)	(288)	(320)	(395)	-23.4	(470)	-19.0	(517)	(569)	(626)
Intangible capital expenditure	0	0	0	0	-	0	-	0	0	0
Net (acquisitions) / disposals	(194)	(2,711)	(50)	(50)	0.0	(50)	0.0	(50)	(50)	(50)
Other investing	(275)	(385)	(200)	(200)	-	(399)	-	(159)	(399)	(382)
Investing cash flow	(731)	(3,384)	(570)	(645)	-13.2	(919)	-42.5	(726)	(1,017)	(1,058)
Equity dividends paid	0	0	0	0	-	0	-	0	0	0
Share issues / (buybacks)	(179)	(271)	(271)	(271)	0.0	(271)	0.0	(271)	(271)	(271)
Other financing	148	176	189	209	10.62	230	10.25	253	278	305
Change in debt & pref shares	0	0	0	0	-	0	-	0	0	0
Financing cash flow	(31)	(95)	(83)	(63)	24.3	(41)	34.2	(18)	7	34
Cash flow inc/(dec) in cash	758	(1,757)	1,699	1,851	9.0	1,938	4.7	2,325	2,456	2,554
FX / non cash items	125	1,784	(524)	47	-	(194)	-	(113)	(267)	256
Balance sheet inc/(dec) in cash	884	27	1,175	1,898	61.6	1,744	-8.1	2,212	2,189	2,810

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.¹Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

Cognizant Technology Solutions (CTSH.O)

Valuation (x)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
P/E (local GAAP, diluted)	17.7	18.8	20.4	16.6	15.0	13.7	12.7	11.6
P/E (UBS, diluted)	17.7	18.8	20.4	16.6	15.0	13.7	12.7	11.6
P/CEPS	15.7	16.7	17.3	14.2	12.8	11.7	10.8	9.8
Equity FCF (UBS) yield %	5.4	4.8	5.3	6.4	7.2	7.6	8.6	8.8
Net dividend yield (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
P/BV x	3.8	3.8	4.1	3.0	2.6	2.2	1.9	1.6
EV/revenues (core)	2.4	2.7	2.8	2.1	1.8	1.5	1.2	1.0
EV/EBITDA (core)	10.5	12.1	12.7	9.6	8.1	6.9	5.7	4.6
EV/EBIT (core)	11.5	13.2	14.3	10.8	9.2	7.8	6.4	5.2
EV/OpFCF (core)	12.4	14.9	13.9	10.7	8.9	7.8	6.2	5.0
EV/op. invested capital	9.6	6.8	6.3	5.2	4.9	4.5	4.1	3.6
Enterprise value (US\$m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Market cap.	23,276	29,689	38,013	33,551	33,551	33,551	33,551	33,551
Net debt (cash)	(2,329)	(2,329)	(2,900)	(4,631)	(6,492)	(8,510)	(10,874)	(13,516)
Buy out of minorities	0	0	0	0	0	0	0	0
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	20,947	27,360	35,113	28,919	27,058	25,040	22,677	20,035
Non core assets	0	0	0	0	0	0	0	0
Core enterprise value	20,947	27,360	35,113	28,919	27,058	25,040	22,677	20,035
Growth (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Revenue	20.4	16.1	21.0	11.9	11.0	10.0	9.0	9.0
EBITDA (UBS)	22.7	13.8	22.4	8.7	10.2	9.6	9.5	9.4
EBIT (UBS)	23.5	13.6	18.5	8.8	10.1	9.6	9.6	9.4
EPS (UBS, diluted)	17.6	19.3	17.3	8.1	10.6	9.5	8.6	9.2
Net DPS	-	-	-	-	-	-	-	-
Margins & Profitability (%)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Gross profit margin	40.5	40.2	40.1	39.9	40.3	40.3	40.6	40.9
EBITDA margin	22.5	22.1	22.4	21.7	21.6	21.5	21.6	21.7
EBIT margin	20.6	20.2	19.7	19.2	19.0	19.0	19.1	19.1
Net earnings (UBS) margin	15.1	15.6	15.1	14.5	14.4	14.3	14.2	14.3
ROIC (EBIT)	83.2	51.8	43.7	48.0	53.2	57.4	63.0	70.1
ROIC post tax	60.5	39.2	33.2	35.5	39.1	42.2	46.0	51.2
ROE (UBS)	24.3	23.0	22.1	19.8	18.5	17.2	16.0	15.1
Capital structure & Coverage (x)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Net debt / EBITDA	(1.9)	(0.9)	(1.3)	(1.9)	(2.2)	(2.6)	(3.0)	(3.4)
Net debt / total equity %	(61.1)	(27.6)	(39.5)	(50.5)	(57.1)	(63.0)	(68.6)	(73.2)
Net debt / (net debt + total equity) %	NM	(38.1)	(65.2)	NM	NM	NM	NM	NM
Net debt/EV %	(17.9)	(7.8)	(10.4)	(19.4)	(27.3)	(38.5)	(53.4)	(74.5)
Capex / depreciation %	151.9	144.1	98.4	112.8	120.9	120.9	122.0	123.2
Capex / revenue %	3.0	2.8	2.6	2.8	3.0	3.0	3.1	3.1
EBIT / net interest	NM	NM	NM	NM	NM	NM	NM	NM
Dividend cover (UBS)	-	-	-	-	-	-	-	-
Div. payout ratio (UBS) %	-	-	-	-	-	-	-	-
Revenues by division (US\$m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Others	8,843	10,263	12,416	13,894	15,423	16,965	18,492	20,156
Total	8,843	10,263	12,416	13,894	15,423	16,965	18,492	20,156
EBIT (UBS) by division (US\$m)	12/13	12/14	12/15	12/16E	12/17E	12/18E	12/19E	12/20E
Others	1,821	2,068	2,450	2,665	2,936	3,217	3,526	3,859
Total	1,821	2,068	2,450	2,665	2,936	3,217	3,526	3,859

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Infosys Ltd

Improved performance, but still some time away from industry leadership

Leadership in large industry segments key to sustainable revenue growth

Over the past few years, Infosys has lost its dominance in its key segments, such as BFSI and retail. We view this, and the re-organisation of the company's delivery units into a horizontal unit separate from its industry-facing businesses, as key impediment to sustainable long-term revenue growth leadership. We are concerned that the company's increasingly horizontal services-led strategy could be detrimental to market share gains amid the rise of new digital services outsourcing models.

Sustaining an aggressive pricing strategy is likely to be a challenge

We believe Infosys' price-aggressive large deal strategy led its revenue improvement in 9M FY16, as was evident from the volume and price trade-off seen in the past four to six quarters. We believe such a strategy is effective only for a limited timeframe, as the industry's competitive nature forces price equilibrium among vendors within a short period of time. We believe unusual seasonality due to the leap year is largely responsible for Infosys' strong Q4 FY16 revenue guidance, and the market is extrapolating this to medium-term revenue growth projections.

We raise FY17/FY18 EPS forecasts by 6%/7% on improved near-term visibility

Given the better-than-expected FY16 revenue guidance, we raise our FY17/FY18 EPS forecasts by 6%/7%; we are 3.3%/7.5% below consensus, compared to 8%/13% below previously.

Valuation: raise price target from Rs810.00 to Rs1,070.00; maintain Sell rating

Our revised price target is based on 15.4x FY18E PE. This implies a discount to our target PE for TCS of 10% (30% previously). Infosys is trading at a 4% premium to its five-year average one-year forward PE and is the only stock that has seen a valuation re-rating in the past 12 months. We still see risks to consensus earnings forecasts and limited potential for valuations to improve from current levels.

Equities

India
Diversified Technology Services

12-month rating

Sell

12m price target

Rs1,070.00
Prior: Rs810.00

Price

Rs1,095.45
RIC: INFY.BO **BBG:** INFO IB

Trading data and key metrics

52-wk range Rs1,180.50-937.00

Market cap. Rs2,504bn/US\$36.6bn

Shares o/s 2,286m (ORD)

Free float 85%

Avg. daily volume ('000) 3,272

Avg. daily value (m) Rs3,581.3

Common s/h equity (03/16E) Rs557bn

P/BV (03/16E) 4.5x

Net debt / EBITDA (03/16E) NM

EPS (UBS, diluted) (Rs)

	From	To	% ch	Cons.
03/16E	57.74	59.06	2	58.83
03/17E	60.98	64.79	6	66.97
03/18E	64.78	69.09	7	74.66

Diviya Nagarajan

Analyst

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Highlights (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenues	403,520	501,330	533,190	624,958	703,174	751,172	802,048	853,711
EBIT (UBS)	104,290	120,410	138,320	155,989	173,382	180,366	187,587	193,538
Net earnings (UBS)	94,210	106,480	123,300	135,000	148,151	158,022	163,478	170,087
EPS (UBS, diluted) (Rs)	41.22	46.59	53.95	59.06	64.79	69.09	71.45	74.32
DPS (Rs)	10.50	15.75	22.25	29.53	32.39	34.54	35.72	37.16
Net (debt) / cash	240,660	302,580	325,860	354,475	390,835	430,543	472,449	517,162
Profitability/valuation	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
EBIT margin %	25.8	24.0	25.9	25.0	24.7	24.0	23.4	22.7
ROIC (EBIT) %	82.6	82.4	84.7	82.4	80.5	74.8	70.3	66.1
EV/EBITDA (core) x	10.4	11.1	12.4	12.7	11.2	10.7	10.0	9.5
P/E (UBS, diluted) x	15.1	16.5	17.4	18.5	16.9	15.9	15.3	14.7
Equity FCF (UBS) yield %	4.4	5.3	4.8	4.3	4.9	5.3	5.5	5.8
Net dividend yield %	1.7	2.1	2.4	2.7	3.0	3.2	3.3	3.4

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of Rs1,095.45 on 17 Feb 2016 20:26 HKT

Investment Thesis

Infosys Ltd

Investment case

While Infosys reported better-than-expected revenue growth for 9M FY16, we remain concerned about its medium-term outlook, due to several concerns: 1) Infosys is not as dominant as TCS in its key industry segments, which could impact medium-term revenue growth; 2) separation of Infosys' delivery business from its industry-facing units could hamper development of its digital solutions; and 3) any gains from an aggressive pricing strategy are likely to be short-lived.

Upside scenario

In our upside scenario, we assume revenue growth of 11% YoY in constant-currency terms, as a pick-up in global GDP growth drives better demand for IT services, eases the pricing pressure on the legacy business and increases market-share gains for Infosys. We also assume the rupee continues to weaken to 69 as the US dollar strengthens against emerging market currencies. We expect EBIT margin to improve to 26% in FY16. The market values Infosys on PE, in line with global trends. We expect Infosys to trade 19x PE, close to one standard deviation above its five-year average. We derive a valuation of Rs1,313.00 per share.

