

SELL

TP: Rs 290 | ▼ 16%

WIPRO

| IT Services

| 19 November 2020

Sweeping structural changes to simplify business model

Wipro's (WPRO) analyst meet was focused on a slew of strategic changes being implemented by its new CEO. Key initiatives include management restructuring, a deep focus on specific geographies and service lines, and de-prioritisation of investments with low returns. The new, simplified organisation structure will have 4 P&Ls, down from 25 earlier, making for a leaner business. These are substantial changes which will cause workforce churn and pay off only if executed effectively. We retain SELL with a Sep'21 TP of Rs 290 (15.2x P/E).

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Business restructuring: In a bid to simplify operations, CEO Thierry Delaporte has announced a new organisational model featuring four focus geographies (America 1 & 2, Europe and APMEA), cut across by two global business lines (primarily digital and cloud). This will shift WPRO towards a leaner business model with just 4 P&Ls, down from 25 earlier, and flatten the structure. Reported operating metrics under the new model will change from Q4FY21.

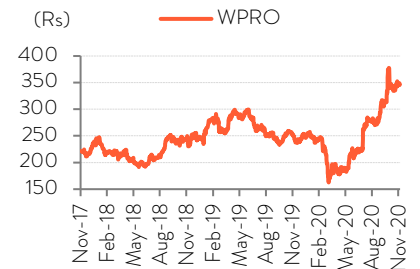
Management restructuring: WPRO will introduce global account executives (GAE) supported by the technology team to focus on key geographies for servicing large accounts. GAEs are expected to form 25% of top management from ~3% now. The company is building a new team directed solely at winning large deals. It also plans to form strong alliances with Google cloud, AWS and SAP by appointing chief growth officers, besides undertaking more acquisitions in emerging markets and setting up a post-merger integration team for smooth transition.

Execution record patchy; reiterate SELL: Though the sweeping structural changes are a positive move intended toward a leaner structure, better resource utilisation and margin gains, they could ratchet up attrition in the near term. Also, given a patchy track record of strategy execution and a laggardly showing amongst peers, we stay apprehensive about WPRO's growth acceleration.

Ticker/Price	WPRO IN/Rs 345
Market cap	US\$ 26.6bn
Shares o/s	5,715mn
3M ADV	US\$ 81.0mn
52wk high/low	Rs 382/Rs 159
Promoter/FPI/DII	74%/9%/17%

Source: NSE

STOCK PERFORMANCE



Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue (Rs mn)	589,060	613,401	626,098	704,410	764,813
EBITDA (Rs mn)	121,661	124,867	134,541	139,668	156,617
Adj. net profit (Rs mn)	90,074	95,295	99,662	98,271	112,784
Adj. EPS (Rs)	14.9	16.7	17.7	17.4	20.0
Adj. EPS growth (%)	12.3	11.6	6.1	(1.4)	14.8
Adj. ROAE (%)	17.1	16.9	17.9	16.5	16.4
Adj. P/E (x)	23.1	20.7	19.5	19.8	17.3
EV/EBITDA (x)	17.0	15.9	14.2	13.9	12.4

Source: Company, BOBCAPS Research

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Other analyst meet takeaways

- **Two global business lines (GBL):** WPRO's new GBLs are IDEAS (integrated digital, engineering and application services) and ICORE (intra cloud, operations, risk and cybersecurity services). The GBLs will be in charge of handling the technology, process and delivery.
- **New strategic priorities:** The company's new focus areas are (1) accelerating growth in specific geographies (then scaling), (2) strengthening relationships with strategic clients and building partnerships to increase large deal wins (combined with M&A), (3) leading with business solutions, (4) building talent at scale (with a focus on hiring the best and reskilling existing talent), and (5) simplifying the operating model (leaner teams centered around clients).

WPRO wants to renew its drive for growth in Europe, the Middle East and Asia (especially Japan, India and Australia). The 'course correction' includes identifying areas of competence to focus on specific sectors in chosen markets.

- **Growing digital spend:** Management emphasised that technology is key to the survival of enterprises. The pace of transformation has accelerated and some of the changes are structural, with collaborative tools coming to the rescue in a Covid-19 world. Traditional services are declining and the shift to new offerings has become more pronounced.

WPRO indicated that digital transformation is encompassing both the front- and back-end, forming 85% of incremental spend. Digital spending is expected to grow 15% over the next five years, with BFSI, retail, energy & utilities, and manufacturing contributing 56% of incremental growth. Per management, the Americas will continue to be the largest by size, but Europe and APMEA will grow faster, contributing 58% to incremental revenue globally. Top strategic spending areas include cloud, AI and cybersecurity.

