

BUY

TP: Rs 4,660 | ▲ 26%

TATA CONSULTANCY SERVICES

Technology & Internet

12 April 2022

Resilient margins

- Q4 revenue growth at 3.2% QoQ CC beat consensus expectations of 2.3% but came in a tad lower than our estimate
- EBIT margin held strong at 25%, ahead of our estimate, aiding an operating profit beat; order book at all-time high of US\$ 11.3bn
- We trim FY23/FY24 EPS by 0.8%/2.6% and roll over to a new TP of Rs 4,660 (vs. Rs 4,770); retain BUY given strong demand and deal wins

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Growth underperforms: TCS's Q4FY22 revenue grew 2.6% QoQ USD, below our estimate of 3.7%. The growth was led by the telecom and media vertical (+5.8% QoQ USD), followed by retail/manufacturing (+4.7%/+3.7%). BFSI grew by a mere 2%. Among major geographies, revenue from North America increased 4.5% QoQ USD and MEA delivered impressive growth at 8%. Among the major demand drivers were cloud, consulting, cognitive business operations, cyber security, IoT and digital engineering, and TCS Interactive. The company added 13 clients QoQ in the US\$ 10mn+/20mn+ revenue buckets and 2 in the US\$ 50mn+ bucket. Net profit grew 1.6% QoQ USD.

Margin shines: TCS reported a stable EBIT margin QoQ at 25%, outperforming our estimate of 24.3% amid a tight supply environment marked by rising attrition as well as elevated hiring. The company saw only a 90bps QoQ impact from the supply crunch which was offset by operational efficiency despite peak attrition levels of 17.4%. TCS hired more than 35,000 employees in Q4FY22, its highest quarterly figure. SG&A expenses were up 20bps QoQ and subcontracting expenses increased 30bps while travel was down 40bps. The company will effect salary hikes from Apr'22, at levels slightly more than its last round of hikes.

Record deal wins: TCS reported a record TCv of US\$ 11.3bn (including two mega deals), with US\$ 8.2bn from BFSI and US\$ 2.6bn from retail. North America had an order book of US\$ 6.1bn in Q4. Ignio signed 36 new clients during the quarter. Cloud adoption in both Horizon I and Horizon II (deals based on cloud-native initiatives) have led to multiple contract wins. Deal pricing has been flattish QoQ but has improved on a full-year basis.

Other takeaways: Europe saw 6%+ growth in Q3 which has normalised due to the high base. TCS plans to announce a new organisation structure with business groups instead of verticals and service lines. It announced final dividend of Rs 22/sh in Q4.

Retain BUY: We tweak estimates to factor in the results and roll valuations to Jun'24, leading to a new TP of Rs 4,660 (vs. Rs 4,770), set at an unchanged 36.5x P/E.

Key changes

| Target | Rating |
|--------|--------|
| ▼ | ◀ ▶ |

| | |
|------------------|-------------------|
| Ticker/Price | TCS IN/Rs 3,696 |
| Market cap | US\$ |
| Free float | 28% |
| 3M ADV | US\$ 145.9mn |
| 52wk high/low | Rs 4,043/Rs 3,004 |
| Promoter/FPI/DII | 72%/17%/11% |

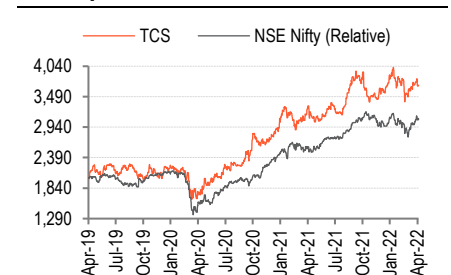
Source: NSE | Price as of 11 Apr 2022

Key financials

| Y/E 31 Mar | FY21A | FY22E | FY23E |
|-------------------------|-----------|-----------|-----------|
| Total revenue (Rs mn) | 1,641,770 | 1,917,540 | 2,182,282 |
| EBITDA (Rs mn) | 465,460 | 530,570 | 607,976 |
| Adj. net profit (Rs mn) | 336,480 | 383,270 | 437,015 |
| Adj. EPS (Rs) | 90.9 | 103.6 | 118.1 |
| Consensus EPS (Rs) | 90.9 | 107.2 | 119.2 |
| Adj. ROAE (%) | 39.2 | 43.3 | 43.2 |
| Adj. P/E (x) | 40.6 | 35.7 | 31.3 |
| EV/EBITDA (x) | 29.7 | 26.1 | 22.8 |
| Adj. EPS growth (%) | 5.5 | 13.9 | 14.0 |