Downside scenario

In this scenario, we assume global GDP slows more than anticipated, exerting pressure on demand for IT services; Infosys' price aggression to win contracts starts to impact profitability; and the rupee strengthens to 65 in a relatively stable Indian economy. Revenue growth in this scenario slows to 6.5% YoY in FY16, and the EBIT margin falls to 23.5%. We expect Infosys to correct to 13x PE, around one standard deviation below its five-year average, implying fair value of Rs788.00 per share.

Upcoming catalysts

Infosys is due to report its next quarterly earnings in April 2016. The company needs to provide FY17 constant-currency revenue growth guidance of 10-12% YoY to meet consensus expectations.

12-month rating

Sell

12m price target

Rs1,070.00

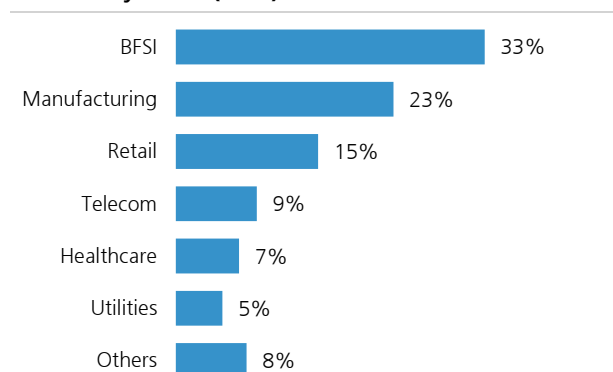
Business description

Infosys is the second-largest IT-services company listed in India, with US\$8.7bn in revenue and about 176,000 employees in FY15. It provides application development and maintenance, consulting and package implementation, business process management, infrastructure management, and testing services. It provides these services to international clients from offshore development facilities in India and other global centres. Infosys derived 61% of its FY15 revenue from North America, 24% from Europe, and the rest from other global markets.

Industry outlook

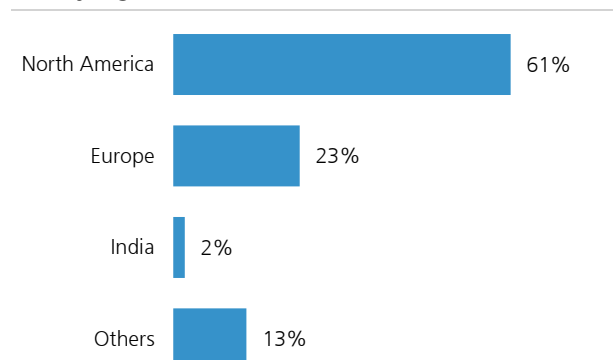
We believe the Indian IT services sector is facing a structural disruption, with large IT users beginning to adopt new outsourcing models for incremental cost efficiencies. Despite stable demand and growth in the global IT outsourcing market, many large Indian offshore vendors missed consensus revenue expectations in FY15, with soft revenue growth across key markets and service lines. Price competition has intensified in the past 12 months, indicating increased pressure on revenue from the legacy business, which contributes 85-90% of the industry's revenue.

Revenue by sector (FY15)



Source: Company data

EBIT by region (FY15)



Source: Company data

Infosys Ltd (INFY.BO)

	03/13	03/14	03/15	03/16E	% ch	03/17E	% ch	03/18E	03/19E	03/20E
Income statement (Rsm)										
Revenues	403,520	501,330	533,190	624,958	17.2	703,174	12.5	751,172	802,048	853,711
Gross profit	150,720	179,920	204,360	232,467	13.8	254,951	9.7	261,493	271,802	282,324
EBITDA (UBS)	115,580	134,150	149,010	170,242	14.2	189,699	11.4	196,141	205,232	212,320
Depreciation & amortisation	(11,290)	(13,740)	(10,690)	(14,253)	33.3	(16,317)	14.5	(15,775)	(17,645)	(18,782)
EBIT (UBS)	104,290	120,410	138,320	155,989	12.8	173,382	11.2	180,366	187,587	193,538
Associates & investment income	0	0	0	0	-	0	-	0	0	0
Other non-operating income	5,670	5,130	7,960	5,462	-31.4	8,802	61.1	13,080	10,639	10,802
Net interest	17,920	21,560	26,310	25,617	-2.6	26,479	3.4	29,120	32,025	35,219
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Profit before tax	127,880	147,100	172,590	187,068	8.4	208,664	11.5	222,567	230,250	239,559
Tax	(33,670)	(40,620)	(49,290)	(52,067)	-5.6	(60,512)	-16.2	(64,544)	(66,773)	(69,472)
Profit after tax	94,210	106,480	123,300	135,000	9.5	148,151	9.7	158,022	163,478	170,087
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	0	0	0	0	-	0	-	0	0	0
Extraordinary items	0	0	0	0	-	0	-	0	0	0
Net earnings (local GAAP)	94,210	106,480	123,300	135,000	9.5	148,151	9.7	158,022	163,478	170,087
Net earnings (UBS)	94,210	106,480	123,300	135,000	9.5	148,151	9.7	158,022	163,478	170,087
Tax rate (%)	26.3	27.6	28.6	27.8	-2.5	29.0	4.2	29.0	29.0	29.0
Per share (Rs)										
EPS (UBS, diluted)	41.22	46.59	53.95	59.06	9.5	64.79	9.7	69.09	71.45	74.32
EPS (local GAAP, diluted)	41.22	46.59	53.95	59.06	9.5	64.79	9.7	69.09	71.45	74.32
EPS (UBS, basic)	41.22	46.59	53.95	59.06	9.5	64.79	9.7	69.09	71.45	74.32
Net DPS (Rs)	10.50	15.75	22.25	29.53	32.7	32.39	9.7	34.54	35.72	37.16
Cash EPS (UBS, diluted) ¹	46.16	52.60	58.62	65.29	11.4	71.93	10.2	75.98	79.16	82.52
Book value per share	166.82	198.05	218.94	243.83	11.4	270.65	11.0	299.24	328.80	359.54
Average shares (diluted)	2,285.61	2,285.61	2,285.61	2,285.96	0.0	2,286.64	0.0	2,287.33	2,288.02	2,288.70
Balance sheet (Rsm)										
Cash and equivalents	240,660	302,580	325,860	354,475	8.8	390,835	10.3	430,543	472,449	517,162
Other current assets	116,410	140,130	159,550	185,317	16.1	209,470	13.0	230,368	252,959	275,076
Total current assets	357,070	442,710	485,410	539,793	11.2	600,305	11.2	660,911	725,408	792,238
Net tangible fixed assets	64,680	78,870	91,250	104,997	15.1	116,680	11.1	130,905	143,260	156,479
Net intangible fixed assets	23,440	24,990	37,290	37,290	0.0	37,290	0.0	37,290	37,290	37,290
Investments / other assets	2,370	2,200	3,310	3,310	0.0	3,310	0.0	3,310	3,310	3,310
Total assets	447,560	548,770	617,260	685,390	11.0	757,585	10.5	832,416	909,268	989,317
Trade payables & other ST liabilities	62,860	91,380	113,830	125,934	10.6	136,647	8.5	145,899	154,908	164,371
Short term debt	0	0	0	0	-	0	-	0	0	0
Total current liabilities	62,860	91,380	113,830	125,934	10.6	136,647	8.5	145,899	154,908	164,371
Long term debt	0	0	0	0	-	0	-	0	0	0
Other long term liabilities	2,680	3,870	2,060	2,060	0.0	2,060	0.0	2,060	2,060	2,060
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	65,540	95,250	115,890	127,994	10.4	138,707	8.4	147,959	156,968	166,431
Common s/h equity	382,020	453,520	501,370	557,395	11.2	618,878	11.0	684,457	752,300	822,886
Minority interests	0	0	0	0	-	0	-	0	0	0
Total liabilities & equity	447,560	548,770	617,260	685,390	11.0	757,585	10.5	832,416	909,268	989,317
Cash flow (Rsm)										
Net income (before pref divs)	94,210	106,480	123,300	135,000	9.5	148,151	9.7	158,022	163,478	170,087
Depreciation & amortisation	11,290	13,740	10,690	14,253	33.3	16,317	14.5	15,775	17,645	18,782
Net change in working capital	(9,760)	390	(11,310)	(13,663)	-20.8	(13,440)	1.6	(11,646)	(13,582)	(12,654)
Other operating	(960)	(580)	3,070	0	-	0	-	0	0	0
Operating cash flow	94,780	120,030	125,750	135,590	7.8	151,028	11.4	162,151	167,540	176,214
Tangible capital expenditure	(19,280)	(27,450)	(22,470)	(28,000)	-24.6	(28,000)	0.0	(30,000)	(30,000)	(32,000)
Intangible capital expenditure	(13,190)	0	0	0	-	0	-	0	0	0
Net (acquisitions) / disposals	0	0	0	0	-	0	-	0	0	0
Other investing	(18,040)	(22,580)	9,680	0	-	0	-	0	0	0
Investing cash flow	(50,510)	(50,030)	(12,790)	(28,000)	-118.9	(28,000)	0.0	(30,000)	(30,000)	(32,000)
Equity dividends paid	(31,230)	(31,430)	(49,350)	(78,975)	-60.0	(86,668)	-9.7	(92,443)	(95,634)	(99,501)
Share issues / (buybacks)	(880)	0	0	0	-	0	-	0	0	0
Other financing	0	0	0	0	-	0	-	0	0	0
Change in debt & pref shares	0	0	0	0	-	0	-	0	0	0
Financing cash flow	(32,110)	(31,430)	(49,350)	(78,975)	-60.0	(86,668)	-9.7	(92,443)	(95,634)	(99,501)
Cash flow inc/(dec) in cash	12,160	38,570	63,610	28,615	-55.0	36,359	27.1	39,708	41,906	44,713
FX / non cash items	18,700	23,350	(40,330)	0	-	0	-100.0	0	0	0
Balance sheet inc/(dec) in cash	30,860	61,920	23,280	28,615	22.9	36,359	27.1	39,708	41,906	44,713

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.¹Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

Infosys Ltd (INFY.BO)