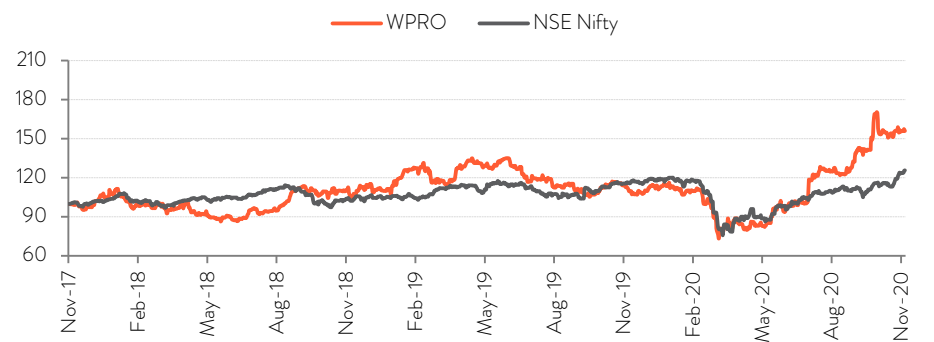
- **Sustained margin focus:** Similar to peers, WPRO expects to sustain margins using traditional levers such as utilisation, offshoring, automation and variable workforce. Management expects increased pricing power to reflect in improved realisations.

Valuation methodology

The new organisational changes focused around geographies and service lines (rather than verticals) are intended for better utilisation of resources and margin improvement. Introduction of GAEs is expected to help streamline the sales process in order to bag more large deals. However, these sweeping structural changes will take time to materialise and potentially pushing up attrition levels in the near term. The benefits of a leaner organisation with fewer layers will drive down costs and aid margins, but only with effective implementation.

Given a patchy track record of strategy execution and a laggardly performance amongst peers, we stay apprehensive about WPRO's resilience in the long term. We reiterate SELL and maintain our Sep'21 target price at Rs 290, set at an unchanged one-year forward P/E multiple of 15.2x.

FIG 1 – RELATIVE STOCK PERFORMANCE



Source: NSE

Key risks

Key upside risks to our estimates are:

- market share gains,
- stronger-than-estimated large deal wins, and
- margin improvement from organisational restructuring.

FINANCIALS

Income Statement

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Total revenue	589,060	613,401	626,098	704,410	764,813
EBITDA	121,661	124,867	134,541	139,668	156,617
Depreciation	19,474	20,281	20,661	23,246	25,239
EBIT	102,187	104,586	113,879	116,423	131,378
Net interest income/(expenses)	15,548	16,752	14,513	9,815	13,465
Other income/(expenses)	0	0	0	0	0
Exceptional items	0	0	0	0	0
EBT	115,458	120,589	128,392	126,238	144,844
Income taxes	25,242	24,799	28,232	27,767	31,860
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	142	495	498	200	200
Reported net profit	90,074	95,295	99,662	98,271	112,784
Adjustments	0	0	0	0	0
Adjusted net profit	90,074	95,295	99,662	98,271	112,784

Balance Sheet

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Accounts payables	0	0	0	0	0
Other current liabilities	158,894	156,761	138,942	156,321	169,726
Provisions	640	612	1,544	1,737	1,886
Debt funds	99,467	78,042	78,042	78,042	78,042
Other liabilities	3,417	2,825	2,825	2,825	2,825
Equity capital	12,068	11,427	10,952	10,952	10,952
Reserves & surplus	558,685	547,906	541,547	628,191	727,601
Shareholders' fund	570,753	559,333	552,499	639,143	738,553
Total liabilities and equities	833,171	797,573	773,852	878,068	991,031
Cash and cash eq.	158,529	144,499	77,799	150,401	236,360
Accounts receivables	100,489	104,474	128,650	127,373	138,295
Inventories	3,951	1,865	5,146	5,790	6,286
Other current assets	129,457	108,891	120,074	149,567	162,392
Investments	233,798	203,345	203,345	203,345	203,345
Net fixed assets	70,601	81,120	85,459	88,213	90,974
CWIP	0	0	0	0	0
Intangible assets	130,742	147,374	147,374	147,374	147,374
Deferred tax assets, net	5,604	6,005	6,005	6,005	6,005
Other assets	0	0	0	0	0
Total assets	833,171	797,573	773,852	878,068	991,031

Source: Company, BOBCAPS Research

Cash Flows

Y/E 31 Mar (Rs mn)	FY19A	FY20A	FY21E	FY22E	FY23E
Net income + Depreciation	109,690	116,071	120,821	121,716	138,222
Interest expenses	(15,548)	(16,752)	(14,513)	(9,815)	(13,465)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	41,128	16,506	(55,527)	(11,287)	(10,690)
Other operating cash flows	14,424	14,919	0	0	0
Cash flow from operations	149,694	130,744	50,782	100,614	114,066
Capital expenditures	(40,798)	(45,057)	(25,000)	(26,000)	(28,000)
Change in investments	0	0	0	0	0
Other investing cash flows	15,548	16,752	14,513	9,815	13,465
Cash flow from investing	(25,250)	(28,305)	(10,487)	(16,185)	(14,535)
Equities issued/Others	0	(105,000)	(95,000)	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(10,840)	(11,469)	(11,994)	(11,827)	(13,573)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(10,840)	(116,469)	(106,994)	(11,827)	(13,573)
Changes in cash and cash eq.	113,604	(14,029)	(66,700)	72,602	85,958
Closing cash and cash eq.	158,529	144,499	77,799	150,401	236,360