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

| (Rs mn) | Q4FY22 | Q4FY21 | YoY (%) | Q3FY22 | QoQ (%) | FY22 | FY21 | YoY (%) |
|--------------------------------|----------------|----------------|--------------|----------------|--------------|----------------|----------------|--------------|
| Revenue (US\$ mn) | 6,696 | 5,989 | 11.8 | 6,524 | 2.6 | 25,707 | 22,174 | 15.9 |
| Revenue | 505,910 | 437,050 | 15.8 | 488,850 | 3.5 | 1,917,540 | 1,641,770 | 16.8 |
| Operating Expenditure | 367,460 | 309,040 | 18.9 | 354,520 | 3.7 | 1,386,970 | 1,176,310 | 17.9 |
| Cost of revenues | 293,640 | 248,600 | 18.1 | 284,010 | 3.4 | 1,110,530 | 940,530 | 18.1 |
| as % of sales | 58.0 | 56.9 | - | 58.1 | - | 232 | 229 | - |
| SG&A expenses | 73,820 | 60,440 | 22.1 | 70,510 | 4.7 | 276,440 | 235,780 | 17.2 |
| as % of sales | 14.6 | 13.8 | - | 14.4 | - | 58 | 58 | - |
| EBITDA | 138,450 | 128,010 | 8.2 | 134,330 | 3.1 | 530,570 | 465,460 | 14.0 |
| Depreciation | 12,170 | 10,670 | 14.1 | 11,960 | 1.8 | 46,040 | 40,650 | 13.3 |
| EBIT | 126,280 | 117,340 | 7.6 | 122,370 | 3.2 | 484,530 | 424,810 | 14.1 |
| Other Income | 7,360 | 7,930 | (7.2) | 9,540 | (22.9) | 32,340 | 24,970 | - |
| PBT | 133,640 | 125,270 | 6.7 | 131,910 | 1.3 | 516,870 | 449,780 | 14.9 |
| Total Tax | 34,050 | 32,450 | 4.9 | 33,850 | 0.6 | 132,380 | 111,980 | 18.2 |
| Adjusted PAT | 99,590 | 92,820 | 7.3 | 98,060 | 1.6 | 384,490 | 337,800 | 13.8 |
| (Profit)/loss from JV's/Ass/MI | (330) | (360) | - | (370) | - | (1,220) | (1,320) | - |
| APAT after MI | 99,260 | 92,460 | 7.4 | 97,690 | 1.6 | 383,270 | 336,480 | 13.9 |
| Reported PAT | 99,260 | 92,460 | 7.4 | 97,690 | 1.6 | 383,270 | 336,480 | 13.9 |
| Reported EPS | 26.8 | 25.0 | 7.4 | 26.4 | 1.6 | 104 | 90 | 15.1 |
| Margins (%) | | | (bps) | | (bps) | | | (bps) |
| EBITDA | 27.4 | 29.3 | (190) | 27.5 | (10) | 27.7 | 28.4 | 70 |
| EBIT | 25.0 | 26.8 | (190) | 25.0 | (10) | 25.3 | 25.9 | 60 |
| EBT | 26.4 | 28.7 | (220) | 27.0 | (60) | 27.0 | 27.4 | 40 |
| PAT | 19.6 | 21.2 | (150) | 20.0 | (40) | 20.0 | 20.5 | 50 |
| Effective Tax rate | 25.5 | 25.9 | (40) | 25.7 | (20) | 25.6 | 24.9 | (70) |