Valuation (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
P/E (local GAAP, diluted)	15.1	16.5	17.4	18.5	16.9	15.9	15.3	14.7
P/E (UBS, diluted)	15.1	16.5	17.4	18.5	16.9	15.9	15.3	14.7
P/CEPS	13.5	14.6	16.1	16.8	15.2	14.4	13.8	13.3
Equity FCF (UBS) yield %	4.4	5.3	4.8	4.3	4.9	5.3	5.5	5.8
Net dividend yield (%)	1.7	2.1	2.4	2.7	3.0	3.2	3.3	3.4
P/BV x	3.7	3.9	4.3	4.5	4.0	3.7	3.3	3.0
EV/revenues (core)	3.0	3.0	3.5	3.5	3.0	2.8	2.6	2.4
EV/EBITDA (core)	10.4	11.1	12.4	12.7	11.2	10.7	10.0	9.5
EV/EBIT (core)	11.5	12.3	13.3	13.9	12.3	11.6	10.9	10.4
EV/OpFCF (core)	12.7	12.3	14.4	15.1	13.3	12.4	11.7	11.1
EV/op. invested capital	9.5	NM	NM	NM	9.9	8.7	7.7	6.9
Enterprise value (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Market cap.	1,429,541	1,757,153	2,154,998	2,503,772	2,503,772	2,503,772	2,503,772	2,503,772
Net debt (cash)	(225,230)	(271,620)	(314,220)	(340,168)	(372,655)	(410,689)	(451,496)	(494,805)
Buy out of minorities	0	0	0	0	0	0	0	0
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	1,204,311	1,485,533	1,840,778	2,163,604	2,131,116	2,093,083	2,052,276	2,008,966
Non core assets	0	0	0	0	0	0	0	0
Core enterprise value	1,204,311	1,485,533	1,840,778	2,163,604	2,131,116	2,093,083	2,052,276	2,008,966
Growth (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenue	19.6	24.2	6.4	17.2	12.5	6.8	6.8	6.4
EBITDA (UBS)	7.9	16.1	11.1	14.2	11.4	3.4	4.6	3.5
EBIT (UBS)	6.6	15.5	14.9	12.8	11.2	4.0	4.0	3.2
EPS (UBS, diluted)	13.3	13.0	15.8	9.5	9.7	6.6	3.4	4.0
Net DPS	-10.6	50.0	41.3	32.7	9.7	6.6	3.4	4.0
Margins & Profitability (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Gross profit margin	37.4	35.9	38.3	37.2	36.3	34.8	33.9	33.1
EBITDA margin	28.6	26.8	27.9	27.2	27.0	26.1	25.6	24.9
EBIT margin	25.8	24.0	25.9	25.0	24.7	24.0	23.4	22.7
Net earnings (UBS) margin	23.3	21.2	23.1	21.6	21.1	21.0	20.4	19.9
ROIC (EBIT)	82.6	82.4	84.7	82.4	80.5	74.8	70.3	66.1
ROIC post tax	60.8	59.6	60.5	59.5	57.1	53.1	49.9	46.9
ROE (UBS)	26.8	25.5	25.8	25.5	25.2	24.2	22.8	21.6
Capital structure & Coverage (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Net debt / EBITDA	(2.1)	(2.3)	(2.2)	(2.1)	(2.1)	(2.2)	(2.3)	(2.4)
Net debt / total equity %	(63.0)	(66.7)	(65.0)	(63.6)	(63.2)	(62.9)	(62.8)	(62.8)
Net debt / (net debt + total equity) %	NM	NM	NM	NM	NM	NM	NM	NM
Net debt/EV %	(20.0)	(20.4)	(17.7)	(16.4)	(18.3)	(20.6)	(23.0)	(25.7)
Capex / depreciation %	170.8	199.8	NM	196.4	171.6	190.2	170.0	170.4
Capex / revenue %	4.8	5.5	4.2	4.5	4.0	4.0	3.7	3.7
EBIT / net interest	NM	NM	NM	NM	NM	NM	NM	NM
Dividend cover (UBS)	3.9	3.0	2.4	2.0	2.0	2.0	2.0	2.0
Div. payout ratio (UBS) %	25.5	33.8	41.2	50.0	50.0	50.0	50.0	50.0
Revenues by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	403,520	501,330	533,190	624,958	703,174	751,172	802,048	853,711
Total	403,520	501,330	533,190	624,958	703,174	751,172	802,048	853,711
EBIT (UBS) by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	104,290	120,410	138,320	155,989	173,382	180,366	187,587	193,538
Total	104,290	120,410	138,320	155,989	173,382	180,366	187,587	193,538

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Wipro Ltd.

Revenue improvement is likely to take time; no upside catalyst

Lack of leadership in key segments to delay revenue revival

Revenue data shows Wipro lags its Indian peers in nearly all large industry segments (banking, manufacturing, healthcare, retail), which we view as a key obstacle to a quick turnaround in revenue growth. The company fared well in digital vendor preferences in our Evidence Lab survey, but stagnant revenue growth suggests that order win rates are yet to meaningfully improve. According to the new management, Wipro is trying to address this, through a combination of M&A and organisational changes, but we believe a revenue pick-up could take longer than expected.

Weakness in seasonally strong quarters is not an encouraging sign

H2 has historically been stronger for Wipro than its peers, but organic revenue momentum in H2 FY15 was unusually tepid, and we expect the weakness to linger in FY16. This was partly due to weakness in segments like energy & utilities, where the company made significant investments. We expect FY17 revenue growth to remain sluggish, with limited improvement in organic revenue visibility in the medium term.

Valuations appear attractive, but upside catalysts remain elusive

Wipro has been trading at a near 20% discount to TCS, and valuations at close to 13x FY18E PE appear inexpensive relative to its peers. However, with consistently low visibility of revenue improvement, we see no upside catalysts in the medium term.

Valuation: maintain Sell rating

Our price target of Rs520 is based on 12.5x FY18E PE.

Equities

India
Diversified Technology Services

12-month rating **Sell**

12m price target **Rs520.00**

Price **Rs525.00**

RIC: WIPR.BO BBG: WPRO IB

Trading data and key metrics

52-wk range Rs671.95-516.10

Market cap. Rs1,285bn/US\$18.8bn

Shares o/s 2,449m (ORD)

Free float 25%

Avg. daily volume ('000) 1,235

Avg. daily value (m) Rs686.5

Common s/h equity (03/16E) Rs458bn

P/BV (03/16E) 2.8x

Net debt / EBITDA (03/16E) NM

EPS (UBS, diluted) (Rs)

	UBS	Cons.
03/16E	36.58	36.71
03/17E	39.23	40.13
03/18E	41.39	43.85

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Analyst

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Highlights (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenues	430,980	437,628	473,182	514,675	551,437	579,179	608,049	635,384
EBIT (UBS)	72,519	89,352	95,423	97,495	103,193	107,924	111,469	115,130
Net earnings (UBS)	66,359	77,966	86,528	90,073	96,922	102,678	107,764	113,231
EPS (UBS, diluted) (Rs)	26.98	31.66	35.14	36.58	39.23	41.39	43.27	45.28
DPS (Rs)	7.02	8.03	12.06	13.50	14.50	15.50	16.30	17.50
Net (debt) / cash	90,193	123,166	133,935	161,719	203,854	245,097	286,960	330,332
Profitability/valuation	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
EBIT margin %	16.8	20.4	20.2	18.9	18.7	18.6	18.3	18.1
ROIC (EBIT) %	34.8	42.9	38.4	34.0	33.8	33.6	32.7	31.8
EV/EBITDA (core) x	10.6	10.2	11.7	10.2	9.4	8.7	8.1	7.5
P/E (UBS, diluted) x	14.4	14.6	16.2	14.4	13.4	12.7	12.1	11.6
Equity FCF (UBS) yield %	6.0	5.0	4.0	4.4	4.8	4.7	4.7	4.9
Net dividend yield %	1.8	1.7	2.1	2.6	2.8	3.0	3.1	3.3

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of Rs525.00 on 17 Feb 2016 20:26 HKT

Investment Thesis

Wipro Ltd.

Investment case

Wipro lags its Indian peers in all large industry segments in terms of revenue and market share gains. We view this as the key impediment to a faster-than-expected improvement in revenue growth for the company. In the absence of revenue acceleration at its top clients, and slowing order flows, we expect organic revenue growth to remain tepid in the medium term.

Upside scenario

In our upside scenario, we assume revenue growth of 7.5% YoY in reported dollar terms, as a pick-up in global GDP growth drives better demand for IT services, which in turn should ease the pricing pressure on the legacy business; energy prices recover; IT spending pressure eases for Wipro's energy clients; the rupee continues to weaken to 69 as the US dollar strengthens against emerging market currencies. We expect EBIT margin to improve to 21% in FY16. The market values Wipro on PE, in line with global trends. We expect Wipro to trade at 16x PE, below +1 standard deviation from its five-year average, as revenue growth is likely to remain below the industry average. We derive a valuation of Rs660.00.

Downside scenario

In this scenario, we assume global GDP slows more than anticipated, exerting pressure on demand for IT services. We also assume the rupee strengthens to 65 in a relatively stable Indian economy. Revenue growth in this scenario slows to 3% YoY in FY16E, with the EBIT margin falling to 19.0%. We expect Wipro to correct to 11x PE, one standard deviation below its five-year average as earnings growth would be negative in this scenario. We derive a valuation of Rs415.00.

Upcoming catalysts

Wipro will report earnings in April 2016. Better-than-expected Q1 FY17 revenue guidance could be a positive catalyst.

12-month rating

Sell

12m price target

Rs520.00

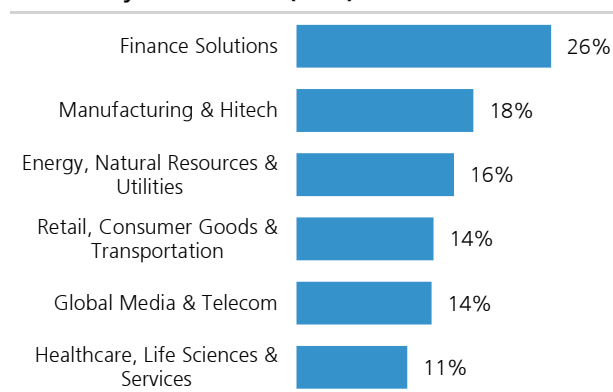
Business description

Wipro is the third-largest listed IT services company in India, with IT services revenue of US\$7.1bn and 158,217 employees in FY15. Its main businesses are financial services (26% of FY15 revenue), manufacturing (18%), and telecom and media (14%). Wipro has diversified service offerings in applications development and maintenance, testing and package implementation, infrastructure services, and business process outsourcing. It derived 51% of its FY15 revenue from the US, 28% from Europe, and the remainder from India and other emerging markets.