Per Share

Y/E 31 Mar (Rs)	FY19A	FY20A	FY21E	FY22E	FY23E
Reported EPS	14.9	16.7	17.7	17.4	20.0
Adjusted EPS	14.9	16.7	17.7	17.4	20.0
Dividend per share	1.5	1.7	1.8	1.7	2.0
Book value per share	94.7	97.9	98.0	113.4	131.1

Valuations Ratios

Y/E 31 Mar (x)	FY19A	FY20A	FY21E	FY22E	FY23E
EV/Sales	3.5	3.2	3.1	2.8	2.5
EV/EBITDA	17.0	15.9	14.2	13.9	12.4
Adjusted P/E	23.1	20.7	19.5	19.8	17.3
P/BV	3.6	3.5	3.5	3.0	2.6

DuPont Analysis

Y/E 31 Mar (%)	FY19A	FY20A	FY21E	FY22E	FY23E
Tax burden (Net profit/PBT)	78.0	79.0	77.6	77.8	77.9
Interest burden (PBT/EBIT)	113.0	115.3	112.7	108.4	110.2
EBIT margin (EBIT/Revenue)	17.3	17.1	18.2	16.5	17.2
Asset turnover (Revenue/Avg TA)	73.9	75.2	79.7	85.3	81.8
Leverage (Avg TA/Avg Equity)	1.5	1.4	1.4	1.4	1.4
Adjusted ROAE	17.1	16.9	17.9	16.5	16.4

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

Ratio Analysis

Y/E 31 Mar	FY19A	FY20A	FY21E	FY22E	FY23E
YoY growth (%)					
Revenue	7.8	4.1	2.1	12.5	8.6
EBITDA	15.4	2.6	7.7	3.8	12.1
Adjusted EPS	12.3	11.6	6.1	(1.4)	14.8
Profitability & Return ratios (%)					
EBITDA margin	20.7	20.4	21.5	19.8	20.5
EBIT margin	17.3	17.1	18.2	16.5	17.2
Adjusted profit margin	15.3	15.5	15.9	14.0	14.7
Adjusted ROAE	17.1	16.9	17.9	16.5	16.4
ROCE	18.6	20.7	21.6	20.6	22.7
Working capital days (days)					
Receivables	62	61	68	66	63
Inventory	3	2	2	3	3
Payables	109	113	105	92	94
Ratios (x)					
Gross asset turnover	8.7	8.1	7.5	8.1	8.5
Current ratio	2.5	2.3	2.4	2.7	3.2
Net interest coverage ratio	6.6	6.2	7.8	11.9	9.8
Adjusted debt/equity	(0.1)	(0.1)	0.0	(0.1)	(0.2)

Source: Company, BOBCAPS Research

Disclaimer

Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

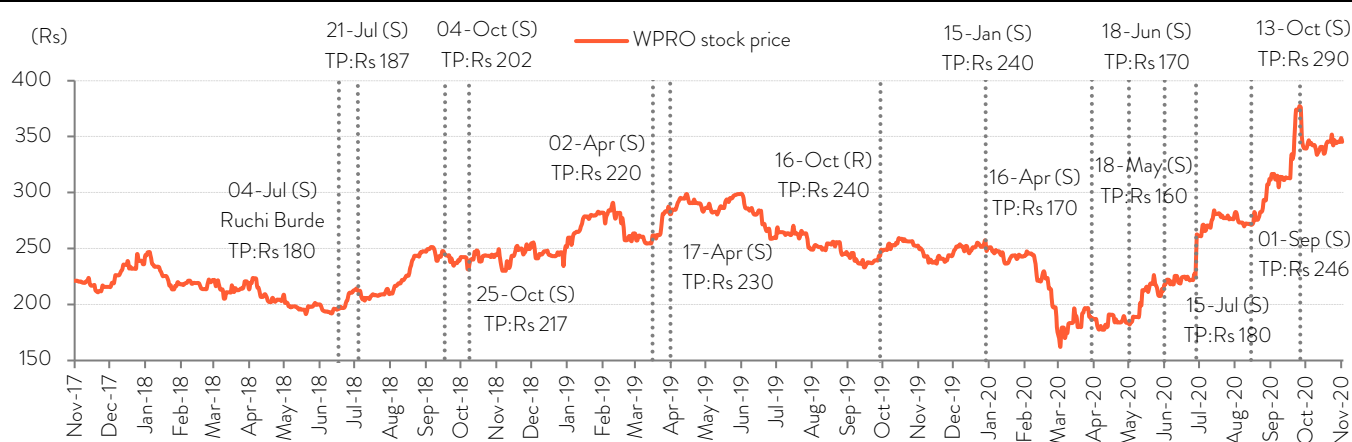
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

RATINGS AND TARGET PRICE (3-YEAR HISTORY): WIPRO (WPRO IN)



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

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