Source: Company, BOBCAPS Research

Fig 2 – Operating metrics

| (in US\$ terms) | Q4FY22 | Growth (%) | |
|-------------------------------|-----------------------|---------------|---------------|
| | (% Contr. to Revenue) | QoQ | YoY |
| Deal win TCV (US\$ mn) | 11,300 | 48.7 | 22.8 |
| Revenue by Geography | | | |
| Americas | 51.6 | 4.5 | 18.7 |
| UK | 15.6 | 2.6 | 9.0 |
| Europe | 15.5 | (0.6) | 3.2 |
| India | 5.1 | (4.8) | 1.8 |
| Asia Pac | 8.5 | 1.4 | 1.1 |
| Ibero America | 1.7 | 2.6 | 2.0 |
| MEA | 2.0 | 8.0 | 11.8 |
| Revenue by Domain | | | |
| BFSI | 31.9 | 2.0 | 10.8 |
| Manufacturing | 10.0 | 3.7 | 16.5 |
| Telecom & Media | 6.7 | 5.8 | 15.2 |
| Life Sciences & Healthcare | 10.0 | 3.7 | 15.3 |
| Retail & CPG | 15.4 | 4.7 | 18.7 |
| Technology & Services | 8.7 | 2.6 | 15.8 |
| Regional Markets & Others | 17.3 | (0.2) | 1.3 |
| | Q4FY22 | Q3FY22 | Q4FY21 |
| Attrition (LTM) (%) | 17.4 | 15.3 | 7.2 |

Source: Company, BOBCAPS Research

Valuation methodology

We trim our FY22/FY23/FY24 EPS estimates by 1.8%/0.8%/2.6% to bake in the Q4FY22 results while keeping our target P/E unchanged at 36.5x. On rolling valuations over to Jun'24, we have a new TP of Rs 4,660 (vs. Rs 4,770 earlier). Maintain BUY on strong deal wins and a robust demand environment.

Fig 3 – Revised estimates

| (Rs mn) | New | | | Old | | | Change (%) | | |
|--------------------|-----------|-----------|-----------|-----------|-----------|---------|------------|---------|-------|
| | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E | FY22E | FY23E | FY24E |
| Revenues (US\$ mn) | 25,707 | 28,816 | 31,996 | 25,776 | 29,114 | 32327 | (0.3) | (1.0) | (1.0) |
| YoY growth (%) | 15.9 | 12.1 | 11.0 | 16.2 | 12.9 | 11.0 | - | - | - |
| Revenues | 1,917,540 | 2,182,282 | 2,431,676 | 1,921,740 | 2,204,897 | 2456875 | (0.2) | (1.0) | (1.0) |
| EBITDA | 530,570 | 607,976 | 680,189 | 527,299 | 614,276 | 687237 | 0.6 | (1.0) | (1.0) |
| EBITDA margin (%) | 27.7 | 27.9 | 28.0 | 27.4 | 27.9 | 28.0 | - | - | - |
| EBIT margin (%) | 25.3 | 25.6 | 26.3 | 25.7 | 25.7 | 26.4 | (40bps) | (10bps) | 0bps |
| Net profits | 383,270 | 437,015 | 491,275 | 390,221 | 440,707 | 504365 | (1.8) | (0.8) | (2.6) |
| EPS (Rs) | 103.6 | 118.1 | 132.8 | 105.5 | 119.1 | 136.3 | (1.8) | (0.8) | (2.6) |

Source: BOBCAPS Research

Key risks

Key downside risks to our estimates are:

- rising attrition impacting margins, and
- demand-supply mismatch resulting in lost revenue.