Industry outlook

We believe the Indian IT services sector is facing a structural disruption, with large IT users beginning to adopt new outsourcing models for incremental cost efficiencies. Despite stable demand and growth in the global IT outsourcing market, many large Indian offshore vendors missed consensus revenue expectations in FY15, with soft revenue growth across key markets and service lines. Price competition has intensified in the past 12 months, indicating increased pressure on revenue from the legacy business, which contributes 85-90% of the industry's revenue.

Revenue by business unit (FY15)



Source: Company data

EBIT by product segment (Rs m)

	FY12	FY13	FY14	FY15
IT services	59,266	69,933	90,333	97,649
IT products	1,787	990	310	374

Source: Company data

Wipro Ltd. (WIPR.BO)

	03/13	03/14	03/15	03/16E	% ch	03/17E	% ch	03/18E	03/19E	03/20E
Income statement (Rsm)										
Revenues	430,980	437,628	473,182	514,675	8.8	551,437	7.1	579,179	608,049	635,384
Gross profit	133,256	142,139	151,899	159,727	5.2	167,234	4.7	172,785	177,342	183,317
EBITDA (UBS)	83,354	100,458	108,246	112,102	3.6	117,530	4.8	122,404	126,671	131,015
Depreciation & amortisation	(10,835)	(11,106)	(12,823)	(14,607)	13.9	(14,337)	-1.8	(14,479)	(15,201)	(15,885)
EBIT (UBS)	72,519	89,352	95,423	97,495	2.2	103,193	5.8	107,924	111,469	115,130
Associates & investment income	(105)	0	0	0	-	0	-	0	0	0
Other non-operating income	2,626	0	0	0	-	0	-	0	0	0
Net interest	10,005	11,653	16,260	18,217	12.0	21,198	16.4	23,845	26,823	30,173
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Profit before tax	85,045	101,005	111,683	115,712	3.6	124,391	7.5	131,770	138,293	145,303
Tax	(18,349)	(22,601)	(24,624)	(25,250)	-2.5	(27,101)	-7.3	(28,708)	(30,129)	(31,657)
Profit after tax	66,696	78,404	87,059	90,462	3.9	97,290	7.5	103,061	108,163	113,646
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	(337)	(438)	(531)	(389)	26.8	(369)	5.2	(384)	(399)	(415)
Extraordinary items	0	0	0	0	-	0	-	0	0	0
Net earnings (local GAAP)	66,359	77,966	86,528	90,073	4.1	96,922	7.6	102,678	107,764	113,231
Net earnings (UBS)	66,359	77,966	86,528	90,073	4.1	96,922	7.6	102,678	107,764	113,231
Tax rate (%)	21.6	22.4	22.0	21.8	-1.0	21.8	-0.2	21.8	21.8	21.8
Per share (Rs)										
EPS (UBS, diluted)	26.98	31.66	35.14	36.58	4.1	39.23	7.2	41.39	43.27	45.28
EPS (local GAAP, diluted)	26.98	31.66	35.14	36.58	4.1	39.23	7.2	41.39	43.27	45.28
EPS (UBS, basic)	27.05	31.76	35.25	36.58	3.8	39.23	7.2	41.39	43.27	45.28
Net DPS (Rs)	7.02	8.03	12.06	13.50	11.9	14.50	7.4	15.50	16.30	17.50
Cash EPS (UBS, diluted) ¹	31.39	36.17	40.34	42.51	5.4	45.03	5.9	47.23	49.37	51.63
Book value per share	115.91	140.29	166.62	185.98	11.6	208.28	12.0	231.50	255.56	280.14
Average shares (diluted)	2,459.18	2,462.63	2,462.58	2,462.25	0.0	2,470.85	0.3	2,480.75	2,490.69	2,500.66
Balance sheet (Rsm)										
Cash and equivalents	154,009	174,758	212,848	239,997	12.8	281,528	17.3	322,198	363,516	406,371
Other current assets	153,394	179,928	223,644	242,263	8.3	262,623	8.4	322,124	305,647	327,881
Total current assets	307,403	354,686	436,492	482,260	10.5	544,151	12.8	605,321	669,163	734,251
Net tangible fixed assets	50,525	51,449	54,206	57,099	5.3	59,761	4.7	63,282	67,081	70,696
Net intangible fixed assets	56,470	65,358	76,009	83,292	9.6	83,292	0.0	83,292	83,292	83,292
Investments / other assets	25,332	30,811	33,326	33,326	0.0	33,326	0.0	33,326	33,326	33,326
Total assets	439,730	502,304	600,033	655,977	9.3	720,531	9.8	785,221	852,862	921,565
Trade payables & other ST liabilities	81,778	95,773	97,823	104,462	6.8	112,907	8.1	118,516	124,464	129,673
Short term debt	62,962	40,683	66,206	66,206	0.0	66,206	0.0	66,206	66,206	66,206
Total current liabilities	144,740	136,456	164,029	170,668	4.0	179,113	4.9	184,722	190,670	195,879
Long term debt	854	10,909	12,707	12,072	-5.0	11,468	-5.0	10,895	10,350	9,832
Other long term liabilities	9,153	10,053	13,669	13,669	0.0	13,669	0.0	13,669	13,669	13,669
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	154,747	157,418	190,405	196,408	3.2	204,250	4.0	209,286	214,689	219,381
Common s/h equity	283,812	343,499	407,982	457,922	12.2	514,634	12.4	574,289	636,527	700,538
Minority interests	1,171	1,387	1,646	1,646	0.0	1,646	0.0	1,646	1,646	1,646
Total liabilities & equity	439,730	502,304	600,033	655,977	9.3	720,531	9.8	785,221	852,862	921,565
Cash flow (Rsm)										
Net income (before pref divs)	66,359	77,966	86,528	90,073	4.1	96,922	7.6	102,678	107,764	113,231
Depreciation & amortisation	10,835	11,106	12,823	14,607	13.9	14,337	-1.8	14,479	15,201	15,885
Net change in working capital	2,822	(10,282)	(7,978)	(11,980)	-50.2	(11,914)	0.6	(14,892)	(16,575)	(17,024)
Other operating	(9,594)	(10,895)	(13,111)	(18,217)	-38.9	(21,198)	-16.4	(23,845)	(26,823)	(30,173)
Operating cash flow	70,422	67,895	78,262	74,483	-4.8	78,147	4.9	78,420	79,567	81,918
Tangible capital expenditure	(10,145)	(7,822)	(11,272)	(17,500)	-55.3	(17,000)	2.9	(18,000)	(19,000)	(19,500)
Intangible capital expenditure	(3,074)	(2,985)	(11,574)	0	-	0	-	0	0	0
Net (acquisitions) / disposals	0	0	0	0	-	0	-	0	0	0
Other investing	(40,191)	8,033	(2,970)	10,934	-	21,198	-	23,845	26,823	30,173
Investing cash flow	(53,410)	(2,774)	(25,816)	(6,566)	74.6	4,198	-	5,845	7,823	10,673
Equity dividends paid	(17,080)	(23,273)	(29,490)	(38,891)	-31.9	(41,918)	-7.8	(44,988)	(47,500)	(51,201)
Share issues / (buybacks)	9	6	5	(1,241)	-	1,708	-	1,966	1,974	1,982
Other financing	(1,044)	(937)	81	0	-	0	-	0	0	0
Change in debt & pref shares	11,394	(10,768)	21,108	(635)	-	(604)	5.00	(573)	(545)	(517)
Financing cash flow	(6,721)	(34,972)	(8,296)	(40,768)	-391.4	(40,813)	-0.1	(43,596)	(46,071)	(49,737)
Cash flow inc/(dec) in cash	10,291	30,149	44,150	27,149	-38.5	41,532	53.0	40,669	41,319	42,854
FX / non cash items	24,091	(9,400)	(6,060)	0	-	0	37.5	0	0	0
Balance sheet inc/(dec) in cash	34,382	20,749	38,090	27,149	-28.7	41,532	53.0	40,669	41,319	42,854

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.¹Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

Wipro Ltd. (WIPR.BO)

Valuation (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
P/E (local GAAP, diluted)	14.4	14.6	16.2	14.4	13.4	12.7	12.1	11.6
P/E (UBS, diluted)	14.4	14.6	16.2	14.4	13.4	12.7	12.1	11.6
P/CEPS	12.4	12.8	14.1	12.3	11.7	11.1	10.6	10.2
Equity FCF (UBS) yield %	6.0	5.0	4.0	4.4	4.8	4.7	4.7	4.9
Net dividend yield (%)	1.8	1.7	2.1	2.6	2.8	3.0	3.1	3.3
P/BV x	3.4	3.3	3.4	2.8	2.5	2.3	2.1	1.9
EV/revenues (core)	2.0	2.3	2.7	2.2	2.0	1.8	1.7	1.5
EV/EBITDA (core)	10.6	10.2	11.7	10.2	9.4	8.7	8.1	7.5
EV/EBIT (core)	12.1	11.5	13.3	11.7	10.7	9.8	9.2	8.5
EV/OpFCF (core)	12.1	11.5	13.3	11.7	10.7	9.8	9.2	8.5
EV/op. invested capital	4.2	4.9	5.1	4.0	3.6	3.3	3.0	2.7
Enterprise value (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Market cap.	954,342	1,133,280	1,392,889	1,285,494	1,285,494	1,285,494	1,285,494	1,285,494
Net debt (cash)	(75,431)	(106,679)	(128,550)	(147,827)	(182,787)	(224,476)	(266,029)	(308,646)
Buy out of minorities	1,171	1,387	1,646	1,646	1,646	1,646	1,646	1,646
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	880,082	1,027,988	1,265,984	1,139,313	1,104,353	1,062,664	1,021,111	978,494
Non core assets	0	0	0	0	0	0	0	0
Core enterprise value	880,082	1,027,988	1,265,984	1,139,313	1,104,353	1,062,664	1,021,111	978,494
Growth (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenue	15.9	1.5	8.1	8.8	7.1	5.0	5.0	4.5
EBITDA (UBS)	17.6	20.5	7.8	3.6	4.8	4.1	3.5	3.4
EBIT (UBS)	19.4	23.2	6.8	2.2	5.8	4.6	3.3	3.3
EPS (UBS, diluted)	18.9	17.3	11.0	4.1	7.2	5.5	4.5	4.7
Net DPS	16.7	14.3	50.3	11.9	7.4	6.9	5.2	7.4
Margins & Profitability (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Gross profit margin	30.9	32.5	32.1	31.0	30.3	29.8	29.2	28.9
EBITDA margin	19.3	23.0	22.9	21.8	21.3	21.1	20.8	20.6
EBIT margin	16.8	20.4	20.2	18.9	18.7	18.6	18.3	18.1
Net earnings (UBS) margin	15.4	17.8	18.3	17.5	17.6	17.7	17.7	17.8
ROIC (EBIT)	34.8	42.9	38.4	34.0	33.8	33.6	32.7	31.8
ROIC post tax	27.3	33.3	29.9	26.6	26.5	26.2	25.6	24.9
ROE (UBS)	23.3	24.9	23.0	20.8	19.9	18.9	17.8	16.9
Capital structure & Coverage (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Net debt / EBITDA	(1.1)	(1.2)	(1.2)	(1.4)	(1.7)	(2.0)	(2.3)	(2.5)
Net debt / total equity %	(31.6)	(35.7)	(32.7)	(35.2)	(39.5)	(42.6)	(45.0)	(47.0)
Net debt / (net debt + total equity) %	(46.3)	(55.6)	(48.6)	(54.3)	(65.2)	(74.1)	(81.7)	(88.8)
Net debt/EV %	(10.2)	(12.0)	(10.6)	(14.2)	(18.5)	(23.1)	(28.1)	(33.8)
Capex / depreciation %	93.6	70.4	87.9	119.8	118.6	124.3	125.0	122.8
Capex / revenue %	2.4	1.8	2.4	3.4	3.1	3.1	3.1	3.1
EBIT / net interest	NM	NM	NM	NM	NM	NM	NM	NM
Dividend cover (UBS)	3.9	4.0	2.9	2.7	2.7	2.7	2.7	2.6
Div. payout ratio (UBS) %	25.9	25.3	34.2	36.9	37.0	37.4	37.7	38.6
Revenues by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	430,980	437,628	473,182	514,675	551,437	579,179	608,049	635,384
Total	430,980	437,628	473,182	514,675	551,437	579,179	608,049	635,384
EBIT (UBS) by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	72,519	89,352	95,423	97,495	103,193	107,924	111,469	115,130
Total	72,519	89,352	95,423	97,495	103,193	107,924	111,469	115,130

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

HCL Technologies

Improved near-term visibility, but longer-term concerns remain

Large exposure to infrastructure services could turn into a risk

HCL Tech's infrastructure services business (35% of revenue) has been the key revenue and valuation driver in the past few years. However, we believe this could reverse as the segment likely faces a greater risk of disruption by digital technologies and new outsourcing models. While we expect HCL Tech to move aggressively to digital services in the next few years, the company runs a disproportionate risk of revenue cannibalisation, due to its large exposure to infrastructure services.

Engineering services segment could help buffer some negatives

We expect HCL Tech's announced acquisition of Volvo's IT unit to boost its engineering services capabilities and add about 3.5% to revenue growth in FY17, though the deal is likely to be margin-dilutive. While we expect improved growth for the engineering services segment in the medium term, it is unlikely to completely offset the slowdown in infrastructure services, as long sales cycles make revenue growth less predictable in the former segment.

Improving near-term outlook likely to cap valuation downside

We believe a stronger revenue growth outlook for FY17 could support higher investor confidence in HCL than its peers, where revenue visibility remains low. We also expect organic margin improvement in the next 12 months, driven by higher revenue growth. This should keep medium-term revenue growth concerns from depressing HCL's valuations in the near term.

Valuation: maintain Neutral rating

We adjust our earnings estimates to reflect the change in HCL's fiscal year-end from 30 June to 31 March, effective FY16 (ending 31 March 2016). We also incorporate the potential financial impact of the Volvo IT acquisition. This impacts our FY16/FY17/FY18 earnings estimates by -23%/+4%/+7%. Despite the correction in its PE in the past 12 months, HCL Tech continues to trade at a 9% premium to its five-year average one-year forward PE and we see limited upside at the current levels. Our price target of Rs950.00 is based on 14.4x FY18E PE.

Equities

India
Diversified Technology Services

12-month rating **Neutral**

12m price target **Rs950.00**

Price **Rs824.60**

RIC: HCLT.BO BBG: HCLT IB

Trading data and key metrics

52-wk range Rs1,033.68-798.30

Market cap. Rs1,159bn/US\$17.0bn

Shares o/s 1,406m (ORD)

Free float 40%

Avg. daily volume ('000) 1,297

Avg. daily value (m) Rs1,095.9

Common s/h equity (03/16E) Rs278bn

P/BV (03/16E) 4.2x

Net debt / EBITDA (03/16E) NM

EPS (UBS, diluted) (Rs)

	From	To	% ch	Cons.
03/16E	-	40.06	-	-
03/17E	-	59.13	-	-
03/18E	-	65.78	-	-

Diviya Nagarajan

Analyst

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Highlights (Rsm)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenues	257,694	329,180	370,620	312,347	473,447	513,435	552,482	595,424
EBIT (UBS)	51,472	79,360	82,520	63,072	91,030	101,095	108,061	114,724
Net earnings (UBS)	40,813	63,720	72,562	56,683	84,135	93,971	101,983	111,035
EPS (UBS, diluted) (Rs)	28.91	45.08	51.40	40.06	59.13	65.78	71.05	76.90
DPS (Rs)	7.88	10.88	15.92	16.00	16.00	16.00	16.00	16.00
Net (debt) / cash	43,352	92,489	113,200	136,525	176,197	259,798	317,105	418,247
Profitability/valuation	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
EBIT margin %	20.0	24.1	22.3	20.2	19.2	19.7	19.6	19.3
ROIC (EBIT) %	52.1	76.4	68.1	45.8	60.7	67.1	71.3	75.5
EV/EBITDA (core) x	7.3	9.0	12.7	15.3	10.3	8.7	7.5	6.4
P/E (UBS, diluted) x	11.3	13.5	16.8	20.6	13.9	12.5	11.6	10.7
Equity FCF (UBS) yield %	9.6	7.3	4.1	4.2	5.3	6.7	7.2	7.6
Net dividend yield %	2.4	1.8	1.8	1.9	1.9	1.9	1.9	1.9

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of Rs824.60 on 17 Feb 2016 20:26 HKT

Investment Thesis

HCL Technologies

Investment case

HCL Technologies' revenue momentum slowed in H1 FY16, but we expect its infrastructure services revenue to pick up in FY17. Organic EBIT margins should remain range-bound within the company's target range of 21-22% for the medium term, especially with the tailwind from a depreciating Indian rupee. This is likely to support better earnings momentum relative to the sector in the near term.

Upside scenario

In our upside scenario, we assume revenue growth of 51% YoY in reported dollar terms, as a pick-up in global GDP growth drives better demand for IT services, easing the pricing pressure on legacy services; infrastructure revenue growth improves, pushing up HCL's overall revenue growth; and the rupee weakens to 69, as the US dollar strengthens against emerging market currencies. We expect EBIT margin to improve to 21% in FY16. Market values HCL Tech on PE, in line with global trends. We expect HCL to trade 18x PE, close to one standard deviation above its five-year average. We derive a valuation of Rs1,180.00.

Downside scenario

In this scenario, we assume global GDP slows more than anticipated, exerting pressure on demand for IT services; and the rupee strengthens to 65 in a relatively stable Indian economy. Revenue growth in this scenario slows to 47% YoY in FY16E, and EBIT margin falls to 18.7%. We expect HCL Tech to correct to 12.5x PE, in line with our target multiple for Wipro. We derive a valuation of Rs705.00.

Upcoming catalysts

Management's demand outlook for FY17 at the earnings announcement in April 2016 could be a key share price catalyst.

12-month rating

Neutral

12m price target

Rs950.00

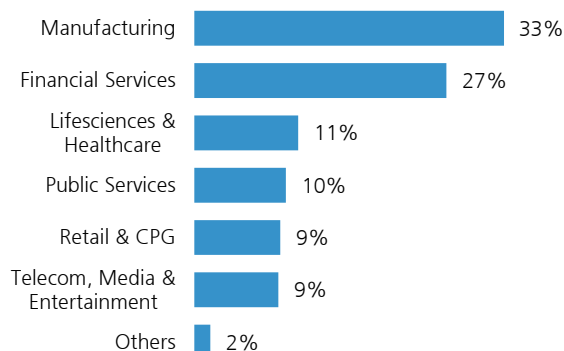
Business description

HCL Technologies is a leading Indian IT services company, with close to US\$6.0bn in revenue and around 106,100 employees in FY15. The company focuses on technology and R&D outsourcing, and provides technology development (development, redevelopment and maintenance of software), enterprise application, infrastructure, and business process outsourcing services.

Industry outlook

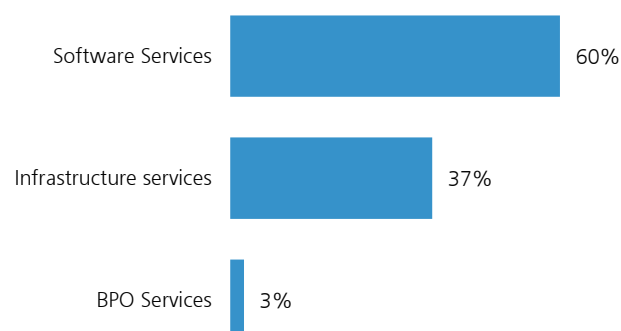
We believe the Indian IT services sector is facing a structural disruption, with large IT users beginning to adopt new outsourcing models for incremental cost efficiencies. Despite stable demand and growth in the global IT outsourcing market, many large Indian offshore vendors missed consensus revenue expectations in FY15, with soft revenue growth across key markets and service lines. Price competition has intensified in the past 12 months, indicating increased pressure on revenue from the legacy business, which contributes 85-90% of the industry's revenue.