Sector recommendation snapshot

| Company | Ticker | Market Cap (US\$ bn) | Price (Rs) | Target (Rs) | Rating |
|---------------------------|------------|----------------------|------------|-------------|--------|
| Coforge | COFORGE IN | 3.5 | 4,312 | 7,080 | BUY |
| eClerx Services | ECLX IN | 1.2 | 2,439 | 3,790 | BUY |
| HCL Technologies | HCLT IN | 40.5 | 1,134 | 1,610 | BUY |
| Infosys | INFO IN | 99.0 | 1,767 | 2,250 | BUY |
| L&T Infotech | LTI IN | 14.0 | 6,060 | 8,490 | BUY |
| Mindtree | MTCL IN | 9.2 | 4,232 | 5,610 | BUY |
| Mphasis | MPHL IN | 7.7 | 3,129 | 3,470 | HOLD |
| Persistent Systems | PSYS IN | 4.8 | 4,515 | 4,580 | HOLD |
| Tata Consultancy Services | TCS IN | 182.6 | 3,696 | 4,660 | BUY |
| Tech Mahindra | TECHM IN | 16.6 | 1,449 | 1,940 | BUY |
| Wipro | WPRO IN | 41.5 | 571 | 850 | BUY |

Source: BOBCAPS Research, NSE | Price as of 11 Apr 2022

Financials

Income Statement

| Y/E 31 Mar (Rs mn) | FY20A | FY21A | FY22E | FY23E | FY24E |
|----------------------------|------------------|------------------|------------------|------------------|------------------|
| Total revenue | 1,569,490 | 1,641,770 | 1,917,540 | 2,182,282 | 2,431,676 |
| EBITDA | 421,100 | 465,460 | 530,570 | 607,976 | 680,189 |
| Depreciation | 35,300 | 40,650 | 46,040 | 49,170 | 40,227 |
| EBIT | 385,800 | 424,810 | 484,530 | 558,806 | 639,961 |
| Net interest inc./(exp.) | 0 | 0 | 0 | 0 | 0 |
| Other inc./(exp.) | 36,680 | 24,970 | 32,340 | 29,403 | 27,884 |
| Exceptional items | 0 | 0 | 0 | 0 | 0 |
| EBT | 422,480 | 449,780 | 516,870 | 588,208 | 667,846 |
| Income taxes | 98,010 | 111,980 | 132,380 | 149,993 | 175,370 |
| Extraordinary items | 0 | 0 | 0 | 0 | 0 |
| Min. int./Inc. from assoc. | (1,070) | (1,320) | (1,220) | (1,200) | (1,200) |
| Reported net profit | 323,400 | 336,480 | 383,270 | 437,015 | 491,275 |
| Adjustments | 0 | 0 | 0 | 0 | 0 |
| Adjusted net profit | 323,400 | 336,480 | 383,270 | 437,015 | 491,275 |

Balance Sheet

| Y/E 31 Mar (Rs mn) | FY20A | FY21A | FY22E | FY23E | FY24E |
|---------------------------------|------------------|------------------|------------------|------------------|------------------|
| Accounts payables | 0 | 0 | 0 | 0 | 0 |
| Other current liabilities | 292,440 | 371,480 | 453,000 | 376,668 | 419,714 |
| Provisions | 0 | 0 | 0 | 0 | 0 |
| Debt funds | 69,060 | 65,030 | 63,680 | 63,680 | 63,680 |
| Other liabilities | 0 | 0 | 0 | 0 | 0 |
| Equity capital | 3,750 | 3,700 | 3,660 | 3,660 | 3,660 |
| Reserves & surplus | 0 | 0 | 0 | 0 | 0 |
| Shareholders' fund | 847,490 | 871,080 | 898,460 | 1,126,296 | 1,382,272 |
| Total liab. and equities | 1,208,990 | 1,307,590 | 1,415,140 | 1,566,644 | 1,865,666 |
| Cash and cash eq. | 86,460 | 68,580 | 124,880 | 92,902 | 285,810 |
| Accounts receivables | 305,320 | 300,790 | 340,740 | 418,520 | 466,349 |
| Inventories | 0 | 0 | 0 | 0 | 0 |
| Other current assets | 239,510 | 295,170 | 247,870 | 358,731 | 399,728 |
| Investments | 273,760 | 318,440 | 362,180 | 362,180 | 362,180 |
| Net fixed assets | 198,410 | 196,690 | 196,150 | 190,625 | 199,032 |
| CWIP | 0 | 0 | 0 | 0 | 0 |
| Intangible assets | 19,930 | 22,780 | 28,880 | 28,880 | 28,880 |
| Deferred tax assets, net | 28,280 | 39,310 | 37,080 | 37,080 | 37,080 |
| Other assets | 57,320 | 65,830 | 77,360 | 77,725 | 86,608 |
| Total assets | 1,208,990 | 1,307,590 | 1,415,140 | 1,566,644 | 1,865,666 |

Cash Flows

| Y/E 31 Mar (Rs mn) | FY20A | FY21A | FY22E | FY23E | FY24E |
|------------------------------------|------------------|------------------|------------------|------------------|------------------|
| Cash flow from operations | 328,975 | 372,880 | 398,330 | 192,644 | 450,157 |
| Capital expenditures | (119,970) | (38,930) | (29,490) | (43,646) | (48,634) |
| Change in investments | (75,780) | 44,680 | (15,220) | 0 | 0 |
| Other investing cash flows | 36,680 | 24,970 | 27,000 | 29,403 | 27,884 |
| Cash flow from investing | (159,070) | 30,720 | (17,710) | (14,243) | (20,749) |
| Equities issued/Others | 0 | (259,499) | 0 | 0 | 0 |
| Debt raised/repaid | 0 | 0 | (14,170) | 0 | 0 |
| Interest expenses | 0 | 0 | (6,980) | 0 | 0 |
| Dividends paid | (155,685) | (161,981) | (133,170) | (210,379) | (236,500) |
| Other financing cash flows | 0 | 0 | 0 | 0 | 0 |
| Cash flow from financing | (155,685) | (421,480) | (154,320) | (210,379) | (236,500) |
| Chg in cash & cash eq. | 14,220 | (17,880) | 226,300 | (31,978) | 192,908 |
| Closing cash & cash eq. | 86,460 | 68,580 | 124,880 | 92,902 | 285,810 |

Per Share

| Y/E 31 Mar (Rs) | FY20A | FY21A | FY22E | FY23E | FY24E |
|----------------------|-------|-------|-------|-------|-------|
| Reported EPS | 86.2 | 90.9 | 103.6 | 118.1 | 132.8 |
| Adjusted EPS | 86.2 | 90.9 | 103.6 | 118.1 | 132.8 |
| Dividend per share | 34.5 | 36.4 | 41.4 | 47.2 | 53.1 |
| Book value per share | 225.8 | 235.4 | 242.8 | 304.4 | 373.6 |

Valuations Ratios

| Y/E 31 Mar (x) | FY20A | FY21A | FY22E | FY23E | FY24E |
|----------------|-------|-------|-------|-------|-------|
| EV/Sales | 8.8 | 8.4 | 7.2 | 6.3 | 5.7 |
| EV/EBITDA | 32.8 | 29.7 | 26.1 | 22.8 | 20.3 |
| Adjusted P/E | 42.9 | 40.6 | 35.7 | 31.3 | 27.8 |
| P/BV | 16.4 | 15.7 | 15.2 | 12.1 | 9.9 |

DuPont Analysis

| Y/E 31 Mar (%) | FY20A | FY21A | FY22E | FY23E | FY24E |
|------------------------------|-------|-------|-------|-------|-------|
| Tax burden (Net profit/PBT) | 76.5 | 74.8 | 74.2 | 74.3 | 73.6 |
| Interest burden (PBT/EBIT) | 109.5 | 105.9 | 106.7 | 105.3 | 104.4 |
| EBIT margin (EBIT/Revenue) | 24.6 | 25.9 | 25.3 | 25.6 | 26.3 |
| Asset turnover (Rev./Avg TA) | 133.1 | 130.5 | 140.9 | 146.4 | 141.7 |
| Leverage (Avg TA/Avg Equity) | 1.4 | 1.5 | 1.5 | 1.5 | 1.4 |
| Adjusted ROAE | 37.0 | 39.2 | 43.3 | 43.2 | 39.2 |