Revenue by industry (FY15)



Source: Company data

EBIT by product segment (FY15)



Source: Company data

HCL Technologies (HCLT.BO)

	06/13	06/14	06/15	03/16E	% ch	03/17E	% ch	03/18E	03/19E	03/20E
Income statement (Rsm)										
Revenues	257,694	329,180	370,620	312,347	-15.7	473,447	51.6	513,435	552,482	595,424
Gross profit	92,586	127,030	132,650	107,159	-19.2	156,206	45.8	172,386	183,363	194,214
EBITDA (UBS)	58,220	86,680	87,020	67,558	-22.4	96,928	43.5	108,696	116,726	124,161
Depreciation & amortisation	(6,747)	(7,320)	(4,500)	(4,485)	-0.3	(5,898)	31.5	(7,600)	(8,665)	(9,437)
EBIT (UBS)	51,472	79,360	82,520	63,072	-23.6	91,030	44.3	101,095	108,061	114,724
Associates & investment income	0	0	0	0	-	0	-	0	0	0
Other non-operating income	(213)	(5,890)	(200)	(403)	-101.4	0	-	0	0	0
Net interest	1,772	5,730	9,320	9,175	-1.6	15,377	67.6	17,751	20,919	25,704
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Profit before tax	53,031	79,200	91,640	71,845	-21.6	106,407	48.1	118,847	128,980	140,428
Tax	(12,218)	(15,480)	(19,080)	(15,162)	20.5	(22,272)	-46.9	(24,876)	(26,997)	(29,393)
Profit after tax	40,813	63,720	72,560	56,683	-21.9	84,135	48.4	93,971	101,983	111,035
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	0	0	2	0	-	0	-	0	0	0
Extraordinary items	0	0	0	0	-	0	-	0	0	0
Net earnings (local GAAP)	40,813	63,720	72,562	56,683	-21.9	84,135	48.4	93,971	101,983	111,035
Net earnings (UBS)	40,813	63,720	72,562	56,683	-21.9	84,135	48.4	93,971	101,983	111,035
Tax rate (%)	23.0	19.5	20.8	21.1	1.4	20.9	-0.8	20.9	20.9	20.9
Per share (Rs)										
EPS (UBS, diluted)	28.91	45.08	51.40	40.06	-22.1	59.13	47.6	65.78	71.05	76.90
EPS (local GAAP, diluted)	28.91	45.08	51.40	40.06	-22.1	59.13	47.6	65.78	71.05	76.90
EPS (UBS, basic)	29.30	45.60	51.65	40.21	-22.2	59.32	47.5	65.86	71.05	76.90
Net DPS (Rs)	7.88	10.88	15.92	16.00	0.5	16.00	0.0	16.00	16.00	16.00
Cash EPS (UBS, diluted) ¹	33.69	50.25	54.59	43.23	-20.8	63.28	46.4	71.10	77.09	83.43
Book value per share	102.62	144.16	176.08	196.99	11.9	236.37	20.0	282.09	332.75	388.95
Average shares (diluted)	1,411.64	1,413.60	1,411.66	1,415.08	0.2	1,422.88	0.6	1,428.58	1,435.33	1,443.96
Balance sheet (Rsm)										
Cash and equivalents	50,312	99,998	117,890	140,042	18.8	178,659	27.6	261,521	318,311	419,092
Other current assets	80,838	98,331	118,240	134,942	14.1	155,677	15.4	170,812	187,545	204,620
Total current assets	131,150	198,329	236,130	274,984	16.5	334,336	21.6	432,333	505,856	623,711
Net tangible fixed assets	27,283	31,465	38,200	41,715	9.2	57,317	37.4	67,716	78,051	89,614
Net intangible fixed assets	49,582	51,492	52,040	57,457	10.4	57,457	0.0	57,457	57,457	57,457
Investments / other assets	22,464	23,618	30,740	32,545	5.9	43,366	33.3	28,674	48,833	34,686
Total assets	230,479	304,904	357,110	406,701	13.9	492,476	21.1	586,181	690,196	805,469
Trade payables & other ST liabilities	80,574	96,581	104,910	125,471	19.6	154,786	23.4	181,985	211,387	243,000
Short term debt	6,960	7,509	4,690	3,518	-25.00	2,462	-30.00	1,724	1,207	845
Total current liabilities	87,534	104,090	109,600	128,988	17.7	157,248	21.9	183,708	212,593	243,845
Long term debt	0	0	0	0	-	0	-	0	0	0
Other long term liabilities	0	0	0	0	-	0	-	0	0	0
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	87,534	104,090	109,600	128,988	17.7	157,248	21.9	183,708	212,593	243,845
Common s/h equity	142,945	200,814	247,510	277,712	12.2	335,228	20.7	402,472	477,603	561,624
Minority interests	0	0	0	0	-	0	-	0	0	0
Total liabilities & equity	230,479	304,904	357,110	406,701	13.9	492,476	21.1	586,181	690,196	805,469
Cash flow (Rsm)										
Net income (before pref divs)	40,813	63,720	72,562	56,683	-21.9	84,135	48.4	93,971	101,983	111,035
Depreciation & amortisation	6,748	7,320	4,500	4,485	-0.3	5,898	31.5	7,600	8,665	9,437
Net change in working capital	(2,085)	(1,928)	(10,903)	(11,505)	-5.5	(13,838)	-20.3	(12,919)	(14,454)	(15,017)
Other operating	4,067	(2,341)	(4,123)	6,566	-	7,043	7.3	7,228	6,150	3,740
Operating cash flow	49,543	66,770	62,036	56,228	-9.4	83,238	48.0	95,880	102,345	109,195
Tangible capital expenditure	(6,301)	(4,858)	(12,259)	(8,000)	34.7	(21,500)	-168.7	(18,000)	(19,000)	(21,000)
Intangible capital expenditure	0	0	0	0	-	0	-	0	0	0
Net (acquisitions) / disposals	0	0	0	0	-	0	-	0	0	0
Other investing	(20,424)	(46,837)	(14,100)	(19,500)	-	(33,165)	-	(32,787)	(44,901)	(55,937)
Investing cash flow	(26,725)	(51,695)	(26,359)	(27,500)	-4.3	(54,665)	-98.8	(50,787)	(63,901)	(76,937)
Equity dividends paid	(8,736)	(13,037)	(28,880)	(26,288)	9.0	(26,490)	-0.8	(26,636)	(26,743)	(26,869)
Share issues / (buybacks)	0	0	0	0	-	0	-	0	0	0
Other financing	(12,917)	774	(2,687)	(1,163)	56.74	(1,038)	10.69	(722)	(500)	(345)
Change in debt & pref shares	0	0	0	0	-	0	-	0	0	0
Financing cash flow	(21,654)	(12,264)	(31,568)	(27,450)	13.0	(27,529)	-0.3	(27,358)	(27,243)	(27,214)
Cash flow inc/(dec) in cash	1,164	2,812	4,110	1,278	-68.9	1,044	-18.3	17,735	11,201	5,044
FX / non cash items	21,152	46,874	13,782	20,874	51.5	37,573	80.0	65,127	45,589	95,737
Balance sheet inc/(dec) in cash	22,316	49,686	17,892	22,152	23.8	38,617	74.3	82,862	56,790	100,781

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.¹Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

HCL Technologies (HCLT.BO)

Valuation (x)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
P/E (local GAAP, diluted)	11.3	13.5	16.8	20.6	13.9	12.5	11.6	10.7
P/E (UBS, diluted)	11.3	13.5	16.8	20.6	13.9	12.5	11.6	10.7
P/CEPS	9.5	12.0	15.8	19.0	13.0	11.6	10.7	9.9
Equity FCF (UBS) yield %	9.6	7.3	4.1	4.2	5.3	6.7	7.2	7.6
Net dividend yield (%)	2.4	1.8	1.8	1.9	1.9	1.9	1.9	1.9
P/BV x	3.2	4.2	4.9	4.2	3.5	2.9	2.5	2.1
EV/revenues (core)	1.7	2.4	3.0	3.3	2.1	1.8	1.6	1.3
EV/EBITDA (core)	7.3	9.0	12.7	15.3	10.3	8.7	7.5	6.4
EV/EBIT (core)	8.3	9.8	13.4	16.4	11.0	9.3	8.1	6.9
EV/OpFCF (core)	8.6	10.1	15.5	20.1	13.0	10.7	9.3	7.9
EV/op. invested capital	4.3	7.5	9.1	7.5	6.7	6.2	5.7	5.2
Enterprise value (Rsm)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
Market cap.	452,056	849,755	1,211,377	1,159,137	1,159,137	1,159,137	1,159,137	1,159,137
Net debt (cash)	(26,063)	(67,920)	(102,844)	(124,862)	(156,361)	(217,997)	(288,451)	(367,676)
Buy out of minorities	0	0	0	0	0	0	0	0
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	425,993	781,835	1,108,533	1,034,274	1,002,776	941,139	870,686	791,461
Non core assets	(77)	(156)	(80)	(80)	(80)	(80)	(80)	(80)
Core enterprise value	425,916	781,679	1,108,453	1,034,194	1,002,696	941,059	870,606	791,381
Growth (%)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenue	22.5	27.7	12.6	-15.7	51.6	8.4	7.6	7.8
EBITDA (UBS)	44.6	48.9	0.4	-22.4	43.5	12.1	7.4	6.4
EBIT (UBS)	48.7	54.2	4.0	-23.6	44.3	11.1	6.9	6.2
EPS (UBS, diluted)	60.9	55.9	14.0	-22.1	47.6	11.2	8.0	8.2
Net DPS	14.5	38.2	46.3	0.5	0.0	0.0	0.0	0.0
Margins & Profitability (%)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
Gross profit margin	35.9	38.6	35.8	34.3	33.0	33.6	33.2	32.6
EBITDA margin	22.6	26.3	23.5	21.6	20.5	21.2	21.1	20.9
EBIT margin	20.0	24.1	22.3	20.2	19.2	19.7	19.6	19.3
Net earnings (UBS) margin	15.8	19.4	19.6	18.1	17.8	18.3	18.5	18.6
ROIC (EBIT)	52.1	76.4	68.1	45.8	60.7	67.1	71.3	75.5
ROIC post tax	40.1	61.5	53.9	48.2	48.0	53.0	56.4	59.7
ROE (UBS)	32.6	37.1	32.4	28.8	27.5	25.5	23.2	21.4
Capital structure & Coverage (x)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
Net debt / EBITDA	(0.7)	(1.1)	(1.3)	(2.0)	(1.8)	(2.4)	(2.7)	(3.4)
Net debt / total equity %	(30.3)	(46.1)	(45.7)	(49.2)	(52.6)	(64.6)	(66.4)	(74.5)
Net debt / (net debt + total equity) %	(43.5)	(85.4)	(84.3)	(96.7)	NM	NM	NM	NM
Net debt/EV %	(10.2)	(11.8)	(10.2)	(13.2)	(17.6)	(27.6)	(36.4)	(52.9)
Capex / depreciation %	93.4	66.4	NM	NM	NM	NM	NM	NM
Capex / revenue %	2.4	1.5	3.3	3.4	4.5	3.5	3.4	3.5
EBIT / net interest	NM	NM	NM	NM	NM	NM	NM	NM
Dividend cover (UBS)	3.7	4.2	3.2	2.5	3.7	4.1	4.4	4.8
Div. payout ratio (UBS) %	26.9	23.9	30.8	39.8	27.0	24.3	22.5	20.8
Revenues by division (Rsm)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	257,694	329,180	370,620	312,347	473,447	513,435	552,482	595,424
Total	257,694	329,180	370,620	312,347	473,447	513,435	552,482	595,424
EBIT (UBS) by division (Rsm)	06/13	06/14	06/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	51,472	79,360	82,520	63,072	91,030	101,095	108,061	114,724
Total	51,472	79,360	82,520	63,072	91,030	101,095	108,061	114,724

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

Tech Mahindra

Revenue outlook still tepid, given a soft telecom segment

Telecom segment unlikely to improve anytime soon

The global telecom sector remains under pressure, which we expect to impact the IT demand from Tech Mahindra's telecom clients (about 50% of revenue). According to management commentary, with the increasing likelihood of M&A in the telecom sector, order flows have also started drying up. In the company's recent earnings call, management noted that delayed contracts are also being altered in scope and structure, which we believe could impact the medium-term revenue outlook for Tech Mahindra.

Digital skills yet nascent compared to its larger peers

Tech Mahindra's digital strategy centres on mobile computing, which is differentiated from its competitors. These offerings are relatively small (about 10% of revenue) and are yet to gain traction in terms of clients' mind share and revenue, in our view. Mobile computing is a much smaller proportion of digital services spending, as per our Evidence Lab survey, which could also limit the revenue growth prospects for Tech Mahindra's digital offerings. The company ranked low in client preferences for mobility in the survey, supporting our view that the company's offerings are yet to gain momentum in the IT services marketplace.

Margin improvement likely, but we expect it to be modest

We believe the company has multiple margin levers, including offshore mix, employee pyramid and post-integration synergies from acquisitions. We expect only modest operating margin improvement for the company in the medium term, given that revenue growth is likely to be slow.

Valuation: cut price target from Rs600.00 to Rs475.00; maintain Neutral rating

We cut our FY17/FY18 earnings forecasts by 4%/5%. Tech Mahindra continues to trade at a 3% premium to its five-year average one-year forward PE and we see limited upside at the current levels. Our price target values Tech Mahindra at 12.8x FY18E PE, in line with our target multiple for Wipro.

Equities

India
Diversified Technology Services

12-month rating **Neutral**

12m price target **Rs475.00**
Prior: Rs600.00

Price **Rs430.15**

RIC: TEMPL.BO BBG: TECHM IB

Trading data and key metrics

52-wk range Rs729.80-423.35

Market cap. Rs413bn/US\$6.05bn

Shares o/s 961m (ORD)

Free float 55%

Avg. daily volume ('000) 1,949

Avg. daily value (m) Rs986.0

Common s/h equity (03/16E) Rs132bn

P/BV (03/16E) 3.1x

Net debt / EBITDA (03/16E) NM

EPS (UBS, diluted) (Rs)

	From	To	% ch	Cons.
03/16E	29.40	29.26	0	32.10
03/17E	34.50	33.09	-4	37.20
03/18E	38.85	37.07	-5	43.05

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Analyst

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Highlights (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenues	143,320	188,313	224,779	264,801	287,078	308,996	331,495	357,616
EBIT (UBS)	26,735	36,615	35,065	34,744	38,903	41,791	45,790	48,914
Net earnings (UBS)	21,154	29,087	25,991	28,814	32,592	36,512	40,054	42,822
EPS (UBS, diluted) (Rs)	22.27	30.44	26.45	29.26	33.09	37.07	40.67	43.48
DPS (Rs)	1.25	5.00	6.00	4.49	5.08	5.69	6.24	6.67
Net (debt) / cash	26,103	32,678	17,303	22,915	33,934	46,442	60,336	73,379
Profitability/valuation	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
EBIT margin %	18.7	19.4	15.6	13.1	13.6	13.5	13.8	13.7
ROIC (EBIT) %	124.1	97.0	53.3	39.6	43.4	46.8	51.4	54.7
EV/EBITDA (core) x	5.2	6.9	12.5	8.9	7.9	7.4	6.7	5.7
P/E (UBS, diluted) x	9.6	11.6	22.3	14.7	13.0	11.6	10.6	9.9
Equity FCF (UBS) yield %	5.8	3.6	2.3	2.7	5.4	5.4	5.9	5.9
Net dividend yield %	0.6	1.4	1.0	1.0	1.2	1.3	1.5	1.6

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied. Valuations: based on an average share price that year, (E): based on a share price of Rs430.15 on 17 Feb 2016 20:26 HKT

Investment Thesis

Tech Mahindra

Investment case

Tech Mahindra has relied heavily on M&A for growth and we expect this trend to continue. We believe currency weakness gives the company an opportunity to shore up its cash reserves, which could be used for further M&A to drive revenue. With demand slowing, organic revenue growth is likely to stay under pressure, in our view. We think current valuations capture the risk of an acquisition-heavy strategy.

Upside scenario

In our upside scenario, we assume organic growth accelerates to 7.5%, as order flows improve in the telecom sector. We also assume the rupee continues to weaken to 69 as the US dollar strengthens against emerging market currencies. We expect EBIT margin to improve to 17% in FY16. The market values Tech Mahindra on PE, in line with global trends. We expect Tech Mahindra to trade at 16x PE, close to one standard deviation above its five-year average, implying a valuation of Rs620.00.

Downside scenario

In this scenario, we assume global GDP slows more than anticipated, exerting pressure on demand for IT services; and M&A activity in the global telecom sector intensifies, impacting Tech Mahindra's exposure to this segment (50% of revenue). We also assume the rupee strengthens to 65 in a relatively stable Indian economy. Revenue growth in this scenario slows to 3.5% YoY in FY16E, with the EBIT margin down to 14.5%. We expect the stock to correct to 10x PE, around 0.5 standard deviation below its five-year average, implying a valuation of Rs300.00.

Upcoming catalysts

Improved revenue growth and operating margin outlooks for FY17 (results likely to be announced in May 2016) should provide positive catalysts. Management commentary about slower-than-expected growth in the telecom segment and a lack of margin expansion would be negative catalysts.

12-month rating

Neutral

12m price target

Rs475.00

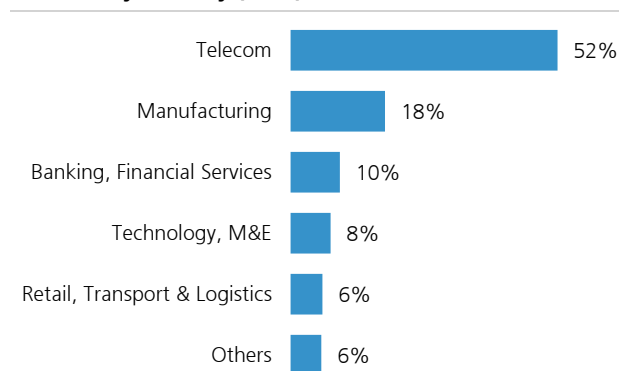
Business description

Tech Mahindra is the fifth-largest IT services vendor listed in India after its merger with Mahindra Satyam. The company's services include application development and maintenance, business process outsourcing and infrastructure management. Tech Mahindra derives over 50% of revenue from the telecom sector; AT&T and BT are among its largest clients.

Industry outlook

We believe the Indian IT services sector is facing a structural disruption, with large IT users beginning to adopt new outsourcing models for incremental cost efficiencies. Despite stable demand and growth in the global IT outsourcing market, many large Indian offshore vendors missed consensus revenue expectations in FY15, with soft revenue growth across key markets and service lines. Price competition has intensified in the past 12 months, indicating increased pressure on revenue from the legacy business, which contributes 85-90% of the industry's revenue.

Revenue by industry (FY15)



Source: Company data

EBITDA by product segment (Rs m)

	FY13	FY14	FY15
IT	21,211	62,962	51,762
BPO	4,130	8,103	6,314

Source: Company data

Tech Mahindra (TEML.BO)