Ratio Analysis

| Y/E 31 Mar | FY20A | FY21A | FY22E | FY23E | FY24E |
|--|-------|-------|-------|-------|-------|
| YoY growth (%) | | | | | |
| Revenue | 7.2 | 4.6 | 16.8 | 13.8 | 11.4 |
| EBITDA | 6.6 | 10.5 | 14.0 | 14.6 | 11.9 |
| Adjusted EPS | 2.6 | 5.5 | 13.9 | 14.0 | 12.4 |
| Profitability & Return ratios (%) | | | | | |
| EBITDA margin | 26.8 | 28.4 | 27.7 | 27.9 | 28.0 |
| EBIT margin | 24.6 | 25.9 | 25.3 | 25.6 | 26.3 |
| Adjusted profit margin | 20.6 | 20.5 | 20.0 | 20.0 | 20.2 |
| Adjusted ROAE | 37.0 | 39.2 | 43.3 | 43.2 | 39.2 |
| ROCE | 35.8 | 37.6 | 42.3 | 43.0 | 41.8 |
| Working capital days (days) | | | | | |
| Receivables | 67 | 67 | 61 | 63 | 66 |
| Inventory | 0 | 0 | 0 | 0 | 0 |
| Payables | 86 | 103 | 108 | 96 | 83 |
| Ratios (x) | | | | | |
| Gross asset turnover | 10.1 | 8.3 | 9.8 | 11.3 | 12.5 |
| Current ratio | 2.4 | 2.0 | 1.7 | 2.5 | 3.0 |
| Net interest coverage ratio | NA | NA | NA | NA | NA |
| Adjusted debt/equity | 0.0 | 0.0 | (0.1) | 0.0 | (0.2) |

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

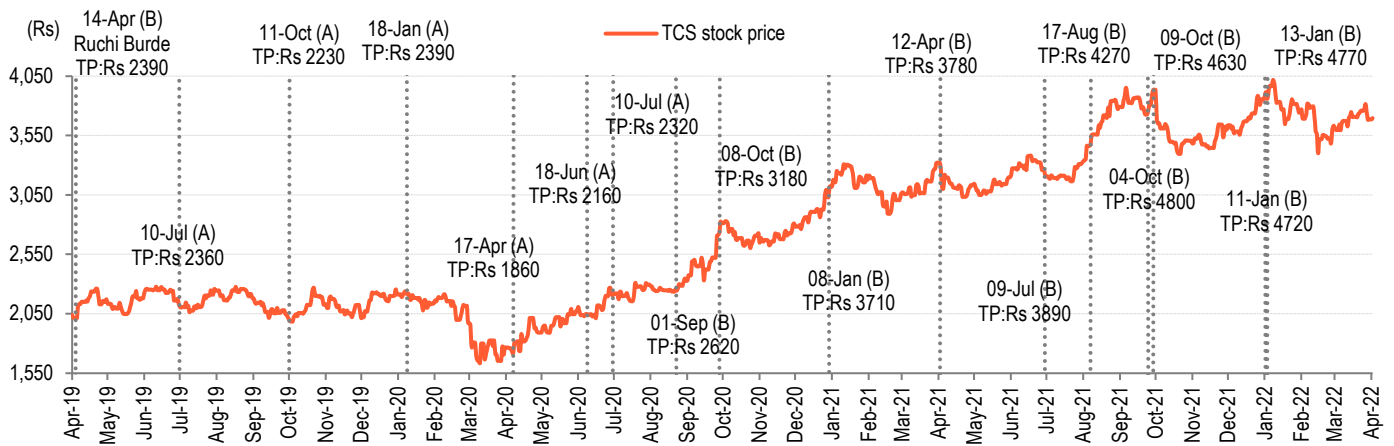
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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Ratings and Target Price (3-year history): TATA CONSULTANCY SERVICES (TCS IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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