	03/13	03/14	03/15	03/16E	% ch	03/17E	% ch	03/18E	03/19E	03/20E
Income statement (Rsm)										
Revenues	143,320	188,313	224,779	264,801	17.8	287,078	8.4	308,996	331,495	357,616
Gross profit	53,313	71,312	74,045	80,918	9.3	90,264	11.6	96,455	104,434	112,179
EBITDA (UBS)	30,631	41,836	41,144	41,967	2.0	46,341	10.4	49,797	54,378	58,179
Depreciation & amortisation	(3,896)	(5,221)	(6,079)	(7,223)	18.8	(7,438)	3.0	(8,006)	(8,589)	(9,265)
EBIT (UBS)	26,735	36,615	35,065	34,744	-0.9	38,903	12.0	41,791	45,790	48,914
Associates & investment income	0	0	0	0	-	0	-	0	0	0
Other non-operating income	2,121	1,129	1,006	4,200	317.6	4,812	14.6	6,813	7,330	7,868
Net interest	(922)	(797)	(298)	(790)	-165.2	(574)	27.4	(309)	(166)	(179)
Exceptionals (incl goodwill)	0	0	0	0	-	0	-	0	0	0
Profit before tax	27,934	36,947	35,773	38,153	6.7	43,141	13.1	48,295	52,954	56,602
Tax	(6,479)	(7,524)	(9,471)	(9,063)	4.3	(10,138)	-11.9	(11,349)	(12,444)	(13,302)
Profit after tax	21,455	29,423	26,301	29,090	10.6	33,003	13.5	36,946	40,510	43,301
Preference dividends	0	0	0	0	-	0	-	0	0	0
Minorities	(301)	(336)	(310)	(277)	10.9	(411)	-48.7	(434)	(456)	(479)
Extraordinary items	(1,600)	1,200	286	14	-95.0	0	-	0	0	0
Net earnings (local GAAP)	19,554	30,287	26,277	28,828	9.7	32,592	13.1	36,512	40,054	42,822
Net earnings (UBS)	21,154	29,087	25,991	28,814	10.9	32,592	13.1	36,512	40,054	42,822
Tax rate (%)	23.2	20.4	26.5	23.8	-10.3	23.5	-1.1	23.5	23.5	23.5
Per share (Rs)										
EPS (UBS, diluted)	22.27	30.44	26.45	29.26	10.6	33.09	13.1	37.07	40.67	43.48
EPS (local GAAP, diluted)	20.59	31.70	26.74	29.27	9.5	33.09	13.1	37.07	40.67	43.48
EPS (UBS, basic)	22.84	31.27	27.16	29.94	10.2	33.87	13.1	37.94	41.62	44.50
Net DPS (Rs)	1.25	5.00	6.00	4.49	-25.1	5.08	13.1	5.69	6.24	6.67
Cash EPS (UBS, diluted) ¹	26.38	35.90	32.63	36.59	12.1	40.65	11.1	45.20	49.39	52.89
Book value per share	73.77	98.32	127.51	136.85	7.3	147.75	8.0	160.01	173.50	187.94
Average shares (diluted)	949.68	955.58	982.69	984.84	0.2	984.84	0.0	984.84	984.84	984.84
Balance sheet (Rsm)										
Cash and equivalents	34,629	33,202	24,049	29,592	23.0	38,944	31.6	49,807	62,075	73,505
Other current assets	53,260	69,745	90,436	96,626	6.8	101,834	5.4	107,079	112,099	118,797
Total current assets	87,889	102,947	114,485	126,218	10.2	140,778	11.5	156,887	174,174	192,302
Net tangible fixed assets	24,913	22,966	28,723	26,500	-7.7	24,562	-7.3	22,556	20,467	18,202
Net intangible fixed assets	0	5,640	17,283	17,283	0.0	17,283	0.0	17,283	17,283	17,283
Investments / other assets	25,303	27,843	37,990	38,643	1.7	39,329	1.8	40,049	40,805	41,599
Total assets	138,105	159,396	198,481	208,644	5.1	221,951	6.4	236,775	252,729	269,386
Trade payables & other ST liabilities	41,220	45,415	50,800	51,286	1.0	55,103	7.4	59,072	62,947	66,559
Short term debt	0	0	0	0	-	0	-	0	0	0
Total current liabilities	41,220	45,415	50,800	51,286	1.0	55,103	7.4	59,072	62,947	66,559
Long term debt	8,526	524	6,746	6,677	-1.0	5,009	-25.0	3,365	1,739	126
Other long term liabilities	18,480	20,199	16,845	17,100	1.5	17,360	1.5	17,625	17,896	18,171
Preferred shares	0	0	0	0	-	0	-	0	0	0
Total liabilities (incl pref shares)	68,226	66,138	74,391	75,063	0.9	77,473	3.2	80,063	82,581	84,857
Common s/h equity	68,535	91,820	122,489	131,703	7.5	142,190	8.0	153,989	166,969	180,871
Minority interests	1,344	1,438	1,601	1,878	17.3	2,289	21.9	2,723	3,179	3,658
Total liabilities & equity	138,105	159,396	198,481	208,644	5.1	221,951	6.4	236,775	252,729	269,386
Cash flow (Rsm)										
Net income (before pref divs)	19,554	30,287	26,277	28,828	9.7	32,592	13.1	36,512	40,054	42,822
Depreciation & amortisation	3,896	5,221	6,079	7,223	18.8	7,438	3.0	8,006	8,589	9,265
Net change in working capital	(5,517)	(11,357)	(8,617)	(8,686)	-0.8	(4,542)	47.7	(4,538)	(3,973)	(5,148)
Other operating	2,435	(3,177)	235	(11,137)	-	(7,603)	31.7	(11,617)	(13,935)	(15,374)
Operating cash flow	20,368	20,974	23,974	16,228	-32.3	27,884	71.8	28,362	30,734	31,565
Tangible capital expenditure	(9,817)	(9,138)	(11,132)	(5,000)	55.1	(5,500)	-10.0	(6,000)	(6,500)	(7,000)
Intangible capital expenditure	0	0	0	0	-	0	-	0	0	0
Net (acquisitions) / disposals	0	0	0	0	-	0	-	0	0	0
Other investing	(2,464)	2,726	(9,672)	(653)	-	(686)	-	(720)	(756)	(794)
Investing cash flow	(12,281)	(6,412)	(20,804)	(5,653)	72.8	(6,186)	-9.4	(6,720)	(7,256)	(7,794)
Equity dividends paid	(1,343)	(1,359)	(5,496)	(3,112)	43.4	(6,328)	-103.4	(7,038)	(7,588)	(7,934)
Share issues / (buybacks)	3,776	497	582	0	-	0	-	0	0	0
Other financing	(3,876)	(974)	(629)	(536)	14.86	(314)	41.34	(44)	105	97
Change in debt & pref shares	(2,974)	(7,887)	(2,356)	(69)	97.07	(1,668)	2,316.94	(1,644)	(1,626)	(1,613)
Financing cash flow	(4,417)	(9,723)	(7,899)	(3,716)	52.9	(8,310)	-123.6	(8,725)	(9,109)	(9,450)
Cash flow inc/(dec) in cash	3,669	4,839	(4,729)	6,858	-	13,389	95.2	12,917	14,369	14,321
FX / non cash items	28,542	(6,266)	(4,424)	(1,316)	70.3	(4,037)	-206.8	(2,053)	(2,101)	(2,891)
Balance sheet inc/(dec) in cash	32,211	(1,427)	(9,153)	5,543	-	9,352	68.7	10,864	12,268	11,430

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.¹Cash EPS (UBS, diluted) is calculated using UBS net income adding back depreciation and amortization.

Tech Mahindra (TEML.BO)

Valuation (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
P/E (local GAAP, diluted)	10.4	11.2	22.1	14.7	13.0	11.6	10.6	9.9
P/E (UBS, diluted)	9.6	11.6	22.3	14.7	13.0	11.6	10.6	9.9
P/CEPS	7.9	9.6	17.6	11.5	10.3	9.3	8.5	7.9
Equity FCF (UBS) yield %	5.8	3.6	2.3	2.7	5.4	5.4	5.9	5.9
Net dividend yield (%)	0.6	1.4	1.0	1.0	1.2	1.3	1.5	1.6
P/BV x	2.9	3.6	4.6	3.1	2.9	2.7	2.5	2.3
EV/revenues (core)	1.1	1.5	2.3	1.4	1.3	1.2	1.1	0.9
EV/EBITDA (core)	5.2	6.9	12.5	8.9	7.9	7.4	6.7	5.7
EV/EBIT (core)	6.0	7.8	14.6	10.8	9.4	8.8	8.0	6.7
EV/OpFCF (core)	7.5	11.3	19.4	14.4	10.7	9.8	8.8	7.5
EV/op. invested capital	7.4	7.6	7.8	4.3	4.1	4.1	4.1	3.7
Enterprise value (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Market cap.	181,203	329,294	557,283	413,200	413,200	413,200	413,200	413,200
Net debt (cash)	(8,627)	(29,390)	(24,990)	(20,109)	(28,425)	(28,425)	(28,425)	(66,857)
Buy out of minorities	1,344	1,438	1,601	1,878	2,289	2,723	3,179	3,658
Pension provisions/other	0	0	0	0	0	0	0	0
Total enterprise value	173,919	301,341	533,894	394,969	387,064	387,498	387,954	350,000
Non core assets	(14,174)	(14,719)	(21,028)	(21,028)	(21,028)	(21,028)	(21,028)	(21,028)
Core enterprise value	159,745	286,622	512,866	373,941	366,036	366,470	366,926	328,972
Growth (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Revenue	161.1	31.4	19.4	17.8	8.4	7.6	7.3	7.9
EBITDA (UBS)	NM	36.6	-1.7	2.0	10.4	7.5	9.2	7.0
EBIT (UBS)	NM	37.0	-4.2	-0.9	12.0	7.4	9.6	6.8
EPS (UBS, diluted)	1.2	36.7	-13.1	10.6	13.1	12.0	9.7	6.9
Net DPS	23.6	NM	20.0	-25.1	13.1	12.0	9.7	6.9
Margins & Profitability (%)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Gross profit margin	37.2	37.9	32.9	30.6	31.4	31.2	31.5	31.4
EBITDA margin	21.4	22.2	18.3	15.8	16.1	16.1	16.4	16.3
EBIT margin	18.7	19.4	15.6	13.1	13.6	13.5	13.8	13.7
Net earnings (UBS) margin	14.8	15.4	11.6	10.9	11.4	11.8	12.1	12.0
ROIC (EBIT)	124.1	97.0	53.3	39.6	43.4	46.8	51.4	54.7
ROIC post tax	NM	NM	39.2	30.2	33.2	35.8	39.4	41.8
ROE (UBS)	38.8	36.3	24.3	22.7	23.8	24.7	25.0	24.6
Capital structure & Coverage (x)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Net debt / EBITDA	(0.9)	(0.8)	(0.4)	(0.5)	(0.7)	(0.9)	(1.1)	(1.3)
Net debt / total equity %	(37.4)	(35.0)	(13.9)	(17.2)	(23.5)	(29.6)	(35.5)	(39.8)
Net debt / (net debt + total equity) %	(59.6)	(53.9)	(16.2)	(20.7)	(30.7)	(42.1)	(54.9)	(66.0)
Net debt/EV %	(16.3)	(11.4)	(3.4)	(6.1)	(9.3)	(12.7)	(16.4)	(22.3)
Capex / depreciation %	NM	175.0	183.1	69.2	73.9	74.9	75.7	75.5
Capex / revenue %	6.8	4.9	5.0	1.9	1.9	1.9	2.0	2.0
EBIT / net interest	29.0	45.9	NM	44.0	67.8	NM	NM	NM
Dividend cover (UBS)	18.3	6.3	4.5	6.7	6.7	6.7	6.7	6.7
Div. payout ratio (UBS) %	5.5	16.0	22.1	15.0	15.0	15.0	15.0	15.0
Revenues by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	143,320	188,313	224,779	264,801	287,078	308,996	331,495	357,616
Total	143,320	188,313	224,779	264,801	287,078	308,996	331,495	357,616
EBIT (UBS) by division (Rsm)	03/13	03/14	03/15	03/16E	03/17E	03/18E	03/19E	03/20E
Others	26,735	36,615	35,065	34,744	38,903	41,791	45,790	48,914
Total	26,735	36,615	35,065	34,744	38,903	41,791	45,790	48,914

Source: Company accounts, UBS estimates. (UBS) metrics use reported figures which have been adjusted by UBS analysts.

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Neutral	FSR is between -6% and 6% of the MRA.	39%	28%
Sell	FSR is > 6% below the MRA.	12%	22%
Short-Term Rating	Definition	Coverage ³	IB Services ⁴
Buy	Stock price expected to rise within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%
Sell	Stock price expected to fall within three months from the time the rating was assigned because of a specific catalyst or event.	<1%	<1%

Source: UBS. Rating allocations are as of 31 December 2015.

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Cognizant Technology Solutions ^{4, 6a, 6b, 7, 16}	CTSH.O	Neutral	N/A	US\$55.01	16 Feb 2016
HCL Technologies	HCLT.BO	Neutral	N/A	Rs821.75	16 Feb 2016
Infosys Ltd ¹⁶	INFY.BO	Sell	N/A	Rs1,081.00	16 Feb 2016
Tata Consultancy Services Ltd.	TCS.BO	Neutral	N/A	Rs2,267.75	16 Feb 2016
Tech Mahindra	TEML.BO	Neutral	N/A	Rs423.35	16 Feb 2016
Wipro Ltd. ^{3, 16}	WIPR.BO	Sell	N/A	Rs526.60	16 Feb 2016

Source: UBS. All prices as of local market close.

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